Aviva Investors' Submission to the BIS Select Committee Inquiry into the Kay Review

Executive Summary

As the UK's largest insurer and owner of a global asset management business with assets under management in excess of £370 billion, Aviva is able to speak as both the owner of, and investor of capital in the market.

We welcome the opportunity to participate in the Committee's inquiry into Professor Kay's Review and the Government's response. We believe that, although Professor Kay produced a thorough and thoughtful analysis of the causes of short-termism in the equity markets, the study failed to fully examine the role of other participants in the investment chain that have a significant influence on the way companies are structured and develop their strategies.

Both Professor Kay and the Secretary of State have made several welcome proposals, for example on narrative reporting, ending quarterly reporting and the establishment of a new investment forum to reinvigorate collective engagement. We welcome these proposals as they fit with our investment beliefs, which are centred on being long term, engaged, active investors running low turnover, focused portfolios.

However, by failing to provide recommendations that address all the participants that influence the investment chain, or its inherent tensions and commercial conflicts, neither the review nor the government's response sufficiently address the underlying causes of why the market is so short term. For example, it misses the opportunity to encourage investment consultants to oversee the way asset holders and their managers engage in stewardship and to examine the significant role played by sell side brokers.

This submission will give a brief overview of the causes of short termism in the capital markets and will then take each Kay recommendation in turn that we believe should be revised or expanded and will conclude with a series of policy recommendations to the Committee.

1. Introduction

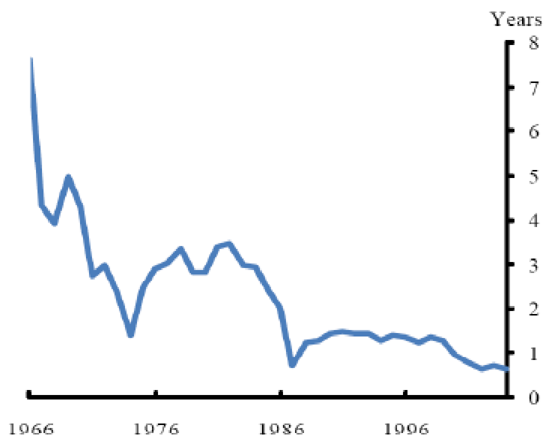
1.1 As a largely long-term, risk-averse equity investor, we are investing for our clients for the long-term. Looking at the broader dynamic in the capital markets, however, the pressures are clearly to the short term, which ultimately affects both investor and company behaviour.

1.2 We therefore welcome the debate about the role that long term investors should play in terms of stability, enabling corporations to focus on long-term strategic decisions and supporting economic growth. This must be significant if good long-term corporate investment opportunities (requiring a higher initial capital investment) that have a lower expected return, but a higher NPV (increase in shareholders' wealth), are being passed up for faster and less value added alternatives.

1.3 At a headline level a distinction needs to be drawn between those who mainly trade shares and those who commit material amounts of capital to companies through the markets. Proprietary and principle traders that buy or sell equities or substitute instruments, often with their own capital, including hedge funds and others with very high portfolio turnover, such as high frequency traders, tend to be driven by short term market trends and turn over their portfolios rapidly. Those that invest will also buy and sell equities but tend to hold them for the long term based on their analysis of the prospects of the company and their perception of the underlying performance.

1.4 The Bank of England's Andrew Haldane has highlighted[1] the sharp decline in average holding periods for UK equities since the mid-60s from a period of almost 8 years to just 7½ months in 2007, a trend that is reflected in the US and other international equity markets:

Figure 3. FTSE Average Holding Periods 1966-2005



Source: London Stock Exchange

1.5 However, the 7½ month figure does not offer a clear insight into the current state of play. Data from Tabb Group, UK National Statistics and the London Stock Exchange, shows that

[1] "Patience and Finance" (September 2010), Bank of England

about two thirds of the turnover in UK equities is accounted for by hedge funds and high-frequency traders. By contrast the average holding periods of more traditional long-only funds in the past decade, who hold a more significant proportion of assets, have varied from 29 to 46 months, although this is still less than it was in the mid-60s.

1.6 Amongst the issues that the review highlighted, of particular interest in this context was the impact of technological advances and automated trading on investment. We believe that this dynamic and the developments that have been seen not only in the context of high frequency trading but also financial product development are particularly significant elements of the short-term orientation of the capital markets.

1.7 Looking back at the origins of high-frequency trading, after London moved from the trading floor to electronic trading in 1986, in what was known as the Big Bang, the average number of daily trades at the London Stock Exchange rose from around 20,000 trades to 839,244 with a peak in excess of 900,000 in 2007, although the crisis has impacted that trend. This is just the market equity volume and does not capture the full picture of related trading in, for example, contracts for differences (CFDs) and other related instruments. It is important, therefore, to recognise the range of parallel and connected trading strategies that exist and the fact that by 2007 Europe had become the most important region in the global derivatives market, with 44% of the global outstanding volume (significantly higher than its share in equities and bonds).

1.8 Compared to estimates of 35% to 60% in the UK, in the US capital markets, it has been suggested that HFT can account for up to 56% to 75% of dollar trading volume in US equities.[2] The US Flash Crash in May 2010 was foreshadowed in the Black Monday crash of 1987. Computerised trading, high frequency traders and what is known as "order flow toxicity"[3], have been attributed with creating the biggest one-day point decline on an intraday basis in Dow Jones Industrial Average history.[4]

1.9 While proponents of high-frequency trading argue that it provides liquidity to the market, there is evidence to the contrary.[5] Amongst other issues, not only is high-frequency trading positively correlated to share price volatility,[6] which HFTs exploit aggressively, but the general liquidity argument (clearly not borne out in the flash crash) is called into question.

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[2] See for example: http://www.bloomberg.com/news/2011-10-05/with-high-speed-trading-market-cannot-hold-commentary-by-mark-buchanan.html or http://xtiburon.com/finance/how-high-frequency-trading-affects-the-market/

[3] "The Microstructure of the „Flash Crash": Flow Toxicity, Liquidity Crashes and the Probability of Informed Trading" (2011) Easley et al, *The Journal of Portfolio Management, Vol. 37, No. 2*

[4] "Findings Regarding the Market Events of May 6, 2010" (Sept 2010), US SEC and CFTC

[5] "High Frequency Trading, Stock Volatility and Price Discovery" (2010), F.Zhang, Yale School of Management

[6] See also "An Empirical Study of Volatility and Trading Volume Dynamics Using High-Frequency Data" (2010) Lu and Lin; "High Frequency Traders, News and Volatility" (2011) Martinez and Rosu; and "Where is the Value in High Frequency Trading" (2011) Cartea and Penalva

However, this must not be taken to mean that all short term investment activities are a problem, although valid concerns continue about the volume and impact of HFT.[7]

1.10 There is also the risk that high frequency traders can create mispricing which is then exploited to the disadvantage of ordinary investors.[8]

1.11 We therefore feel that steps need to be taken to curb the focus on and trends around HFT that seem to dominate the capital markets, although we are firmly opposed to the EU's proposed Financial Transaction Tax, which would be both damaging to long term risk averse investors and London, as well as ineffective in raising the (net) revenues envisaged (See Appendix 1). More broadly, these issues form part of the wider, inherent or endogenous risks that financialisation, the increase in speculation and decrease in investing, the growth of derivatives and use of leverage, the practice of shadow banking and lack of transparency, and institutions that are "too big to fail" all link together to create.

1.12 The practical issues for long-term investors, the trends being seen in asset allocation, and the issues of myopia and short-termism are apparent not only in the market's increasing focus on high frequency trading, the broader level of portfolio turnover and falling holding periods, but also in the incentives of both market participants and corporate managers.

1.13 Dynamics such as short corporate reporting cycles/milestones and short-term performance measurement of investment portfolios are factors that both feed off and contribute to the short-term orientation of the capital markets and, in some cases, the behaviour of companies.

1.14 As the regulatory and standards frameworks, incentives and practice have all converged towards accommodating shorter time horizons, behaviours have normalised around and exacerbated that and the dynamic has become self-perpetuating, with increasing emphasis on immediacy and trading. This was neatly summed up by the founder of one US trading house who observed, in the context of the US flash crash, that "Over $1 trillion of market value evaporates in less than 15 minutes and people say, "Who is to blame?". No one is to blame. This is the market that we have. This is the by product of a market structure that has gone horribly wrong."[9]

1.15 A recent McKinsey survey[10] found that most executives believed that their companies were too loss averse in their approach. Two-thirds of the respondents indicated that their companies underinvested in product development[11], and more than half that they

[7] e.g. "High Frequency Trading: The growing Threat of Rogue Trading" (2011) Weber, London Business School
[8] "A Dysfunctional Role of High Frequency Trading in Electronic Markets" (2011), R. Jarrow and P.Protter
[9] "Speed-addicted traders dominate today‟s stock market" (2010) Los Angeles Times - http://www.themistrading.com/article_files/0000/0557/051610LosAngelesTimes.pdf
[10] "A bias against investment?" (2011), Kholler et al, McKinsey Quarterly
[11] In this context see: "Innovation and Performance in British-based Manufacturing Industries – a Policy Analysis" (2002) Cox and Frenz

underinvested in sales and marketing and in the financing of start-ups for new products or new markets. This should be of significant interest to policymakers as, as the authors note, these are not just missed opportunities for individual companies: the investment dearth hurts whole economies and job creation efforts as well. To solely blame the capital markets, however, would be unreasonable; they are one piece of the jigsaw.

2. The Stewardship Code

2.1 The Kay Review recommended that the Stewardship Code should be expanded to focus on more strategic issues as well as corporate governance. An interest in and assessment of strategy, competitive positioning, operational efficiency and the leadership of businesses, clearly form part of the active investment process and approach we deem necessary for long-term investment.

2.2 The Stewardship Code sets out clear good practice and although there are clearly examples of effective practice and activity in equity investment, the integration of stewardship activities and what those activities are deemed to involve varies between fund management houses. Except for the most focused funds and listed turnaround vehicles, which often have highly concentrated portfolios and a relatively high level of resource per investment, the levels of resource that are available or indeed viable mean that a selective approach and prioritisation is needed. This is particularly true when spread across hundreds or indeed thousands of investments globally.

2.3 The take up and/or disclosure on the Code by asset owners has been more muted than amongst asset managers. This is an area where considerable uncertainty and lack of conviction still exists. Policymakers need to build on the solid foundations provided by the UK's Stewardship Code and, amongst other things, the Pensions Regulator should be asked to re-examine its own regulations and to re-task its Investor Governance Group to take a more proactive interest and review their guidance around the Myner's Principles. This work should also take account of market developments and how these frameworks should accommodate trends, such as that towards Fiduciary Management.

2.4 Furthermore, policy-makers should establish mechanisms that promote, encourage and require investors to maintain an appropriate oversight role of companies; for example, investors could be required to publicly disclose their voting record and pension trustees to report to their beneficiaries on how their ownership rights have been exercised.

2.5 There should also be regulatory enforcement measures of the stewardship codes and improved accountability of voting agencies, which have considerable power to either influence or control a substantial portion of the market at shareholder meetings. The voting recommendations of voting agencies are based on best practice, but cannot take sufficient account of individual circumstances. In some instances, this creates a box-ticking approach to corporate governance. This situation could be improved if proxy voting agencies were to explain their processes and explain the rationale for their voting decisions.

2.6 Responsible ownership is a non-excludable public good, i.e., the benefits of engagement are enjoyed by all owners regardless of whether they behave as responsible long term owners. Consequently, the vast majority of profit maximising commercial fund management institutions free ride and either do not do stewardship at all, or invest only token resources in this work. Professor Kay's review does not consider how to significantly increase either the economic demand for, or the financial funding of stewardship. In general, it is assumed that fund managers will be responsible and accept their public interest role for them to conduct stewardship and voluntarily invest more in their stewardship work. This is misguided at best and economically naive at worst.

2.7 Fortunately, as Professor Kay recognises, there is no shortage of money in the system for financing the work of the various market intermediaries; global commission spend is between $25-$33 billion[12] In the UK, commission flows are overseen by the FSA and to control what fund managers spend this money on, the FSA has established a series of tests that fund managers have to apply before funding their research with commission (as this is generated from a small percentage charge on their client's assets under management rather than from their own balance sheet).

2.8 A few fund managers - including Aviva Investors - are directing this research commission towards brokers and independent research providers of long term investment research, voting advice and stewardship work. We are clear that investment stewardship passes these tests and adds value to investment decisions.

2.9 We believe that if policy-makers were to take the following four steps, then it would significantly increase the scale of stewardship resources in the market and fundamentally transform the delivery of long term investment analysis and investor stewardship:

I. Policy-makers could clarify that long term investment research that is orientated towards good stewardship behaviour by investors can be paid for in this way;

II. Policy-makers could suggest as a guide that it is good practice for a material proportion of the commission research (say 10-25%) to be spent in this way;

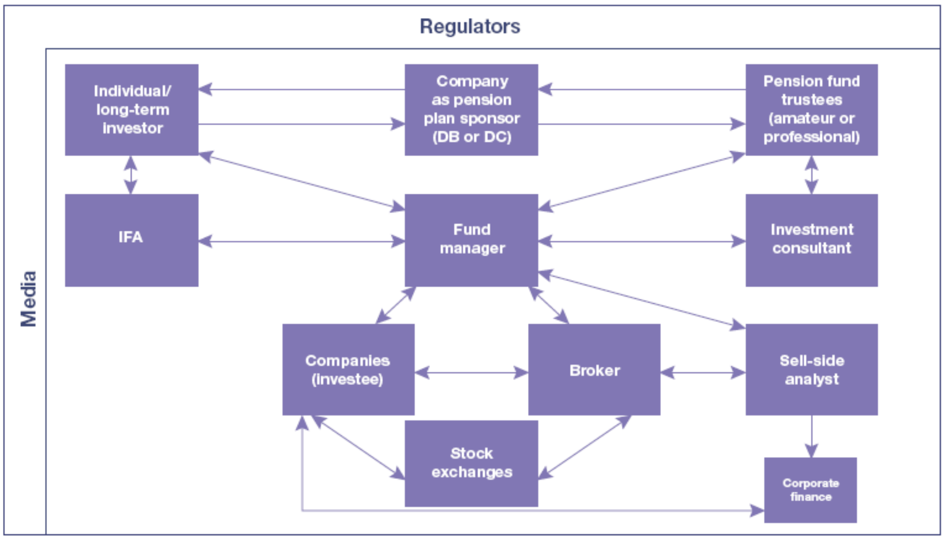
III. Policy-makers could say that it is good practice for fund managers to be transparent to their clients that this was taking place; and,

IV. Policy-makers could say that it is good practice for clients to be allowed to opt out of this, as long as they are clear to their beneficial owners what their rationale is for so doing.

[12] Source: Frost Consulting, July 2012

3. Good Practice Statements for company directors, asset managers and asset holders

3.1 The Good Practice Statements are welcome but fail to cover all relevant players in the capital market. The below diagram represents the impacts and interactions of incentives across the capital system. The arrows represent the direction of these impacts:



Source: Tomorrow's Company, 2012

3.2 Tomorrow's Company conducted a piece of research on potential issues for long-term stewardship and the alignment of incentives in partnership with Aviva Investors and found that potential conflicts of interest included:

3.2.1 Pension fund trustees and investment consultants

- Investment consultants tend to charge a fixed hourly rate and therefore have an incentive to be active in order to maximise their income. They therefore offer an increasingly wide range of services that they encourage trustees to use.
- Pension fund trustees will monitor the performance of their investment consultants according to a number of criteria that are not generally related to the fund's performance. It can be argued that this is necessary as investment consultants are not the investment decision-makers, but it does create a misalignment of interests.
- The degree to which investment consultants take into account factors relating to the long-term sustainability of companies is dependent on: the degree to which pension fund trustees wish to take them into account; and the cost of maintaining dedicated research teams and the lack of good long-term comparable data.

3.2.2. Investment consultants and fund managers

- Investment consultants have differing views on the key aspect of their role which adds most value for their pension fund clients. Some believe it is through advice on asset allocation while others believe it is through the fund manager selection process.

- There is an opportunity to generate substantial income through the fund manager selection process, so consultants may be incentivised to encourage fund manager turnover.

3.2.3 Pension fund trustees and fund managers

- The close and frequent monitoring of fund management performance by trustees can result in fund managers feeling pressured to maintain high levels of short-term performance relative to the benchmark to retain funds.
- 66% of pension funds formally review fund manager performance every quarter (92% annually or less), despite the key investment period for trustees appearing to be longer than a rolling or calendar year for 62% of them.[13] This can create incentives that affect fund managers' approach to risk taking.

3.2.4 Sell-side analysts, brokers and fund managers

- Brokers' remuneration is directly tied to trading volumes. As a result they have a powerful incentive to encourage market activity.
- Even when sell-side analysts are aware of corporate governance or sustainability concerns, these analysts do not report this in their reports to buy-side analysts for fear of losing access to those boards

3.2.5 Corporate financiers and sell-side analysts

- As highlighted by the SEC in the US, analysts who work within the umbrella of a larger investment bank may have a potential conflict of interest around IPOs and new rights issues. The existence of such a relationship should not be taken to automatically mean an analysts' research is biased as there are strict codes of conduct, but research has shown that analysts may still feel under pressure to produce positive reports on the client company.[14]

3.2.6 Corporate financiers and investee companies

- Corporate financiers' incentives are weighted towards deal completion. This can lead to a misalignment of interests as investment bankers' motivation to complete a deal may ignore what is in the longer-term interests of the company and its shareholders.

3.2.7 Fund managers, stock exchanges and investee companies

- Nearly half of all exchanges are companies listed on their own exchange and are therefore subject to shareholder pressure to maximise returns. The largest sources of revenue for demutualised, for-profit stock exchanges are reliant on market activity. This results in an incentive for exchanges to create inducements for trading activity.

[13] "NAPF/IMA Short-Termism Study Report" (2004) MORI

[14] See: US Securities and Exchange Commission. "Analysing Analyst Recommendations". Available at: http://www.sec.gov/investor/pubs/analysts.htm

3.3 In short, there is a lack of alignment between incentives, the interests of beneficiaries and business strategy. The criteria on which performance and hence reward is based are still too often founded on excessively short-term measures.

3.4 Simple measures could be implemented to align these incentives, for example: fund manager performance should be reviewed over longer time horizons than the typical quarterly cycle; excessive reliance on measuring performance relative to a market index should be reduced; pension funds should have voting and engagement policies that should be integrated into the investment process; shareowner activism should be given more weight in the selection and retention of fund managers and other matters; all advisors to institutional investors should have a duty to proactively raise ESG issues and encourage adherence to the Stewardship Code; fund management contracts and fund managers' performance should include an evaluation of long-term ability to beat benchmarks; investment consultants' fee structures should not reward them for moving clients between fund managers; and within companies the implementation of strong cultural norms should be supported by independent whistleblowing mechanisms, overseen by professional bodies who offer the whistleblower appropriate protection.

4 The scale and effectiveness of merger activity of and by UK companies should be kept under careful review by BIS and by companies themselves;

4.1 The role of incentives in this context is particularly important. Half or more of the mergers, acquisitions, and alliances that take place, fail to create significant shareholder value both in our experience and according to much of the research that has been undertaken on major deals.[15] For some time now, academics have flagged that company size is the factor that has the highest and most significant positive correlation with levels of executive pay.[16] This is echoed in academic work on UK M&A,[17] which has highlighted the significant and substantial executive pay increases, in excess of those generated by the growth in firm size, consequent upon mergers.

4.2 A way needs to be found to break this dynamic and re-align the incentives and economic interests of all participants in taking a longer-term approach. This applies not just to capital markets participants but to Boards of directors and their remuneration committees.

[15] See "Deals that create value" (2001) Biesharr et al. or "Why do acquisitions so often destroy Shareholder Value?" (2002) PA Consulting Group or "Deals from Hell: M&A Lessons That Rise Above the Ashes" (2005) R.Bruner

[16] "How Much Does Performance Matter? A Meta-Analysis of CEO Pay Studies" (2000) Tosi et al.

[17] See for example "Merger Activity and Executive Pay" (2002) Gima et al.

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5 Asset managers should make full disclosure of all costs, including actual or estimated transaction costs, and performance fees charged to the fund;

5.1 Looking at the question of whether and how asset managers should be more transparent, we quite understand the concerns around, for example, some fee structures.[18] This broad area is one that we are generally interested in seeing explored and debated further.

5.2 We support the Good Practice Statements recommended by Professor Kay and welcome the initiatives on cost transparency by the ABI and the Investment Managers Association and are complying with both.

6 Mandatory IMS (quarterly reporting) obligations should be removed;

6.1 We welcome the proposal to amend the Directive on Transparency Requirements for Listed Companies so that the requirements to produce interim management statements and quarterly reports are abolished. Such short term reporting cycles contribute to short-term thinking and can discourage investment for the long-term, given the impact that could have on short-term performance. It is also important to recognise the effects of peer pressure and competition between companies in this context.[19]

6.2 Unilever Plc is often cited as an example of the hurdles companies have to overcome and mindset needed in breaking away from short term dynamics. Their move away from providing regular short-term guidance to embed a longer-term approach and practices was welcome and interesting. Initially the response from short term investors pushed the share price down around 10 per cent, but it subsequently outperformed.[20] This highlights the importance of recognising that the dynamic here should not be characterised as just a capital markets issue. Unilever is not alone though in having sought to face up to this challenge and, looking at more cyclical businesses, others that would be worth exploring the issues with might include Aggreko Plc or Marshalls Plc.

6.3 On reporting more widely, the International Financial Reporting Standards (IFRS) are pro-cyclical in nature and played a notable role in facilitating and exacerbating both the dynamic and behaviours that drove the credit bubble and the subsequent crisis. Despite a common assertion of some standard setters, IFRS are not just presentational, they have real world effects, not just for pensions, capital management, behavioural biases, risk taking, and ability to be prudent but also, and not least, financial product innovation. The effects and problems have arisen both as a result of how the standards have been implemented and their effects on accounts. Not least, critical concepts like prudence and accounting conservatism have been superseded by a compliance orientated model. Concepts like the “true and fair view” have also been diluted. IFRS

[18] “Fund Management Fees” (2010) Terry Smith (http://www.terrysmithblog.com/straight-talking/2010/09/fund-management-fees.html)
[19] See for example http://www.ft.com/cms/s/0/5d6c466c-6a00-11e0-86e4-00144feab49a.html#axzz1dOaOWc00
[20] http://www.mckinsey.com/en/Features/Capitalism/Paul_Polman.aspx

compliance allows significant discretionary scope within fair values. The standards have also resulted in the Companies Act accounting requirements being obfuscated, e.g. in relation to distributable reserves and dividends. From an investor perspective, a significant proportion of bank capital raising over the crisis went to redress precisely the results of that.

6.4 Looking at the broader accounting frameworks, long-term investors are interested not just in the decision usefulness model pursued by accounting standard setters, which is more orientated towards the trading markets than it is to corporate stewardship or to long-term ownership and investment. As the preliminary report of The Sharman Inquiry[21] noted, investors and "quite a lot of others" have raised questions about the suitability of IFRS accounts as a basis for assessing the solvency of businesses. As the report notes, overall, capital management is important to us as shareholders. However, IAS 1 disclosures are not generally providing what long-term shareholders want, although they could in theory be used to do so.

7 High quality, succinct narrative reporting should be strongly encouraged;

7.1 It is extremely difficult for any within the investment chain to demonstrate the value of non-financial information without widespread reporting on these areas by companies, in accordance with a consistent framework and standards.

7.2 Information should be disclosed in an integrated manner with strategy, risk and performance on: remuneration and incentive plans, material sustainability issues and the culture and values of a company.

7.3 The current framework and practices mean that many companies are failing to provide the level of information needed for investors to be able to judge the sustainability of businesses, affecting long-term strategic analysis. Globally, of 20,000 publicly listed companies recently reviewed through Bloomberg's database, less than one in five publicly reported on even a single item of quantitative data on environmental, social or governance issues.[22]

8 Remuneration

8.1 Most institutional client mandates tend to run for a minimum of three years. However, despite the long term nature of the liabilities institutions face, a norm for fund manager incentives is to have one- and three-year rolling performance horizons, i.e. the short and medium term, but not the long term. Although the dynamic is not always so simple, asset managers know that if they under-perform for a short period within this time they could be replaced. Therefore, some asset managers may take risks to get the required returns over a shorter time frame.[23] Efforts, such as

[21] "Going Concern and Liquidity Risks: Lessons for Companies and Auditors – Preliminary Report and Recommendations of the panel of Inquiry" (2011) The Sharman Inquiry
[22] http://www.guardian.co.uk/sustainable-business/aviva-chief-city-failure-sustainability
[23] See for example "Employment Risk, Compensation Incentives and Managerial Risk taking – Evidence from the Mutual Fund Industry" (2007) Kempf et al.

that of the Universities Superannuation Scheme, have been made in the past to devise longer term mandates but the need to plug pension scheme deficits has, in recent times, been the greater priority and so aggressive pursuit of short term performance continues.

8.2 According to National Employment Savings Trust (NEST) chief investment officer, Mark Fawcett, improving companies through corporate governance will remain "a fantasy" until pension trustee's better align their managers' incentives. Speaking at the OECD - WPC World Pensions and Investments Forum in December 2010, Fawcett suggested that pension scheme trustees are too focused on short term returns by hiring and firing fund managers on a three year cycle, whereas they should be looking at five years as a minimum, maybe ten. Fawcett maintains that "until pension funds start behaving the right way by aligning the incentives for fund managers... the idea that corporate governance is going to make a change is unrealistic."[24]

8.3 We believe that some Trustees consider it just as much a risk to award long term mandates as to not remove under-performing fund managers before their mandates are completed. However, as it takes time to discern the extent to which a fund manager's performance is attributable to luck or skill, we consider it often inappropriate for managers to be judged solely on their short term performance. Indeed, over time as luck evens out, skill, where it exists, will shine through. Academics have, in the past,[25] examined the process in which asset owners hire and fire their fund managers and found a tendency to hire managers who had recently performed well and fire managers who had recently performed badly. The point of note was that the fired managers, on average, subsequently outperformed those hired, albeit marginally, notwithstanding the sizeable transition costs incurred in changing managers.

[24] See Professional Pensions, 15 December 2010

[25] See for example "The Selection and Termination of Investment Management Firms by Plan Sponsors" (2008) Goyal and Wahal

9. Recommendations

There are four key areas that need to be addressed in order for the capital market to deliver on long-termism and sustainability. These are:

- **Investor advocacy influence**

a) Sustainability or CSR report should be put to a vote at a company's AGM on a comply or explain basis

b) Policy-makers should establish mechanisms that promote, encourage and require investors to maintain appropriate oversight role of companies; for example, investors could be required to publicly disclose their voting record and pension trustees to report to their beneficiaries on how their ownership rights have been exercised

c) Regulatory enforcement measures of the Stewardship Code

d) Regulation and improved accountability of voting agencies

- **Incentives of all players in the capital markets**

a) Fund manager performance should be reviewed over longer time horizons than the typical quarterly cycle

b) Excessive reliance on measuring performance relative to a market index should be reduced

c) Pension funds should have voting and engagement policies that should be integrated into the investment process

d) Shareowner activism should be given more weight in the selection and retention of fund managers and other matters.

e) Implementation of strong cultural norms supported by independent whistleblowing mechanisms, overseen by professional bodies who offer the whistleblower appropriate protection

f) All advisors to institutional investors should have a duty to proactively raise ESG issues and encourage adherence to the Stewardship Code

g) Fund management contracts and fund managers' performance should include an evaluation of long-term ability to beat benchmarks

h) Investment consultants' fee structures should not reward them for moving clients between fund managers

- **Availability of market information**

a) Policy-makers could clarify that long term investment research that is orientated towards good stewardship behaviour by investors can be paid for in this way;

b) Policy-makers could suggest as a guide that it is good practice for a material proportion of the commission research (say 10-25%) to be spent in this way;

c) Policy-makers could say that it is good practice for fund managers to be transparent to their clients that this was taking place; and,

d) Policy-makers could say that it is good practice for clients to be allowed to opt out of this, as long as they are clear to their beneficial owners what their rationale is for so doing.

e) Disclosure from investors and their agents on integration of ESG issues into the investment process
f) Integrated narrative reporting should be required from all listed companies on a comply or explain basis

- **Training and education**

a) Fund manager and analyst training centres e.g. the Chartered Financial Analyst Institute should use their syllabus and charterholder exam to look at how sustainable development work of companies may enhance corporate valuation

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