ICGN mid-year conference Madrid

March 2015

Building on the themes and outcomes of previous ICGN conferences, the most recent event held in Madrid provided a platform for the participants to interrogate critical continental and global issues of relevance to investors and issuers across countries, under the theme "Celebrating 20 years of inspiring good Governance".
As delegates, Sodali representatives were pleased to return from the conference where encouraging messages towards good Governance replicate what it has been advocated by our company all along.

Spanish Corporate Governance developments

The Spanish Corporate Governance Code for listed companies in contrast to its predecessors, is influenced by two unique circumstances: on the one hand, it was preceded by a broad reform of the Spanish Companies Act (Ley de Sociedades de Capital), a reform that made mandatory many of the rules, considered by the previous code to merely be recommendations; on the other hand, the severe economic crisis that has afflicted the companies markedly **increased the awareness of the convenience of improving the control and degree of transparency** in the management of companies, specifically in the largest companies.

Large Spanish companies have made visible progress into aligning with the global practices already anticipating the issuance of the new Code, through ever closer adherence. We find it remarkable the swift change towards better Governance mentality seen through the efforts made by Spanish companies in the last two years and are proud to be part of these achievements.

Stewardship

Stewardship was a key topic of the conference, as fundament to a constructive approach to Governance.
It has been once again underlined that effective **Stewardship benefits companies, investors and the economy** as a whole. The importance investors place on good Corporate Governance is reflected in a comprehensive and robust approach to Stewardship.

However, generally adherence to Stewardship principles by investors has been yet undetermined. As to practical steps for adopting Stewardship principles by institutional investors, **important prerequisites are to be considered**: engagement with investors should take place throughout the year, not only before the annual or a special general meeting; asset managers, aside from investment managers, should be regularly involved related to their ownership; the companies themselves must truly consider an open relationship with investors; the focus of the dialogue and both parties should be on the long-term and not only on the current context of the company.

An increasing focus of investors that relates to their Stewardship approach is placed on ESG issues. **Integrated Reporting** has become an advanced initiative in certain jurisdictions and several companies have adopted such reporting in line with the International Integrated Reporting Council (IIRC) guideline in this regard. In order to have a successful implementation, it is vital for companies to establish who has the responsibility of Integrated Reporting within the company and specifically within Board supervision of the process.

Debate around recent corporate scandals revealed the importance of **accountability of the Board**, but also **investors' accountability**. The composition of the Board in terms of skills has an important role in the proper supervision of the corporate internal processes up to monitoring of financial reporting. A common view was towards **investor constructive and regular engagement** could have been **a solution to many corporate problems**.

Engagement

A factor as well as a consequence of the Stewardship principle is the increased communication between companies and investors.

There is full agreement on the fact that public company executives are engaging institutional investors on Governance and related matters much more now than in the past. And in an increasing number of situations in which companies face particular challenges, **outside directors also are involved in engagement** efforts. These interactions, in person and by telephone, are conducted both during proxy solicitation periods and in the 'off season', the latter being of importance as companies attempt to establish relationships, sound out investors on various issues, and lay the groundwork for voting success at the annual general meeting. **Collective engagement** is also acknowledged as valuable for an effective investor dialogue with issuers.

All major current **regulatory initiatives address the importance of Stewardship and engagement**: OECD revised Corporate Governance Principles, the Shareholder Rights Directive, Transparency Directive and the Accounting Directive. The approach to engagement in Europe has been appreciated by US market representatives, the latter looking to make smaller steps in this regard.

Different approaches to litigation as a final step of any failed "engagement" process have also been discussed. The difficulties to recover money through litigation processes in many jurisdictions discourage investors to take this approach while in other countries it is considered a valid option. Investors' policies do count when evaluating the litigation for a recovery process as a final or parallel alternative to an engagement activity.

The main message of this debate is for investors to understand their issuers and also for the companies 'to know' their investors.

Boards of Directors

Board of Directors is another area that has got much attention in the past conferences, taking centre stage in the latest event as well, as the main entity responsible and accountable for good Governance.

The **variety of Board models** in Europe and beyond has been acknowledged as a major factor influencing the overall Governance context. Regulators are expected to respect such variety and not impose certain Board models, nor enhance regulatory pressure. The main principle that has been the fundament for a proper Governance model is, nevertheless, applicable across countries and across companies: the division of responsibilities between the key Governance bodies: Board and Management.

An **appropriate selection process** is critical for shaping the Board, and need to be accustomed to the industry and to the evolution of the capital market in the jurisdiction where the company is based.

A topic that enjoyed particular focus was the strengthening of the role of **Lead Independent Director**, as an essential balance to boardroom power and its role is all the more important in a context where the Chair and the CEO have dual role; however expected to promote a culture of independence within the Board and its Governance processes. Consideration is given to the variety of Board models in this regard, which call for acceptance of the dual role at companies, depending on their context; albeit not a general best practice.

The **role of the Corporate Secretary** in supporting the Board's enhanced approach to Corporate Governance has become much more advanced and this has been a very interesting topic discussed at the event. The function is encouraged to enhance knowledge of the market and investors, up to engaging with investors together with the Board. The characteristics, experience, attitudes a Corporate Secretary should have to perform efficiently its role are in effect the ones that could bring value added inside the boardroom. An interesting debate relates to the Corporate Secretary role as Board member, which is a practice at some companies in specific jurisdictions.

From our perspective, a **holistic approach seeing Investor Relations and Corporate Secretary** working closer towards higher engagement and achievement of Governance best practices is foremost key to Board efficiency.

The key message coming out from the debate sees the "Board of the future" as the one that contextualizes the activity and context of its company, one that embraces **diversity of perspectives**, that respects **independence of thinking** and that is **refreshed regularly** rather than becoming stale.

Value creation and disclosure through integrated thinking

Investors have clearly evolved their **approach to ESG portfolio** through: optimal E (Environment), S (Social), G (Governance). Companies now have a duty to follow through such expectations, and adopt appropriate mechanisms for promoting Sustainability within their own context and the overall capital markets. Boards have clear responsibilities in this area. Corporate Sustainability is a key issue of corporate governance for Boards of Directors and is on most agendas worldwide. When managed properly it enhances the competitiveness of the business and improves wealth creation.

Driving Sustainability into the company operations is a well-known goal for Sustainability departments. In contrast to traditional Governance, in order for Sustainability to become a part of everyday business, its Governance has to involve everyone's contribution to the organization, including internal and external stakeholders. But this is not so easy. It needs people who embrace Sustainability across all operations in order to generate new ways of doing things.

In order to facilitate the making of better decisions in this environment, Boards require a new role model. The **Sustainability success requires strong Governance** that sets at the tone at the top and a vision supported through policies and tools that will drive to progress in the organization.
Sustainability can truly become an embedded principle.

Shareholder rights

The main theme of the European Shareholder Rights Directive did not miss from the conference agenda. In fact, a recurring theme of the conference was the encouraging of investor long-term investment, as well as companies' adoption of mechanisms to support such approach. Some of the key points of debate have once again raised the aspect of **transparency** from the part of the company, specifically as to related party transactions and the strategic Governance and operational decisions of the company, as well as the **voting process and related communication**, in this regard the need for 'voting confirmation' being among the major expectations.

Shareholder double-voting rights have continued to raise pro- and con- arguments, the two regulations in place in France and Italy having to still justify such approach to institutional investors, which are normally considered 'minority shareholders' and who express wide concerns as to the risk of loosing their voice in the decision-making of the issuers. Other mechanism to **encourage long-term sustainable investment** need to be considered, most importantly Engagement, the keyword of the current Governance approach.

Sodali's recommendation to companies and investors
Be responsible, accountable, engage and really get to know each other.

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