

Relations with Investee Companies

Guidance on Good Practice

October 2004

RELATIONS WITH INVESTEE COMPANIES – GUIDANCE ON GOOD PRACTICE

Introduction

This paper sets out a number of examples of good practice in communicating with the boards of investee companies, which the IMA Board commends to Members. It follows discussions earlier in 2004 with the Confederation of British Industry (CBI) at which a number of concerns were expressed.

The suggestions in this paper should not be read either as a mandatory or an exhaustive list. They are intended to be examples drawn from experience which may help to facilitate good communications with the companies in which fund managers invest.

Facilitating understanding of the investment process

In certain instances, it may be necessary for managers to facilitate companies' understanding of the investment process. Examples are set out below.

- Fund managers do not act as principals but are fiduciaries acting as agents on behalf of their clients, the beneficial owners. In many cases, decisions about voting and other issues are delegated by the client to the fund manager, although some clients will give specific instructions, for example, to follow the recommendations of a particular voting service. As they act for different beneficial owners, fund managers may vote a particular block of shares different ways according to their clients' instructions.
- Different fund managers may have different views, in which case they will vote their shares different ways.
- Most company meetings with fund managers will be on issues about company strategy/performance and not longer-term stewardship and therefore are attended in the main by portfolio managers and research analysts. Fund managers often, however, employ governance experts, with voting and other agencies to assist, and in some cases these individuals may have different lines of communication with companies, for example, via the Company Secretary rather than the head of investor relations. Fund managers seek to ensure that different messages do not pass along these different channels of communication. If companies feel they do, then they should raise their concerns at an appropriately senior level (see below).
- Most corporate governance issues are not price sensitive and communication between portfolio managers and corporate governance specialists does not raise conflicts of interest. However, in the few instances when information is price sensitive and conflicts do arise, Chinese Walls operate between the corporate governance specialists and those that actively trade shares.

Providing clarity on who to contact

The fact that different individuals handle different aspects of engagement can cause confusion in that companies may be unclear as to whom enquiries should be directed and how issues relating to engagement should be escalated as and when they arise.

Managers can help this by:

- making available to companies – perhaps by publishing on their web site – a list of contacts within their firms, together with the issues each will cover;
- including in this, one individual as the nominated central contact point for companies, who is able to direct enquiries to the appropriate person to deal with, including those relating to voting matters; and
- nominating a senior member of staff (perhaps the Chief Executive or the Chief Investment Officer) as the person to whom a company Chairman or other senior individual can turn in the event of an issue having arisen which cannot be resolved otherwise.

Raising issues in a timely manner

If issues are raised in a timely manner then the parties involved may be able to resolve them easily. To facilitate this, IMA intends to discuss with the Institute of Chartered Secretaries and Administrators the development of a timetable as to when issues should be raised.

Communicating voting decisions

A particular concern of companies is that fund managers may sometimes vote against management without explaining why or vote against management when previous communications indicated they were likely to support it. This is exacerbated by the fact that, as voting is concentrated in the Spring, the timeframes for discussion are inevitably limited.

The Institutional Shareholders' Committee's Statement of Principles on the Responsibilities of Institutional Shareholders and Agents states in Section 4: "institutional shareholders and agents.....will not automatically support the board; if they have been unable to reach a satisfactory outcome through active dialogue then they will register an abstention or vote against the resolution. In both instances it is good practice to inform the company in advance of their intention and the reasons why". In addition, the Combined Code states that institutional shareholders have a responsibility to make considered use of their votes and to apply the principles set out by the Institutional Shareholders' Committee.

Specifically, therefore, fund managers could help meet these concerns by:

- agreeing to a dialogue with companies on their rationale for voting, particularly if that vote is negative (most already do this);
- alerting companies in advance to any negative vote; and
- where votes are particularly contentious, making the appropriate level of seniority available to the Chairman of the company.

Media relations

There is a widespread perception that damage can be caused to relations between companies and fund managers by public disagreement and unattributed press comments. While the circumstances by which such comments come to appear are sometimes contentious – unattributed comment in the media may not always reflect the actual words used by an individual fund manager – there is no doubt about the potential harm that can be done.

Fund managers may therefore wish to consider a written policy on media relations and a list of individuals that are authorised to speak to the media, including procedures for those not authorised to seek temporary permission to do so.