CFA Institute

STEWARDSHIP 2.0

Awareness, Effectiveness, and Progression of Stewardship Codes in Asia Pacific

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1. Executive Summary

In the investment management industry, stewardship is generally defined as the engagement by institutional investors with publicly listed companies to generate long-term value for shareowners. It is considered vital to the healthy functioning of markets, supports market integrity, improves capital allocation, and helps deliver good outcomes for their ultimate beneficiaries.

In the past decade, stewardship codes have proliferated across global markets. They are intended to provide guidance to institutional investors (including asset owners and asset managers) on how best to fulfil their responsibilities to their clients and beneficiaries and act as "stewards" of capital. They are part of the wider corporate governance framework, in which publicly listed companies are guided by corporate governance codes and institutional investors are guided by stewardship codes.

The stewardship code movement started in the United Kingdom in 2010. Since then regulators and other industry bodies across the world have put stewardship codes in place to encourage a higher level of shareholder participation in the engagement with listed companies in the expectation of better outcomes.

In general, stewardship codes take the form of several best practice principles accompanied by descriptions of how to comply with each principle. Some principles, like the following, are present in nearly all stewardship codes:

- Establishing and disclosing a stewardship policy
- Having a policy to manage conflicts of interests
- Monitoring and engaging with investee companies
- Disclosing voting policies and voting actions taken
- Reporting to clients and beneficiaries on stewardship responsibilities

The organizations that issue stewardship codes are typically government entities or industry bodies. In practice, regulators are often involved to some degree with the issuance of local stewardship codes, though the actual sponsoring entity may be an industry body. Codes are most often applied on a comply-or-explain basis, which is an elevated form of voluntary compliance. Firms that choose to adopt stewardship codes are often disclosed as signatories to a code. Such disclosure also functions as a form of positive signalling.

Academic studies so far have produced mixed results on the economic impact of complying with stewardship codes, and little has been done to examine the impact on environmental or social issues. This inevitably leads to questions on investor awareness and areas of stewardship codes that require strengthening. In Asia Pacific, for example, while regulators and industry bodies have been proactive in the adoption and development of such codes, the effectiveness of these codes remains an area of debate. Although codes are considered a component of a broader corporate governance framework, there has been no systematic regional comparison as to how aware institutional investors are of the codes and if there have been any tangible, positive outcomes from compliance with them.

This report seeks to address this gap through a survey of CFA Institute members in selected Asia Pacific markets; a review of available academic research; and discussions with stakeholders, including asset owners, asset managers, and regulators. In particular, we focus on the following areas:

- How aware of stewardship principles are investors in Asia Pacific?
- To what extent do investors engage in stewardship activities?
- Does the enforcement framework of stewardship codes need to be more stringent?
- What are the key concerns preventing investors from more widely applying stewardship principles?
- How, if at all, can stewardship codes be strengthened to improve effectiveness and to encompass environmental and social factors?

By answering these questions, this report looks to provide unique insights from the perspective of institutional investors to show how they have applied stewardship codes in their professional capacity. Given that regulators and industry bodies in Asia Pacific are reviewing existing codes or contemplating the implementation of new ones, we believe these results will be useful in guiding the development of future codes. This report aims to provide recommendations to increase the awareness and effectiveness of stewardship codes specifically within the Asia Pacific markets.

CFA Institute promotes best practices for investors around the world and has published standards and guidelines that outline ethical and professional responsibilities for asset managers and pension fund trustees, including the Asset Manager Code[1] and the Pension Trustee Code of Conduct[2]. We believe that stewardship codes play an important part in addressing the long-term needs of all stakeholders in terms of both financial goals and sustainability.

[1] CFA Institute, "Asset Manager Code," 2017, https://www.cfainstitute.org/-/media/documents/code/amc/asset-manager-code.ashx

[2] CFA Institute, "Pension Trustee Code of Conduct," 2019, https://www.cfainstitute.org/-/media/documents/code/other-codes-standards/pension-trustee-code-of-conduct-2019.ashx

Summary of Key Findings

Emerging trends

- **Sustainability and environmental, social, and governance (ESG) factors:** One of the major shifts is an increased focus on sustainability. In the updated UK Stewardship Code, which became effective in January 2020, ESG integration was elevated to a separate principle. In March 2020, the Financial Services Agency (FSA) in Japan updated its definition of stewardship, which specifically incorporates the consideration of sustainability and ESG factors. The majority of our survey respondents support incorporating sustainability into stewardship responsibilities. It should be noted that asset owners and asset managers have a fiduciary duty to clients and that incorporating a focus on sustainability should be seen to complement these duties.
- **Coverage beyond listed equities:** Another key trend is the expansion of the scope of stewardship codes to include asset classes beyond listed equity investments. The 2020 UK Stewardship Code has included specific language regarding responsibilities of fixed-income investors. Japan has also made this explicit in its 2020 revision. Although many stewardship principles are applicable for other asset classes from fixed-income to private equity, the application may not be uniform; hence it is important to provide clear guidance in order for these principles to be effective and avoid superficial compliance. The majority of our survey respondents believe that an expanded scope is appropriate.
- **Explicit reference to service providers:** In their early iterations most stewardship codes targeted only asset owners and asset managers. Increasingly the discussions have broadened to incorporate other stakeholders, including proxy advisors and investment consultants. Explicit principles for service providers have been incorporated in the United Kingdom as well as in the second EU Shareholder Rights Directive (SRD II). They are also being introduced in Japan's 2020 update. Requirements include, for example, a statement of purposes and policies for identification and management of conflicts.
- **Increased transparency and better reporting:** Reporting and disclosures have been important features in stewardship codes. So far the focus has been on disclosure of voting and engagement policies, but increasingly there is a move towards disclosure of voting records, as well as the reasons for such voting. Disclosures of conflicts are high on the priority list too. The updated 2020 UK Stewardship Code goes further in asking their signatories to focus on outcomes and effectiveness reporting, not just policies.

Issues and challenges

- **Enforcement:** One key criticism of stewardship codes is that applying the principles may turn into a box-ticking exercise. This reflects concerns that investors may maintain only superficial adherence to the principles with little actual result. As such, the enforcement of stewardship codes has been questioned ever since the UK Stewardship Code was originally issued in 2010, and considerations need to be made for a higher bar of compliance. This lays out a key debate in the application of stewardship codes: should codes remain voluntary, or is a stricter regime required?
- **Uncertain benefits:** While stewardship codes can promote best practices amongst investors, the actual benefits to beneficiaries remain unclear. As agents, asset owners and asset managers have a duty in the most basic sense to pursue economic returns on behalf of their clients. In the past, this may have included driving improvements in capital structure, dividend policy, or replacing underperforming directors. In recent years, this sense of duty has expanded to include more stakeholders, and a focus on ESG issues has now become widely expected. These benefits are relatively more difficult to quantify, given the long-term nature of these issues.
- **Cost of compliance:** Stewardship is costly. A key consideration for institutional investors is what, if any, benefits they would derive from it and how much it costs. Compliance with a stewardship code often comes down to a return-on-investment calculation. Such returns may come from an increase in value of the companies an investor engages with or from the virtue-signals and differentiating factors that would bestow a competitive advantage to an asset manager. Neither is easy to quantify, and hence this is a judgement call commercial firms have to make.
- **Ownership structure:** The high levels of ownership concentration in Asia Pacific and the low levels of institutional ownership, vis-à-vis the United States and the United Kingdom, mean that institutional investors in Asia Pacific may be less effective and less motivated when it comes to stewardship.
- **Passive investing and stewardship:** As passive investors increasingly dominate the shareholder registries of listed companies across the globe, the expectations and pressure on passive managers to be active stewards are becoming more intense. Many passive investors have expanded their resources in this area and have put in place voting and engagement policies.
- **Cultural norms and local context:** In the United Kingdom, the original UK Stewardship Code was designed to encourage institutional investors to act as responsible stewards of capital and aimed to provide checks and curbs against excessive risk-taking and short-termism behaviours that were rampant in the run up to the 2008 global financial crisis. However, not all stewardship codes have the same motivations.

Companies in Japan, for example, were widely perceived to be risk averse, and one of the motivations for the stewardship code there was to encourage more risk taking.

- **Conflict of interest:** Asset managers and service providers both serve their clients (institutional and retail fund holders) and corporate shareholders. The interests of these two sets of shareholders often diverge, however. In a utopian world client interests would always come first, but employees are likely incentivized to put their company's interests first.

Survey Results

The member survey covered a wide array of topics related to awareness, effectiveness of stewardship codes in Asia Pacific, and areas for improvement. Responses came from a broad range of respondents, the majority of which were institutional investors in the region. Some of the major takeaways are as follows:

- **Awareness:** Respondents were more skewed towards "less understanding" rather than "more understanding" of stewardship codes. They appeared to have less awareness of the specifics of local stewardship codes than of concepts of stewardship in general.
- **Engagement:** Investors generally considered stewardship principles to some extent when making investment decisions, but engagement levels were mixed. Over 50% of investors indicated an engagement frequency of quarterly or more, whereas 30% engaged only on an annual basis or less.
- **Specific principle on ESG:** Including ESG integration as a separate stewardship code principle was generally seen as having the potential to improve a firm's ESG practices. Similarly, although there is often a principle promoting collective engagement, this was not widely practiced—only one-third of respondents do so.
- **Impact:** Investors noted that stewardship had a stronger impact on corporate governance practices than did economic, environmental, or social factors, which were more similarly distributed.
- **Challenges:** The top two challenges identified by respondents were the high cost of engagement and the lack of a clear link between value creation and engagement. For investors, cost appeared to be a particular concern, whereas for the wider group the unclear link between value creation and engagement was the overriding issue.
- **Enforcement:** An overwhelming majority of respondents believed that stewardship codes should be principles-based, rather than written in statutory law. While roughly half of respondents thought the widely used "comply-or-explain" standard was suitable, over a quarter considered this level of enforcement ineffective.

- **Improvements:** Key areas noted include improvements in education, promotion, and awareness as well as better clarification and simplification of codes. Oversight and monitoring of stewardship codes by a regulator was widely seen as important, and enforcement by a government entity would likely provide a higher level of credibility.

Recommendations

CFA Institute encourages an outcomes-focused establishment or update of stewardship codes. A continuing critical eye should be placed on any stewardship code to ensure that compliance with codes truly raises the bar of engagement rather than ticking the box. Upon review of our findings, we have compiled the following recommendations when considering the creation, revision, and application of stewardship codes:

- **Aspirational standard:** Stewardship codes should remain a comply-or-explain standard and should be sufficiently monitored to ensure that signatories follow through on stated policies and represent a high professional standard. A comply-or-explain standard also allows flexibility.
- **Promotion and awareness:** Local regulators or industry bodies should ensure that institutional investors have ample opportunities to learn in detail how best to act responsibly as shareholders and apply stewardship principles in a practical manner.
- **Flexibility:** This means accommodating investors with different business models, investment strategies, and levels of resources.
- **Need for global best practices, with flexibility to cater for market differences:** Notwithstanding a high degree of overlap in stewardship principles, significant differences exist in objectives, market structures, and corporate governance frameworks across markets. Oversight bodies may wish to address the most pressing issues in their own markets when designing their codes.
- **Leading from the top:** Stewardship codes should be promoted from the highest levels of the investment chain to align incentives of all parties. In this regard, asset owners have a unique role to play in encouraging a higher level of stewardship.
- **Inclusion of ESG:** Recently updated stewardship codes have incorporated the consideration of ESG factors as a specific principle. We welcome this development. CFA institute believes that material ESG factors are key drivers of long-term value and that investors should integrate such factors in the investment process so that they and their beneficiaries benefit from a complete analysis.

2. Setting the Scene

2.1 Introduction

CFA Institute encourages shareowners globally to participate in exercising their rights as prefaced in our 2013 position paper *Shareowner Rights across the Markets*. However, each shareowner may have disproportionate abilities to effectively exercise these rights and engage with corporations. In particular, institutional investors (including asset owners and asset managers) have a critical role in exercising these duties, a function broadly known as stewardship. Furthermore, with the rise in passive investing via index funds, exchange-traded funds (ETFs), and other investment vehicles, the responsibility for voicing minority shareholder concerns increasingly falls on those institutional investors who are willing to actively engage with managements and boards. To better guide institutional investors in their stewardship activities, stewardship codes have been established as a tool to encourage a higher level of engagement and voting with listed companies, in accordance with the fiduciary duties expected of an institutional investor. Since the issue of the first stewardship code in the United Kingdom in 2010, similar codes have proliferated internationally and in a number of markets in Asia Pacific.

2.2 Definition of Stewardship

The definition of stewardship has evolved over time, but the key concept has remained consistent, which is to motivate investors to act as responsible owners by monitoring and engaging with their investee companies (or issuers) to generate long-term value for shareholders. Stewardship is increasingly seen as a way for institutional investors to discharge their fiduciary obligations, to improve long-term returns, and to enable them to exercise their governance responsibilities efficiently.[3] Variations of this definition exist, as we will see. Recently, the concept of stewardship has expanded further, with definitions now including other participants in the investment management ecosystem, such as proxy advisors, as well as making references to sustainability, or environmental, social, and governance (ESG) goals in the investment process.[4]

[3] Financial Reporting Council (FRC), "The UK Stewardship Code," July 2010, https://www.frc.org.uk/getattachment/e223e152-5515-4cdc-a951-da33e093eb28/UK-Stewardship-Code-July-2010.pdf

[4] FRC, "The UK Stewardship Code 2020," December 2019, https://www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/Stewardship-Code_Final2.pdf

2.3 Scope and Application

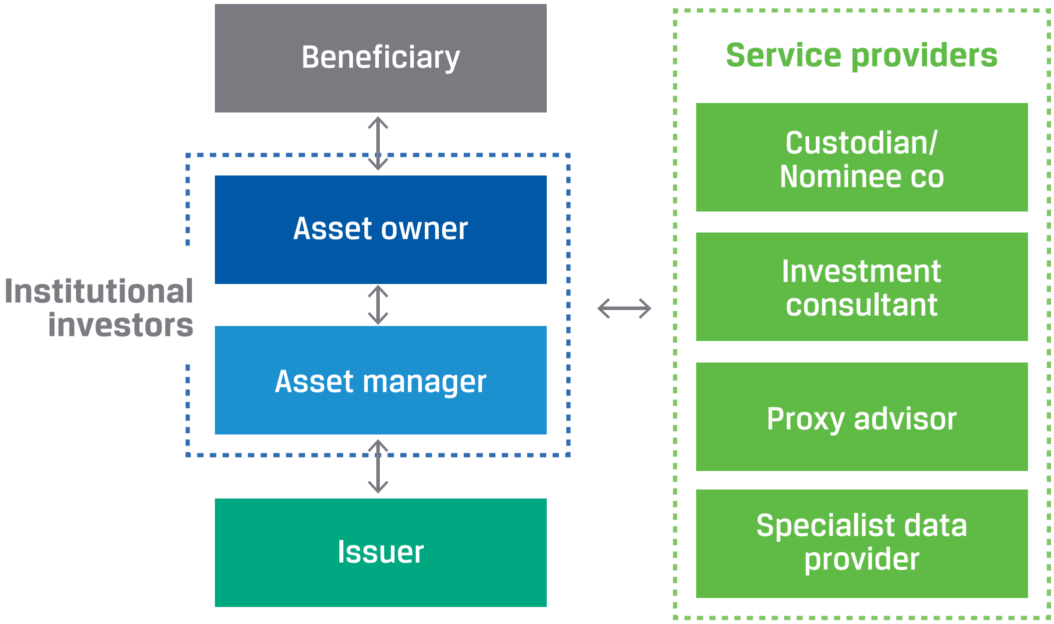
The original UK Stewardship Code was derived from the Combined Code on Corporate Governance and was then envisaged as a key component in the broader reforms in corporate governance. Where companies are expected to follow best practices for corporate governance, investors are expected to follow best practices for stewardship. Stewardship is vital to the healthy functioning of markets—it supports market integrity, improves capital allocation, and helps deliver good outcomes for end beneficiaries. The investment community performs an important role in allocating the capital accumulated by savers to useful, rewarding enterprises that will provide a return to such capital providers.

In this light, stewardship codes are counterparts to corporate governance codes (to which listed companies adhere). They are designed to provide investors, in their role as "stewards" of capital, with guidance on how best to fulfil their responsibilities to their clients and beneficiaries. They typically apply to institutional investors—that is, asset managers who are investing funds that ultimately belong to someone else and asset owners such as insurance and pension funds. Like corporate governance codes that aim to reduce friction between agents (boards and management) and principals (shareholders) in companies, stewardship codes aim to reduce friction between agents (institutional investors) and principals (clients and ultimate beneficiaries) in investing.

While stewardship codes can be applied to non-institutional investors, in practice most stewardship codes target only these agents that are subject to a certain standard for duty of care. This applies not just to asset owners and asset managers but also to others in the broader investment community, and hence the recent trend to extend its application to service providers such as proxy advisors and investment consultants.[5] However, stewardship codes do not generally apply to retail investors.

[5] FRC, "The UK Stewardship Code 2020."

Chart 1: Institutional Investment Ecosystem



Source: Adapted from Financial Conduct Authority, "Building a Regulatory Framework for Effective Stewardship: Feedback to DP19/1."

Chart 1 shows the key participants in an investment management community. Each participant has a unique function:

- **Asset owners:** These are typically defined as managed collective pools of capital that include pension funds, insurance firms, and investment trusts. Clients and beneficiaries of asset owners are the ultimate stakeholders. Some asset owners manage their own portfolios, but many also hire institutional asset managers. Hence, in the stewardship discussion, asset owners have an important role in determining broader changes in behaviour amongst asset managers (where appropriate) and promoting more engagement in a way that is consistent with their fiduciary obligations.

- **Asset managers:** They have direct responsibility for portfolio management and making day-to-day investment decisions. This is where they can have a direct impact on their investee companies through engagement with company management and voting decisions. Each investment mandate is different, and it is incumbent upon asset owners and asset managers to clearly set out the expectations in relation to stewardship and engagement.
- **Service providers:** To fulfil their duties, asset owners and asset managers may use service providers such as investment consultants, proxy advisors, and data providers. Increasingly, stewardship is seen to cover the role of service providers as well. In the updated 2020 UK Stewardship Code, for example, signatories who are service providers not only have to explain their purposes, how they go about promoting effective stewardship, and how they identify conflicts of interest vis-à-vis their clients; they have also been asked to explain "how they have identified and responded to market-wide and systemic risks, as appropriate."[6]

2.4 Components of Stewardship Codes

2.4.1 Key principles

Typically, stewardship codes take the form of best practice principles accompanied by descriptions of how to comply with each principle. Some principles are present in nearly all stewardship codes. These include

- establishing and disclosing a stewardship policy,
- having a policy to manage conflicts of interests,
- monitoring and engaging with investee companies,
- disclosing voting policies and voting actions taken, and
- reporting to clients and beneficiaries on stewardship responsibilities.

Other principles are present in some markets but not others; these include

- participating in collective engagement,
- establishing a policy for escalation of engagement,
- integrating environmental and social risks and opportunities,
- identifying and responding to market risks and financial systems, and
- reviewing internal governance procedures.

[6] FRC, "The UK Stewardship Code 2020."

Principles that are not present in one code may have been combined into the description of a different principle. This is often the case with principles for monitoring, engagement, collective action, and escalation. Similarly, ESG-related principles are often included in the local definition of stewardship or within the description of engagement.

2.4.2 Oversight

There are two areas to consider with regards to the oversight of stewardship codes: the governing body and the compliance mechanism.

Governing body (or sponsor): This is generally the organization that has issued the stewardship code and is typically a government entity, a regulator, or an industry body. While the first stewardship code was issued by the Financial Reporting Council (FRC) in the United Kingdom, a regulatory body that has oversight for accountants, auditors, actuaries, and the corporate governance system, the predecessor to the UK Stewardship Code was issued by the Institutional Shareholders' Committee (ISC), an industry body. In practice, regulators are often involved to some degree, though the actual sponsoring entity may be an industry body.

In addition to developing and issuing a code, an active governing body would also engage with stakeholders, encourage adoption and adherence, and review the code periodically to ensure its relevance. The nature, attitude, and approach of the governing body have an important impact on the degree of adoption as well as the level of compliance.

Compliance: There are broadly three degrees of compliance with regards to stewardship codes: mandatory, comply-or-explain, and voluntary.

- **Mandatory:** A mandatory compliance requirement for stewardship codes is rare because it is often difficult in practice to set a mandatory compliance standard, given the wide range of business models of the entities for whom the codes are intended.
- **Comply-or-explain:** This is the most common method of application. It is a form of soft law and allows a flexible mandate for each firm to apply the principles in a way that is most appropriate to its circumstances. Relative to a voluntary standard, comply-or-explain sets a higher bar for compliance, given the request to explain reasons for non-compliance.

- **Voluntary:** Voluntary adoption means there is no specified enforcement of compliance. Often when applied to stewardship codes, voluntary adoption is accompanied by a recommendation to explain reasons for non-compliance, which effectively makes the application of the code a comply-or-explain standard. One reason a voluntary application may be set out is to avoid confusing the stewardship code with a statutory law that has specific regulatory consequences.

Compliance standards have been evolving. In the recently updated 2020 UK Stewardship Code, the FRC now promotes "apply-and-explain." This is an elevated form of the previous comply-or-explain application. Firms that follow the code will now be asked to describe how the practices they have implemented achieved the intent of the principles and what outcomes were achieved. By focusing on explanations and results, the apply-and-explain standard aims to raise the effectiveness of stewardship codes. Though rare, instances of mandatory compliance are growing—for example, in Australia and most recently in India.

2.4.3 Signatories

Some codes invite followers to sign up, and the number of signatories can be seen as an indicator of the momentum behind a certain set of principles. Being a signatory to a code allows firms to demonstrate support and can send important market signals to clients and service providers. In Asia Pacific names of signatories to local codes are publicly available in Australia, Japan, Korea, Malaysia, Taiwan, and Thailand. Similarly, firms often sign up to global codes such as the Principles for Responsible Investment (PRI) or the Asset Manager Code established by CFA Institute. Governing bodies are careful to note that being a signatory does not equate to compliance or an endorsement by them.[7]

A tiering of signatories was introduced in 2016 in the United Kingdom to distinguish the reporting quality of signatories and to encourage firms in the bottom tier, with lower quality reporting, to make improvements. Given the mixed results, the bottom tier was eventually removed.[8] This raised concerns that tiering could actually disincentivize firms from adopting the code.[9]

[7] FRC, "Tiering of 2012 Stewardship Code Signatories," 2016, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements

[8] "Beacon of British Stewardship Needs a Brighter Flame," *Financial Times*, accessed 7 May 2020, https://www.ft.com/content/1a3a57be-5c15-3e03-bae0-10bd5804bf20

[9] Susanna Rust, "FRC Scraps Lowest Category of Stewardship Code Reporting Ranking," *IPE Magazine*, 3 August 2017, https://www.ipe.com/frc-scraps-lowest-category-of-stewardship-code-reporting-ranking/10020107.article

2.4.4 Asset classes

Because of the association of stewardship with engagement and voting, hitherto stewardship codes have mostly been applied to holders of listed equity. The 2012 revision to the UK Stewardship Code made this explicit:[10]

"The Code is directed in the first instance to institutional investors, by which is meant asset owners and asset managers with equity holdings in UK listed companies."

Other codes have adopted a similar stance and focused on listed equity, given that principles like voting and disclosure may not be as relevant to other asset classes such as fixed income.

Nevertheless, an emerging trend is for the scope to be broadened to include fixed income, private equity, infrastructure, and other asset classes. The UK Stewardship Code 2020 acknowledged that investments in various asset classes have different terms, investment horizons, rights, and responsibilities, and hence it is important to allow sufficient flexibility for different firms to exercise stewardship and meet expectations in ways aligned with their own business models and investment strategies. Further, it provides instructions on how to apply certain principles to investors of other asset classes (e.g., managers of fixed income investments). For example, by establishing covenants in indenture agreements to protect their creditor rights, fixed-income investors can influence an investee company's governance and advance strong stewardship practices.

[10] FRC, "The UK Stewardship Code," September 2012, https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf

3. Origins and Development of Stewardship Codes

3.1 United Kingdom

While the underlying concepts of stewardship and the monitoring role of institutional investors are not new, the adoption of defined principles as set out by regulators or industry bodies has been in existence only in the last decade. The first regulatory backed stewardship code started in the United Kingdom in 2010. Its predecessor was the Code on the Responsibilities of Institutional Investors, issued by the ISC, which had existed in some form since 1991.[11] The initial principles drafted by the ISC were specific to how institutional investors engaged in shareholder activism, which is arguably a different focus than the current concept of stewardship. These principles evolved over time to encompass most of the core concepts found in stewardship codes globally today.

The 2008 global financial crisis threw the need for responsible engagement into sharp relief—by acting as responsible stewards of capital, and by dealing with company underperformance, institutional investors (including asset owners and asset managers) can check and curb excessive risk-taking and short-termism behaviours. In light of the critical loss and failure experienced by the banking system as a result of the global financial crisis, the British government commissioned Sir David Walker to review and examine the corporate governance of banks and financial institutions in the United Kingdom. The ensuing review (the Walker Review), published in November 2009, provided recommendations under five headings, including composition and size of the board, board dynamics and evaluation of performance, institutional shareholder engagement, governance of risk, and remuneration. Institutional shareholder engagement was seen as an important component to prevent a recurrence of the banking crisis, since in the period leading to the crisis "there appears to have been a widespread acquiescence by institutional investors and the market in the gearing up of balance sheets of banks as a means of boosting returns on equity."[12] Had there been robust scrutiny and engagement by institutional investors, the

[11] UK Parliament, Select Committee on Trade, "Appendices to the Minutes of Evidence," 13 May 2003, Appendix 8, https://publications.parliament.uk/pa/cm200203/cmselect/cmtrdind/439/439ap09.htm

[12] David Walker, "A Review of Corporate Governance in UK Banks and Other Financial Industry Entities," November 2009, Recommendation 1, https://webarchive.nationalarchives.gov.uk/+/www.hm-treasury.gov.uk/d/walker_review_261109.pdf

worst excesses may have been prevented. Hence, a separate code for shareholder stewardship was proposed and specifically noted:

"The Code on the Responsibilities of Institutional Investors, prepared by the Institutional Shareholders' Committee, should be ratified by the FRC and become the Stewardship Code."[13]

Importantly, the Walker Review recommended that the UK Stewardship Code be a "statement of best practice" to be applied on a comply-or-explain basis. This level of compliance would become widely replicated in stewardship codes of other jurisdictions. Further, it was acknowledged that independent and credible monitoring was required, and a related recommendation was that the FRC's remit be extended to cover the development of stewardship activities. The FRC formally released the UK Stewardship Code in July 2010. Subsequently amended in September 2012, it became the cornerstone version for the majority of stewardship codes throughout Asia Pacific. In 2016, motivated by a desire to raise standards and to differentiate signatories' commitment to the principles, the FRC introduced a tiering structure for signatories.[14] Signatories were tiered according to reporting quality; those in the bottom tier were encouraged to make improvements.

In 2018, following accounting irregularities and collapses of high-profile companies such as Carillion, Patisserie Valerie, and BHS, the British government ordered a review of the FRC. The resulting review by Sir John Kingman (the Kingman Review) not only examined issues in relation to audit regulation, audit quality, and corporate reporting but also reviewed the effectiveness of FRC's stewardship function. The Kingman Review concluded that the "Stewardship Code, whilst a major and well-intentioned intervention, is not effective in practice" and recommended a fundamental shift in approach to "more clearly differentiates excellence in stewardship" and to "focus on outcomes and effectiveness, not on policy statements."[15]

Following the Kingman Review, the FRC engaged in a broad consultation with stakeholders and in October 2019 introduced the UK Stewardship Code 2020, a significant revision of the previous code, to address several of the criticisms noted in the Kingman Review.

[13] Walker, "A Review."

[14] FRC, "Tiering of 2012 Stewardship Code Signatories," 2016, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements

[15] John Kingman et al., "Independent Review of the Financial Reporting Council," OGL, December 2018, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/767387/frc-independent-review-final-report.pdf

3.2 The Second EU Shareholder Rights Directive

The second EU Shareholder Rights Directive, dubbed "SRD II," became effective in June 2019. SRD II focuses on shareholder rights as well as shareholder responsibilities. It seeks to encourage long-term shareholder engagement by imposing greater transparency on shareholder engagement activities, asset management mandates, and investment strategies. The underlying objectives are to

- contribute to the long-term sustainability of EU companies,
- enhance the efficiency of the chain of intermediaries, and
- encourage long-term shareholder engagement.[16]

Key SRD II requirements include, among others, disclosures of

- engagement policies with investee companies, including an annual report of the implementation of such policies, details of engagement, and voting behaviour; and
- how institutional investors take the long-term interests of their beneficiaries into account and how asset managers are incentivized to do so.

These rules are based on a comply-or-explain approach, although institutional investors are not obliged to vote or engage. Like institutional investors, proxy advisors are required to disclose key information about the preparation of their recommendations and advice and to report on the application of their codes of conduct.

3.3 Asia Pacific

The adoption of the first UK Stewardship Code in 2010 inspired a number of markets in Asia Pacific to follow suit. In February 2014, as part of a wider structural, economic reform to focus on the creation of shareholder value, Japan became the first market in Asia Pacific to introduce a stewardship code. In just over four months, nearly 130 institutional investors in Japan became signatories, including Japan's Government Pension Investment Fund, the largest pool of retirement savings in the world. In the same year, The Malaysian Code for Institutional Investors was launched jointly by the Securities Commission Malaysia and the Minority Shareholders Watch Group. Between 2016 and 2017, as shown in **Chart 2**, a flurry of activity took place in this space, with codes adopted in Hong Kong SAR (March 2016), Taiwan (June 2016), Singapore (November 2016),

[16] European Commission, "Shareholders' Rights Directive Q & A," 14 March 2017, https://ec.europa.eu/commission/presscorner/detail/en/MEMO_17_592

Thailand (February 2017), India (March 2017), South Korea (March 2017), and Australia (July 2017).

3.4 Rest of the World

While the United Kingdom was the first jurisdiction to release a regulatory backed stewardship code in 2010, similar sets of principles, such as the ISC principles, were available globally before the issuance of the UK Stewardship Code. The Canadian Coalition for Good Governance has since 2005 maintained principles on shareholder engagement, which were updated as Stewardship Principles in 2017. Similarly, on a global basis the International Corporate Governance Network (ICGN) has maintained a Statement of Principles for Institutional Investor Responsibilities, dating back to 2003,[17] which was updated as the ICGN Global Stewardship Principles in 2016. That said, the spread of "stewardship" codes rather than "responsible investor" principles did not occur until after the release of the UK Stewardship Code in 2010. Since then, several markets have followed with codes developed by industry bodies as well as regulators.

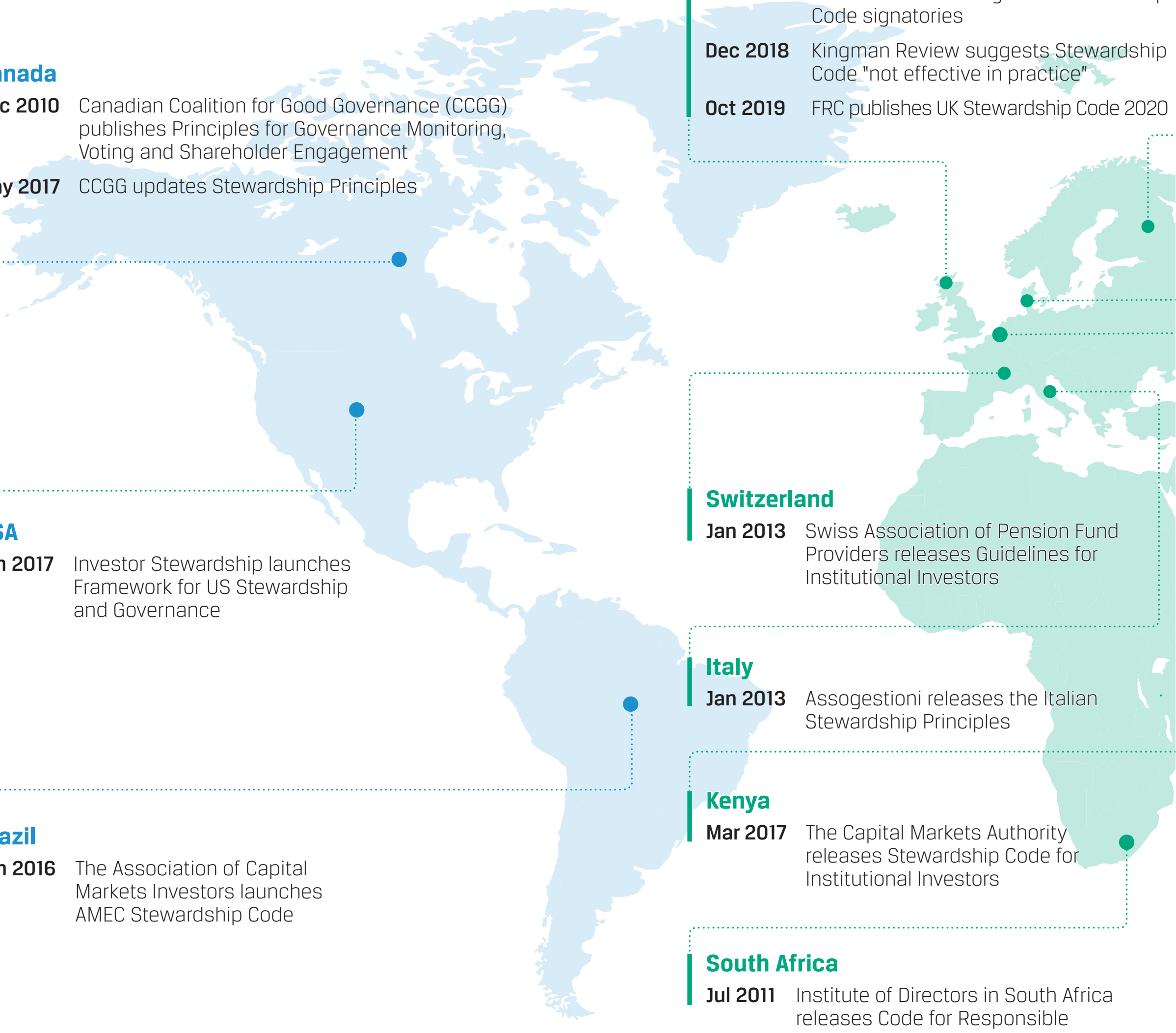
In the United States, a coalition of investors launched the Framework for US Stewardship and Governance (the Framework) in the 2017. The Framework provides a set of corporate governance and stewardship principles for institutional investors in the United States, covering areas such as being accountable to their beneficiaries, disclosure of conflicts of interest, proxy voting, and constructive engagement.

In Europe, the European Fund and Asset Management Association (EFAMA) released their EFAMA Stewardship Code in 2011. This was followed by industry bodies in European markets such as Norway (2012), Italy (2013), and Switzerland (2013). The Institute of Directors, an industry body in South Africa, was also early to adopt a code, in 2011. As of May 2020, the ICGN noted 22 stewardship codes that are active globally.[18]

[17] International Corporate Governance Network (ICGN), "ICGN Global Stewardship Principles," 2016, https://www.icgn.org/sites/default/files/ICGNGlobalStewardshipPrinciples.pdf

[18] ICGN, Global Stewardship Codes Network, accessed 13 May 2020, https://www.icgn.org/policy/global-stewardship-codes-network

Chart 2: Development of stewardship codes



Canada

Dec 2010 Canadian Coalition for Good Governance (CCGG) publishes Principles for Governance Monitoring, Voting and Shareholder Engagement

May 2017 CCGG updates Stewardship Principles

USA

Jan 2017 Investor Stewardship launches Framework for US Stewardship and Governance

Brazil

Jun 2016 The Association of Capital Markets Investors launches AMEC Stewardship Code

United Kingdom

Nov 2009 Walker Review recommendation for Stewardship Code published

Jul 2010 The Financial Reporting Council (FRC) publishes UK Stewardship Code

Sep 2012 UK Stewardship Code revised

Nov 2016 FRC introduces tiering of UK Stewardship Code signatories

Dec 2018 Kingman Review suggests Stewardship Code "not effective in practice"

Oct 2019 FRC publishes UK Stewardship Code 2020

Switzerland

Jan 2013 Swiss Association of Pension Fund Providers releases Guidelines for Institutional Investors

Italy

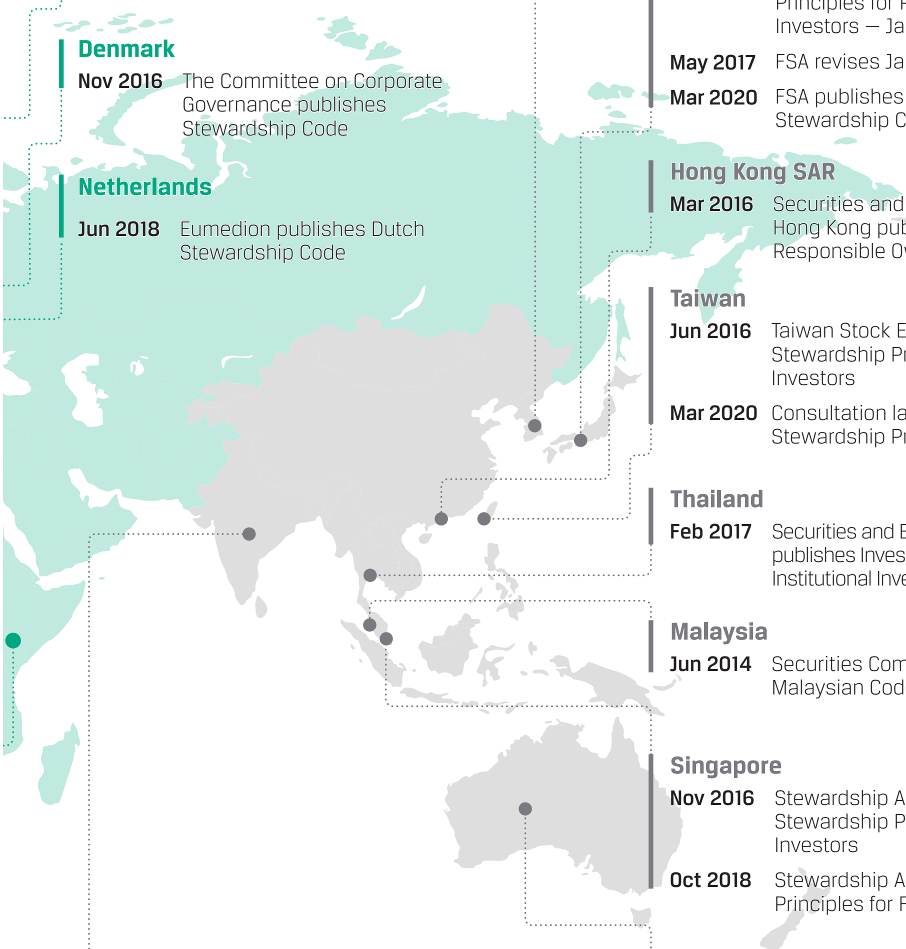
Jan 2013 Assogestioni releases the Italian Stewardship Principles

Kenya

Mar 2017 The Capital Markets Authority releases Stewardship Code for Institutional Investors

South Africa

Jul 2011 Institute of Directors in South Africa releases Code for Responsible Investing in South Africa



European Union

Apr 2011 European Fund and Asset Management Association (EFAMA) launches EFAMA Code for External Governance

Apr 2018 EFAMA revises Code for External Governance, renames to EFAMA Stewardship Code

Denmark

Nov 2016 The Committee on Corporate Governance publishes Stewardship Code

Netherlands

Jun 2018 Eumedion publishes Dutch Stewardship Code

India

Mar 2017 Insurance Regulatory and Development Authority releases Guidelines on Stewardship Code for Insurers

Dec 2019 Security and Exchange Board of India releases Stewardship Code for mutual funds

South Korea

Dec 2015 Financial Services Commission Korea issues draft Stewardship Code

Dec 2016 Korea Corporate Governance Service publishes Stewardship Code

Japan

Apr 2014 Financial Services Agency (FSA) publishes Principles for Responsible Institutional Investors — Japan's Stewardship Code

May 2017 FSA revises Japan's Stewardship Code

Mar 2020 FSA publishes 2020 revision to Japan's Stewardship Code

Hong Kong SAR

Mar 2016 Securities and Exchange Commission of Hong Kong publishes the Principles of Responsible Ownership

Taiwan

Jun 2016 Taiwan Stock Exchange launches Stewardship Principles for Institutional Investors

Mar 2020 Consultation launched to update the Stewardship Principles

Thailand

Feb 2017 Securities and Exchange Commission Thailand publishes Investment Governance Code for Institutional Investors

Malaysia

Jun 2014 Securities Commission Malaysia launches Malaysian Code for Institutional Investors

Singapore

Nov 2016 Stewardship Asia launches Singapore Stewardship Principles for Responsible Investors

Oct 2018 Stewardship Asia launches Stewardship Principles for Family Businesses

Australia

Jul 2017 Financial Services Council (FSC) releases FSC Standard 23: Principles of Internal Governance and Asset Stewardship

May 2018 Australian Council of Superannuation Investors releases Australian Asset Owner Stewardship Code

4. Implementation Issues and Practical Realities

4.1 Overview

Even after a decade of existence, stewardship codes remain at the center of much debate over their effectiveness and the purpose they serve in society. Perhaps the most critical verdict came in the FRC's 2018 Kingman Review, which noted that

"the Code remains simply a driver of boilerplate reporting, serious consideration should be given to its abolition."[19]

One criticism of stewardship codes is a lack of enforcement. As mentioned in the previous section, most of these codes are voluntary. While some believe that having a set of clearly defined principles concerning company monitoring, voting, and engagement has much value, others doubt that institutional investors would voluntarily acquiesce to a stewardship code without the threat of penalties or sanctions.

Another concern involving stewardship codes is that investors will only maintain superficial adherence to the principles, with few concrete outcomes directly attributable to their stewardship efforts or benefitting their clients. Without such outcomes, questions inevitably arise about the cost-effectiveness and commercial benefits of stewardship activities. Investors who put resources behind stewardship and make genuine, systematic efforts in engagement do not stand to capture all the value they create. Rather, some of it will accrue to other shareholders too, giving rise to the issue of free riding.

The underlying ownership structure of each market is also an important consideration. Publicly listed companies in the United States and in the United Kingdom have dispersed shareholders and a higher percentage of institutional shareholders than do those in Asia Pacific. Listed companies in Asia Pacific tend to have concentrated ownerships either by families, states, or other corporations, which are arguably engaged owners. The introduction of dual-class share structures (in which some shareholders enjoy super voting rights) in the region further renders active engagement by institutional shareholders inconsequential.

[19] Kingman et al., "Independent Review," p. 10.

Can passive investors be active shareholders? The debate arising from this question continues to develop as passive investors increasingly dominate the shareholder registries of listed companies worldwide and the expectations and pressure on passive managers to be active stewards are becoming more intense. Many passive investors have expanded their resources in this area and are putting in place voting and engagement policies, amid skepticism over some of the issues highlighted here, such as costs and benefits.

Different markets may also have different objectives when introducing stewardship codes. For example, in the United Kingdom, the UK Stewardship Code was designed to motivate institutional investors to become responsible and engaged shareholders and curb excessive risk taking. In Japan, however, the aim was to promote a focus on increasing shareholder value,[20] which came as part of the government's wider structural and economic reform. Hence, the local context is important, and each market will have its own motivations and considerations.

Asset managers and service providers serve both their clients (institutional and retail fund holders) and their corporate shareholders, and the interests of these two sets of shareholders diverge. In a utopian world, client interests would always come first; but in the real world, how are conflicts of interest really being managed?

In this section we take a closer look at the following issues:

- Enforcement
- Uncertain benefits
- Cost of compliance
- Ownership structure
- Passive investing and stewardship
- Cultural norms and local context
- Conflict of interest

[20] Gen Goto, "The Logic and Limits of Stewardship Codes: The Case of Japan," NUS Centre for Asian Legal Studies Working Paper 18/08, November 2018, https://law.nus.edu.sg/cals/pdfs/wps/CALS-WPS-1808.pdf

4.2 Enforcement

As regulators seek to rachet up the level of reporting obligations in stewardship codes, how best to enforce such principles has been a much discussed question. Some are arguing for stronger oversight and a "more intrusive approach to shareholder engagement."[21] Stewardship Asia Centre, a Singapore-based stewardship think tank and the sponsor of the Singapore stewardship code, believes that this sort of compliance turns into a box-ticking exercise rather than promoting real engagement.[22]

Much of this comes down to the degree of enforcement. At their core, stewardship codes are a set of best practices for institutional investors to follow. The application of a comply-or-explain framework is primarily to address the wide disparity in business models and resources of institutional investors. Comply-or-explain provides flexibility for investors to follow the principles that apply within their own capabilities. This in turn broadens the range of investors to whom stewardship codes may apply. In its review of the previous UK Combined Code, the FRC found strong support for a comply-or-explain approach to corporate governance from companies as well as investors. However, they also noted concerns regarding the quality and effectiveness of engagement between institutional investors and boards of listed companies.[23]

Stewardship codes, whether under a voluntary or comply-or-explain regime, require a strong degree of self-regulation to attain effective results.[24] In this sense the current stewardship codes are inherently structured as aspirational standards rather than statutory law. They provide an opportunity for investors to differentiate themselves from peers by reporting a high degree of adherence. By engaging in a strategic and meaningful manner with its investee companies, an institutional investor may be able to demonstrate influence, with potential positive outcomes and commercial benefits for its clients. This is the proverbial "carrot" in the "carrot and stick" metaphor.

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[21] Brian Cheffins, "The Stewardship Code's Achilles' Heel," *The Modern Law Review* 73, no. 6 (2010): 40, https://onlinelibrary.wiley.com/doi/abs/10.1111/j.1468-2230.2010.00828.x

[22] Didier Cossin, Sophie Coughlan, and Ong Boon Hwee, "Stewardship: Fostering Responsible Long-Term Wealth Creation," Stewardship Asia and IMD Global Board Center, 2016, p. 27, http://www.stewardshipasia.com.sg/sites/default/files/Stewardship-%20Fostering%20Responsible%20Long-term%20Wealth%20Creation%20(SAC)%202016.pdf

[23] FRC, "2009 Review of the Combined Code: Final Report," December 2009, https://www.frc.org.uk/getattachment/31de1771-1020-4568-9b22-ab95796a1da5/2009-Review-of-the-Combined-Code-Final-Report1.pdf

[24] Andrew Keay, "Comply or Explain: In Need of Greater Regulatory Oversight?" SSRN, 10 September 2012, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2144132

Another aspect of the "carrot" is the power of clients and consumers. Asset owners' focus on engagement and voting will in turn motivate asset managers to step up their efforts in this area. By demonstrating to the market that they are taking stewardship seriously and investing appropriately in this area, asset managers may create a competitive advantage that will be good for business.

How does the "stick" work, then? Stewardship codes as "a stick" have yet to be widely tested, as specific regulatory consequences for non-compliance are not typically specified. That said, the level of enforcement by governing bodies of stewardship codes appears to be on the rise. The updated UK Stewardship Code 2020 has shifted the focus of reporting from disclosure of policies to an activities and outcomes report wherein signatories to the code are expected to detail their results from engagement. This has raised the bar for compliance, which is now described as "apply-and-explain." At this moment it is too early to determine whether the shift to outcomes-based reporting will have a significant impact on the effectiveness of the UK Stewardship Code, but at least the shift reflects that the FRC is taking a more hands-on approach to enforcement. In Asia Pacific, there are instances of some form of mandatory compliance in markets such as Australia and most recently in India.

4.3 Uncertain Benefits

While stewardship codes can promote best practices amongst institutional investors, the actual benefits to beneficiaries derived from such compliance remain unclear. As agents, asset owners and asset managers have a duty in the most basic sense to pursue economic returns on behalf of their clients. In the past, this may have included driving improvements in capital structure, steering dividend policy, or replacing underperforming directors. In recent years, this sense of duty has expanded to cover other stakeholders, and a focus on ESG goals has now become widely expected.

4.3.1 Economic value

On an economic level, academic research on the impact of stewardship codes has been inconclusive. A Bond University report on the economic impact from compliance with the UK Stewardship Code finds that

"Code compliance by institutional investors does not strengthen the influence of institutional investors on investee companies such that they obtain a higher quality of reported earnings."[25]

However, a separate study by the Research Institute of Economy, Trade and Industry in Japan, using a wider global dataset, argues a different conclusion. Focusing on the monitoring effect of institutional investors, the authors conclude that

"stewardship codes enhance monitoring by institutional investors, and the enhanced monitoring in the post-code-introduction period improves the value of firms with high institutional ownership."[26]

At this stage, whether stewardship codes in and of themselves provide positive economic value remains inconclusive. One reason is that stewardship is typically defined as the pursuit of long-term improvements that could take several years to play out. A multi-decade study over several economic cycles would provide better evidence of the economic impact of stewardship codes, but the data for this do not yet exist.

4.3.2 ESG considerations

Focus on including ESG considerations in stewardship has been increasing. This was most recently noted in the 2020 UK Stewardship Code, which incorporates "sustainable benefits for the economy, the environment and society" into the definition of stewardship. This, however, generated a great deal of debate during the consultation process, and in its feedback statement the FRC noted:[27]

"Approximately half of respondents commented that the primary purpose of stewardship is to deliver financial returns for clients. They acknowledged that in doing so there may be positive impacts for the economy and society, but that they did not see creating sustainable value for the economy and society as the primary aim of investor stewardship."

[25] Chun Lu, "Does Compliance with the UK Stewardship Code by Institutional Investors Enhance Investee Earnings Quality?", Bond University, Australia, 2016, https://pure.bond.edu.au/ws/portalfiles/portal/36100506/Chun_Lu_Thesis.pdf

[26] Yutaro Shiraishi et al., "Stewardship Code, Institutional Investors, and Firm Value: International Evidence," RIETI Discussion Paper Series 19-E-077, September 2019, https://www.rieti.go.jp/jp/publications/dp/19e077.pdf

[27] FRC, "Consulting on a Revised UK Stewardship Code," Feedback Statement, October 2019, p. 4, https://www.frc.org.uk/getattachment/2912476c-d183-46bd-a86e-dfb024f694ad/200206-Feedback-Statement-Consultation-on-revised-Stewardship-Code-FINAL-(amended-timetable).pdf

The impact of stewardship codes on improving issuers' ESG performance is even more difficult to ascertain. Only some stewardship codes explicitly include ESG either as part of the definition of stewardship or as one of the principles of the code. This trend does appear to be shifting, as seen in the revisions to codes in the United Kingdom and other markets. Also, given that the current debate on how best to measure and quantify ESG impact is ongoing, the framework to evaluate stewardship codes under these criteria remains unclear.

That said, governance impacts are expected to be the most evident, given that stewardship codes promote engagement with company management. This could, in theory, be witnessed more immediately via voting activities and other forms of shareholder activism. This creates a paradox: those institutional investors at the forefront of stewardship are sometimes deemed activist investors and seen as "bullying and short-termist, dangerous to the industry,"[28] when the essence of stewardship codes is to focus investors on longer-term results. This debate has yet to be settled, with one study describing this situation as "a Manichean divide"[29]—that is, as a black-and-white issue. Regardless, stewardship code adoption should most directly affect an investee company's governance practices, which is also why stewardship codes are typically part of the wider corporate governance framework.

4.4 Cost of Compliance

For many institutional investors, as commercial, for-profit organisations, whether and how they adhere to a stewardship code comes down to incentives, or put simply, to return on investments. Lucian Bebchuk argues that "investment managers bear the costs of stewardship activities, but capture only a small fraction of the benefits they create."[30] This creates the issue of free riding, where some asset managers may have less incentive to allocate resources on active engagement with issuers if they receive the benefits from their peer group already engaging with the same set of issuers. The FRC and the FCA have identified this issue as one of the key challenges to stewardship codes, noting that some

[28] Jennifer G. Hill, "Good Activist/Bad Activist: The Rise of International Stewardship Codes," *Seattle University Law Review* 41, no. 2 (2018): 502, https://researchmgt.monash.edu/ws/portalfiles/portal/278144661/278144617_oa.pdf

[29] Hill, *Good Activist*, p. 27.

[30] Lucian A. Bebchuk, Alma Cohen, Scott Hirst, "The Agency Problems of Institutional Investors", Journal of Economic Perspectives, Summer 2017, https://www.jstor.org/stable/44321281?seq=1#metadata_info_tab_contents

investors "may not invest as fully as they otherwise might and instead 'free-ride' on the stewardship of others."[31]

Yet free riding should be a secondary consideration. As discussed, stewardship codes should at their core be aspirational standards. Free riding can then coexist with stewardship codes, as the goal should not be for every institutional investor to follow the codes, but for those that choose to follow the codes to do so effectively and uphold a higher standard. Those that can meet this standard should then be deemed responsible stewards of capital, with a strong reputation, which will in turn differentiate them from free-riding firms. Publishing public signatories is therefore an important stewardship role, providing marketing incentive for firms to comply beyond explicit financial cost-and-benefit considerations. In some markets, investors are encouraged to collaborate and pool resources. With a critical mass of investors engaging in effective stewardship, the problem of free riding could be mitigated.

Similarly, asset management firms looking to comply with several stewardship codes in different jurisdictions have an additional burden. As investing has become increasingly global, local funds do not necessarily invest only in local companies. Such funds then need to prepare stewardship reports that meet the requirements for each local jurisdiction they invest in so that they comply with local stewardship guidelines. This could pose both an administrative and a financial burden for smaller firms with limited resources. Although sometimes language in certain national stewardship codes allows for other codes to fulfil local disclosures requirements (e.g., Korea), typically certain items in each national code are unique to that jurisdiction. Establishing a more widely recognized core set of stewardship principles and supplementary principles for each jurisdiction could aid in simplifying the compliance process and allowing a wider range of firms to adopt stewardship principles.

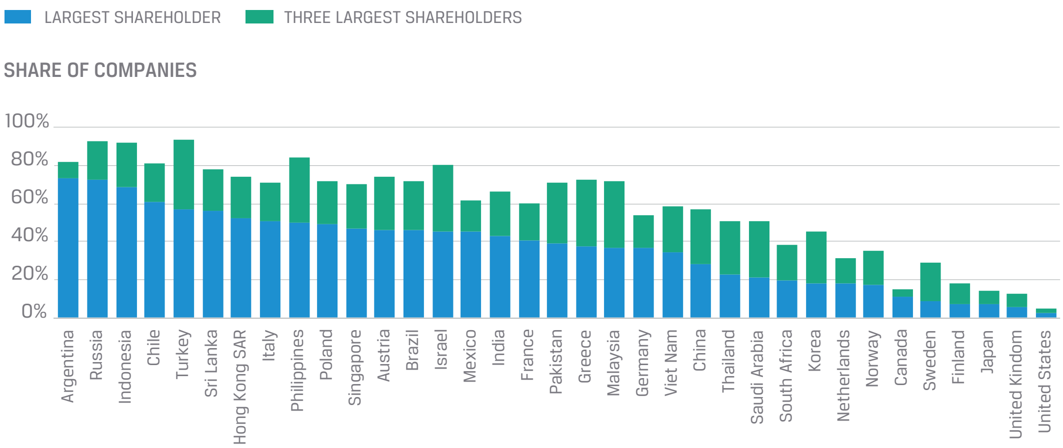
4.5 Ownership Structures

In Asia Pacific, there have historically been various forms of concentrated ownership, whether as chaebols in Korea, cross-shareholdings in Japan, or family and state ownership in Singapore and Hong Kong. This contrasts with the low levels of ownership concentration in the United States and the United Kingdom. According to the OECD, the proportion of US and UK listed companies with the largest shareholder, or the top three shareholders, holding more than half of equity is the lowest of the markets studied. The OECD data in **Chart 3** also show that ownership concentration levels in Hong Kong and Singapore are among the highest in Asia Pacific. This reflects the potential for a handful

[31] Financial Conduct Authority (FCA) / FRC, "Building a Regulatory Framework for Effective Stewardship", Discussion Paper, January 2019, p. 9, https//www.fca.org.uk/publication/discussion/dp19-01.pdf

of owners, typically governments or private individuals, to wield outsized influence on corporate decisions and could limit the effectiveness of stewardship activities.

Chart 3: Ownership concentration by market

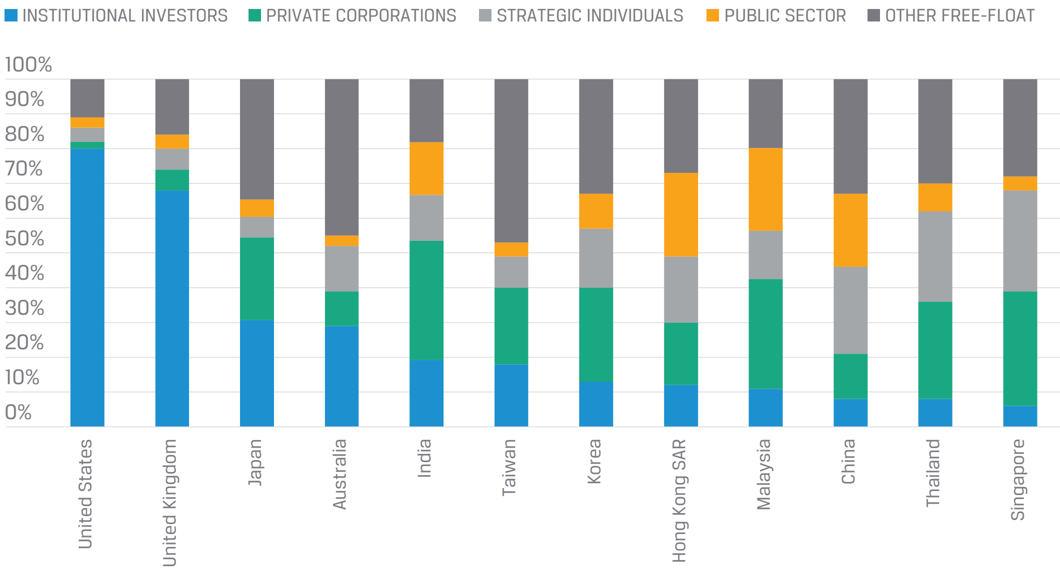


Source: A. De La Cruz, A. Medina, and Y. Tang, "Owners of the World's Listed Companies," OECD Capital Market Series (Paris, 2019)

Another key difference is the high level of institutional ownership in the United States and United Kingdom, with average ownership of markets by institutional investors at 80% and 68% respectively.[32] Of the Asia Pacific markets featured in **Chart 4**, Japan and Australia have the highest levels of institutional ownership, but even their levels are less than half of those in the United States and the United Kingdom. This disparity is even more pronounced when compared to markets like Singapore, where institutional investors own only 6% of the local equity market.

[32] A. De La Cruz, A. Medina, and Y. Tang, "Owners of the World's Listed Companies," OECD Capital Market Series (Paris: OECD, 2019), www.oecd.org/corporate/Owners-of-the-Worlds-Listed-Companies.htm

Chart 4: Average ownership by category of investor, end-2017



Source: A. De La Cruz, A. Medina, and Y. Tang, "Owners of the World's Listed Companies," OECD Capital Market Series (Paris, 2019)

Institutional investors' ability to influence corporate behavior links directly to the level of institutional ownership. In highly concentrated ownership situations, it may simply not be worth an investor's time and effort to engage. In addition, if a government is the controlling shareholder, an institutional investor may be disinclined to vote against it and would be extra cautious in how to engage. Given the local market structures, institutional investors in the United States and United Kingdom appear to be better positioned to provide effective stewardship relative to other jurisdictions, especially some of those in Asia Pacific. Notwithstanding this, listed companies that desire to diversify their shareholder and capital bases tend to be sensitive to the positions of institutional investors and their voting patterns, even if changes may take time.

4.6 Passive Investing and Stewardship

"In a passive investing world, small shareholders have little-to-no voice and no realistic possibility of banding together, while the biggest shareholders have no skin in the game so long as the money manager does not underperform the index."[33]

Paul Singer, 2017

"[W]e will be increasingly disposed to vote against management and board directors when companies are not making sufficient progress on sustainability-related disclosures and the business practices and plans underlying them."[34]

Larry Fink, 2020

Should passive managers engage with the companies they invest in? How much engagement should they do, and how effective are they? These questions have caused much debate in the last few years as passive assets have risen relentlessly—assets under management in global index funds surpassed the USD 10 trillion mark in early 2020, compared with USD 2.3 trillion a decade ago—at the expense of actively managed strategies.[35] It is a trend observed in equities and increasingly in fixed income. The popularity of index funds and ETFs arises chiefly from their decent performance, largely as a result of rising markets, and importantly, their low cost. As the competition for new funds becomes more acute, active managers have sought to emphasize the role they play in price discovery or raising corporate governance standards via their stewardship activities.

In the past, passive managers were probably more concerned with providing product liquidity or minimizing tracking error. Stewardship is costly, and may erode the cost advantages of ETFs and passive tracker funds. Since index trackers are long-term shareholders, divestment is not an available option for them. But as passive investors increasingly dominate the shareholder registries in listed companies across the globe, the expectations and pressure on passive managers to be active stewards are also becoming more intense. Gone are the days when passive managers unquestioningly vote with management; now end clients are scrutinizing how passive managers are engaging on issues such as corporate governance and climate change. Some passive managers are rising to the challenge by proxy voting, management engagement, shareholder activism, or a

[33] Paul Singer, "As ETFs Blow Past Hedge Funds, Paul Singer Has Had Enough, Says They Are 'Devouring Capitalism'," CNBC, 4 August 2017, https://www.cnbc.com/2017/08/04/as-etfs-blow-past-hedge-funds-paul-singer-has-had-enough-says-they-are-devouring-capitalism.html

[34] Larry Fink, "A Fundamental Reshaping of Finance," BlackRock, 2020, https://www.blackrock.com/hk/en/larry-fink-ceo-letter

[35] "Index Funds Break through $10tn-in-Assets Mark amid Active Exodus," *Financial Times*, accessed 7 May 2020, https://www.ft.com/content/a7e20d96-318c-11ea-9703-eea0cae3f0de

combination of these activities. Passive investors own large percentages of companies but are unable to sell, and so one of their main levers to increase returns is to engage with these companies to seek improvements. Certainly passive managers hold a great deal of power given their shareholding. By exercising such powers proactively, they are seen as better fiduciaries, with elevated levels of reputation and branding.

Concerns remain about coverage. The large number of companies in which passive managers hold stakes means these managers have to be selective regarding the companies with which they engage with. Cost is another obstacle to stewardship. In a landmark movement, Japan's Government Pension Investment Fund started to pay higher fees to two passive managers for carrying out stewardship activities in 2018. Few clients are keen to pay higher fees, however, and these costs are borne much better by larger firms because of their economies of scale.

In a survey carried out by the *Financial Times*, the big three passive managers—Vanguard, BlackRock, and State Street Global Advisors—have all increased their stewardship teams in recent years, "although they remain relatively small."[36] All of them are signatories to the PRI, and each publishes an annual stewardship report covering such areas as engagement principles and themes, case studies, and voting record and giving some indication on outcomes achieved.

Nonetheless, it is not always straightforward for institutional clients (such as pension funds) to evaluate a passive manager's performance in this regard. Clients are becoming more savvy and discerning, though; by scrutinizing voting records, for example, some clients may conclude that some passive managers are more proactive in exercising their voting rights, voting against management on important, thematic issues rather than just paying lip service to it. Some cultures prefer behind-the-scenes engagement; thus instead of proxy fights, institutional investors seek to collaborate with management to unlock shareholder value.

To return to our opening questions, there appear to be rising expectations for passive investors to act as active owners. However, their effectiveness remains a fluid question and the debate continues to evolve.

[36] "Pension Funds Raise Concern over Index Manager Stewardship," *Financial Times*, accessed May 7 2020, https://www.ft.com/content/f75459e3-3a6d-383e-843b-6c7141e8442e

4.7 Cultural Norms and Local Context

The effectiveness of stewardship codes is also subject to differences in cultural norms. Given that global stewardship codes primarily stem from the UK Stewardship Code, there remains a debate as to whether the Anglo-Saxon model of corporate governance is appropriate for each and every market. Earlier we noted how ownership structures may render stewardship codes targeting institutional investors irrelevant in markets where ownership is dominated by governments or families, so perhaps what is needed are codes targeting families or sovereign wealth funds.[37]

When looking specifically at the region, Stewardship Asia Centre has listed several cultural reasons why stewardship codes may not apply uniformly throughout Asia:[38]

- Conflicting forces in Asian cultures make generalizations difficult.
- Collectivism is valued more highly relative to individualism.
- A long-term orientation prevails, which may be more conducive to stewardship behaviours.
- Greater emphasis is placed on hierarchy, which may lessen the degree of stewardship.

Indeed, each jurisdiction may differ in its motivations for establishing a stewardship code. In the United Kingdom, the objective was to encourage thoughtful engagement by institutional investors, which would in turn provide a higher level of checks and balances to corporate boards and management, and to prevent excessive risk taking. In Japan, the motivation was different. For a long time the Japanese stock market had traded at a discount to international ones. The reasons for this included a lack of risk appetite (which led to cash hoarding), a lack of focus on shareholder value creation (which led to low returns on capital and on equity), cross-shareholdings (which led to entrenched interests), and diversified operations (which led to conglomerate discounts). Active, engaging institutional investors were to nudge Japanese listed companies out of their comfort zone, take more risks, and improve shareholder and market returns—an entirely different premise from that of the United Kingdom.

[37] Two years after releasing the first stewardship code in Singapore, Stewardship Asia issued a second code, called the "Stewardship Principles for Family Businesses: Fostering Success, Significance and Sustainability," with the objective of guiding family business in Asia by "articulating the right mindset, attitude and practices that foster successful and sustainable Family Businesses."

[38] Cossin et al., "Fostering Responsible Long-Term Wealth Creation," p. 17.

In Singapore, the story is yet again different. As shown in the previous section, companies listed in Singapore tend to be dominated by the government and families as controlling shareholders. Institutional investors hold little sway. Singapore already had a robust, well-recognized corporate governance system. So what is the motivation for Singapore to have a stewardship code? A study by Gen Goto, Alan Koh, and Dan Puchniak[39] argues that to indicate adherence to a high standard of corporate governance sends an important "halo signaling" effect, even if the intended function of the Singapore Code was vastly different from that of the UK Stewardship Code, on which the Singapore Code was modelled and which it resembles.

In this light it is perhaps obvious, but nevertheless worthwhile, to point out that not all stewardship codes are equal, that having a stewardship code does not in itself lead to better corporate governance, and that better governance may mean different things to different people.

4.8 Conflict of Interest

The financial industry is rife with conflicts of interest, and the investment management industry is no exception. Asset managers and service providers both serve their clients (institutional and retail fund holders) and corporate shareholders, and the interests of these two sets of shareholders often diverge, especially when it comes to stewardship. An asset manager may, for example, refrain from rocking the boat with an issuer, particularly if the said issuer is a client and is invested with the asset manager, or if the asset manager is competing for a mandate from the issuer. In a utopian world perhaps client interests would always come first, but employees are probably most likely incentivized to put their own, and their company's interests first. Jack Bogle, the founder of Vanguard and pioneer of index funds, has repeatedly called for an ownership structure for asset managers that eliminates such conflicts,[40] and indeed Vanguard is itself unique in its ownership structure: it is owned by its funds, which are in turn owned by their investors, thus eliminating the sort of conflict we have outlined.

[39] Gen Goto, Alan K. Koh, and Dan W. Puchniak, "Diversity of Shareholder Stewardship in Asia: Faux Convergence," NUS Law Working Paper No. 2019/077, 6 November 2019 (revised 13 December 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3481543

[40] John C. Bogle, "The Modern Corporation and the Public Interest," *Financial Analysts Journal* 74, no. 3 (2018): 1, https://www.cfainstitute.org/en/research/financial-analysts-journal/2018/faj-v74-n3-1

Other conflicts exist within the institutional investment community. The 2012 review by Professor John Kay (the Kay Review) concluded that systemic short-termism was caused by "the decline of trust and the misalignment of incentives throughout the equity investment chain."[41] This sentiment was echoed in a 2019 discussion paper issued jointly by the UK FCA and the FRC.[42] Thus when awarding an investment mandate, for example, asset owners may prioritize cost reduction or short-term performance, but this may not be aligned with the long-term interests of their beneficiaries. In turn, asset managers may focus on short-to medium-term performance or remuneration incentives, which, again, may not be aligned with the financial interests or the investment horizon of the beneficiaries. Misalignment occurs not only between asset owners and asset manager but also with service providers such as proxy advisors and investment consultants, where limited competition and scrutiny may compromise the quality of their advice and recommendations.

Stewardship codes are both inhibited by, and offer a solution to, some of these conflicts. The 2020 UK Stewardship Code is a valiant attempt in addressing these issues: by improving transparency and disclosures, by incorporating other service providers into its purview, and by ensuring the identification and management of conflicts of interest, the code raises expectations and encourages a long-term perspective across the investment community.

[41] John Kay, "The Kay Review of UK Equity Markets and Long-Term Decision Making: Final Report," OCL, July 2012, p. 9, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf

[42] FCA, "FS19/7, Building a Regulatory Framework for Effective Stewardship: Feedback to DP19/1," 24 October 2019, p. 23, https://www.fca.org.uk/publication/feedback/fs19-7.pdf

5. Industry Feedback on Awareness, Effectiveness, and Areas for Improvement

5.1 Introduction

To better gauge investor perceptions of stewardship codes in Asia Pacific, between 18 and 31 December 2019 CFA Institute conducted a survey of its membership in relevant Asia Pacific markets that have adopted stewardship codes. These markets are Australia, Hong Kong SAR (China), Japan, Korea, Malaysia, Singapore, Taiwan, and Thailand.

The survey consisted of 22 questions, with the following objectives:

- **Questions 1–3, demographics:** Identify roles, occupations, and firm characteristics of respondents for segmentation purposes
- **Questions 4–9, awareness:** Gauge the awareness and application of stewardship codes in the region
- **Questions 10–13, effectiveness:** Collect survey respondents' views on the effectiveness of stewardship codes, including how current codes have influenced the integration of ESG factors in the investment process
- **Questions 14–22, areas of improvement:** Canvass how stewardship codes could be improved, with the final question an open-ended response

In total 270 responses were received. They represented a wide spectrum of investors, corporates, service provides, academics, regulators, and other professionals. The specialized nature of this topic gives rise to a potential for self-selection bias; that is, those members with a degree of knowledge on the subject were more likely to respond to the survey than those less knowledgeable. Accordingly, the results reflect the best efforts of CFA Institute to provide a representative sample of informed members.

5.2 Summary of Survey Findings

Some of the major takeaways are these:

- **Awareness:** Respondents were more skewed towards "less understanding" rather than "more understanding." They appeared less aware of the specifics of local stewardship codes than of the concepts of stewardship in general. Awareness could also be even lower among the general population of investors, given the potential for self-selection among survey respondents. To improve awareness, respondents suggested more education, promotion, and clarity regarding local stewardship codes.
- **Engagement:** Investors generally considered stewardship principles to some extent when making investment decisions. However, engagement levels were mixed. While 30% engaged only on an annual basis or less, more than 50% of investors responded as engaging quarterly or more with investee companies. The most common forms of engagement were via management discussions and proxy voting. Roughly 20% of investors reported engaging via other methods, including management presentations, shareholder letters, and proposals. The degree of engagement across investee companies was also mixed, with most investors engaging with less than 25% of their investee companies.
- **Specific principles:** ESG integration included as a distinct principle within a stewardship code was generally seen as having the potential to improve an investment firm's ESG practices. This has been observed in recently revised stewardship codes such as the 2020 UK Stewardship Code. Similarly, although codes often include a principle promoting collective engagement, this was not widely practised—only one-third of respondents reported doing so. When considering expanding the scope, nearly all investors believed stewardship codes could apply to asset classes other than listed equities. This is a global trend observed in recent code updates.
- **Impact:** Investors did note a stronger impact of stewardship on corporate governance practices when compared to economic, environmental or social factors, which were more evenly distributed. This appears to reflect how stewardship codes often are issued alongside local corporate governance codes and are meant to be complementary. Furthermore, the impact of governance is often more visible as the direct results of proxy voting where economic, environmental, and social factors may require a longer-term horizon for impacts to become tangible.

- **Challenges:** Lack of impact was also seen as one of the major challenges limiting stewardship codes. In particular, respondents were concerned that following stewardship codes did not directly result in any meaningful outcomes. Similarly, respondents felt the cost of engagement was a possible barrier to further stewardship activities. A lack of knowledge, awareness, and expertise were other potential challenges cited.
- **Enforcement:** While roughly half of respondents thought the widely used comply-or-explain standard was adequate, a sizable number (over a quarter) considered this level of enforcement ineffective. Given that oversight and monitoring of stewardship codes by a regulator was widely seen as important, enforcement by a government entity would likely provide a higher level of credibility. Notwithstanding the above, respondents were overwhelmingly in favor of keeping stewardship codes as best practice principles rather than writing them into statutory law. Making stewardship codes mandatory, most investors felt, would place additional burdens on their firms and be a key hurdle to effectiveness. Some respondents believed self-regulation was possible, whereas others looked for a more cohesive international standard.
- **Improvements:** Respondents noted that the effectiveness of stewardship codes could be vastly improved by a higher degree of education, promotion, and awareness as well as better clarification and simplification of codes. This is a balancing act: whereas some respondents called for stronger enforcement by regulators, others were against making stewardship codes mandatory. Incentives remain an issue; hence having asset owners push more strongly for stewardship was another common recommendation, given their direct influence on asset managers.

5.3 Demographics

Key criteria examined are the views of investment professionals as well as those involved in the industry more broadly. As such the responses were segmented as follows:

- **Identification by firm:** Categories include investors (defined as asset owners and asset managers, 49%), service providers (proxy advisors, sell-side researchers, and investment consultants, 23%), corporates (securities issuers, 6%), and others (academia, government, retired, etc., 22%).
- **Identification by invested markets:** Investors often invest in more than one market, and respondents could select the top three markets most relevant to them.

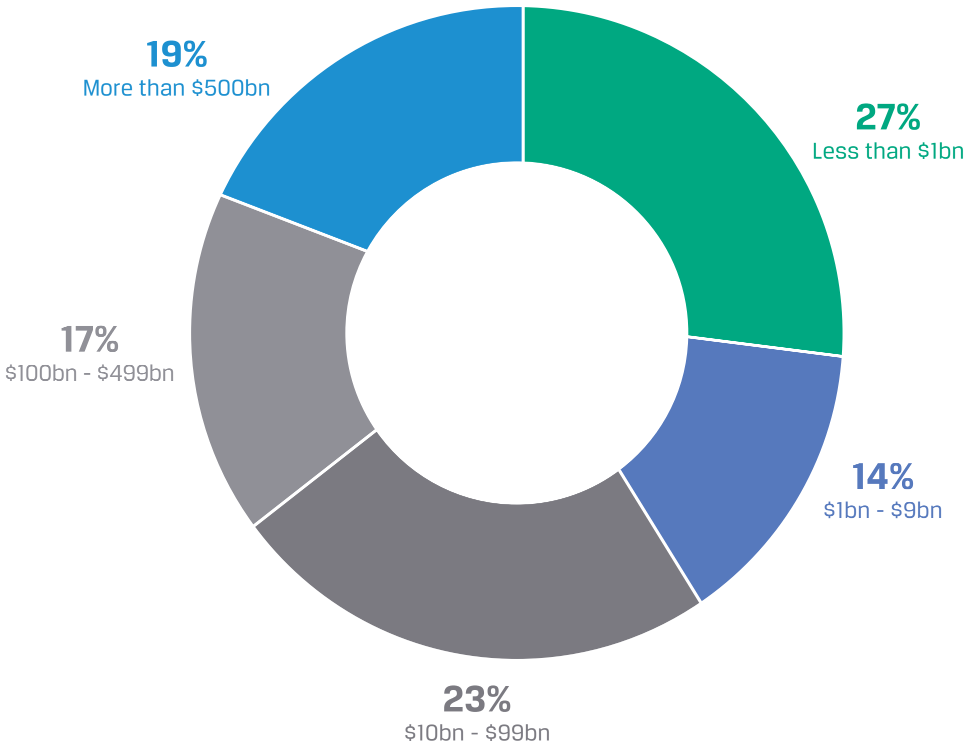
The following table sets out the segmentation of respondents by firm type and by invested market.

Table 1: Segmentation of respondents

Respondents by Firm Type		Number of Respondents by Invested Market	
Institutional investors	49%	Hong Kong SAR	84
Service providers	23%	Australia	69
Corporates	6%	Singapore	58
Other	22%	Japan	47
		Malaysia	26
		South Korea	22
		Taiwan	14
		Thailand	7

As shown in **Chart 6**, the distribution of respondents by assets under management (AUM) was well balanced, with institutional investors representing asset sizes from under USD 1 billion (27%) to greater than USD 500 billion (19%). These figures exclude respondents for whom AUM was irrelevant and who responded "not applicable."

Chart 6: AUM of respondents



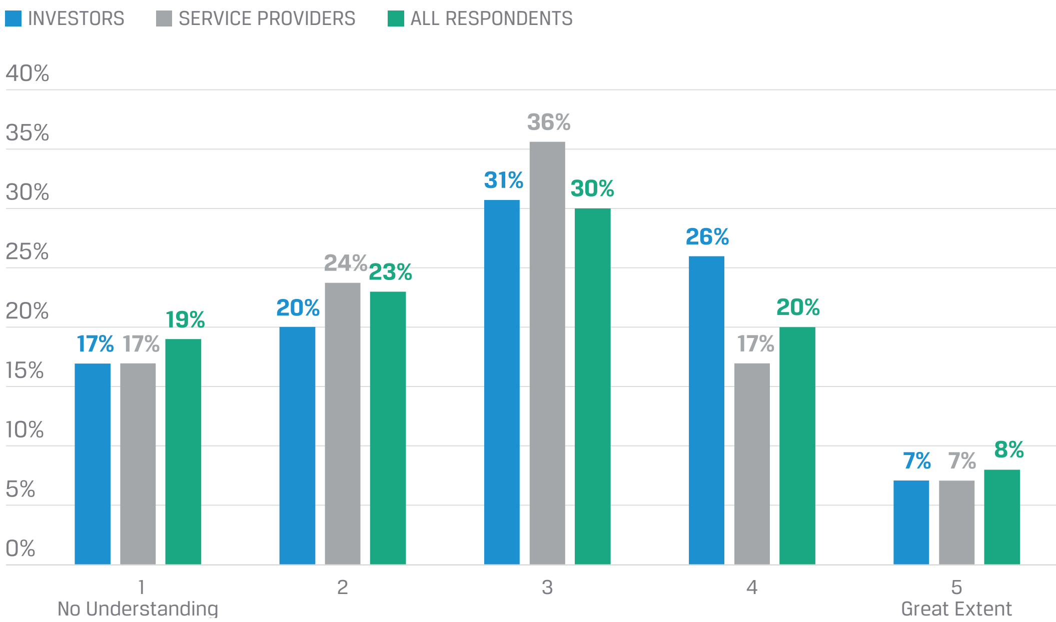
5.4 Awareness

5.4.1 General understanding of stewardship codes

This question allowed respondents to rate their general understanding of stewardship codes on a scale of 1 to 5, with 1 representing no understanding of stewardship codes and 5 representing a high degree of knowledge.

As shown in **Chart 7**, the responses were evenly distributed, with 30% of all respondents rating themselves as having some understanding of stewardship codes, though the results were skewed towards “not at all” with nearly 20% of all respondents. Institutional investors appeared to be slightly more knowledgeable, with a higher percentage of respondents rating themselves as 4 and 5.

Chart 7: To what extent would you rate your general understanding of stewardship codes?



5.4.2 Compliance with stewardship codes

To understand the level of adherence to stewardship codes, the survey asked if and where respondents complied. Whereas 53% of investors noted compliance with stewardship codes in their own jurisdictions, 34% noted complying with stewardship codes outside of their own jurisdictions.

Table 2: How would you describe your firm's compliance with stewardship codes?

	Institutional Investors	All Respondents
Primarily comply with the stewardship code of my home jurisdiction	60%	49%
Primarily comply with the stewardship code of the jurisdiction in which I invest	37%	26%
None of the above	16%	34%

5.4.3 Awareness by market

Examining stewardship codes by market showed that more respondents rated their awareness as low (rating of 1 or 2) in nearly all markets compared to the understanding of stewardship codes noted in question 1. These results appear to reflect that, although respondents have some knowledge of the concepts of stewardship codes broadly, they are less aware of the specifics of local codes. By market, Japan stands out as having the highest level of awareness: it has both the highest percentage of respondents reporting high awareness and the lowest percentage of low awareness.

Table 3: To what extent are you aware of stewardship codes in the specific markets you primarily conduct investment activities in?

	1 Not at all	2	3	4	5 To a great extent
Australia	31%	16%	26%	18%	9%
Hong Kong SAR	28%	18%	27%	17%	10%
Japan	7%	13%	24%	27%	29%
Malaysia	40%	16%	24%	16%	4%
Singapore	25%	21%	16%	28%	11%
South Korea	33%	10%	19%	19%	19%
Taiwan	21%	29%	36%	14%	0%
Thailand	43%	14%	29%	14%	0%

5.4.4 Compliance with other standards

One possibility for demonstrating stewardship is to adopt a global standard such as the PRI. This can either be in place of or in addition to local codes. The survey examined the extent to which survey respondents have adopted PRI. Of all respondents, 27% noted that their firms were signatories to PRI, but notably this figure was higher among institutional investors, at 40%. That said, awareness remains an issue, with more than a third of total respondents either unsure or unaware of PRI.

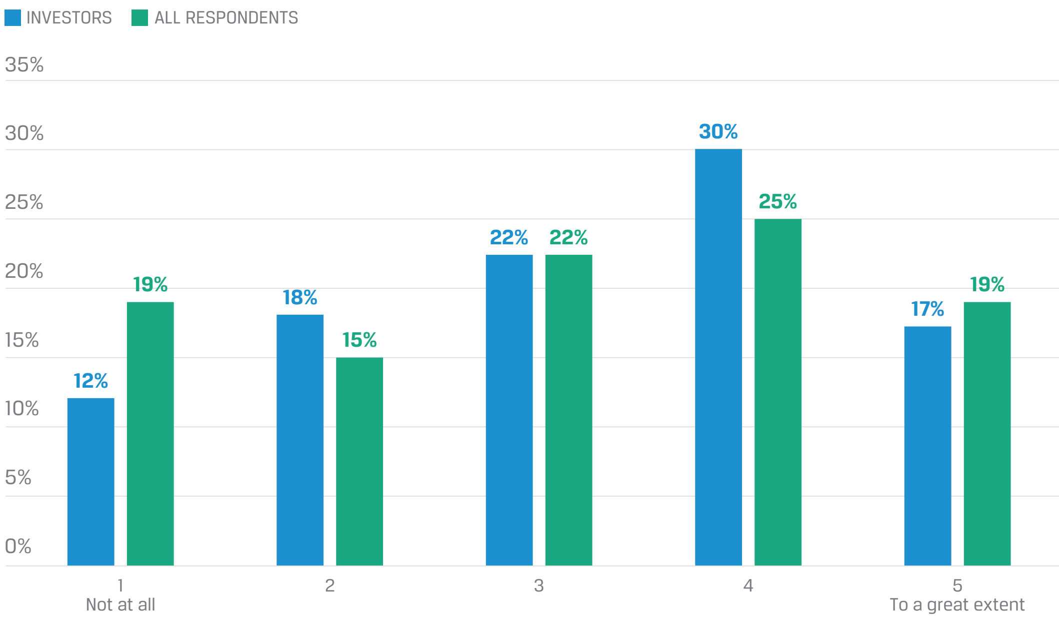
Table 4: Is your firm a signatory to the Principles for Responsible Investment (PRI)?

	Institutional Investors	All Respondents
Yes	40%	27%
No	32%	36%
Not sure	21%	23%
I am not aware of PRI	8%	14%
Total	100%	100%

5.4.5 Consideration of stewardship principles when making investment decisions

One criticism of stewardship codes is that compliance is mostly superficial. As shown in **Chart 8**, the survey reveals a balanced distribution among all respondents, with 34% responding at the lower end of the spectrum (rating 1 of "not at all" or 2), though this result was outweighed by those at the higher end of the spectrum (rating 5 of "to a great extent" or 4), at 44% of total respondents. These figures were slightly improved when isolating institutional investors, at 30% and 47% respectively. These results provide some evidence that investors do consider stewardship principles in investment decisions, though there remains the possibility of self-selection bias.

Chart 8: To what extent do you consider stewardship principles when making investment decisions?



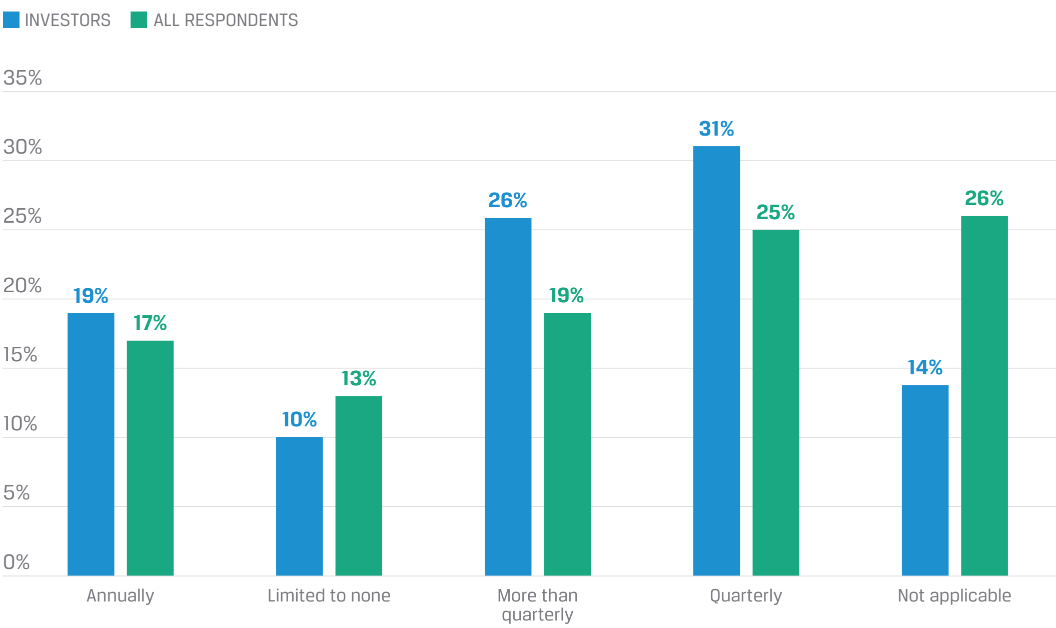
5.5 Effectiveness

The effectiveness of stewardship is difficult to quantify. The survey approached effectiveness by assessing three areas of engagement: frequency, methods of engagement, and portfolio coverage.

5.5.1 Engagement frequency

While the frequency of engagement does not necessarily equate to effective stewardship, a higher frequency suggests that an investor is more actively considering the suitability of investee firms. As shown in **Chart 9**, the most common response was quarterly engagement, accounting for 25% of all respondents and 31% of investors. However, 30% of all respondents and 29% of investors noted annual or limited to no engagement. On the whole, investors did show a higher propensity towards frequent engagement, with 26% of investors responding that they engage with portfolio companies more than quarterly.

Chart 9: How would you characterize your typical engagement frequency with portfolio companies?



5.5.2 Methods of engagement

To better understand the method of engagement, the survey included several possible responses as well as an open response for other methods not listed. The survey asked respondents to select all that applied.

Table 5: What areas of engagement have you/your firm conducted?

	Institutional Investors	All Respondents
Regular management discussions	55%	41%
Active proxy voting	57%	37%
Presentations to management	19%	22%
Shareholder letters	19%	14%
Shareholder proposals	23%	18%
Other	3%	4%
Not applicable	19%	31%

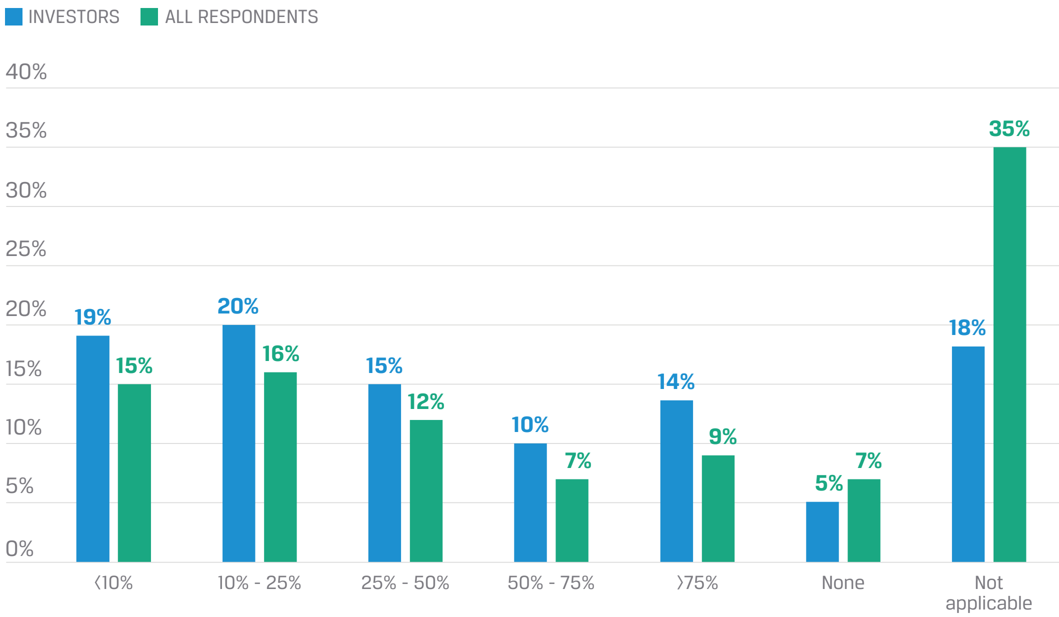
Of the sample of investors, more than half engaged in regular management discussions and active proxy voting, while approximately 20% of investors also engaged with management via presentations, shareholder letters, or shareholder proposals. Other responses provided were

- collaboration with other asset managers,
- board-level representation,
- advocacy sessions on sustainability reporting,
- questions on conference calls, and
- review of finances.

5.5.3 Coverage

The survey looked to gauge the degree of engagement across the entirety of an investor's portfolio. This was to determine whether institutional investors engage with companies systematically. As shown in **Chart 10**, whereas 35% of all respondents and 18% of investors did not find this question applicable, the remaining investors showed a broad range of engagement. More than half of the remaining investors noted engagement with less than 25% of portfolio companies. The results suggest that although engagement is common, the scale may be limited to a small portion of investment portfolios.

Chart 10: Based on the total number of firms invested in, what is the estimated percentage of portfolio companies that your firm is engaging with at any point in time?



5.5.4 Impact of compliance

Benefits of applying stewardship codes remain unclear. To gauge investor perception the survey asked respondents to rate the impact of stewardship code compliance on each of the following four factors: economic, environmental, social, and governance. The distribution of responses is similar for economic, environmental, and social factors with a slight tilt towards ratings of 3 and 4, suggesting perceptions of some positive impact. The strongest perceived impact of stewardship was on governance, where 60 % of respondents observed a positive impact (rating 4 or 5) and only 17% of respondents rated it weak (rating 1 or 2). This provides evidence that stewardship codes are perceived to have a positive effect on improving governance.

Table 6: In your opinion, what general impact has the compliance with stewardship codes generated among the following?

	1 No impact at all	2	3	4	5 Strong positive impact
Economic	14%	14%	35%	23%	14%
Environmental	18%	13%	29%	29%	12%
Social	12%	15%	32%	28%	14%
Governance	9%	8%	22%	35%	28%

5.6 Challenges and Potential Areas of Improvements

5.6.1. Challenges of stewardship codes

To understand how best to improve the implementation of stewardship codes, the survey looked to determine reasons why investors felt stewardship codes were ineffective. Respondents selected the two issues they felt most strongly about. For each selection the response reflects the portion of respondents that selected this as a top-two issue. The two issues most widely selected by both investors and all respondents were the high cost of engagement and the unclear link between value creation and engagement. Investors selected cost of engagement as their top concern, with 44% of investors selecting this response compared to 36% among the entire sample. This suggests that costs related to stewardship are of more concern to investors than the broader community. Despite academic discussion as a potential limiting factor,[43] free riding was the least common selection among respondents as a potential reason preventing stewardship effectiveness.

Table 7: In your opinion, what are the top two challenges preventing stewardship codes from being more effective?

	Institutional Investors	All Respondents
High cost of engagement	44%	36%
Unclear link between value creation and engagement	41%	38%
No clear requirement from regulators	30%	32%
No clear mandate from beneficiaries	26%	27%
Unwillingness for issuers to engage	23%	25%
Problem of free riding	12%	16%
Other	3%	4%

Some other responses included

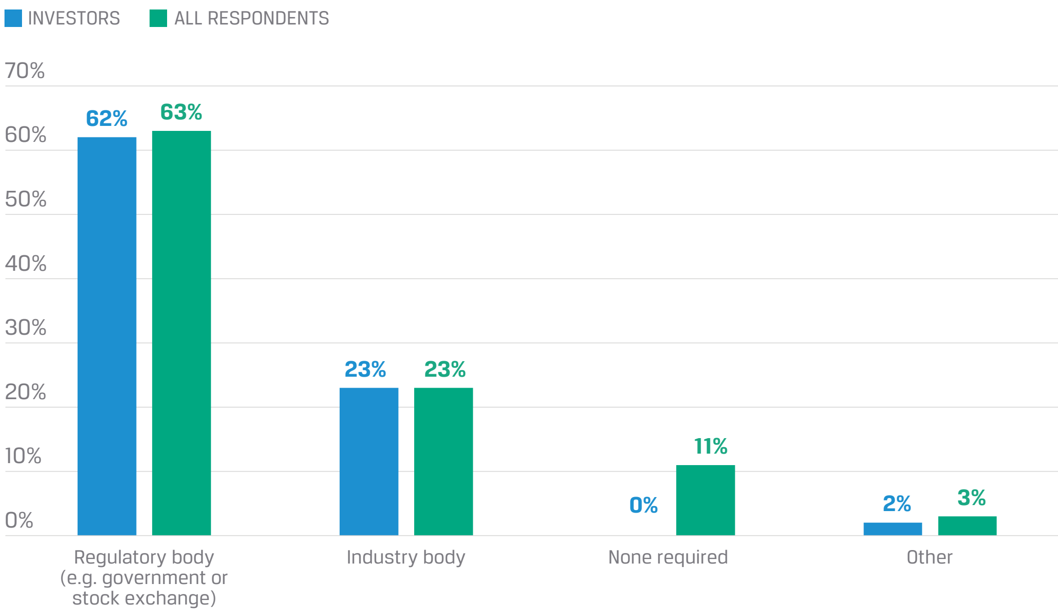
- lack of knowledge,
- inconsistencies across countries and markets,
- lead times from decision to change and effective implementation, and
- lack of investment experience by oversight bodies.

[43] Lucian A. Bebchuk, Alma Cohen, and Scott Hirst, "The Agency Problems of Institutional Investors," Journal of Economic Perspectives 31, no. 3 (Summer 2017): 98, say that "*a move by any given index fund manager to improve stewardship and raise fees would unravel, because its investors would prefer to free-ride on the investment manager's efforts by switching to another investment fund that offers the same indexed portfolio but without stewardship or higher fees.*"

5.6.2 Sponsors of stewardship codes

The legitimacy of a stewardship code requires a strong entity as a supporter, sponsor, or regulator. To understand the respondents' views of who should manage and oversee stewardship codes, the survey asked respondents to suggest an entity, selecting either a regulatory body (government, stock exchange, etc.), an industry body (self-regulatory organization of industry participants), "none required" or "other". As shown in **Chart 11**, nearly two-thirds of respondents believed a regulatory body was most suited to oversee stewardship codes, whereas just under a quarter believed an industry body was appropriate. This result was consistent across different respondent types, suggesting that some level of regulatory credibility is desired to support stewardship codes.

Chart 11: Which designated body is required to support and oversee stewardship codes?



Some suggestions for other entities are as follows:

- Self-monitoring by shareholders/stakeholders
- An international body like the International Accounting Standards Board
- CFA Institute in coordination with regulators

5.6.3 Rules-based versus principles-based codes

Debate remains as to whether stewardship codes should be more stringent in order to be more effective. Would they carry more weight as a regulatory statute versus a comply-or-explain or voluntary framework? The results overwhelmingly favored maintaining stewardship codes as a regulatory principle (77%). Only 19% of respondents thought that statutory law was more favorable. Of those who responded "other," selected comments are set out here:

- *Ethical guiding principles and fiduciary duties are more important.*
- *Should be equivalent to a Code of Ethics—not law nor regulated but a kind of self-regulation*
- *Purely voluntary*
- *No extra compliance cost*

Table 8: Should stewardship codes be issued as statutory law or regulatory principle?

	Institutional Investors	All Respondents
Regulatory principle	78%	77%
Statutory law	17%	19%
Other	5%	5%

5.6.4 Level of enforcement

Given that comply-or-explain has become the most common standard for applying stewardship codes, the survey looked to determine respondents' views on how effective comply-or-explain is in practice. Of all respondents, 45% believed that the comply-or-explain standard has been effective, 27% that it has not been effective, and 29% were unsure. The breakdown by firm type shows a similar distribution of responses, with 49% of investors responding the comply-or-explain standard has been effective, 23% replying not effective, and 29% unsure. Given the relatively even split between effective and ineffective/unsure, there appears to be no consensus among respondents and more specifically investors on whether comply-or-explain is the optimal framework for stewardship codes.

Table 9: Is the comply-or-explain model a sufficient level of oversight for effective enforcement of stewardship codes?		
	Institutional Investors	**All Respondents**
Yes	49%	45%
No	23%	27%
Not sure	29%	29%

5.6.5 Burden of compliance

While there has been a push to raise the bar for stewardship code compliance, one common concern among investors, and certainly the top concern as indicated in the survey, is the costs related to stewardship and reporting. More than three-quarters of investors believed that mandatory compliance would create additional burdens, 11% did not expect any further burdens, and 13% were unsure. This result suggests that given the potential for additional costs, implementing mandatory compliance with codes would not be preferable to investors.

Table 10: Would mandatory compliance with stewardship codes cause additional burdens (e.g., administrative, financial) to your firm?		
	Institutional Investors	**All Respondents**
Yes	76%	68%
No	11%	13%
Not sure	13%	19%

5.6.6 Systematic ESG integration

Another trend in stewardship codes has been to clarify the importance of ESG as a facet of stewardship. Codes in Australia, Malaysia, and Thailand emphasize the importance of ESG factors, and the 2020 UK Stewardship Code incorporates environmental and social factors into its definition of stewardship and includes a separate principle focused on ESG integration. Survey results show that 50% of investors believed including a separate ESG principle would affect ESG practices, whereas 27% believed no impact would result. This suggests that creating an additional principle focused on ESG could change some investors' behaviors and attitudes in considering ESG factors.

Table 11: Would a separate principle requiring systematic ESG integration in stewardship codes noticeably impact your firm's current ESG practices?

	Institutional Investors	All Respondents
Yes	50%	47%
No	27%	26%
Not sure	23%	27%

5.6.7 Collective engagement

Not all jurisdictions have included collective shareholder engagement as a separate principle within their stewardship codes. In the updated 2020 UK Stewardship Code, the wording of the principle on collective engagement has changed slightly, now using the term "collaborative engagement." The survey sought to understand whether investors thought collective engagement was regularly practised. Of investors responding to the survey, 63% answered that they did not engage in collective engagement. This suggests that a separate principle on this issue may be required if collective engagement is something the market or the regulator would like to encourage.

Table 12: Have you ever collaborated in collective shareholder engagement with other investors for the purposes set out in the stewardship code?		
	Institutional Investors	All Respondents
Yes	19%	16%
No	63%	63%
Not sure	17%	21%

5.6.8 Other asset classes

Hitherto, the application of stewardship codes has been focused on listed equities within the respective local markets. Although certain codes (such as Korea) have opened the door to other asset classes, only recently has there been a strong push to expand the scope of stewardship to include asset classes such as fixed income and private equity. The survey shows that 81% of all respondents and 86% of investors believe other asset classes could benefit from applying stewardship principles.

Table 13: Can stewardship codes improve investor engagement in asset classes other than listed equities?		
	Institutional Investors	All Respondents
Yes	86%	81%
No	14%	19%

5.6.9 Potential improvements

The survey requested respondents to make suggestions on how best to improve the effectiveness of stewardship codes.

Can Stewardship Codes Improve Investor Engagement in Asset Classes other than Listed Equities?

Some common suggestions included:

- improving education and awareness,
- clarifying and simplifying the codes,
- ensuring better disclosure of stewardship activities,
- calling for stronger enforcement by regulators, and
- having asset owners push for stewardship.

A sample of responses include the following:

- *More widespread education would create awareness.*
- *Make it more understandable to the layman.*
- *An application of a consistent set of stewardship codes across jurisdictions.*
- *Not too many rules, more guiding principles, and a clear and unwavering focus on the best interests of shareholders and/or end investors.*
- *We should broaden the scope of stewardship by including private companies. Owner CEO companies sometimes show lack of governance. Those companies tend not to go public.*
- *They need to have a higher profile (and be valued by) with asset owners.*
- *More involvement and leadership shown by federal governments.*
- *Making them compulsory to comply with.*
- *Made mandatory by starting with a few requirements and then fine-tuning over time.*
- *Have asset owners insist upon it.*
- *Publish in each manager website the details of stewardship undertaken. A policy from regulators will also help.*
- *Investee companies need to see additional value in taking the trouble to engage with asset owners/managers on stewardship issues.*

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6. Stewardship Codes in Asia Pacific

This section provides an overview of stewardship codes in the following Asia Pacific markets:

- Australia
- Hong Kong SAR
- India
- Japan
- Malaysia
- Singapore
- South Korea
- Taiwan
- Thailand

We also include highlights of and make reference to the UK Stewardship Code.

6.1 Australia

Title

1. Principles of Internal Governance and Asset Stewardship (PIGAS)
2. Australian Asset Owner Stewardship Code (AAOSC)

Background

In Australia there are two different sets of principles for stewardship catering to asset managers and asset owners respectively.

Table 14: Stewardship codes by market

MARKET	AUSTRALIA (FSC)	AUSTRALIA (ACSI)	HONG KONG SAR
NAME OF CODE	Principles of Internal Governance and Asset Stewardship	Australian Asset Owner Stewardship Code	Principles of Responsible Ownership
YEAR ISSUED	2017	2018	2016
CODE SPONSOR	Financial Services Council	Australian Council of Superannuation Investors	Hong Kong Securities and Futures Commission
SPONSOR TYPE	Industry body	Industry body	Government
COMPLIANCE	Mandatory (for FSC full members)	Comply-or-explain	Voluntary
SIGNATORIES	No	Yes	No
PUBLIC DISCLOSURE OF SIGNATORIES	No	Yes	No
PRINCIPLES			
Stewardship policy/ public disclosure	6. Disclose principles used for policy advocacy	1. Publicly disclose stewardship policy	1. Establish and report policies to stakeholders
Purpose/belief			
Governance/resources/ knowledge/capabilities			
Conflicts of interest management			7. Establish a policy on conflicts of interest and management
Market alignment		5. Encourage alignment with the interests of long-term investors	
Policy review/assurance			
Reporting to beneficiaries	7. Disclose approach to client engagement, education and communication	6. Report to beneficiaries	6. Report to stakeholders
ESG integration	3. Consider ESG risks and opportunities		
Monitor managers/ service provides		4. Monitor asset managers' stewardship activities	
Monitor/engage investee companies	1. Monitor investee companies		2. Participate in and engage with investee companies
Collective engagement	5. Participate in collaborative engagement		5. Participate in collective engagement
Engagement/ escalation policy	2. Engage with investees and escalate where appropriate	3. Engage with companies (directly or indirectly)	3. Establish a policy of escalation
Voting policy and disclosure	4. Participate in proxy voting	2. Publicly disclose voting policy	4. Establish a policy on voting guidance

INDIA	JAPAN	MALAYSIA	SINGAPORE
Stewardship Code for Mutual funds and all Categories of Alternative Investment Funds (AIFs)	Principles for Responsible Institutional Investors – Japan's Stewardship Code	Malaysian Code for Institutional Investors	Singapore Stewardship Principles For Responsible Investors
2019	2014, revised in 2017 and 2020	2014	2016
Securities and Exchange Board of India	Financial Services Agency	Institutional Investor Council Malaysia	Stewardship Asia Centre
Government	Government	Industry body	Industry body
Mandatory	Comply-or-explain	Voluntary	Voluntary
No	Yes	Yes	No
No	Yes	Yes	Yes
1. Publicly disclose stewardship policy	1. Publicly disclose stewardship policy	1. Publicly disclose stewardship policy	1. Establish and articulate stewardship policy
	7. Develop skills and resources to fulfil stewardship activities		
2. Establish a policy on conflicts of interest management	2. Have a clear policy onconflicts of interest management	4. Adopt a policy on managing conflicts of interest	4. Publish policy on conflicts of interest management
6. Report periodically on stewardship activities	6. Report to clients beneficiaries on stewardship activities		6. Report stewardship activities to beneficiaries
		5. Incorporate governance and sustainability in investment decisions	
	8. Require service providers to contribute and fulfil their stewardship responsibilites		
3. Monitor investee companies	3. Monitor investee companies	2. Monitor investee companies	3. Monitor investee companies
4b. Establish and disclose clear policy for collaboration with other institutional investors			7. Participate in collective engagement, where appropriate
4a. Formulate a clear policy on active intervention	4. Engage with investee companies	3. Engage with investee companies	2. Communicate regularly with investee companies
5. Develop a voting policy and disclose voting results	5. Establish a voting policy and disclose voting activities	6. Publish voting policy	5. Publish voting policy

Table 14: Stewardship codes by market

MARKET	SOUTH KOREA	TAIWAN	THAILAND
NAME OF CODE	Korea Stewardship Code - Principles on the Stewardship Responsibilities of Institutional Investors	Stewardship Principles for Institutional Investors	Investment Governance Code for Institutional Investors
YEAR ISSUED	2016	2016	2017
CODE SPONSOR	Korea Corporate Governance Service	Corporate Governance Center of the Taiwan Stock Exchange	Securities and Exchange Commission
SPONSOR TYPE	Industry body	Exchange	Government
COMPLIANCE	Comply-or-explain	Comply-or-explain	Comply-or-explain
SIGNATORIES	Yes	Yes	Yes
PUBLIC DISCLOSURE OF SIGNATORIES	Yes	Yes	Yes
PRINCIPLES			
Stewardship policy/ public disclosure	1. Publicly disclose stewardship policy	1. Establish and publicly disclose stewardship policy	1. Adopt clear stewardship policy
Purpose/belief			
Governance/resources/ knowledge/capabilities	7. Discharge stewarship responsibilities capably		
Conflicts of interest management	2. Formulate and disclose policy on conflicts of interest management	2. Establish and disclose policy on conflicts of interest management	2. Manage conflicts of interest
Market alignment			
Policy review/assurance			
Reporting to beneficiaries	6. Report stewardship activities to beneficiaries	6. Report stewardship activities to beneficiaries	7. Disclose governance policy publicly
ESG integration			
Monitor managers/ service provides			
Monitor/engage investee companies	3. Monitor and engage with investee companies	3. Monitor investee companies	3. Monitor investee companies, including ESG principles
Collective engagement			6. Participate in collective engagement
Engagement/ escalation policy	4. Form consensus and guidelines for stewardship with investees	4. Maintain dialogue with investee companies	4. Apply enhanced monitoring if needed
Voting policy and disclosure	5. Formulate and disclose voting policy and reasons for voting	5. Establish voting policy and disclose voting results	5. Establish voting policy and disclose voting results

UNITED KINGDOM	UNITED KINGDOM	ICGN GLOBAL PRINCIPLES
The UK Stewardship Code	The UK Stewardship Code 2020	Global Stewardship Principles (prev. Statement of Principles for Institutional Investor Responsibilities)
2010, 2012 revision	2020	2003, 2016 revised
Financial Reporting Council	Financial Reporting Council	International Corporate Governance Network
Government	Government	Industry body
Comply-or-explain	Apply-and-explain	Voluntary
Yes	Yes	No
Yes	Yes	Yes
1. Publicly disclose stewardship policy		2. Develop stewardship policy
	1. Purpose, culture, value of organization	
	2. Governance structures, resource	
2. Establish policy on conflicts of interest management	3. Manage conflicts of interest	
	4. Identify and respond to market/systemic risks	
	5. Review and assurance of policies	1. Establish policy review of internal governance
7. Report on stewardship and voting activities	6. Communicate stewardship activities to clients	7. Report to beneficiaries and clients
	7. Systematic integration of material ESG issues	6. Promote long term value and ESG integration
	8. Monitor asset managers and/or service providers	
3. Monitor investee companies	9. Engage with issuers to maintain or enhance asset value	3. Monitor investee companies
5. Participate in collective engagement	10. Participate in collaborative engagement	4. Engage with companies and investor collaboration
4. Establish guidelines on escalation	11. Escalate stewardship to influence issuers	
6. Establish voting policy and disclosure	12. Actively exercise rights and responsibilities	5. Exercise voting rights

The Financial Services Council (FSC) sets mandatory standards and develops policy for over 100 member financial services companies. The FSC developed the PIGAS as a replacement for previous guidance on corporate governance of fund managers, FSC Guidance Note No. 2.[44] Formerly codified as FSC Standard No. 23, these principles are mandatory for FSC full member asset managers. Despite the stricter compliance standard, the PIGAS aims to take a broader view compared to other global stewardship codes and covers the internal governance of asset managers. PIGAS was launched in July 2017.

In May 2018, the Australian Council of Superannuation Investors (ACSI) developed the AAOSC after consultation with their members and relevant stakeholders. AAOSC is more aligned with stewardship codes internationally and was created to support Australian asset owners.[45]

Definition of stewardship

- **PIGAS:** *"Stewardship is the careful and responsible management of something entrusted to one's care."*
- **AAOSC:** *"Stewardship refers to the responsibility asset owners have to exercise their ownership rights to protect and enhance long-term investment value for their beneficiaries by promoting sustainable value creation in the companies in which they invest."*

Governing body

- For **PIGAS:** FSC
- For **AAOSC:** ACSI

Applicable parties

- **PIGAS:** Asset managers, that is, institutions with the responsibility for managing or overseeing the management of assets of clients. Specifically, any FSC member who is an asset manager or undertakes asset management activities
- **AAOSC:** Australian asset owners who have equity holdings in Australian-listed companies, regardless of whether the holding is passively or actively held

[44] Financial Services Council, Australia, "FSC Standard 23: Principles of Internal Governance and Asset Stewardship," July 2017, https://www.fsc.org.au/web-page-resources/fsc-standards/1522-23s-internal-governance-and-asset-stewardship

[45] Australian Council of Superannuation Investors (ACSI), "Australian Asset Owner Code," May 2018, https://acsi.org.au/wp-content/uploads/2020/01/AAOSC_-The_Code.pdf

Application of principles

- **PIGAS:** While it is mandatory for FSC members who are asset managers to follow the standard, the actual disclosure is described as a comply-or-explain approach. Asset managers are not forced to comply with the entire standard but instead are asked to provide reasons why the standards are not applicable if not followed.
- **AAOSC:** This is a voluntary standard, applying a principles-based approach to stewardship. Guidance is provided for each principle but is intended as suggestions and not mandatory.

Key principles/guidelines

PIGAS

- **Principle 1:** Clearly state the purpose, values, and underlying investment philosophy or approach of their organization.
- **Principle 2:** Either publicly disclose their internal governance policies or provide a clear description of their approach to key aspects of internal governance and management of business activities that could affect client assets.
- **Principle 3:** Regularly monitor investee companies. The FSC notes seven disclosures to be included
    1. monitoring of company performance on financial and non-financial matters;
    2. engagement with company management and the board (as appropriate) and escalation of issues in instances where initial engagements have not been adequately responded to;
    3. approach to considering ESG factors (risks and opportunities) and whether these considerations influence investment decision-making and company engagement;
    4. proxy voting;
    5. collaborative engagement with other investors, including involvement with industry groups and associations;
    6. principles used for policy advocacy, including participation with industry groups and associations; and
    7. the approach to client engagement, education, and communication regarding asset stewardship.

AAOSC

- **Principle 1:** Publicly disclose how they approach their stewardship responsibilities

- **Principle 2:** Publicly disclose their policy for voting at company meetings and voting activity
- **Principle 3:** Engage with companies either directly, indirectly (e.g., via collective action or third-party providers), or both
- **Principle 4:** Monitor asset managers' stewardship activities
- **Principle 5:** Encourage better alignment of the operation of the financial system and regulatory policy with the financial interests of long-term investors
- **Principle 6:** Report to beneficiaries about their stewardship activities

PIGAS is meant to provide a mandatory standard for FSC members, which is one reason for the broader view the FSC has taken on developing the principles. That said, the description of asset stewardship in Principle 3 essentially mirrors typical stewardship code disclosures as promoted in the 2012 UK Stewardship Code, though one key difference is an explicit reference to ESG concerns in the description.

AAOSC principles are mostly aligned with the 2012 UK Stewardship Code. There is no specific principle on collective action, although that is discussed under Principle 3, which suggests that engagement via collective action needs to follow relevant ASIC regulations. Similarly, while there is no explicit principle related to disclosure of conflicts of interest, this issue is mentioned within Principle 2 under public disclosure of voting activities. Unique to the AAOSC principles is Principle 5, which asks for better alignment of financial systems and policy with long-term investors. This principle appears to be specific to asset owners, given their significant clout with the Australian economy. Lastly, AAOSC principles have several references to incorporating and promoting ESG policies and disclosures.

Public signatories

- **PIGAS:** There are no signatories as such to the PIGAS because it is a mandatory requirement for all FSC asset manager members. Asset managers are required to post disclosures on their public websites.
- **AAOSC:** Signatories will be required to publish a stewardship statement that describes how they apply these principles. ACSI maintains a list of signatories on its website, including a link to the signatories' stewardship statements and contact details.

Number of signatories

- **AAOSC:** 16 (as of 1/8/2020)[46]

6.2 Hong Kong SAR

Title

Principles of Responsible Ownership

Background

In March 2015, the Hong Kong Securities and Futures Commission (SFC) issued "Principles of Responsible Ownership," a paper for public consultation that ended in June 2015. This consultation helped form the Principles of Responsible Ownership (the HK Principles) with the aim to provide guidance on how investors should to fulfil their ownership responsibilities in relation to investments in Hong Kong listed companies. The HK Principles were finalized in March 2016 with the aim of encouraging "an investment culture where engagement with investee companies is seen as paramount and fundamental and which in turn strengthens corporate governance."[47]

Definition of stewardship

"Ownership of shares brings with it important responsibilities, particularly the right to speak and vote on matters that can influence the way in which a business is conducted. Owners of company equity should not blindly delegate these responsibilities. Even when they employ agents, directly or indirectly, to act on their behalf, owners should ensure that their ownership responsibilities are appropriately discharged by those agents."

Governing body

SFC

[46] ACSI, "Australian Asset Owner Stewardship Code," ACSI Publications, May 2018, https://acsi.org.au/members/australian-asset-owner-stewardship-code/

[47] Securities and Futures Commission, Hong Kong (SFC), "SFC Publishes Consultation Conclusions on Principles of Responsible Ownership," 7 March 2016, https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=16PR23

Applicable parties

All investors who are invested in shares of Hong Kong listed companies.

The HK Principles are unique in that institutional investors are not specifically targeted. During consultation, one key point of discussion was the scope of investors.[48] This is a reflection of the market's relatively high equity ownership by individuals and corporates. In an earlier draft, the SFC included references to individual and retail investors; however, this was removed in the final draft after consultation. The SFC noted that the term "investors" will be left deliberately undefined in the HK Principles to allow for flexible application.

Application of principles

Voluntary

During the consultation period, references to "comply" were removed because of concerns that there would be misunderstandings regarding the regulatory consequences were the HK Principles not adopted.

Key principles/guidelines

- **Principle 1:** Establish and report to their stakeholders their policies for discharging their ownership responsibilities
- **Principle 2:** Monitor and engage with their investee companies
- **Principle 3:** Consider and establish clear policies on when they will escalate their engagement activities
- **Principle 4:** Have clear policies on voting guidance
- **Principle 5:** Be willing to act collectively with other investors where appropriate
- **Principle 6:** Report to their stakeholders on how they have discharged their ownership responsibilities
- **Principle 7:** Have policies on managing conflicts of interests when investing on behalf of clients

[48] SFC, "Consultation Conclusions on the Principles of Responsible Ownership," 7 March 2016, https://www.sfc.hk/edistributionWeb/gateway/EN/consultation/conclusion?refNo=15CP2

Overall the HK Principles mirror the 2012 UK Stewardship Code, with the notable changes in scope and application as noted. Certain principles have been pared down, such as Principle 5, which does not include guidelines for disclosures of policy on collective engagement, though this may reflect the broader scope of investors in the HK Principles relative to the 2012 UK Stewardship Code, which specifically applies to institutional investors only.

Public signatories

Not applicable. In their conclusion to their consultation paper, the SFC notes that as "the Principles are voluntary in nature, their adoption and application will not be monitored at this stage."[49]

Number of signatories: Not applicable.

6.3 India

Title

Stewardship Code for Mutual Funds and All Categories of Alternative Investment Funds

Background

The Securities and Exchange Board of India (SEBI) published a circular on stewardship code for mutual funds and alternative investment funds (AIFs) in December 2019. The circular was originally scheduled to come into force on 1 April 2020 but was delayed until 1 July 2020 on account of the Covid-19 pandemic.

SEBI introduced mandatory requirements for mutual funds to disclose their voting policies and actual voting on various resolutions of their investee companies through circulars published in 2010 and 2014. The proposal for a stewardship code targeting institutional investors was initially discussed and approved in a subcommittee meeting of the Financial Stability and Development Council (FSDC), an apex-regulatory body, in 2016. Subsequently, regulators introduced three separate but similar codes for their respective sectors: for insurance companies in 2017, and subsequently revised in February 2020; for pension funds in early 2018; and most recently for mutual funds and AIFs in December 2019. For the purpose of this report, we focus on the principles of the stewardship code for mutual funds and AIFs introduced by SEBI.

[49] SFC, "Consultation Conclusions."

Definition of stewardship

SEBI's circular describes stewardship as follows:

"The importance of institutional investors in capital markets across the world is increasing the world over; they are expected to shoulder greater responsibility towards their clients / beneficiaries by enhancing monitoring and engagement with their investee companies. Such activities are commonly referred to as 'Stewardship Responsibilities' of the institutional investors and are intended to protect their clients' wealth. Such increased engagement is also seen as an important step towards improved corporate governance in the investee companies and gives a greater fillip to the protection of the interest of investors in such companies."

Governing body

SEBI

Applicable parties

- **Asset managers:** SEBI-registered asset management companies that are responsible for managing funds on behalf of their clients and asset owners
- **AIFs:** Privately pooled investment vehicles that invest funds for India or foreign investors in accordance with a defined investment policy and that are covered under SEBI's Alternative Investment Fund Regulations, 2012

Application of principles

Mandatory

Key principles/guidelines

- **Principle 1:** Formulate a comprehensive policy on the discharge of their stewardship responsibilities, publicly disclose it, and review and update it periodically
- **Principle 2:** Have a clear policy on how to manage conflicts of interest in fulfilling their stewardship responsibilities and publicly disclose it
- **Principle 3:** Monitor investee companies
- **Principle 4:** Have a clear policy on intervention in their investee companies; also where required have a clear policy for collaboration with other institutional investors to preserve the interests of the ultimate investors, which should be disclosed
- **Principle 5:** Have a clear policy on voting and disclosure of voting activity
- **Principle 6:** Report periodically on their stewardship activities

Broadly speaking, the principles in the code mirror those of the 2012 UK Stewardship Code. The devil is in the detail, however. SEBI's stewardship code provides much more operational guidance on the principles, covering, for example, aspects a conflicts of interest policy or a voting policy should address. SEBI's code also places a greater emphasis on review processes and training. On the flipside, unlike the UK Stewardship Code, SEBI's does not require an assurance opinion on engagement and voting processes.

Public signatories

Because compliance is mandatory, all mutual funds and AIFs regulated by SEBI are expected to come out with their policies by the effective date of July 1, 2020.

Number of signatories: Not applicable

6.4 Japan

Title

Principles for Responsible Institutional Investors—Japan's Stewardship Code

Background

The development of a stewardship code in Japan began in earnest in December 2012 with the establishment of Japan's Economic Revitalization Strategy. Its goal is to develop economic policies that would drive growth of the Japanese economy.[50] A top-down initiative, this was seen as part of the broader economic reform agenda driven by Prime Minister Abe Shinzo. The establishment of a stewardship code was recommended as part of the broader corporate governance reforms. The Financial Services Agency (FSA) created a council of experts in August 2013 to help formulate what would become the Principles for Responsible Institutional Investors—Japan's Stewardship Code (the Japan Code). The Japan Code was released in February 2014 and subsequently revised in May 2017. The FSA revised and released an updated Japan Code in March 2020.

[50] Financial Services Agency (FSA),The Council of Experts on the Stewardship Code, "Principles for Responsible Institutional Investors," 29 May 2017, https://www.fsa.go.jp/en/refer/councils/stewardship/20170529/01.pdf

Definition of stewardship

"The responsibilities of institutional investors to enhance the medium- to long-term investment return for their clients and beneficiaries by improving and fostering the investee companies' corporate value and sustainable growth through constructive engagement, or purposeful dialogue based on in depth knowledge of the companies and their business environment and consideration of sustainability (medium- to long-term sustainability including ESG factors) consistent with their investment management strategies)."

A unique aspect of the Japan Code is its inclusion of "corporate value and sustainable growth." This is a key message repeated throughout. That said, the term "sustainable" here does not necessarily refer to environmental or social factors, which were originally conceived only as risks.

Governing body

FSA

Applicable parties

The Japan Code primarily targets institutional investors, defined as asset managers and asset owners, investing in Japanese listed shares. The Japan Code also applies to proxy advisors and other service providers commissioned by institutional investors. In particular, the 2017 revision describes how proxy advisors should ensure sufficient resources to properly satisfy the principles laid out in the Japan Code.

Application of principles

Comply-or-explain

Key principles/guidelines

- **Principle 1:** Have a clear policy on how to fulfil stewardship responsibilities and publicly disclose it
- **Principle 2:** Have a clear policy on how to manage conflicts of interest in fulfilling stewardship responsibilities and publicly disclose it
- **Principle 3:** Monitor investee companies to appropriately fulfill stewardship responsibilities with an orientation towards the sustainable growth of the companies
- **Principle 4:** Seek to arrive at an understanding in common with investee companies and work to solve problems through constructive engagement with investee companies
- **Principle 5:** Have a clear policy on voting and disclosure of voting activity

- **Principle 6:** Report periodically to clients and beneficiaries on how stewardship responsibilities were fulfilled, including voting responsibilities
- **Principle 7:** Develop skills and resources needed to appropriately engage with the companies and to make proper judgements in fulfilling their stewardship activities based on in-depth knowledge of the investee companies and their business environment and consideration of sustainability consistent with their investment strategies
- **Principle 8:** Require service providers to endeavor to contribute to the enhancement of the functions of the entire investment chain by appropriately providing services for institutional investors to fulfil their stewardship responsibilities

In form, the Japan Code is very similar to the 2012 UK Stewardship Code, and the recently released version has also incorporated elements of the 2020 UK Stewardship Code such as an explicit principle for service providers and application of stewardship principles on other asset classes beyond listed equity. A few points are worth noting:

- One area the Japan Code looks to emphasize is a longer-term view on corporate value and growth; hence in Principle 3, on the monitoring of investee companies, "sustainable growth" is included as a focus for investors.
- Similarly, the Japan Code emphasizes a more congenial approach to investee companies, and so Principle 4 notes "constructive engagement" rather than list out ways to "escalate" as in the 2012 UK Stewardship Code.
- One area initially de-emphasized is collective engagement, which is not a separate principle as in the 2012 UK Stewardship Code. In the 2014 version of the Japan Code, collective engagement was not included in any of the principles but was subsequently added to the guidance for Principle 4 in the 2017 revision. In the latest 2020 revision, the Japan Code has changed the reference on "collective" engagement to "collaborative" engagement, similar to the 2020 UK Code.
- Finally, Principle 7 highlights the need for the knowledgeability and capability required of investors. This is not specified in the UK Stewardship Code. In this regard, the Japanese version attempts to set a higher threshold for asset owners and asset managers.

Public signatories

The FSA publishes a list of institutional investors who have notified the FSA of their intention to accept the Japan Code. The FSA updates the list as institutional investors notify it of their acceptance of the Japan Code. Most of the signatories are investment managers.

Number of signatories: 273 (as of 12/27/2019)[51]

[51] FSA, "Stewardship Code : 281 Institutional Investors Have Signed Up to the Principles for Responsible Institutional Investors as of April 30, 2020," accessed 7 May 2020, https://www.fsa.go.jp/en/refer/councils/stewardship/20160315.html

6.5 Malaysia

Title

Malaysian Code for Institutional Investors

Background

In 2011, the Securities Commission Malaysia (SC) developed their Corporate Governance Blueprint 2011 (CG Blueprint), which included several key initiatives targeting the improvement of discipline in the markets. One recommendation of the CG Blueprint was to create an "industry-driven code" to improve the accountability of institutional investors in Malaysia.[52] As a response, the Minority Shareholder Watchdog Group was formed and convened a steering committee. In June 2014, the Malaysian Code for Institutional Investors (MCII) was launched. Malaysia was the first market in ASEAN and second in Asia Pacific to launch such a code for institutional investors. This led to the establishment of the Institutional Investors Council Malaysia (IIC) in July 2015 to create greater awareness of the MCII's importance among local institutional investors.[53]

Definition of stewardship

Although the MCII is not titled as a stewardship code, it contains a definition of stewardship:

"Stewardship is investor stewardship from the perspective of a long-term institutional investor in particular asset owners such as pension funds. It includes the responsible management and oversight of assets for the benefit of the institutional investors' ultimate beneficiaries or clients. The discharge of effective stewardship responsibilities would include development of a set of principles/policies, application of the principles/policies, oversight of agents, communications of expectations and reporting to their clients or beneficiaries. These activities also include monitoring and engagement with the investee companies on matters relating to strategy, performance, risk management, voting, corporate governance or sustainability issues."

[52] Securities Commission Malaysia, "Corporate Governance Blueprint: Toward Excellence in Governance," July 2011, https://www.sc.com.my/api/documentms/download.ashx?id=0a494b24-2910-4b14-98e0-ac6b99916d87

[53] Institutional Investor Council Malaysia (IIC), "Investor Stewardship and Future Key Priorities, 2016," August 2016, http://www.iicm.org.my/wp-content/uploads/2018/05/INVESTORS-STEWARDSHIP-AND-FUTUER-KEY-PRIORITIES-2016.pdf

Governing body

IIC

Applicable parties

Institutional investors consist of asset owners and asset managers with equity holdings in corporations listed on Bursa Malaysia.

- **Asset owners:** collective investment vehicles that collect funds on behalf of their beneficiaries or clients and manage them internally or externally such as pension funds, private retirement scheme providers, insurance companies, takaful operators, and investment trusts
- **Asset managers:** agents responsible for managing the funds on behalf of the asset owners through an investment mandate
- **Service providers:** providers such as custodians, proxy advisors, investment consultants, and trustees of asset owners and asset managers

Application of principles

Voluntary

Application of the MCII is considered voluntary even though signatories are encouraged to explain how they have applied the code. Signatories can also explain why certain parts of the MCII may not be relevant to them, given their business model. In practice this appears equivalent to comply-or-explain.

Key principles/guidelines

- **Principle 1:** Disclose the policies on their stewardship responsibilities
- **Principle 2:** Monitor their investee companies
- **Principle 3:** Engage with investee companies as appropriate
- **Principle 4:** Adopt a robust policy on managing conflicts of interest, which should be publicly disclosed
- **Principle 5:** Incorporate corporate governance and sustainability considerations into the investment decision-making process
- **Principle 6:** Publish a voting policy

Several key differences exist between the MCII and the 2012 UK Stewardship Code:

- The MCII includes a specific principle promoting the integration of corporate governance and sustainability. Arguably the most proactive principle is Principle 5, which explicitly supports integration of corporate governance, sustainability, and ESG factors. The 2012 UK Stewardship Code has no equivalent principle, although the 2020 revision does include a new principle that explicitly encourages the integration of ESG factors.
- There is no specific principle that encourages collective action with other investors. In relation to engaging in investee companies, Principle 3.4 does mention engaging jointly with other intuitions on particular issues, but this point appears to be de-emphasized and vague.
- Disclosure of voting results does not appear to be emphasized within Principle 6. Whereas publication of voting policies is noted directly in the principle, the disclosure of voting activities and voting record is mentioned only in the guidelines.

Public signatories

The MCII encourages institutional investors to be signatories and to explain how they have applied the MCII principles. Institutional investors are also encouraged to have their service providers apply the principles where relevant. Hence, service providers are also encouraged to be signatories and are expected to provide annual reports on how they have applied the principles in some public form.

Number of signatories: 22 (as of 12/31/2019)[54]

[54] IIC, "List of Signatories," IIC Publications, 2019, http://www.iicm.org.my/list-of-signatories/

6.6 Singapore

Title

Singapore Stewardship Principles for Responsible Investors

Background

The Singapore Stewardship Principles for Responsible Investors (SSP) was the result of a nearly two-year effort led by an industry working group, which first met in September 2014 and was chaired by the Stewardship Asia Centre (SAC), a non-profit organization established in 2011 under the Temasek Trust. Members of this working group moved on to become members of the steering committee that helped to promote and administer the SSP.[55] The SSP was officially released in November 2016.

Subsequent to the SSP, SAC also released the Stewardship Principles for Family Businesses in October 2018. Unique to Singapore, this set of principles was created to encourage a values-based, long-term perspective among family businesses. The principles list specific values for family businesses to consider and include issues such as succession planning.[56] While in name a set of stewardship principles, the Stewardship Principles for Family Businesses in substance differs from typical stewardship codes targeted primarily at institutional investors holding minority stakes in publicly listed firms.

Definition of stewardship

"Stewardship is about building and growing sustainable businesses to produce long-term benefits for all stakeholders, and in the process contributing to the community and economy as a whole. It goes beyond short-term considerations and includes the sustainability of a company's long-term performance."

Governing body

SAC

[55] Stewardship Asia Centre (SAC), "Shareholder Stewardship Gets a Push in Singapore," Directors' Bulletin 2017 Q1, https://www.sid.org.sg//images/PDFs/Publications/DirectorsBulletin/2017Q1/Shareholder%20stewardship%20gets%20a%20push%20in%20Singapore.pdf

[56] SAC, "Stewardship Principles for Family Businesses Fostering Success, Significance and Sustainability," Stewardship Asia Publications, 2018, https://www.stewardshipasia.com.sg/sites/default/files/SSP-brochure-0913_approved%20for%20printing.pdf

Applicable parties

The SSP refers to the term "investors" in a broad sense to include institutional investors who are asset owners and asset managers. It states that the stewardship principles are "most applicable to Singapore-based institutional investors with equity holdings in Singapore-listed companies." They also apply to other investor groups and to service providers that give advice on investment and corporate governance to investors, including proxy advisors and investment consultants.

Application of principles

Voluntary

The SSP differs from the 2012 UK Stewardship Code in adopting a purely voluntary application. The argument is that effectiveness is based on "application in the right spirit." The SSP specifically notes that the principles "are not intended to be a 'box-ticking' exercise." Furthermore, the voluntary nature of adoption is meant to limit any administrative burden to subscribing to the SSP.

Key principles/guidelines

- **Principle 1:** Establish and articulate their policies on their stewardship responsibilities
- **Principle 2:** Communicate regularly and effectively with their investee companies
- **Principle 3:** Actively monitor their investee companies
- **Principle 4:** Make known their approach to managing conflicts of interest
- **Principle 5:** Establish clear policies on voting and exercise their voting rights in a responsible fashion
- **Principle 6:** Document and provide relevant updates on their stewardship activities
- **Principle 7:** Willingly engage responsibly with one another where appropriate

The SSP largely mirrors the principles of the 2012 UK Stewardship Code. For example, similar to the 2012 UK Code, only a passing mention is made to social and environmental stewardship within Principle 2 under topics to engage investee companies with. One noted difference is the SSP application is on a voluntary basis only.

Public signatories

The SSP has no signatories as such and no mechanism for monitoring or enforcement. The IMAS website does list members who express their support for the SSP.[57]

Number of supporters: 54 (as of 9/3/2019)[58]

6.7 South Korea

Title

Korea Stewardship Code—Principles on the Stewardship Responsibilities of Institutional Investors

Background

The Korea Stewardship Code (the Korea Code) was released after two years of development and extensive consultation with various stakeholders.[59] Initially a draft was presented by Korea's Financial Services Commission in December 2015, but this was not adopted because the local business community pushed back with concerns over excessive influence from investors.[60] In response, in August 2016 a private industry group, the Korea Corporate Governance Services (KCGS), created a separate Stewardship Code Council consisting of members from the private sector. This eventually led to the current version, which was finalized in December 2016.

Definition of stewardship

"The responsibility institutional investors bear in taking care of or managing assets entrusted by others refers to a sense of responsibility to promote the mid- to long-term interests of their clients and ultimate beneficiaries by pursuing the mid- to long-term value enhancement and sustainable growth of investee companies."

[57] Investment Management Association of Singapore (IMAS), "Companies Expressing Support for the Singapore Stewardship Principles ('SSP')," 3 September 2019, http://www.imas.org.sg/Articles/267-singapore-stewardship-principles-ssp-.html

[58] IMAS, "Companies Expressing Support," 3 September 2019, http://www.imas.org.sg/public/media/2019/09/03/1722_190903_-_SSP_supporters_overall_.pdf

[59] Korea Corporate Governance Service (KCGS), "Korea Stewardship Code," History, 2018, http://sc.cgs.or.kr/eng/reform/progress.jsp

[60] Mee-Hyon Lee, "Introduction of the Stewardship Code in Korea," accessed 7 May 2020, https://sydney.edu.au/law/events/2017/Aug/EMWpaper_Meehyon_Lee.pdf

Governing body

KCGS

Applicable parties

The Korea Code applies to domestic and overseas institutional investors holding shares of publicly listed companies in Korea, more specifically, asset owners and asset managers. Any institutional investor from Korea or abroad is free to participate in the Korea Code if it has shareholdings in a locally listed company.

Uniquely, the Korea Code also notes that private equity funds, including limited and general partners, can participate as asset owners and asset managers. Similarly, discretionary investment managers may also participate, even though local laws prevent them from voting on behalf of their clients. By participating in other forms of shareholder activities, such managers can still exercise a degree of stewardship.[61]

Application of principles

Comply-or-explain

Key principles/guidelines

- **Principle 1:** Formulate and publicly disclose a clear policy to faithfully implement their responsibilities
- **Principle 2:** Formulate and publicly disclose an effective and clear policy as to how to resolve actual or potential problems arising from conflicts of interest in the course of their stewardship activities
- **Principle 3:** Regularly monitor investee companies to enhance investee companies' mid- to long-term value and thereby protect and raise their investment value
- **Principle 4:** While aiming to form a consensus with investee companies, where necessary formulate internal guidelines on the timeline, procedures, and methods for stewardship activities
- **Principle 5:** Formulate and publicly disclose a voting policy that includes guidelines, procedures, and detailed standards for faithfully exercising votes, and publicly disclose voting records and the reasons for each vote so as to allow the verification of the appropriateness of their voting activities

[61] KCGS, "Korea Stewardship Code," Information, 2018, http://sc.cgs.or.kr/eng/resources/faq.jsp

- **Principle 6:** Regularly report their voting and stewardship activities to their clients or beneficiaries
- **Principle 7:** Have the capabilities and expertise required to implement stewardship responsibilities in an active and effective manner

The Korea Code is broadly aligned with the principles of the 2012 UK Stewardship Code, with a few exceptions:

- Principle 4 states that investors should try to "form a consensus" with investee companies. This approach differs from that of the 2012 UK Stewardship Code, which provides guidelines on escalation of stewardship activities. The wording in the Korea Code appears to suggest that investors may wish to refrain from taking strong actions against issuers.
- Unlike the 2012 UK Stewardship Code, the Korea Code does not include explicit mention of collective engagement among investors.
- Principle 7 is unique in requiring "capabilities and expertise" for stewardship activities. This seems to imply a higher standard of compliance, which also potentially requires more resources from signatory firms. The Korea Code does consider "available internal resources and financial conditions" and suggests that external services should be used.
- Notably, for signatories to the Korea Code who are already in compliance with overseas stewardship codes or the PRI, the Korea Code does not require separate disclosure and reporting, so long as any differences in the specifics between the Korea Code and the overseas codes are reflected and explained.

Public signatories

Institutional investors are asked to publicly disclose their compliance on their websites.

Number of signatories: 116 (as of 1/9/2020)[62]

[62] KCGS, "Korea Stewardship Code," Participants List, 2018, http://sc.cgs.or.kr/eng/participation/investors.jsp

6.8 Taiwan

Title

Stewardship Principles for Institutional Investors

Background

In December 2013, the Financial Supervisory Commission in Taiwan (FSC TW) published a five-year Corporate Governance Roadmap.[63] This eventually led the Taiwan Stock Exchange (TWSE) to create the Corporate Governance Center to promote corporate governance practices in cooperation with the government and relevant stakeholders. In response to the increasingly important role institutional investors had in monitoring investee companies, the FSC TW instructed the Corporate Governance Center to prepare Stewardship Principles for Institutional Investors (the TWSE Stewardship Principles), opened for public consultation in February 2016 and officially launched in June 2016.[64] In March 2020, the TWSE consulted the market on revisions to the Stewardship Principles. Proposed changes included new references to sustainability and ESG factors, commitment by passive investors to engagement and voting, disclosures of voting rationale, and enhanced reporting requirements.

Definition of stewardship

During the consultation, the TWSE defined stewardship as follows:

"Responsibilities of investors as equity owners or managers are referred to as stewardship responsibilities. It is more than exercise of shareholder's rights at shareholder's meetings but involves monitoring investee companies' strategies, risks, capital structures, corporate governance, and investment returns, as well as to seek the greatest interests for investee companies and the shareholders through constructive dialogue and engagement."

Governing body

TWSE Corporate Governance Center

[63] Financial Supervisory Commission, Taiwan (FSC), "Corporate Governance Roadmap, 2013," accessed 7 May 2020, https://cgc.twse.com.tw/img/Corporate%20Governance%20Roadmap%202013.pdf

[64] Corporate Governance Center, Taiwan (CGC), "Stewardship Principles for Institutional Investors," Taiwan Stock Exchange / Corporate Governance Center, accessed 7 May 2020, https://cgc.twse.com.tw/static/stewardship_en.pdf

Applicable parties

Institutional investors under the TWSE Stewardship Principles are defined as equity owners or managers investing in the Taiwan capital market, whether domestic, foreign, governmental, or private institutions.

Equity owners are defined as persons investing with their own funds or funds collected from beneficiaries, such as pension funds, insurance companies, and investment trusts.

Equity managers are defined as persons investing with funds entrusted to management by their clients, such as discretionary investment under a mandate of equity owners.

Application of principles

Comply-or-explain

Key principles/guidelines

- **Principle 1:** Establish and disclose stewardship policies
- **Principle 2:** Establish and disclose policies on managing conflicts of interest
- **Principle 3:** Regularly monitor investee companies
- **Principle 4:** Maintain an appropriate dialogue and interaction with investee companies
- **Principle 5:** Establish clear voting policies and disclose voting results
- **Principle 6:** Periodically disclose to clients or beneficiaries the status of fulfilment of stewardship responsibilities

The TWSE Stewardship Principles are mostly aligned with the principles of the 2012 UK Stewardship Code, with the notable exception of collective engagement as a separate principle (Principle 5 of the 2012 UK Stewardship Code). In Taiwan, this was not included in the initial draft of the TWSE Stewardship Principles but has been incorporated as sub-principle 4.3, noting:

"Under circumstances where an institutional investor judges it necessary to take action, it may act collectively with other institutional investors, so as to protect the rights and interests of clients or beneficiaries."

Although this sub-principle is included, the Taiwan Stewardship Principles does not explicitly define the need for disclosure of any policies concerning collective engagement, which is noted in the UK Stewardship Code.

Similarly, Principle 4 makes no explicit mention of escalation of stewardship responsibility as noted in the UK code, though possible methods for dialogue and interaction with investee companies are included.

Public signatories

TWSE encourages institutional investors to publicly sign up and to display their commitment. Signatories are publicly disclosed on the Corporate Governance Center website.[65]

Number of signatories: 149 (as of 12/31/2019)

6.9 Thailand

Title

Investment Governance Code for Institutional Investors

Background

The Securities and Exchange Commission (SEC) of Thailand developed the Investment Governance Code (I Code) alongside the Corporate Governance Code (CG Code). Both were adopted in early 2017. The development of the I Code followed a peer review and consultation with relevant local stakeholders, including the Office of Insurance Commission, Government Pension Fund, Social Security Office, Federation of Thai Capital Market Organizations, Association of Investment Management Companies, Thai General Insurance Association, Thai Life Assurance Association, Association of Provident Funds, and directors and management of asset management companies. Derived from the principles set out in the UK Stewardship Code, the I Code is a voluntary code that applies to institutional investors.[66]

[65] CGC, "List of Signatories," Taiwan Stock Exchange / Corporate Governance Center, accessed 7 May 2020, https://cgc.twse.com.tw/stewardshipList/listEn

[66] Securities and Exchange Commission, Thailand (SEC), "Investment Governance Code for Institutional Investors (I Code)," Rules/ Regulations, 2019, https://www.sec.or.th/cgthailand/en/pages/rulesregulation/icodeii.aspx

Definition of stewardship

Notably, the SEC has chosen the term "investment governance" rather than "stewardship." Although this semantic choice does not affect the substance of the code, it perhaps better mirrors the use of the term "corporate governance" as it relates to companies. Within the objectives of the I Code the SEC notes:

"Institutional Investors . . . have important investment management responsibilities to ensure delivery of sustainable long-term value to their investment owners and beneficiaries. These responsibilities include consideration of the risk profiles of Investee Companies. Institutional Investors should ensure to invest in companies that integrate Environment, Social and Governance (ESG) factors in their business practices. Furthermore, in the event that an Investee Company fails to implement ESG principles, the Institutional Investor should engage with the Investee Company to improve the company's ESG performance."

Governing body

SEC, Thailand

Applicable parties

- **Asset managers:** SEC-licensed asset management companies responsible for managing funds on behalf of their clients and asset owners
- **Asset owners:** organizations that pool funds of clients in collective investment vehicles, including government pension funds, social security funds, insurance companies, provident funds, and the like
- **Related service providers:** fund supervisors, custodians, proxy advisors, investment consultants, and trustees who support the activities of asset owners and asset managers

Application of principles

Comply-or-explain

Key principles/guidelines

- **Principle 1:** Adopt a clear written investment governance policy
- **Principle 2:** Properly prevent and manage conflicts of interest and prioritize advancing the best interest of clients
- **Principle 3:** Make informed investment decisions and engage in active ongoing monitoring of investee companies

- **Principle 4:** Apply enhanced monitoring of and engagement with the investee companies if monitoring pursuant to Principle 3 is considered insufficient
- **Principle 5:** Have a clear policy on exercising voting rights and disclosure of voting results
- **Principle 6:** Act collectively with other investors and stakeholders as appropriate
- **Principle 7:** Regularly disclose the investment governance policy and compliance with it

The principles in the I Code closely follow those of the 2012 UK Stewardship Code. One notable difference, however, is in the inclusion of ESG factors in a number of areas in the I Code. In the 2012 UK Stewardship Code, ESG factors are explicitly referenced only in Principle 4, whereas the integration of ESG factors is included in the objective statement as well as in the details of Principles 1, 3, and 6 of the Thai I Code. In fact, Principle 3.3 provides a clear list of ESG factors to be considered, which is unique among stewardship codes in Asia Pacific.

Public signatories

The SEC suggests that all institutional investors should adopt the I Code voluntarily and become signatories by filing a letter of intent with the office of the SEC. The SEC publicly discloses the list of signatories. Signatories are also expected to publish a letter of intent on their websites and in their annual reports.

Number of signatories: 65 (as of 12/31/2019)[67]

[67] SEC, "Investment Governance Code," Rules/ Regulations, List of Code Signatories, 2019, https://www.sec.or.th/cgthailand/en/pages/rulesregulation/icodelists.aspx

7. Conclusions and Recommendations

Stewardship codes have evolved significantly over the last decade and will continue to remain an important form of guidance for institutional investors. Following the update to the UK Stewardship Code in 2020, CFA Institute expects that other jurisdictions will look to refresh their own stewardship codes, as Japan has done. This report has identified several common trends and issues that need to be addressed to increase awareness and strengthen enforcement of stewardship codes, thereby improving their effectiveness.

Trends

- Inclusion of environmental and social factors in the definition of stewardship
- Extension of the scope of stewardship codes to asset classes beyond listed equities
- Application of the principles of stewardship to service providers
- A shift from reporting on policy disclosures to reporting on outcomes

Issues

- Limited enforcement
- Uncertain benefits
- Cost of compliance
- Ownership structure
- If and how passive investors are carrying out their stewardship activities
- Cultural norms and local context
- Conflict of interest

As stewardship codes become more widespread across Asia Pacific, CFA Institute encourages the establishment of codes that promote an outcomes-focused adherence to stewardship principles. Compliance should be monitored to ensure that the stewardship code truly raises the bar of shareholder engagement rather than incentivizing a "tick-the-box" mentality.

We offer the following recommendations for the creation, revision, and application of stewardship codes:

1. **Aspirational standard: Codes should remain a comply-or-explain standard. They should be sufficiently monitored to ensure that signatories follow through on stated policies and live up to a higher professional standard.**

Investors are more receptive towards stewardship codes that remain a comply-or-explain standard than to ones that become statutory law. Moreover, it is difficult to create a prescriptive set of rules that is not only flexible enough to suit a broad range of investors but also specific enough to be properly enforced. A stewardship code should incorporate public recognition of compliance by signatories. Such recognition reinforces the role of stewardship codes as an aspirational standard rather than a mandatory rule. The bodies overseeing stewardship codes should ensure that signatories have relevant policies in place and that they have followed up on their responsibilities. This requires a higher standard of oversight from such bodies and from investors. If industry players wish to create and sign on to such codes, they do it out of their free will, with full intent and conviction. When governments or regulatory authorities mandate such matters, the firms' main motivation is compliance. By complying, a firm does not signal virtue and caring, but only that it follows the rules.

2. **Promotion and awareness: Local regulators or industry bodies should ensure that institutional investors have ample opportunities to learn in detail how best to act responsibly as shareholders and how to apply stewardship principles in practice.**

Programs that aim to increase institutional investors' awareness of responsible share ownership should be more widely promoted. Within Asia Pacific, the awareness of stewardship codes is higher in Japan, where the top-down push on corporate governance reform is stronger. Such awareness remains relatively low in other markets, and more support is required from regulators or other relevant industry bodies. While CFA Institute supports stewardship codes as a comply-or-explain standard, whether to comply should be decided only with sufficient knowledge of what is expected of signatories. Such knowledge should focus on how investors can create better outcomes rather than on policy implementation.

3. **Need to establish global best practices, with flexibility to cater for market differences: Notwithstanding a high degree of overlap in core stewardship principles, significant differences in objectives, market structures, and corporate governance frameworks exist across markets. Oversight bodies may wish to address the most pressing issues in their own markets when designing their codes.**

Several global standards for responsible ownership already exist, including the PRI and the ICGN Global Principles. CFA Institute has identified common definitions and principles among market-specific and global stewardship codes. These include the following:

- Establishing and disclosing a stewardship policy
- Having a policy to manage conflicts of interests
- Monitoring and engaging with investee companies
- Disclosing voting policies and voting actions taken
- Reporting to clients and beneficiaries on stewardship responsibilities

These principles, together with a focus on long-term investing, form the core of essentially all stewardship codes in Asia Pacific. Convergence of principles of and approaches to stewardship would allow institutional investors operating in several jurisdictions to adopt a more streamlined approach. Nevertheless, oversight bodies could create supplemental principles to recognize differences in stewardship codes among jurisdictions and to accommodate local practices. This would allow investors to subscribe to a core stewardship code and to provide supplemental documentation for each market. CFA Institute believes that minimizing the complexity of reporting will lead to a higher level of adoption and a stronger focus on outcomes rather than on policies.

4. **Lead from the top: Stewardship codes should be promoted from the highest levels of the investment chain to align incentives of all parties.**

At the apex of the investment chain, institutional asset owners, such as national pension funds, sovereign wealth funds, insurance firms, endowments, and corporate pensions, have a unique responsibility. Because asset owners provide incentives to asset managers and services providers, they have a great deal of influence in motivating asset managers to be more active stewards. For example, the Government Pension Investment Fund of Japan has been vocally pushing for increased stewardship of its assets.[68] Such leadership from the largest asset owners could create a virtuous cycle of increased awareness and higher level of adoption by other asset owners and asset managers.

[68] "World's Biggest Pension Fund Steps Up Passive Stewardship Efforts," Financial Times, accessed 7 May 2020, https://www.ft.com/content/8e5e0476-f046-3316-b01b-e5b4eac983f1

5. **Inclusion of ESG: Material ESG factors are key drivers of long-term value, and it is important for investors to integrate such factors in the investment process so that investors and their beneficiaries benefit from a more fulsome analysis.**

Recently updated codes have incorporated the consideration of ESG factors as a key principle. We welcome the development. CFA Institute has long supported the incorporation of material ESG factors in the investment process. Explicit inclusion of ESG factors in stewardship codes not only encourages investors to be more mindful of such issues but also motivates listed companies to consider ESG factors in their business strategies and risk assessments for the sake of long-term value creation for investors.

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The mission of CFA Institute is to promote the highest standards of ethics, education, and professional excellence in the financial industry. As part of this mission, we strive to strengthen investor protection, market integrity, and professionalism of industry practitioners.

To this end, CFA Institute supports establishing clear guidelines for asset owners, asset managers, investment advisors, and other financial professionals to help them discharge their duties to the ultimate benefit of their clients and the society.

Stewardship codes play an important part in protecting the interests of investors and other stakeholders by promoting best practices and a focus on long-term outcomes among asset owners. We welcome and support the ongoing development of stewardship codes in all markets, and encourages their adoption and implementation by practitioners.

Appendix

A. United Kingdom

Title

UK Stewardship Code

Background

Following the publication of the Walker Review in November 2009, the FRC created a code of best practices in stewardship for institutional investors of UK listed companies. It was based on the UK Code on the Responsibilities of Institutional Investors, originally drafted by the now defunct ISC in 2002.[69] After a public consultation, the FRC published the first version of the UK Stewardship Code in July 2010. A revised version published in September 2012 (2012 Code) included more guidance on the respective responsibilities of asset managers and asset owners, clearer explanations on conflicts of interest, and greater assurance of stewardship activities. In 2016, a tiering system for signatories was adopted. Following the Kingman Review in December 2018, the FRC pursued a further revision of the stewardship code. The updated code (2020 Code) was published in October 2019 and took effect from January 2020.

Definition of stewardship

- **2012 Code:** *"Stewardship aims to promote the long-term success of companies in such a way that the ultimate providers of capital also prosper. Effective stewardship benefits companies, investors and the economy as a whole."*
- **2020 Code:** *"Stewardship is the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society."*

The major change in the definition of stewardship in the 2020 Code is the inclusion of sustainability, environmental, and social benefits. This was not necessarily a unanimously

[69] FRC, "Origin of the UK Stewardship Code," accessed 7 May 2020, https://www.frc.org.uk/investors/uk-stewardship-code/origins-of-the-uk-stewardship-code

desired revision, as approximately half of the consultation responses to the 2020 Code did not believe environmental and social issues were primary goals of stewardship.[70]

Governing body

FRC

Applicable parties

- **2012 Code:** asset managers, asset owners, and service providers of UK listed equities
- **2020 Code:** separate principles for asset owners/asset managers across asset classes and service providers

The 2020 Code expands its application by incorporating asset classes other than listed equity. Specific guidelines govern how listed equity and fixed-income signatories may differ in their approach to reporting. Also, the 2020 Code provides a separate set of principles for service providers.

Application of principles

- **2012 Code:** Comply-or-explain
- **2020 Code:** Apply-or-explain

The 2020 Code remains voluntary and adopts an apply-and-explain approach to compliance. While this is a slight difference in wording, the reporting expectations for signatories of the 2020 Code are higher. In particular, signatories are expected not just to report on their policies and compliance but also to describe the effectiveness and outcomes of their stewardship activities. A key criticism of the 2012 Code, and of stewardship codes in general, is the fear that compliance may become a box-ticking exercise. Specifying the need to describe effectiveness and outcomes, however, raises the bar for compliance. This is also consistent with the recommendations in the Kingman Review.

[70] FRC, "Consulting on a Revised UK Stewardship Code," Feedback Statement, October 2019, https://www.frc.org.uk/getattachment/2912476c-d183-46bd-a86e-dfb024f694ad/191023-Feedback-Statement-Consultation-on-revised-Stewardship-Code-FINAL.pdf

Key principles/guidelines

2012 Code

- **Principle 1:** Publicly disclose their policy on how they will discharge their stewardship responsibilities
- **Principle 2:** Have a robust policy on managing conflicts of interest in relation to stewardship that should be publicly disclosed
- **Principle 3:** Monitor their investee companies
- **Principle 4:** Establish clear guidelines on when and how they will escalate their stewardship activities
- **Principle 5:** Be willing to act collectively with other investors where appropriate
- **Principle 6:** Have a clear policy on voting and disclosure of voting activity
- **Principle 7:** Report periodically on their stewardship and voting activities

2020 Code

Principles for Asset Owners and Asset Managers

- **Purpose and Governance**
  1. Purpose, strategy, and culture
  2. Governance, resources, and incentives
  3. Conflicts of interest
  4. Promotion of well-functioning markets
  5. Review and assurance

- **Investment approach**
  6. Client and beneficiary needs
  7. Stewardship, investment, and ESG Integration
  8. Monitoring of managers and service providers

- **Engagement**
  9. Engagement
  10. Collaboration
  11. Escalation

- **Exercising rights and responsibilities**

  12. Exercise of rights and responsibilities

Principles for Service Providers

1. Purpose, strategy, and culture
2. Governance, resources, and incentives
3. Conflicts of interest
4. Promotion of well-functioning markets
5. Support of client's stewardship
6. Review and assurance

The 2020 Code has been revised significantly, expanding the number of principles from seven to 12. The content is similar, but the 2020 Code has a wider remit and now incorporates sustainability, asset classes beyond listed equities, reference to adequate governance and resources, better disclosure of investors' stewardship practices and outcomes, and new principles covering service providers, among other changes. One key change is that ESG integration is elevated to a separate principle (Principle 7), further emphasizing the importance of sustainability issues in the updated 2020 Code. There are also wording changes such as the shift from "collective engagement" to "collaborative engagement" in Principle 10.

The format of the principles in the 2020 Code has also changed. Rather than providing guidance on principles, each principle now sets out reporting expectations with specific activities and outcomes to be disclosed by signatories. This has shifted the focus from policy reporting to an outcomes-based disclosure.

Furthermore, the 2020 Codes provides six principles for service providers. These help to clarify the specific principles most relevant to service providers rather than suggest that all principles apply.

Public signatories

In 2016 the FRC introduced a system of tiering signatories as a method to assess signatories by the quality of their reporting.[71] This initially included three tiers for asset managers, with the bottom tier, Tier 3, needing significant reporting improvements. In 2017, after engagement with the FRC, some Tier 3 signatories made sufficient improvements to be upgraded to Tier 1 and 2, while the rest withdrew their names from the list of signatories. Since then there have only been two tiers.[72]

The 2020 Code requires signatories to submit a single stewardship report to cover how they have applied the principles of the 2020 Code in the previous 12 months. This includes reporting on activities and outcomes achieved. The report is expected to be updated and resubmitted annually. The FRC will be responsible for monitoring the reporting quality of these submissions.

Number of signatories

	Tier 1	Tier 2
Asset managers[73]	120	57
Asset owners[74]	81	22
Service providers[75]	12	–
Total (Tier 1 and Tier 2)	292	

[71] FRC, "Tiering of 2012 Stewardship Code Signatories," accessed 7 May 2020, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements

[72] Rust, "FRC Scraps Lowest Category."

[73] FRC, "Asset Managers," accessed 8 May 2020, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements/asset-managers

[74] FRC, "Asset Owners," accessed 8 May 2020, https://www.frc.org.uk/investors/uk-stewardship-code/uk-stewardship-code-statements/asset-owners

[75] FRC, "Service Providers," accessed 8 May 2020, https://www.frc.org.uk/investors uk-stewardship-code/uk-stewardship-code-statements/service-providers

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