

Market Conduct Division
The Treasury
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Greater transparency of proxy advice

Submission by the Responsible Investment Association Australasia

The Responsible Investment Association Australasia (RIAA) welcomes the opportunity to make a submission to the Treasury on its consultation into the adequacy of the current regulatory regime and help develop reform options that would strengthen the transparency and accountability of proxy advice.

About RIAA and our members

RIAA champions responsible investing and a sustainable financial system in Australia and New Zealand and is dedicated to ensuring capital is aligned with achieving a healthy society, environment, and economy.

With over 350 members managing more than \$9 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across Australia and New Zealand. RIAA's membership includes superannuation funds, fund managers, banks, consultants, researchers, brokers, property managers, community trusts, foundations, faith-based groups, financial advisers, financial advisory groups, and others involved in the finance industry, across the full value chain of institutional to retail investors. As of December 2020, RIAA has 23 RSE members providing 6% of its annual operating revenue.

Scope of this submission

1. ensuring independence between superannuation funds and proxy advice
2. facilitating engagement between companies and proxy advisers

Key recommendation

RIAA's membership is broad, and members' business models are equally diverse. However, making voting records public is a sound governance practice; leading responsible investors are already doing this as a demonstration of them delivering on their stewardship responsibilities. Our [Responsible Investment Certification Program](#) requires this transparency as a demonstration of this leading commitment. The challenges outlined by Treasury may be better addressed by the introduction of a **government-supported, Stewardship Code** that would cover superannuation funds and other asset managers.

Despite the efforts of the Financial Services Council in launching the first industry code in 2017, as of 2019, only eight RSEs are required to comply with it. Furthermore, the code is largely designed for investment managers rather than asset owners, but to the extent that an FSC asset-owner member manages money in-house it is covered by the code. In 2018, Australian Council of Superannuation Investors introduced its stewardship code and as at November 2019, 14 of APRA's 50 largest regulated funds were signatories.

Treasury building a government-supported Stewardship Code, modelled on the UK version, would go a long way towards addressing the issues outlined in this consultation paper.

Context – Super funds, stewardship, and the use of proxy advisers

The context in which RIAA's submission is made, comprises the following facts:

- a. Based on the SIS Act, trustees of RSEs are legally obligated to act the best interests of beneficiaries. Super fund beneficiaries are aged anywhere between 16 and 83 years, or even older. Trustees, or fiduciaries are making decisions for a broad range of member interests over very large timeframes.
- b. Trustees are obligated to act prudently, by for example, fulfilling stewardship duties, when making investment decisions on behalf of beneficiaries.
- c. The common understanding of being a fiduciary in the 21st Century, among other things, includes voting on as many company resolutions as meaningfully possible. As universal owners, superfunds are likely to hold many of the 2,033 companies listed on the ASX and possibly thousands more of others listed in markets overseas.
- d. As explained in Treasury's consultation paper, given the volume of company resolutions a trustee may be required to vote on each year, some super funds engage proxy advisers to provide additional information and recommendations on how to exercise their voting rights.
- e. Proxy advice is one of many inputs into voting decisions; it is not the only source of information – super funds also consider the information including broker research (and others) to inform their analysis and decisions.
- f. Quality professional advice and information is essential for fiduciaries to navigate the increasingly complex area of corporate governance, environmental, and social issues. By engaging proxy advisers to assist with a complex and sizable task, super fund trustees are more likely to be able to exercise these duties, than not, and create cost efficiencies thereby avoiding additional costs being passed on to beneficiaries.

Context – the use of proxy advice by super funds

It is still a matter for the super fund to ultimately determine how to exercise their voting rights. Industry and government research shows that it is the case that super funds are exercising their own views when it comes to voting. In ASIC's 2017 review:

“There were also reports during the 2017 AGM season of large institutional shareholders deciding to vote against resolutions that were the subject of a ‘for’ recommendation by proxy advisers. This is consistent with representations made to ASIC by institutional shareholders that they do not follow proxy advisers’ recommendations automatically, but make their own voting decisions,”¹

¹ <https://www.afr.com/companies/financial-services/push-to-kneecap-super-proxy-advisers-20210430-p57nvp> - referring to earlier article at <https://www.afr.com/companies/companies-proxies-told-to-play-nice-20180627-h11xpn>

Interesting RIAA's own [Responsible Investment Super Study 2019](#) also showed considerable divergence of APRA's largest regulated RSEs from proxy advisory voting advice.

“Of the 30 [RSEs] providing responses to how they voted in 2018-19, two funds voted with the company board and five funds voted with their proxy voting adviser on every occasion. In contrast to this, three funds voted independently of board and proxy voting advisers on at least 10% of occasions.”

Addressing the terms of reference

1. Ensuring independence between superannuation funds and proxy advice

Codifying aspects of Option 1 (improved disclosure of trustee voting) as mandatory, would deliver additional transparency to the superannuation sector and members of superannuation funds, that we believe is strongly consistent with leading practice, as set out in stewardship codes that have been developed in various markets globally (see for example the [UK's Financial Reporting Council's Stewardship Code 2020](#)). Voting and engagement activities are seen globally as leading practice for investors to ensure they are protecting and enhancing the investment outcomes for beneficiaries. A recommendation to develop a stewardship code in Australia was part of the [Australian Sustainable Finance Roadmap](#) report launched in December 2020 (recommendation 21).

The format for reporting would need to be meaningful and further consultation may be required to identify the key stakeholders who would use this information, the format in which they need it and any other content or process aspects to enhance usefulness.

The burden for compiling and delivering this reporting would rest on the super funds and their suppliers (including both proxy advisers and underlying fund managers in the case where equities are managed by underlying managers). As above, RIAA recommends engaging with RSEs to understand how this can be most efficiently and effectively done. It would not be helpful to unduly create reporting obligations that are costly and passed through to beneficiaries, without being useful.

Proxy adviser business models depend on them understanding their client needs, executing sound research, and providing considered recommendations to their clients. A super fund analysing the advice from a proxy adviser over how to vote on company resolutions is no different to a super fund receiving advice from a human resources agency on how to restructure its REM system. A prudent trustee would first check the alignment of the advice with the scope of work agreed.

2. Facilitating engagement between companies and proxy advisers

Transparency and scrutiny are part-and-parcel of being a publicly listed company, and so directors should not shy away from such engagement.

Options 3 and 4 are challenging to support, for the following reasons:

1. **Independence comprised:** If implemented, these options could unintentionally diminish the independence of research provided and relied upon by super funds, ultimately impacting the super fund beneficiary.
2. **Regulatory bias:** The options do not provide a level playing field for all the other advice that goes into investment decisions, such as broker research and/or the underlying managers of equities that are engaged to vote for and on behalf of the holdings invested in by the asset manager for the RSE.

3. Beneficiary cost burden: these measures would add compliance costs to super funds which would ultimately be borne by beneficiaries.
4. Responsibility shifting: the options shift the burden of responsibility from companies – who are ultimately the ones being held account for their behaviours, disclosures etc. – onto proxy advisers and their clients. Done well, information being voted on in an AGM, should be relevant, reliable, and accessible, meaning that it is in the domain of shareholders in the least (or ideally it is public). Accordingly, proxy advisers, relying on this information should be adequate. Information that is *not* in the public domain or requires further context to be provided by the company, should probably already be in the public domain and/better disclosed to key stakeholders, such as shareholders. The ASX platform exists for public announcements and making these disclosures is responsibility of company directors. Given there are so few proxy advisory firms operating in Australia, then engaging with them should be relatively cost efficient for companies – rather than putting the onus of responsibility on the proxy adviser to engage with companies.

Summary

Overall, RIAA supports the concept that trustees of RSEs should be held to the highest standards of governance, transparency, and efficiency to ensure assets are managed to maximise members' retirement savings. Therefore, RIAA supports strong transparency in voting undertaken by super funds. However, we are concerned that the proposed options are overreaching, are inconsistent with how other parts of the financial system are regulated and risk passing on significant additional costs to beneficiaries.

It is our view that there is a better approach to ensuring high levels of transparency based on an industry-wide standard for disclosure and recommends to the Treasury the [UK Stewardship Code](#) as an example of a suitable model. Given the existence of the two Australian voluntary stewardship codes to date, it may be appropriate for any incoming code to have support from the Commonwealth to administer and cover super funds and asset managers.

Should you wish to receive a briefing on the UK Stewardship Code, and how it is currently used by some of RIAA's members, please do not hesitate to contact me at RIAA.

Yours sincerely,



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