



2nd April 2019

STEWARDSHIP 360 PROGRAMME

Making the case for the long term is one of the Forum's core objectives. The Stewardship 360 Programme focuses on issues where we can make a unique contribution.

12 Members joined a working group organised by the Investor Forum to investigate voting issues connected to ADR programmes of UK-listed companies.

The working group reviewed the programmes and documentation of the 29 UK-listed companies with listed ADRs. A number of participating members reviewed ADR voting solicitation records.

We sought input from a number of experts, including our Legal Panel. We would like to thank them for their assistance on this project.

The ADR project page in the Members' area of our website contains further background information, extracts from each company's ADR agreement and the letters exchanged with the Forum.

Background

Investors have long identified voting issues with American Depositary Receipt (ADR) programmes. The International Corporate Governance Network (ICGN) put forward recommendations to improve practice in 2004, but the global nature of the issuer base hindered adoption.

During 2018, a Member alerted us to two ADR voting issues: **auto-proxy** (the discretionary voting by companies of the uninstructed shares of ADR holders) and **non-solicitation** of votes. They asked us to investigate these issues, as they **have the potential to impact not only ADR holders but also aggregated voting outcomes, and therefore all shareholders.**

Our investigations indicated that **focus should be on auto-proxy**, as voting non-solicitation issues were rare. The Forum wrote tailored letters directly to the Chairs of the 28 UK-listed companies with listed ADRs, applauding those with best practice arrangements and requesting clarification or specific changes in other cases.

Summary

- **Positive response** – 9 of the 11 companies with auto-proxy discretion in their Depositary Agreements (DAs) committed not to use this discretion.
- **Best practice** – A best practice standard has now been established with UK ADR issuers.
- **Further engagement** – 10 companies committed to amend their agreements to address one or both issues, but 12 companies have committed only to a 'review'. Further encouragement from shareholders to amend wording would be welcome.
- **Extending the impact** – We are liaising with ICGN to establish if industry bodies in other markets can utilise our approach, with a view to establishing a global standard.



Executive summary of results and next steps

- ADRs are complex instruments, and holders do not have all the rights of shareholders. The rights that ADR holders do have can be difficult to understand as the contractual language is complex and opaque and does not always appear to have investor interests in mind.
- **The companies we wrote to generally acknowledged the concerns of members regarding the inconsistency of elements of the Depositary Agreements (DAs) of their ADR programmes with principles of good UK corporate governance.**
- **Of the 11 companies we approached to request a commitment not to use auto-proxy rights in future, 9 agreed, one did not respond, and one did not agree.** 7 agreed to amend their DAs at the time of the next review to remove auto-proxy rights, with others stating that they would consider amendment. Ryanair intends to continue to use auto-proxy rights; they have agreed to disclose the percentage of votes cast in this manner and how these votes were cast, but only in the following year's Annual Report.
- **The absence of pro-active voting solicitation does not appear to be a widespread issue.**
 - Those companies with NYSE-listed ADRs (27 out of the 29 companies) pointed out their obligations under NYSE rules to solicit proxies. It would be helpful for companies to align the wording of their DAs with these rules and practices. 7 out of the 20 companies we contacted committed to amending their agreements on this point.
 - For NASDAQ issuers the rules are more ambiguous, and investors need to rely on company disclosure and the wording of the agreements. Vodafone confirmed that it would continue to solicit, and that it will review its agreement. Ryanair, having previously not solicited ADR holder votes, has done so since 2018.
- For the 12 companies which have, at present, committed to *reviewing* (rather than *amending*) their DAs, **encouragement from investors would be helpful.**
- We believe **a best practice standard has been established for voting practices for ADR programmes** (see Table 1). **Six companies were recognised as already having best practice (BT Group, Carnival, CRH, National Grid, Prudential and WPP).**
- Consideration could be given to agreeing an industry-standard wording for DAs, or at least the voting-related provisions. Members have asked us to offer an outline of our approach to ICGN to see if this approach could be helpful for ADR issuers from other markets.

Table 1. Statement of Best Practice

The Investor Forum and investors in its ADR Working Group have established the following principles of Best Practice for the Depositary Agreements for UK-listed companies with listed ADR programmes:

- 1. Registered ADR Holders should receive notice of meetings and solicitation of proxy.**
- 2. If voting instructions are not received from the Registered ADR Holders, the shares should not be voted. The Depositary should not direct votes, and no discretionary proxy should be granted to a person designated by the Company to vote the Deposited Securities represented by ADRs as to which the Depositary has not received instructions from the Holders.**

Table 2 summarises the starting point for UK-listed companies with listed ADR programmes and the responses we received on auto-proxy and solicitation issues. Background to the project is presented in the Appendix, including a table summarising the key provisions governing voting clauses in the individual company ADR agreements, as well as the relative importance of ADRs as a proportion of Ordinary shares.

Table 2. Auto-Proxy and Voting Discretion in Depository Agreements (DAs) of UK-listed Companies with Listed ADRs

Starting Position		New Agreed Position following IF engagement	
AUTO PROXY DISCRETION (1)			
Have, but have never used - 6 companies	BP IHG Lloyds RELX Smith & Nephew Unilever	Will not use (2) - 9 companies	BP Diageo GSK IHG Lloyds RBS RELX Smith & Nephew Unilever
	Diageo GSK RBS Ryanair Shire		Ryanair (3)
	Verona Pharma		Verona Pharma
Have, and have used - 5 companies		May continue to use	
Have; unknown if have used		No response received	
VOTING SOLICITATION DISCRETION		No longer listed	
Have, but have never used - 17 companies	AstraZeneca Barclays BAT BHP Diageo GSK HSBC Lloyds Micro Focus Intl Pearson RBS RELX Rio Tinto RDS Smith & Nephew Unilever Vodafone	Will not use (4) - 18 companies	AstraZeneca Barclays BAT BHP Diageo GSK HSBC Lloyds Micro Focus Intl Pearson RBS RELX Rio Tinto RDS Ryanair (5) Smith & Nephew Unilever Vodafone (5)
	Ryanair		Motif Bio Verona Pharma
	Shire Motif Bio Verona Pharma		Shire
Have, and have used		No response received	
Have; unknown if have used		No longer listed	
BEST PRACTICE			
No Auto-Proxy or Voting Solicitation Discretion - 6 companies	BT Group plc Carnival plc CRH plc National Grid plc Prudential plc WPP plc	No need to amend	BT Group plc Carnival plc CRH plc National Grid plc Prudential plc WPP plc

(1) In addition, AstraZeneca, BAT and BHP allow use of auto-proxy in rare circumstances. AstraZeneca have committed to amend their DA in advance of their 2020 AGM, BHP have committed to amend their DA in advance of their 2019 AGM, while BAT confirmed they would review these provisions at their next review.

(2) The 7 bolded companies have committed to amend their DAs. BP and Diageo have committed to review these provisions at their next review.

(3) Ryanair has agreed to disclose the percentage of votes cast by any Ryanair designated person granted discretionary proxy and how those votes were cast.

(4) The 7 bolded companies have agreed to amend their DAs to clarify this position at the time of their next review; others have agreed to consider the wording at the time of their next review or made a commitment to always solicit for votes.

(5) Nasdaq-listed companies. Nasdaq rules are more ambiguous and investors are more reliant on company disclosures and DA wording to confirm solicitation rights for ADR holders.

Key:

- Highest investor concern
- Wording causing Investor concern
- Best practice; wording may be under review

Results of Working Group: auto-proxy

Issue

The practice of companies potentially voting the unexercised shares of ADR holders was the key focus of this project. The granting of discretionary voting rights to a person designated by the company, unless explicitly authorised by the beneficial owner, is not in accordance with principles of good UK corporate governance. The usual position in the UK is that if votes are not instructed, they are not voted. Investors were concerned about the lack of transparency regarding the use of these rights in reported voting outcomes at AGMs.

With an estimate that only c70% of ADR votes are typically instructed, a material number of votes could potentially be directed by a company's auto-proxy policy. The higher the percent of the ordinary share capital that is held in ADRs, the more significant this could be for voting outcomes. **For 9 FTSE 100 companies, ADRs represent 10-30%** of the share capital – across the 29 companies the range was under 1% to over 68% (see the Appendix for information on each company). **Auto-proxy could therefore potentially have a material impact on voting outcomes for all shareholders.**

Review

We reviewed the DAs of the 29 UK-listed companies with listed ADRs to understand if they granted auto-proxy rights, and found a wide range of practices. **In half (14 instances) there were no auto-proxy rights.** It was therefore clear that it is legally possible, and as such has been viewed by investors as best practice.

12 companies granted auto-proxy rights in their DAs; all but 2 had provisions which are intended to prevent the use of auto-proxy in contentious circumstances where substantial opposition exists. Given the lack of transparency regarding the governance of the process to determine whether such opposition exists, as well as the lack of a requirement to disclose use of these rights, investors remained concerned about the inclusion of these provisions. In the final **3** companies auto-proxy rights are granted, but only under very limited circumstances which are unlikely to materially affect voting outcomes.

Letters

We engaged directly with the Chairs of the 28¹ companies. Letters were tailored based on the text of each company's Depositary Agreement. Copies of correspondence is available to members on our website. In the case of the 14² companies who were deemed to have auto-proxy provisions which fell short of Best Practice we requested:

- a **clear public statement** of their policy with regard to uninstructed ADR votes;
- **not to exercise the discretion** given; and
- to **clearly disclose** the number of uninstructed ADR proxies voted in support of company recommendations when reporting on the outcome of any General Meeting.

We requested that the DA be amended to remove auto-proxy rights, ideally by no later than their 2020 AGM. We noted in each case that we understood that the companies may not, in practice, direct the votes of these shares, or may do so only after consideration of whether substantial opposition exists. We also recognised that the impact may be immaterial in the context of the total votes cast. However, given the lack of transparency about the exercise of these rights, and the principle at stake, investors felt it was important to raise the issue and seek simplification.

¹ We reviewed 29 DAs, but given its pending takeover by Takeda, we did not request a formal response from **Shire plc**.

² Shire's DA gave it discretion around auto-proxy (including in contentious circumstances), but, as per note 1, we did not engage with them on this issue.

Company responses

Of the 14 companies who were asked to take action on auto-proxy issues, 13 responded. (The one that did not respond, Verona Pharma, is AIM-listed and not widely held by members, and so we did not follow up.)

- **4 companies confirmed that they had used the discretion to vote undirected shares. Of these, 3 (Diageo, GSK and RBS) committed not to use auto-proxy rights going forward.** GSK and RBS committed to amend their DAs, and Diageo has said it would consider doing so at the next review. GSK noted that it had only used this right sparingly and when non-contentious, and RBS noted that ADRs represent less than 1% of its share capital. **Ryanair** did not agree to change their practice, but did agree to disclose in subsequent annual reports the percentage of votes cast at future general meetings by any Ryanair designated person granted discretionary proxy and on how those votes were cast. They plan to continue to vote these shares as they deem the numbers to be “immaterial” (representing only 3.4% of shares voted in 2018). In the event of a hard-Brexit, the company will restrict the voting rights of all non-EU shareholders, and so this issue may become temporarily irrelevant.
- **6 companies confirmed that they had not used auto-proxy rights and confirmed explicitly that they had no intention to do so.** 5 made a commitment to amend this provision (**IHG, Lloyds Banking Group, Smith & Nephew, Unilever, RELX**), while **BP** committed to consider amendment at their next review. **Of the 3 companies with very limited auto-proxy clauses: AstraZeneca** confirmed that they had never used this right and committed to remove it by their 2020 AGM. **BAT** and **BHP** confirmed that they had only used this authority in rare cases which were immaterial to results, and will review these rights at their next scheduled review of their DA.

In their responses, companies provided assurance that they strive to have the right processes and procedures in place to ensure that shareholder votes are cast in a fair and proper manner in line with the highest standards of corporate governance. There were comments that companies retained auto-proxy rights to give flexibility, or because they felt it was immaterial to the voting outcome, or that such provisions were a relic of a historical voting practices. Where the DA had provisions to prevent the use of auto-proxy where substantial opposition exists, many felt that this offered sufficient protection that the rights cannot be abused.

Smith & Nephew has provided an early example of a clear public statement in their 2018 Annual Report:

Table 3. Smith & Nephew 2018 Annual Report.

AMERICAN DEPOSITARY SHARES ('ADSS') AND AMERICAN DEPOSITARY RECEIPTS ('ADRS')

In the US, the Company's ordinary shares are traded in the form of ADSs, evidenced by ADRs, on the New York Stock Exchange under the symbol SNN. Each American Depositary Share represents two ordinary shares. Deutsche Bank is the authorised depositary bank for the Company's ADR programme. This relationship is governed under a Depositary Agreement that contains a clause which the Company has been advised by different Depositary Banks was previously considered as standard. This clause supports what we understand to be the normal practice under the US voting system, whereby votes which have not been instructed are then deemed to have given a discretionary proxy ('auto-proxy'). Whilst the wording of our Depositary Agreement does grant auto-proxy rights, the Company can confirm that we do not believe that it is appropriate, within a UK context, to utilise this clause. The Company has therefore always instructed our Depositary Bank to not exercise this right and to only vote those ADRs which have been specifically instructed. The Company will look to remove this clause when updating the Depositary Agreement clause during the course of 2019. It is also the Company's practice to always notify our ADR holders of upcoming Annual General Meetings and General Meetings and the availability of relevant documentation on the Company website as well as providing instructions on how to submit votes, where applicable. This is in accordance with US regulations, which require NYSE ADR listed issuers to solicit ADR votes regardless of the wording in their Depositary Agreement.

We are encouraged that most large UK-listed companies with auto-proxy rights in ADR programmes have committed to remove or consider removing these provisions at their next review.

Results of Working Group: voting solicitation

Issue

The origin of this project was a voting solicitation issue raised by a member. The member had noticed that while they had been solicited to vote their Ordinary shares in a company (**Ryanair**), they had not received notice through their electronic voting platform to vote the ADRs they held in the same company. Further discussion by the investor with the company led to the discovery that the agreement with the Depositary Bank did not require the bank to solicit the votes of the ADR holders, but relied on the ADR holder to pro-actively lodge instructions directly with the Depositary Bank. This raised concerns over possible wide spread issues with ADR solicitation.

Review

In order to investigate the solicitation issue, we conducted three reviews:

- A number of our **members reviewed their electronic ADR and Ordinary share voting records** on Broadridge and ISS, to help determine whether or not there were other instances where they had not been pro-actively solicited.

Result: In all cases where the Ordinaries and ADRs were held, the voting notice was made through the system in a timely manner, with minimal timing differences between the two votes.

- We asked members of the Investor Forum **Legal Panel to review the position regarding the obligation of companies** to solicit votes from ADR holders in all circumstances.

Result: Where companies' ADR programmes are listed on the New York Stock Exchange, companies are obliged to solicit proxies from their ADR holders. Section 402.04 of the NYSE Listed Company Manual states that "actively operating companies are required to solicit proxies for all meetings of shareholders" and Section 402.05 requires proxies solicited through brokers to comply with SEC proxy rules, which in turn require issuers to solicit proxies from beneficial shareholders. Foreign Private Issuers are exempt from the SEC proxy rules and therefore are not required to conduct broker searches. UK ADR issuers have therefore interpreted NYSE rules as requiring them to solicit proxies from ADR holders.

Similarly, NASDAQ Rule 5620(b) requires companies to solicit proxies for all meetings of shareholders. However, NASDAQ Rule 5615(a)(3)(A) states that Foreign Private Issuers are exempt from this requirement if they follow their "home country practice", which means the corporate governance requirements of the company's local applicable law. UK and Irish corporate law does not require companies to solicit ADR holders (as they are not considered "members" of the company) and this may be why the solicitation issue discovered by our member arose with a NASDAQ-listed company.

- The Investor Forum **reviewed the relevant wording in the DAs** of the 29 companies.

Result: In spite of the NYSE requirement, the wording in the DAs is often complex.

- In 5 cases the Depositary is contractually required to solicit votes in all cases once they have received notice of any meeting.
- In 3 cases, either the Depositary or the company is required to do so.
- In 3 cases the Depositary is required to do so by default, but the company has reserved the right to inform them not to.
- In the majority of cases (18), the Depositary only solicits votes "if requested in writing by the Issuer," or similar wording.

While we concluded that lack of solicitation of votes was not a widespread issue, investors believe that there should be no circumstances where the Depositary Bank would not deliver notice of meetings or solicitations of proxies to ADR holders. They do not believe retaining discretion around this issue is appropriate, irrespective of any listing requirements that protect their rights.

Company responses

We wrote to 20³ companies to request that companies should review DA language to reflect an intention to solicit votes in all circumstances, ideally no later than by their 2020 General Meeting.

17 companies responded by confirming that they had always solicited proxies and committed to doing so in the future, and 7 of these committed to review the wording to remove ambiguity. 2 NYSE-listed companies have not responded, but we do not propose following up, as the listing rule requirement appears to provide the necessary shareholder protection.

The two companies with Nasdaq-listed ADRs (**Vodafone** and **Ryanair**) responded.

- Vodafone confirmed that it requires and will continue to require their Depositary Bank to actively solicit votes, where there is not a US legal prohibition, and also committed to reviewing this wording at the next appropriate opportunity. They reaffirmed that, as stated in their Annual Report, ADR holders are entitled to receive notices of shareholders' meeting and are entitled to attend, speak and vote at any general meeting.
- **Ryanair** drew our attention to fact that their ADR programme has been in place for over 20 years. Its terms, which were outlined in Ryanair's initial prospectus of 29 May 1997, have not been amended since and are "fully transparent and publicly available". Their annual report states: "NASDAQ requires that each issuer solicit proxies and provide proxy statements for all meetings of shareholders and provide copies of such proxy solicitation to NASDAQ. The Company is exempt from this requirement as the solicitation of holders of ADSs is not required under the Irish Listing Rules or the Irish Companies Act. Details of Ryanair's annual general meetings and other shareholder meetings, together with the requirements for admission, voting or the appointment of a proxy are available on the website of the Company in accordance with the Irish Companies Act and the Company's Articles of Association. ADS holders may provide instructions to The Bank of New York, as depositary, as to the voting of the underlying Ordinary Shares represented by such ADSs. Alternatively, ADS holders may convert their holding to Ordinary Shares in order to be eligible to attend Ryanair's annual general meetings or other shareholder meetings." As with the auto-proxy issue, in the event of a hard-Brexit, the voting rights of ADR holders will be removed, so this issue may become temporarily irrelevant. Given this, while the company solicited votes ahead of its 2018 AGM as a result of shareholder engagement, it has not made any firm commitments regarding its future intentions.

On a related note, Unilever encouraged all investors to opt for electronic communication to reduce unnecessary printing and physical distribution of documentation, stating that 180,000 copies of the simplification documents were printed for ADR holders alone. This sentiment was echoed by Royal Dutch Shell, who, in mailings which their Depositary works with Broadridge to undertake, encourage both registered and beneficial holders to take the option of electronic communication.

³ Shire's DA gave it discretion around voting solicitation but, as per note 1, we did not engage with them on this issue.

Conclusions

This project is an excellent example of how investors can work collectively to clarify their understanding of an issue, provide a clear investor view of the need for change and then follow up with companies to enhance best practice.

Rather than try to address the issue at a systems level through a generic letter, we wrote to the Chairman of each company, given that it is the responsibility of the Chair to ensure that votes are cast in a fair and proper manner to ascertain the true sense of a General Meeting. The Working Group were clear that companies should act in the interests of investors, and that their expectation was that ADR voting practices should be aligned with the principles of good UK corporate governance. A contractual ability to exercise discretion, whether or not it is used in practice, was felt to be inappropriate, particularly given the lack of transparency of the use of these rights.

Companies responded very positively to our engagement, and we are pleased to be able to report a commitment to significant improvement in practices and the DA terms. We are now liaising with the International Corporate Governance Network to encourage other jurisdictions to conduct such a review and engagement exercise. If possible, we will seek to establish a global agreement on a position of best practice for the two issues of auto-proxy and vote solicitation in DA agreements.

Appendix: Background Information

American Depository Receipts (ADRs) are dollar shares issued in the US by a Depository Bank, representing foreign shares held by the bank outside the US. The terms of the ADRs are defined in an operating contract – the Deposit Agreement (“DA”) - that is filed with the SEC and is available for inspection. For a non-US company, ADRs provide the access to the US clearing system (DTCC), which is necessary for a US listing, US public offering or US public exchange offer. ADRs can be listed or unlisted, sponsored or unsponsored; this project focuses on listed sponsored ADRs.

The number of ADRs in issue in any company can change daily, based on trading activity. Each ADR represents either one, or several, underlying shares listed on the company’s local stock market. An underlying ordinary share and an ADR are fully fungible with one another. For companies domiciled in the UK, issuing ADRs attracts a 1.5% creation fee, making issue activity costly and relatively rare.

For a company, an ADR broadens the potential US investor base outside of global funds, to include US domestic and retail investors, which in theory creates a level playing field for global companies. The benefits of an ADR to an investor are mainly around ease of administration (eg: ease of purchase through the US clearing and custody systems, notifications and filings in English, and dividends paid in dollars).

Market size⁴

Globally, there are over 3,000 programs in 77 countries, with concentrations in Russia, Brazil, Mexico, China and the UK. Over \$1trn is invested in equities held in DR form. The total top 10 issuers account for almost 50% of the invested assets.

Over 3,000 US institutions, and over 1 million retail investors, hold DRs. The top 10 institutional holders of DRs worldwide have invested circa \$200bn through these instruments.

Top 10 DR issuers globally		
	Value held in DR: \$bn	# institutions
Alibaba	176	1,852
Baidu	57	1,215
Shell	49	1,641
Taiwan Semi	39	1,020
BP	37	1,069
BAT	31	1,277
Novartis	27	1,080
JD.com	26	841
Nestle	21	313
Ctrip	19	796
Top 10 total ADR issuance	482	

Top 10 institutional holders of DRs worldwide		
	Value invested in DR \$bn	# stocks
Capital World	26	55
Baillie Gifford	24	55
Fidelity	23	176
Fisher	23	154
BlackRock	22	374
T.Rowe Price	17	97
Dodge & Cox	17	26
Capital Re	16	56
Wellington	16	191
Vanguard	16	179
Top 10 total ADR ownership	200	

⁴ Source: Bloomberg, NYSE, NASDAQ and adr.com as at September 2018



The total current investment in European ADRs of approximately \$445bn, across more than 800 companies, appears to suggest widespread investment by US investors. In reality ADR investment is fairly concentrated:

- 82% of all reported investment is held in just 82 issuers with ADRs listed on the NYSE or NASDAQ.
- A further 14% is held in the 258 sponsored OTC ADRs, many of which delisted from the NYSE or NASDAQ in 2007 when the SEC amended its deregistration rules.

In total 259 UK companies have ADRs:

- 121 are sponsored by the company
- 138 are unsponsored

29 of the sponsored ADRs are listed on US exchanges (24 on the NYSE, and 5 on NASDAQ), with the remaining traded OTC. This project focused on those 29 US-listed sponsored ADR programs for UK issuers.

Vote solicitation

Although ADR holders have the right to vote, they do not automatically have the right to be informed of the vote. Voting turnout of ADRs is typically consistent with that of ordinary shares in the US, at around 70%.

In the universe of 29 listed ADRs that we examined:

- **the Depositary Agreement contractually requires the Depositary to solicit votes in only 17% of cases (5 companies).** Typical wording is as follows:

*“As soon as practicable after receipt of notice of any meeting of holders of Shares or other Deposited Securities, the **Depositary will** mail to the Holders a notice that will contain (a) such information as is contained in such notice of meeting and (b) a statement that the Holders ...will be entitled ... to instruct the Depositary as to the exercise of voting rights,.... and (c) a brief statement as to the manner in which such instructions may be given”*

- **In 20% of cases**, the default is that the Depositary will do the above unless actively requested not to, or that one of either the Depositary or the Company will complete the actions (3 companies in each class).
- **In 62% of cases**, the Depositary will only do the above **“if requested by the Company in writing in a timely manner”**.

We understand from companies that the cost of physically mailing out the information can amount to around \$1.5m, which is clearly substantial. Set against this cost, we have heard of a number of situations where companies receive income from Depositary banks derived from the fees associated with the creation of new ADRs. We have not attempted to calculate the net cost to the company of running an ADR programme.

Auto-proxy

The practice of the company voting unexercised proxies was a core focus of this project. Given that only 70% of ADR votes are typically instructed, a material number of votes could potentially be directed by a company's auto-proxy policy. The higher the % of the ordinary share capital that is held in ADRs (shown in the table in the Appendix), the more significant it will be.

In reviewing the 29 DAs we discovered a wide range of practice:



- **59% of cases had either no (14 companies) or very narrowly defined (3 companies) auto-proxy rights.** Typical wording is as follows:

*“Shares or other Deposited Securities represented by ADSs for which no specific voting instructions are received by the Depositary from the Holder **shall not be voted** by the Depositary or its nominee.”*

- **In 41% of cases (12 companies), if no instruction is received, the Depositary will give a discretionary proxy to a person nominated by the Company to vote the shares.** Example wording is as follows:

*“If no instructions are received by the Depositary from any Owner with respect to any of the Shares and Deposited Securities ... the Depositary shall deem such Owner to have instructed the Depositary to **give a discretionary proxy to a person designated by the Company** with respect to such Shares and Deposited Securities and the Depositary shall give a discretionary proxy to a person designated by the Company to vote such Deposited Securities”*

We discovered a wide range of practice from our discussions with companies and Depositaries. We discussed with a Company Secretary of a company who has such a provision whether the discretion is used. The company had taken legal advice, and had been advised that ADR holders assume that the default position of giving no voting instruction would be that the shares would be voted in favour of management recommendations, and that therefore the company had a duty to do so.

Some clauses include a caveat to the above discretion, for example with the wording *“unless otherwise specified in the notice distributed to Owners”*. This gives the Company the ability to make it clear that, even though they have the discretion, they would not use it.

We understand from a Depositary Bank that many companies do not as a matter of course exercise the discretion that they have, without first specifying in the notice whether or not they will do so.

In many cases, exceptions are put around the giving of this proxy:

“... provided, however, that no such discretionary proxy shall be given by the Depositary, and the Depositary shall not itself vote, with respect to any matter to be voted upon as to which the Company informs the Depositary that (A) the Company does not wish such proxy to be given, (B) substantial opposition exists, or (C) such matter prejudices any substantial existing rights of holders of Shares or Other Deposited Securities.”

We discussed with a Company Secretary of a company which has such a provision how the company decides whether “substantial opposition” to a resolution exists. She said that it was her role to monitor media coverage, feedback from shareholders, and the recommendations of the proxy agencies, and to recommend to the Board in exceptional cases that the discretion is not exercised. Investors were concerned about the lack of transparency of the exercise of this decision-making or of the votes cast in this manner. Moreover, in two of the existing Depositary Agreements, no exceptions are specified, meaning the Company could theoretically exercise the discretion, however controversial the proposal, without disclosure.

S-360 REPORT

Investigating ADR Proxy Voting Issues



THE INVESTOR FORUM



THE INVESTOR FORUM

Voting of Deposited Securities Clauses in Depositary Agreements of Dual-Listed ADRs of UK Issuers ⁽¹⁾

Company	Depositary Bank	Year of Depositary Agreement	ADR as % of Ordinaries ⁽²⁾	Proxy				Solicitation				
				Auto-Proxy	Auto-proxy even if substantial opposition exists	Auto-proxy in narrow circumstances	No Auto-Proxy (Best Practice)	Depositary shall mail (Best Practice)	Depositary or company shall mail (Best Practice)	Shall unless otherwise requested by company	At written request of company	
AstraZeneca	Citi	2015	18.4%			1						1
Barclays	JPM	2018	4.6%				1					1
British American Tobacco	Citi	2018	11.3%			1						1
BHP	Citi	2007	2.6%			1						1
BP	JPM	2017	27.5%	1					1			
BT Group	JPM	2015	1.6%				1		1			
Carnival	JPM	2003	1.3%				1		1			
CRH	BNY	2006	4.5%				1		1			
Diageo	Citi	2013	17.4%	1								1
GlaxoSmithKline	BNY	2015	19.0%	1						1		
HSBC	BNY	2001	4.1%				1					1
Intercontinental Hotels Group	JPM	2015	7.1%	1					1			
Lloyds Banking Group	BNY	2008	3.6%	1								1
Micro Focus Intl	Deutsche	2017	33.0%				1					1
Motif Bio	BNY	2017	8.8%				1					1
National Grid	BNY	2013	11.2%				1		1			
Pearson	BNY	2014	3.1%				1					1
Prudential	JPM	2008	2.3%				1		1			
RELX	Citi	2015	2.6%	1								1
Rio Tinto	JPM	2016	6.8%				1			1		
Royal Bank of Scotland Group	BNY	2007	0.9%	1								1
Royal Dutch Shell	JPM	2018	18.8%				1					1
Ryanair Holdings ⁽³⁾	BNY	2007	43.7%	1								1
Shire	Citi	2016	22.4%	1	1					1		
Smith & Nephew	Deutsche	2014	8.9%	1	1							1
Unilever	Deutsche	2014	4.6%	1								1
Verona Pharma	Citi	2017	68.1%	1								1
Vodafone	Deutsche	2017	17.9%				1					1
WPP	Citi	2013	6.3%				1			1		
Total	29			12		3	14	5	3	3	18	
				41%		10%	48%	17%	10%	10%	62%	

(1) Source: Company SEC 13-F Filings.

(2) Source: Bloomberg, 18 September 2018. Note % varies on a daily basis, based on trading activity.

(3) Data from June 2018 Annual Report.



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