THE INVESTOR FORUM

BRIDGING THE GAPS BETWEEN COMPANIES & INVESTORS

Shaping Tomorrow's Dialogues

Investor Forum

We are a non-profit community interest company set up by institutional investors in UK equities. With support from more than 50 institutions, we prioritise long-term sustainable value creation as the ultimate purpose of stewardship and the one goal that can unite the investment chain.

Sitting in the heart of UK equity markets, we leverage our expertise and networks to tackle challenges, convene dialogues, and deliver solution-focused engagement outcomes through our collective engagement framework. We seek to bridge gaps that arise between companies and investors to align interests, build trust and focus on creating and maintaining long-term value for all stakeholders.

In rapidly evolving markets, we facilitate dialogue by identifying investor concerns and presenting those perspectives to boards in a comprehensive and consistent manner. We seek to ensure better informed boards and to enhance trust and understanding between issuers and investors.

Acknowledgements:

We would like to thank all the participants from UK listed companies and investor organisations for their valuable contributions. We also extend our thanks to our Advisory Panel, composed of experts from our membership, and to our strategic partners from The Investor Relations Society (IRS), Accounting for Sustainability (A4S), The Audit Committee Chairs Independent Forum (ACCIF) and the representatives from the GC100 executive committee. We appreciate the time and commitment invested by each individual and organisation in advancing our shared objectives.

Promoting Best Practice Dialogue

INTRODUCING THE INITIATIVE

This paper presents the findings from our programme to identify and promote Best Practice Dialogue between corporates and investors. Our goal was to create a comprehensive assessment of the state of key dialogues between UK companies and investors.

In conjunction with strategic partners, we organised individual conversations and hosted workshops over a six month period with experts from 28 UK listed companies and 25 investors. We assessed the health of the relationship and identified a series of practical steps which might enrich key elements of the dialogue between companies and investors.

The foundations of the relationships between companies and investors are robust and can serve as a platform for enhancing the quality of dialogue between Boards and investors. This is of vital importance if we are to address the many challenges ahead and revitalise UK equity markets.

We believe that by addressing the concerns and opportunities which emerged during this project, companies and investors can reduce friction and strengthen relationships enabling them to focus their efforts on the issue of long-term value creation.

We view this report as just the beginning, not the end, capturing a specific point in time. Given the rapid pace of change, we envision it as laying the foundation to build and enhance relationships.

The project has been led by Sallie Pilot working with partners from The Investor Relations Society (IRS), Accounting for Sustainability (A4S), The Audit Committee Chairs Independent Forum (ACCIF), leading Company Secretaries and the Investor Forum's Senior Advisers. We are enormously thankful that so many experts have engaged in this vital debate.

We are encouraged to find so many passionate and dedicated professionals in both companies and investors who are committed to the success of the UK's publicly listed companies. We hope that you will take away practical insights to inform your individual interactions, whether as investors, companies or broader stakeholders.

Finally, we hope that you will be inspired to contribute to rejuvenating the dialogue with UK companies for the benefit of all. If you are, then please do join one of our ongoing programmes, or reach out to us to discuss new opportunities.

The Investor Forum
March 2024

Contents

Taking a Focused Approach

PRIORITISING INVESTMENT MANAGER AND COMPANY EXCHANGES

The investment chain is complex, linking together asset owners, with asset managers, companies (in the case of equities) and stakeholders in the broader market ecosystem.

This project focuses on the critical exchange between investment managers and companies, and specifically on a number of key dialogues that characterise the relationship:

- Investor Relations
- Sustainability
- Audit & Assurance
- Voting & Governance

Throughout the project, we uncovered several surprising misperceptions. Consequently, the report aims to debunk these 'myths' and, by sharing a series of insights from participants on what works well, we seek to establish a basis for enriched dialogue and focused engagement.

Each of these dialogues is very different in terms of both maturity – ranging from well-established in the case of Investor Relations and Voting & Governance to nascent in the case of Sustainability and Audit & Assurance – and intensity, with Audit & Assurance being the least active dialogue by far.

Irrespective of maturity or intensity, in each dialogue we observed a commitment to honesty and openness and a rich appetite from participants to better understand the differing perspectives and to find efficient and effective ways to enhance communication.

A number of key observations emerged from our discussions, which we believe are critical to ensuring an effective understanding between companies and investors. If both parties grasp the opportunities presented, they can ensure that strong foundations are in place for a resilient partnership. Such alignment, will support more informed decision-making to the benefit of both companies and investors.

The findings are not static, but a starting point and a foundation to build on. The market dynamics are rapidly evolving, requiring continuous re-evaluation and adaptation of relationships and dialogues to ensure their effectiveness and efficiency in the future.

Recognising Some Uncomfortable Truths

CHANGING MARKET DYNAMICS

Companies and Investors Are Becoming Overwhelmed

The roles and responsibilities of companies and investors in society are undergoing a significant shift as governments increasingly require them to address complex societal and environmental issues. The result is an overwhelming proliferation of initiatives, requirements and challenges, relating to an expanding array of issues with a growing number of influencers exerting pressure. The changing nature of ownership in the UK market is a further complicating factor.

The current system was not designed to cope with such multifaceted demands. It is critically important that companies and investors work together to navigate this complexity.

Navigating a Tipping Point

We identified three major challenges which are stretching, and in some cases challenging, relationships between companies and investors:

Reporting is crowding out critical dialogue:

- The focus on reporting is distracting market participants, both companies and investors. Action is needed to create decision-useful information to inform dialogue rather than a compliance-driven approach to increasing disclosure. Dialogue builds relationships that data alone cannot – information is necessary but not sufficient to build trust.
- The quality of interaction is key not the quantity of activity.

Systems are being created that only the biggest can afford:

- Increasing demand for comprehensive information exchange and reporting requirements – whether voluntary or regulatory in nature - are an enormous challenge for everyone.
- We must recognise that only the largest companies and asset managers will have the resources to meet the disclosure challenges ahead.

Voting Against is not a sign of effective stewardship:

- Voting practice is changing. The landscape is evolving dramatically in terms of both shareholder composition, scrutiny, and priorities.
- Addressing misconceptions and conflicts – from the role of proxy agents to ESG impact – is an urgent priority.

Language Matters in Company and Investor Dialogue

Across all these dialogues, a standout observation is that language matters when we talk about ESG and sustainability. Furthermore, we have identified several best practices reflecting what investors and companies perceive to work effectively and constitutes what excellent dialogue and interaction looks like.

In addition to the overarching insights derived from our exploration of the individual dialogues, specific findings have emerged within each dialogue. These findings, we believe, if addressed, hold the potential to enhance and enrich the ongoing dialogue significantly.

Highlighting Key Insights

COMPANY-INVESTOR DIALOGUES

1. Clearing the Path for Strategic Conversations

Companies and Investors have strong relationships, but these relationships need to evolve to address the increasing complexity. As the dynamics evolve there is a need to bolster and expand the core relationships across both companies and investment institutions to pave the way for positive, multi-faceted conversations that focus on value creation. *For more: Unifying Element is Value Creation (Page 7)*

2. Co-Creating an Effective Model for Stewardship

To navigate the evolving investment landscape and address, the at times, overwhelming plethora of initiatives, it is imperative that Asset Owners, Asset Managers, Companies and Regulators collaborate beyond their respective stakeholder group. By co-creating a model of stewardship and engagement, stakeholders can contribute to a more vibrant UK market. *For more: Navigating Change in an Evolving Landscape (Page 9)*

3. Establishing a Common Understanding

The cornerstone of resilient partnerships between investors and companies is effective dialogue that establishes a common understanding. Listening attentively is paramount to achieving this understanding – it enables us to transcend individual interests and lay the groundwork for valuable interactions. *For more: Listening serves as the Cornerstone of Relationships (Page 10)*

4. Busting Myths About the Investor-Company Relationship

There are a surprising number of unresolved misperceptions and misunderstandings that need debunking – from the role of proxy agents and voting decision-making to the debate on remuneration and the impact of ESG. These misunderstandings are eroding confidence and undermining relationships. *For more: Paving the Way for Meaningful Dialogue (Page 13)*

5. Focusing on Meaningful and Relevant Dialogue

The evolving dynamics of relationships and interactions across various stakeholder groups reveal a spectrum of maturity and intensity. Some are well-established and intense, while others are nascent and less frequent. It is critical to prioritise meaningful and relevant dialogues which drive progress and understanding, irrespective of their maturity level or frequency. *For more: Examining the Maturity and Intensity of Each Dialogue (Page 18)*

Seeking a New Equilibrium

PRACTICAL ACTIONS FOR MARKET PRACTITIONERS

The Investor Forum is committed to driving forward actions from this initiative in the coming months. This report marks the beginning of a journey – a journey aimed at building stronger relationships between companies and investors that endure and evolve over time.

Our intent extends far beyond these pages. We aspire to cultivate an environment where collaboration thrives and where the exchange of ideas and initiatives can create practical outcomes.

We believe that bringing together market practitioners – companies and investors is of paramount importance. It is through the collaboration and the concerted efforts of all parties that we can most effectively address the multifaceted challenges that we face.

We will share the insights in this paper with participants and influencers across the ecosystem and develop partnerships and seek to create practical actions to address the issues identified.

By coming together, we not only seek to overcome obstacles but also to lay the groundwork for restoring trust within our markets. The alignment of interests, transparency, and accountability addressed in these collaborations can contribute to rebuilding and sustaining trust – a cornerstone of a robust and resilient market.

The path ahead may be challenging, but the potential benefits – both tangible and intangible – can help to revitalise the UK's equity market. Together, we can contribute to rejuvenating the dialogue with UK companies for the benefit of all, navigating a path to generate sustainable long-term value.

Investor Forum Priorities

- **Creating an Investor and Issuer Forum:** We will create an Investor and Issuer Forum, to address the key points of friction that inhibit a more effective marketplace and to foster collaborative dialogue between companies and the investment community.
- **Facilitating Collaborative Engagement:** We will continue to promote clearer communication and efficient information exchange between companies and investors.
- **Addressing Material Issues:** Proactively tackling broader material issues impacting both companies and investors, the Forum will seek to convene investors to collectively address challenges like voting, sustainability reporting, working practices, and climate change.
- **Enhancing Education Initiatives:** We will continue to enhance investor understanding regarding best practices, and provide the opportunity for education on emerging issues in collaboration with strategic partners and other stakeholders.
- **Advancing strategic dialogue:** We will work with Members, our strategic partners, and other interested parties to identify a series of practical actions to enhance each of the specific dialogues, strengthen the relationships between companies and investors, and to encourage a focus on sustainable value creation.

Clearing the Path for Strategic Conversation

PRIORITISING THROUGH A COMMON FOCUS ON VALUE CREATION

Our belief is that dialogue is critical to building trust. Trust forms the bedrock of any successful investor-company relationship, underpinning the confidence that investors place in a company's ability to deliver sustained value. From the investor's perspective, trust is multifaceted, built up from a range of conversations, disclosures and questions that must be answered to establish a solid foundation of understanding and awareness.

To build a bridge between investors and companies, we concentrated on four pivotal stakeholder dialogues, assessed the overall health of those relationships, the quality of engagement, and the effectiveness of information exchange.

We believe that by addressing the identified concerns and achieving clarity, companies and investors can reduce friction, enabling boards and CEOs to focus both their efforts and their interactions with shareholders on the issue of long-term value creation.

	Exchanging Information	Understanding Impact	Ensuring Accountability	Building Confidence in Assurance
	Investor Relations Dialogue	**Sustainability Dialogue**	**Voting & Governance Dialogue**	**Audit & Assurance Dialogue**
Companies	Investor Relations Professionals	Sustainability Professionals or those with responsibility	Company Secretariat	Audit Committee Chairs
Investors	Analysts Stewardship Teams	ESG Teams	Governance Specialists	Portfolio Managers Governance Specialists
	Go To Dialogue >	Go To Dialogue >	Go To Dialogue >	Go To Dialogue >

Clearing the Path for Strategic Conversation

PRIORITISING THROUGH A COMMON FOCUS ON VALUE CREATION

	Exchanging Information	Understanding Impact	Ensuring Accountability	Building Confidence in Assurance
	Investor Relations Dialogue	**Sustainability Dialogue**	**Voting & Governance Dialogue**	**Audit & Assurance Dialogue**
Question We Set Out To Address	How can we create a seamless information ecosystem that caters to the needs of both investors and corporates, promoting transparency, trust and informed decision making?	How can we better measure, communicate and align the impact of investments with corporates' strategy efforts, benefitting both investors and corporates in pursuing sustainable goals?	How can we refine the framework to ensure timely, accurate and transparent corporate information, fostering investor and corporate confidence?	How can we establish a robust framework that instils confidence in the reliability and accuracy of corporate information, benefiting both investors and companies alike?
What We Discovered	**Expertise** is vital in this dialogue. There needs to be a high level of skill in identifying and communicating key strategic elements to build investor trust and encourage long term commitment combined with a detailed knowledge of a heterogeneous investor universe, and effective strategies to engage with and build long-term relationships with a wide range of investors.	**Complexity** is a key theme of this dialogue. Rapidly changing regulations, diverse stakeholder expectations, and emerging technical issues combine to create a complex environment in which to analyse and communicate the impact of corporate sustainability efforts and ensure alignment with stakeholder expectations. There are a wide variety of views, which means a nuanced approach is needed to enhance mutual understanding and support improved decision-making, in order to enable both investors and corporates to deliver sustainable outcomes.	**Consistency** emerges as a crucial theme in this dialogue. Both investors and companies seek to establish consistency in the voting process, emphasising the need for more uniformity in interpretation, execution and feedback. The dialogue also considered the sources of friction and a range of frustrations with the current system.	**Integrity** emerged as the linchpin of this dialogue, underscoring its fundamental role in the audit and assurance processes. The discussion centred on how to ensure confidence in the reliability of corporate information through a better understanding of assurance and transparent high-quality dialogues to develop enduring trust for the benefit of investors and corporates.

Navigating Change in an Evolving Landscape

CO-CREATING A MORE EFFECTIVE MODEL FOR STEWARDSHIP

In the evolving investment landscape, one thing is clear: the environment has become much more complex. Companies, asset managers and asset owners all face enormous pressures as they strive to reshape business models to deliver sustainable returns.

Amidst this complexity, the UK equity market has many positive characteristics, including:

- Some of the best access to companies and most transparent information flows of any market;
- A series of investor protections that have proved their worth over decades.

That said, recent years have seen an overemphasis on evidencing how investors hold companies accountable and on codification over action. While much of this agenda has been shaped in response to corporate failures, risk has not been eliminated. Instead, relations between investors and companies have been strained, to the detriment of UK listed markets.

Markets work best when there is a clear alignment of interests between savers, asset owners, asset managers and companies. In the UK, this chain has been fragmenting for 20 years.

Dedicated resources devoted to UK equities have reduced significantly, reflecting the decline in importance of the asset class. Experienced portfolio managers, who have the respect of boardrooms, have stepped down from managing money, and UK teams are being integrated into broader European and Global equity teams.

In the midst of the plethora of initiatives introduced over recent years, there lies opportunity for streamlining and synergy. **Asset Owners, Asset Managers, Companies and Regulators all possess the potential to step outside of their own stakeholder group to co-create a more effective model of stewardship and engagement.**

With the growing tensions between Asset Owners and Asset Managers and between Companies and Asset Managers, it is vital that all participants are motivated to re-align the investment chain around the common goal of creating long-term sustainable value. What's critical now is a clear recognition and mutual understanding of the roles, responsibilities and priorities of all agents in the chain.

The efforts to reform the market, to ensure that it is 'match fit', are beginning to take shape, and the proposed package of reforms is wide ranging. Now is the time to move forward with conviction to establish the conditions that will underpin a vibrant listed equity market.

Developments in the Landscape:

- Decline of UK equities as an asset class.
- Remuneration is a point of contention.
- Broadening of the stewardship agenda.
- Focus on codification over action. This has impacted market relationships the most – for companies and investors alike. The complex raft of overlapping rules and requirements requires urgent simplification.
- Changing political and economic environment. Government policy has shifted significantly to focus on the competitiveness of UK markets.

Establishing a Common Understanding

LISTENING IS THE CORNERSTONE OF RELATIONSHIPS

From our discussions, there are several critical observations that we believe serve as the cornerstone for effective dialogue and the establishment of a resilient partnership between investors and companies. To address the rapidly changing landscape, we believe that it is critical to recognise and internalise these observations as they transcend individual interests, and lay the groundwork for interactions geared towards achieving the overarching objective of long-term value creation. Embracing these observations is paramount for nurturing strong relationships, enabling informed decision-making, and unlocking opportunities to enrich the investor-company dialogue within the intricate ecosystem in which it operates.

Characteristics of the Relationship

1. The investor-company relationship is built on robust foundations

Despite the noise and occasional friction in the market, investors and companies share fundamentally strong relationships built on a foundation of robust connections and a common imperative – value creation. This shared goal is the unifying force across the investment chain.

2. No two investors or companies are the same

Every company and investor is different, shaped by their purpose, values, and approach. Companies vary in their cultures, strategies, and products or services offered, reflecting the diverse landscape of industries and geographies they operate in. Likewise, investors encompass a wide spectrum of individuals and entities, from asset owners to asset managers, with diverse objectives, approaches, risk appetites, time horizons and investment philosophies. It is crucial for both companies and investors to tailor interactions to enable efficient communication.

3. Strong relationships underpin quality dialogue

Dialogue surpasses mere disclosure requests and the exchange of factual information, offering insights that disclosure alone cannot provide. Relationships are pivotal in all dialogues. Investors value timely conversations and having pre-existing relationships which help to facilitate quick access when needed. On the corporate side, identifying the right contact within the investor institution to talk about the right issue is crucial.

4. Language matters when talking about ESG and sustainability

There is confusion and inconsistency in discussions about ESG and sustainability due to the frequent interchangeability of terms and/or the use of disparate definitions. ESG, being multifaceted and inherently subjective, leads to a spectrum of interpretations. Although recognised universally as an assessment framework the emphasis and scope of ESG considerations vary widely among individuals, organisations, and industries. Consequently, everyone's understanding of ESG is slightly different. This highlights the importance of clearly defining language to ensure meaningful dialogue and actions.

Changes Impacting the Landscape

5. Clearer reporting is part of the journey, not the final destination

Companies are inundated with reporting requirements. Prioritising what truly matters for a company's business is essential – the solution is not in the quantity but in the materiality of information. Likewise, investors are grappling with escalating reporting demands, feeling the effect from asset owners, regulatory pressures, and fund labelling requirements. A collaborative approach to enable an informed exchange of information can deliver significant benefits.

Establishing a Common Understanding

LISTENING IS THE CORNERSTONE OF RELATIONSHIPS

6. Meeting stakeholder needs presents inherent challenges

Companies have to navigate multiple stakeholders needs, including investors, employees, customers, and communities. The reality is that stakeholders often have diverse and sometimes conflicting interests and priorities; it is challenging to meet all expectations simultaneously. Effective stakeholder management involves prioritising concerns, making trade-offs, and transparently communicating decisions and their rationale. Strong relationships with investors are therefore critical to ensure a transparent and timely exchange of information.

7. Technology and sustainability evolve at an accelerated pace

There is a dramatically accelerating pace in the development and adoption of technological change – from big data to machine learning and artificial intelligence. While many believe that investors 'know all', in reality they can struggle to keep up. Investors have a wide variety of resources; not all have the bandwidth for in-depth detailed analysis. Companies shouldn't assume that investors have innate knowledge, and should remind them of business, strategy, and key issues at each interaction. As emerging issues, like biodiversity and nature, gain prominence, a mutual benefit arises from sharing knowledge and expertise.

Actions That Can Make a Difference

8. Incremental changes can wield substantial impact

Numerous small refinements can in aggregate combine to create significant improvements. If open to continuous improvement, investors and corporates can implement small changes that deliver easy wins on both sides, reducing friction, improving understanding, and breaking down barriers.

9. Best practice is rapidly adopted in a competitive market

Striving for best practice helps companies to enhance efficiency, quality, risk management and innovation, and build a competitive edge. Each investment organisation will have a unique culture and individual processes. Nevertheless, best practice initiatives can spread quickly through the marketplace and offer the potential to ensure efficient, effective, and high-quality relationships.

10. Understanding the purpose of the dialogue

To ensure effective dialogue, it is important to consider the reasons why investors talk to companies. When an investment decision is being made, active investors undertake extensive due diligence before investing / or divesting from a company. Once invested, dialogue can have many different objectives, can involve different people from the company and the investment organisation and can take several forms.

Reasons Why Investors Engage

Information Gathering:

- Investors seek facts and information to inform their assessment of the company and / or the broader industry or wider market.

Strategic Dialogue:

- Investors seek to understand how effectively company is executing against its stated strategy and investor expectations.
- These dialogues can include specific asks for the company to consider to align expectations, enhance performance or realise value.

Challenging Discussions:

- Investors raise concerns to assess whether a company is managing risks and addressing challenges effectively.
- If these discussions are not satisfactory, investors can escalate and active investors can decide to sell shares.

Thematic Engagement:

- Investors undertake targeted discussions and assessments related to their specific thematic priorities.
- The discussions may consider emerging systemic risks and opportunities, which the company may view as externalities.

Establishing a Common Understanding

BUSTING MYTHS ABOUT THE INVESTOR-COMPANY RELATIONSHIP

Paving the Way for Meaningful Dialogue

In addition to the critical observations guiding investor-company relationships and dialogue, we identified several myths that required debunking – unexpected misperceptions revealed during the individual dialogues on Investor Relations, Sustainability, Voting & Governance and Audit & Assurance. These myths are highlighted to set the stage for each dialogue. Through deliberate and thoughtful discussions between investors and corporates, we formulated a series of practical recommendations, paving the way for more meaningful dialogue and focused engagement in the future.

Investor Relations Myths

ESTABLISHING A COMMON UNDERSTANDING

Myth: All Engagement Is Good Engagement

Reality: No, strategic engagement is good engagement. Understanding the purpose behind engagement is vital – whether aimed at information gathering or transformative change. Clear objectives, well-defined agendas, and robust feedback mechanisms are essential components for impactful dialogue. Recognising that not all engagement is equal underscores the necessity for intentionality and strategic alignment in every interaction between investors and companies.

Myth: Consistently Applying the Same Approach Guarantees Success

Reality: This is misleading. Dynamic markets, different investment approaches, evolving investor expectations, and increasing stakeholder demands necessitate a shift toward redefined relationships. Rather than adhering to conventional practices, success hinges on establishing agreed-upon expectations before delving into specifics.

Myth: All Companies and Investors Are the Same

Reality: No two companies or two investors are the same. Companies vary in size, structure, industry, geography, strategy, governance and financial health, while investors have diverse objectives, approaches, risk tolerances, time horizons and investment preferences. Recognising and understanding these differences is crucial for effective communication and collaboration, ensuring tailored approaches that acknowledge the unique characteristics of each company and investor.

Sustainability Myths

ESTABLISHING A COMMON UNDERSTANDING

Myth: ESG Considerations Are Only Relevant for Certain Industries and Sectors

Reality: Environmental, social and governance factors are integral to all businesses but manifest in different ways and at differing levels of materiality. With the UK's commitment to a net-zero target, companies and investors alike must evidence their plans, activities, and actions towards sustainability. There are broader shifts in societal expectations and increased regulatory efforts that need to be addressed.

Myth: ESG Is Exclusively a Risk Management Tool for Investors

Reality: ESG entails more than just risk mitigation. It spans both risks and opportunities. While effectively managing environmental, social, and governance risks is pivotal, embracing ESG also unveils opportunities for innovation, market differentiation, and sustainable growth. Recognising the dual nature of ESG, as a risk management tool and a source of opportunities, positions investors to make well-informed decisions that align with holistic success, resilience, and long-term value creation and it is incumbent on companies to communicate in this light.

Myth: More Data Is the Answer

Reality: While sustainability data is undeniably crucial for gaining insights into a company's practices and track record, it is essential to understand that collecting data alone is not the solution to drive change. The true impact of sustainability efforts will be in capital allocation decisions that drive strategic investments and decisive actions. Investors play a pivotal role in providing the support needed to drive tangible and sustainable outcomes. Both companies and investors need to move beyond a sole emphasis on data reporting and collection and prioritise a longer-term perspective, recognising that strategic investments are crucial for achieving meaningful transition.

Governance & Voting Myths

ESTABLISHING A COMMON UNDERSTANDING

Myth: Investors Blindly Follow Proxy Advisors' Advice

Reality: This is a misconception, the reality is much more complex. While proxy advisors wield substantial influence, particularly for asset managers with limited resources, it's important to note that not all investors unquestioningly follow their advice. Almost all asset managers have bespoke, publicly available, voting policies which provide guidelines for proxy agencies to follow when executing voting instructions. Asset Managers review voting outcomes and investigate any discrepancies from stated policies. Proxy advisors serve a valuable role in providing information, especially for investors facing time constraints and resource limitations. There are questions about the quality, accuracy and timeliness of proxy research and recommendations. However many asset managers, the reality involves a discerning approach that integrates insights from proxy advisors with considerations of the needs, preferences, goals, and strategies of the asset owners they represent.

Myth: Voting Against Is a Sign of Good Stewardship

Reality: No, this oversimplifies stewardship. Voting, being a binary measure, is just one facet. True stewardship goes beyond, emphasising active engagement, thoughtful dialogue, and collaboration focused on preserving and enhancing the value of entrusted assets. The intense focus on 'holding to account' often crowds out constructive dialogue that aligns interests. Effective stewardship involves a multifaceted approach that considers the broader spectrum of actions aimed at ensuring the sustainable growth and success of the invested assets.

Governance & Voting Myths

ESTABLISHING A COMMON UNDERSTANDING

Myth: UK Investors Reject High Executive Pay

Reality: UK investors are not averse to recognising and rewarding excellence. Their apprehension, centres around compensating mediocrity. While acknowledging this, there is growing sentiment that the current approach to executive pay is overly complex. Investors wholeheartedly support executive pay structures linked to long-term performance and strategic alignment. The nuanced perspective of UK investors underscores the importance of linking remuneration to genuine merit and sustained value creation.

Myth: Extensive Engagement Around Remuneration Is Imperative

Reality: Over-engagement can yield a poor return on investment, fostering a perpetual cycle of tinkering that diminishes the effectiveness of each engagement. Investors frequently struggle to convey clear messages, and companies may find it challenging to extract actionable insights. This underscores the importance of steering away from excessive consultation and, instead, prioritising targeted and impactful interactions. Quality over quantity is key in remuneration discussions, ensuring that engagements are purposeful, focused, and capable of delivering clear, meaningful outcomes for both investors and companies.

Audit & Assurance Myths

ESTABLISHING A COMMON UNDERSTANDING

Myth: Investors Are Indifferent to the Audit and Assurance Processes

Reality: Investors operate under the assumption and trust that audit and assurance processes are conducted with precision and in compliance with rigorous standards. While they may not require a regular dialogue on audit matters, they are interested in maintaining an open line of communication, and are prepared to engage when necessary.

Myth: Audit Committee Chairs Are Reluctant To Engage With Investors

Reality: No, many Audit Committee Chairs recognise the importance of investor engagement. While investors may not feel the need for regular engagement, ensuring they have access when necessary is crucial. To further strengthen this connection, companies should proactively communicate the availability of Audit Committee Chairs for discussions. Additionally, there's an opportunity for companies to play a more active role in educating investors about key matters. Audit Committee Chairs take their responsibilities seriously, understanding that dialogue and transparency are pivotal for building trust.

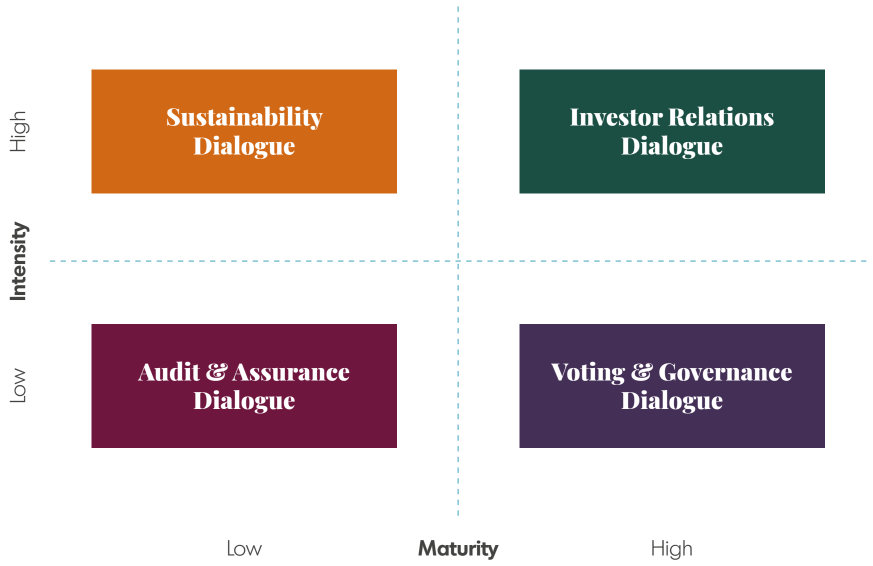
Focusing on Meaningful, Necessary, & Relevant Dialogue

EXAMINING THE MATURITY AND INTENSITY OF EACH DIALOGUE

This section provides a summary overview of the current landscape surrounding the four key dialogues critical to the relationship between companies and investors: Investor Relations, Governance and Voting, Audit and Assurance, and Sustainability. Through a clear examination, we delve into the state of play regarding each of the relationship's overall dynamics, assessing its maturity level and the intensity of engagement. By exploring these areas, we aim to highlight the evolving nature of interactions between companies and investors. It's also important to recognise that these relationships are not static; they are dynamic and require continuous adaptation and reassessment to effectively respond to market demands.

More detail is provided in each of the individual chapter reviews as well as insights into the intricacies shaping their collaborative endeavours and strategic decision-making processes.

Dialogue Characteristics



Focusing on Meaningful, Necessary, & Relevant Dialogue

EXAMINING THE MATURITY AND INTENSITY OF EACH DIALOGUE

	Investor Relations Dialogue	Sustainability Dialogue	Voting & Governance Dialogue	Audit & Assurance Dialogue
Overall Relationship	Well-established and well-formed process, marked by strong relationship development between corporates and investors.	Dialogue is rapidly evolving due to increasing significance. Driven by shifting regulations, diverse stakeholder expectations and emerging technical issues dialogue is being reshaped as sustainability gains recognition as a core driver of value creation.	Conversations have traditionally been clear and focused. However, the landscape is shifting due to emerging climate and ESG concerns, heightened pressure on asset managers from owners, the rise of pass-through voting, and the influence of proxy advisors. This has introduced complexity into the ecosystem.	Much less established than other stakeholder dialogues. With increasing focus from regulators and wider stakeholders there is a need for further development and understanding.
Maturity	**Matured:** Highly developed and mature relationship where there is a strong, transparent, and open communication channel between investors and companies. Both parties actively collaborate on strategic matters, and trust is well-established.	**Developing:** Evolving from an early stage, necessitating ongoing adaptation to emerging standards, regulations, and stakeholder expectations. Focus shifting to delivery and practical actions.	**Mature:** Core conversation about voting is clear, it is facing major disruptions due to market changes, emphasising the need for adaptability and proactive engagement.	**Nascent:** Limited engagement and communication between investors and companies, with a lack of established channels for information exchange.
Intensity	**Intense:** High-frequency and deep engagement with opportunities for better dialogue, collaboration, and exchange of insights and feedback.	**Moderate:** Exchanges and discussions between investors and companies occur at varying levels, frequency and depth.	**Frequent:** Regular and consistent dialogue around AGM season, with opportunities for improving efficiency and effectiveness of information exchange and meaningful discussions.	**Minimal:** Infrequent or sporadic interactions with limited dialogue or engagement although willingness from both parties to engage when relevant and necessary.

Exploring the Key Insights From Each Dialogue

WHAT WE DISCOVERED

These pages offer a synthesis of the overarching insights gleaned from our exploration of the four dialogues between investors and companies. Across each dialogue, participants demonstrated a strong desire to comprehend diverse perspectives and seek efficient ways to enhance these dialogues. For each of the dialogues, we identified an overarching theme which we believe encapsulates the essence of the relationship between investors and companies. Subsequently, our exploration uncovered several key findings for each dialogue which, if addressed, we believe hold the potential to enhance and enrich the ongoing dialogue.

Information Dialogue With Investor Relations Professionals

Expertise is vital in this dialogue necessitating a high level of skill in identifying and communicating key strategic elements to build investor trust and encourage long term commitment combined with a detailed knowledge of a heterogeneous investor universe, and effective strategies to engage with and build long-term relationships with a wide range of investors.

What We Discovered:

Strategic Engagement Reimagined: It is essential for companies and investors to differentiate between two very important needs:

- Engagements for information; and
- Engagements focused on value creation.

There is much to be done to establish the right people to speak to and the purpose of each engagement – whether addressing concerns or meeting reporting needs – to ensure efficient interaction.

Navigating Regulatory Complexities: Both corporates and investors are grappling with the immense challenge of keeping up with a myriad of regulatory and reporting requirements. There is a danger that compliance and reporting requirements frame conversations and crowd out dialogue centred on strategic issues.

Holistic integration of sustainability considerations into strategy: The evolving sustainability landscape demands a more synchronised approach from both corporates and investors. Joint effort is needed to navigate the upcoming reporting frameworks and initiatives and to ensure a focus on decision-useful information and value creation.

Impact Dialogue with Sustainability Professionals

Complexity is a key theme of this dialogue. Rapidly changing regulations, diverse stakeholder expectations, and emerging technical issues combine to create a complex environment in which to analyse and communicate the impact of corporate sustainability efforts and ensure alignment with stakeholder expectations. There are a wide variety of views, which means a nuanced approach is needed to enhance mutual understanding and support improved decision-making, in order to enable both investors and corporates to deliver sustainable outcomes.

What We Discovered:

The shift from Aspiration to Action: Both corporates and investors recognised the need for a practical and action-oriented approach to sustainability. The common

Exploring the Key Insights From Each Dialogue

WHAT WE DISCOVERED

thread is the urgency to move beyond philosophical discussions to translate ambitions into tangible actions and impactful outcomes, on top of the tsunami of regulation and legislation surrounding sustainability that is impacting corporates and investors alike.

The value of Investor influence: Investors were seen to possess a significant power to drive change, yet there may be an underestimation of their influence. Corporate representatives responsible for sustainability initiatives expressed a desire for investors to be more assertive in their expectations from senior management and boards with regards to their sustainability-related action and performance. Insightful questions posed by investors, especially to leadership figures such as Chairs, CEOs, and CFOs, serve not only to keep sustainability atop the agenda but also act as a litmus test, signalling the importance of sustainability to them.

Reporting taking centre stage: Reporting, especially in environmental, social, and governance (ESG) areas, is overtaking the agenda for companies and investors. This focus often overshadows discussions on real world impact as both entities grapple with rising regulations and stakeholder expectations.

Acknowledging Shared Vulnerability: Both corporates and investors shared a vulnerability in their pursuit of sustainability, distinguishing it from conventional decision-making. The inherent uncertainty in data quality, the rapid pace of change, capital investment required, and the extended time horizons make this pursuit challenging. These factors necessitate a different style of dialogue to enables a deeper understanding and connection between corporates and investors.

Accountability Dialogue on Governance and Voting with Company Secretariat

Consistency emerges as a crucial theme in this dialogue. Both investors and companies seek to establish consistency in the voting process, emphasising the need for more uniformity in interpretation, execution and feedback. The dialogue also considered the sources of friction and a range of frustrations with the current system.

What We Discovered:

Positive Dialogue: Investors generally expressed positive sentiments about the dialogue with corporates in the UK market. They recognised value in transparency and governance practices, distinguishing the UK from other markets. However, there was acknowledgment that improvements can be made to enhance the dialogue, as corporate experiences with investors were less positive. The increasing impact of the evolving relationship of asset managers with their clients – asset owners – would need to be considered.

Remuneration Simplification: Unsurprisingly, investors advocated for a simplification of remuneration packages, with a unanimous message underscoring the necessity for clarity in this domain. Their emphasis was not solely on the reduction of complexity but also on aligning compensation structures with performance metrics and strategy. There was a broad concern within the investment community about the efficacy and transparency of executive pay structures.

Strategic Engagement for Tangible Outcomes: It was agreed by all that efforts were needed to focus on the purpose of engagement, moving beyond engagement for its own sake. The emphasis should be on enhancing

Exploring the Key Insights From Each Dialogue

WHAT WE DISCOVERED

value and ensuring tangible outcomes. Increased effectiveness in engagement may involve a wider range of approaches by companies and perhaps even a reduction in the frequency of interactions, allowing a shift towards more profound discussions on topics such as social and environmental issues, where a deeper understanding from both parties will be essential to achieve meaningful results.

Perception Gap: For companies there is a perception that governance professionals and investment teams are not joined up. Investors are adamant there is clear coordination and almost all asset managers have publicly available voting policies, and decisions rarely deviate from this policy without some review by the investment team. While asset managers strive for consistency, there is scope for misunderstanding after early soundings, particularly on remuneration issues. This perception gap is undermining trust and needs closing.

Assurance Dialogue with Audit Committee Chairs

Integrity emerged as the linchpin of this dialogue, underscoring its fundamental role in the audit and assurance processes. The discussion centred on how to ensure confidence in the reliability of corporate information through a better understanding of assurance and transparent high-quality dialogues to develop enduring trust for the benefit of investors and corporates.

What We Discovered:

Educating Investors: As Annual reports are long and complex, the roundtable emphasised the value of proactively providing investors with deeper insights into the responsibilities undertaken by Audit Committees and their Chairs. A focused programme would enrich investors' existing knowledge and address key investor issues to foster a more nuanced and comprehensive understanding of these critical functions.

Building Investor Confidence: It was felt that success in illuminating the roles and functions of Audit Committees could set the stage for heightened investor confidence. If actions can be taken to build a shared and comprehensive understanding, investors will be better equipped to assess the value and reliability of audit and assurance processes, establishing a solid foundation for meaningful conversations when needed.

Promoting Quality Dialogues: The desired outcome is not just informed investors but the initiation of high-quality corporate/investor conversations, as wanted and needed. Audit Committee Chairs (ACCs) are open to being readily available to be held to account, but neither investors nor companies see value in simply adding yet one more round of meetings to already crowded agendas. The focus should be to ensure that dialogues are substantive, meaningful, necessary and relevant, not simply routine.

What Companies & Investors Think

WHAT WORKS WELL OVERALL

In this section of our report, we delve into what constitutes excellent dialogue and interactions between investors and corporates, capturing best practices shared by both parties. Companies and investors alike have contributed insights into what "works well" from their respective standpoints, offering invaluable perspectives on effective engagement. We outline overarching best practices applicable to any dialogue or engagement between investors and companies, as well as specific observations from three of the four key dialogues – governance and voting, assurance and audit and sustainability. Together, these insights provide a comprehensive set of best practices for both investors and companies to consider, to build productive and mutually beneficial interactions.

What Companies & Investors Think

WHAT DO COMPANIES DO WELL?

Overall

- Companies that prioritise clear communication and proactive engagement in favourable times build strong trust and confidence among investors, laying a robust foundation for enduring relationships.
- Streamlining reporting and communications to present a summary investment case, value drivers, and key differentiators in a clear and accessible manner at each interaction helps investors' understanding amidst the information overload.
- Investors appreciate when corporates assist in balancing short-term trading updates with the broader context of the business. Including strategy, business model insights, and historical data in quarterly presentations, often available in an appendix, enhances transparency and investor understanding.
- Companies that share their questions in advance of a meeting give investors the opportunity to reflect and discuss internally, leading to more productive and insightful discussions during engagements.
- When companies connect and synthesise their reporting and communications in a strategically driven manner, integrating the importance of sustainability issues with financial performance, it results in consistent and coherent messaging that is more easily accessible.
- When companies prioritise clarity and transparency regarding their material issues, and connect those issues to their overall strategy, rather than focus on compliance-driven reporting, it demonstrates a deep understanding and confidence in their operations.
- When companies clearly demonstrate that ESG matters are fully endorsed by the CEO and the board, it sends a strong signal to investors regarding integration into the company's strategy and operations. This integration and commitment to transparency is reinforced when linked to remuneration practices and when substantial changes in sustainability targets are treated with the same gravity as financial target adjustments.
- When companies provide access to sustainability specialists for investors, it facilitates deeper conversations that lead to a comprehensive understanding of broader business and strategic aspects. This collaborative approach helps to focus on the holistic integration of sustainability into the company's operations and strategy, enhancing understanding and trust and mutual learning between investors and companies.

Sustainability

- Companies that emphasise their sustainability angle in initial meetings, highlighting their company thesis, strategy, and business model. A CEO's strong emphasis on sustainability signals genuine commitment, serving as a green flag for investors.
- Maintaining consistency in data across all reports and communication so that investors

What Companies & Investors Think

WHAT DO COMPANIES DO WELL?

receive a cohesive and consistent story, builds credibility and trust and reliability in reporting practices.

- Best practice for companies is to centralise all relevant information in one easily accessible location on their website, typically within the investors section. This centralised hub could include clear descriptions of the contents of each report to guide investors effectively. Additionally, cross-referencing tables to commonly used frameworks such as CSRD, SASB, and GRI can enhance transparency and ensure that investors understand the company's intentions regarding sustainability reporting.
- Companies that focus on consistency and standardisation across sustainability metrics, with clear measurement principles and disclosure of assumptions help investors understand reliability and comparability.
- Investors appreciate companies increasing acknowledgement of the necessity of external assurance for sustainability data and value when companies remain adaptable and committed to learning and improving in this evolving area.
- Companies that anticipate and adapt to changing regulatory and reporting landscapes with a practical approach to disclosures and seek clarity on investor preferences foster greater alignment and understanding.
- When companies invest effort in understanding investors' objectives, including diverse client demands and internal policies a more effective dialogue will result. Understanding whether investors are focusing on systemic risks or specific company issues and their underlying motivations and request will ensure that information and actions are tailored.

Governance & Voting

- Companies that proactively ask 'how do you make voting decisions'?
- Investors prefer clear and concise outlines of key policy changes from companies.

Assurance & Audit

- When companies provide clarity on what they are doing above and beyond regulatory requirements
- Board governance days, where companies will have all their Audit Committee, and other committee chairs and the Board Chair available to speak to investors. The Audit Committee Chair could present on the key issues with opportunity for investors to ask questions.
- When Audit Committees put out a letter once a year outlining the key changes they are making, this provides a clear understanding to investors and an opportunity to engage or not.

What Companies & Investors Think

WHAT DO INVESTORS DO WELL?

Overall

- Corporate access teams within institutions were praised by companies for facilitating broader access and coordination with various parts of the organisation. Some of the bigger investors have set up corporate access desks, for both fund management and stewardship issues, which are seen to very effective and valuable.
- Forward-thinking investors are innovating by deploying internal tools that enhance information exchange and streamline coordination efforts with companies.
- Some institutions openly tell companies exactly which of their funds hold their shares and who is responsible for the position and this was cited as very helpful with targeting engagement efforts more effectively.
- Several institutions had put on 'reverse roadshows' for companies, inviting them to hear more generally about their approach, structure, strategy, policies and key focus areas.
- Investment Bank industry conferences were cited as being great conduits for meeting large numbers of investors and particularly the 'fireside chats' for their CEOs to get messages out more broadly.
- When companies sense that an investor is genuinely 'invested in the management team,' fostering constructive conversations even during challenging times, a strong sense of support and trust emerges. This supportive dynamic allows for open two-way dialogue and enables the business to make informed and long-term decisions.
- When investors act as effective 'non-executives', companies find themselves engaged in broader, more meaningful strategic dialogues. This engagement allows for a deeper understanding of each other's perspectives and long-term considerations for the company, fostering a relationship built on mutual learning and shared strategic vision.
- Clear messaging and reinforcement from shareholders that it is acceptable to prioritise three or four issues relevant to their business, rather than attempting to cater to every stakeholder's demands was welcomed. This targeted focus allows companies to streamline their efforts and allocate resources more effectively, fostering a strategic alignment around the core objectives.
- When investors delve beyond the surface-level data and invest time in understanding the nuances behind the numbers, it signals a productive relationship. For instance, shifting the focus from generic metrics like 'number of women on the board' to exploring the dynamics and operations of the board reflects a commitment to understanding the intricacies of the company's governance and decision-making processes.

Sustainability

- Companies value when investors are clear on issues and support companies to test, learn, and make progress and appreciate when investors understand that solving challenges overnight isn't realistic and

What Companies & Investors Think

WHAT DO INVESTORS DO WELL?

they emphasise a gradual process of improvement and adaptation.

- Investors that move beyond short-term returns and engage in a deeper dialogue that involves understanding a company's long-term vision, its strategies for navigating sustainability challenges, and the integration of ESG considerations into core business practices.
- Open and clear dialogue, where both corporates and investors acknowledge the dynamic nature of sustainability challenges, share insights and commitment to learning and adapting.
- Investors who set the tone of a conversation by providing context for their data requests make a significant impact. For instance, they may explain that in order to retain companies in their fund, they require specific information to meet reporting and labelling requirements. This transparency helps companies understand the importance and urgency behind the requests.
- Investors that engage with companies meaningfully, seeking data points that truly help understand the business, focusing on quality over quantity.
- Some institutions openly communicate to companies the external ratings, agencies, and data providers they value, along with how this information feeds into their proprietary systems. For instance, institutions such as LGIM provide an online database which shows companies information about the metrics they use and how companies are assessed.
- Investors who invest time in reviewing a company's key materials and familiarise themselves with key issues are highly valued. This allows discussions to move beyond superficial information gathering to meaningful engagement focused on addressing real issues.
- When investors recognise the evolving nature of sustainability standards and acknowledge the infancy of data and reporting in some areas it gives companies confidence to continually learn, develop and refine approaches.

Governance & Voting

- Investors that explain their voting process and decision-making more thoroughly and advise companies in advance how they are going to vote.

Assurance & Audit

- Investors who proactively reach out to speak directly with Audit Committee Chairs to build relationships and gain insight into their roles and responsibilities are highly valued.
- Investors that provide clarity on the questions they have and the issues they're concerned about enable the Audit Committee Chairs to better comprehend their perspective and address their concerns effectively.
- Clear discussion between investors and Audit Committee Chairs on broader issues helps transparency and enhances the quality of the interactions.

INVESTOR RELATIONS DIALOGUE:

Building on Strong Foundations

The business of 'investor relations' is well established – companies seek to build a compelling equity thesis that resonates with investors. This revolves around a well-defined strategy and business model that outlines the company's objectives, competitive advantage, and growth prospects. Increasingly activity extends across asset classes and covers a much wider dialogue than the historic financial conversation. By effectively communicating the strategic elements, companies seek to build investor trust and encourage long-term commitment.

The question that we set out to address in this dialogue:

> ***How can we create a seamless information ecosystem that caters to the needs of both investors and corporates, promoting transparency, trust, and informed decision-making?***

Investor Relations
Dialogue Contents

Highlights of this Dialogue

INVESTOR RELATIONS

What Is the Key Principle?

Expertise plays a pivotal role in this dialogue. Effective Investor Relations requires:

- A high level of expertise in identifying and communicating key strategic elements to build investor trust and encourage long term commitment.
- Detailed knowledge of a heterogeneous investor universe, and effective strategies to engage with and build long-term relations with a wide range of investors.

What Did We Discover?

Strategic Engagement Reimagined:
It is essential for companies and investors to differentiate between two very important needs:

- Engagements for information; and
- Engagements focused on value creation.

There is much to be done to establish the right people to speak to and the purpose of each engagement – whether addressing concerns or meeting reporting needs – to ensure efficient interaction.

Navigating Regulatory Complexities:
Both corporates and investors are grappling with the immense challenge of keeping up with a myriad of regulatory and reporting requirements. There is a danger that compliance and reporting requirements frame conversations and crowd out dialogue centred on strategic issues.

Strategic Integration of Sustainability:
The evolving sustainability landscape demands a more synchronised approach from both corporates and investors. Joint effort is needed to navigate the upcoming reporting frameworks and initiatives and to ensure a focus on decision-useful information and value creation.

What's Next?

A joint commitment by companies and investors to:

- Build clearer lines of communication to create efficient and effective information exchange and dialogue; and
- Focus on holistic narratives and integrated strategies to mitigate challenges and create lasting value.

Key Expectations of Investor Relations

Investor relations (IR) professionals are crucial bridges between the company's leadership and the investors. Investors value professional IR. Key expectations include:

Spokesperson for Leadership:
IR professionals should reflect the views of the CFO and CEO effectively, and the importance of being joined up should not be underestimated.

Communication of Company Narrative:
IR should effectively communicate the company's thesis, while recognising that challenges to the strategy and future focus might demand direct engagement with the CEO or CFO.

Availability for Communications:
IR should ensure they are easily accessible to investors for addressing concerns or seeking clarification following an announcement.

Integration with Business Operations:
IR's connection and integration with the broader business and operational aspects demonstrates to investors a comprehensive understanding and optimises communication of the company's thesis including strategic issues.

Facilitation of Meaningful Conversations: An IR's willingness to have substantive discussions is exemplified by their proactive engagement of specialists from around the business, including areas like climate, sustainability and audit to address investors questions or concerns directly.

Overview of the Current Market Landscape

The investor relations dialogue has evolved into a well-established and well-formed process, marked by strong relationship development between corporates and investors. This dialogue has reached a high level of maturity, fostering trust through consistent communication and a clear understanding of investor expectations.

Access to UK Boards is perceived as a significant advantage. Numerous investors have highlighted favourable access to Boards, and individual Non-Executive Directors (NEDs), as a major positive in comparison to most continental European markets, and US markets, where such access is deemed challenging, sometimes "almost impossible," and frequently viewed as a significant escalation.

> ***"UK companies are absolutely available to talk to."***
>
> *- Head of ESG and Stewardship, Asset Manager*

However, there is broad consensus that the remuneration discussion has become disproportionately emphasised, potentially overshadowing a myriad of other crucial discussions. It is recognised that redirecting attention to a more holistic range of topics is essential for a comprehensive understanding and effective decision-making dialogue.

Investors generally perceive well-established communication and reporting practices with investee companies, particularly the FTSE350, where they are encouraged by the quality of interactions with Investor Relations professionals and the adequacy of information received. However, smaller companies face challenges due to limited focus and resources, often resulting in reactive approaches and increased reliance on third-party assistance, such as brokers, for communication.

Despite its maturity, there are important issues to be addressed, which will help to enhance transparency and align strategies for long-term value creation. There is recognition that there has been a decline in resources dedicated to UK company analysis by investors compared to a decade ago. Large UK-based investors who previously dedicated a significant proportion of their assets to UK companies have diversified their investments globally across various asset classes and/or moved into bonds.

The interconnectedness of the UK within the global financial ecosystem and the need to effectively tackle systemic issues like climate change, means that it is imperative to consider how to operate effectively within the international architecture, especially from an ESG perspective.

Investment management firms are facing a lot of pressure and demand from their clients – asset owners – on multiple themes and it is important that they demonstrate their engagement with companies. Different clients have different expectations – whether driven by the need to meet regulatory requirements, sustainability objectives, or risk to portfolio rather than impact of portfolio.

> ***"It's not all just about investment return. There are multiple different client considerations that we try and take into account."***
>
> *- Head of Stewardship, Asset Manager*

This pressure to obtain information from companies to meet client demands combined with investors having to engage in an environment which is increasingly regulated, is leading to more focus and scrutiny on disclosure and reporting, particularly where ESG issues are relevant and has diverted some of the focus from long-term value.

There is an acknowledgment that investors and companies need to come together, listen to challenges, and work collaboratively towards solutions, to determine the most effective means of communication in this evolving environment.

Summary of market considerations to be acknowledged:

- Time constraints for both investors and companies
- Proliferation of regulation and reporting requirements for both investors and corporates
- Increasing importance of ESG to all stakeholders
- Decline in investor resources dedicated to UK company analysis
- Diverse asset manager approaches
- Increased pressure from asset owners
- Resource limitations of smaller companies

Investor Relations Myths

Before delving into key challenges, what works well and actions, it's important to 'bust' some of the myths that we uncovered specific to this dialogue to help set a clear framework for a more productive dialogue.

Myth: All Engagement Is Good Engagement

Reality: No, Strategic engagement is good engagement. Understanding the purpose behind engagement is vital – whether aimed at information gathering or transformative change. Clear objectives, well-defined agendas, and robust feedback mechanisms are essential components for impactful dialogue. Recognising that not all engagement is equal underscores the necessity for intentionality and strategic alignment in every interaction between investors and companies.

Myth: Consistently Applying the Same Approach Guarantees Success

Reality: This is misleading. Dynamic markets, different investment approaches, evolving investor expectations, and increasing stakeholder demands necessitate a shift toward redefined relationships. Rather than adhering to conventional practices, success hinges on establishing agreed-upon expectations before delving into specifics.

Myth: All Companies and Investors Are the Same

Reality: No two companies or two investors are the same. Companies vary in size, structure, industry, geography, strategy, governance and financial health, while investors have diverse objectives, approaches, risk tolerances, time horizons and investment preferences. Recognising and understanding these differences is crucial for effective communication and collaboration, ensuring tailored approaches that acknowledge the unique characteristics of each company and investor.

What Companies Think

KEY CHALLENGES

Access Within Investment Firms

While relationships between investors and companies are well established, for the most part – the general decline in resources focused on UK equities, combined with compliance regulations such as MiFID which have in practice limited interactions, is making it more challenging for corporates to establish new relationships with investors. Not all corporates have difficulties with access, but many FTSE350 companies shared challenges in accessing investors, including major shareholders, for informal discussions. Garnering interest from the buy side was becoming increasingly difficult for formal road shows and capital markets days.

> **"Access is hard. I feel ignored, even by the bigger shareholders – it's a challenge to have a chat."**
>
> *- FTSE50 Investor Relations Director*

Extending Relationships Within Institutions

There was a realisation by corporates that they need to establish relationships beyond the fund managers, with the stewardship teams, to understand how their processes work and what information they need. Common across all company participants was that in larger institutions, they often encountered difficulties reaching beyond a particular analyst or fund manager who controls access, hindering the development of broader relationships and the dissemination of their thesis. Many companies had set up governance road shows, to address these issues, which had been well received by investors.

> **"We need to establish relationships with people that vote the shares and understand what they look at, how their process works, as we know that our information and messaging might need to be a bit more nuanced compared to what we are discussing with the fund managers."**
>
> *- FTSE100 Investor Relations Director*

Building Relationships Off Season

Many corporates had attempted to contact investors off-season, only to face difficulties in establishing engagement outside of specific issues. This limited interaction frustrates companies, as it prevents relationship-building opportunities and restricts engagement to specific, often reactive, responses.

Lack of Engagement From Passive Funds

Another common theme was frustration over the passive funds' stewardship teams' lack of engagement. There is a widespread sentiment among companies that these institutions need to enhance their stewardship efforts and allocate resources for broader market interaction, given their investment in the entire market – a missed opportunity for both parties.

Obstacles Intensify for Small – Midcap Companies

Access is even more challenging for small to midcap companies, which often have minimal portfolio weightings and receive limited attention. Moreover, their engagement with entities like ISS may be less sophisticated, posing challenges around voting season.

> **"You are trying to do the right thing and reach out to these people, but nobody seems to be listening or interested."**
>
> *- FTSE250 Head of Investor Relations*

Securing Investor Feedback

It is also difficult to get feedback from investors particularly with the declining influence of corporate brokers. There is a desire for investors to be more open about giving feedback after meetings, fostering a two-way discussion instead what often feels like a one-way flow of information. Companies are receptive to investors' preferences regarding how feedback is shared but are keen to increase commitment and structure within the process.

What Companies Think

WHAT DO INVESTORS DO WELL?

- Corporate access teams within institutions were praised by companies for facilitating broader access and coordination with various parts of the organisation. Some of the bigger investors have set up corporate access desks, for both fund management and stewardship issues, which are seen to very effective and valuable.
- Forward-thinking investors are innovating by deploying internal tools that enhance information exchange and streamline coordination efforts with companies.
- Some institutions openly tell companies exactly which of their funds hold their shares and who is responsible for the position and this was cited as very helpful with targeting engagement efforts more effectively.
- Several institutions had put on 'reverse road' shows for companies, inviting them to hear more generally about their approach, structure, strategy, policies and key focus areas.
- Investment Bank industry conferences were cited as being great conduits for meeting large numbers of investors and particularly the 'fireside chats' for their CEOs to get messages out more broadly.

What Investors Think

WHAT DO COMPANIES DO WELL?

Simplifying Investor Interactions

A common desire from all investors was simplification of investor interactions. There was a sense that corporates didn't recognise the significant time constraints faced by investors amidst the overflow of information in today's landscape. Investors are inundated with a vast array of data, reports, and communication from numerous companies vying for their attention. The huge volume of information makes it challenging for many investors to allocate sufficient time to engage meaningfully with each company.

> ***"It's getting all a bit bloated and quite challenging for investors to really understand the material issues."***
>
> *- Portfolio Manager, Asset Manager*

Many investors expressed the frustration at the lack of understanding by corporates that within investor organisations, different roles necessitate diverse information tailored to specific purposes, whether to inform investment decision-making processes or to fulfil client requests, regulatory requirements or compliance requirements.

Optimising Engagement Timing

Optimising engagement timing is a multifaceted challenge for investors, as they strive to strike a delicate balance between engaging with companies only when necessary and satisfying company desires which are typically for more immediate interactions. Investors recognise the importance of engaging with companies at strategic times, such as after results, in advance of annual meetings or when significant developments occur. These engagements allow investors to gain insights into companies' performance, strategies, and governance practices, enabling informed decision-making regarding their investment portfolios. However, the challenge arises when investors face the pressure to engage more frequently.

> ***"There isn't necessarily expectation to have regular dialogue throughout the year because we respect the fact that management need to do their day jobs."***
>
> *- Head of Stewardship, Global Asset Manager*

Moreover, the challenge of optimising engagement timing is compounded by the diverse preferences and priorities of investors, within an institution and across the market. Some investors may prioritise regular updates and real-time communication, while others may prefer a more selective and strategic approach to engagement.

What Investors Think

WHAT DO COMPANIES DO WELL?

- Companies that prioritise clear communication and proactive engagement in favourable conditions build strong trust and confidence among investors, laying a robust foundation for enduring relationships.
- Streamlining reporting and communications to present a summary investment case, value drivers, and key differentiators in a clear and accessible manner at each interaction helps investors' understanding amidst the information overload.
- Investors appreciate when corporates assist in balancing short-term trading updates with the broader context of the business. Including strategy, business model insights, and historical data in quarterly presentations, often available in an appendix, enhances transparency and investor understanding.
- Companies that share their questions in advance of a meeting give investors the opportunity to reflect and discuss internally, leading to more productive and insightful discussions during engagements.

What Companies & Investors Think

SHARED CHALLENGES

Navigating the Regulatory Maze

Navigating the regulatory maze presents a huge challenge for both investors and corporates, as they adapt their strategies and engagement approaches amidst a fast-changing landscape for reporting requirements and evolving legislation, especially around ESG.

For corporates, the challenge lies in ensuring compliance with a myriad of regulations, reporting standards and disclosure requirements while focusing on what is material and relevant for their business. This requires a balance between meeting regulatory obligations, delivering business as usual and pursuing strategic initiatives that drive long-term value creation. Many corporates shared the concern that there was an overreliance and focus on ESG data from investors, which is often in a nascent stage and which puts at risk the understanding of the dynamics behind the data and a more holistic view of the business.

Similarly, investors are confronted with the task of staying abreast of regulatory changes and assessing their implications on investment decisions. They must navigate through complex regulatory frameworks and evolving legislation to make informed investment choices that align with their compliance requirements, risk tolerance and investment objectives as well as those of their clients. In addition, investors must also consider how regulatory developments may impact corporate performance, governance practices, and overall investment viability of the companies they invest in.

> ***"Don't throw a load of ESG boilerplate in the mix – it confuses everyone. It confuses your business, but it also confuses investors."***
>
> *- Fund Manager, Asset Manager*

Both investors and corporates expressed concerns about being inundated with reporting regulations. On both sides, teams tend to find a need to disproportionately focus on reporting rather than on actual operational activities.

Aligning Corporate Sustainability Journeys with Investor Expectations

Navigating the transition towards sustainability presents a significant challenge for the dialogue between investors and corporates, as both parties seek to align corporate sustainability journeys with evolving expectations while maintaining a focus on performance.

Corporates are increasingly recognising the importance of integrating sustainability principles into their business strategies as part of their long-term commitment to environmental, social, and governance factors. However, incorporating sustainability practices into corporate operations involves a complex and ongoing journey that requires significant investments in resources, infrastructure, and cultural transformation which is seen not to always be appreciated.

At the same time, investors are placing greater emphasis on sustainability factors when evaluating investment opportunities due to the demands of the market and their clients. So, increasingly they need more information about ESG performance and commitment to sustainable business strategies to help them manage their risks, compliance requirements and to meet eligibility requirements and client demands. Therefore, they expect corporates to disclose relevant ESG information to enable informed investment decisions.

Many companies, primarily those recognised as sustainability leaders, are having more demanding conversations with investors. This increased scrutiny is often because they are perceived to have a core sustainability dynamic, which is attracting attention from numerous funds and intermediaries.

> ***"The quality of engagement on ESG issues with IR Directors and companies overall is improving, but there is also an acknowledgement that everyone can't know everything about everything."***
>
> *- FTSE100 IR Director*

What Companies & Investors Think

SHARED CHALLENGES

Focusing On Materiality

Balancing corporate sustainability commitments with investor expectations poses a dual challenge for corporates – they must navigate the complexities of integrating sustainability principles into their operations while ensuring alignment with performance objectives. This requires clear strategic alignment, robust governance structures, and effective communication channels to articulate the business case for sustainability and demonstrate its impact on long-term value creation. Both companies and investors are increasingly acknowledging the importance of ESG reporting. While some companies may initially approach it as a superficial exercise, there is a growing realisation of the need for focusing on the material issues and a deeper integration of ESG practices into their overall strategy.

> **"Companies should focus on what's really important and material."**
>
> *- Head of Research and Engagement, Asset Manager*

On the other hand, investors must assess corporate sustainability efforts within the broader context of financial performance and risk management. They seek transparency, accountability, and consistency in corporate sustainability disclosures to evaluate the resilience and sustainability of investment portfolios.

Further complicating this dynamic is the demand for data requests, experienced by both corporates and investors alike, particularly tailored surveys demanding information that has usually already been disclosed through reporting. Companies often find expectations surrounding data, the detail and its verification to be unrealistic, sometimes surpassing those placed on financial data.

> **"I think that there must be a little bit of trust with ESG, in the same way you would trust a management team to manage a business for revenue generation and profit. They will manage the business in best way in terms of ESG."**
>
> *- FTSE100 IR Director*

The scrutiny on sustainability efforts, while essential, can obscure the focus on action. There's a growing concern that sustainability efforts are receiving disproportionate attention, potentially overshadowing other critical business areas. It's crucial to maintain a balanced perspective and avoid the risk of sustainability initiatives detracting from overall long-term strategy and business goals.

What Companies & Investors Think

WHAT DO COMPANIES AND INVESTORS DO WELL?

Investors

- When companies connect and synthesise their reporting and communications in a strategically driven manner, integrating the importance of sustainability issues with financial performance, it results in consistent and coherent messaging that is more easily accessible.
- When companies prioritise clarity and transparency regarding their material issues, and connect those issues to their overall strategy, rather than focus on compliance-driven reporting, it demonstrates a deep understanding and confidence in their operations.
- When companies clearly demonstrate that ESG matters are fully endorsed by the CEO and the board, it sends a strong signal to investors regarding integration into the company's strategy and operations. This integration and commitment to transparency is reinforced when linked to remuneration practices and when substantial changes in sustainability targets are treated with the same gravity as financial target adjustments.
- When companies provide access to sustainability specialists for investors, it facilitates deeper conversations that lead to a comprehensive understanding of broader business and strategic aspects. This collaborative approach helps to focus on the holistic integration of sustainability into the company's operations and strategy, enhancing understanding and trust and mutual learning between investors and companies.

Companies

- When companies sense that an investor is genuinely 'invested in the management team,' fostering constructive conversations even during challenging times, a strong sense of support and trust emerges. This supportive dynamic allows for open two-way dialogue and enables the business to make informed and long-term decisions.
- When investors act as effective 'non-executives', companies find themselves engaged in broader, more meaningful strategic dialogues. This engagement allows for a deeper understanding of each other's perspectives and long-term considerations for the company, fostering a relationship built on mutual learning and shared strategic vision.
- Clear messaging and reinforcement from shareholders that it is acceptable to prioritise three or four issues relevant to their business, rather than attempting to cater to every stakeholder's demands. This targeted focus allows companies to streamline their efforts and allocate resources more effectively, fostering a strategic alignment around the core objectives.
- When investors delve beyond the surface-level data and invest time in understanding the nuances behind the numbers, it signals a productive relationship. For instance, shifting the focus from generic metrics like 'number of women on the board' to exploring the dynamics and operations of the board reflects a commitment to understanding the intricacies of the company's governance and decision-making processes.

Actions for Companies & Investors

TOP TIPS FOR COMPANIES

Improving Effectiveness and Efficiency

- Tailor engagement strategies by identifying preferred modes of communication with your investors, such as meetings, emails, or conference calls and agreeing on the frequency and timing of engagements to ensure mutual convenience and effectiveness.
- Determine the purpose of any meeting – information gathering or investment decision-making.
- Set clear agendas for all meetings and establish clarity on the attendees and their roles/interests.
- Encourage investors to share questions or topics of interest before the meeting to maximise effectiveness and address specific concerns.
- Build in 5-10 minutes at the end of each meeting for direct feedback from investors.
- Understand the specific information needs of the investor, whether it's financial performance updates, strategic insights, sustainability issues or governance practices and investor expectations in terms of attendee.
- Tailor communications to meet the needs of your different audiences – credit, equity, ESG – as each has different interests and priorities, investment strategies, risk appetite, and long-term goals.
- Make conscious decisions how to use corporate brokers effectively.
- Take time to assess investor perceptions.
- Corporates should maintain a generic [IR@plc.com] email address to enable easier communicationss from investors.

Navigating Complexity of Regulation and Sustainability

- Be bold in crafting and owning your narrative, emphasising your unique value proposition and sustainability journey.
- Communicate with straightforwardness and authenticity in all interactions to build trust and credibility.
- Understand the materiality of issues within your company and use this understanding proactively to address regulatory requirements.
- Align reporting efforts with strategic objectives to ensure coherence and relevance.
- Avoid unnecessary complexity in reporting by providing clear summaries and linkages and present information in various formats tailored to the needs of different investors.
- Clearly articulate the reporting frameworks and standards used, explaining the rationale behind their selection.
- Be selective in responding to surveys and data requests, ensuring alignment with your narrative and strategic priorities.
- Understand the diverse needs of different investors and how they utilise data and reporting. Be aware of the pressure and influence of different asset owners mandates on asset managers.
- Tailor your communication and reporting strategies to effectively meet different needs.

Actions for Companies & Investors

TOP TIPS FOR INVESTORS

Improving Accessibility and Understanding

- Create and monitor a centralised contact@ email to enable companies to make direct contact.
- Consider setting up corporate access desks to facilitate broader access and coordination across organisation.
- Create fact sheets on investment organisation, including voting policies.
- Consider providing greater transparency to companies on which funds are invested in the company, and which are passive.
- Encourage internally joined up meetings with governance specialists and portfolio managers, and where appropriate fixed income investors, when discussing key issues.
- Instigate reverse road shows to explain structure, approach and key focus areas (e.g. leverage Stewardship reporting).
- Collaborate with other like-minded investors on key issues to amplify the collective voice and influence. By pooling resources and expertise when relevant, investors can enhance their effectiveness on some issues.

Navigating Complexity of Regulation and Sustainability

- Reinforce the acceptance of prioritising three or four issues relevant to the company's business.
- Encourage companies to streamline efforts and allocate resources effectively, aligning with core objectives and strategic focus.
- Invest time in understanding the nuances behind the numbers and metrics presented by companies.
- Provide clarity on your key issues of interest.
- Join up thinking internally between fund managers and stewardship teams.
- Ensure consistency and joined up demands on company involvement in voluntary initiatives such as Net Zero alliance.
- Provide greater clarity on how you use external rating agencies and data providers.
- Share commitments and preferences to reporting standards, metrics and frameworks.

SUSTAINABILITY DIALOGUE:

Aligning Investor Influence with Corporate Sustainability

Companies face expectations from various stakeholders including employees, customers, consumers, regulators and investors to demonstrate their commitment to address sustainability issues. Investors are also increasingly incorporating sustainability into their investment and stewardship considerations.

The question that we set out to address in this dialogue:

> ***How can we better measure, communicate, and align the impact of investments with corporate strategy efforts, benefitting both investors and corporates in pursuing sustainable goals?***

Sustainability
Dialogue Contents

Highlights of this Dialogue

SUSTAINABILITY

What Is the Key Principle?

Complexity is a key theme of this dialogue. Rapidly changing regulations, diverse stakeholder expectations, and emerging technical issues combine to create a complex environment in which to analyse and communicate the impact of corporate sustainability efforts and ensure alignment with stakeholder expectations. There are a wide variety of views, which means a nuanced approach is needed to enhance mutual understanding and support improved decision-making, in order to enable both investors and corporates to deliver sustainable outcomes.

What Did We Discover?

The shift from Aspiration to Action: Both corporates and investors recognised the need for a practical and action-oriented approach to sustainability. The common thread is the urgency to move beyond philosophical discussions to translate ambitions into tangible actions and impactful outcomes, on top of the tsunami of regulation and legislation surrounding sustainability that is impacting corporates and investors alike.

The value of Investor influence: Investors were seen to possess a significant power to drive change, yet there may be an underestimation of their influence. Corporate representatives responsible for sustainability initiatives expressed a desire for investors to be more assertive in their expectations from senior management and boards with regards to their sustainability-related action and performance. Insightful questions posed by investors, especially to leadership figures such as Chairs, CEOs, and CFOs, serve not only to keep sustainability atop the agenda but also act as a litmus test, signalling the importance of sustainability to them.

Reporting taking centre stage: Reporting, especially in environmental, social, and governance areas, is overtaking the agenda for companies and investors. This focus often overshadows discussions on real world impact as both entities grapple with rising regulations and stakeholder disclosure expectations.

Acknowledging Shared Vulnerability: Both corporates and investors shared a vulnerability in their pursuit of sustainability, distinguishing it from conventional decision-making. The inherent uncertainty in data quality, the rapid pace of change, capital investment required, and the extended time horizons make this pursuit challenging. These factors necessitate a different style of dialogue to enable a deeper understanding and connection between corporates and investors.

What's Next?

In such a complex environment, corporates and investors both face enormous challenges as they seek to create and coalesce around compelling and integrated sustainability. Targeted dialogue can help investors and corporates align expectations and identify approaches to ensure a focus on decision – useful information.

Ultimately corporates and investors will need to determine if they want to tackle these challenges via relationships based on mutual respect and trust or to engage via a disclosure and assurance regime that seeks to hold to account by raising questions over greenwashing and limited ambition.

Overview of the Current Market Landscape

The dialogue with Chief Sustainability Officers or those responsible for sustainability is new and evolving at an exponential pace, driven by its ever-increasing importance in today's business environment. There is a heightened level of complexity resulting from rapidly changing regulations, diverse stakeholder expectations, and emerging technical issues. The growing recognition of sustainability as a core driver of organisational value and resilience, coupled with the escalating importance of sustainability considerations in investment decisions, is reshaping this dialogue between companies and investors at it adapts to the business landscape.

Motivations: Companies are coming to the sustainability conversation for various reasons – eg the business opportunity, to manage risks, regulation and reporting requirements compelling them to, because capital markets reward them for doing so, heightened scrutiny from society – or because they genuinely want to make a positive real-world difference.

Investors also come with differing reasons – eg client mandates, to fulfil portfolio reporting requirements, to spot early opportunities, to manage systematic and company specific risks, or to demonstrate commitment to a single issue they have chosen to differentiate themselves in the eyes of the market.

Maturity: The dialogue overall is evolving from an early stage, necessitating ongoing adaptation to emerging standards, regulations, and stakeholder expectations. After a period of discussion and development the focus has shifted to delivery and practical actions.

Challenges and Opportunities: The fast-paced changes pose challenges in keeping up with this rapidly developing dialogue, but they also offer opportunities for both corporates and investors to demonstrate commitment to sustainability goals and for aligning strategies with evolving ESG considerations.

Corporate approaches: Companies are embarking on huge programmes of internal change and introducing new architectures to operationalise aspirations, deliver net zero intentions, and gather the data required to comply with new reporting regimes.

It is evident that each company must tailor its governance, systems and processes to suit its unique business context and its point on the sustainability journey. Sustainability teams are becoming much more cross-functional and can comprise individuals from finance, IR, policy, or specialist backgrounds, and have a variety of reporting structures. Increasingly individuals are transitioning from traditional sustainability roles to finance, especially for investor engagement and reporting, while many finance professionals are enhancing their skills to handle sustainability matters. In some cases, sustainability teams are reporting into CFOs.

Regardless of the approach, top-level endorsement and strategic guidance are essential for sustainability teams to be truly effective, with CEO buy-in playing a crucial role, as well as Board level oversight.

Participants emphasised the importance of sustainability expertise and credibility at the Non-Executive Director (NED) level in driving management toward sustainability goals. Finance teams are also assuming a more prominent role in ESG integration, particularly in data management and reporting, signalling a shift towards holistic financial disclosure and accountability.

> ***"We are all learning and many corporates are evolving to create roles to help drive change internally and deal with the myriad of reporting and disclosure requirements, as well as support the CR team from a finance perspective on a number of workstreams."***
>
> *- Director ESG Finance, FTSE100*

Overview of the Current Market Landscape

Investor approaches: Investors are actively recalibrating their strategies and engagement approaches to align with their sustainability agendas and to meet client demands. Structures and resources have been realigned to accommodate the ESG integration, with dedicated teams and specialised expertise brought in.

Impact on relationships: There is a growing emphasis on transparency and disclosure from both companies and investors to assess long-term sustainability performance. The complexity and volume of sustainability reporting necessitates dedicated resources and expertise to ensure robust compliance and meaningful impact assessment and continued investment in sustainability governance and capacity-building initiatives.

The dialogue between companies and investors is diverse and often in its early stages. Both need to exchange insights and perspectives on emerging sustainability trends, regulatory developments, and industry best practices. As sustainability issues grow in complexity and scope, collaborative engagement and knowledge-sharing become increasingly important to navigate the challenges of sustainability integration and impact measurement.

> ***"There isn't a clear blueprint for how collaboration between investors and corporations on sustainability initiatives is supposed to work."***
>
> *- Director of Sustainable Business, FTSE100*

Changing paradigm: Participants indicated that pursuing a sustainability agenda presents both companies and investors with a unique uncertainty, unlike conventional business decisions. The difficulties surrounding sustainability data, the longer timeframes needed for meaningful impact, and the evolving understanding of ESG factors create a dynamic landscape where traditional risk assessments may not suffice.

> ***"Not having all of the answers requires an unusual amount of vulnerability, which a lot of leaders aren't used to demonstrating. It's not in their DNA, because that is not the way that they've been running businesses for the last 25-30 years."***
>
> *- Director of Sustainable Business, FTSE100*

Consequently, a paradigm shift is occurring in how companies and investors engage in dialogue, involving more individuals being upskilled on sustainability issues, additional use of specialist expertise and commitment to improving understanding on both sides. Traditional metrics and financial indicators, while still relevant, must be complemented by a deeper understanding of ESG factors and a willingness to embrace a longer-term investment horizon. The uncertainty inherent in sustainability data necessitates

Overview of the Current Market Landscape

a commitment to ongoing transparency and collaboration among experts from both companies and investor groups. There is recognition that there is underlying value in these broader conversations, but frustration because its nascent nature and the ecosystem isn't fully developed, often resulting in a suboptimal and inefficient dialogue.

> ***"Whilst there are massive benefits from investors focusing on non-financial performance as well as financial performance, it's hugely onerous and time-consuming, and it can be somewhat disengaging."***
>
> *- Investor Relations Director FTSE100*

This is a work in progress, but ultimately, companies and investors embracing this vulnerability as an opportunity for collaboration and innovation will be better positioned to navigate the complexities of sustainability and contribute to a more resilient and responsible future.

Summary of market considerations to be acknowledged:

- Growing recognition of the importance of sustainable business practices.
- Proliferation of regulation and reporting requirements for both investors and corporates.
- Time and resource constraints for both investors and companies.
- No 'one size fits all' solution to optimal governance and reporting of sustainability issues – although board-level endorsement is key.
- Investors are recalibrating investment strategies and adjusting how they integrate ESG considerations in response to client demand.
- ESG ratings are useful tools, and external agencies can flag areas of concern for investors. Corporates need to be mindful of methodologies and scoring criterial to provide right inputs to achieve the right outputs.
- There's no established blueprint for sustainability collaboration between investors and companies. However, exchanging insights on sustainability trends, regulations, and best practices is crucial for mutual learning.
- Pursuing sustainability exposes both companies and investors to unique vulnerabilities, requiring a paradigm shift in engagement and specialised expertise on both sides.
- The discussions surrounding ESG and sustainability is mired in confusion and inconsistency, as terms are often used interchangeably or with disparate definitions, highlighting the importance for clearly defined language to ensure meaningful dialogue and actions.

Sustainability Myths

Before delving into key challenges, what works well and actions, it's important to 'bust' some of the myths that we uncovered specific to this dialogue to help set a clear framework for a more productive dialogue.

Myth: ESG Considerations Are Only Relevant for Certain Industries and Sectors

Reality: Environmental, social and governance factors are integral to all businesses but manifest in different ways and at differing levels of materiality. With the UK's commitment to a net-zero target, companies and investors alike must evidence their plans, activities, and actions towards sustainability. There are broader shifts in societal expectations and increased regulatory efforts that need to be addressed.

Myth: ESG Is Exclusively a Risk Management Tool for Investors

Reality: ESG entails more than just risk mitigation. It spans both risks and opportunities. While effectively managing environmental, social, and governance risks is pivotal, embracing ESG also unveils opportunities for innovation, market differentiation, and sustainable growth. Recognising the dual nature of ESG, as a risk management tool and a source of opportunities, positions investors to make well-informed decisions that align with holistic success, resilience, and long-term value creation and it is incumbent on companies to communicate in this light.

Myth: More Data Is the Answer

Reality: While sustainability data is undeniably crucial for gaining insights into a company's practices and track record, it is essential to understand that collecting data alone is not the solution to drive change. The true impact of sustainability efforts will be in capital allocation decisions that drive strategic investments and decisive actions. Investors play a pivotal role in providing the support needed to drive tangible and sustainable outcomes. Both companies and investors need to move beyond a sole emphasis on data reporting and collection and prioritise a longer-term perspective, recognising that strategic investments are crucial for achieving meaningful transition.

What Companies Think

KEY CHALLENGES

Resource Investment and Meaningful Reporting

All corporates emphasised the substantial investment needed for reporting, investor engagement and action on sustainability issues not only in terms of financial resources but also in technology, human resources, and governance structures. There was an underlying commitment to addressing the needs of the market head on with the overriding objective to avoid turning ESG reporting into a burdensome process without meaningful impact. Many highlight the significant challenge corporations face in gathering and disclosing ESG data, especially for large, multinational companies. The scale involves dealing with diverse operations across numerous countries. For most companies the process is currently very manual with mixed quality, with recognition there is much work to be done to improve. There was a hope that new technology might make things more efficient in the future.

> ***"It is a huge undertaking in terms of the resource required, the systems investment, the people, and the controls and governance."***
>
> *- Director ESG Finance, FTSE100*

Investors look for signals on whether the sustainability story is integrated, in consistency of communications and level of transparency and disclosure.

Integrating ESG Into Core Business Practices

All corporates expressed optimism about sustainability becoming an integral part of standard business practice. Some corporates acknowledge that there is still a prevailing perception that ESG is primarily the responsibility of corporate responsibility / sustainability team. This points to the ongoing challenge of shifting this perception and making ESG considerations a fundamental part of business operations and 'a part of everyone's day job'.

Maintaining Focus on Material Issues

The challenge for companies is maintaining a balance between sustainability efforts and commercial performance. While acknowledging the importance of disclosure and doing the right thing, many emphasised the need to avoid detrimental impacts on commercial performance. Striking a balance between sustainability and financial performance is crucial to meet shareholders expectations.

> ***"Shareholder returns ultimately need to go up – that's what our shareholders are going to want us to do, as well as all the ESG stuff. So, it's just trying to keep everything in context, maintain that perspective and strike that balance."***
>
> *- Sustainable Finance Director, FTSE100*

Encouragingly most companies were comfortable with their material issues and suggested they would use this framework to help navigate and provide focus on the increasing disclosure requirements. Many companies shared a layering approach from their material issues to their additional disclosures so that they remained relevant and strategic.

> ***"We need to draw out what's material, and explain why things are not material. I want to focus on the key areas and explain why these are important, and why the other things I'm asked about are not important."***
>
> *- Investor Relations and Sustainability Director, FTSE100*

Investors appreciate companies having a strong narrative about what is important to them and why and accept push back if a disclosure request is on something that really isn't material, is confidential or

What Companies Think

KEY CHALLENGES

at odds with the way they manage the business. However, they expect companies to be able to communicate on the full range of potential issues, to demonstrate that they have no blind spots.

Gaining Insight into Investors' Methods of Accessing and Utilising Data

Companies are at different stages of their sustainability journey – both operationally within their business and in their engagement with investors. Some proactively engage with investors, while others take a more reactive approach, waiting for investor queries.

The lack of homogeny within the investment industry presents companies with a confused and opaque picture of priorities and information needs. Many corporates are conscious of the need to avoid greenwashing and want to ensure meaningful and relevant communication. This reflects the delicate balance companies must strike in presenting their ESG efforts transparently and authentically. Many find that investors generally understand key issues well and engaged fundamental investors are often understanding of the long-term challenges and uncertainties.

> **"Clever investors have listened well over the years, focused on the material issues and understand the impact on the business."**
>
> *- Investor Relations and Sustainability Director, FTSE100*

Clarifying What Data is Relevant for Investors

Companies seek greater insight into what specific data and metrics investors are interested in, especially amidst the escalating complexity of core themes like climate, biodiversity, and human capital. Some companies have experienced a lack of consistency and tension from within the same investor institutions.

Understanding key focus areas amid the abundance of potential disclosures would help companies in prioritising. Companies expressed a desire to focus on meaningful data that informs better decision making and which is also strategic internally. However, they also expressed concerns about possibly not meeting all investors' needs.

Overall, companies accept disclosure and regulation as necessary. They emphasise the importance of identifying material ESG issues and linking metrics to strategy, remuneration and financial statements. However, there's an overarching concern that with excessive requirements there was a risk of diverting from meaningful decision-useful data to compliance, hindering innovation and progress. Companies hope that the focus on the interoperability between reporting frameworks and standards will enable consistency and reduce the burden on preparers, and help address the volume of ad hoc requests they receive from investors.

> **"If I'm spending all my time on reporting the numbers, then I don't have time to actually act on the numbers."**
>
> *- Chief Sustainability Officer, FTSE100*

Managing Third Party Data Providers

There were mixed views on the external ratings, agencies and data providers among the companies. While all companies acknowledge that investors use research to varying extents, they face challenges in interpreting different criteria and ranking systems used by various providers. They recognise the importance of actively participating in the market disclosures but would like clearer guidance from investors on which disclosures hold the most value.

Companies would prefer to engage directly with investors to provide them the accurate and reliable information that

What Companies Think

KEY CHALLENGES

they need. While they understand the role of external providers, experiences with ratings agencies and data providers vary. Some companies have had positive engagements, to verify and contextualise data, while others have found the experience less favourable. In response to increasing burden, diminishing resources, many companies have streamlined their focus to include only CDP, MSCI, Sustainalytics, and Ecovadis when relevant for their sector.

> *"We've got different viewpoints on how investors use ESG ratings output, and how they feed this into their in-house analysis."*
> *- Sustainability Reporting Director, FTSE100*

Understanding Investors' Preferred Methods for Accessing Information

Companies shared the challenge they face in providing information to investors. Understanding the diverse preferences of investors regarding formats, methods, and channels to access information is a primary concern. Companies are struggling to navigate the varied preferences of investors, who may prefer detailed reports, concise summaries, or interactive presentations. Additionally, the complexity and sheer quantity of information needing to be communicated in a clear and understandable manner poses difficulties. Many companies feel frustrated that, despite providing detailed information, investors may not be reading their materials. They are uncertain about the most effective way to ensure that their messages resonate with investors. Companies are also aware that they must adapt to technological advancements, which offer a wide array of communication channels, including traditional reports, online platforms, digital tagging and social media. Meeting regulatory requirements while ensuring transparency and clarity further adds to the complexity.

> *"How do we produce this much information in the best format we can with minimal effort?"*
> *- Chief Sustainability Officer, FTSE100*

What Companies Think

WHAT DO INVESTORS DO WELL?

Overall

- Companies value when investors are clear on issues and support companies to test, learn, and make progress and appreciate when investors understand that solving challenges overnight isn't realistic and they emphasise a gradual process of improvement and adaptation.
- Investors that move beyond short-term returns and engage in a deeper dialogue that involves understanding a company's long-term vision, its strategies for navigating sustainability challenges, and the integration of ESG considerations into core business practices.
- Open and clear dialogue, where both corporates and investors acknowledge the dynamic nature of sustainability challenges, share insights and commitment to learning and adapting.
- Investors who set the tone of a conversation by providing context for their data requests make a significant impact. For instance, they may explain that in order to retain companies in their fund, they require specific information to meet reporting and labelling requirements. This transparency helps companies understand the importance and urgency behind the requests.
- Companies value investors that engage meaningfully, seeking data points that truly help understand the business, focusing on quality over quantity.

Specific to this Dialogue

- Some institutions openly communicate to companies the external ratings, agencies, and data providers they value, along with how this information feeds into their proprietary systems. Some institutions provide an online database which shows companies information about the metrics they use and how companies are assessed.
- Investors who invest time in reviewing a company's key materials and familiarise themselves with key issues are highly valued. This allows discussions to move beyond superficial information gathering to meaningful engagement focused on addressing real issues.

What Investors Think

KEY CHALLENGES

Balancing Client Demands and Demonstrating Comprehensive Consideration of All Issues

Investors face several challenges in their roles, including managing the diverse demands of their own clients and demonstrating that all issues have been thoroughly considered. With asset owners having varied stewardship priorities, investors often grapple with the need to stand out while attempting to reach consensus on focal points. Additionally, simplifying information poses a significant hurdle as investors contend with time constraints and the inundation of data. Balancing the need for comprehensive insights with the limitations of time necessitates strategies to streamline information effectively.

"Investors have a hugely diverse range of stewardship priorities, and 'being different' can be a USP, so companies are unlikely to get an agreement on the few things they should focus on."

- Stewardship Director, Global Investment Manager

Effectively Managing Time Amidst an Abundance of Information

Investors encounter the huge challenge of navigating information to address their time constraints amidst an overflow of data. With a deluge of information available, investors must sift through vast quantities of data to extract pertinent insights efficiently.

Investors stressed the importance of companies being clear about their key issues and prioritising their communication efforts. They advise companies not to attempt to address every possible concern but rather to focus on what truly matters. According to investors, information provided by companies should be firmly anchored in their business and strategy. This approach ensures that sustainability initiatives are closely aligned with core objectives, enabling investors to better understand and evaluate a company's sustainability efforts within the broader context of its strategy and performance.

"Companies need to be more rigorous in saying these are the ESG priorities. Companies have got too caught up in the idea that they need to be all things to all people. They need more of a grip on their own agenda – need to be much clearer themselves as to what the key issues are."

- Sustainability Reporting Director, FTSE100

Investors are aware that the complexity of various reports, sustainability metrics, and industry analyses further compounds this challenge. Consistency in data is the most important thing. Giving the same data in different reports is imperative. Effectively distilling complex information into concise, digestible formats with clear linkages and cross referencing is helpful for investors to make informed decisions within limited timeframes. When companies are meeting reporting requirements or adhering to frameworks and standards such as SASB, it is helpful to cross reference information in reporting for clarity and accuracy. Streamlining information not only enhances comprehension but also facilitates quicker analysis and decision-making processes, enabling investors to navigate the dynamic financial landscape with agility and precision.

What Investors Think

WHAT DO COMPANIES DO WELL?

Overall

- Companies that prioritise clear communication and proactive engagement in favourable conditions build stronger trust and confidence among investors, laying a robust foundation for enduring relationships.
- Streamlining reporting and communications to present a summary investment case, value drivers, and key differentiators in a clear and accessible manner at each interaction helps investors' understanding amidst the information overload.
- Investors appreciate when corporates assist in balancing short-term trading updates with the broader context of the business. Including strategy, business model insights, and historical data in quarterly presentations, often available in an appendix, enhances transparency and investor understanding.
- Companies that emphasise their sustainability angle in initial meetings, highlighting their company thesis, strategy, and business model. A CEO's strong emphasis on sustainability signals genuine commitment, serving as a green flag for investors.
- Maintaining consistency in data across all reports and communication so that investors receive a cohesive and consistent story, builds credibility and trust and reliability in reporting practices.
- Best practice for companies is to centralise all relevant information in one easily accessible location on their website, typically within the investors section. This centralised hub could include clear descriptions of the contents of each report to guide investors effectively.
- Cross-referencing tables to commonly used frameworks such as CSRD, SASB, and GRI can enhance transparency and ensure that investors understand the company's intentions regarding sustainability reporting.

What Companies & Investors Think

SHARED CHALLENGES

Focusing on Materiality With Evolving Investor Expectations

One of the key challenges for both investors and companies was determination of materiality in the context of sustainability issues. For companies focusing on material issues helps them to effectively allocate resources, streamline reporting efforts and address the key concerns of investors and other stakeholders. This in turn helps investors better understand companies. However, this is often complicated by the presence of differing reporting standards, regulation and client expectations which can obscure clarity and consistency.

> ***"We are getting hit by an alphabet soup of regulation, all with different materiality thresholds."***
>
> *- Chief Sustainability Officer, FTSE100*

All of the companies involved had a clear idea of the material issues for their business, which were integrated into their strategic pillars of the business and their valuation creation story. All emphasised that they focus on prioritising this in their communication and reporting. (Note: not all companies are that advanced, but the participants in this dialogue were very established.)

Companies understood the dynamic nature of materiality and the need to be refreshing and reviewing materiality assessments on a regular basis. Interestingly, all companies also shared that they were undertaking a 'double materiality' approach this year to understand more clearly the externalities of their business and prepare for better understanding of their stakeholders and impact as well as upcoming mandatory requirements of CSRD.

In addition, all participants shared that their director remuneration was linked to ESG metrics in some way – either short- or long-term plans. There was an appreciation that it was still a small percentage of overall target (30% or less), but a helpful one to align the business objectives and strategy. Many companies were also looking across their organisations to develop relevant sustainability linked performance targets for all levels across the organisation. It's still early to determine whether this is in response to investor expectations and/or if it's effectively changing behaviours and driving real-world change.

Investors acknowledge that materiality evolves over time, often influenced by media coverage, legislation changes, or global commitments, and should always align with a company's strategy and value creation narrative. While SASB is considered a valuable starting point for materiality assessment, investors advocate for companies to conduct their own evaluations rather than relying solely on standardised versions. Identifying issues as material signifies an understanding of their impact, a willingness to address them, and a commitment of resources, indicating a serious approach to sustainability.

Investors also highlight the necessity for investor relations to comprehend materiality matrices, understanding the rationale behind identified issues and their implications.

> ***"We understand companies can't measure everything that matters in pure data. But having a measure shows awareness, and a way for progress to be tracked."***
>
> *- Portfolio Manager, Asset Manager*

Investors recognise the limitations of measuring every relevant aspect solely through data but stress the importance of demonstrating awareness and tracking progress. However, they expect companies to be able to articulate the return impact of their sustainability initiatives. Challenges arise when discrepancies occur between material issues highlighted in sustainability reports and those identified as principal risks in regulatory filings. Finally, while companies may define their material issues, investors

What Companies & Investors Think

SHARED CHALLENGES

stress the importance of engaging on areas they identify, which may represent blind spots or systemic concerns for the company.

> ***Identifying an issue as being material shows the company understand the impact, has a willingness to commit resources to address them, and takes it seriously."***
>
> *- Investment Analyst, Asset Manager*

Addressing Data Quality, Standardisation and Assurance

Corporates want information to be as accurate as possible and increasingly acknowledge the necessity of external assurance for sustainability data. They emphasise that assurance for this data may differ significantly from financial assurance due to its evolving nature and lack of clarity. The complexity and the maturity of sustainability metrics further complicates matters, with carbon-related metrics benefiting from established protocols while other areas, such as biodiversity, lack consistency in measurement. Bridging the gap between internal tracking and external disclosure, alongside determining materiality, remains a crucial challenge. Some corporates noted the challenge posed by this uncertainty for both management teams and investors.

In practice, the audit committee typically oversees assurance efforts, often engaging audit firms for limited assurance, with the audit committee ultimately signing off on the results. However, there is a notable lack of clarity surrounding the mechanics of assurance processes, compounded by confusion regarding the role of major auditing firms. Corporates also recognise the substantial task of upskilling internal teams and audit committees to comprehend data intricacies, as they may not be accustomed or comfortable with such levels of assumption. Companies recognise there is significant work to be done in this evolving area.

> ***The challenge is people feeling comfortable with the unknown, if they don't have the exact number. A lot of this is estimated data. As we learn more, data quality will improve and people will get more sophisticated in their understanding."***
>
> *- Director of Sustainable Business, FTSE100*

Investors have sympathy with the difficulties associated with auditing non-financial information but do expect that over time, such data will attain a level of assurance equivalent to financial data. There is agreement on the importance of consistency and standardisation across data metrics. Data providers are recognised for their pivotal role in data aggregation, with many investors relying on these systems as primary sources. In addition, there is anticipation about the potential of AI to enhance data processing capabilities in the future.

Some investors caution against unrealistic expectations regarding the assurance process for non-financial information, emphasising its inherent differences from financial data assurance. They highlight the value of narrative reporting in providing insights into risk management attitudes and long-term perspectives. There is a desire for concise reporting formats that focus solely on the most material issues, incorporating case studies, data, and narratives for clarity.

> ***We start with the assumption that the data is correct. Lack of validation is not end of the world. Keep consistent measurement principles and disclose assumptions. At some point, we will want the data audited, but we don't want to encourage this now if it's too difficult."***
>
> *- Socially Responsible Investment Analyst, Investment Manager*

What Companies & Investors Think

SHARED CHALLENGES

There's a recognition that while initial assumptions about data accuracy are made, lack of validation isn't catastrophic, as long as consistent measurement principles and disclosure of assumptions are maintained. Investors also acknowledge the imperfections in ESG data scores from external agencies but find them valuable as starting points for analysis. Ensuring consistency in data remains a top priority, as different information across various reports undermines investor trust.

Navigating the Regulatory Maze

Adapting to evolving landscapes while maintaining compliance poses a shared challenge for both corporates and investors. Corporates recognise there is becoming a much more codified sense of disclosure with all the changes in regulation, legislation and the adoption of reporting standards. They anticipate that quality will improve over time but acknowledge the need to absorb the changes efficiently. There is a desire for a more practical and pragmatic approach to company disclosures and they are hopeful that this will provide a level playing field for that more useful discussion. Companies anticipate investors may emphasis compliance with standards like CSRD (Corporate Sustainability Reporting Directive) and ISSB (International Sustainability Standards Board), viewing these as benchmarks for ESG reporting. Companies seek clarity from investors regarding their preferences on global regulations and standards that they endorse for sustainability reporting and compliance.

> ***"The reporting landscape is completely overwhelming. We'd like to understand whether investors are supportive of more regulation and what other things will be important in the future – nature?"***
>
> *- Head of Rating Agency Relations, FTSE100*

Investors also expressed anticipation for the ISSB and the CSRD acknowledging the anticipated rigour and structure these standards may bring to sustainability reporting. They see benefits in the associated taxonomies in facilitating consistent and comparable reporting across companies and industries. However, they also admitted uncertainty about how they would utilise the abundance of new data points generated by these regulations. Despite this uncertainty, investors are generally supportive of efforts to enhance regulatory and compliance frameworks in the sustainability reporting landscape.

> ***"We will want to see taxonomy aligned revenue."***
>
> *- Investment Analyst, Asset Manager*

What Companies & Investors Think

WHAT DO COMPANIES AND INVESTORS DO WELL?

Companies

Overarching

- When companies prioritise clarity and transparency regarding their material issues and connect them to their overall strategy instead of solely focusing on compliance-driven reporting, it demonstrates a deeper understanding and confidence in their operations.
- When companies clearly demonstrate that ESG matters are fully endorsed by the CEO and the board, it sends a strong signal to investors regarding integration into the company's strategy and operations. This integration and commitment to transparency is reinforced when linked to remuneration practices and when substantial changes in sustainability targets are treated with the same gravity as financial target adjustments. Demonstrating awareness and understanding of the return impact of sustainability initiatives strengthens credibility.
- When companies connect and synthesise their reporting and communications in a strategically driven manner, integrating the importance of sustainability issues with financial performance, it results in consistent and coherent messaging that is more easily accessible.
- When companies provide access to sustainability specialists for both investors and themselves, it facilitates deeper conversations that lead to a comprehensive understanding of broader business and strategic aspects. This collaborative approach helps to focus on the holistic integration of sustainability into the company's operations and strategy, enhancing understanding and trust and mutual learning between investors and companies.

Specific to this dialogue

- Companies that focus on consistency and standardisation across sustainability metrics, with clear measurement principles and disclosure of assumptions help investors understand reliability and comparability.
- Investors appreciate companies increasing acknowledgement of the necessity of external assurance for sustainability data and value when companies that remain adaptable and committed to learning and improving in this evolving area.
- Companies that anticipate and adapt to changing regulatory and reporting landscapes with a practical approach to disclosures and seek clarity on investor preferences foster greater alignment and understanding.
- When companies invest effort in understanding investors' objectives, including diverse client demands and internal policies a more effective dialogue will result. Understanding whether investors are focusing on systemic risks or specific company issues and their underlying motivations and request will ensure that information and actions are tailored.

What Companies & Investors Think

WHAT DO COMPANIES AND INVESTORS DO WELL?

Investors

Overarching

- When companies sense that an investor is genuinely 'invested in the management team', fostering constructive conversations even during challenging times, a strong sense of support and trust emerges. This supportive dynamic allows for more open dialogue and enables the business to make informed and longer-term decisions.
- When investors act as effective 'non-executives', companies find themselves engaged in broader, more meaningful strategic dialogues. This engagement allows for a deeper understanding of each other's perspectives and long-term considerations for the company, fostering a relationship built on mutual learning and shared strategic vision.
- Providing clear messaging and reinforcement that it's acceptable to prioritise three or four issues relevant to their business, rather than attempting to cater to every stakeholder's demands. This targeted focus allows companies to streamline their efforts and allocate resources more effectively, fostering a strategic alignment with their core objectives.
- When investors delve beyond the surface-level data and invest time in understanding the nuances behind the numbers, it signals a productive relationship. For instance, shifting the focus from generic metrics like 'number of women on the board' to exploring the dynamics and operations of the board reflects a commitment to understanding the intricacies of the company's governance and decision-making processes.

Specific to this dialogue

- When investors recognise the evolving nature of sustainability standards and acknowledge the infancy of data and reporting in some areas it gives companies confidence to continually learn, develop and refine approaches.

Actions for Companies & Investors

TOP TIPS FOR COMPANIES

- Not every business needs to be the best at ESG; focus should align with the company's core values and mission and show progress over time.
- Understand the materiality of issues within your company and use this understanding proactively to address regulatory requirements. Align reporting efforts with strategic objectives to ensure coherence and relevance.
- Be bold in crafting and owning your narrative, emphasising your unique value proposition and sustainability journey.
- Communicate with straightforwardness and authenticity in all interactions to build trust and credibility.
- Avoid unnecessary complexity in reporting by providing clear summaries and linkages and present information in various formats tailored to the needs of different investors.
- Clearly articulate the reporting frameworks and standards used, explaining the rationale behind their selection.
- Be selective in responding to surveys and data requests, ensuring alignment with your narrative and strategic priorities.
- Understand the diverse needs of different investors and how they utilise data and reporting. Be aware of the pressure and influence of different asset owners' mandates on asset managers.
- Tailor your communication and reporting strategies to effectively meet different needs.

Actions for Companies & Investors

TOP TIPS FOR INVESTORS

- Encourage internally joined-up meetings with both ESG specialists and portfolio managers when discussing key issues.
- Collaborate with other like-minded investors on key issues to amplify the collective voice and influence. By pooling resources and expertise when relevant, investors could enhance their effectiveness on some issues.
- Encourage companies to streamline efforts and allocate resources effectively, aligning with core objectives and strategic focus.
- Invest time in understanding the nuances behind the numbers and metrics presented by companies. Read the reports that are produced.
- Provide clarity on your key issues of interest.
- Help promote consistency of demands on companies from involvement in collaborative initiatives such as IIGCC.
- Provide greater clarity on how you use raters, rankers and data internally, and use some professional scepticism when consuming their research on complex areas.
- Share commitments and preferences to reporting standards, metrics and frameworks.

GOVERNANCE & VOTING DIALOGUE:

The Role of Shareholder Voting in Stewardship

Issues frequently arise with the mechanics of voting, the role of proxy agents and the interpretation of voting signals. There is a need for greater clarity on the roles of different actors in the system – from investors to corporates and proxy advisers – and a need to reduce friction in order to enable an effective exchange of views.

The question that we set out to address in this dialogue:

> ***How can we refine the framework to ensure timely, accurate, and transparent corporate information, fostering investor and corporate confidence?***

Governance & Voting
Dialogue Contents

Highlights of this Dialogue

GOVERNANCE AND VOTING

What Is the Key Principle?

Consistency emerges as a crucial theme in this dialogue. Both investors and companies seek to establish consistency in the voting process, emphasising the need for more uniformity in interpretation, execution and feedback. The dialogue also considered the sources of friction and a range of frustrations with the current system.

What Did We Discover?

- **Positive Dialogue:** Investors generally expressed positive sentiments about the dialogue with corporates in the UK market. They recognised value in transparency and governance practices, distinguishing the UK from other markets. However, there was acknowledgment that improvements can be made to enhance the dialogue, as corporate experiences with investors were less positive. The increasing impact of the evolving relationship of asset managers with their clients – asset owners – would need to be considered.
- **Remuneration Simplification:** Unsurprisingly, investors advocated for a simplification of remuneration packages, with a unanimous message underscoring the necessity for clarity in this domain. Their emphasis was not solely on the reduction of complexity but also on aligning compensation structures with performance metrics and strategy. There was a broad concern within the investment community about the efficacy and transparency of executive pay structures.
- **Strategic Engagement for Tangible Outcomes:** It was agreed by all that efforts were needed to focus on the purpose of engagement, moving beyond engagement for its own sake. The emphasis should be on enhancing value and ensuring tangible outcomes. Increased effectiveness in engagement may involve a wider range of approaches by companies and perhaps even a reduction in the frequency of interactions, allowing a shift towards more profound discussions on topics such as social and environmental issues, where a deeper understanding from both parties will be essential to achieve meaningful results.
- **Perception Gap:** For companies there is an issue of contention on governance professionals and investment teams being joined up. Investors are adamant there is clear coordination and almost all asset managers have publicly available voting policies and decisions rarely deviate without formal input by the investment team. While asset managers strive for consistency, there is scope for misunderstanding after early soundings, particularly on remuneration issues. This perception gap is undermining trust and needs closing.

What's Next?

- The Investor Forum will monitor developments in the 2024 AGM season:
    - Our platform is available to help connect companies and investors to clarify issues and facilitate dialogue in advance of company AGM's;
    - We will convene investors and companies to reflect on lessons learned from the AGM season; and
    - We will work to create an Investor and Issuer Forum which will seek to address issues of systemic concern.

Overview of the Current Market Landscape

Conversations within the Company Secretariat, especially around voting, have traditionally been quite clear, but the landscape is undergoing significant changes with the emergence of climate and a broad range of ESG issues, increasing pressure on asset managers from asset owners, the emergence of pass-through voting and the role of proxy advisors, resulting in an ecosystem that is not very well understood.

Maturity: While the core conversation about voting is well established, the effectiveness of the dialogue can be enhanced and the system is facing major disruptions due to market changes, highlighting the need for proactive engagement.

Challenges and Opportunities: The evolving landscape presents challenges in ensuring clarity, but it also opens up opportunities to shape the dialogue around new voting mechanisms, technology advances and enhancing transparency in decision-making processes.

Access and Governance Are Strengths of the UK Market

Access to UK Boards is perceived as a significant advantage in the UK equity market. Numerous investors have highlighted favourable access to Boards, and individual Non-Executive Directors (NEDs), as a major positive in comparison to certain continental European markets, and US markets.

> *"Overall, the nature of the dialogue between companies and investors is very valuable and positive."*
>
> *- Head of ESG and Stewardship, Asset Owner*

Many recognised the positive nature of governance in the UK and the strength of frameworks such as the Corporate Governance Code and the Investment Association principles. These frameworks serve as comprehensive guidelines widely recognised by all parties.
There was acknowledgement that the Corporate Governance Code ensures that all actors in the market can rely on the same minimum standards. The commitment to these principles ensures not only strong governance standards but also elevated levels of transparency, distinguishing UK approach from practices seen in other markets.

> *"We think it kind of works pretty well and that's not to say we don't vote against things from time to time. But I think from our perspective, the system in the UK works."*
>
> *- Director Stewardship, Global Assets Manager*

Challenge however was noted in the layers upon layers of incremental change over the years, combined with the complex and overlapping, but not always co-ordinated, remits of the various regulators in the UK, which is felt to have enhanced complexity in the market.
The prevailing sentiment is that strong governance distinguishes the UK approach and provided it remains proportionate, can offer a competitive edge. It was emphasised that the focus needed to be on a 'force for good' and a 'race to the top not a race to the bottom' with overly burdensome and prescriptive regulation.

Many did however acknowledge that there would be different experiences on both sides, and that generalisations were not helpful given the diverse nature of both the investor and corporate participants. Depending what size and type of investor, there is likely a big difference in the access you have to big companies and companies experience different approaches from active and passive investors. Companies increasingly deal with proxy advisors and are concerned about the impact on direct engagement. There were also examples of intermediary hinderances – for example brokers and investment bankers which can hinder direct dialogue.

Although, the UK market was seen overall to have a culture of engagement and constructive dialogue between

Overview of the Current Market Landscape

corporates and investors, when it comes to pay, there is broad consensus that the current emphasis on pay has become a disproportionate focus, overshadowing other crucial discussions. Many investors referenced the heightened sensitivity on this topic in the UK.

> *Why do we have to spend so much time on remuneration? Why is it getting more complicated all the time?"*
>
> *- Head of ESG and Stewardship, Asset Owner*

It's recognised that redirecting attention to a more holistic range of topics is essential for a comprehensive understanding and effective decision-making dialogue.

Voting Against Risks Becoming a Sign of Good Stewardship

There is a need to shift the perception that voting against a company proposal represents good stewardship, accompanied by a caution against the detrimental impact of benchmarking asset managers' voting behaviours.

> *The idea that voting against is a sign of stewardship needs to change. Benchmarking asset managers' voting patterns is very harmful."*
>
> *- Senior Global ESG Manager, Asset Manager*

A focus on system-level voting is also on the rise, presenting unique challenges in how stewardship is perceived. This trend tends to favour policy-driven approaches over tailored, nuanced evaluations of individual companies.

With the vast number of resolutions, across potentially large numbers of companies, investors are confronted with a formidable task to execute votes. With the sheer volume of voting tasks, delivering bespoke voting decisions at the individual company level presents a significant challenge.

The challenge often lies in policies dictating votes, resulting in a disconnect from the essence of the individuals elected to the board or the proposals put forth. With the sheer volume of voting tasks, the core intentions may sometimes be overlooked. Depending on the decision-making process, investors may find themselves increasingly reliant on third-party assessments.

> *It's too simple to just focus on votes against."*
>
> *- Associate Director, Stewardship, Asset Manager*

There is an acknowledgment that investors and companies need to come together, listen to challenges, and work collaboratively towards solutions, to determine the most effective means of communication in this evolving environment.

Summary of market considerations to be acknowledged:

- Access to UK Boards is seen as a significant advantage.
- Strong governance in the UK is considered advantageous, offering a competitive edge if proportionate.
- While the UK market fosters a culture of engagement and constructive dialogue, there's a consensus that the current emphasis on pay overshadows other crucial discussions.
- There's a need to shift the perception that voting against evidences good stewardship.
- Collaboration between investors and companies is needed to address challenges and determine effective communication methods in this evolving landscape.

Voting & Governance Myths

Before delving into key challenges, what works well and actions, it's important to 'bust' some of the myths that we uncovered specific to this dialogue to help set a clear framework for a more productive dialogue.

Myth: Investors Blindly Follow Proxy Advisors' Advice

Reality: This is a misconception, the reality is much more complex. While proxy advisors wield substantial influence, particularly for asset managers with limited resources, it's important to note that not all investors unquestioningly follow their advice. Almost all asset managers have bespoke, publicly available, voting policies which provide guidelines for proxy agencies to follow when executing voting instructions. Asset Managers review voting outcomes and investigate any discrepancies from stated policies. Proxy advisors serve a valuable role in providing information, especially for investors facing time constraints and resource limitations. There are questions about the quality, accuracy and timeliness of proxy research and recommendations However for many asset managers, the reality involves a discerning approach that integrates insights from proxy advisors with considerations of the needs, preferences, goals, and strategies of the asset owners they represent.

Myth: Voting Against Is a Sign of Good Stewardship

Reality: No, this oversimplifies stewardship. Voting, being a binary measure, is just one facet. True stewardship goes beyond, emphasising active engagement, thoughtful dialogue, and collaboration focused on preserving and enhancing the value of entrusted assets. The intense focus on 'holding to account' often crowds out constructive dialogue that aligns interests. Effective stewardship involves a multifaceted approach that considers the broader spectrum of actions aimed at ensuring the sustainable growth and success of the invested assets.

Voting & Governance Myths

Myth: UK Investors Reject High Executive Pay

Reality: UK investors are not averse to recognising and rewarding excellence. Their apprehension, centres around compensating mediocrity. While acknowledging this, there is growing sentiment that the current approach to executive pay is overly complex. Investors wholeheartedly support executive pay structures linked to long-term performance and strategic alignment. The nuanced perspective of UK investors underscores the importance of linking remuneration to genuine merit and sustained value creation.

Myth: Extensive Engagement Around Remuneration Is Imperative

Reality: Over-engagement can yield a poor return on investment, fostering a perpetual cycle of tinkering that diminishes the effectiveness of each engagement. Investors frequently struggle to convey clear messages, and companies may find it challenging to extract actionable insights. This underscores the importance of steering away from excessive consultation and, instead, prioritising targeted and impactful interactions. Quality over quantity is key in remuneration discussions, ensuring that engagements are purposeful, focused, and capable of delivering clear, meaningful outcomes for both investors and companies.

What Companies Think

KEY CHALLENGES

Accessing Investors

The nature of engagement and dialogue has evolved over time, accompanied by changes in practicalities. Meetings are now more meticulously planned and are characterised by focused discussions with clear agendas centred around specific topics. Outcomes from these discussions are often recorded to evidence fulfilment of stewardship obligations. There is also an acknowledgement of the need for efficient information dissemination.

Another significant issue is the power and influence wielded by proxy advisors, coupled with the lengthy process required to challenge or understand investors' voting behaviours. Voting decisions are usually not taken until after the publication of reports from entities like ISS, which means that companies often only become aware of voting patterns very close to the AGM, making effective dialogue to address differing perspectives challenging.

Compounding this issue is the difficulty in explaining nuances to proxy advisors, often staffed with junior personnel. Investors heavily rely on proxy advisors due to resource constraints, which is an inevitability of the landscape. The limited ability of investors to engage with every company, especially with some considering investments in over 10,000 companies, makes it practically impossible to manage without external assistance.

> ***"We are voting 10,000 meetings a year. It's impossible, and unnecessary, to go through every full report and consider each resolution individually. ISS as our vendor applies our policies to the company AGMs."***
>
> *- Head of Stewardship, Global Asset Manager*

Understanding Where the Votes Are in the Voting Chain

Corporates have recognised the importance of establishing relationships beyond fund managers, extending to stewardship teams, to grasp their processes and information needs. Bringing these teams together has been helpful in resolving issues and effectively conveying corporate narratives.

> ***"We need to establish relationships with the people that vote the shares and understand what they look at, and how their process work."***
>
> *- Company Secretary, FTSE100*

Companies do not find it easy to understand the voting processes and decision-making dynamics of different investor institutions. Often, companies experience a notable disparity between conversations with portfolio managers, interactions with stewardship teams and final voting decisions. Companies often struggle to determine precisely where the votes are being cast within the voting chain. This presents a challenge for companies in understanding who the investment decision-makers are, and how the voting decisions are made. This challenge is compounded by the complexity and late nature of the process, especially during the compressed AGM season.

Investors believe that companies should be aware of the multifaceted nature of voting decisions (which often involve input from various internal stakeholders, including portfolio managers, analysts, and ESG specialists) and shouldn't expect spontaneous decisions. Companies find the decision-making process, and the many steps from early consultation through to the final voting decisions, challenging to navigate.

> ***"Companies shouldn't have the expectation that we'll be able to give a definitive answer on the day."***
>
> *- Associate Director Stewardship, Global Asset Manager*

What Companies Think

KEY CHALLENGES

For companies there is an issue of contention with governance professionals and investment teams being joined up. Investors are adamant that there is clear co-ordination. In practice governance and Investment teams will have differences of opinion. While asset managers strive for consistency, voting decisions are not taken until immediately before an AGM, which means there is scope for misunderstanding after early soundings, particularly on remuneration issues. This perception gap is undermining trust and needs closing. Ultimately almost all asset managers have publicly available voting policies, and it is extremely unlikely that a decision to deviate from a voting policy can be taken without formal input with the investment team

Many investors recognised the need to explain voting decisions more thoughtfully to both corporates and to clients. Best practice would be investors advising companies in advance how they are going to vote. In addition to comprehending the internal dynamics of individual institutional investors, there is the added challenge of understanding the broader framework of the asset owner and asset manager dynamic. Increased transparency would greatly facilitate navigating these complexities.

> **"*It's a challenge for us to understand the context within the investor organisation as well as within the context of the asset owner/ asset manager dynamic. More transparency would be helpful.*"**
>
> *- Group Company Secretary, FTSE50*

Many companies had set up governance road shows, to address these issues, which had been well received by investors.

What Companies Think

WHAT DO INVESTORS DO WELL?

Overall

- Corporate access teams within institutions were praised by companies for facilitating broader access and coordination with various parts of the organisation. Some of the bigger investors have set up corporate access desks, for both fund management and stewardship issues, which are seen to very effective and valuable.
- Some institutions openly tell companies exactly which of their funds hold their shares and who is responsible for the position, and this was cited as very helpful with targeting engagement efforts more effectively.
- A number of institutions put on 'reverse road' shows for companies, inviting them to hear more generally about their approach, structure, strategy, policies and key focus areas.

Specific to this Dialogue

- Investors that explain their voting process and decision-making more thoroughly and advise companies in advance how they are going to vote.

What Investors Think

KEY CHALLENGES

Simplifying Investor Interactions

Investors across the board express a common desire for simplified interactions when it comes to engaging with companies. There's a prevailing sentiment that companies tend to overlook the significant time constraints faced by investors amidst the deluge of information in today's landscape. With investors inundated by a vast array of data, reports, and communication from numerous companies vying for attention, it becomes challenging to allocate sufficient time to engage meaningfully with each company.

Many investors express frustration over the excessive consultation required each year, particularly concerning remuneration issues where there's a lack of clarity on what necessitates consultation. This often leads to poor returns on effort, encouraging unnecessary tinkering annually which is usually driven by remuneration consultants' recommendations.

> ***"Rem consultations provide a poor return on effort. Consultations encourage tinkering every year."***
>
> *- Head of Stewardship, Global Asset Manager*

Investors and companies alike recognise the need for guidance on which issues warrant consultation, streamlining the process and reducing unnecessary correspondence. Some investors propose that unless there are significant deviations from the remuneration policy, annual consultation should not be necessary, advocating for a more efficient approach aligned with policy renewal cycles, providing companies with a three-year window to act on approved policies, fostering confidence in decision-making processes.

> ***"If the rem policy has been approved, the company has a three year window to act on it and should have the confidence to do so."***
>
> *- Head of Stewardship, Global Asset Manager*

Optimising Engagement Timing

Optimising engagement timing is a multifaceted challenge for investors, as they strive to strike a delicate balance between engaging with companies only when necessary and satisfying company desires which are typically for more immediate interactions. Investors recognise the importance of engaging with companies at strategic times, after results, in advance of annual meetings or when significant developments occur. These engagements allow investors to gain insights into companies' performance, strategies, and governance practices, enabling informed decision-making regarding their investment portfolios. However, the challenge arises when investors face the pressure to engage more frequently.

> ***"There isn't necessarily an expectation to have regular dialogue throughout the year, because there is also respect that we would like to see management do their day jobs."***
>
> *- Head of Stewardship, Global Asset Manager*

Moreover, the challenge of optimising engagement timing is compounded by the diverse preferences and priorities of investors within an institution and across the market. Some investors may prioritise regular updates and face to face meetings, while others may prefer a more lighter touch approach to engagement.

What Investors Think

WHAT DO COMPANIES DO WELL?

Overall

- Companies that prioritise clear communication and proactive engagement in favourable conditions build strong trust and confidence among investors, laying a robust foundation for enduring relationships.
- Streamlining reporting and communications to present a summary investment case, value drivers, and key differentiators in a clear and accessible manner at each interaction helps investors' understanding amidst the information overload.
- Investors appreciate when corporates assist in balancing short-term trading updates with the broader context of the business. Including strategy, business model insights, and historical data in quarterly presentations, often available in an appendix, enhances transparency and investor understanding.

Specific to this Dialogue

- Companies that share their questions in advance of a meeting give investors the opportunity to reflect and discuss internally, leading to more productive and insightful discussions during engagements.
- Companies that proactively ask 'how do you make voting decisions?
- Investors prefer clear and concise outlines of key policy changes from companies.

What Companies & Investors Think

SHARED CHALLENGES

Managing Effective and Timely Engagement Efforts Whilst Balancing Time and Resources

Optimising engagement timing, especially around the AGM season, presents a multifaceted challenge for investors and companies alike. Early engagement is encouraged to allow investors time for internal consultation, yet the biggest challenge remains companies knowing when to engage with investors and when not to. Many investors feel inundated with requests for engagement on issues they perceive as unnecessary, consuming valuable time and effort. Moreover, engagement trends are shifting towards more automatic processes, sometimes overlooking the 'G' (governance) aspect, which is considered a hygiene factor, raising questions about where and how to make the most valuable use of everyone's time. This dynamic underscores the importance of strategic and purposeful engagement practices that balance the needs of investors and companies, particularly during critical periods such as the AGM season.

A number of companies seek consultation outside of the AGM season, particularly around remuneration, and even though well intentioned can present challenges. Initial off-season meetings with the Chair and Remco Chair to share thinking on policy changes, new remuneration proposals or broader strategic priorities are well received by investors and companies often take away 'warm fuzzy feelings'. However, sometimes by early spring, when actual voting decisions are taken, the world may have evolved, rendering previous discussions outdated. This evolution can create complications, as investors' initial feedback may no longer be valid. Consequently, the Company Secretary attempts to reconnect with investors, but this process can be cumbersome. Circumstances may have evolved, and investors may not have communicated updated perspectives. This lack of synchronisation often leads to misunderstandings, and surprises.

Despite its cumbersome nature, investors have expressed appreciation for early consultation, well ahead of the AGM season, and have indicated a desire for more companies to adopt it to mitigate surprises. That said, since actual voting decisions are not taken until the run up to the AGM, at the end of an early consultation process, it would be helpful for companies to provide a concise summary of the status of the consultation in an effort to avoid misinterpretation.

> ***"The problem is that investors don't give clear responses to consultations. As a result, Investors often feel they haven't been listened to and companies don't take away clear messages."***
>
> *- Company Secretary, FTSE100*

Investors emphasised the importance of differentiating between engaging on policy matters and having a clear conversation about expectations regarding votes and the remuneration report. Since investors won't have access to the details until March or April when outcomes for the past year are available, companies should aim to engage on any issues that may arise in the remuneration report.

Simplifying the Complexity of Remuneration

The overarching message from investors was that remuneration simplification is needed. Packages are too complex and driven by consultants. Call for companies to streamline and simplify their plans and reporting with an acknowledgement that this has grown over time and is stifling the ability of companies to perform.

In principle, investors are happy to pay for performance, but they will assess each company proposal at the time of the AGM and make voting decisions on a case-by-case basis.

What Companies & Investors Think

SHARED CHALLENGES

Over the years, more regulation has been added and investors have requested more information, more granular targets and more nuanced metrics and have contributed to what we see now as a hugely complex set of matrices for both bonus plans and long-term incentive plans. There is a feeling that we have lost sight of the core principles on executive pay which are recruit, retain, motivate, align.

> ***"We are not opposed to a fair reward, but there seems to be an issue with peer groups not being representative. There needs to be a link between remuneration, strategic execution and the impact on employees. Rarely do companies talk about key risk in Rem discussions."***
>
> *- Global Head of Equity Research, Global Asset Manager*

A few investors made the point that asset managers and asset owners look at different things when it comes to remuneration. Asset managers look at structure and incentives and want the executive team aligned with them, while asset owners may focus more on quantum and fair distribution.

> ***"More and more controls have been added – deferrals, clawblack and malus, downside only discretion, introduction of ESG metrics etc. There are so many restrictions that Exec pay can't deliver what it was designed to do."***
>
> *- Global Head of ESG Investments, Global Asset Manager*

Some investors expressed the feeling that the metrics for remuneration have expanded to a 'very long laundry list' of targets including personal targets and once they get measured, the sense from many investors is that the nature of the metrics makes it almost impossible not to get a payout.

> ***"Timing of engagement is important and can make a big difference. When companies are consulting on rem, we want to be involved in seeing the proposal at an early stage– so we have an opportunity to shape it in some way."***
>
> *- Associate Director Stewardship, International Asset Manager*

The challenges in navigating remuneration votes are a widespread source of concern and friction, especially when companies face differing preferences from investors on metrics such as Total Shareholder Return (TSR) versus alternative metrics.

> ***"If you look at the UK as an example, we have all the different elements to imply good governance around pay, and it kind of makes sense. But if you add all the component parts together, it's excessive and maybe too restrictive."***
>
> *- Associate Director, Stewardship, International Asset Manager*

What Companies & Investors Think

SHARED CHALLENGES

Given that remuneration policies may not satisfy every investor – some preferring TSR while others don't – it's crucial to understand investors' policies. Some companies have found that if an investor opposes use of a particular metric, engaging may prove futile.

Changing Asset Owner/Asset Manager Dynamic

Many asset managers expressed concerns about companies' lack of understanding regarding the demands and scrutiny placed on them by their clients, asset owners, and NGOs. Asset managers face significant pressure from asset owners to deliver strong returns on investment while also considering ESG factors. Asset owners, increasingly demand responsible and sustainable investment strategies that align with their values and risk management goals. This pressure often translates into asset managers exerting influence on companies to improve their ESG practices.

As asset owners increasingly mandate asset managers to demonstrate engagement outcomes, the pressure on asset managers has led to the evolution of engagement practices. This shift means that sometimes engagements can become issue-driven, rather than about the company itself and, sometimes, the focus can shift to outcomes that can be easily measured, such as voting patterns, letters written, or the number of engagements undertaken. These changes reflect the evolving expectations and priorities within the investment landscape.

> ***"One of challenges we face is how we can better communicate to companies that we are representing the interests of our clients, and our clients may have multiple different preferences dependent on their ESG-related objectives."***
>
> *- Head of Stewardship, Global Asset Manager*

This discord underscores the complexity inherent in balancing competing interests. Moreover, the imperative to demonstrate impact and outcomes through voting and engagement can sometimes clash with achieving optimal results for the company. While a company's practices may not always align with industry best practices, they may be reasonable within the company's unique circumstances.

> ***"The need to demonstrate impact and outcomes through voting and engagement can conflict with getting the right outcomes for the company. A company's practices might not align to what is considered best practice for the UK Code, but may be reasonable in the company circumstances."***
>
> *- Head of Corporate Governance, Global Asset Manager*

This divergence can create a breakdown in communication between asset managers and companies and can also exacerbate a divide between asset managers and asset owners. A positive approach centred around identifying common interests and fostering alignment is essential for effective engagement strategies, highlighting the importance of companies understanding the dynamics with asset owners.

> ***"There is often a challenge between what corporates want to cover, what clients want us to cover and what regulators want us to cover – these don't aways match!"***
>
> *- Head of Stewardship, Global Asset Manager*

In the future more asset owners might directly vote their holdings – so there will be a challenge for companies to understand voting patterns given much more fragmented voting outcomes, and potentially mixed messages. Companies will need to navigate the different parties

What Companies & Investors Think

SHARED CHALLENGES

who control the investment and the voting decisions with particular vigilance when facing contentious issues.

> ***Companies will need to understand that the underlying owner who retains the voting rights won't necessarily appear on their register – so they will need to be prepared to reach out to ensure that they are covering all the bases."***
>
> *- Corporate Governance and Voting Lead, Asset Owner*

> ***If Asset Owners take more control, we need to think what the repercussions might be."***
>
> *- Senior ESG Manager Global Asset Manager*

Balancing the Need for Broader ESG Information

The heightened focus on ESG criteria presents a significant challenge for companies, primarily because it may not always align with material issues pertinent to their operations. While companies acknowledge the importance of addressing ESG considerations, the challenge lies in determining which factors are truly material to their business and stakeholders. In some cases, the ESG priorities emphasised by asset managers may not directly correlate with the core challenges and opportunities faced by individual companies. Consequently, companies may find themselves diverting resources towards addressing ESG issues that are perceived as less relevant or impactful to their long-term sustainability and performance. Striking a balance between addressing ESG concerns and focusing on material issues requires careful strategic alignment and transparent communication between companies and their investors to ensure that efforts effectively contribute to sustainable value creation.

Navigating the Regulatory Maze

Navigating the regulatory maze presents a huge challenge for both investors and corporates given the intricate relationship within the value chain, spanning from supply chains to asset owners. This challenge is amplified by the need to adapt strategies and engagement approaches amid a fast-changing landscape of reporting requirements and evolving legislation on a global level, especially concerning ESG factors.

> ***Fundamentally, what we all want as employees, as perspective pensioners – we all want to ensure there's a vibrant economy in the UK, and that companies can be individual in their approach and not marked off against a checklist."***
>
> *- Company Secretary, FTSE100*

For corporates, compliance with a myriad of regulations, reporting standards, and disclosure requirements is paramount, while they focus on what is material and relevant to their business operations. Striking a balance between meeting regulatory obligations in different markets, maintaining business as usual, and pursuing strategic initiatives that drive long-term value creation is crucial. Many corporates express concern regarding the overreliance and emphasis on nascent ESG data by investors, which jeopardises a comprehensive understanding of business dynamics.

> ***The appropriate governance structure for companies that operate solely in the UK versus those that operate globally are likely to be different. We need to ensure that UK companies that operate globally are competitive in that context."***
>
> *- Company Secretary, FTSE100*

What Companies & Investors Think

SHARED CHALLENGES

Also, investors grapple with staying abreast of regulatory changes and assessing their implications on investment decisions. They must navigate complex regulatory frameworks and evolving legislation to make informed investment choices aligned with compliance requirements, risk tolerance, and investment objectives. Moreover, investors must consider how regulatory developments may influence corporate performance, governance practices, and overall investment viability of the companies they invest in, ensuring a holistic approach to value creation and risk management throughout the value chain.

The increasing emphasis on asset managers demonstrating outcomes as a form of stewardship in their reporting is posing challenges for companies. Companies are mindful of avoiding discussions that could lead to negative mentions in an investor's stewardship report. This aspect adds complexity to the engagement process. Case studies posed a significant challenge for companies. Many investors shared their intended case studies for approval with the companies in advance. Company secretaries have advised Chairs and RemCo chairs that clarity is essential if they wish to avoid certain topics being documented as case studies. However, case studies have emerged as a crucial method for investors to demonstrate engagement outcomes. As a result of the discussion, there was a consensus on the importance of understanding this dynamic. Participants emphasised the need for collaborative efforts to develop approaches that satisfy all parties involved.

What Companies & Investors Think

WHAT DO INVESTORS DO WELL?

- When companies sense that an investor is genuinely 'invested in the management team,' fostering constructive conversations even during challenging times, a strong sense of support and trust emerges. This supportive dynamic allows for open two-way dialogue and enables the business to make informed and long-term decisions.
- When investors act as effective 'non-executives', companies find themselves engaged in broader, more meaningful strategic dialogues. This engagement allows for a deeper understanding of each other's perspectives and long-term considerations for the company, fostering a relationship built on mutual learning and shared strategic vision.
- Clear messaging and reinforcement from shareholders that it is acceptable to prioritise three or four issues relevant to their business, rather than attempting to cater to every stakeholder's demands. This targeted focus allows companies to streamline their efforts and allocate resources more effectively, fostering a strategic alignment around the core objectives.

What Companies & Investors Think

WHAT DO COMPANIES DO WELL?

- When companies connect and synthesise their reporting and communications in a strategically driven manner, integrating the importance of sustainability issues with financial performance, it results in consistent and coherent messaging that is more easily accessible.
- When companies prioritise clarity and transparency regarding their material issues, and connect those issues to their overall strategy, rather than focus on compliance-driven reporting, it demonstrates a deep understanding and confidence in their operations.
- When companies clearly demonstrate that ESG matters are fully endorsed by the CEO and the board, it sends a strong signal to investors regarding integration into the company's strategy and operations. This integration and commitment to transparency is reinforced when linked to remuneration practices and when substantial changes in sustainability targets are treated with the same gravity as financial target adjustments.

Actions for Companies & Investors

TOP TIPS FOR COMPANIES

- Establish a feature on all corporate websites where investors interested in engaging with the company based on their holdings can easily sign up and be added to the distribution list. This centralised approach would mitigate the challenge investors often face in locating the appropriate person to engage with. All company secretaries would agree to maintain uniformity across their respective company websites, streamlining the engagement process for investors.
- Ensure broad consultation when implementing significant changes. Failure to do so may catch the rest of the market by surprise close to the AGM, leading to potential negative responses in voting outcome.
- Tailor engagement strategies by identifying preferred modes of communication with your investors, such as meetings, emails, or conference calls and agreeing on the frequency and timing of engagements to ensure mutual convenience and effectiveness.
- Determine the purpose of any meeting – information gathering or investment decision-making.
- Set clear agendas for all meetings and establish clarity on the attendees and their roles/interests.
- Encourage investors to share questions or topics of interest before the meeting to maximise effectiveness and address specific concerns.
- Build in 5-10 minutes at the end of each meeting for direct feedback from investors.
- Understand the specific information needs of the investor, whether it's financial performance updates, strategic insights, sustainability issues or governance practices and investor expectations in terms of attendee.
- Tailor communications to meet the needs of your different audiences – credit, equity, ESG – as each has different interests and priorities, investment strategies, risk appetite, and long-term goals.
- Communicate with straightforwardness and authenticity in all interactions to build trust and credibility.
- Understand the materiality of issues within your company and use this understanding proactively to address regulatory requirements.
- Align reporting efforts with strategic objectives to ensure coherence and relevance.
- Understand the diverse needs of different investors and how they utilise data and reporting. Be aware of the pressure and influence of different asset owners mandates on asset managers.
- Tailor your communication and reporting strategies to effectively meet different needs.

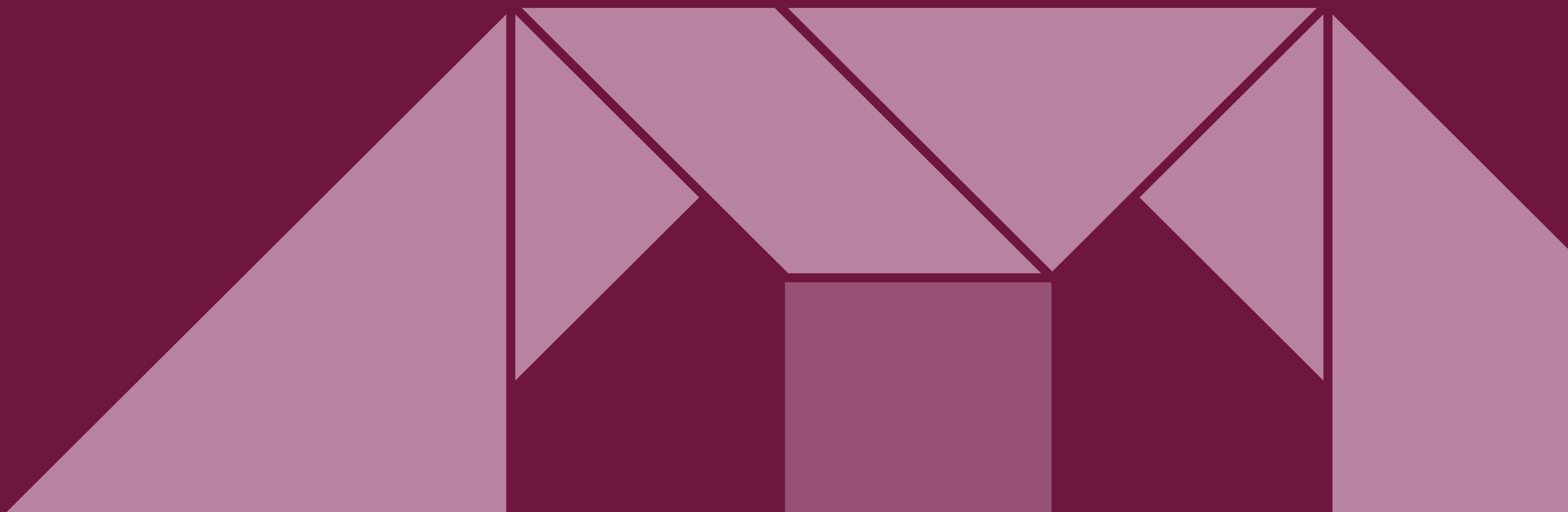
Actions for Companies & Investors

TOP TIPS FOR INVESTORS

- Create one-page expectation documents focusing on specific issues, complementing lengthy stewardship reports. These succinct documents would highlight the most significant topics of interest, ensuring clarity and accessibility for companies.
- Create and monitor a centralised contact@ email to enable companies to make direct contact.
- Consider setting up corporate access desks to facilitate broader access and coordination across organisation.
- Create fact sheets on investment organisation. Including voting policies.
- Consider providing greater transparency to companies on which funds are invested in the company, and which are passive.
- Encourage internally joined up meetings with governance specialists and portfolio managers, and where appropriate fixed income investors, when discussing key issues.
- Instigate reverse road shows to explain structure, approach and key focus areas (e.g. leverage Stewardship reporting).
- Collaborate with other like-minded investors on key issues to amplify the collective voice and influence. By pooling resources and expertise when relevant, investors can enhance their effectiveness on some issues.
- Reinforce the acceptance of prioritising three or four issues relevant to the company's business.
- Encourage companies to streamline efforts and allocate resources effectively, aligning with core objectives and strategic focus.
- Invest time in understanding the nuances behind the numbers and metrics presented by companies.
- Provide clarity on your key issues of interest.
- Join up thinking internally between fund managers and stewardship teams.

AUDIT & ASSURANCE DIALOGUE:

Ensuring Robust & Reliable Information for All Stakeholders



Investors seek robust safeguards to ensure the accuracy and transparency of a company's corporate information. Although much of the broader governance reform agenda has been retracted, revisions to the UK Corporate Governance Code on audit, risk and internal controls remain and there is still a need to ensure an effective corporate/investor dialogue on audit and assurance.

The question that we set out to address in this dialogue:

> ***How can we establish a robust framework that instils confidence in the reliability and accuracy of corporate information, benefiting both investors and corporates alike?***

Audit & Assurance
Dialogue Contents

Highlights of this Dialogue

AUDIT AND ASSURANCE

What Is the Key Principle?

Integrity emerged as the linchpin of this dialogue, underscoring its fundamental role in the audit and assurance processes. The discussion centred on how to ensure confidence in the reliability of corporate information through a better understanding of assurance and transparent high-quality dialogues to develop enduring trust for the benefit of investors and corporates.

What Did We Discover?

Educating Investors: As annual reports are long and complex. the roundtable emphasised the value of proactively providing investors with deeper insights into the responsibilities undertaken by Audit Committees and their Chairs. A focused programme would enrich investors' existing knowledge and address key investor issues to foster a more nuanced and comprehensive understanding of these critical functions.

Building Investor Confidence: It was felt that success in illuminating the roles and functions of Audit Committees could set the stage for heightened investor confidence. If actions can be taken to build a shared and comprehensive understanding, investors will be better equipped to assess the value and reliability of audit and assurance processes, establishing a solid foundation for meaningful conversations when needed.

Promoting Quality Dialogues: The desired outcome is not just informed investors but the initiation of high-quality corporate/investor conversations, as wanted and needed. Audit Committee Chairs are open to being readily available to be held to account, but neither investors nor companies see value in simply adding yet one more round of meetings to already crowded agendas. The focus should be to ensure that dialogues are substantive, meaningful, necessary and relevant, not simply routine.

What's Next?

- Confirming investors' confidence in Audit Committee Chairs to represent their interests and recognise their openness to discussions and communication sets the stage for mutual understanding. This paves the way for increased collaboration and effective oversight.
- Further collaboration to enhance investor education regarding audit and assurance best practices and the audit committee's oversight of those.
- There is a clear need to proactively build relationships to enhance understanding and come together to discuss significant issues. By establishing dialogue, relationships can strengthen, ensuring a solid foundation for collaboration when needed. An established dialogue can serve as a crucial transmission mechanism that has been lacking in the investor-company relationship.
- Opportunity for collaboration on ESG reporting and how it impacts financials, audit and assurance: For example by establishing a working group comprising investors, Audit Committee Chairs and key sustainability representatives to navigate uncertainty and change, developing mutually beneficial approaches.

Overview of the Current Market Landscape

The dialogue with Audit Committee Chairs is much less established than other stakeholder dialogues. With increasing focus from regulators and wider stakeholders there is a need for further development and understanding in this relationship.

Maturity: There is a recognised gap in the maturity of this dialogue, indicating the potential for substantial improvements in communication and collaboration between investors and audit committees.

Challenges and Opportunities: The under-established nature of this dialogue presents challenges in terms of building understanding, but it also offers significant opportunities to enhance transparency, align expectations, and foster trust in financial and non-financial reporting processes, audit and assurance.

Audit committees face increasing challenges to achieving high-quality information amid a landscape of escalating regulatory demands. Collaboration between Audit Committee Chairs and investors is critical to ensure that the output meets the expectations and requirements of investors and other stakeholders, especially regarding understanding the impact of ESG reporting and sustainability matters on the financials. This requires efficient solutions and alignment of interests amidst regulatory revisions and evolving governance standards.

Both investors and companies widely acknowledge the critical role of audit in fostering trust within capital markets, serving the public interest, and maintaining confidence in the reliability of corporate information.

> ***"From my perspective, the role of audit is about promoting trust within capital markets and serving the public interests. There is no doubt about that, and I think investors and corporates all agree on its importance."***
>
> *- VP Responsible Investment, Asset Manager*

The relationship between Audit Committee Chairs and investors exists within a dynamic market landscape characterised by evolving regulatory frameworks – including UK corporate governance and stewardship codes, changing investor expectations, and intense scrutiny of corporate governance practices.

It is important to consider the entire ecosystem and understand the objectives of stewardship, governance, and audit, how they intersect and complement each other. Clarifying the different roles and expectations associated with these processes lays the groundwork for more meaningful dialogue and collaboration. Currently, despite its importance, the dialogue between Audit Committee Chairs and investors remains underdeveloped compared to other stakeholder interactions.

However, a key challenge in the dialogue between Audit Committee Chairs and investors lies in determining the optimal level of communication and engagement. Neither investors nor companies necessarily require or seek regular communication, but efforts could be made to establish more open lines of communication, so that they are available for use when necessary. Audit Committee Chairs are eager for investors to better understand their role and are open to conversation.

From an investor perspective, while audit is acknowledged as vital, it doesn't receive daily attention due to a general trust in the audit process. Investors generally expressed satisfaction with the level of engagement with companies and indicated that engagement is preferred on an as-needed basis rather than a regular occurrence. Investors typically assume that the numbers presented in financial reports have undergone rigorous review and auditing, trusting in their accuracy and fairness.

However, this trust is not unconditional, as any lapses in audit quality can have significant consequences. Hence, investors often focus on the overall quality of the board, believing that a strong board will help ensure the delivery of effective audit processes. Despite the importance of audit,

Overview of the Current Market Landscape

particularly in relation to understanding a company's risk profile, unless specific concerns arise investors tend to focus time on areas that that are newer or less regulated. There is a valuable role in investment organisations for accounting specialists to work closely with portfolio managers to help them gain additional insights from audit committee reports and annual report disclosures.

> *"Investors as a whole do not engage with the issue of the audit, and with the audit committee, as much as they should do."*
>
> *- Senior Investment Manager, Asset Owner*

The relative under-establishment of this dialogue presents both challenges and opportunities. An interesting development which is driving knowledge and awareness is that many investors are expanding their knowledge and capabilities as they undergo the internal audit and assurance process for their own ESG and stewardship reporting.

So, while there may be initial hurdles in terms of building understanding, there are significant opportunities to strengthen transparency, align expectations, and build trust in financial and non-financial reporting processes, audit, and assurances of both companies and investors.

Key Takeaways

- The nature of dialogue between Audit Committee Chairs and investors requires deeper understanding. It's clear that engaging in dialogue surpasses a desire for more disclosures as it provides invaluable insights and perspectives inaccessible through disclosure alone.
- While audit is crucial, investors don't always focus on it given broad based trust in the process.
- The under-establishment of this dialogue presents opportunities for alignment and improvement.
- Clarifying roles and expectations can enhance dialogue and collaboration between the parties.
- While it is crucial to delineate the boundaries of this relationship, neither investors nor companies feel the necessity for regular dialogue but are seeking to establish stronger connections.

Audit & Assurance Myths

Before delving into key challenges, what works well and actions, it's important to 'bust' some of the myths that we uncovered specific to this dialogue to help set a clear framework for a more productive dialogue.

Myth: Investors Are Indifferent to the Audit and Assurance Processes

Reality: Investors operate under the assumption and trust that audit and assurance processes are conducted with precision and in compliance with rigorous standards. While they may not require a regular dialogue on audit matters, they are interested in maintaining an open line of communication, and are prepared to engage when necessary.

Myth: Audit Committee Chairs Are Reluctant To Engage With Investors

Reality: No, many Audit Committee Chairs recognise the importance of investor engagement. While investors may not feel the need for regular engagement, ensuring they have access when necessary is crucial. To further strengthen this connection, companies should proactively communicate the availability of Audit Committee Chairs for discussions. Additionally, there's an opportunity for companies to play a more active role in educating investors about key matters. Audit Committee Chairs take their responsibilities seriously, understanding that dialogue and transparency are pivotal for building trust.

Improving Understanding Between Companies & Investors

ESTABLISHING A FOUNDATION

In preparing for this roundtable, it became evident that the absence of an established dialogue between investors and Audit Committee Chairs underscored the significant benefits to be gained by investors hearing directly from Audit Committee Chairs about their roles and responsibilities. Recognising that trust and transparency underpin this relationship, taking time to delve into intricacies before moving forward was a crucial and valuable step.

In all four dialogues, one overarching theme is that companies and investors alike are overwhelmed by the influx of reporting requirements and requests, both compulsory and voluntary, which has escalated over the years due to expanding requirements and increasing stakeholder demands. Companies face challenges with resources and capability to deliver and investors face a mounting challenge of insufficient time to thoroughly review the abundance of information presented.

Audit Committee Chairs: Role and Responsibilities

The Audit Committee Chair is responsible for leading the activities of the audit committee and facilitating effective communication and collaboration among committee members, management, external auditors, and other stakeholders. The responsibilities of audit committees have been steadily increasing, necessitating a proactive approach to anticipate and understand forthcoming changes and challenges.

Typically, Audit Committee Chairs have long-established executive careers, combining technical expertise, leadership skills, industry knowledge, and professional conduct. They also fulfil the requirement for recent and relevant financial expertise, ensuring effective oversight and financial integrity within the organisation.

Audit Committee Chairs serve as independent non-executive directors on the board, bearing significant responsibilities in addition to chairing the audit committee. When there are new appointments, investors should scrutinise the selection of the Audit Committee Chair, their skills, experience, background, ensuring alignment with their expectations for robust challenge and oversight. If necessary, shareholders retain the right to vote against appointments that do not meet their standards. Upon appointment, Audit Committee Chairs seek trust and the latitude to effectively carry out their duties.

> **"Let us do our jobs, and show us a degree of trust, because you've appointed us to do it."**
>
> *- FTSE100 Audit Committee Chair*

Key Takeaway: Audit Committee Chairs are committed professionals with extensive experience and steadfast dedication, mindful of the best interests of shareholders in their roles.

Relationship Between Audit Committee Chair, Auditor and Management

The relationship between the Audit Committee, auditors, and management is critical in ensuring effective governance, transparency, and accountability within an organisation. Each party plays a distinct role in ensuring the integrity of corporate reporting and the effectiveness of internal controls.

The relationship between the Audit Partner, Finance Director, and the Audit Committee Chair was described as 'an equilateral triangle', where each party holds equal importance. Ensuring this balance demands proactive efforts

Improving Understanding Between Companies & Investors

ESTABLISHING A FOUNDATION

from Audit Committee Chairs to cultivate relationships rooted in trust and openness, facilitating effective collaboration and communications. It's crucial for Audit Committee Chairs to maintain the principle of "nose in, fingers out" to uphold independence and objectivity in their non-executive oversight role.

> *The Audit Committee Chair plays a significant role in fostering scepticism, a crucial aspect of the audit process. However, it's essential to recognise that audit oversight is a year-round endeavour. Building the right relationship between the Audit Committee Chair and CFO ensures that critical challenges are addressed, and judgment issues are debated, well in advance of the audit itself."*
>
> *- FTSE100 Audit Committee Chair*

Key Takeaway: The Audit Partner, Finance Director, and Audit Committee Chair form an 'equilateral triangle,' which the Audit Committee Chair balances, through independence and objectivity.

Overview of What Is Covered in the Audit Committee Report and the Auditors' Report

There is a significant amount of time taken in preparing the Audit Committee Report and the audit opinion. These are two separate documents that need to be read together to understand where assurance has been achieved and how internal controls have functioned. There's frustration about the effort invested in reporting, detailing risk identification, testing procedures, and challenges encountered – and if these reports fail to meet the needs of investors, they become considerably less useful.

A recurring theme discussed was the challenges associated with the annual report and accounts. Given the constraints of the written word and limited space, it's difficult to convey nuanced complexities without risking sounding overly dramatic or raising alarm bells, especially considering the key role of the auditor to 'challenge' .

> *There is only so much you are going to put in the annual report and accounts. It's difficult to capture the nuances of 'challenge' in a written document."*
>
> *- FTSE250 Audit Committee Chair*

Furthermore, it's an iterative process, making it hard to comprehend from an external perspective or accurately document in written form. Often, the report provides a general understanding, but for insight into the degree of challenge, engaging in conversation with the Audit Committee Chair could be valuable to shed light on the complexities of judgments, particularly regarding impairments and other significant matters.

Audit Committee Chairs acknowledge and recognise the challenges associated with reporting and would welcome engagement with investors to provide them with a better understanding of the processes involved.

> *I would encourage investors to really push for that line of communication with the Audit Committee Chair, because you are going to get a much better feel for whether someone is on top of something by having a conversation."*
>
> *- FTSE100 Audit Committee Chair*

Key Takeaway: To understand nuances in the annual report, investors are encouraged to reach out to Audit

Improving Understanding Between Companies & Investors

ESTABLISHING A FOUNDATION

Committee Chairs, who are open to discussing and clarifying any queries.

Key Factors in Determining Audit Quality

There are many factors that determine audit quality such as the competence and independence of auditors, the effectiveness of audit processes and procedures, adherence to professional standards and ethical guidelines, robust risk assessment methodologies, the rigour of audit documentation and evidence gathering, the thoroughness of internal control evaluations, and the clarity and accuracy of audit reporting. Adapting swiftly and effectively to changes in the regulatory environment, along with fostering collaboration between auditors, management and audit committees, is essential for ensuring high quality audits.

"What makes audit quality high or low is pretty simple. It comes down to processes and systems, areas where major firms like the Big Four are heavily investing, especially in technologies like AI, to automate audit elements. While machines can handle some tasks sensibly, they fall short in making effective judgments. Judgments require the expertise of someone who's done the job for 30 years, who can read a room of executive management. Non-executives bring their wide experience to bear in this regard."

- FTSE250 Audit Committee Chair

Well-planned audits involve the appropriate use of technology, led by experienced people with the right skills, the right level of engagement at the right time with the company and the ability to stand their ground and be brave on those occasions when they need to hold the line and exhibit moral courage on a particular treatment or issue.

These elements significantly enhance audit quality, and while they may seem straightforward individually, integrating them consistently and effectively is key. Investors, management, and non-executives all share responsibility in ensuring these elements converge to optimise audit outcomes.

Key Takeaway: Audit quality relies on a balance of process, technology and expertise with the challenge of consistently and effectively integrating them to produce high quality outcomes.

Better Understanding of How Auditors Have Challenged Management

Audit Committee Chairs play a crucial role in capturing and understanding how auditors have challenged management throughout the audit process, enabling them to provide effective oversight and support to auditors as needed. This is something that investors are confident that Audit Committee Chairs do, but they have little understanding of the extent of that challenge and how much time they have spent on engaging on specific issues and the detail of the challenge.

"The reporting should help us as investors get a better feel for how the audit committee satisfies itself that it was a high-quality audit, which did what it needed to do. I would like to be able to see some of that for myself."

- Senior Investment Manager, Asset Owner

This remains a difficult area to effectively capture and communicate within an

Improving Understanding Between Companies & Investors

ESTABLISHING A FOUNDATION

annual report. The Audit Committee Chair's responsibility is to help bring 'high-quality professional scepticism to the audit process. While every effort is made to convey the intricacies of this in reporting, the Audit Committee Chairs enthusiastically invite investors to engage in conversation. Through dialogue, investors can gain deeper insights and understanding, enabling them to grasp the nuances of the audit process more comprehensively.

Key Takeaway: The Audit Committee Chair's role is to encourage and support high-quality professional scepticism and challenge in the audit. While efforts are made to convey this complexity in reporting, they actively encourage investors to initiate discussions for deeper understanding.

Understanding the Wider Engagement the Audit Committee has within the Business

There is recognition by investors that the Audit Committee Chair is probably one of the busiest in terms of high commitment roles on a board because they must engage with the CFO, the external auditors, the finance function, as well as other parts of the business. There's an interest in understanding the wider engagement Audit Committee Chairs have within and across the business.

> ***"The thing I try to get an understanding of is how much an Audit Committee Chair and the audit committee as a whole get visibility within the firm, across all the different parts of the business."***
>
> *- VP Responsible Investment, Global Asset Manager*

Audit Committee Chairs often have regular one-on-one meetings with the CEO, CFO, CRO, CIO, heads of divisions, and other relevant stakeholders throughout the organisation. These interactions supplement those occurring during committee meetings. Additionally, many Audit Committee Chairs serve on other committees such as risk or sustainability, ensuring alignment across various governance functions.

A given for investors is 'making sure that the information is rigorous and right and accurate and reliable'. What's important to investors is that the board has the right management information to make the right strategic decisions.

> ***"It's hard to understand more about what the actual issue is with audit quality because that's quite a subjective thing. As an investor, I'm trying to understand how much an Audit Committee Chair is committed to get that issue resolved."***
>
> *- VP Responsible Investment, Global Asset Manager*

Key Takeaway: Audit Committee Chairs' engagement with the wider business is crucial for gaining insights into the organisation's operations, risk management practices, and financial health, all of which contributes to informed decision-making.

What Investors Think

WHAT DO COMPANIES DO WELL?

- Audit committees that go beyond narrow assurance. Having an ex-CFO on the committee is highly valued because of their ability to ask nuanced operational questions and challenge management from a unique perspective. Additionally, industry or sector-specific experience is considered beneficial.
- Investors emphasise the collective skill and experience of the committee members while ensuring that tenure is appropriately managed. There's a growing interest in whether Audit Committee Chairs have formal training and how auditors transfer their expertise to committee members. These factors contribute to investors' confidence in the audit committee's ability to provide robust oversight and maintain financial integrity.
- There is a growing demand to delve deeper into how investors have confidence, regarding audit committee engagement levels and audit quality, although such thorough engagement is unlikely to be necessary for every company every year.
- There's a call for companies to structure their annual reports effectively, with a focus on the story and alignment. Investors stress the importance of consistency throughout the year, aligning with the strategy for investment decision-making.
- Alignment between the front and the back end is becoming increasingly important, for issues such as climate change. Some investors compare closely the risk disclosures, the Audit Committee Chair's letter and the report and financial statements, to check for consistency.
- Graphs illustrating the level of risk appetite based on both impact and probability are helpful to investors. For enhanced understanding, companies could highlight the timing of shifts in risk appetite and the specific factors influencing the mindset of the audit committee or the board as a whole that drive such changes.
- Transparent audit quality indicators, including things such as: insights on audit engagement levels, showcasing the depth of involvement from auditors, details on the amount of time spent by mid-level auditors on the audit process, assessments of whether auditors consistently receive information in a timely manner.

What Companies & Investors Think

SHARED CHALLENGES

Addressing the Regulatory Landscape

Audit committees play a crucial role in advocating for the quality of information necessary for organisational transparency and accountability. It's essential for Audit Committee Chairs and investors to collaborate effectively to understand and align their interests, ensuring that the organisation delivers the necessary information to meet regulatory requirements and investor expectations.

This is particularly the case given that there is a sense that regulatory demands have been steadily increasing over the years, with new requirements continually added without any corresponding reductions elsewhere. While governance is essential, there's a need for a considered approach to maintain an effective work environment. The continual layering of regulations risks overwhelming individuals and organisations. With revisions to the corporate governance and stewardship codes it will be important for investors and companies to collaborate to come up with effective solutions.

Regulatory changes have unfolded rapidly creating uncertainty about the driving forces behind them and how to navigate interactions with different actors, government bodies and regulators in the UK. Initiatives like the Green Finance Initiative, Transition Plan Taskforce, and regulations for achieving Net Zero have evolved swiftly, placing the responsibility on companies to establish relevant processes, management and assurance mechanisms and investors are tasked with extracting key information and asking relevant questions, often with limited guidance or connectivity across the spectrum of regulatory changes.

As the market evolves and there's a demand for more non-financial data the question of greenwashing and evidence will become increasingly important. The imminent arrival of green taxonomies was referenced as a game changer. This will open up the debate about accountability and responsibility much more widely.

> **"*Audit committees are really important actors in helping to advocate for the quality of information that organisations need to deliver. And it would be helpful for both investors and companies to collaborate and align interests in navigating these challenges.*"**
>
> *- FTSE250 Audit Committee Chair*

Navigating the Evolving Nature of ESG/Narrative Reporting/Assurance

Some Audit Committees are dedicating more time to ESG and sustainability matters as these issues become increasingly prominent. The current landscape demands a significant allocation of committee time due to the complexity and abundance of nuances surrounding ESG reporting. Audit Committees are monitoring the evolving landscape to ensure that organisations are well-equipped to address these issues effectively. However, navigating this space poses challenges in discerning relevance and understanding the important aspects amidst the myriad of considerations.

Audit Committee Chairs recognise the importance and relevance of audit committees engaging with sustainability reporting, particularly regarding assurance. Practice tends to vary depending on the company's stage in its sustainability journey. Many Audit Committee Chairs also serve as members of the Sustainability or Risk Committees within their organisations to enhance understanding and connections. Looking ahead, cross-fertilisation between Board committees will be crucial to ensure a cohesive and integrated approach to sustainability reporting and oversight. There is unlikely to be any 'one size fits all' approach, the governance structure for oversight will depend on the organisation, the skills and expertise at the board level, and the maturity of the sustainability journey.

What Companies & Investors Think

SHARED CHALLENGES

"What will be essential is to ensure alignment between committees throughout the year rather than having a disjointed approach where an ESG committee handles data throughout the year and then shifts responsibility to the audit or risk committee once annually."

- FTSE100 Audit Committee Chair

As non-financial data becomes ever more important, the audit committee aims to ensure that processes and controls surrounding it are of the highest quality. Their expertise lies in applying rigorous financial skills to ensure completeness, consistency, and relevance in data and reporting and the ability to interpret complex standards. They emphasise the importance of these skills to provide the necessary challenge and the need for strong organisational structures, including the three lines of defence. It is also important to ensure that the management team possesses the appropriate skills.

"Unless you are applying the same kind of rigour, you have a set of accounts which is really robust with 100 years of control and process done by accountants and then some flaky stuff done by people who've never had a background in internal control."

- FTSE100 Audit Committee Chair

Investors see ESG as an integral part of a company's DNA and suggested that this should be considered at the strategic board level. Investors were open about ESG reporting oversight, not feeling it needs to be the sole responsibility of the audit committee. It was seen to be what's best for the company, because they all have different risks and issues. What was emphasised is the importance of clarity on why such oversight falls under a specific committee's jurisdiction and that it should be a board committee.

"I don't feel ESG reporting needs to sit with the audit committee. Just tell us why you've decided that this should have received oversight from that particular committee, and we will consider whether we feel that is appropriate."

- Investment Manager, Stewardship and ESG, Asset Owner

External Assurance

The quality of external ESG assurance is emerging as a critical focal point within the reporting landscape. While there is a growing recognition of its importance, a significant portion of non-financial data remains unassured. This poses a challenge for both companies and investors, as the market for assurance is currently highly fragmented, ranging from major players like the big four accounting firms to smaller boutique agencies. The considerable variation in fees paid for assurance services, spanning from several thousand pounds to several hundred thousand, further compounds the issue and highlights the lack of standardisation in the industry.

Investors are seeking clarity regarding the different types of assurance available for non-financial data, underlining the need for clearer explanations to bridge the current confidence gap in this area. Striking the right balance in assurance providers is crucial. Currently there is a range from the four major audit firms to a multitude of smaller entities handling assurance on climate and other ESG factors. Investors envision a scenario where a select group of experts can proficiently handle all aspects of ESG assurance in a sophisticated manner.

"The prevailing opinion is that the Big Four aren't yet very good and don't necessarily have the skill sets to provide adequate assurance over ESG metrics and non-financial information."

- Head of Governance, Asset Manager

What Companies & Investors Think

WHAT DO INVESTORS DO WELL?

Overarching

- When companies sense that an investor is genuinely 'invested in the management team', fostering constructive conversations even during challenging times, a strong sense of support and trust emerges. This supportive dynamic allows for more open dialogue and enables the business to make informed and longer-term decisions.
- When investors act as effective 'non-executives', companies find themselves engaged in broader, more meaningful strategic dialogues. This engagement allows for a deeper understanding of each other's perspectives and long-term considerations for the company, fostering a relationship built on mutual learning and shared strategic vision.
- Providing clear messaging and reinforcement that it's acceptable to prioritise three or four issues relevant to their business, rather than attempting to cater to every stakeholder's demands. This targeted focus allows companies to streamline their efforts and allocate resources more effectively, fostering a strategic alignment with their core objectives.

Specific to this dialogue

- Investors who proactively reach out to speak directly with Audit Committee Chairs to build relationships and gain insight into their roles and responsibilities are highly valued.
- Investors that provide clarity on the questions they have and the issues they're concerned about enable the Audit Committee Chairs to better comprehend their perspective and address their concerns effectively.
- Clear discussion between investors and Audit Committee Chairs on broader issues helps transparency and enhances the quality of the interactions.

What Companies & Investors Think

WHAT DO COMPANIES DO WELL?

Overarching

- When companies prioritise clarity and transparency regarding their material issues and connect them to their overall strategy instead of solely focusing on compliance-driven reporting, it demonstrates a deeper understanding and confidence in their operations.
- Companies that anticipate and adapt to changing regulatory and reporting landscapes with a practical approach to disclosures and that seek clarity on investor preferences foster greater alignment and understanding.
- When companies invest effort in understanding investors' objectives, including diverse client demands and internal policies a more effective dialogue will result. Understanding whether investors are focusing on systemic risks or specific company issues and their underlying motivations and requests will ensure that information and actions are tailored.
- When companies connect and synthesise their reporting and communications in a strategically driven manner, integrating the importance of sustainability issues with financial performance, it results in consistent and coherent messaging that is more easily understood.
- Investors appreciate companies' increasing acknowledgement of the necessity of external assurance for sustainability data and value when companies remain adaptable and committed to learning and improving in this evolving area.

Specific to this dialogue

- When companies provide clarity on what they are doing above and beyond regulatory requirements.
- Board governance days, where companies make their Audit committee, and other committee chairs and the board chair available to speak to investors. The Audit Committee Chair could present on the key issues with an opportunity for investors to ask questions.
- When an Audit Committees puts out a letter once a year outlining the key changes they are making, this provides a clear understanding to investors and an opportunity to engage.

Actions for Companies & Investors

TOP TIPS FOR INVESTORS AND COMPANIES

Companies

- Ensure it is understood that Audit Committee Chairs are open and willing to engage with investors. Provide a direct line of contact through investor relations and/or the company secretary.
- Encourage Audit Committee Chairs to attend results presentations and make it known they are present and available to answer questions from investors.
- Audit Committee Chairs should occasionally join CFO roadshows post-results to provide additional insights and perspectives to investors, if there is a demand for this.
- Clearly communicate the governance and oversight structures when it comes to ESG and sustainability.
- Don't be offended if investors don't engage regularly but ensure that the lines of communication are available and open.

Investors

- Ensure that internal teams comprehend the significance of audit and audit committee reporting in providing deeper insights into the risk profile of companies.
- Take the initiative to understand more about the importance and status of internal controls, ESG assurance, and other pertinent issues.
- Take the time to scrutinise the appointment of Audit Committee Chairs, including their skills, experience, and the overall composition of the audit committee.
- Don't hesitate to engage with companies on key issues or areas where you seek further understanding, especially regarding what appears in their reporting.

Our Methodology

We formed an Advisory Panel of experts from our membership with significant experience and knowledge of both the UK and global markets. This group provided direction at the beginning of the project, sharing their thoughts, insights and experiences of the market which helped to formulate our approach to each of the four dialogues. Many of the Advisory Panel also participated in individual work streams and this group will oversee the project's final output, alongside the strategic partners.

We prioritised four pivotal conversations between asset managers and companies and identified a strategic partner to represent the corporate voice in each dialogue. These partners included: Investor Relations Society, Accounting for Sustainability (A4S), Audit Committee Chairs Independent Forum (ACCIF) and leading Company Secretaries.

During the fourth quarter of 2023, we interviewed investors and company representatives in each of the workstreams and organised roundtable discussions in conjunction with each of the four partner organisations. Each roundtable was chaired and facilitated by the Investor Forum with five to eight experienced corporate representatives and five to eight of their investor counterparts in attendance.

The investor representatives included analysts, portfolio managers, ESG specialists and stewardship experts who came together to help enhance the quality of dialogue. In total over 60 individuals participated in the dialogues – representing 25 Member organisations and 28 FTSE350 companies.

List of Abbreviations

The following abbreviations are commonly used in the investment industry, and have been used throughout this report.

A4S: Accounting for Sustainability

ACCIF: Audit Committee Chairs Independent Forum

AGM: Annual General Meeting

AI: Artificial Intelligence

CEO: Chief Executive Officer

CFO: Chief Financial Officer

CIO: Chief Investment Officer

CRO: Chief Responsibility Officer

CSO: Chief Sustainability Officer

CSRD: Corporate Sustainability Reporting Directive

ESG: Environment Social and Governance

GRI: Global Reporting Initiative

IIGCC: Institutional Investors Group on Climate Change

IRS: Investor Relations Society

IR: Investor Relations

ISS: Institutional Shareholder Services

ISSB: International Sustainability Standards Board

NED: Non-Executive Director

NGO: Non-Governmental Organization

RemCo: Remuneration Committee

SASB: Sustainability Accounting Standards Board

THE INVESTOR FORUM

www.investorforum.org.uk
info@investorforum.org.uk

The Investor Forum CIC
183 Euston Road
London, NW1 2BE