

**SHAREHOLDER RIGHTS AND THE SECRETS OF SUCCESSFUL
ENGAGEMENT**

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STEWARDSHIP AT STANDARD LIFE INVESTMENTS LIMITED, AT THE
STANHOPE HOTEL IN BRUSSELS ON 9 DECEMBER 2014**

Good evening, Ladies and Gentleman,

I discovered at a relatively young age that one could become a seasoned veteran in the world of governance & stewardship. Over 20 years ago – when Standard Life was Europe's largest mutual company - I was asked to put down my cheque book as a fund manager at Standard Life and pick up my conscience by developing an approach as to how we should fulfil our responsibilities and exercise our rights as an institutional investor in the field of corporate governance. At the time, in the UK, Sir Adrian Cadbury had just published his Code. This was aimed at listed companies, in the main, but recognised that its purpose as a 'comply or explain' code, was to enable boards of directors to have conversations with their institutional investors about the financial aspects of corporate governance. For me, it was a leap of faith. A leap of faith I say, with a blank sheet of paper, because we had no European Shareholder Rights Directive, we had no UK-inspired Stewardship Code and we had no UN-accredited Principles of Responsible Investment to work with. Looking back over those 20 years, my regrets are few. The European corporate governance and shareholder rights movement has travelled a long way and I am proud on behalf of Standard Life Investments, to have been on that journey from its very beginning – and still be travelling in the vanguard.

This evening I want to share with you a few observations on SRDII and I want to go beyond the Directive and share with you secrets of successful engagement that we have used in the UK and are pursuing increasingly in Europe.

Ultimately, SLI believes that corporate governance and shareholder rights must be seen as a means to an end rather than an end in themselves. It is with this in mind that I shall conclude on the critical link to the revived EU's economic growth agenda and challenge Europe's definition of Public Interest Entities to underline that one size does not always fit all.

SHAREHOLDER RIGHTS DIRECTIVE II

We, Standard Life Investments – and in particular Mike Everett here and I - have been following, and arguably contributing, to the evolution of the proposed changes to the Shareholder Rights Directive since they emanated in the 2010 Green Paper and the EU Corporate Governance Framework, which led to the Corporate Governance Action Plan in 2012. We have pounded the pavements of Brussels and knocked on many doors – not to lobby but rather to share our many years of experience with a view to constructively influencing the development of practical proposals. Our views were based on sound principles that would strengthen the rights of shareholders to hold boards to account in a responsible, efficient and transparent way. With this in mind, I am pleased that our efforts were not in vain. Indeed, we are very supportive of the Directive, for the most part, and although we believe there are still a few outstanding issues to be worked out, we are very keen to see the Directive proceed largely in its current form and not get diluted or delayed. At the same time, we would not want to see an escalation of requirements burdening European industry at a time when we as asset managers are being asked to contribute

to the long-term investment culture of the EU. In this regard, the Directive provides, in all material respects, a framework to align to the long-term interests of directors of investee companies with those of institutional investors and asset managers. It also involves the wider stakeholder community, notably European savers, thereby enabling everybody to play a part in contributing to our long-term prosperity both at an individual and a national and European level.

I mentioned there were a few outstanding issues – as a relatively young veteran I don't think you would expect me to say otherwise. So allow me for a few minutes to address some wrinkles of detail – but important detail - that should be addressed and not ignored.

First, we support the proposals relating to the identification of shareholders and other aspects designed to enable the facilitation of exercise of shareholder rights. Indeed, coming from the UK where transparency of ownership and facilitation of rights has been standard practice for many years, I confess that we find it somewhat surprising that these provisions have not been introduced elsewhere in Europe before now. However, I recognise that the wide divergences across the EU in investment cultures, the role of governments in industry, data protection and tax rules contributes to explaining this. But, there is one practical aspect that we should like to see addressed. On one hand, we believe it is both appropriate and important that companies should be able to identify those who exercise the rights over their shares and, in particular, have the power to vote, attend AGMs and raise questions. It is critical that the EU-wide legal and administrative arrangements for holding shares should allow this to happen. On the other hand, our view is that this should not – should not – require the disclosure of the end beneficial owner who has the economic exposure to the shares. As you will be aware, it is normal for pension funds and insurance companies to arrange for asset managers to exercise the rights of share ownership. Hence the process of identification should provide to companies the details of only those with the responsibility to exercise those rights. It is this arrangement which already operates in many markets and we earnestly hope that member states would not interpret Article 3a so as to require the disclosure of all end investors. To do this would be very, very inefficient and problematic, and based on the purpose of the Directive we see no benefit from identifying entities beyond those that are responsible for the exercise of rights, notably to vote and raise questions. Therefore, great care should be taken in defining at which level of ownership the disclosure should be made – and for what purpose.

Second, we support the provisions to improve the transparency of institutional investors, asset managers and proxy advisers. We believe all these parties need to be transparent and accountable and uphold high standards in order to maintain their license to operate and their license to invest. But there is one concern: the proposed requirement to measure the performance of an asset manager 'taking into account long-term absolute performance' under Article 3g. Institutional investors will often select a number of asset managers, with each being responsible for a particular section of the overall portfolio. This selection is part of an overall investment and liability matching strategy to meet the objectives of the institutional investor concerned. In our experience, the asset managers selected are measured against the achievement of coordinated targets and metrics, which may or may not be absolute performance. Therefore, we stress that it would not be appropriate to monitor the performance of all appointed managers on an absolute basis. Rather the requirement to measure the performance of an asset manager should be aligned with achievement of the long-term investment objectives of the institutional investor. A revised rewording is called for that permits the necessary degree of flexibility that is consistent with delivering - and not frustrating - the high level objectives of the Directive.

Third, we support the right to vote on related party transactions. In our experience, many of the companies which have been wrecked by corporate governance failures have had a high incidence of related party transactions over which minority shareholders have had no say. Income has been extracted for the benefit of the few at the expense of many. At these companies the lax approach to related party transactions has contributed to cultures and behaviours that have not been sustainable. Therefore, the provisions of Article 9c, which provide shareholders with the right to vote on related party transactions that represent more than 5% of the company's assets or transactions which have a significant impact on profit or turnover is welcome – it is very welcome. But we recognise not only the need to be practical but also the fact that many related party transactions, particularly those arising in the normal course of business, are conducted on an arm's length basis and do not pose any undue problems. Therefore, we are concerned that the

Directive should not result in the major upheaval in normal business operations, and, importantly, it should not result in a large number of voting resolutions that would make it difficult for shareholders to distinguish the wood from the trees. Accordingly, we would urge that the Directive includes the provision of adequate rights to shareholders to exercise control over related party transactions that could significantly impact their investment, while balancing the need for such transactions that arise in the normal course of business and are conducted on an arm's length basis to proceed without impediment.

THE SECRETS OF SUCCESSFUL ENGAGEMENT

The engagement that takes place between shareholders and companies isn't just about respecting codes and directives, and nor is it about voting and ticking boxes. Compliance and box ticking can be blunt instruments and conceal the reality of the relationship that should exist between long-term investors and their investee companies. Rather, at the heart of engagement is making sure that the board and the company's shareholders are on the same page, the same paragraph and ideally the same sentence – at the same time. Engagement should be a two way dialogue. On one hand, it should enable shareholders to hold boards to account - effectively and constructively. On the other hand, it's about shareholders responding to the needs of directors. This way, directors are encouraged to make better informed decisions in the boardroom and have a better understanding of the interests of shareholders when making decisions. This is especially relevant when they impact on the company's long-term strategy, financial position and risk profile.

I may be biased but I believe that it is fair to say that Standard Life Investments enjoys one of the best reputations for the way in which we actively engage with companies. Don't just ask me. Our reputation is largely recognised by both our clients and the companies with which we engage.

I believe there are five reasons that contribute to our success. I shall mention them only briefly.

First, we attach a lot of importance to preparing for our engagement. We invest a huge amount of time in researching the company – its governance arrangements, its risks, its finances, its strategy and a whole host of other factors. Increasingly we look at the company's performance in ethical, environmental and social policies. Importantly, we involve our fund managers and others at Standard Life Investments who bring useful perspectives and insights to bear.

Second, is the importance of being both patient and persistent. If you are looking for instant gratification, indulging in corporate governance engagement and shareholder rights is likely to leave you feeling frustrated, more often than not.

Third, as an asset manager one has to demonstrate an appetite to escalate engagement with the investee company, when the time is right. At Standard Life Investments we generally go to four or five AGMs – mainly in the UK – each year. Not only do we go to them but we go and speak at them. No board of directors likes being criticised in public – least of all by us - but in my experience a willingness to speak at AGMs in exceptional situations is an important tool in the stewardship toolkit to hold boards to account and bring about change. It is striking just how few other asset managers demonstrate such an appetite to escalate the engagement at AGMs. I have to tell you that this is a problem that needs to be addressed across Europe, even in the UK.

Fourth, we resource our governance and stewardship activities at a senior level – Mike was our Head of Compliance before he joined our Governance & Stewardship Team and I was Head of our Private Equity and Smaller Companies Teams, and two other Governance & Stewardship Directors are former fund managers – one was Head of Fidelity in Edinburgh. At Standard Life Investments we recognise the importance of having senior high-calibre, professionally experienced people in these roles. Not only does this contribute to the quality of decisions but it is appropriate to the substance of the matters being discussed and the standing of the individuals at the companies with whom we engage. Far too many fund managers are unwilling to commit this right level of resource. The commitment and instructions from the top hierarchy in the asset management firm, and the way it manifests itself is as important within the firm as it is at the investee company – if not more so.

Last, we seek to be in a long-term relationship with our investee companies. Mike and I don't just turn up on the doorstep when there is a problem. Rather, we go out and proactively engage with companies when there isn't a crisis in order that we can discuss what's changing – on both sides. This not only improves our understanding of the dynamics of corporate governance at the company concerned but also provides the company with a shareholder sounding board on the issues of the day. This takes time and effort. We cannot do it for all the companies that we invest in but nevertheless we make a considerable effort – and go the extra mile - to make our long-term relationships stand the test of time.

REDEFINING PUBLIC INTEREST ENTITIES

Let me conclude my speech by drawing attention to the definition and scope of Public Interest Entities, and the potential impact of this draft Directive, and indeed other EU corporate governance-related legislation. Public Interest Entities, as I understand it, refers to all entities – all companies - listed on recognised stock exchanges in the European Union. It thus covers listed undertakings such as banks, insurance companies or undertakings which are of significant public relevance because of the nature of their business, their size or their corporate status.

We need to be vigilant, however, in ensuring that such legislation does not inadvertently find itself being applicable to a very large number of smaller growth companies who have little or no impact on the wider public but are keen to foster and enable entrepreneurial spirit to flourish, and deliver the growth that we so much need.

Indeed, last September I welcomed Council's adoption of the directive for the disclosure of non-financial and diversity information by certain large companies. This essentially exempts PIE SME's from the new core reporting requirement to draw up, on a yearly basis, a statement relating to environmental, social and employee-related matters as well as respect for human rights, anti-corruption and bribery matters. It applies only to PIEs with over 500 employees.

At a time when Europe is striving to restore growth I question seriously why we continue to impose on such entrepreneurial companies the same burden and cost of corporate governance as applies to genuinely Public Interest Entities. To my mind this issue is not so much about the application of law and regulation. It is more about sending a clear message from Brussels to emerging growth companies that it recognises that they need a different and lighter burden of corporate governance rules to enable them to be flexible, entrepreneurial and successful in delivering the growth we all need. The JOBS Act in the US provides an interesting role model. Europe should not be afraid to take the risk. Indeed it should recognise that growth isn't just about capital and finance it is about behaviours and culture. And it is corporate governance which sets the tone for behaviours and culture, as well as many of the other good things in life.

As they say, there is no such thing as a free dinner. After Susannah has responded I should welcome your views as to how you think we can all play a part in supporting the implementation of stronger shareholder rights and redefining Public Interest Entities. At Standard Life Investments we believe it is essential that corporate governance and shareholder rights make a contribution to the successful, sustainable growth of the European Union and its long-term prosperity. Ladies and Gentlemen thank you for listening.

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