Corporate Governance

Ethical compliance in the asset management industry

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Introduction

The role of investors, particularly institutional investors, and the improvement of their best practices in the overall scheme of corporate governance are a topic which is much discussed in the fields of science, practical application and media.

The investors, in their capacity as promoters, are assigned a variety of tasks. They are expected to assume an active monitoring role with regard to the management and to positively influence the company's own corporate governance[1], which now also incorporates social and ecological tasks.

A crucial element in the investors' actions is the reasoning that active involvement can, by lowering agency costs, lead to an increase in enterprise value and, at the very least, secure the invested capital. Considered ethically, one should necessarily be able to assume that the aforementioned reasoning derives from the fiduciary responsibility which the investor holds with regard to the beneficial owners - the people and institutions whose money he manages.

In technical terms, all investors basically have access to two courses of action in the event of dissatisfaction or otherwise: "exit" and "voice".[2] The third choice, "loyalty", is not considered here as it means that investors behave passively, adopting a wait-and-see attitude and avoiding all forms of influence.

Exit strategies incorporate the sale of shares, which causes price losses and thus increases the likelihood of a (hostile) takeover. The new investor takes over the rights and responsibilities associated with the share ownership. Conversely, in voice strategies, institutional investors retain their shares and take over active internal control of management decisions by attending and/or exercising their voting rights at the general meeting or by taking

[1] Cf. for example Bassen (2002), Zöllner (2005), Arnold (2008) or Brenner (2008).
[2] Cf. Hirschmann (1970).

over mandates.[3] That the first case occurs only rarely[4] is explained by some institutional investors by the need to avoid public criticism in order to prevent possible damage to the company's reputation; the low attendance at general meetings is apparently characteristic of this.[5] In order to counter such arguments and as a reminder of the general meeting's significance as the most important decision-making organ within a company, efforts are currently being made to offer practical solutions – such as virtual general meetings – which make it easier to participate. There is also talk of making it mandatory for institutional investors to exercise their voting rights or to offer incentives such as bonuses.[6]

It is surprising that the voting behaviour at general meetings generates relatively little attention, even in scientific dialogue. There is a lack of awareness regarding how investors value the right to vote, which factors may influence this value, and how and why the right to vote is used at general meetings.

These are the questions tackled by this first international investor survey. It aims to discover the extent to which the topic of general meetings and the exercise of votes in the asset management industry is seen as a significant aspect of good corporate governance (in the company and in one's own firm) and how far it is implemented as an ethical claim.

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[3] For a detailed analysis of the different options available under voice strategies, cf. Bassen (2002), p. 120. The current discussion regarding this conceptional "exit or voice" paradigm, which contemplates a change or expansion of this reasoning here under consideration of current stockbroking strategies (cf. Lysandrou / Stoyanova (2007)), is not relevant to our study.

[4] Cf. Arnold (2008), p. 226.

[5] Cf. Birds et al. (2000), p. 361, p. 387.

[6] Cf. Zetzsche (2005); cf. DAI (2008); cf. Arnold (2008).

II. Voting rights, active shareholders and general meetings

In the field of international company law, companies are regarded as representative democracies in which the members act through their representatives. This defines a legitimising role of the shareholders' right to vote[7] and shares many similarities with political theories, although shareholders' decision-making authorities are very limited compared to those of voters in the decision-making process.

In a political context, the votes of voters whose interests are affected by the decision-making processes perform the following functions: they aggregate individual opinions and preferences, thus enabling group decisions; they reduce the likelihood of error; they authorise the decisions of the agent and the supervisory rights of the principal. These general functions will need to be modified for public limited companies.

Here, it is only shareholders and not all stakeholders who have voting rights. The voting right is linked to the security, not to the shareholder as a person, and can be bought or sold. As such, shareholders can use their assets to add greater weight to their opinions via the one share, one vote principle.

It is agreed that shareholders are useful in monitoring management and there are calls for more extensive rights of co-determination.[8] To lend support to the economic legitimacy of these arguments, many studies have been carried out to investigate the success of active

[7] Cf. Thompson / Edelman (2009).

[8] The SEC is therefore bringing in new reforms to strengthen the rights of shareholders as of 2010. Shareholders receive consultative votes on the payment systems of companies which received state support in the financial crisis. In Germany, the Shareholders' Directive Implementation Act introduced in November 2008 makes it easier for shareholders to exercise their voting rights and improves information for shareholders.

shareholders[9] as part of the corporate governance system; it is assumed here that there is a positive link to the enterprise value.[10] However, results do not give a single clear picture. This could be due to a lack of comparability between the studies. Some of them, for example, record shareholder proposals and others contractual negotiations, causing the enterprise value measurements and/or the timeframes to vary. What is more, the studies mostly focus on traditional institutional investors such as investment and pension funds, meaning that regulations concerning disclosure and liquidity, for instance, generate influencing factors which could reduce the investors' willingness to actively participate.[11] Hedge funds on the other hand are able to employ leverage effects, work with short-selling strategies and purchase larger shares in companies by using derivatives, without being subject to disclosure requirements.

These larger shares justify the view held by some parties that hedge funds are better potential supervisors with regard to corporate governance. Plus, the remuneration of hedge funds managers, which is based on absolute profits, is claimed to provide a suitable incentive. [12]

Yet the objectives of active hedge funds, such as changing corporate strategies, buyouts or acquisitions, increased dividends or share buybacks[13] hardly differ from those of general shareholders. The Deutsche Aktieninstitut - DAI (German Shares Institute) (2009) can only make additional reference to requirements concerning the capital structure. Initial findings regarding the approach taken by active shareholders would therefore seem to be

[9] It should be noted at this juncture that there is a difference between active shareholders and activists. Nordberg (2009, p. 3) talks of "being active and being activists". Active shareholders are understood here as institutional investors in their capacity as capital-collecting agencies – irrespective of the investment strategies used. As such, both traditional investment funds and hedge funds are taken into account. The DAI (German Shares Institute) makes a similar differentiation in cooperation with McKinsey & Company (2009).
[10] An overview of empirical studies is provided by Karpow (2001), Bassen (2002), Zöllner (2007) or Norli / Ostergaard / Schindele (2009), for example.
[11] Cf. Zöllner (2005), p. 251 ff.
[12] For an overview of empirical studies on hedge funds as active shareholders cf. Brenner (2008).
[13] Cf. Brenner (2008), p. 7.

transferable.

Hardly any theoretical models which justify why and when shareholders vote are currently available.[14] Plus, there is only a handful of empirical studies on voting behaviour. They focus on the central question of whether shareholders still vote in favour of management proposals even if they are unsuitable for increasing the enterprise value or indeed cause it to decrease. In addition, they also analyse whether shareholders vote strategically and take into account the weight of their vote.[15]

The classic function of the general meeting is to use voting to obtain shareholders' consensus on important decisions. The general meeting also offers the shareholders in attendance a forum for discussion and exchange with the members of the management board and the supervisory board.[16] The monitoring function that shareholders are often said to perform with regard to the actions of the management and supervisory board is not explicit, but rather a logical consequence of the shareholders' decision-making powers to approve the actions of the two bodies.

Well practised corporate governance is expected to make conflicts of interests between company management and owners – shareholders in the case of public limited companies – transparent. As a democratic process within the CG system, the general meeting helps to highlight such conflicts and define responsibilities accordingly.[17] The general meeting brings

[14] Cf. Thompson / Edelman (2009), p. 145. For an overview of voting behaviour in a general context cf. Feddersen (2004). This takes the "paradox of non voting" as its base: if voters only vote to influence the result, even a minimal cost such as travel expenses should prevent anyone who votes strategically from voting in major ballots.

[15] Cf. Maug / Rydqvist (2006).

[16] Cf. Strätling (2003), p. 74 ff.

[17] Cf. Strätling (2003), p. 74 ff.

the company to the interest of the often critical public,[18] even if participation is principally reserved for the shareholders (in some companies this principle is being relaxed by means such as full coverage on the internet).

Despite the differences between financial and corporate governance systems in different countries, which are also the reason behind the differences in shareholder structures, there are generally two groups of shareholders who meet at the general meeting: individual investors and institutional investors.

The latter often prefer direct communication channels in order to exert influence on the management's conduct. Individual investors exercise their voting rights out of an interest "in their company" and thus in their investment. The relationship is more direct, almost "emotional" and tied to a feeling of responsibility. Some use the platform of the general meeting as an opportunity to make themselves heard by the public and to use protests to hold the company accountable in terms of its social responsibility, for instance.

This image is supported by a current study by Norden/Strand (2008)[19], which examines the behaviour of Swedish portfolio managers at general meetings. The result shows that voting behaviour and tendencies to raise opinions are related to company characteristics: portfolio managers are more likely to be active, in the sense defined here, in large firms which appear a lot in the media and have a large proportion of institutional ownership. The company's economic situation, however, was of little significance. The authors' explanation for this behaviour is that it is the managers' primary intention to gain benefit for themselves and not the company, thus rationalising the act of attracting attention to themselves as active

[18] This is reinforced with examples: following the introduction of voting on remuneration systems in Great Britain in 2002, there have been several examples of these reports receiving heavy public criticism from institutional investors during the general meeting. Cf. Apostilides (2007) p. 1279.

[19] Norden/Strand (2008), Shareholder Activism among Portfolio Managers: Rational Decision of 15 Minutes of Fame? Working Paper, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=991542

investors at the general meetings of large companies with a lot of media interest.

Alongside the initial findings, it is clear that many questions remain to be answered with regard to voting behaviour, the value of voting rights and the general meeting. Besides the ethical attitude to voting rights and how they are exercised, it must also be discussed which other factors affect behaviour (such as the investment strategy pursued or the size of the share) and under what circumstances voting decisions are made by institutional investors. The special position of hedge funds raises still further questions. This study was carried out to gain initial findings over as broad a spectrum of the problem as possible.

III. Method

A global survey of shareholders was carried out concerning the significance and exercise of voting rights. The survey was performed using a questionnaire to be answered online. The questionnaire was divided into ten main sections: significance of voting rights; relevance of ESG (environment, social and governance); the fiduciary role of institutional investors; voting behaviour - more specifically the use of voting rights; possible transfer of voting rights; rejections or approval frequencies; use of external service providers or standards; and the special role of hedge funds. The last section calls for an evaluation of the questionnaire. The questionnaire was developed by the working group and then made available in a pre-test to several experts from the field of science, investor groups and organisations, investment funds and banks. Subsequently the target network was informed of the link and requested to participate by e-mail via the Club of Florence network. Of the 5,449 addresses in the target group, we received 193 data records for responses, giving a return rate of 3.54%.

Some sections of the questionnaire require the respondent to give their own stance on a statement, using one of five possible answers – from "not important" to "full agreement". Most direct questions also have five possible answers, unless they require a yes/no answer or numerical data. The third question type requires the respondent to rank specific aspects according to significance.

Not all 193 data records are complete, which is why we subjected them to a more detailed analysis with regard to the missing values. It is likely that the design of the questionnaire is the reason for the missing values, as its implementation deliberately refrained from using a monitoring function to ensure that every single question was answered. This means that respondents can deliberately leave out a question and that they receive no notification if they overlook or accidentally fail to answer a question.

Next, the sample size was determined for each individual question to check whether this could be used as a basis for reducing the missing values. The sample size per question was evaluated both for the overall data record and for the "completed questionnaire" data record. The evaluation shows that the sample size for the overall data record for question blocks 1-3 rises much more sharply than for the other questions in comparison to the sample size of the "completed questionnaire "data record. This makes it clear that for the questionnaires which were not completed, most respondents stopped answering after question block three or even earlier. It is also apparent that in question block nine, which deals with the firm's general standards, it was mainly the questions concerning in-house guidelines and the local code that were more frequently left out. This is very likely due to the fact that this information is usually considered confidential. It was furthermore revealed that the respondents more often left questions F4.2 and F6.3 unanswered, as these questions required them to formulate the answers themselves. The country distribution for the data records was also examined. This showed that for both the overall data record and the "completed questionnaire" data record, the majority of respondents (over two thirds) came from Europe, whereby continental Europe was used as the basis for classification. In summary however, no specific approach was revealed to significantly reduce the number of missing values by eliminating individual questions, question blocks or nationalities. For this reason, only the empty data records contained in the original data record were removed, resulting in a population of 149 data records.

The first step in selecting the suitable analysis methods was to determine the scales of measurement. Most questions used an ordinal scale of measurement. The characteristics can therefore be put into rank order. In some cases, a nominal and metric scale of measurement was used. For all scales of measurement, the first step was to calculate the absolute and relative frequency distributions and display them as a bar chart. The mean values were then calculated: for the nominally scaled data, this was the mode, whereas the median was used for ordinally scaled data. For the metrically scaled data, both the median and the arithmetic mean were calculated.

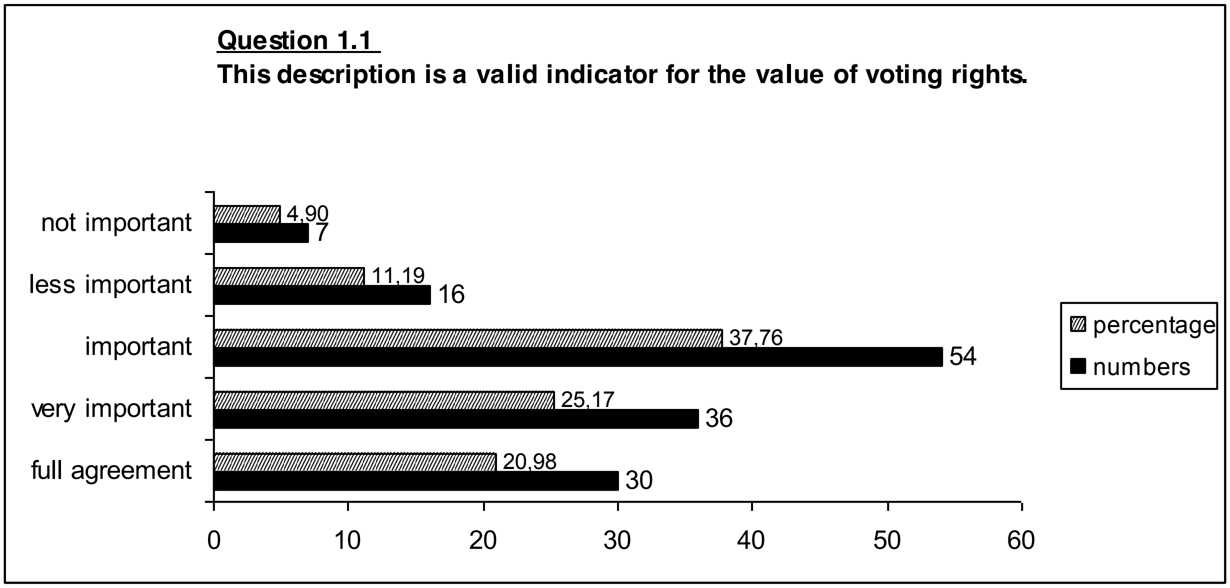
III. Results

Voting rights and voting behaviour

(Questions 1.1-1.3 and 2.1-2.4)

The argument concerning efficient internal control by active shareholders is based on the implicit hypothesis that they value and use their voting rights. This hypothesis is analysed in the first question block. A voting decision between ordinary shares and non-voting preference shares is used to indicate the perceived value of voting rights. If companies have issued both types of share, the latter is often quoted at a lower price on the market.

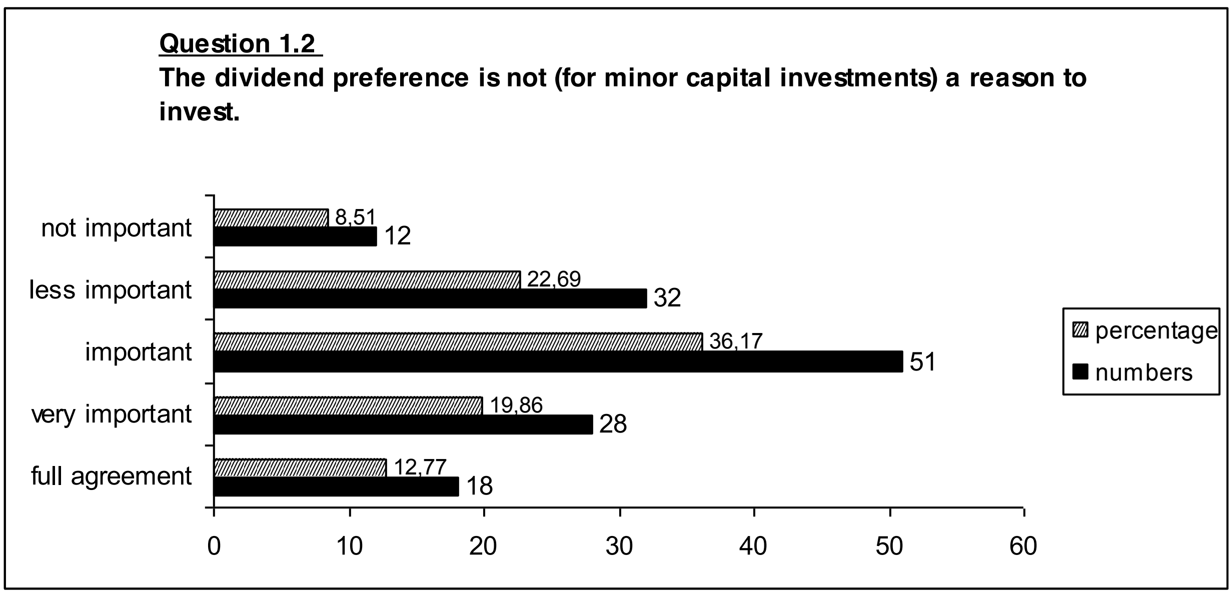
This difference in value can be seen as a valid indicator of the value of voting rights. On an answer scale with five options from "full agreement" to "not important", 83.9% agreed that this statement was at least "important", 20.9% even giving the answer "full agreement". Similarly, the dividend preference associated with preference shares was not identified as a reason to invest by the majority of respondents – only 68.8% in this case however. As concerns the direct question regarding the preference of ordinary shares over preference shares, an impressive majority of 91.37% answered with at least "important". This is a significant indication that voting rights are important and that their value is recognised; a value which can be measured via the different market evaluation of ordinary and preference shares.

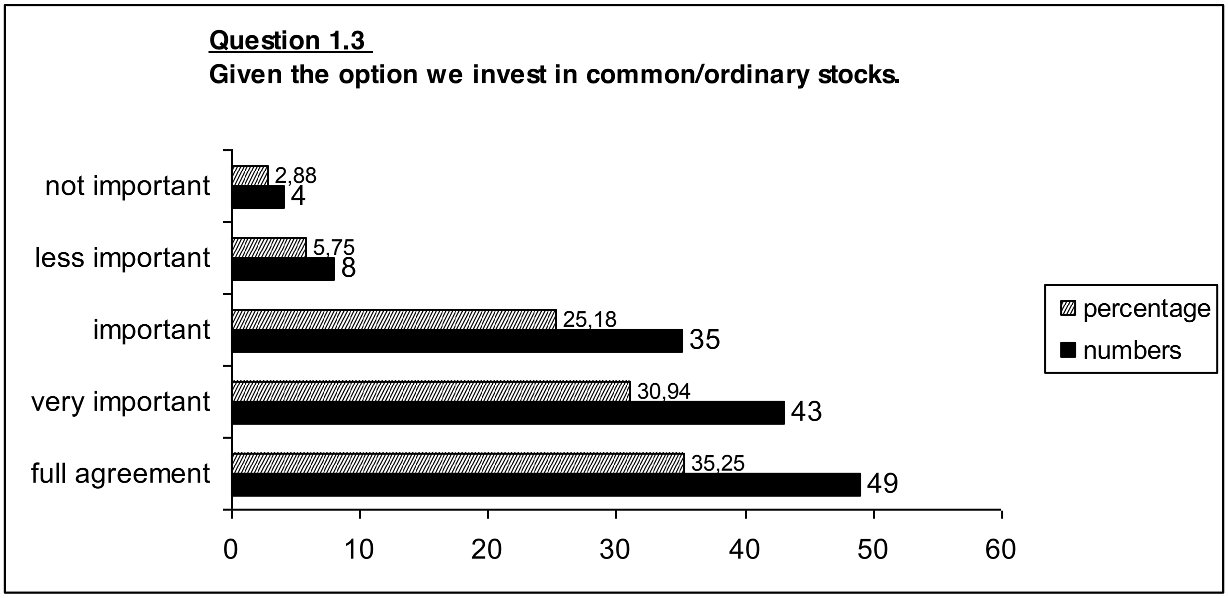


This fundamental question throws up a variety of interesting factors which may influence the value of the voting right and its use, thus explaining observed behaviour. The emphasis was not placed here on factors arising from a firm's attributes or the market situation, but on characteristics of the investors themselves.

The respective investment strategy of the investment fund could be an influencing factor. As such, certain non-financial ESG value drivers (environment, social and governance) are sometimes of significance. These include environmental sustainability, for example energy efficiency or the use of renewable energy; social aspects such as employee qualification, diversity and child labour; and corporate governance. Firms usually only provide information on these aspects voluntarily, making them difficult to quantify. Personal communication with the management could therefore have a higher value, while the influence exerted by exercising voting rights takes on a lesser importance.

Around half of all respondents (44.62%) are in agreement with the statement that they do not follow a particular investment strategy, so that there is no differentiation in their attitude to the value of voting rights, classifying it at least as "important". Support is lent to this impression by the fact that almost all respondents (96.44%) agreed that the statement that voting rights are valuable and should be used to influence behaviour whatever investment strategy is pursued was at least "important". A similar level of agreement (89.82%) was reached for the opinion that personal communication has a higher value for non-financial value drivers. This increase in value or the consideration that personal communication is an important control instrument does not detract from the value attributed to voting rights.

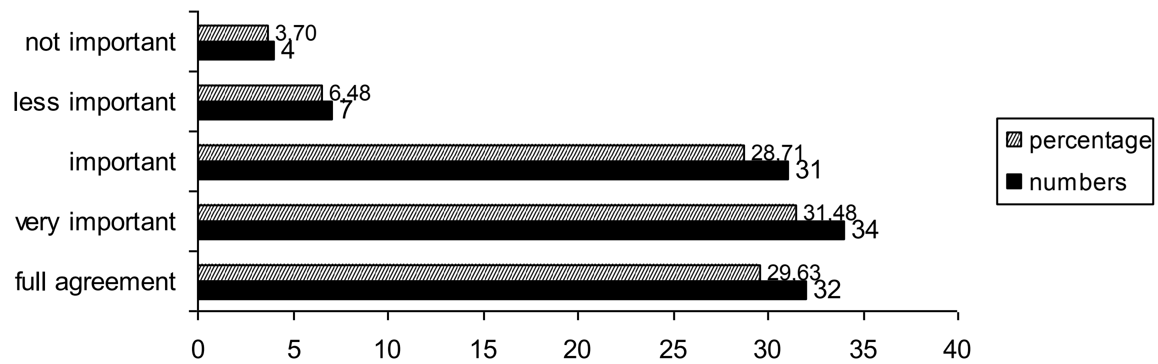




The empirical study by Nordén / Strand (2008) mentioned above observes the behaviour of portfolio managers and implicitly assumes that they decide on how votes are made. However, our results make clear that decision-making authority is actually distributed among different parties. The portfolio managers only make the decisions for 30.7% of respondents. Although this makes them the largest group, the difference between them and proxy voting committees (27.71%) and the executive management (24.74%) is not especially large. The senior officer or share limited partnership have hardly any decision-making authority. These results can be interpreted in a number of ways. The importance of the committee and the management act as an indicator of the relevance ascribed to voting behaviour. The portfolio manager's closer proximity to the company can be used as an argument in his favour. It should also be discussed whether Nordén / Strand's assumption that decisions are influenced by personal benefit or reputation can be transferred to other groups.

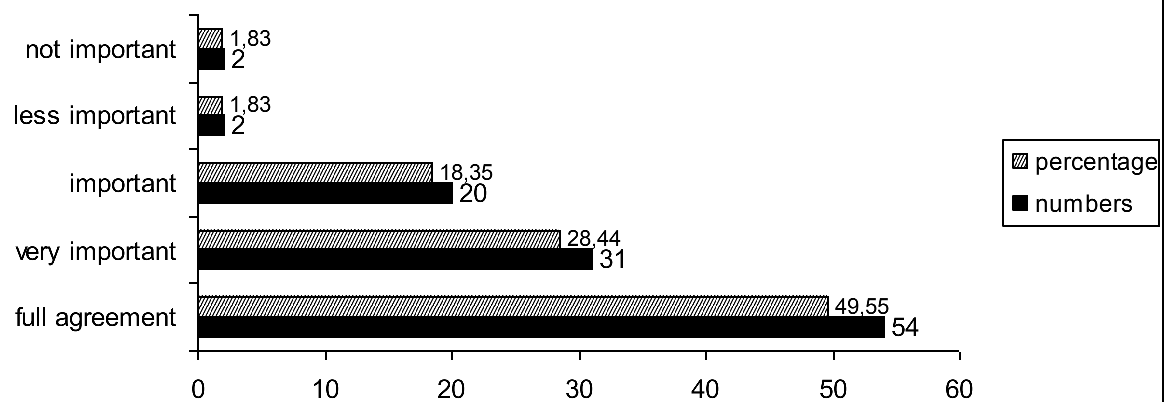
Question 2.1

Information about different value drivers - especially non-financial issues - is often given only voluntarily and is difficult to quantify. Thus, personal communication instruments have a higher value.

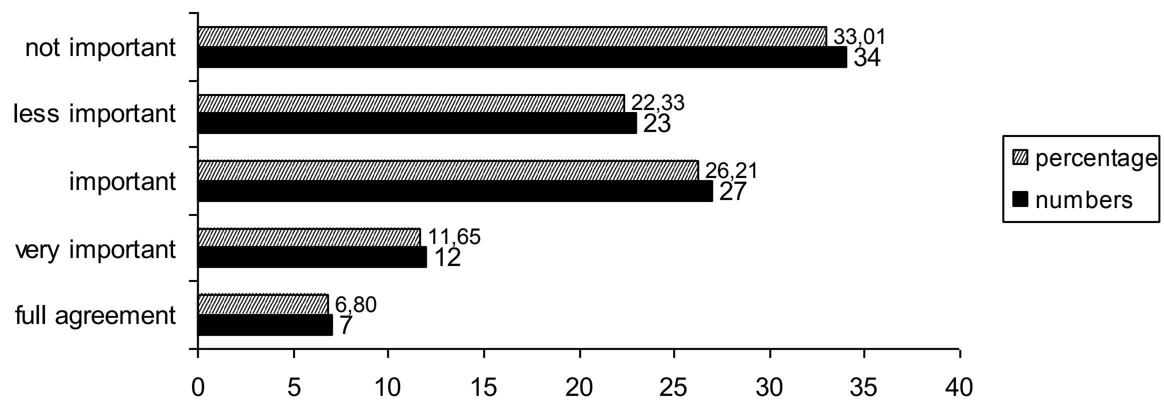


Question 2.2

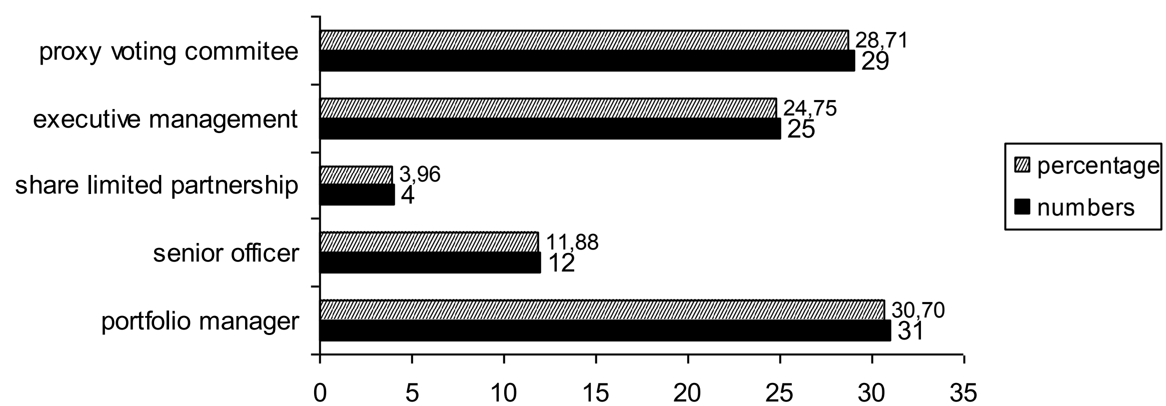
Voting rights are valuable and should be used to influence behaviour whatever investment strategy the particular shareholder pursues.



Question 2.3
We do not follow a particular investment strategy, so that there is no differentiation in our attitudes.



Question 2.4
Who determines voting behaviour in the end?

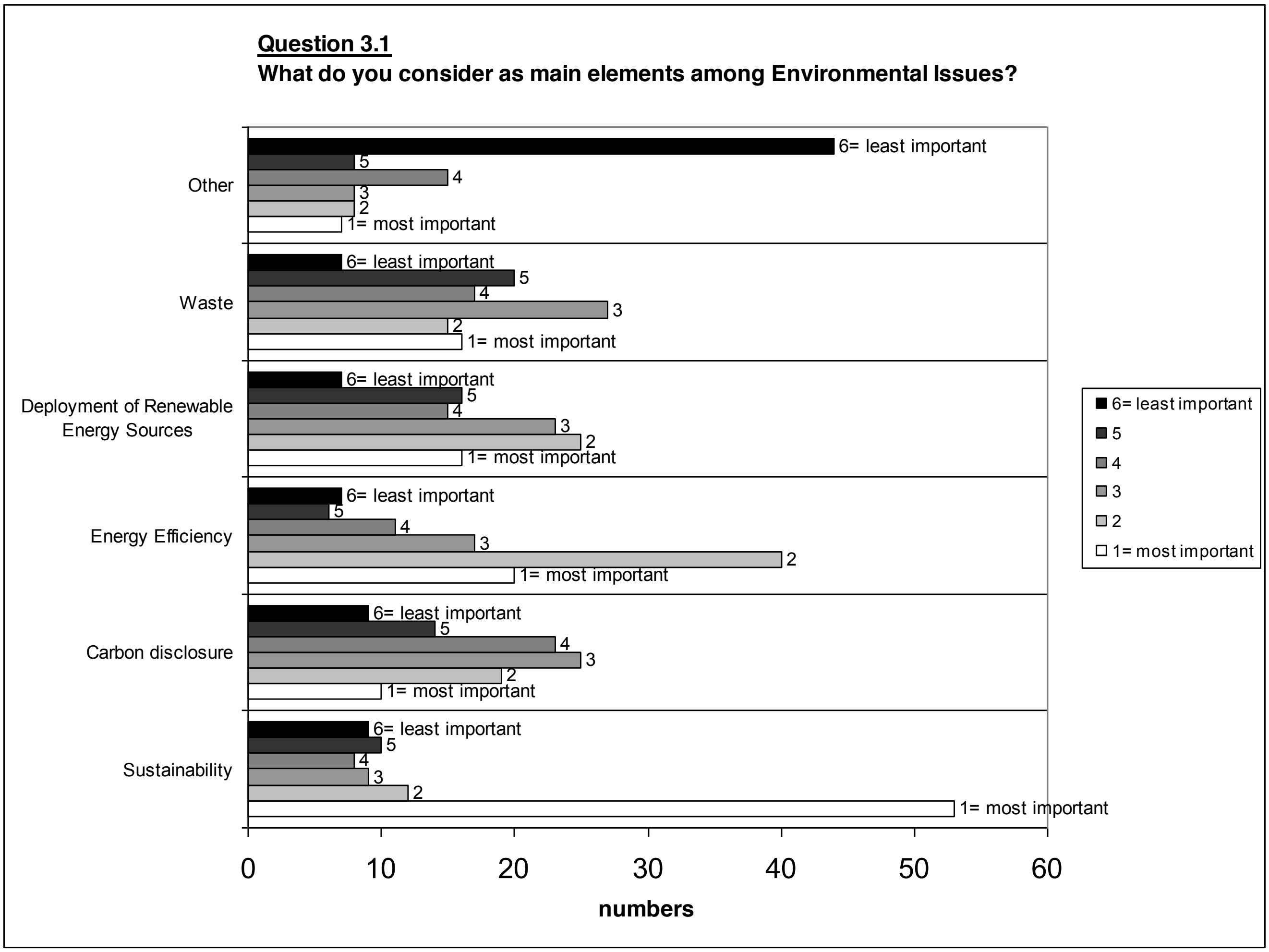


ESG aspects

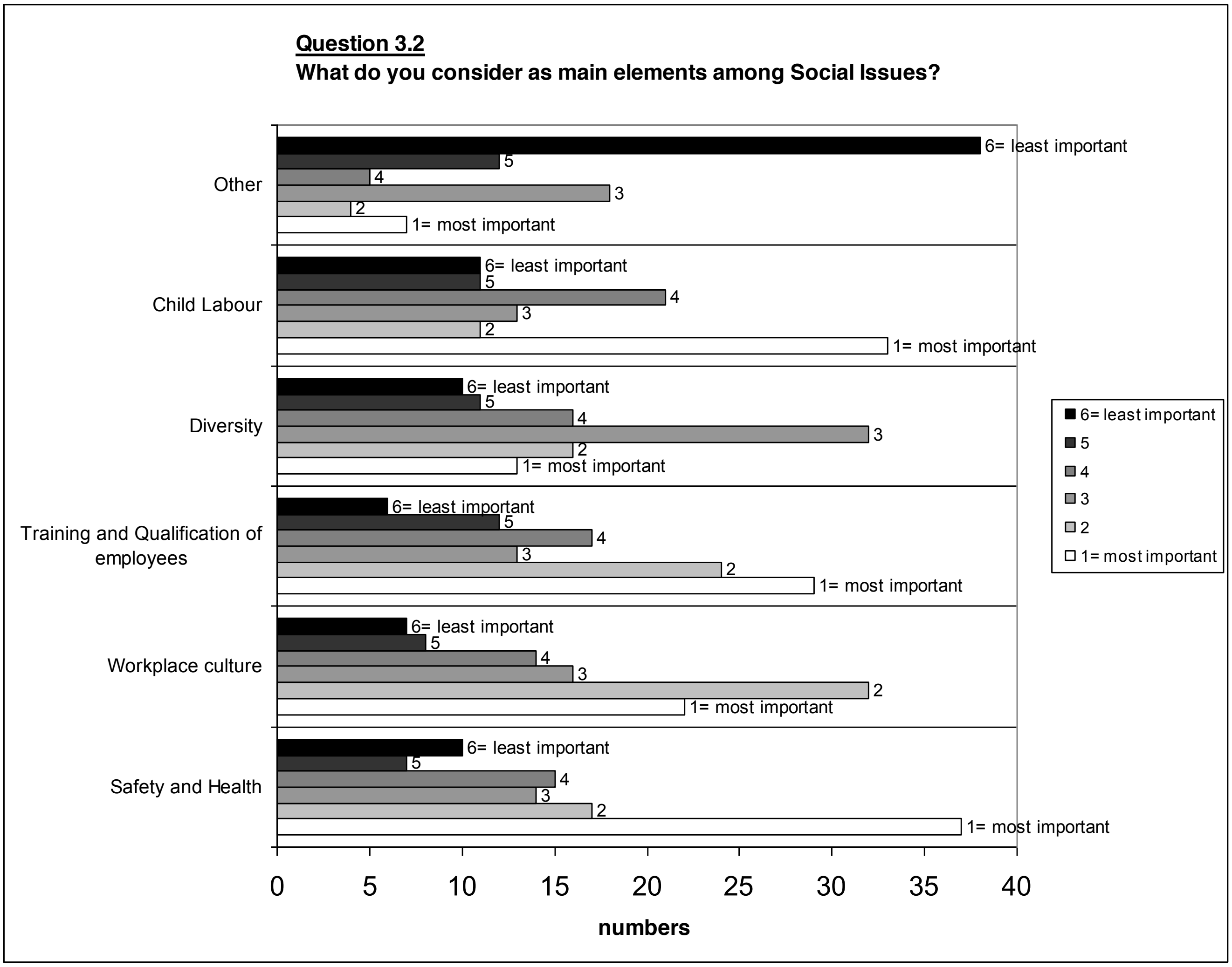
(Question 3.1-3.4)

The third part of the questionnaire takes into account the weighting and priorities of individual aspects of environmental, social and governance-oriented topics. The most important and most common individual elements of the three topic areas are listed in each case and the respondents are asked to evaluate their significance. The resulting ranking ranges from grades 1 to 6, based on the German school marking system: 1 is the most important aspect and 6 the least important.

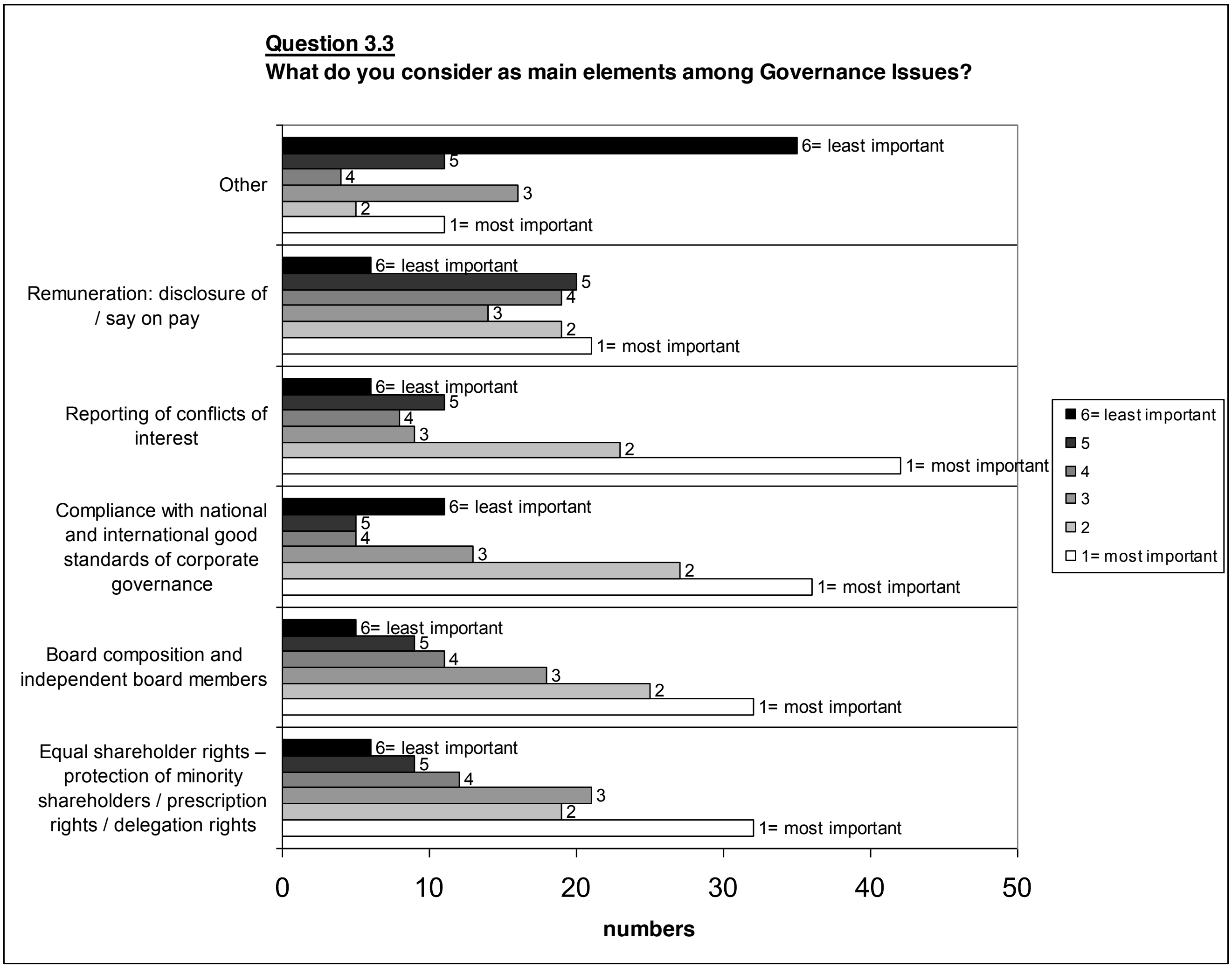
Individual elements of the environmental topic were sustainability, carbon disclosure, energy efficiency, deployment of renewable energy resources, waste and an option for "others". 52.48% put sustainability in first place, followed by energy efficiency (19.8%), the deployment of renewable energy resources (15.69%) and waste (15.69%). This makes it clear that the individual aspects chosen provide a suitable selection.



The individual elements of social aspects were listed as safety and health, workplace culture, training and qualification of employees, diversity, child labour and, again, a category for "others". However, the ranking was closer than it was for environmental issues. The forerunner with 37% was safety and health, followed by the prevention of child labour (33%) and training/qualification of employees (28.71%).



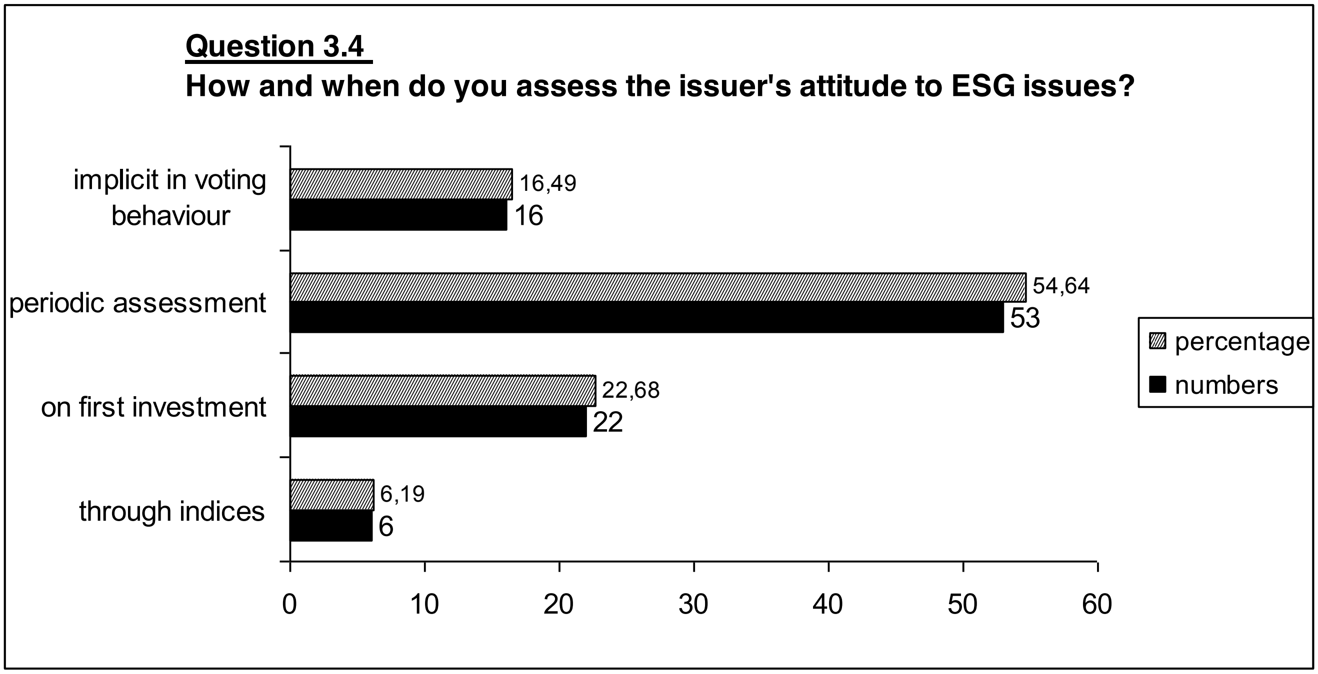
The selection of the corporate governance elements focuses on internal mechanisms which can be influenced by the firm or the shareholders: equal shareholder rights and protection of minority shareholders; board composition and independent board members; compliance with national and international good standards; reporting of conflicts of interest; disclosure of pay; and "others", again in last place with 42.68%. Here, too, the ranking is close-run. Reporting of conflicts of interest (42.43%) comes before compliance (37.12%), board composition (32%) and shareholder rights (32.32%). Yet disclosure of pay, which is currently a subject of heated discussion and regulated by law in Germany, is assigned the greatest significance by only 21.2% of investors.



All of these non-financial aspects are dynamic and difficult to quantify and measure. It is therefore interesting to note how and when the investors record and measure their introduction and implementation in the company: through indices; on first investment; via periodic assessment; or implicitly in voting behaviour. Astonishingly only 6% of respondents use indices. This raises scepticism about the growing discussion regarding the broader and/or more intensive distribution of existing indices.

Such conspicuous disregarding of the indices could be attributed to doubts about the ability to measure these "soft" attitudes, each of which is individual to the company, using standardised models.

22.68% only assess ESG issues upon first investment, while the majority, 54.64%, also takes changes into account through periodic assessment.



Institutional investors and fiduciary responsibility

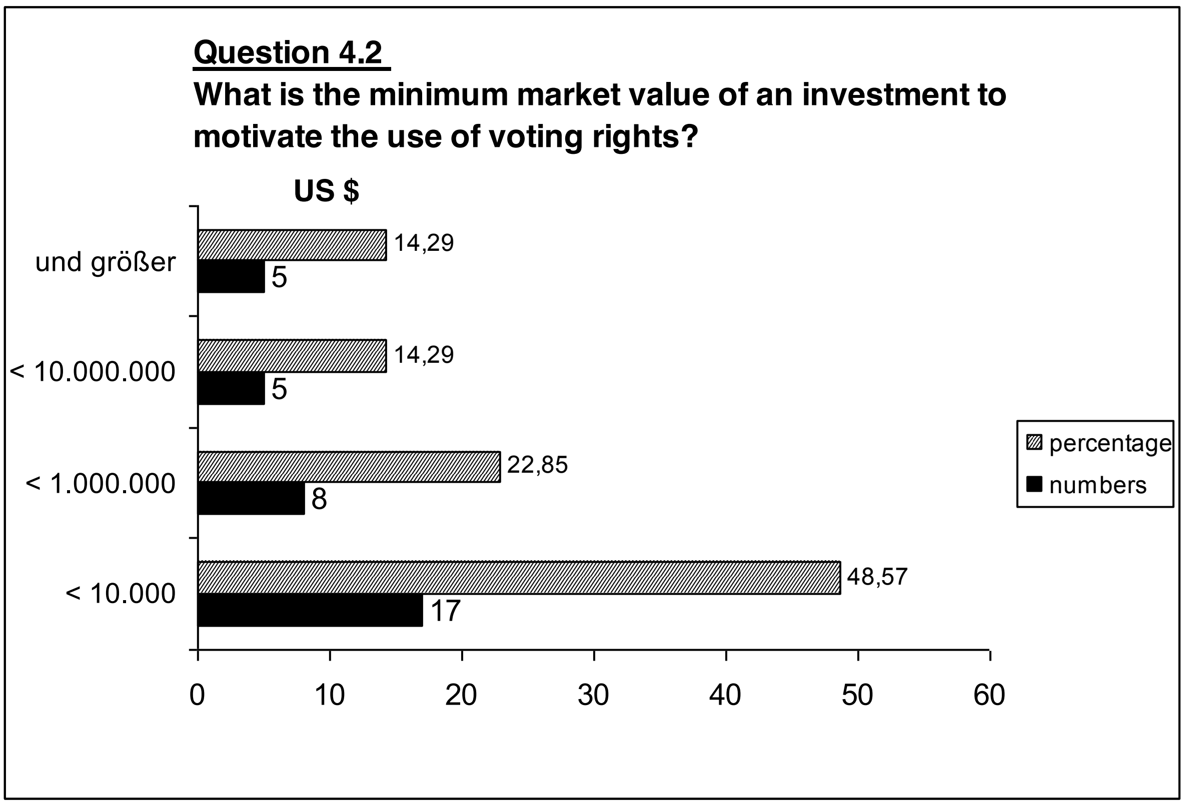
(Question 4.1-4.7)

As active shareholders, investors use different tools which vary greatly in terms of transparency and disclosure. Voting rights and voting behaviour are just one of the alternatives.

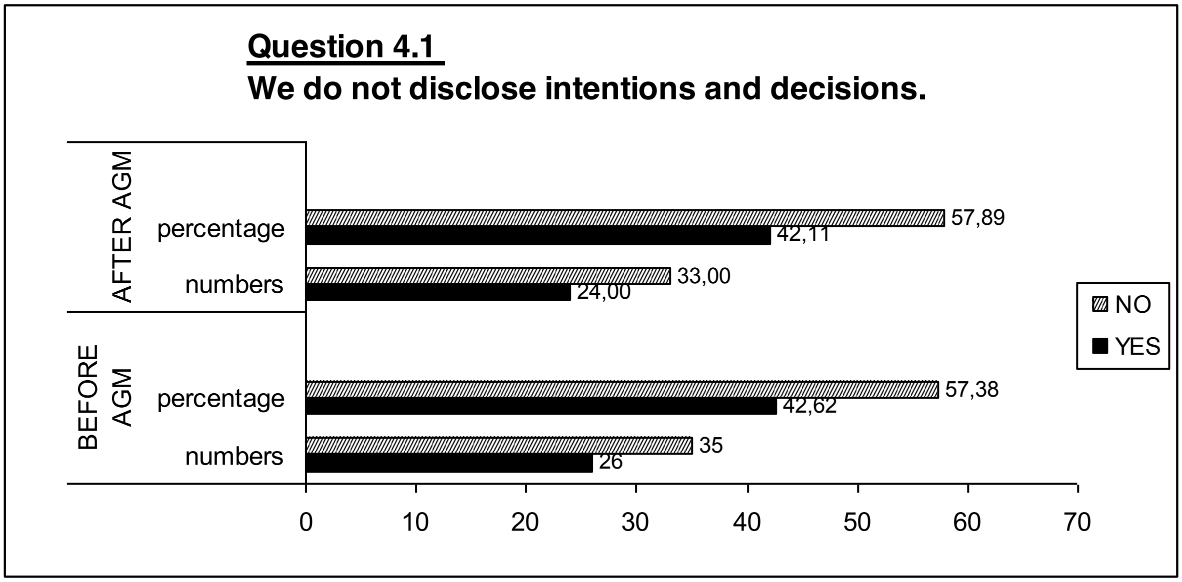
Transparency and disclosure on the use of voting rights and the associated voting behaviour become more important when viewed in terms of the fiduciary responsibility of institutional investors as capital-collecting agencies. They can also be employed in combination with a critical public as an additional tool to influence management behaviour.

To gain current information here, it is first necessary to record whether voting rights are exercised directly, through proxies or not at all.

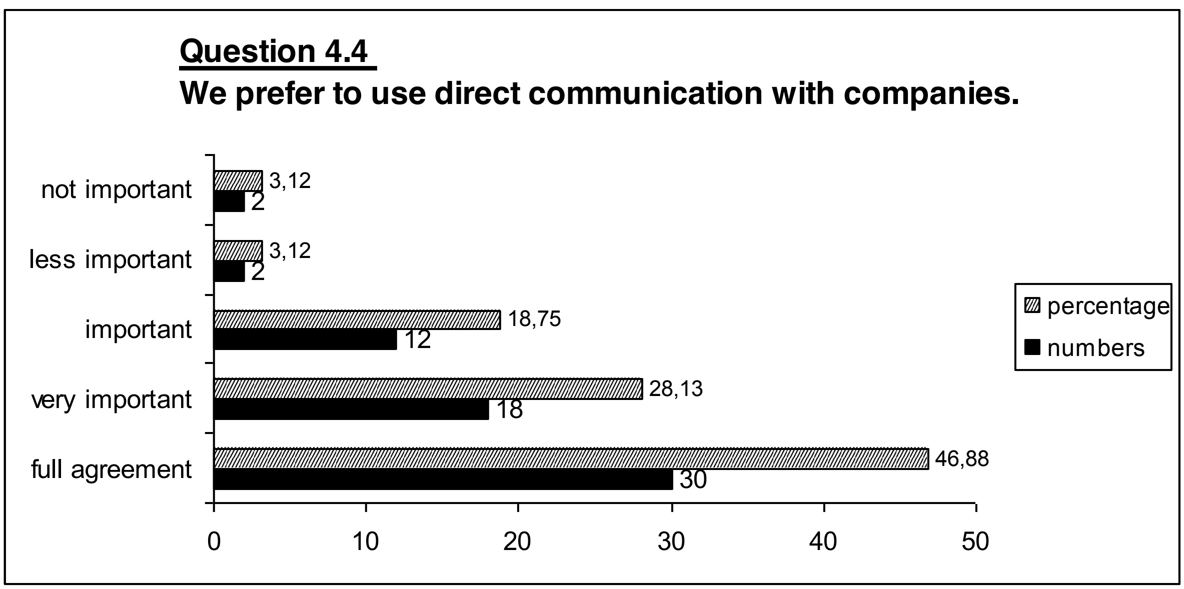
If voting rights are exercised directly, it is possible that the investment volume could decide the degree of involvement. As such, a lower investment volume can mean that the investor is less motivated to use active control due to cost/benefit analyses, additionally backed up by free-rider arguments. However, this notion is not supported. 48.57% of respondents stated that they used their voting rights even for investments below US$10,000 and only 14.29% only use voting rights for an investment volume of over US$10 million.



Investors which currently exercise their voting rights directly or plan to do so in future were asked whether and, if so, when they disclose their intentions and decisions – before or after the general meeting. The results are surprisingly clear and support critics who accuse investors of being unaware of their fiduciary responsibility. 42.62% of respondents do not disclose their voting intentions and decisions before the general meeting, and 42.11% do not make a disclosure afterwards. Hence, investors in the funds are unable to assess how voting rights are used and whether and to what extent active control is exercised.

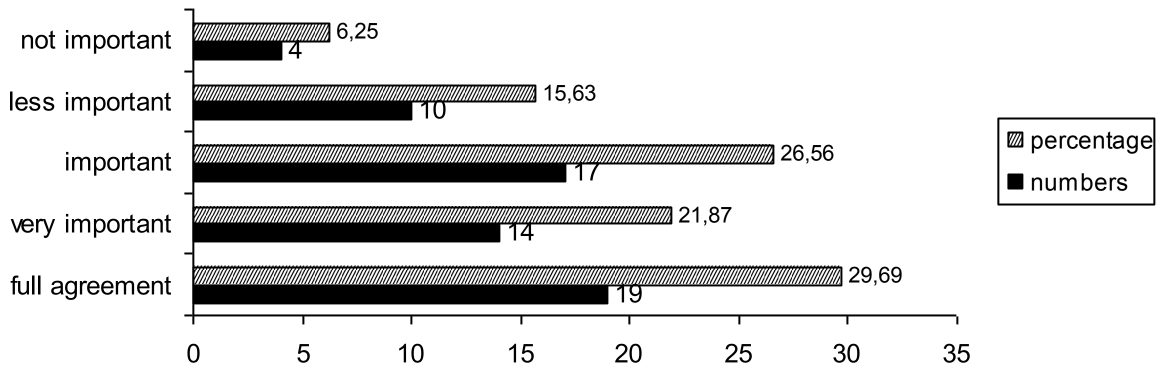


This is all the more relevant when we see that 92.76% of respondents claim to prefer direct communication with the management (classified as at least "important").



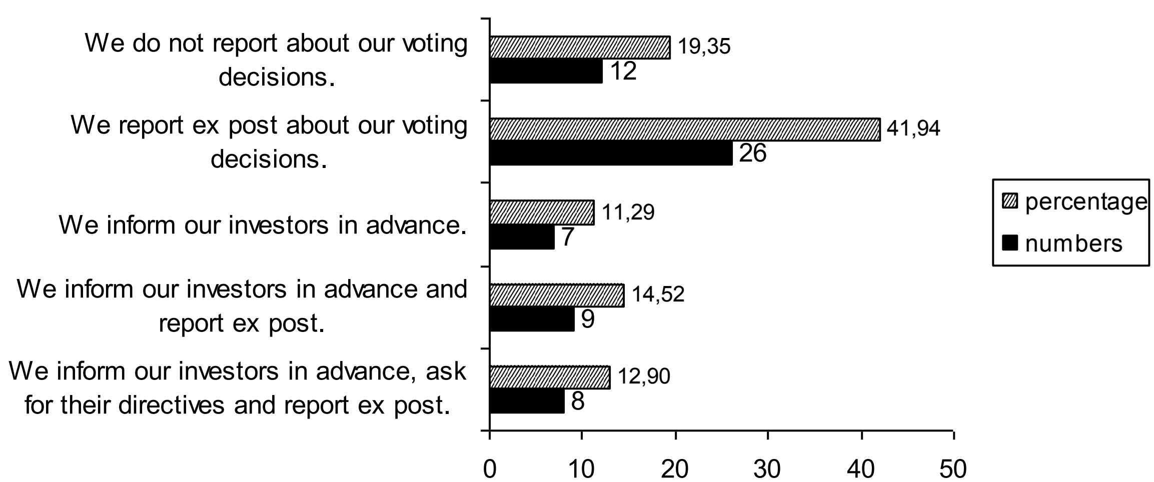
Yet the disclosure decision and information policy of investors may vary. 76.52% responded to the statement that they issue information about their voting behaviour only on a selective basis with at least "important". This could be the case if criticism or even rejections are involved.

Question 4.6
We inform companies and other investors about our voting behaviour only on a selective basis.



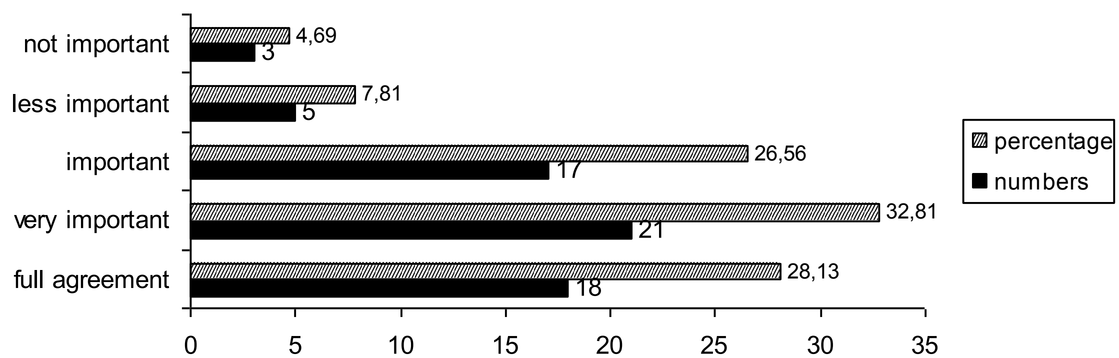
There are various possibilities for informing beneficiaries of the fiduciary exercise of votes. 19.35% of respondents said that they do not report at all; 41.94% only report ex post; 11.29% provide information in advance; 14.52% do both; and only 12.9% inform their investors in advance, ask for their directives and report ex post. Thus further support is lent to critics who complain about the lack of transparency in the use of voting rights by fiduciary investors.

Question 4.7
In the fiduciary exercise there are various possibilities for informing your beneficiaries.

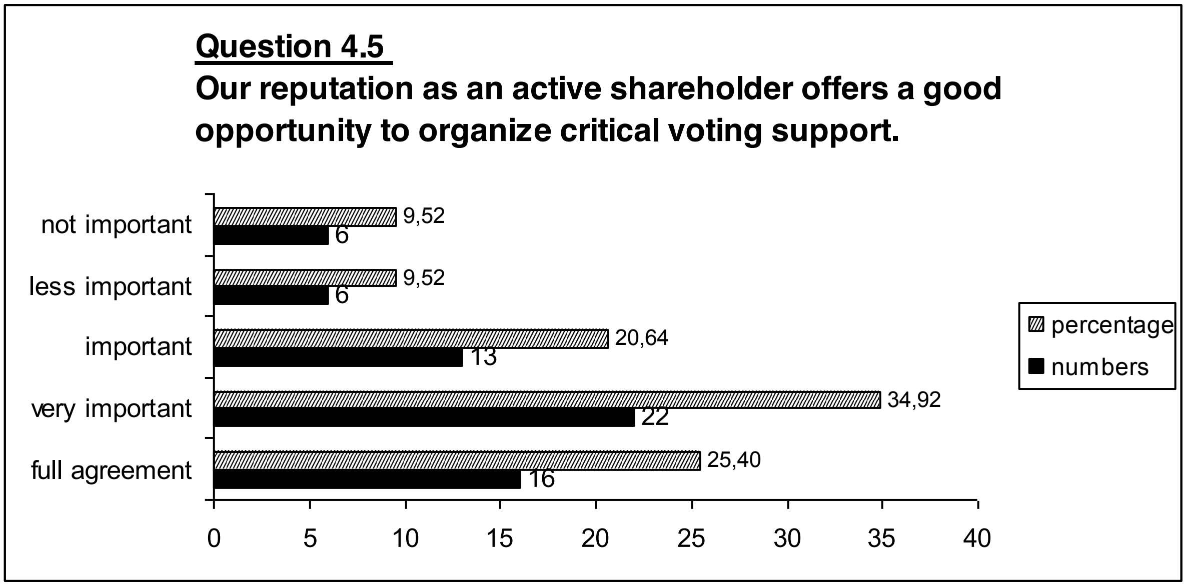


Firms often publicly criticise private investors who use the general meeting as a stage for expressing personal and usually political opinions. However, institutional investors also make use of this opportunity to attract public attention for their own purposes, as this can increase their influence on the management. This statement was considered by 81.2% of respondents as at least "important".

<u>Question 4.3</u>
The general meeting offers a good stage for public attention. This increases the influence on companies.



Another element considered was the reputation of the institutional investor itself. Respondents were asked to comment on whether they agreed with the hypothesis that a reputation as an active shareholder increases the opportunities to organise critical voting support. Here, too, an impressive 92.71% majority felt that this was at least "important".



Transfer of voting rights

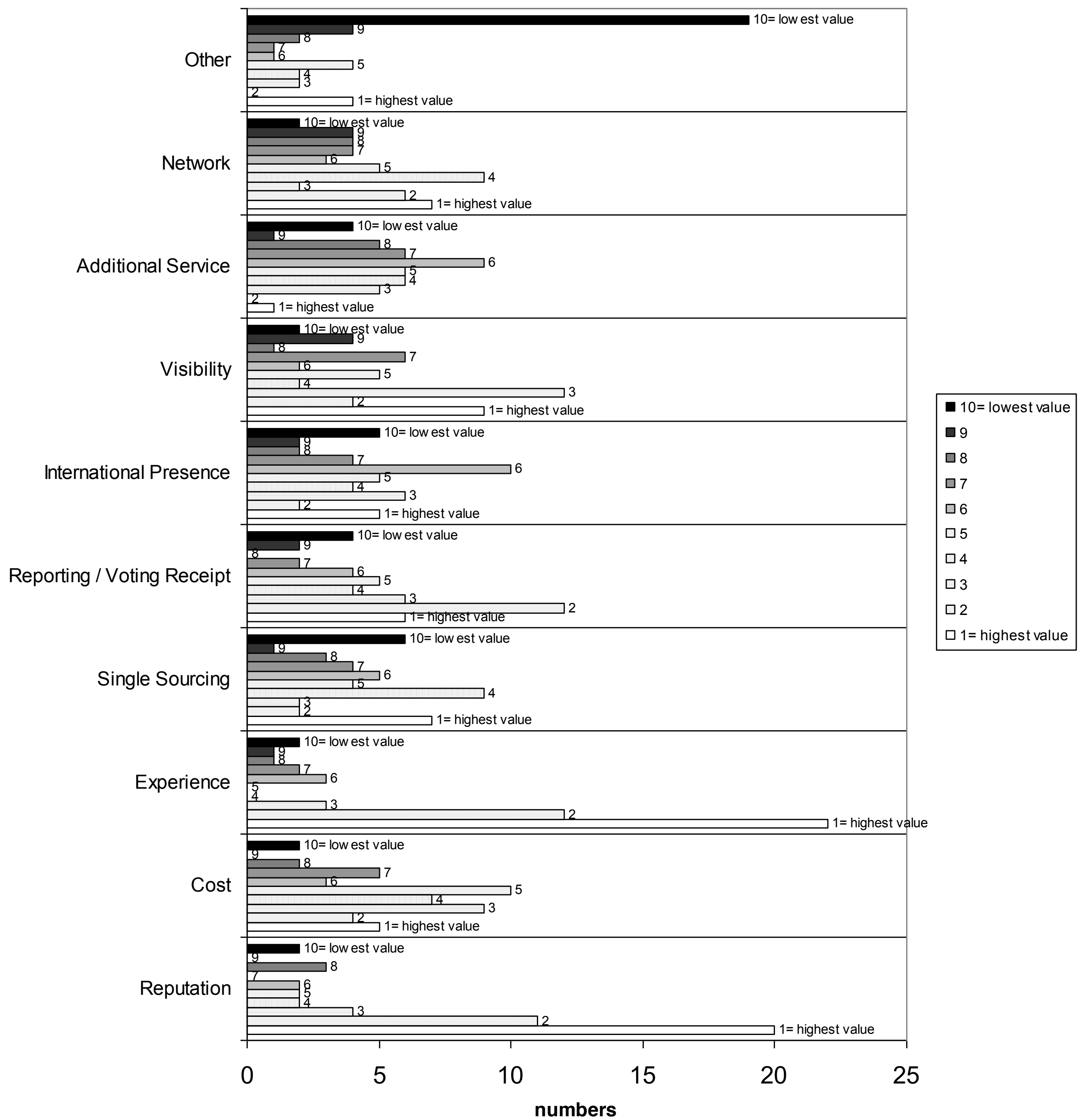
(Question 5-5.3)

The interesting thing about the transfer of voting rights to other fiduciaries is how these fiduciaries are selected and how information is provided in such cases.

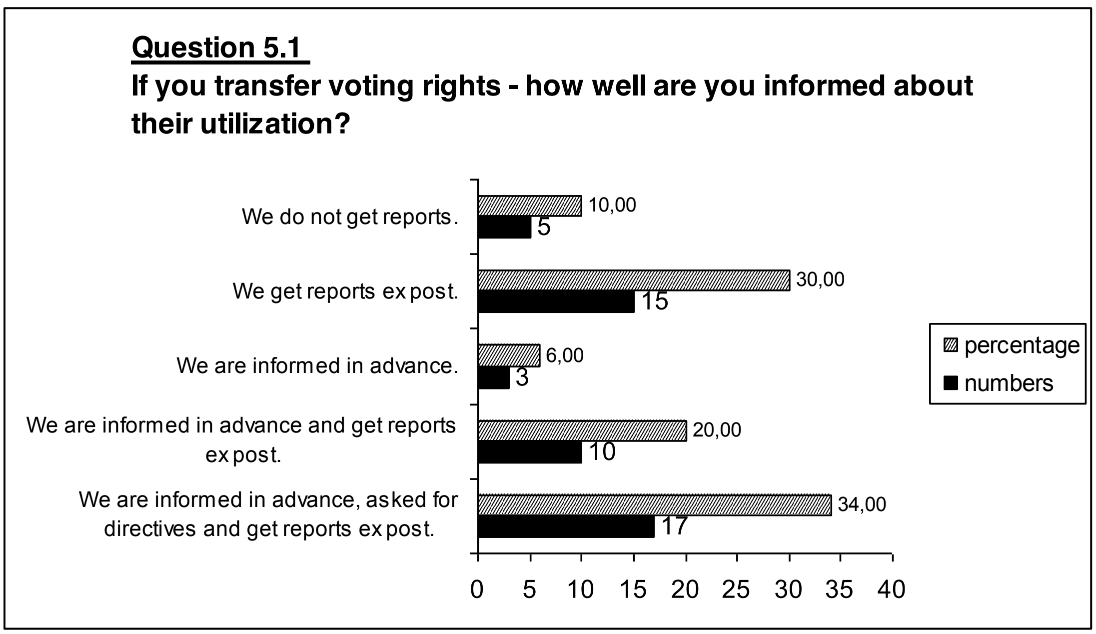
The first task for this group of respondents was to evaluate the criteria which influence their selection. They were asked to evaluate the criteria of reputation, cost, experience, single sourcing, reporting/voting receipt, international presence, visibility, additional service, network and other on a scale of 1 to 10 (due to the larger number of criteria), with 1 being the highest value. The results show that the respondents consider some criteria to be significantly more important than others. Both experience and reputation were ranked number one, the highest level of relevance, by over 40% of respondents. The overall ranking for the criteria is as follows: 1.) reputation and experience, 2.) reporting/voting receipt and visibility, 3.) cost and network, 4.) single sourcing, 5.) international presence and additional service and 6.) other. We can take this as an indication that reputation and experience as an active shareholder are very important.

Question 5

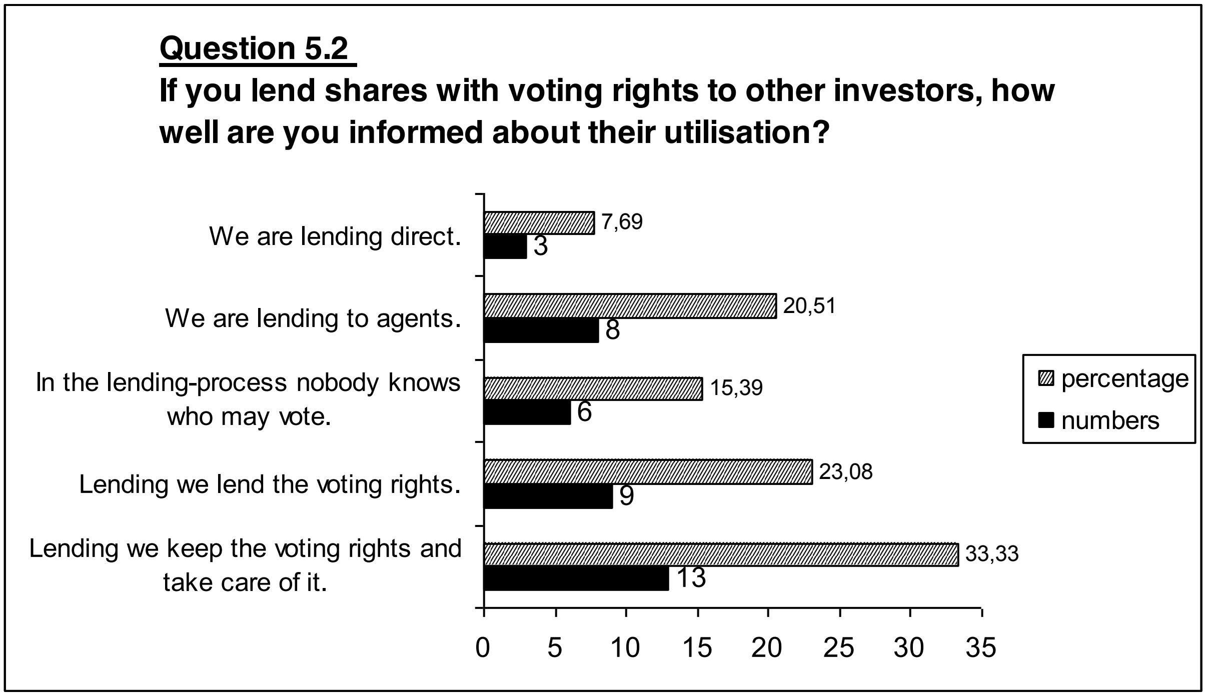
If you give your voting rights to other fiduciaries, what are the criteria that influence your selection?



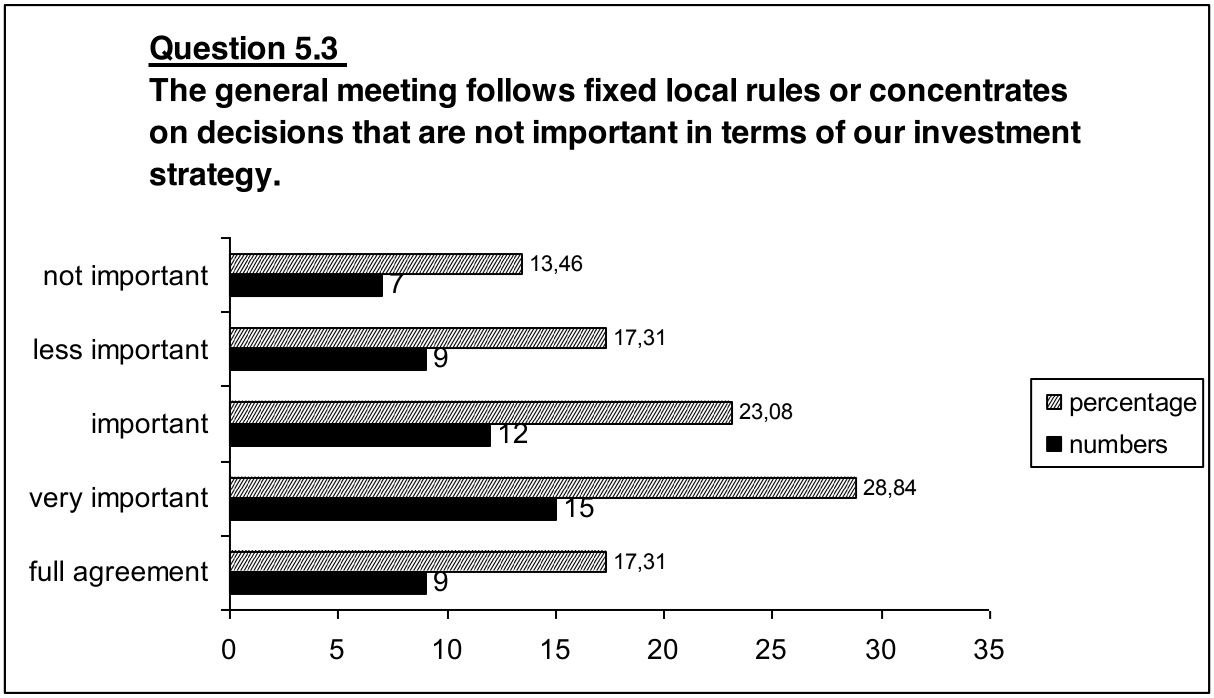
If they transfer voting rights, respondents were also asked to assess how well and comprehensively they are informed about the use of these rights. As with the series of questions directed at investors which exercise voting rights directly, the respondents could select their answer from five levels of information: (1) they are informed in advance, asked for directives and get reports ex post. (2) They are informed in advance and get reports ex post. (3) They are informed in advance. (4) They get reports ex post. (5) They do not get reports. The smallest group with just 6% were those who were only informed in advance (3). By contrast, 30% receive reports after the voting rights have been used and 10% do not receive any reports. 20% of respondents receive information in advance and additional reports after the voting rights have been used. However, at 34% most of the respondents who transferred voting rights are well informed about their use, as they receive information in advance, are asked for directives and get reports ex post. This paints a much better picture.



If investors lend shares with voting rights to other investors, they were then asked how well they were informed about the use of these rights. They were able to choose between the following grades: (1) when lending, we retain and take care of the voting rights. (2) We also lend voting rights. (3) In the lending process nobody knows who may vote. (4) We lend to agents. (5) We lend directly. One third, and therefore most of respondents, retain the voting right and take care of it themselves. Although this can be interpreted as a value indicator, it is contradicted by the fact that approximately 15% of respondents assume that it is unclear who may vote in the lending process.



Yet this could also be due to the fact that the general meeting only votes on certain decisions, which might not be classified as relevant. Participants are therefore asked for their view on the following statement: "the general meeting follows fixed local rules or concentrates on decisions that are not important in terms of our investment strategy". The evaluation showed that over 70% considered this statement to be at least "important". The respondents therefore clearly tend towards agreement with the statement.



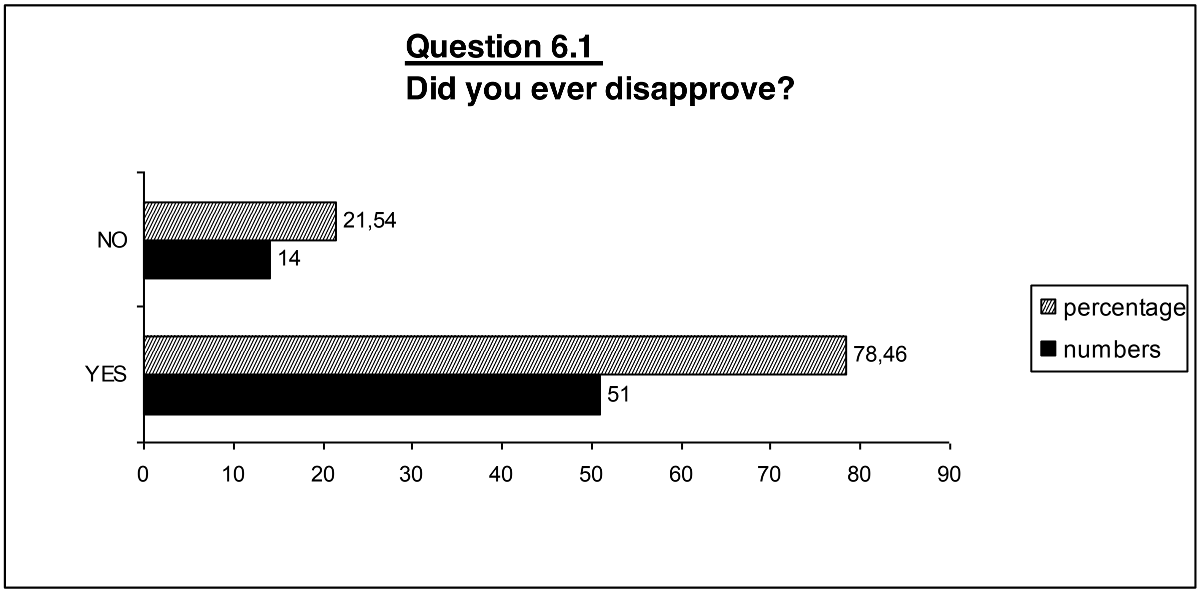
Another indicator for assessing the relevance of general meetings or the decisions already made is the current voting behaviour.

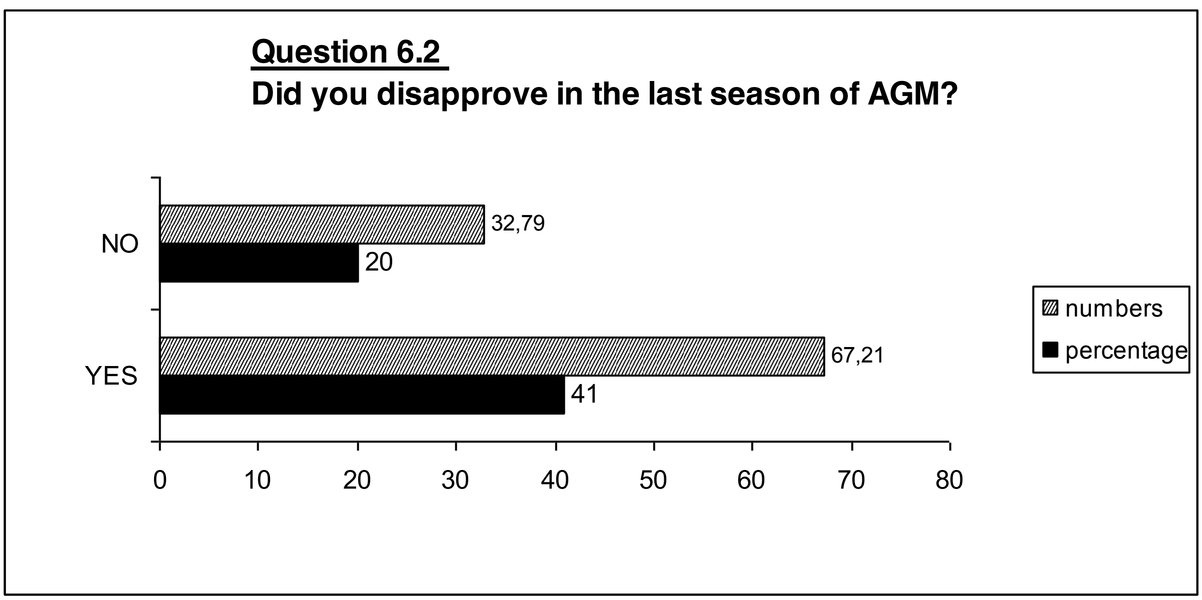
Voting behaviour 2008

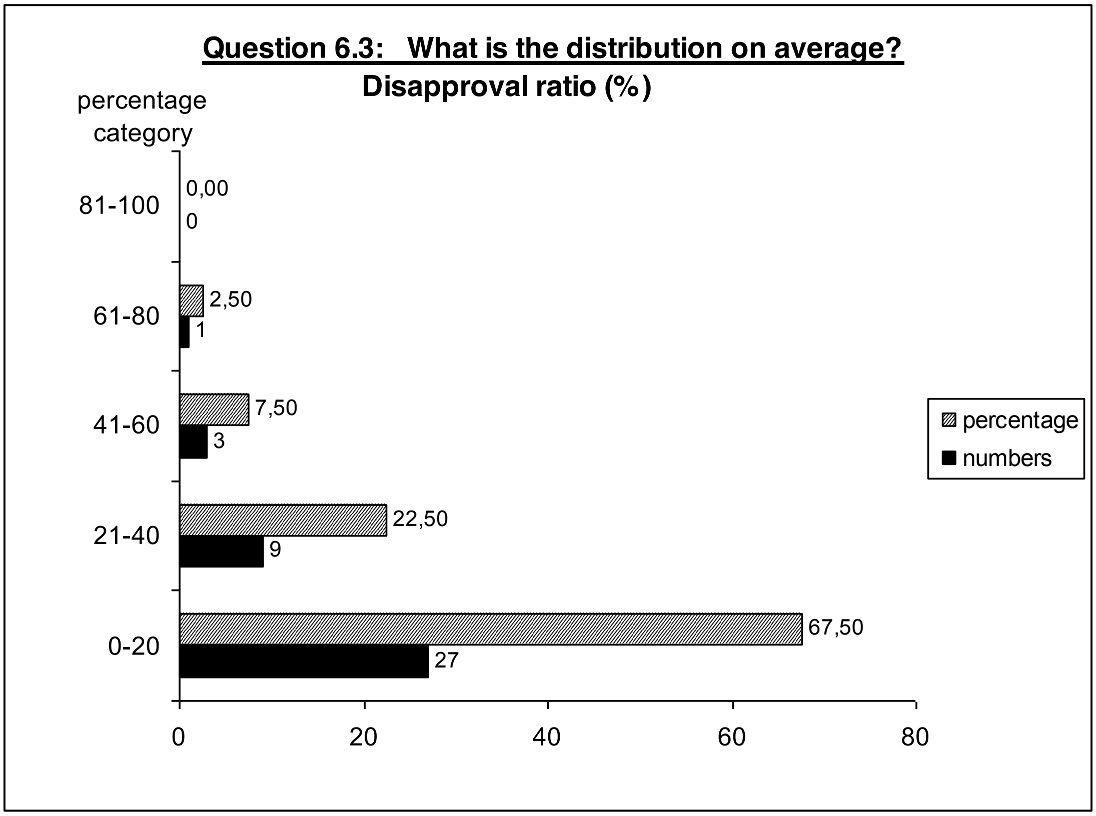
(Question 6-6.3)

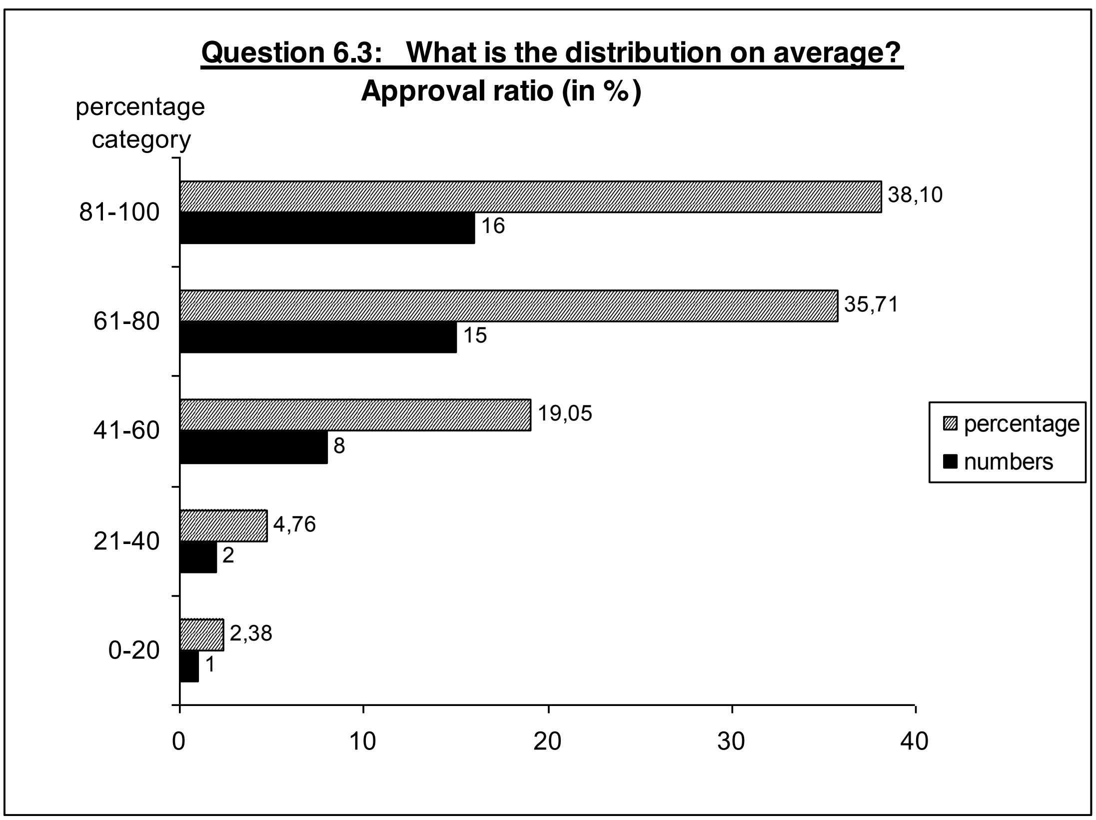
The first question asked was whether the respondents had expressed disagreement in the 2008 season, or indeed at all. 78% answered this question in the affirmative. In addition, around 67% had expressed disagreement in the last round of general meetings. Respondents were then requested to assess how often they expressed approval and disapproval, and how often they abstained, giving a ratio value for all three cases. We see that over 70% gave an abstention ratio of under 10%, meaning that respondents seldom use the option of withholding a vote. Instead they express approval or disapproval at the general meeting. Over

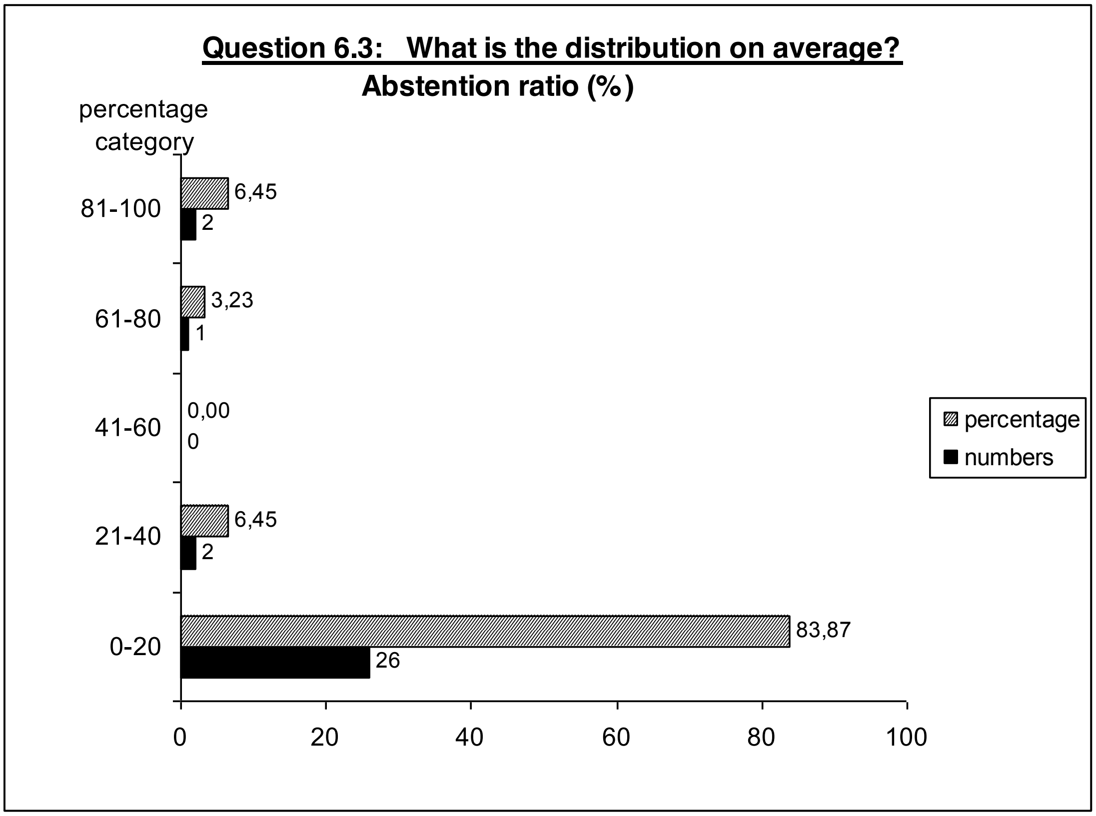
85% of respondents stated a value greater than 50% for their approval rate and a value of less than 30% for their disapproval rate.






Question 6.3: What is the distribution on average?
Disapproval ratio (%)
percentage category
81-100
61-80
41-60
21-40
0-20
0,00
0
2,50
1
7,50
3
22,50
9
67,50
27
0
20
40
60
80
percentage
numbers


Question 6.3: What is the distribution on average?
Approval ratio (in %)
percentage category
81-100
61-80
41-60
21-40
0-20
38,10
16
35,71
15
19,05
8
4,76
2
2,38
1
0
10
20
30
40
percentage
numbers



The relatively high disapproval values are surprising. As such, the subsequent questions which deal with the decision-making process behind voting behaviour demand particular attention.

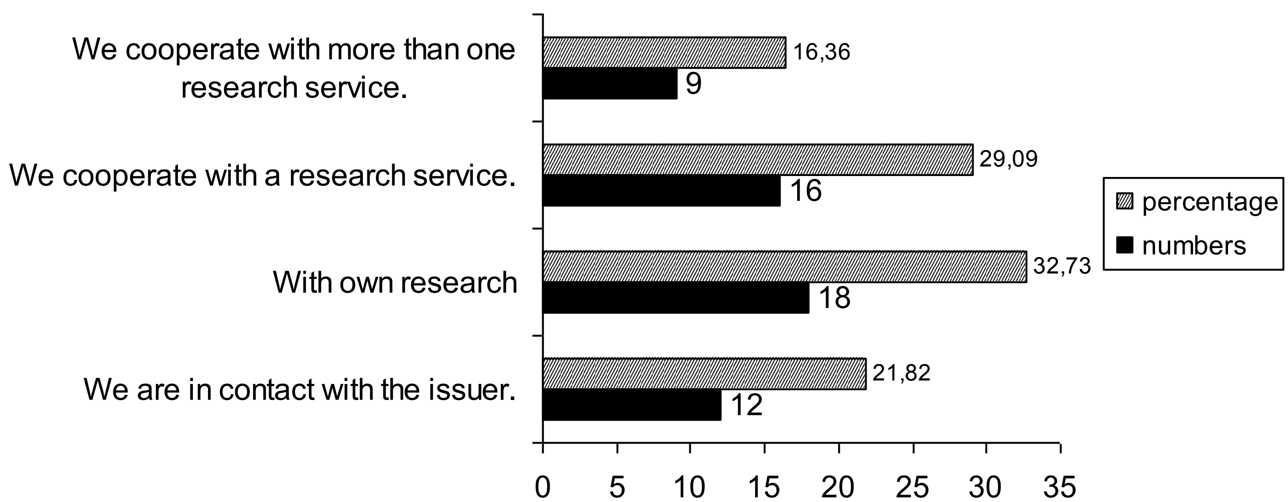
Voting decisions

(Question 7.1-7.3)

The first issue considered is that institutional investors make use of support from different parties to make their voting decisions, such as shareholders' associations. What we are interested in here is how they support the actual decision-making process concerning their votes. Respondents could choose from the following answers: (1) we are in contact with the issuer. (2) We use our own research. (3) We cooperate with a research service. (4) We cooperate with more than one research service.

Over 30% use their own research to make decisions, while over 45% cooperate with at least one research service. Of these, most use just one research service rather than several. By contrast, contact with the issuer is only considered helpful in the decision-making process by just under 22% of respondents.

Question 7.1
How do you support the decision process concerning your votes?

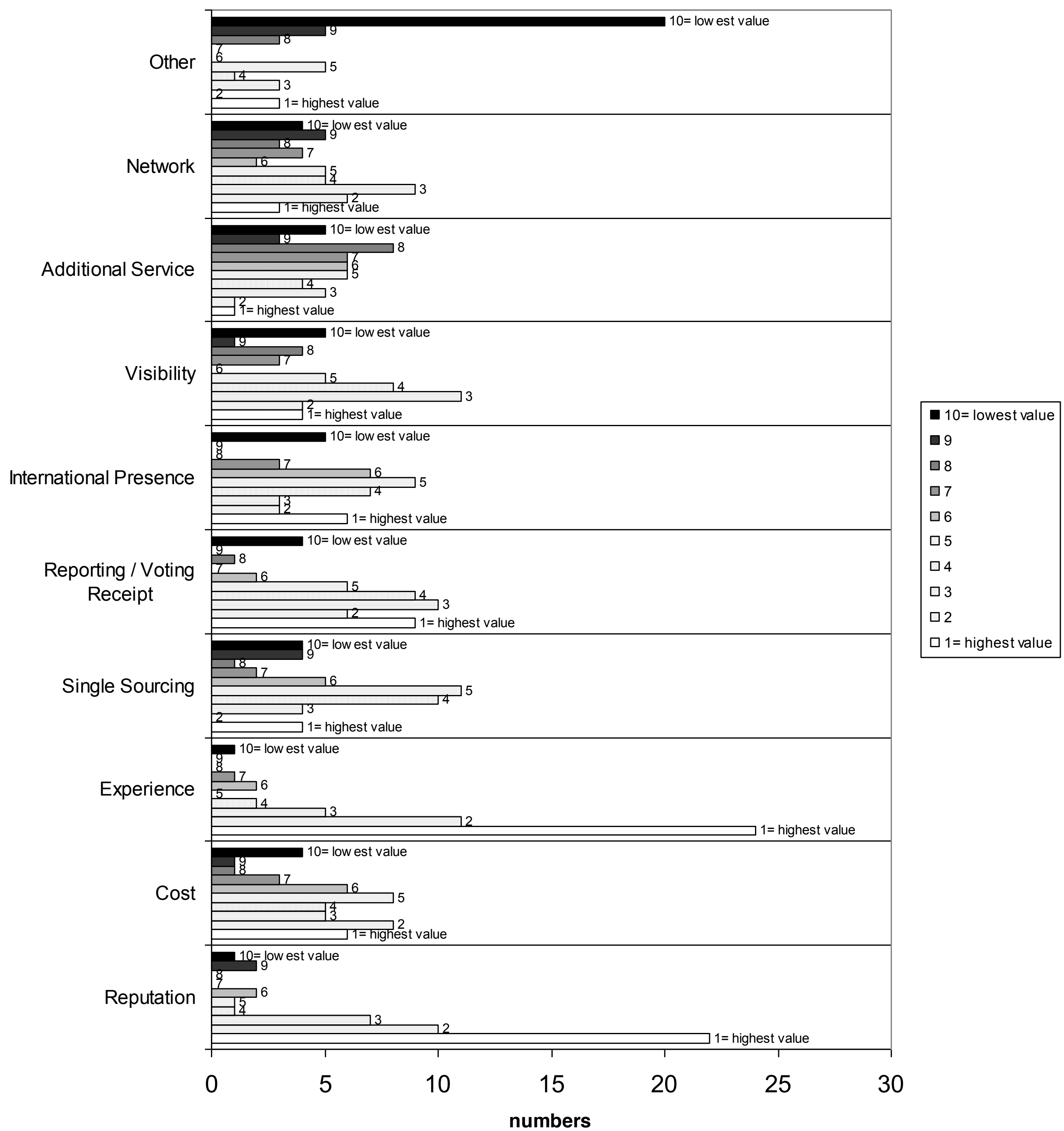


The significance attached to external support raises the question of which criteria influence its selection. Respondents were therefore asked to rate the following criteria in terms of their influence or relevance to the vote on a scale of 1 to 10, whereby 1 is the most relevant: reputation, cost, experience, single sourcing, reporting/voting receipt, international presence, visibility, additional service, network and other.

The frequency distributions of the criteria indicate that certain ones are more relevant than others in the eyes of the respondents. The median values were used to rank the evaluation criteria for providers as follows: 1.) experience, 2.) reputation, 3.) reporting/voting receipt, 4.)

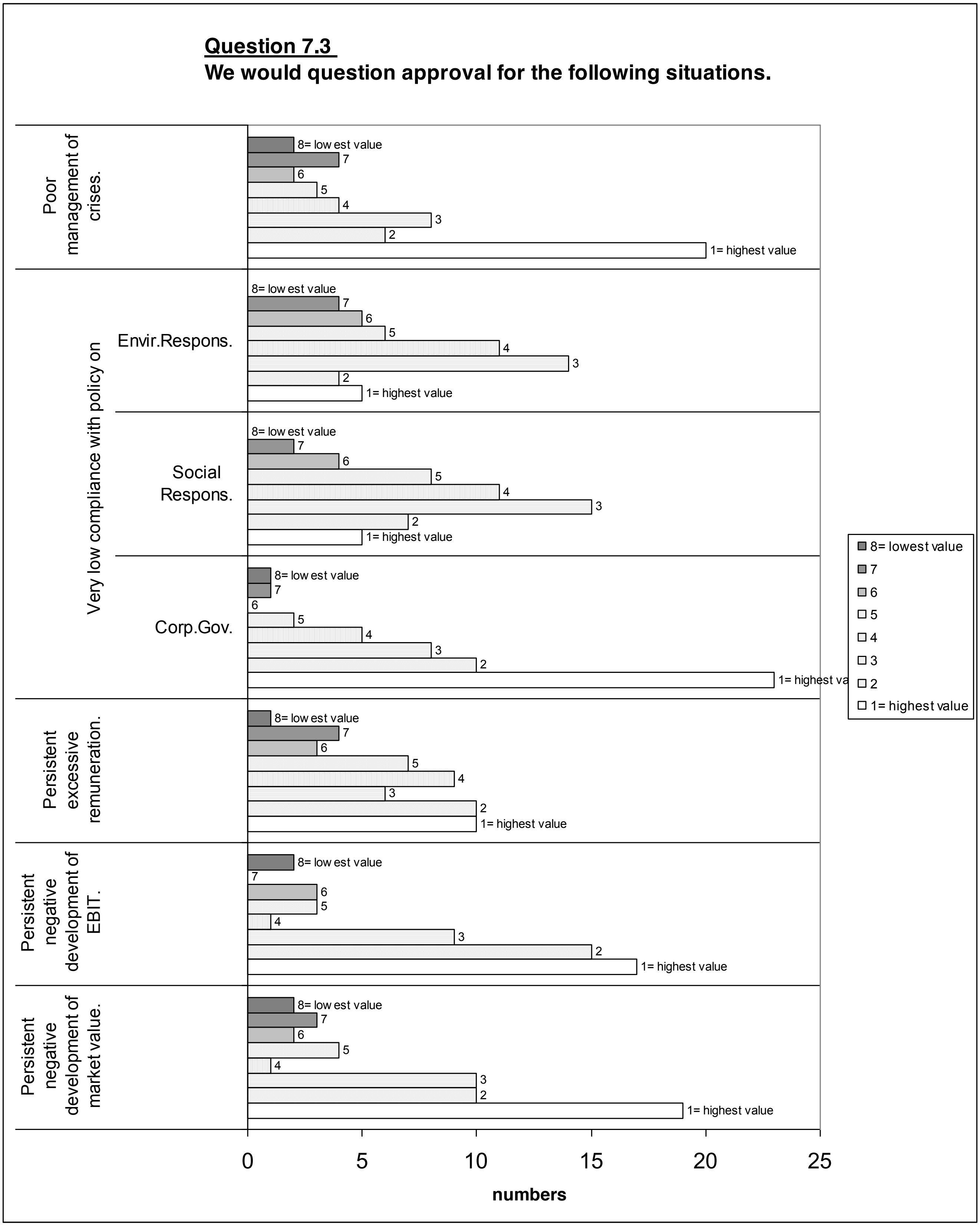
cost and visibility, 5.) network, 6.) single sourcing and international presence, 7.) additional service and 8.) other. As such, the respondents made their selection based primarily on experience and reputation. This corroborates the results for the selection of fiduciaries when transferring voting rights.

Question 7.2
What are the criteria that influence your selection?



We also examined which situations could raise doubts concerning approval at the general meeting. The following situations were given as alternatives: (1) persistent negative development of market value. (2) Persistent negative development of EBIT. (3) Persistent excessive remuneration. (4) Very low compliance with policy on a) corporate governance, b) social responsibility and c) environmental responsibility. (5) Poor management of crises. The situations were to be assessed on a scale of 1 to 8, whereby 1 is the most relevant value.

Overall, the respondents agreed with all the situations described. Unlike the previous question, however, it was not possible to rank the situations. However, the trend towards agreement was not as apparent for situations 3, 4b and 4c as for the other situations, which is reflected in a higher median value. This reveals that individual elements of ESG aspects are of a lesser significance: pay models, social and environmental responsibility. However this may also be a reflection of the fact that these aspects are not dealt with at general meetings, but rather in direct communication.


Question 7.3
We would question approval for the following situations.
Poor management of crises.
Very low compliance with policy on
Envir.Respons.
Social Respons.
Corp.Gov.
Persistent excessive remuneration.
Persistent negative development of EBIT.
Persistent negative development of market value.
8= lowest value
7
6
5
4
3
2
1= highest value
0
5
10
15
20
25
numbers

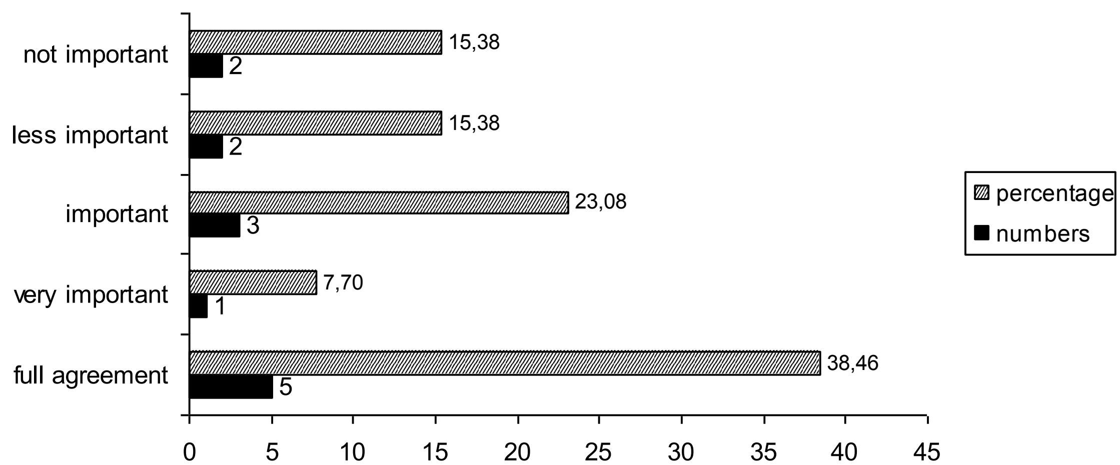
Hedge funds

(Question 8.1-8.3)

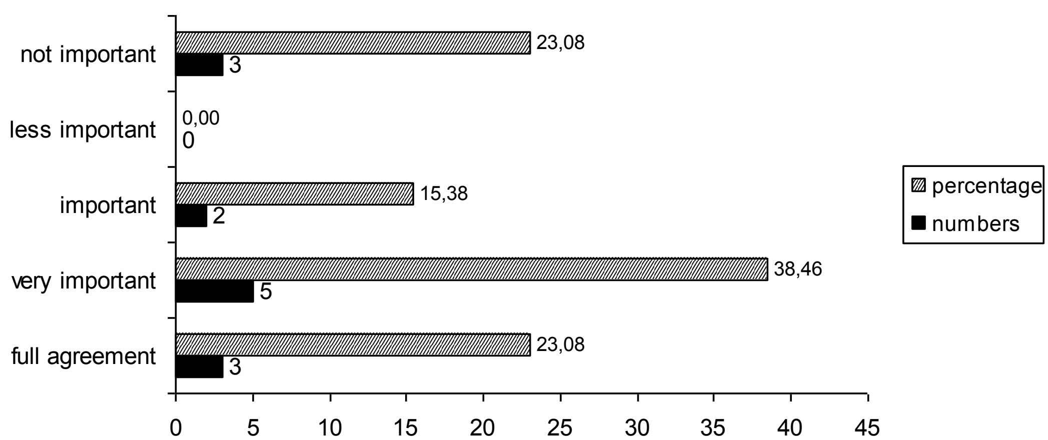
Hedge funds play a special role, in that they also pursue short-selling strategies with loaned shares. Section eight of the questionnaire therefore deals with the question of whether the transfer of voting rights is guaranteed in connection with hedge funds, which are involved in short-selling strategies with externally financed shares, and, if so, whether these voting rights are used. The respondents were asked to specify how strongly they agree with the following three statements: (1) we guarantee the transfer of voting rights – we value and utilise the voting rights. (2) In case of short-selling strategies we do not utilise voting rights. (3) Utilising voting rights has prohibitively high transaction costs. A five-step scale was used: full agreement, very important, important, less important, not important. This resulted in the following frequency distributions for the three statements:

Over 85% consider question 8.1 as important. However, there were no significant differences between the steps "important", "very important" and "full agreement". Yet when short strategies are used, the voting right loses importance. This is evident from the fact only just under 70% consider (2) to be at least important. That said, just under 40% were in full agreement with the statement that they do not use voting rights in the event of short-selling strategies. This lends no support to critics who expect that in the hands of hedge funds, the voting right could be used to the detriment of the company in short-selling operations. The high transaction costs involved in utilising voting rights were considered as at least important by over 75% of respondents. Correspondingly, over 20% considered the high transaction costs to be unimportant. It must be noted, however, that these questions were only to be answered by survey participants which also represent a hedge fund. For this reason, only a few of the participants answered section 8, meaning that the results are less well suited to generalisation and merely reflect the opinion of those questioned.

Question 8.2
In case of short-selling strategies we do not utilize voting rights.



Question 8.3
Utilizing voting rights has prohibitively high transaction costs.



Role of general standards

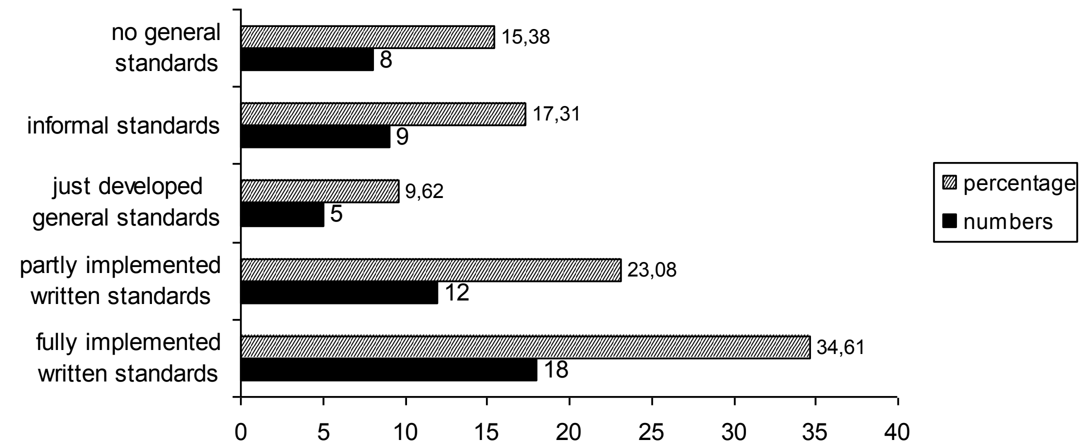
(Question 9.1-9.4)

Both institutional investors and various external organisations develop general standards for different areas – for investment strategies, active control, crises and share lending. What we are interested in is whether and to what extent the respective standards are being used. We therefore examined whether the firms in which the respondents work have general standards regarding (1) investment strategy, (2) active control of portfolio enterprises and (3) alert situations. The question distinguished between whether written standards had been fully or only partly implemented, general standards had only just been developed, informal standards were in place or no general standards were used.

Overall it was shown that general standards concerning investment strategies are more widely distributed than others in the companies surveyed, as just under 60% had at least partly implemented written standards for this. By contrast, only just under 40% of companies had implemented at least written general standards for active control or alert situations. Instead, over 45 firms or 50% have at most informal standards for these situations. For all situations, the results show that either general standards have been fully or partly implemented in writing or only informal standards are available, if at all. On the other hand, there are only a few companies which have just developed general standards.

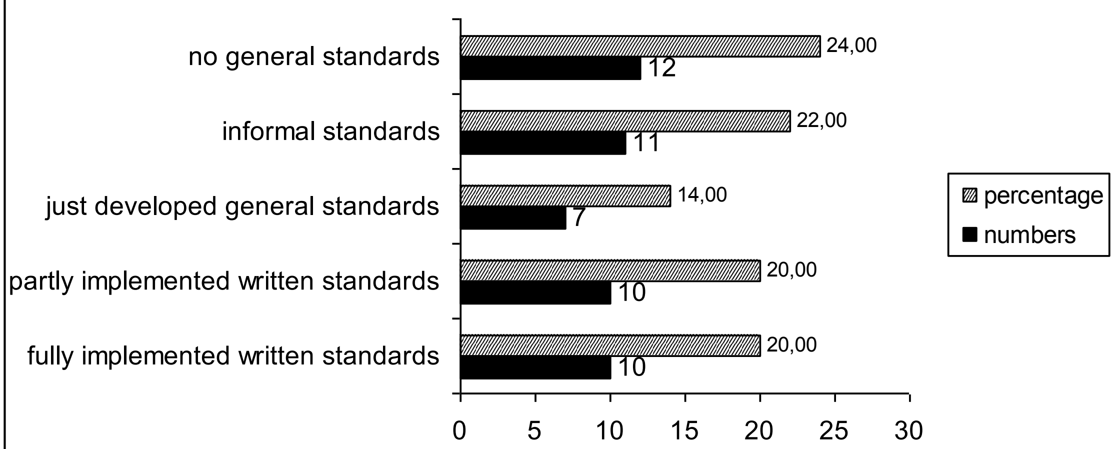
Question 9.1

Does your company follow a general standard concerning the investment strategy?



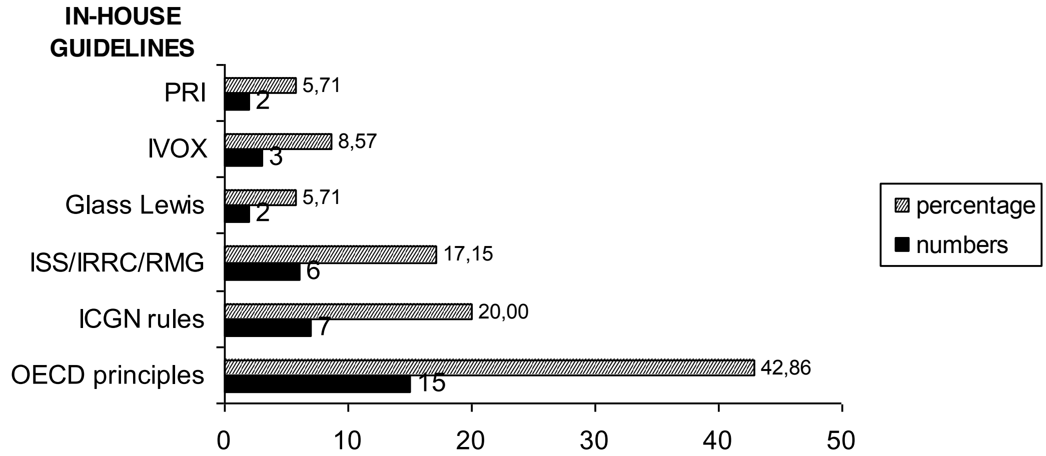
Question 9.2

Does your company follow a general standard concerning active control of portfolio enterprises?



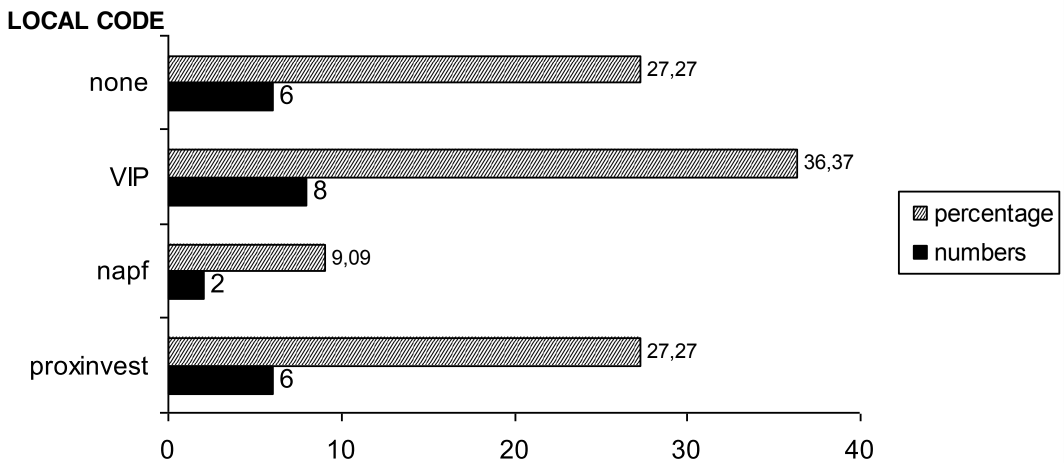
Question 9.2.2

Does your company follow a general standard concerning active control of portfolio enterprises?



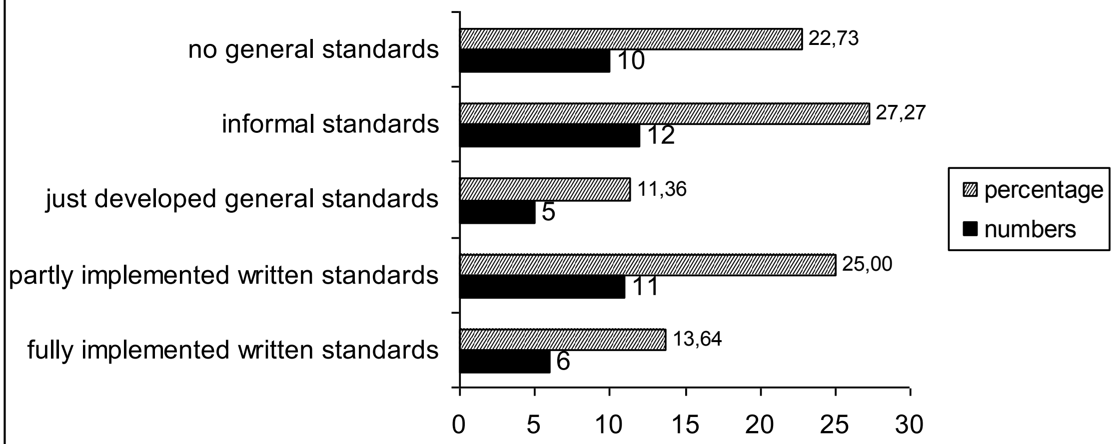
Question 9.2.4

Does your company follow a general standard concerning active control of portfolio enterprises?



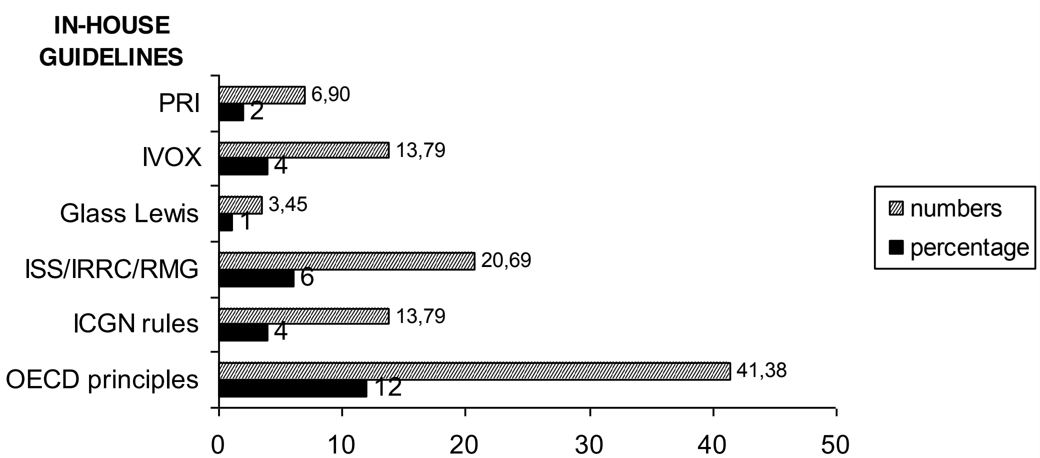
Question 9.3

Does your company follow a general standard concerning alert situations?

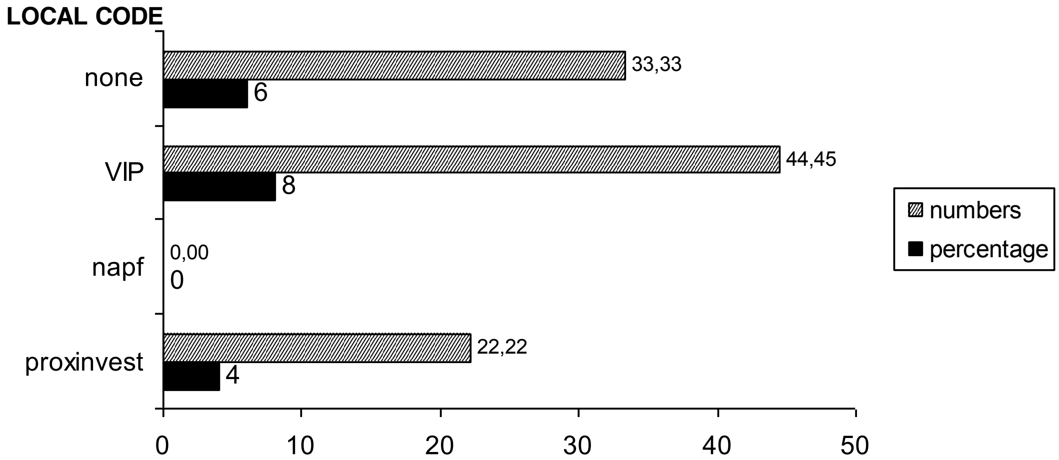


Question 9.3.2

Does your company follow a general standard concerning alert situations?



Question 9.3.4
Does your company follow a general standard concerning alert situations?



In addition, the respondents on general standards were also questioned on their in-house guidelines or local code with regard to points (2) and (3). The in-house guidelines they could choose from were as follows: OECD principles, ICGN rules, ISS/IRRC/RMG, Glass Lewis, IVOX or PRI. For the local codes, the following four options were available: Proxinvest, Napf, VIP or none. In both situations, over 40% of firms use the OECD principles as their in-house guidelines. Likewise in both situations, it was revealed that the Glass Lewis and PRI guidelines were each used by less than 7% of the firms. The only differences between the two situations were in the second most frequently used guidelines. While 20% of the firms apply the ISS, IRC or RMG guidelines as general standards in alert situations after the OECD principles, the second most common general standards for the active control of portfolio enterprises are the ICGN rules (also applied by 20% of the companies).

As for the local codes, around 30% of firms do not use one in either situation. Both situations show a similar distribution, with VIP as the most frequently used local code, followed by no local code and Proxinvest. Only a minority of companies use Napf as their local code. It should be noted that none of the companies use Napf as their local code for alert situations.

5. Summary

Voting behaviour and general meetings are tools which institutional investors can use to actively control management and are therefore relevant corporate governance instruments. They both reduce imbalances of information and are a democratic means of resolving conflicts of interest. Which makes it all the more surprising that scientific discussion of this topic is relatively scant and also focuses mainly on criticising the running of general meetings and their possible causes. This survey enabled us to obtain the first important new findings, both confirming existing plausible assumptions and disclosing surprising theories. The latter in particular present valuable starting points for further research.

It was established that voting rights are valued and that this value can be validly recorded by means of discounts for preference shares. However, the use of voting rights is influenced by the respective investment strategy; for instance personal communication has a dominating influence on soft ESG value drivers. There is a broad consensus regarding the priority of the ESG sub-aspects, with sustainability, health and safety, and reporting on conflicts of interests playing a dominant role. It became clear that investors also call firms to account in these aspects. So it is surprising then that conduct is so reticent as regards transparency and disclosure.

In addition to voting rights, the general meeting also plays its part as an event. Individual activists and institutional investors alike use the general meeting as a stage for playing to the public to better reach their own goals. At the same time, the public appearance is used to strengthen the investor's own reputation, as it is seen as an important aid in forming critical majorities. Even when voting rights are transferred, reputation and experience play an important role in the selection. If reputation is interpreted as an indicator for or of credibility, then it is clear that both one's own reputation and that of cooperation partners is ascribed a strong relevance. In keeping with companies' own reticence to disclose information, the study revealed that investors are also quite poorly informed, even if they transfer their voting rights. However, when shares are lent, 30% do not include their voting rights in the loan.

Due to the financial crisis, the 2008 general meeting season can certainly not be taken as representative, which is why past years were also included in the voting behaviour recorded. It is surprising that 78% claim to have expressed disapproval on at least one occasion. This is due more to poor economic performance than to a criticism of ESG policies.

External support is often sought when deciding on voting behaviour. Here too, experience and reputation are the deciding selection factors. At the same time, there is a strong orientation towards general standards within investment, controlling and crisis strategies.

In conclusion, we can say that within the asset management industry, behaviour at general meetings (valuation/attitude, attendance habits, exercise of voting rights, secure procedures or placebo products, decision making, etc.) is certainly valued by each individual as part of their personal fiduciary responsibility. At decision-making level, ethical compliance appears to stand little chance when faced with ingrained practical and formal considerations regarding cost and reputation.

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Appendix