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Promoting Long-Term Value Creation – The Launch of the Investor Stewardship Group (ISG) and ISG’s Framework for U.S. Stewardship and Governance

A long-running, two-year effort by the senior corporate governance heads of major U.S. investors to develop the first stewardship code for the U.S. market culminated today in the launch of the [Investor Stewardship Group](#) (ISG) and ISG’s associated [Framework for U.S. Stewardship and Governance](#). Investor co-founders and signatories include U.S. Asset Managers (BlackRock; MFS; State Street Global Advisors; TIAA Investments; T. Rowe Price; Vanguard; ValueAct Capital; Wellington Management); U.S. Asset Owners (CalSTRS; Florida State Board of Administration (SBA); Washington State Investment Board); and non-U.S. Asset Owners/Managers (GIC Private Limited (Singapore’s Sovereign Wealth Fund); Legal and General Investment Management; MN Netherlands; PGGM; Royal Bank of Canada (Asset Management)).

Focused explicitly on combating short-termism, providing a “framework for promoting long-term value creation for U.S. companies and the broader U.S. economy” and promoting “responsible” engagement, the principles are designed to be independent of proxy advisory firm guidelines and may help disintermediate the proxy advisory firms, traditional activist hedge funds and short-term pressures from dictating corporate governance and corporate strategy.

Importantly, the ISG Framework would operate to hold investors, and not just public companies, to a higher standard, rejecting [the scorched-earth activist pressure tactics to which public companies have often been subject](#), and instead requiring investors to “address and attempt to resolve differences with companies in a constructive and pragmatic manner.” In addition, the ISG Framework emphasizes that asset managers and owners are responsible to their ultimate long-term beneficiaries, especially the millions of individual investors whose retirement and long-term savings are held by these funds, and that proxy voting and engagement guidelines of investors should be designed to protect the interests of these long-term clients and beneficiaries. The divergent needs and time horizons of these ultimate beneficiaries have long been emphasized by Chief Justice Leo Strine (see, for example, Justice Strine’s provocative article, *Can We Do Better by Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law*), and implicates the [new theory of corporate governance](#) espoused by Professors Zohar Goshen and Richard Squire. While the ISG Framework is not intended to be prescriptive or comprehensive in nature, with companies and investors being free to apply it in a manner they deem appropriate, it is intended to provide guidance and clarity as to the expectations that an increasingly large number of investors will have not only of public companies, but also of each other.

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Key highlights of the ISG Stewardship Framework for Institutional Investors and the ISG Corporate Governance Framework for U.S. Listed Companies are outlined below. The ISG has also supplemented each of these high-level principles with examples of illustrative implementation. Many of the principles in the ISG Frameworks will be familiar to those who have recognized the emergence of, and supported, [The New Paradigm: A Roadmap for an Implicit Corporate Governance Partnership Between Corporations and Investors to Achieve Sustainable Long-Term Investment and Growth](#), sought to [adapt their communication, engagement and governance practices](#) to reflect the New Paradigm and [tracked the heightened expectations and scrutiny placed on public company boards](#).

Stewardship Framework for Institutional Investors

- Principle A: Institutional investors are accountable to those whose money they invest.
- Principle B: Institutional investors should demonstrate how they evaluate corporate governance factors with respect to the companies in which they invest.
- Principle C: Institutional investors should disclose, in general terms, how they manage potential conflicts of interest that may arise in their proxy voting and engagement activities.
- Principle D: Institutional investors are responsible for proxy voting decisions and should monitor the relevant activities and policies of third parties that advise them on those decisions.
- Principle E: Institutional investors should address and attempt to resolve differences with companies in a constructive and pragmatic manner.
- Principle F: Institutional investors should work together, where appropriate, to encourage the adoption and implementation of the Corporate Governance and Stewardship principles.

Corporate Governance Framework for U.S. Listed Companies

- Principle 1: Boards are accountable to shareholders.
- Principle 2: Shareholders should be entitled to voting rights in proportion to their economic interest.
- Principle 3: Boards should be responsive to shareholders and be proactive in order to understand their perspectives.

- Principle 4: Boards should have a strong, independent leadership structure, which may be evidenced by an independent chair or a lead independent director.
- Principle 5: Boards should adopt structures and practices that enhance their effectiveness.
- Principle 6: Boards should develop management incentive structures that are aligned with the long-term strategy of the company.

ISG's goals are ambitious, seeking to have "every institutional investor and asset management firm investing in the U.S." sign the framework and incorporate the stewardship principles in their proxy voting, engagement guidelines and practices. It should be noted that while the ISG guidelines emphasize the need for a framework to promote long-term value creation, the current version does not specifically commit investors to support long-term investment but does express the view that it "is the fiduciary responsibility of all asset managers to conduct themselves in accordance with the preconditions for responsible engagement in a manner that accrues to the best interests of stakeholders and society in general, and that in so doing they'll help build a framework for promoting long-term value creation on behalf of U.S. companies and the broader U.S. economy."

The Framework is intended to be effective January 1, 2018 and apply to the 2018 proxy season; nevertheless, as companies conduct off-season and in-season shareholder engagement and finalize their 2017 proxy statement disclosures and associated annual letters to shareholders from the Board and/or management, they may wish to incorporate into their communications some of the themes highlighted in the ISG Framework and benchmark their disclosures and practices against the Framework.

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