THE
INVESTMENT
ASSOCIATION

The Investment Association Guidelines on Responsible Investment Disclosure

January 2007
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The Investment Association is a company limited
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Following the merger of ABI Investment Affairs with the IMA on 30th June, 2014, the enlarged Investment Management Association (IMA), which was renamed The Investment Association in January 2015, has assumed responsibility for guidance previously issued by the ABI.

Background and Introduction

Public debate on corporate responsibility and new legislation in both the EU and UK has furthered understanding of corporate responsibility to the point where it seems helpful for institutional shareholders to set out fresh disclosure principles, which will guide them in assessing narrative reporting and seeking to engage with companies in which they invest.

The guidelines below are a modification of the Socially Responsible Investment Guidelines launched by the ABI in 2001. They take account of the EU Accounts Modernisation Directive and the UK Companies Act, as well as recent experience of narrative reporting and the clarification by the UK Government of directors' liability for narrative statements. They do not involve substantial change but aim to highlight aspects of responsibility reporting on which shareholders place particular value. This is narrative reporting which:

- sets environmental, social and governance (ESG)[1] risks in the context of the whole range of risks and opportunities facing the company;
- contains a forward looking perspective; and
- describes the actions of the board in mitigating these risks.

Institutional shareholders are anxious to avoid unnecessary prescription or the imposition of costly burdens, which can restrict the ability of companies to generate returns. They do not intend that these modified guidelines should add to the reporting burden facing companies, but rather that they should help companies understand and respond to the needs of investors when they set out to comply with new reporting requirements under UK and European company law.

Investors continue to believe that, by focusing on the need to identify and manage ESG risks to the short and long-term value of the business, the guidelines highlight an opportunity to enhance value. They are grateful for the positive response of companies to the original guidelines. However, they believe it is desirable for reporting in connection with these risks to be set firmly in the context of the full range of strategic, financial and operational risks facing the business. Institutional shareholders also value forward-looking assessment of risks in the annual reports of companies in which they invest.

Investment Association members recognise that it is also incumbent on institutional investors to consider these risks and opportunities in the context of their overarching objective of

[1] The term "environmental, social and governance" replaces the reference to social, environmental and ethical risks in the previous guidelines. This reflects the evolution of market thinking which now seeks to stress accountability in a broader sense. Ethical issues are seen as a subset of a company's overall accountability responsibilities.

enhancing shareholder value. Addressing them should be an integral part of the investment process, rather than a separate "add-on" consideration.

It is not the intention of these guidelines to set a limit on the amount of information companies should provide on their response to environmental, social and governance matters. Some shareholders with specific ethical investment objectives may seek more detailed information. Some companies may choose to make additional information available, for example through separate corporate responsibility reports, in order to enhance their appeal to investors.

The Investment Association hopes that these guidelines will provide a helpful basic benchmark for companies seeking to enhance best practice.

The Disclosure Guidelines

The guidelines take the form of disclosures which institutions would expect to see included in the annual report of listed companies. Specifically they refer to disclosures relating to board responsibilities and to policies, procedures and verification.

With regard to the board, the company should state in its annual report whether:

1.1 As part of its regular risk assessment procedures, the board takes account of the significance of environmental, social and governance (ESG) matters to the business of the company.

1.2 The board has identified and assessed the significant ESG risks to the company's short and long-term value, as well as the opportunities to enhance value that may arise from an appropriate response.

1.3 The board has received adequate information to make this assessment and that account is taken of ESG matters in the training of directors.

1.4 The board has ensured that the company has in place effective systems for managing and mitigating significant risks, which, where relevant, incorporate performance management systems and appropriate remuneration incentives.

With regard to policies, procedures and verification, the annual report should:

2.1 Include information on ESG related risks and opportunities that may significantly affect the company's short and long-term value, and how they might impact on the future of the business.

2.2 Include in the description of the company's policies and procedures for managing risks, the possible impact on short and long-term value arising from ESG matters. If the annual report and accounts states that the company has no such policies and procedures, the board should provide reasons for their absence.

2.3 Include information, where appropriate using Key Performance Indicators (KPIs), about the extent to which the company has complied with its policies and procedures for managing material risks arising from ESG matters and about the role of the board in providing oversight.

2.4 Where performance falls short of the objectives, describe the measures the board has taken to put it back on track.

2.5 Describe the procedures for verification of ESG disclosures. The verification procedure should be such as to achieve a reasonable level of credibility.

With regard to the board, the company should state in its remuneration report:

3.1 Whether the remuneration committee is able to consider corporate performance on ESG issues when setting remuneration of executive directors. If the report states that the committee has no such discretion, then a reason should be provided for its absence.

3.2 Whether the remuneration committee has ensured that the incentive structure for senior management does not raise ESG risks by inadvertently motivating irresponsible behaviour.

Towards Best Practice

Institutional shareholders consider that adherence to the principles outlined above will help companies to develop appropriate policies on corporate responsibility.

The principles should also provide a constructive basis for engagement between companies and their shareholders. Over time this will allow both parties to develop a clear joint understanding of best practice in the handling of environmental, social and governance matters that will help preserve and enhance value. Current understanding of best practice leads to the following conclusions and indications as to how the guidelines should operate:

1. The guidelines are intended to apply to all companies, including small and medium companies.

2. The cost of managing risks should be proportionate to their significance. Ideally, procedures should be integrated into existing management structures and systems.

3. Statements relating to significant risks should be made in the annual report as part of the Business Review or voluntary Operating and Financial Review, and not separately as part of the summary accounts or on a web site dedicated to social responsibility. This would not preclude a cross reference to other parts of the report where more detailed disclosure of the type of risks involved and systems for managing those risks may also fit with other content.

4. With regard to the implementation, shareholders are anxious to leave space for companies to establish their own systems best suited to their business. However, they believe that, with regard to clause 1.1, best practice would require the full board to consider the issues on a regular basis, although some on-going detailed work might be delegated to a committee. Disclosure should include a brief description of the process undertaken by the board for identifying significant risks and indicate which risks are the most significant in terms of their impact on the business.

5. Examples of initiatives for reducing and managing risks (see 1.4 and 2.2) include regular contact with stakeholders, mechanisms to ensure that appropriate standards are maintained in the supply chain, and a clear policy for mitigating environmental impact which is monitored by the board through published KPIs. Evidence of such initiatives would be viewed positively by shareholders.

6. Reporting on performance over time in complying with policies to reduce risk will help shareholders monitor improvement in compliance.

7. Independent external verification of ESG disclosures would be regarded by shareholders as a significant advantage. Credible verification may also be achieved by other means, including internal audit. It would assist shareholders in their assessment of ESG policies if the reason for choosing a particular method of verification were explained in the annual report.

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APPENDIX 1

Questions on environmental, social and governance matters

Disclosure could be addressed by response, in the annual report, to the following questions:

1. Has the company made any reference to each of environmental, social and governance (ESG) matters? If so, does the board take these regularly into account?
2. Has the company identified and assessed significant risks and opportunities affecting its long and short-term value arising from its handling of ESG matters?
3. Does the annual report contain a forward-looking assessment of ESG and other risks facing the company?
4. Does the annual report describe the role of the Board in overseeing risk management?
5. Does the company state that it has adequate information for identification and assessment?
6. Are systems in place to manage the ESG risks?
7. Does the remuneration committee take account of the handling of ESG risks when setting performance targets?
8. Does directors' training include ESG matters?
9. Does the company disclose significant short and long-term risks and opportunities arising from ESG issues? If so, how many different risks/opportunities are identified?
10. Are policies for managing risks to the company's value described?
11. Does the company state whether it has followed ASB guidance on narrative reporting?
12. Does the company produce KPIs on material ESG risks?
13. Does the company produce KPIs on material ESG risks for each business unit?
14. Does the company report on the effectiveness of the ESG strategy through a review of these KPIs?
15. Are verification procedures described?

APPENDIX 2

Questions for investment trusts

1. Has the company made any reference to each of environmental, social and governance (ESG) matters?
2. Is the voting policy of the trust publicly available?
3. Does the voting policy make reference to ESG matters?
4. Is the manager encouraged actively to engage with companies to promote better ESG practice?