Code of good practices for institutional investors, asset managers and proxy advisors in relation to their duties in respect of assets entrusted to or services provided by them ("Stewardship Code")

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1 Introduction

Institutional investors, in their capacity as asset owners, and asset managers have a fiduciary duty of management and administration in relation to the assets entrusted by their clients and beneficiaries,[1] having to act in their best interest, for which reason it is advisable for them to adopt a long-term orientation.

This in turn implies encouraging listed companies or other entities in which they invest, and their administrative bodies, to have among their objectives:

- Obtaining long-term performance and value creation (hereinafter, long-term performance or return).
- Having an appropriate corporate governance regime.
- Appropriate management and integration into their policies and strategies of the risks and opportunities related to social and environmental aspects.
- Management of the possible impacts that these may imply, be it a financial impact on the entity or through an externality beyond the strictly financial aspects.
- All this in consideration of their potential to generate the long-term return referred to.

The hope is that as a result a virtuous circle takes shape, promoting responsible investment that avoids undue pressure on investee entities to adopt a predominantly short-term approach. This will contribute in turn to the sustainability of investee entities and of society and the economy in general.

Service providers, including proxy advisors, have a responsibility vis-à-vis investors and managers, as a result of their contractual relationship with them – that of diligently performing the functions that investors and managers have assigned them.

One of the objectives of the recent amendment of several delegated acts[2] in relation to the fiduciary obligations of asset managers, insurance and reinsurance entities and

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1 Depending on the legal form of the investment vehicle, the beneficiaries could be participants (for example, in an investment or pension fund) or shareholders, in the case of an investment company or other instrument with a similar legal form managed by an asset manager.

2 Commission Delegated Directive (EU) 2021/1270, of 21 April 2021, amending Directive 2010/43/EU as regards the sustainability risks and sustainability factors to be taken into account for UCITS; Commission Delegated Regulation amending Delegated Regulation (EU) No. 231/2013, as regards those to be taken into account by AIFMs, and other delegated acts forming part of the sustainable finance package.

investment firms is to clarify that they must integrate sustainability factors and risks, such as those deriving from climate change and environmental degradation, into their investment advice and procedures.

An effective way to contribute to achieving the aforementioned positive impacts on society and on companies is through a greater engagement of shareholders in the life of the companies in which they invest. As institutional investors and asset managers (hereinafter, managers) are important shareholders or actors in a large number of companies, their engagement is essential to achieve an efficient business management and governance model.

It should be noted that many international pension funds and insurance companies include, among the variables for selecting their managers, the practices specifically related to their policies on engagement and voting, as well as the results derived from them.

Finally, it is worth referring to some studies[3] that clearly show the need to define principles that promote institutional investment with a long-term vision.

Stewardship codes, regulatory context and code model

At the international level, in recent years there has been a proliferation of stewardship codes,[4] almost all of them based on principles and conforming to the "comply or explain" or "apply and explain" approaches.

These principles are generally designed in such a way that an entity wishing to adopt one of the codes that is potentially applicable to it, establishes policies on engagement and voting in investee companies, publishes them on its website, and reports periodically on how these policies and the principles of the code were applied in the financial year last ended. Some of the policies that these codes recommend, and having them available to clients and beneficiaries on these entities' websites, have become legally obligatory in the European Union.[5]

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3 In particular the reports prepared by the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA), in 2019: EIOPA BOS 19-537 *Potential undue short-term pressure from financial markets on corporates: Investigation on European insurance and occupational pension sectors*. Available at: https://www.eiopa.europa.eu/sites/default/files/publications/reports/eiopa-bos-19-537_report_on_investigation_undue_short_term_pressure.pdf and ESMA 30-22-762. *Undue short- term pressure on corporations from the financial sector*. Available at: https://www.esma.europa.eu/sites/default/files/library/esma30-22-762_report_on_undue_short-term_pressure_on_corporations_from_the_financial_sector.pdf

4 At the date of this Code, more than 20 countries, seven of them European, have drawn up stewardship codes, including Australia, Brazil, Canada, Denmark, Germany, Hong Kong, India, Italy, Japan, Kenya, Malaysia, Netherlands, Norway, Singapore, South Africa, South Korea, Switzerland, Taiwan, Thailand, the United Kingdom and the United States.

5 Through the transposition into the corresponding national legal systems of Directive (EU) 2017/828, of 17 May, amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement, and through Regulation (EU) 2019/2088, of 27 November, on sustainability-related disclosures in the financial services sector (SFDR).

In this context, the CNMV considers it important for entities voluntarily deciding to adopt the Stewardship Code (hereinafter the Code) to commit to applying each and every one of its principles. That is, the Code adopts the "apply and explain" model, as detailed below.

However, given the newness of the Code in the Spanish market, an adjustment period could be appropriate for some of the entities to which it is potentially applicable. It has therefore been decided to establish a transitional period of three years, counting from the approval of the Code, during which entities that decide to adopt it may apply the "comply or explain" criterion in their annual report, explaining why certain principles have not been followed and indicating which principles have been applied, and how, during the reporting period. The application of this transitional period will allow entities that decide to adopt the Code to select which principles they will comply with and which not, appropriately explaining the reasons why they have decided not to comply. Although each entity will determine which principles it can apply from the outset and which ones require new structures or internal procedures, depending on its particular circumstances, it is considered that Principle 6, regarding the policy for managing conflicts of interest, must be applied from the outset since it is consubstantial with the operations of any investor or manager.

Additionally, it is relevant to point out that entities deciding to make use of the transitional period must show a public commitment to apply all the principles after three years, for which they must publish a plan and a specific adaptation schedule, explaining the degree of progress in each of the three years.

Without prejudice to the optional transitional period, the Code adopts the "apply and explain" model, similar to that seen in the UK Stewardship Code. There are three reasons for choosing this approach as opposed to the "comply or explain" criterion. In the first place, the subjective scope to which the Code is addressed is open and variable. Secondly, the principles are expressed in a generic, non-prescriptive way. Thirdly, entities that choose not to adopt the Code are under no obligation to explain or state their position regarding it. These three characteristics make a code of this type very different from others, such as the *Good Governance Code of Listed Companies*, which adopt the "comply or explain" approach: they address a closed subjective field of obligated subjects, present a prescriptive and precise wording of multiple recommendations, and are subject to a legal obligation to declare.

Additionally, as a way of alleviating the costs or difficulties that accession to the Code may entail, the entities that adopt it may take into account the so-called "proportionality criterion", as explained below.

Entities deciding voluntarily to adopt the Code must indicate in their annual report how they have applied the various principles of the Code in the previous year, in accordance with the proportionality criterion and taking into account, therefore, their particular conditions and circumstances, such as size, the nature and complexity of the entity, its business strategy and the nature and magnitude of its investments, as well as the exposure to and nature and management of both financial risks and environmental, social and governance risks[6] of such investments. The proportionality criterion also

6 ESG risks.

means taking into account the complexity, size and resources available for engagement with the entities in which they invest.

Those entities that have a part of their assets or vehicles with a short-term time horizon – for example, because they belong to the trading portfolio – or where the amount or relative weight in an investee is very insignificant may decide to carry out engagement or voting activities to a lesser degree with regard to these entities, and must explain in their annual report the judgements and criteria used in said determination.

The Code is structured in accordance with a principle-based approach. The clarifications or expectations included after each principle must not be considered inflexible prescriptions that all entities must comply with, but rather, in application of the proportionality criterion, it will be the entities that determine how best to apply each principle, bearing in mind such clarifications or expectations, but adapting them to their particular circumstances and conditions.

Finally, the CNMV may review and adjust the Code to the evolution of the economic, social or institutional environment, or the regulatory framework, in particular as regard engagement and exercise of the vote.

This Code has been the object of consideration and advice by a consultative group, and was also submitted to public consultation from 24 June to 16 September 2022.

2 Characteristics of the Code

2.1 Scope of application

Investors and asset managers

The Code is addressed to institutional investors and asset managers based in Spain.

For the purposes of this Code, "institutional investors" includes life insurance and re-insurance companies and employment pension funds. However, given its voluntary nature, the possibility is left open for other entities, such as non-life insurance and re-insurance companies, holding or portfolio companies or other similar entities to also adopt the Code if they so wish. In the case of employment pension funds, both the accession and the application of the principles will be carried out through the control commissions or their management entities.

In this regard, and taking into account the significance of the investment of family groups and private investors in the ownership structure of Spanish companies, listed or not, it seems appropriate for them to have the opportunity of adopting the Code, with the necessary particularities. For example, among others, those who have significant influence over the companies.

In the case of entities that carry out different activities, such as insurers that simultaneously carry out life and non-life insurance activities, they may apply the principles only with respect to a part of their activities or decide to extend them to other similar actions, if they deem it appropriate. Similarly, in the event that an entity has the dual status of investor and asset manager, it may adopt this Code only as an investor, exclusively as a manager, or as both.

In the case of investors that are part of a group, when there is a unity of decision in investment management and each company performs the same or similar functions, in the absence of legal impediments – as could happen, in certain cases, in the field of the managers – or serious permanent conflicts of interest that make it non-viable, compliance with the principles could be made effective through policies, strategies and reports at the group level. In these cases, it is especially important to take account of Principle 6 as it relates to conflicts of interest.

Regarding managers, the following entities are included:

– Collective investment scheme management companies.

– Management companies of closed-ended collective investment schemes.

– Investment companies that have not assigned management to a manager.

– Investment firms and credit institutions in relation to the discretionary and individualised portfolio management services they provide.

Even when they do not have the status of asset managers for the purposes of this Code, and given the voluntary nature of the Code, the possibility is left open for other management entities, such as pension fund managers, to adopt the Code if they deem it appropriate. In the event that these entities, or the investment firms and credit institutions for the discretionary management services they provide, do not have the possibility of exercising the vote corresponding to the assets managed because they do not own these assets and have not been granted delegated powers, or such powers include the obligation to apply the voting policy of the delegator, these entities must take such circumstances into account for the purpose of applying the various principles of this Code, in particular, Principle 4.

The principles of the Code are intended for investors and managers, regardless of their size and the amount or relative weight in each entity in which they have invested or that they have under management, or the number of clients to whom they provide services.

The principles of the Code are aimed at entities based in Spain. However, given its voluntary nature, the possibility of the Code being adopted by investors and managers based outside of Spain is left open. This need not entail significant additional burdens or obligations, given the consistency of this Code with other international codes and standards.

Service providers

The term “service provider” refers to any person or entity that provides services to investors and managers in the performance of their responsibility, such as in their engagement activities or in respect of voting, or that provides them with certain data or analyses about their investments. However, considering the breadth and diversity of the group of potentially affected parties and the particular investment ecosystem in Spain, for the purposes of this first Code, it has been considered reasonable to limit its scope to proxy advisors only.

Proxy advisors with headquarters or establishment in Spain are therefore within the potential scope of the Code. In this regard, proxy advisors that decide to adopt the Code, depending on their particular circumstances, must adapt the principles to the activities and functions that have been entrusted to them and that they perform in relation to the investment, engagement and voting processes, incorporating in their annual report, to be published on their website, information on how they have applied these principles in practice.

Given that the range of functions entrusted to them may be very broad, proxy advisors must apply their professional judgement to determine which principles are incumbent on them and to what degree, and must indicate those principles that have not been affected by their actions in the reporting year. The fact that one or more principles do not concern them in the course of their actions does not prevent them from adopting the Code. The only thing that would prevent it is if a proxy advisor

were affected by one or more of the principles but did not to take it or them into account in its actions.

In any case, when investors or managers contract the services of any service provider, mechanisms must be established to ensure that such services are executed in such a way that they contribute positively to the business strategy and to the engagement and voting policies of the investor or manager.

2.2 Voluntary nature and proportionality

Adoption of this Code is voluntary.[7] Investors, managers and proxy advisors wishing to adopt the Code shall declare such adoption by means of a letter addressed to the CNMV, indicating the full corporate name of the adopting entity, the date of approval and the internal body approving the adoption, the particulars of the contact persons and, if available, their legal entity identifier (LEI), and an indication as to whether or not they have decided to avail themselves of the transitional period. The letter must also state whether the Code is adopted in the capacity only as investor, only as manager, or as both, or, in the case of insurance entities, whether the Code is adopted only as regards the life insurance activity, or also non-life or general insurance.

It should be noted that there is no provision for partial adoption, excluding certain assets, funds or other investment vehicles, for example, depending on the nature of their assets or their investment strategy. The entity must adopt the Code from a global perspective, assessing how each principle is applied in substance, taking into account its spirit and purpose, and not only their letter, and based on said nature or strategy, which could justify, for example, having less engagement, or even none at all, as would be the case with assets held in the very short term, the rotation and expected time horizon of which could also imply that no vote is exercised either.

The CNMV will establish and publish on its website a list of all the adopting entities and a link to the website of each, on which they must publish their engagement and voting policies in a visible and clear manner, and information on the integration of sustainability risks, to the degree deemed most appropriate, in their investment strategy and operations. Annual reports on how they have applied these policies and the principles of this Code in the year last ended, including the main incidents and main actions carried out and most significant objectives attained, must also be published on the website of each entity. The CNMV website will also indicate whether the entities have availed themselves of the transitional period.

The foregoing will be without prejudice to the actions of supervision of legal obligations in relation to these policies and annual reports, by virtue of such powers as may be entrusted to the CNMV, the General Directorate of Insurance and Pension Funds, the Bank of Spain or any other competent authority as the case may be.

For each principle, possible ways of incorporating proportionality into its application are set out. This proportionality criterion does not have a specific time limit; entities

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7 As has been pointed out, there are currently various EU proposals to amend the legal regime, which could mean that some of the current practices, so far voluntary, would become mandatory, in accordance with the "comply or explain" criterion.

that apply it may continue taking into account such circumstances and conditions for as long as they remain subscribed to the Code and the reasons justifying the proportional application of a principle are maintained.

Notwithstanding the above criterion, entities of any size that adopt the Code may, additionally – although exclusively for a period not exceeding three years from the approval of the Code – opt for a gradual application and report annually during that period, applying the "comply or explain" criterion. In this case, they must define and publish a calendar or adaptation plan, in which the pace of application of each of the principles is established until full application of all of them is achieved.

After the transitional period, if the Code is not applied in its entirety using the "apply and explain" criterion, the entity must declare it as such and may not continue to declare that it subscribes to the Code.

The principles must be applied, in any case, with respect to and subject to such general or sectoral regulations as may be applicable in each situation. Likewise, the Code must be applied so as not to impede fulfilment of contractual or legal obligations, including the obligation to respect both due confidentiality and the limitations on disclosure of inside information, and with due consideration being given to the extent to which the publication of information could harm the financial situation, competitive position or value creation of the investor or manager, or of the companies in which they invest. These limitations must be especially taken into account in the application of Principles 3 and 5.

In any declaration of compliance, it will not be enough to state that a certain principle has been applied; it must be explained how each one has been applied and implemented in practice and to what extent, what specific actions have been carried out, what changes if any have taken place either in the investors or managers or in the entities in which they invest, and whether the established objectives have been achieved.

2.3 Reasoning behind the principles

It would be desirable for investors and managers to make their investments so as to maximise the long-term economic value, directly or indirectly, of the funds provided by or managed for their clients and beneficiaries.

For these entities, Principle 1 assumes that long-term value creation for their clients and beneficiaries is closely linked to the increase in value of their investments, which in turn is directly linked to value creation by the investee entities. Likewise, it is recalled that, just as important as having an appropriate organisational framework and the practices and structures of internal governance required by the regulations or adopted voluntarily, is the periodic assessment of these, of the events occurring during the year and of the assigned resources, so that any necessary changes can be made to keep them permanently up to date and in line with current circumstances.

Principle 2 is based on the fact that the creation of value from their investments is linked to adequate knowledge of the companies in which they invest, and implies having sufficient knowledge of their strategies, their profitability objectives, their exposure to financial and non-financial risks, and the environment, competition and structure of the markets in which they operate, and regularly monitoring these.

Principle 3 addresses the importance of clients and beneficiaries being able to find out about the engagement policy and the extent to which investors and managers intend to become involved in practice and promote proper management of the companies in which they invest.

Principle 4 recognises that one of the most important activities of engagement policies is the responsible exercise of voting rights by investors and managers.

The exercise of the right to vote, fully integrated with the other actions of engagement with the companies in which they invest, constitutes their essence and is a key aspect for publicly expressing their degree of agreement, or disagreement, with the management and strategy of the management body of the companies in which they invest.

Principle 5 establishes that, in order for clients and beneficiaries to properly assess the extent to which investors and managers are committed to engagement and voting activities, it does not seem sufficient for them to publicly report the policies adopted; it is considered highly recommendable that they also report on how these policies have been implemented in practice, the actions carried out and the objectives achieved.

Investors and managers may find themselves in situations of actual or potential conflicts of interest, both because of the business group to which they belong and because of the other activities they carry out. For these reasons, Principle 6 indicates that it is desirable for them to have an appropriate policy for managing conflicts of interest, prioritising the interests of their clients and beneficiaries.

In accordance with Principle 7, it is considered desirable to use an appropriate remuneration structure to encourage executives of investors and managers to effectively apply their strategies and objectives so as to obtain long-term performance for their firms.

3 Principles

These principles are understood without prejudice to the various applicable legal and regulatory obligations, which shall prevail in the event of conflict with any of the provisions of the Code.[8]

Long-term strategy

Principle 1: Investors and managers shall guide their actions towards the long-term profitability of their investments for the benefit of their clients and beneficiaries, and shall integrate, to the degree they deem appropriate, as part of their fiduciary obligations, environmental, social and governance factors, as well as the associated risks, in their investment strategies, policies and decisions.

Investors and managers must also maintain, periodically review and update, where appropriate, their internal governance structures and practices to ensure that they are consistent with the principles of this Code.

i) Development of policies, procedures and strategies

It is considered advisable that investors and managers design their policies, procedures and strategies so as to aim at creating long-term value in their investments, reciprocally promoting the creation of value and a long-term profitable business in listed companies or other entities in which they invest, thus avoiding undue pressure from a short-term vision of the business.[9] Investors and managers should integrate, to the extent they deem appropriate, environmental, social and governance factors and risks into their investment strategies, policies and decisions.[10] It is recommended that these investment strategies and value creation be consistent

8 Among such legal or community obligations, it is worth mentioning, without intending to be exhaustive, at the community level, Regulation (EU) 2088/2019 of the European Parliament and of the Council, of 27 November 2019, on sustainability-related disclosures in the financial services sector (SFDR) and its delegated regulations, or the European Commission's Guidelines on non-financial reporting and double materiality, regulated by Directive 2013/34/EU.

9 It should be noted that, without prejudice to the importance of a general long-term orientation, all investors and managers face sustainability risks, such as those arising from the mitigation of climate change and the transition in response to it, for which reason the principles of this Code are potentially applicable to any investor or manager.

10 In line with the provisions, at the entity level, of the SFDR. And those who consider it so, in line with said regulation and with the concept of double materiality defined by the European regulatory framework, shall also bear in mind the management of the main impacts, including adverse ones, as provided for in Article 4 of the SFDR and the European Commission's Communication "Guidelines on non-financial reporting" (2017/C215/01).

with the profile and duration of investors' liabilities, in particular their long-term liabilities.[11]

ii) Corporate governance culture of the investor or manager

It is recommended that investors and managers be guided by a solid corporate culture that reflects values aligned with the above objectives and serves as the foundation of their substantially fiduciary role towards their clients and beneficiaries.

In this regard, it is considered advisable that they have codes of conduct integrating the principles of this Code, so that their directors, employees and managers are bound by them, and that they equip themselves with appropriate corporate governance structures for this purpose, the approval and supervision of which corresponds to the administrative body. It is seen as important for codes of conduct to be of a prescriptive nature, not merely hortative, and for them to establish criteria and prohibitions specifically, as well as the consequences of non-compliance.

It is also considered good practice for investors and managers to have a dynamic internal corporate governance structure, which can be quickly updated in response to any pertinent changes, whether internal or in the environment, allowing them to exercise their fiduciary responsibilities effectively, identifying any event or circumstance that implies the need for change and in such case making the appropriate change(s), for which they should have the necessary capacity to act appropriately, as fiduciary managers of the investments, in the best interest of their clients and beneficiaries.

It is considered desirable for the annual report on the application of the engagement and voting policies to report on the review of their governance and organisational structures and any changes made, as well as any improvements that it was not possible to complete, informing of the schedule for their completion. It should also be indicated whether an external advisor participated in said review.

iii) Particularities of application

For investors who have significant influence or have appointed proprietary directors and decide to adopt the Code, it is considered appropriate for them to explain what their strategy and long-term performance objectives are, how they plan to achieve them and to what extent their investment strategies and decisions take into account the corporate interest and the interests of other stakeholders, including those of the other shareholders, of the companies in which they invest.[12]

Proportionality: this long-term orientation can be attenuated by the nature and global magnitude of the assets in which they invest, depending on the time horizon of the investment or the absolute and relative weight of their investment in a given company.

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11 In line with the provisions of Article 3h, section 1, of Directive 2007/36/EC, of 11 July, on the exercise of certain rights of shareholders in listed companies, as amended by Directive (EU) 2017/828, of 17 May, as regards the encouragement of long-term shareholder engagement.

12 In line with the definition of corporate interest in the CNMV Good Governance Code, recommendation 12.

Likewise entities may, in view of their small size, or in accordance with their investment strategy, incorporate the consideration of sustainability factors only partially, confining them to only a very specific portion of their assets, for example those most exposed to a certain risk, or incorporate only those factors whose non-consideration could imply a greater material risk to their investment, depending, among other things, on the relative weight of their investments, whether they have sufficient information and the resources available.

Knowledge and monitoring of companies

Principle 2: Investors and managers must monitor and acquire adequate knowledge of the companies in which they invest and the extent to which these companies contribute to the objective indicated in Principle 1 above, and must have sufficient resources for their monitoring work.

i) Analysis and monitoring of companies

It seems pertinent for investors and managers to carry out periodic research, analysis and monitoring of the material aspects that affect the long-term value creation of the main companies in which they invest. These material aspects may refer, among other things, to these companies' strategies, objectives and business plans, their capital structure, their financial and non-financial reporting, how they evaluate and take into account sustainability factors, risks and opportunities, the degree of compliance with their corporate culture, the quality of their corporate governance and the degree of compliance with the good governance codes that apply to them. They could also include an analysis and monitoring of the main impacts, positive or adverse, potential or real, of their investments.[13]

ii) Monitoring processes

It is important that, in order to meet this objective, investors and managers have effective procedures and systems, adequate material resources and the necessary training for their staff, or subcontracted staff, in order to carry out this task without bias and regardless of the interests of any group to which the entity might belong, and must be publicly reported annually, in the report referred to in Principle 5, on how they have equipped themselves with and organised these procedures, systems, resources, etc. These monitoring processes should also extend to the monitoring that investors, in their capacity as asset owners, carry out on the actions of the managers to whom they have entrusted the management.

iii) Identification of events

It is recommended that their monitoring actions should include the means to identify incidents or events that could imply significant losses in the companies in which they invest or expose them to high risks, inconsistent with their investment policy. In these situations, they should assess whether it is appropriate to communicate such fact to the investee(s) concerned and if so, based on the outcome of dialogue, to analyse what other measures it would be more reasonable to adopt,

13 In accordance with Article 4 of the SFDR.

both in terms of how to vote at the AGM and the possibility of getting involved and collaborating with other investors and stakeholders.

Proportionality: this monitoring may be attenuated by the nature and global magnitude of the assets in which they invest or by the absolute and relative weight of their investment in a particular company. Since its use is generally appropriate to all investors and asset managers, those of small size, or depending on the complexity of their assets, could entrust their more intensive monitoring to service providers, including investment analysts and proxy advisors. In any case, it must be ensured that such service providers act and properly fulfil the commitments assumed and that the contractually pre-established quality levels are met, since the investors and managers retain responsibility for the investments made.

Development and publication of the engagement policy

Principle 3: Based on their knowledge of the companies in which they invest, investors and managers shall develop, publish and keep up to date an engagement policy, focused on generating a return consistent with that indicated in Principle 1 and on helping to ensure that the business strategies of the companies in which they invest are appropriate.

It is recommended that investors' and managers' engagement policy be clear, precise and complete, contain measurable criteria and objectives and reflect a joint approach to the total investment. The policy should be available on the entity's website, together with the annual report on its application in practice in the previous year, in a visible and well-identified area that can be accessed with no more than three clicks from the home page. The above criteria are also applicable to the voting policy, in the event that it exists separately from the engagement policy.

It is also recommended that entities use as a reference the engagement regime established by Article 3g of Directive (EU) 2017/828 of the European Parliament and of the Council, of 17 May 2017, implemented in Spain mainly through Law 5/2021, of 12 April, even if they are not subject to compliance with the content of the engagement policy determined by said regulations.

It is considered advisable that this policy be subject to periodic review, evaluating whether or not it is aligned with the objectives, strategies and responsibilities of the investor or manager, an evaluation in which it might be a good idea for independent external advisers to participate from time to time. The last review date carried out should be indicated on the website, as well as its scope and the main changes made, if any, and whether any external adviser participated in these actions.

Taking into account their knowledge of the companies in which they invest, as a result of their monitoring actions, investors and managers, as part of their engagement activities, should be in a position to enter into a communication and, where appropriate, into a fluid dialogue with them and with the members of their administrative body and senior management, in those situations in which it is considered necessary. Said communication will seek to express their concerns and to promote, where necessary, the actions they deem appropriate, for example, in relation to the mitigation of certain risks, the non-renewal or dismissal of certain directors, or even divestment if the investors or managers judge that the companies' actions carried out or planned, or the pace

of their implementation, are not appropriate, all with the aim of maintaining a constructive engagement. For this, it is considered important for the policy to provide for the need to have the material and human resources necessary for it to be carried out properly.

It seems desirable that the dialogue take place in a context in which the investor or manager, in addition to actively voting, publicly states in its engagement policy how said engagement and dialogue with the companies in which it invests could influence how it votes.

It is considered advisable for the engagement policy to encourage investee companies to have appropriate governance structures and practices, taking into account the recommendations of the CNMV's *Good Governance Code of Listed Companies* or other similar ones.

Said policy should foresee the cases in which it might be opportune to establish a dialogue and cooperate with other shareholders, managers or investors, in order to more effectively achieve its objectives. This policy could also provide for the desirability in certain cases of dialogue and cooperation being carried out with other stakeholders, such as groups of clients or suppliers, or with representatives of the workers or of certain local communities in which they operate.

It is also considered important for the engagement policy itself to provide for an escalation strategy addressing and explaining the situations in which it is deemed appropriate to escalate the nature of their actions vis-à-vis investee companies, when these or members of their governing bodies or senior management do not adequately address their concerns, or when they consider that a certain risk exposure continues to be excessively high. Such actions may include, among others, contacting the chairperson, the independent directors or their coordinating director if there is one, taking into consideration as guidance the communication policy of the investee company, publicly communicating their positions and concerns, or expose them at a general meeting. In this regard, in accordance with the legally established terms and deadlines, they may propose or ask the directors to call a general meeting or to include new items on the agenda, or promote the adoption of new resolutions or voting proposals.

In the event that entities plan to use ESG rating agencies for the purposes of analysing the practices of the companies in which they invest, it is recommended to disclose this fact in the engagement policy, also indicating, in the annual report, the nature and scope of the service received and informing of the existence of any possible conflict of interest and how it has been managed.

In their engagement actions, it is considered particularly important for family groups and other investors with significant influence or that have appointed proprietary directors to have effective mechanisms for identifying and managing conflicts of interest, giving due consideration to the corporate interest and the interests of the other stakeholders, including minority shareholders. In particular, it is considered desirable that in their engagement they ensure that such proprietary directors as they have appointed are aware of their responsibility, like the other directors, in relation to the defence of the corporate interest, prevailing over the interests of the *dominus*.

Lastly, it seems advisable that the investor or manager engagement policy include an expectation of how they consider that the entities in which they invest, and their directors, should address and follow up on proposals that are submitted to the meeting and that may have a significant percentage of votes against.

Proportionality: entities may determine to limit their direct engagement with those companies in which they exceed a certain amount or percentage of investment, or with those that respond to the priorities of their engagement policy, in line with their long-term strategies. It would even be possible for entities of any size to fully entrust their execution to service providers, subject to establishing adequate quality requirements and checking that the level of service provided conforms to what was contractually agreed. In the event that engagement and voting are outsourced, in whole or in part, it is recommended that investors and managers develop and publish policies that are precise enough to serve as a guide and reference to the service provider or manager, in the case of discretionary portfolio management, when exercising engagement and delegated voting, and on occasions, when the issues subject to voting and the direction of the vote are specifically covered in the policy, without even needing specific *ad hoc* instructions.

The engagement could also be affected, regardless of the size of the entities, by the nature of the assets; for example, the degree of engagement could be substantially less for investments that have a short-term orientation, such as shares in the trading book or those held for liquidity purposes, or for some investments in debt, taking into account their maturity and risk profile. The evaluation of the above factors could mean, however, that, in relation to certain assets, it is considered appropriate to carry out a certain engagement or exercise a vote, even if the amount or percentage of investment is small, as could happen in the case of exposure to certain legal or reputational risks.

In addition, engagement should be exercised in a proportionate manner, in terms of the time and incremental costs that it may generate, both for investors and managers and for the companies in which they invest, depending on their policy for attending to the various investors and managers.

Exercise of the right to vote

Principle 4: Investors and managers shall actively exercise their rights as shareholders in the companies in which they invest, participating and exercising their right to vote responsibly at general shareholders' meetings, in the interest of their clients and beneficiaries, in accordance with their engagement and voting policies.

It is highly recommended that investors and managers, in accordance with their voting policy, actively exercise the voting rights they have at their discretion in the companies in which they invest.[14] In the case of delegation in favour of third parties,

14 It should be noted that, in relation to the discretionary and individualised portfolio management services provided by managers, it will be the clients who hold ownership of the securities and the associated voting rights, and who will generally exercise such rights, if they are not delegated to said managers.

this should be with precise instructions on the direction of the vote. For the above purposes, and as indicated, it is recommended that these entities establish clearly and precisely, and with a sufficient level of detail, what their voting policy is and make it available to the public on their website. This could avoid the need, on certain occasions and specific matters, to issue specific *ad hoc* instructions if they are covered by the policy, and the policy indicates what the direction of the vote should be on such occasions.

In this regard, it is considered important for the policy to provide that the direction of the vote will take into account the result of the actions carried out in accordance with Principles 1, 2 and 3, and, in the event that the matter to be voted on refers to the appointment, re-election or dismissal of directors, account should be taken of whether the director concerned contributes positively to the appropriate composition of the board, with particular reference to the diversity of profiles, and of the extent to which in the process the listed company has followed the principles of good governance set out in the CNMV's *Good Governance Code of Listed Companies* and *Technical guide 1/2019 on nomination and remuneration committees* or equivalents. It is also considered good practice to take into account, in voting on the re-election of directors, the conduct of the director in the exercise of his or her office, based on the information available and obtained during the engagement, and whether he or she is considered to have had any responsibility, direct or indirect, for any matter generating concern to the investor or manager during its engagement.

Investors or managers should apply the utmost caution and extreme scepticism if asked to support any proposal at the general meeting, such as for the removal of independent directors, if such proposal had not previously been included on the agenda (whether at the time of the call or through new points or resolution proposals introduced later, in accordance with the applicable regulations). In these cases, an analysis of these proposals should be carried out after ensuring that the reasons given in them are fully compatible with their engagement policies and the principles of this Code.

The voting policy should provide for investors and managers, in deciding which way to vote, to take account of the communication and dialogue established with the companies subject to their engagement policy and, if applicable, the actions carried out by such entities after the investors or managers have informed them of their vision and interests, conveyed their concerns and cooperated, when necessary, with other investors and stakeholders. When the concerns have not been adequately resolved, the policy should provide for the advisability of evaluating, for each specific situation, whether it is appropriate to communicate to the companies in which they invest and their administrative bodies, in advance, the direction in which they expect to vote and the reasons for it, even if the shareholders' meeting has not yet been called, to the extent that such eventualities have not been clearly dealt with in their voting policy.

A situation that may imply the need to abstain or vote against the proposed resolution of the directors or a shareholder and, when it refers to significant issues, even to publish their voting intentions in advance would occur in those cases in which the directors had not provided all the information and documentation necessary for an informed and reasoned vote sufficiently in advance.

In the case of stock lending, the voting policy should clarify the cases and circumstances in which the loaned shares should be recovered to exercise the vote and they should report annually how, if at all, stock lending has influenced their exercise of the vote.[15] Shares should not be borrowed for the primary purpose of exercising the related voting rights.

If the investor or manager uses the services of a proxy advisor, it is considered advisable that the advisor's recommendations not be followed automatically, but rather that the right be exercised in an informed manner and by forming their own judgement in defence of the interests of their clients and beneficiaries, which should be reported in sufficient detail in the annual public report.

Proportionality: without prejudice to its being a generally admissible practice, smaller investors and managers may use the delegation of their vote to service providers to a greater extent, provided that they maintain the general criterion of transmitting specific instructions, given that they retain responsibility for the direction of the vote. As an alternative, they may develop an explicit and complete voting policy that provides for all the relevant cases, thus avoiding having to give specific instructions for such cases. It is also considered advisable, taking into account their particular circumstances, that they gain knowledge and experience regarding the companies in which they invest, in order to gradually improve their ability to exercise their fiduciary responsibilities in the most appropriate manner. On the other hand, entities of any size could decide not to vote in those companies that represent insignificant investments, less than a certain monetary amount or percentage of the portfolio, depending on the nature and time horizon of the investment (such as the case of investments belonging to the trading portfolio), or depending on the nature and low relevance of the decision, it being advisable to explain and justify the reasonableness of the criteria established in the policy, both in general and regarding the specific judgements made in the particular cases that have arisen. It seems important for these criteria to cover certain cases in which the exercise of voting is considered appropriate, even when the absolute or relative weight of their investment is small, for example, when cases of corruption or other serious legal or reputational risks are identified.

Transparency of the engagement and voting actions carried out and their results

Principle 5: Investors and managers shall publish an annual report on how they have applied the engagement and voting policies in the immediately preceding financial year, which will include an evaluation of the actions carried out and an explanation of how these policies have contributed to the objectives established in Principles 1, 2 and 3 and the achievement of the business strategy of the companies in which they invest.

It is considered desirable that the annual report on the application of the engagement and voting policies be clear, complete, precise and published on the entity's website under the conditions set forth in Principles 3 and 4 with respect to said policies. This annual report will also explain how the entity has applied each of the principles of this Code. This annual report should be published within a period of 12 months from the

15 In a manner consistent with what is indicated in Recital 21 of Directive (EU) 2017/828, of 17 May.

closing date of the financial year to which it refers, provided that the applicable general or sectoral regulations do not establish a different period.

To the extent that they have delegated a part of their monitoring, engagement or voting activities, they must explain what steps and actions they have taken to ensure that proxy advisors or other service providers have carried out their actions as stipulated contractually and to what extent they have positively contributed to the achievement of the strategy and objectives by such investors or managers.

i) Engagement policy application

This section of the report should contain clear, complete and objective information, both quantitative and qualitative, on the actions carried out by the investor or manager in the exercise of their engagement policy, and how they consider that these activities have contributed to the creation of value for long-term for its clients and beneficiaries, to the business strategy of the companies in which it invests and to the improvement of its corporate governance. It is considered relevant to explain how engagement practices have varied between the different funds or investment vehicles and types of assets.

To the extent that it is relevant, it should contain examples and specific actions carried out by investors or managers, indicating whether these actions have been accompanied by any change in the behaviour of the companies in which they invest, or, if not, what measures have been adopted in this regard, among others, their voting direction at the meeting or, if deemed appropriate, on their divestment decision, also indicating, when relevant, those pending actions.

ii) Application of the voting policy

In this section of the report, it is considered relevant that investors and managers publicly disclose, on an annual basis, how they have applied their voting policy, including, when they have the power to exercise it at their discretion, a general description of their voting behaviour, an explanation of the most important votes and whether they have used the services of proxy advisors or other providers, and explaining, in the latter case, the degree to which their recommendations were followed.

They should also publish the direction of the vote cast at the general meetings of the companies in which they own shares, for which it would be sufficient to include a link to their voting records. Said publication may exclude votes that have been insignificant due to the object of the vote or the dimension of the investor's or manager's participation in the company.[16] Nor would it be necessary to report the details of the votes made when, for example, in the case of discretionary portfolio management, the vote is exercised following specific instructions from its clients. In these situations, it would be sufficient to indicate the assets that are in that situation and explain that the discretionary power to vote is lacking with respect to them, and that it has only been exercised following instructions from their owners.

16 In a manner consistent with what is established in Article 3g of Directive (EU) 2017/828.

Proportionality: the degree of detail in the annual report should depend on the relevance of the actions carried out. In any case, investors and managers may refrain from including information that could cause damage to their financial situation, competitive position or value creation to them or to the companies in which they invest. Likewise, the report should include the way in which proportionality has been applied in the other principles, which could imply that smaller investors or managers have availed themselves of certain exceptions and proportionalities provided for in other principles, which in turn time could result in a report of less complexity and size.

Conflict of interest management policy

Principle 6: Investors and managers must have a conflict of interest management policy that must be focused on prioritising the interests of their clients and beneficiaries.

Investors and managers should develop a policy that establishes, in a clear, complete and precise manner, the measures adopted to identify, manage and resolve conflicts of interest that may eventually arise in the performance of their engagement and voting activity, either by forming part of your general conflict of interest policy or in a separate document.[17]

In the resolution of these conflicts, the interest of clients and beneficiaries should always prevail, respecting the legality, uses and good practices of corporate governance. To this end, entities should establish effective policies and equip themselves with both governance systems that allow them to identify potential or real conflicts of interest and the appropriate mechanisms to manage, mitigate or prevent them, ensuring due independence in resolving these conflicts.

This policy for managing conflicts of interest should be made available to the public through the investors' and managers' website, in the terms set forth in Principle 3 regarding the engagement policy, and the annual report should also state how it has been applied in practice in the previous year and indicate, to the extent deemed relevant, specific examples of potential or actual conflicts of interest that have arisen, and how they have been managed and resolved, taking into account in any case, the need to maintain the confidentiality required by applicable regulations and to avoid significant undue damage to the entity itself or to a third party, including the companies in which they invest.

Proportionality: it seems reasonable that the policy on conflicts of interest and its practical application should be adapted to the nature and relevance of such conflicts, potential or real, to the particular circumstances of each investor or manager and to the characteristics of the products offered to clients. Likewise, it is possible to define objective quantitative thresholds below which conflicts are clearly immaterial and do not require management.

17 For this, taking into account what is indicated in this regard by Directive (EU) 2017/828 and Law 5/2021 that transposed it.

Remuneration policy

Principle 7: The remuneration policy shall establish and publicly indicate what part of the variable remuneration of the executive directors and senior managers of the investors and managers will be linked to the attainment of objectives related to their strategies and to how their effective application has been carried out during the year and, in particular, it will be oriented towards the achievement of long-term performance by such investors and managers.

In accordance with the remuneration policy, it is considered desirable that a part of the variable remuneration of the executive directors and senior managers of investors and managers be linked to the achievement of objectives that refer to the effective application of their strategy and that, in particular, it be oriented towards the achievement, by the investor or manager, of a long-term return, including, where appropriate, for those people who have responsibilities in the application of the engagement and voting policies, objectives linked to the achievement of these policies. The foregoing will be adjusted to what is applicable according to the sectoral legislation, when it regulates said issue.

In this regard, it is important for investors and managers to justify, both in the remuneration policy and in the annual report, that the remuneration structure and the amounts annually accrued are aligned with their business strategy and with the objective for such investors or managers of the achievement of long-term performance, it being advisable to explain the connection between the metrics set and the objectives pursued. If this information is contained in any other report required by the regulations, it would suffice to include in the annual report referred to by Principle 5 the minimum information necessary for its proper understanding, with a reference to the other report to obtain additional, more detailed, information. This recommendation does not cover the detail of individual remuneration earned by each person.

Proportionality: the complexity of the remuneration policy and the proportion of specific incentives linked to compliance with their business strategy and long-term performance, including, if applicable, engagement and voting policies, can be affected by multiple factors, such as the size and organisational structure of each entity.

The specific weighting to be determined by each entity and for each category of affected persons is a matter that requires significant judgement and will depend on the particular circumstances of each investor or manager, as well as the functions and hierarchical position of each subject, although this weighting should be sufficient to be capable of influencing the behaviour of the beneficiary.