



Corporate Governance and Engagement update

CiPFA November 2013

Introduction

Presentation to CiPFA November Seminars 2013:

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Regulated by the Financial Conduct Authority

Developments in stewardship

Emerging issues in 2013



EUROPEAN
COMMISSION



- **Corporate taxation:** Legal compliance no longer enough, more political and public press on companies to act fairly (Starbucks, Google etc). Will investors begin to take a closer look?
- **The banks:** The BoE says the UK banks need more capital. Parliamentary Commission report requires significant reform. Continuing concerns over IFRS effect on accounts.
- **Audit:** EC progress with reforms like mandatory rotation, limits on non-audit work etc. Competition Commission report recommends similar changes in the UK.
- **Labour standards:** Bangladesh factory collapse should lead to renewed scrutiny. Also allegations about anti-union activity at companies like Deutsche Post DHL and National Express continue.
- **Remuneration policy:** Expect more scepticism on performance related pay, but support for binding vote on pay.



Shareholder engagement: Emerging Issues 2013

Developments in stewardship

How did the 2013 season look?



GlencoreXstrata

- **A drop off in opposition to pay?** Big votes against Jupiter, Chime Communications, Balfour Beatty etc. But overall votes against remuneration policy seem to be lower than 2012.
- **Two defeats:** As of today, two companies have lost the vote on their remuneration report, Afren the most notable. By this point in 2012 five companies had already been defeated.
- **Directors forced out:** Again, not on the scale of 2012, but Sir John Bond's ejection from Glencore Xstrata was significant.
- **What does it mean?** Some investors argue votes are down because companies are putting forward more acceptable proposals. But it may look like shareholder activism declining.

Shareholder Engagement: The LAPFF Workplan 2013



Employees & labour standards

- **Lonmin's 5 Point Plan**

- Employee Relations

- Empowerment

- Migrant & Local Labour

- Use of Capital & Infrastructure

- Housing & Accommodation



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Carbon emission reductions: Aiming for 'A'

Aiming for A: high carbon emitting companies using CDP data

- BP meeting, Rio Tinto, National Grid
- Other highest largest UK emitters include British Airways.





Fracking: Environmental & Social Risks



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- Fracking lessons from the US: rapid development, minimal regulation, favourable land access laws
- Key risks: water & chemicals, land disturbance, emissions & climate change, communities, employees & contractors
- Regulatory, environmental and social context in UK is different
- UK shale gas likely to develop slower, with higher costs



Executive Pay Expectations and Action Plan

Expectations

- Emphasis on fixed over variable pay
- Phase out LTIPs
- Set pay of incoming execs below the outgoing ones
- Claw-back bonuses where ethical or ESG standards are breached
- Disclose pay ratios – top/bottom 10% and average employee/highest paid
- Exec recruitment transparency
- No golden hellos
- Canvass employee views
- Discretion only to reduce pay
- **NOT INCLUDED:**
 - employee to exec pay ratio (i.e. 1:75)
 - a 'cap' on variable pay (i.e. 200% of salary)
- Note: EU considering regulations to cap bankers bonuses at 100% of salary.



International Financial Reporting Standards:

- Developed by the audit and accounting industry, defective in identifying real assets and liabilities, divergent from Companies Act requirements
- Banks financial health overstated: contributed to global financial crisis
- What happened? Standard setters and company audits created false sense of financial security
- Directors ignorant of true liabilities in company accounts
- Auditors failed to alert directors of risks: over £40billion of understated liabilities in banks' accounts from 2008
- One consequence: any dividends paid off defective accounts deemed to be unlawful
- LAPFF campaign to re-assert the 'true and fair' view.

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