FairPensions™
The campaign for **responsible** investment

Fairshare Educational Foundation
Trowbray House
108 Weston Street
London SE1 3QB
020 7403 7800
fairpensions.org.uk

Briefing: Queen's Speech 2012
Towards a more responsible capitalism?

This briefing focuses on the government's proposals on **executive pay**. It sets out the background and recent developments, analyses the government's proposals and explores what more might need to be done. Although this issue was not mentioned in the Queen's Speech, government has confirmed that measures will be brought forward in the Enterprise and Regulatory Reform Bill.

You can find out more about the fast-moving developments of the 'Shareholder Spring', and about FairPensions' new initiative to help savers hold their agents accountable for their votes on high pay, at our briefing event on **Tuesday 15 May, 3.00-3.45pm,** in **Committee Room 15** of the House of Commons.

Executive pay: Key facts and figures

- From 2010 to 2011, mean FTSE 100 executive pay rose by 49%, compared with 2.7% for the average employee.[1]
- The median total remuneration of FTSE 100 CEOs rose an average of 13.6% a year between 1999 and 2010, while the FTSE index rose by just 1.7% a year over the same period[2].
- In the aftermath of the 2008/9 financial crisis, FTSE 100 companies lost almost a third of their value but the salaries of their executives still rose by an average of 10%.[3]
- Since the introduction of the advisory vote on pay in 2002, just nineteen remuneration reports have been rejected by a majority of investors.
- In 2011, no FTSE 100 company had its remuneration report voted down by more than 50% of its investors.[4]

Recent developments: the 'Shareholder Spring'

- ***Barclays*** suffered a shareholder revolt this year over Bob Diamond's £17m payout, with concern focussing particularly on a £5.7m 'tax equalisation' payment. However, at their AGM on Friday 27 April, only 26% of shareholders voted against the remuneration report. Although far in excess both of last year's figure (9.5%) and the average for the FTSE 350

[1] http://highpaycommission.co.uk/wp-content/uploads/2011/11/HPC_final_report_WEB.pdf
[2] http://www.bis.gov.uk/assets/biscore/business-law/docs/e/11-1287-executive-remuneration-discussion-paper.pdf
[3] TUC report 'Unfair to Middling' November 2009
[4] http://www.guardian.co.uk/business/2012/mar/14/vince-cable-shareholders-vote-executive-pay

THE CHARITY AWARDS 2010 HIGHLY COMMENDED

(10%),[5] this still fell far short of a defeat.

- On Thursday 3 May, ***Aviva*** became only the fourth FTSE 100 company ever to have their remuneration report defeated, with 54% of shareholders voting against.[6] Chief executive Andrew Moss announced his resignation on 8 May as a result of the vote.

- Unusually high votes against remuneration reports have been seen at various other company AGMs, including ***William Hill***, ***Man Group*** and ***UBS***. This has been dubbed a 'Shareholder Spring' by some commentators. However, to date Aviva remains the only FTSE 100 company to have its remuneration report defeated outright.

- Major shareholder rebellions have generally only been seen at companies whose share price performance has been exceptionally poor. A higher share price can mask poor practice and poorly aligned incentives. Companies which have performed well this year but whose remuneration reports have included elements which are generally regarded as bad practice (for example, ***Rolls Royce***, whose incoming Chief Executive received a golden hello) have emerged relatively unscathed.

Queen's Speech: Key Points

The Queen's Speech did not make any direct mention of the government's plans regarding executive pay and shareholder rights. However, BIS has confirmed that the Enterprise and Regulatory Reform Bill, one of the 19 Bills announced in the Speech, will include measures to "*strengthen the framework for setting directors' pay by introducing binding votes*".[7]

BIS is currently consulting[8] on Vince Cable's proposals, announced in January,[9] to give shareholders better tools to rein in excessive pay. The key proposals are:

- A binding vote for shareholders on future pay policy, in addition to the advisory vote on the previous year's pay.
- A binding vote on exit payments of over one year's salary.
- Requiring companies to publish simpler and more comprehensive information about pay, including a single figure for each director's total remuneration and a 'distribution statement' showing how executive pay compares with dividends, staff costs and investment.

Analysis & FairPensions' Response

- It is disappointing that neither the Queen's Speech nor the accompanying statement from the Prime Minister and Deputy Prime Minister makes any mention of the government's plans to strengthen shareholder oversight. This has taken many commentators by surprise, including the FT, which confidently predicted just the day before the speech that *"plans to give investors more power over boardroom pay will be set out as a key element in the government's legislative programme."*[10]

- The recent wave of shareholder rebellions on pay - dubbed the 'Shareholder Spring' - makes this omission all the more surprising. It would be a mistake to interpret these

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[5] Average levels of dissent (i.e. votes against and witheld) in the FTSE350, taken from ISS Voting Results Report Europe 2011www.issgovernance.com/docs/2011EuropeanVotingResultsReport
[6] http://www.aviva.com/media/news/item/voting-results-of-2012-annual-general-meeting-16915/; http://www.bbc.co.uk/news/business-17938865
[7] http://www.bis.gov.uk/news/topstories/2012/May/queens-speech-2012
[8] http://www.bis.gov.uk/Consultations/executive-pay-shareholder-voting-rights?cat=closingsoon
[9] HOC Hansard 23 January 2012, Col 23: http://www.publications.parliament.uk/pa/cm201212/cmhansrd/cm120123/debtext/120123-0001.htm
[10] http://www.ft.com/cms/s/0/2266d4b2-990f-11e1-9da3-00144feabdc0.html#axzz1uGVJiR9P

events as a sign that shareholders are resolving the issue without the need for government intervention. On the contrary, the enhanced scrutiny arising from the government's focus on improved shareholder oversight has undoubtedly been an important driver of shareholders' newfound willingness to rebel on pay. If anything, these results demonstrate that signals sent by government can make a difference to behaviour in the City. This Queen's Speech therefore represents a missed opportunity to reaffirm the government's commitment to promoting 'responsible capitalism' in general, and stronger shareholder oversight in particular.

- Regarding the proposals in the Enterprise and Regulatory Reform Bill, FairPensions welcomes the introduction of the binding vote, a move we have advocated for some time.[11] However, this alone will not be sufficient to tackle the problem of excessive pay. Recent events have demonstrated that companies do react when their remuneration report is defeated. The underlying problem is that, even in the midst of the 'Shareholder Spring', such defeats remain exceptionally rare.

- If government intends to rely on shareholders to hold companies to account, it must also address the question of who holds the shareholders themselves to account. This should include measures such as mandatory voting disclosure to make institutional investors (such as pension funds and ISA providers) more transparent and responsive to the ordinary savers whose money they manage.

- There is also an urgent need to clarify and modernise investors' legal duties to the people whose money they manage (fiduciary duties). For more on our proposals in this area, see below.

Fiduciary duties

Interpretations of investors' duties to the people whose money they manage are outdated. This threatens consumer outcomes for pension savers and holds back effective shareholder oversight. The need for government action in this area is two-fold.

The law must be clarified to overcome the misperception that investors' duties begin and end with maximising quarterly returns.

- This contributes to a neglect of stewardship and engagement activities and an assumption that investors cannot take account of savers' views or the role of business in society.
- One large pension fund recently received legal advice to the effect that it might be contrary to their fiduciary duties even to exercise their voting rights at company AGMs, if the cost of doing so was not justified by monetisable benefits to the fund.

Government and regulators must promote better understanding and enforcement of investors' true fiduciary duties, in particular the duty to avoid conflicts of interest.

- Asset managers, who are generally responsible for casting votes on behalf of pension funds, will generally have fiduciary duties but this is not widely accepted or understood.
- The Financial Services Bill offers an opportunity to address this problem, but the government has so far resisted amendments to this effect.
- There is anecdotal evidence that conflicts of interest are holding back effective oversight on executive pay and other issues. For example, one recent paper recounts how "*the company secretary of a UK manufacturer reminded a fund manager who was intending to vote against the company's remuneration report that his firm was bidding for an investment mandate from the corporation's pension plan*".[12]

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[11] See http://www.fairpensions.org.uk/sites/default/files/uploaded_files/WalkerReviewSubmission.pdf

[12] Wong S., '*How conflicts of interest thwart institutional investor stewardship*', Butterworths Journal of International Banking and Financial Law, September 2011

Further reading

FairPensions Briefings

'Protecting our Best Interests: Rediscovering Fiduciary Obligation' (May 2011) http://www.fairpensions.org.uk/sites/default/files/uploaded_files/NuffieldParliamentaryBriefing_final.pdf

'The Enlightened Shareholder: Clarifying investors' fiduciary duties' (March 2012) http://www.fairpensions.org.uk/sites/default/files/uploaded_files/EnlightenedShareholderBrief.pdf

The Financial Services Bill (Feb 2012)
http://www.fairpensions.org.uk/sites/default/files/uploaded_files/FSB2R_Feb2012.pdf

Relevant articles

Catherine Howarth, Comment is Free, 1 May 2012, 'Executive pay is out of control - shareholders must step up', http://www.guardian.co.uk/commentisfree/2012/may/01/executive-pay-shareholders

Paul Farrow, Telegraph, 8 May 2012, 'Shareholder power topples Aviva's Andrew Moss – who's next?', http://www.telegraph.co.uk/finance/personalfinance/investing/9251500/Shareholder-power-topples-Avivas-Andrew-Moss.-Whos-next.html

Robert Peston, BBC, 8 May 2012, 'Is it curtains for big executive pay?', http://www.bbc.co.uk/news/business-17987965

Simon Wong, 6 Nov 2011, 'How conflicts of interest thwart institutional investor stewardship', http://blogs.law.harvard.edu/corpgov/2011/11/06/how-conflicts-of-interest-thwart-institutional-investor-stewardship/

Further information
For more information please contact: Christine Berry | Policy Officer, FairPensions | christine.berry@fairpensions.org.uk | 0207 403 7833