The Missing Link: Lessons from the 'Shareholder Spring'

Executive pay was a defining political issue of 2012. The political response has focussed largely on giving shareholders better tools to hold companies to account. The wave of shareholder rebellions over executive pay was widely seen as proof that investors were 'waking up' to their responsibilities. But was it all that it seemed?

New research from FairPensions concludes that we should be cautious about overstating the significance of the so-called 'Shareholder Spring'. We analysed:

- voting information disclosed by asset managers,
- institutional investors' responses to government consultations on pay, and
- pension providers' responses to customer emails sent as part of FairPensions' 'Your Say On Pay' initiative.

While last year's six defeats have clearly had a ripple effect on company behaviour, they did not represent an unprecedented wave of activism. They also appear to have been prompted more by the political and media spotlight on pay than by a fundamental shift in institutional investors' approach to engagement.

Policymakers should now focus on measures to sustain greater shareholder activism after the spotlight moves on.

KEY FINDINGS

- There was no significant trend towards greater dissent on remuneration across the board: analysis by PIRC puts the average level of dissent at 7.64%, compared to 6.4% in 2011.[1]
- There were significant differences between asset managers in their appetite for challenging management: for example, BlackRock, the world's largest asset manager with $3.6trn under management, voted against only one of the seven companies for which it disclosed its votes (of a total of 10 companies we analysed).
- It is difficult to discern a pattern linking those companies who did suffer defeats, either in terms of poor remuneration practice or poor performance. For example, shareholders revolted against WPP CEO Martin Sorrell's maximum bonus of 500% of base salary, but most waved through a maximum 923% of base salary for BP's Bob Dudley.
- Investors' voting disclosures rarely provide explanations for such decisions: of the 20 asset managers we analysed, only one explained controversial votes in support of management – with a further eight explaining only votes against management or abstentions, and 11 giving no explanations at all.
- In the government's initial consultation, nearly three-quarters of institutional investors opposed the introduction of a binding vote on executive pay. For some, this appeared to stem from a reluctance to take on enhanced ownership responsibilities; for others, it was rooted in a belief that the real problem was not a lack of tools but the unwillingness of many investors to make use of existing tools.

POLICY BRIEFING

Fairshare Educational Foundation is a company limited by guarantee registered in England and Wales number 05013662 and a registered charity number 1117244

SHIFTING THE SPOTLIGHT

As the above evidence shows, institutional investors' willingness to exercise shareholder rights robustly is far from a given. Policy debates on pay too often proceed as if the asset managers who usually exercise these rights are the owners of companies, when in fact they are agents acting on behalf of the real owners - the individual pension savers or ISA holders. The logical extension of making companies more accountable to their shareholders is to make institutional shareholders themselves more accountable to underlying savers and investors.

> *"In our view the key is less to invent new tools for investors, rather to ensure that a more significant component of the institutional investor community makes diligent use of existing tools."*
> - F&C

Conflicts of interest

Asset managers may face conflicts of interest when deciding whether to challenge companies on strategy or remuneration. One example from the 2012 AGM season is where shareholder rebellions targeted financial services companies who themselves had asset management arms. We found two strikingly different approaches to managing this conflict:

- Aviva Investors has a clear conflicts of interest policy stating that it will not vote shares in Aviva plc unless in accordance with specific instructions from clients.[2] Aviva Investors did not vote on Aviva plc's remuneration report, which suffered a high-profile defeat.

- M&G, the asset management arm of Prudential, has no specific policy on voting the shares of its parent company.[3] M&G voted in favour of Prudential's remuneration report, which suffered a 30.3% rebellion.

FairPensions has advocated the extension of fiduciary standards of care to all investment intermediaries. Fiduciary obligations require conflicts of interest to be avoided or resolved in the interests of the client. We have also urged investors to follow Aviva's lead and produce more meaningful conflicts of interest policies.

Transparency and accountability to savers

Institutional investors should also be much more directly accountable to the individuals whose money they manage. FairPensions is committed to fostering this accountability. This year, our 'Your Say on Pay' initiative provided an online tool enabling savers to contact their pension or ISA provider asking about their voting intentions on executive pay. We asked savers to forward us any responses they received, and analysed the (anonymised) results. Whilst there were a handful of good responses, the overall picture was disappointing.

Key findings of the 'Your Say on Pay' analysis

- Only 26 responses were forwarded to us, out of 246 providers who received emails from savers. This suggests that a significant number of providers may not have responded at all.
- Eight responses made no reference whatsoever to remuneration, and a further seven acknowledged that this was the issue they had been contacted about but gave no relevant information. This leaves only 11 substantive responses, which varied considerably in quality and detail.
- Only 11 providers confirmed that they would disclose their voting records, and only five gave direct links to webpages where savers could find these disclosures.
- One provider simply said that it *"cannot …respond to requests of individual holders of our funds to provide details of the way in which we have voted."* This fund is a signatory to the UK Stewardship Code Code, whose principles include public disclosure of voting records.
- No one offered to follow up with the saver to let them know how they had voted: even the best responses relied on savers to proactively trawl the provider's public voting disclosures to find the relevant information.

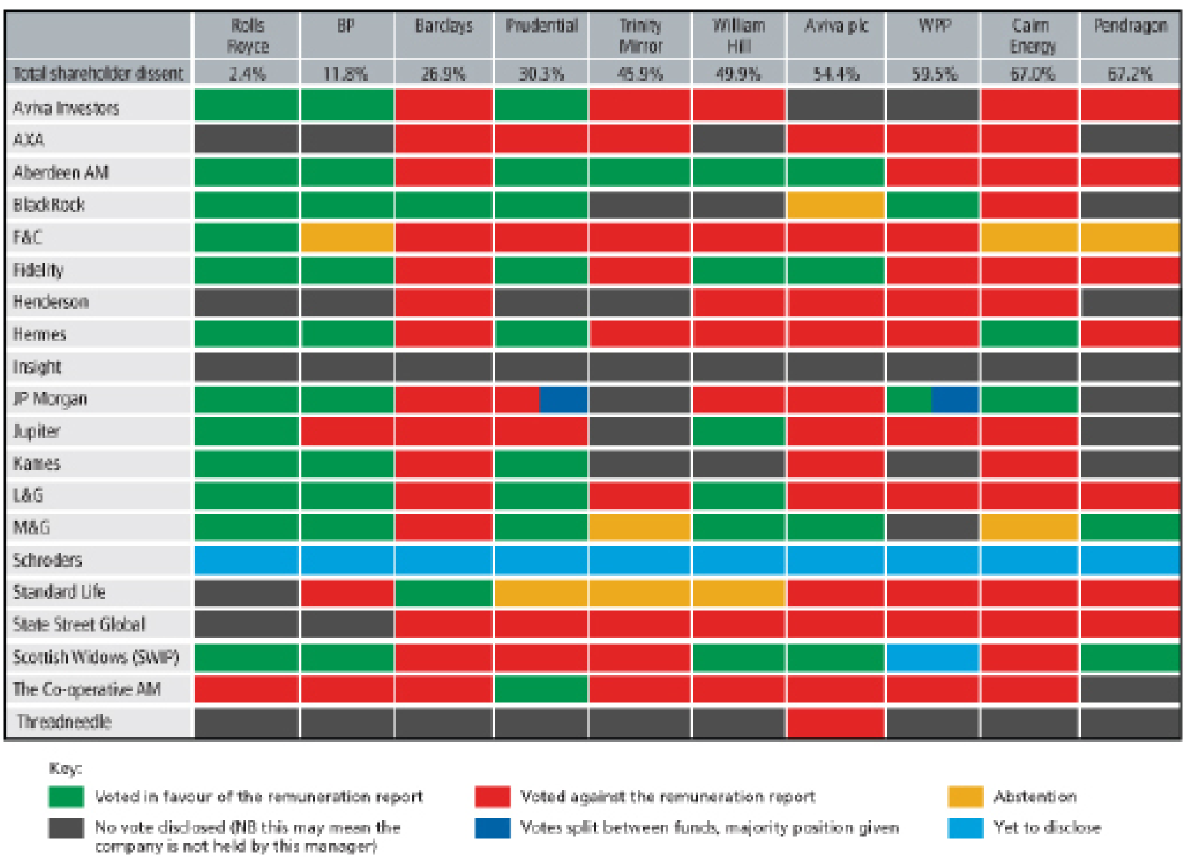
We also investigated how easy it is to find out how the UK's largest asset managers voted on controversial pay packages. We analysed 20 asset managers' votes on ten companies' remuneration reports, and found that, although most now disclose some relevant information, this

- is often difficult to find and confusing to search;
- is often incomplete, e.g. only discloses votes cast a certain way, on certain types of resolution or in certain markets; and
- usually lacks full explanations for why managers voted as they did.

This variation is disguised by aggregate figures on levels of voting disclosure, such as the IMA survey's finding that 73% of respondents disclose some voting information.[4] This figure includes not only those who disclose partial information about individual votes, but also those who disclose only summary statistics about the percentage of votes cast for and against management across their portfolio – of very little use to end-investors.

Research by PIRC suggests that, even among Stewardship Code signatories, the proportion of asset managers disclosing full information is just 21%.[5] Even according to the IMA survey, disclosure levels only improved by 4% in 2010-11, suggesting that the rate of voluntary improvement is beginning to plateau.[6]

Chart: How did fund managers vote on this year's most controversial pay packages?



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KEY RECOMMENDATIONS FOR POLICYMAKERS

- Empower savers to hold to account those who manage their money. This should start with the exercise of the government's powers to require mandatory disclosure of voting activities for institutional investors.

- Clarify institutional investors' fiduciary duties:
  - firstly, to reorient interpretations away from short-term return-seeking and towards long-term stewardship;
  - secondly, to extend this refreshed interpretation to all those with responsibility for other people's money.

  This would help to promote diligent long-term stewardship by institutional investors on behalf of end-investors. We broadly welcome the government's response to the Kay Review's recommendations on this issue.

FURTHER INFORMATION

The full report, *'The Missing Link: Lessons from the Shareholder Spring'*, is available to download at www.fairpensions.org.uk/research. Hard copies are available on request.

If you have any questions about this research or the work of FairPensions, please contact:

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ABOUT FAIRPENSIONS

FairPensions is a registered charity established to promote Responsible Investment (RI) by pension schemes and fund managers, and to ensure that ultimate beneficiaries are well served by institutional investors and other professional agents in the investment world.

RI most often entails engagement with investee companies, including through the exercise of shareholder rights, to ensure that extra-financial issues which pose potential financial risks are monitored and managed.

FairPensions is a member organisation whose members include various organisations representing pension savers, including the National Federation of Occupational Pensioners, UNITE and Unison, as well as thousands of individual pension fund members.

[1] http://www.pirc.co.uk/news/uk-2012-half-year-voting-trends
[2] Aviva Investors Stewardship Policy, http://www.avivainvestors.com/internet/groups/internet/documents/salessupportmaterial/pdf_024453.pdf
[3] Prudential, 'Issues arising from share ownership', November 2010.
http://www.mandg.co.uk/Corporate/Images/Share-ownership_tcm1485-53750.pdf
[4] http://www.investmentuk.org/research/stewardship-survey/
[5] http://www.pirc.co.uk/news/voting-disclosure-revisited
[6] http://www.investmentuk.org/research/stewardship-survey/

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