Written evidence from CORE Coalition Oxfam GB (CGP0027)

CORE Coalition is the UK civil society coalition on corporate accountability. We aim to advance the protection of human rights with regards to UK companies’ global operations, by promoting a stronger regulatory framework, higher standards of conduct, compliance with the law and improved access to remedy for people harmed by UK-linked business activities.

Oxfam GB – Oxfam is an international confederation of 20 organizations networked together in more than 90 countries, as part of a global movement for change, to build a future free from the injustice of poverty.

We welcome the opportunity to give evidence to this inquiry. Contact William Meade <William@corporate-responsibility.org>

Executive Summary:

- Proposed statutory instruments on pay ratio reporting are welcome, but must not be laid in isolation. Further reforms should target the underlying causes of extreme pay disparity and the impact firms have on macro-levels of inequality.

- Important recommendations made by the BEIS Committee in its 2017 report on Corporate Governance in relation to executive pay have not been implemented or encouraged by Government. Implementing them would be a step towards a wider approach to pay disparities. These recommendations include:
  - Phasing out of long-term incentive plans (LTIPs).
  - Developing new metrics of ‘success’ for performance related pay other than profit, including broader corporate responsibilities and a focus on different stakeholders.
  - Creating a ‘people policy’ and reporting on the company’s employment model.
  - Worker representation on remuneration committees and increased two-way engagement with workers on setting pay policy.

- The Committee should consider the issue of executive pay in the wider context of corporate governance reforms and practices. In particular, we stress that extreme pay inequalities have been driven by the enlightened shareholder model and that this root cause can only be fixed by a transition to a stakeholder-based approach to governance.

What progress has been made on implementing the recommendations on executive pay by the previous Committee in its 2017 report on Corporate Governance?

1. The Committee will be aware of BEIS’ proposed statutory instruments in relation to corporate governance and specifically executive pay ratios released for private consultation in February. CORE members welcomed the proposed introduction of pay ratio reporting, especially the median and quartile reporting. We made specific comments on the proposed methodology and approach which we would be happy to share with the Committee.

2. We are, however, concerned that the reforms to pay reporting, done in isolation, will not get to the underlying causes of extreme pay disparity and the impact firms have on macro-
levels of inequality. Moreover, like the Committee, we have been advocating that the Government introduce legislation that aligns pay to broader social and environmental objectives. Accordingly, we expressed our disappointment to BEIS and the minister that action has not been taken to address pay inequality in a more systemic way. We believe that reforming legislation regarding executive and worker pay should be designed to:

i. Remove perverse incentives that reward executives for placing pressure on employee and supply chain worker income. We deem it unacceptable that incentives can reward executives for pushing workers into poverty and harming the natural environment.

ii. Reduce the firm’s contribution to macro-levels of economic inequality which Oxfam’s research has shown: (a) is a barrier to poverty reduction; (b) undermines economic growth; (c) compounds inequality between women and men; (d) drives inequalities in health, education and life chances; and (e) is associated with a range of health and social problems, including mental illness and violent crime.¹

iii. Challenge, often gendered, social norms, that value an individual’s contribution to a firm’s success in a vastly different and unfair way. This contributes to the discrimination and inequality that exist based on gender, race, class and educational attainment.

3. The 2017 Committee report on Corporate Governance made a number of recommendations in relation to executive pay that unfortunately have not been pursued by the Government in its recent reforms. The Government should reconsider implementing these recommendations in developing a more systemic approach to pay inequality.

Paragraph 86: ‘We recommend that companies make it their policy to align bonuses with broader corporate responsibilities and company objectives and take steps to ensure that they are genuinely stretching. Policy in this respect would be considered by the FRC in their corporate governance rating system.’

Paragraph 90: ‘We conclude that LTIPs should be phased out as soon as possible. No new LTIPs should be agreed from the start of 2018 and existing agreements should not be renewed.’

4. The recent collapse of Carillion highlighted the problems with current pay related incentive practices. The use of complex LTIPs and share options set very restricted performance metrics, often encouraging short-term decision making and financial engineering rather than responsible and effective governance. In Carillion’s case, the collapse of the company has occasioned significant social costs. We therefore urge the Committee to encourage the Government once again to implement this recommendation.

5. In addition, we made recommendations in the recent consultation on the proposed FRC Corporate Governance Code that the Code propose the adoption of different performance metrics based on ESG factors, systemic risks and stakeholder satisfaction. This would promote remuneration practices that better align with the long-term interests of the company, its current as well as future shareholders, and its stakeholders. We suggest that the Committee

¹ Even It Up, Oxfam International, October 2014
look at other ways to encourage the integration of these metrics into remuneration package design.

**Paragraph 112:** ‘We recommend that companies should set out clearly their people policy, including the rationale for the employment model used, their overall approach to investing in and rewarding employees at all levels throughout the company, as well as reporting clearly on remuneration levels on a consistent basis.’

6. We agree with the Committee’s recommendation for a ‘people policy’. Building on this we have suggested to BEIS that beyond reporting on pay, reforms should recognise the systemic issue of precarious employment in the UK and suggests that companies should publish the number and proportion of workers employed (a) through an intermediary such as an agency, umbrella party or personal service company; (b) as an independent contractor or freelancer; and (c) on a variable hour contracts, such as zero-hours or short-hours contracts. In each case, the company should state the justification for their use and the role these employment patterns play in the company’s employment model.

7. We have also proposed that the Government set out a long-term direction for changes to the rules that govern executive pay which we would be happy to share with the committee.

8. We would highlight that we have also proposed that the highest paid employee’s total pay should be capped to a ratio of median worker pay. The remuneration committee should set this ratio, and it should be approved via a binding vote at the AGM. This proposal should sit alongside other proposals to increase worker and stakeholder involvement in a company’s ownership and governance structures in order to give them a say in how this ratio, and other considerations about the company’s direction, are made.

**Paragraph 108:** ‘Employee representation on remuneration committees would represent a powerful signal on company culture and commitment to fair pay. This option should be included in the Code and we expect leading companies to adopt this approach.’

9. The proposed FRC Corporate Governance Code does not include a requirement to have employee representation on remuneration committees. In general, the proposed Code encourages a one-way relationship between remuneration committees and the workforce. Despite the extension of remuneration committee remit to look at wider pay policy, the Code does not specifically require the remuneration committee to explain or justify executive remuneration schemes and practices to the workforce. This disregards the opinion of the BEIS Committee report which outlined that there should be ‘meaningful engagement by remuneration committees with the wider workforce’.

10. The committee engagement with the workforce should be a two-way process and the workforce and their representatives should be involved in the discharge of the remuneration committee’s new responsibilities. Ideally, this should include having a worker representative on the committee. However, this engagement could also take place through the established employee voice mechanism should the company choose to adopt the Code’s ‘worker on board’ option.

11. Crucially, we suggest that the Committee examine executive pay in the context of wider corporate governance reforms. Current unequal pay practices result from the
UK's corporate governance framework that prioritises shareholders and profits over the interests of other stakeholders, including workers.

12. In this respect, CORE members support a transition towards a stakeholder-based approach to governance. In the first place, we have expressed our disappointment that the Prime Minister has not followed through with her commitment to ‘have not just consumers represented on company boards, but workers as well’ and instead adopting a weaker range of options on a ‘comply or explain’ basis governed through the FRC. CORE will continue to advocate for far more meaningful involvement of stakeholders in the decision-making process to ensure that power is more fairly distributed among stakeholder groups.

13. We have also expressed our disappointment that the Government has not chosen to address the wording of s.172, which puts member interests above all other stakeholders. S.172 and the concept of ‘enlightened shareholder value’ fails to consider that there is often an inherent trade-off between ‘doing the right thing’ for society and the environment, and profitability. The Government should commit to review the wording of s.172 in a way that puts other stakeholders on a par with shareholders. As a part of this, the law should better encourage the adoption of different metrics of success including the proper capitalisation of the company across human, social, intellectual and other relevant capitals. It should also discourage metrics that contribute to unsustainable levels of inequality or reward directors for harming the environment. At a minimum, s.172 should be amended to include a positive obligation on directors to mitigate against causing adverse harms.

14. As civil society organisations we will continue to urge the Government to implement meaningful reforms on:

i. **Internal governance**: stakeholder representation in decision making, executive incentive structures and directors’ fiduciary duties.

ii. **External governance**: reform the investment system so that our economy incentivises shareholders to own, not extract from, companies; reward businesses who tackle in-work poverty and protect the environment; and give ownership, not just to those who provide capital, but to all those who contribute to a company’s success.

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