Written evidence from Aberdeen Standard Investments (CGP0039)

As one of the world’s largest active asset managers Aberdeen Standard Investments (ASI), the asset management arm of Standard Life Aberdeen plc, takes its responsibilities towards corporate stewardship extremely seriously.

As a global investor with assets under management of £575.7bn (at 31 December 2017), ASI aims to support the companies in which it invests to develop, implement and comply with the highest standards of corporate governance. ASI therefore welcomes the interest of the Business, Energy and Industrial Strategy Committee in this issue and the opportunity to contribute to its short inquiry into executive pay.

Standard Life Aberdeen was created in August 2017 through the merger of Standard Life plc and Aberdeen Asset Management plc. In addressing the committee’s points it is necessary to recognise that Standard Life Investments (SLI) and Aberdeen Asset Management (AAM) operated independently of each other up to this point. However, SLI and AAM both have strong track records in holding company boards to account and seeking to influence good corporate governance policy. This represents a strong legacy on which the merged company is well placed to build and exercise stronger influence.

In addition to the information provided in the answers below, further details of our work on corporate governance is contained in our 2017 stewardship reports which are published on our website:


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

The previous committee made a wide range of recommendations and in the interim the Financial Reporting Council (FRC) has undertaken a public consultation with a view to updating and strengthening the UK Corporate Governance Code. The Code – in conjunction with the UK Stewardship Code - has successfully raised standards in the UK. However, as envisaged when they were put in place, these codes are now in need of a comprehensive review and revision to raise standards yet higher and take account of recent developments. While the core concept of the codes remain valid and should continue, we have made the following recommendations on the Corporate Governance Code:

- It should remain a high level statement of principles, as opposed to being detailed and prescriptive, and we believe it should be shortened and sharpened to make it clearer and more concise.

- It should continue to embody a ‘comply or explain’ approach which requires companies to explain how the principles are met. However, we would like to see a more intelligent explanation from companies as to how they embrace and satisfy these principles rather than just ‘tick box’ compliance.

- It should continue to work in tandem with the UK Stewardship Code and the success of both Codes relies on corporate boards and institutional investors being accountable for the roles they play.
The review process is ongoing and an updated Code is expected to be published over the summer. On that basis we would expect any changes in the Code to be applicable from the accounting periods beginning 1 January 2019 with any impact becoming apparent during 2020. It is likely that a number of the recommendations in the previous committee’s report will be included in the revised Code.

2. What improvements have been made to reporting on executive pay in the last 12 months?

As a major investor we are supportive of initiatives which improve transparency and accountability. Within the next few weeks the Government will publish legislation which will require listed public companies to publish and explain the pay ratio between CEO and average employee salaries. This builds on the requirement on companies with more than 250 employees to disclose data on their Gender Pay Gap.

We believe it is important that executive remuneration is justifiable when considered against pay across the company as a whole. We are therefore supportive of greater transparency and the additional data on pay ratios and the gender pay gap will enable us to have better informed discussions with remuneration committees.

As mentioned above, the FRC’s review of the Corporate Governance Code is still underway and it may be some time before we see any structural change. In the interim the introduction of the Investment Association’s register of significant votes against management resolutions (of 20% or more on pay and other resolutions) has been an important development. We have noticed when undertaking remuneration consultations that companies have generally been more willing to listen and amend policies that are not receiving shareholder support. We see this as a sign that the process continues to develop for the better.

There continues to be some instances where badly designed remuneration arrangements have resulted in outcomes which detract from the general improvement in remuneration policies and outcomes. A recent example was the proposed remuneration package for the CEO of Persimmon plc. Due to a combination of factors, the CEO was expected to receive a long-term incentive award worth in excess of £100m through the company’s long term incentive scheme. After we and other shareholders expressed concerns this award was reduced to £75m. However, we did not regard this reduced award as acceptable and we voted against it at the company’s AGM on 25 April 2018.

Euan Stirling, Head of Stewardship and ESG Investment, made a statement at the AGM in which he expressed dissatisfaction on behalf of our clients and underlined the threat to the company’s reputation of such a grossly excessive award.

“…the executive team at Persimmon have been very successful and are highly regarded in the industry for their technical and managerial expertise. But being a company director, and in particular a Chief Executive, requires more. It requires a broader context. It requires a personal motivation that goes beyond simply amassing a fortune. It requires an understanding of where the company sits within the society within which it operates. Little of that is evident currently at Persimmon.”

It is ‘outliers’ such as Persimmon which distort the debate around executive pay, raising concerns about a misalignment of interests between senior executives and stakeholders, including employees. As a major investor our position is that companies should be able to design remuneration policies that allow them to attract and retain talent. However, this must take account of the views of other stakeholders, including the wider workforce and society as a whole, to ensure that all risks including damage to a company’s reputation are adequately considered. Remuneration committees should also frame their Long Term Incentive Plans...
(LTIPs) in a manner that is linked to the company strategy; designed to deliver corporate success while ensuring they deter behaviours and decisions that could benefit individuals in the shorter term but have detrimental consequences on the long term success of the company.

If LTIPs are to be viewed as mechanisms to encourage company decision making to consider the consequences in the long term rather than rewarding short term outcomes, remuneration committees may need to review their methods of remuneration. Better alignment of executive decisions with long term consequences could be achieved through the creation of a mechanism – possibly through significant personal equity holdings in the company - where senior executives have their wealth at risk from the decisions they make rather than their annual income.

3. What steps have been taken by Remuneration Committees and institutional investors to combat excessive executive pay in the last 12 months?

In our experience most listed companies consult with shareholders on their remuneration policies with a constructive dialogue being the norm rather than the exception. Companies appear to be aware of the public push back on excessive pay and more willing, in most cases, to address it. The introduction of binding votes on remuneration reports (from 2014 onwards) may have helped to encourage this kind of behaviour.

As a major investor we devote significant resources to our engagement with remuneration committees. In most instances this has a positive outcome. However, where the process does not reach a satisfactory result we have the option of voting against remuneration resolutions, as we did in the case of Persimmon. While we regard this as a last resort after all other options have been exhausted, we have no hesitation in doing so when we feel it is necessary.

Last year Standard Life Investments voted against 13.9% of remuneration resolutions put forward by UK listed companies, while Aberdeen Asset Management voted against 10.2% of remuneration resolutions.

4. What further measures should be considered?

The UK has a highly developed and effective framework of legislation and corporate governance codes and is viewed as a world leader by many other countries. It is important, however, that companies, investors and regulators such as the FRC continue to raise standards of stewardship and engagement, thereby ensuring the UK retains this pre-eminent status.

As stated above, we believe it is important that pay structures and levels of executive remuneration are justified with regard for the levels of pay across the company as a whole. In many instances this explanation would be more beneficial than disclosure of a particular ratio. We note that the Investment Association encourages the use of the ratio between the CEO pay and the median employee, and the CEO and Executive Committee to provide context to remuneration decisions. We support this view while encouraging companies to better justify executive pay in terms of the overall remuneration arrangements across the company as a whole.

Improving standards of corporate governance goes well beyond the boundary of executive remuneration. It should also consider other factors such as requiring companies to explain how they are considering the interests of all stakeholders. Remuneration decisions made by a company are often indicative of broader governance performance. However, we recognise
that executive remuneration is a major consideration and one which has significant relevance to the level of public trust in business generally.

As acknowledged in the Government's corporate governance Green Paper, remuneration policies can be extremely complicated, particularly the metrics and targets used to calculate annual bonuses and long term incentives. It is clear that remuneration committees can find it difficult to calibrate targets to deliver the pay outcomes that either they or shareholders are happy with. In many cases, supposedly stretching targets have proven easier to deliver than expected (e.g. Persimmon). If remuneration committees find it difficult to set appropriate targets, it is unlikely that shareholders are better placed to assess their effectiveness.

In our previous submissions to the committee (in October 2016) SLI and AAM made separate recommendations aimed at aligning the interests of senior executives with shareholders. We believe some of these recommendations remain valid. Specifically:

- Creating a stronger connection between executive decision-making and long term success by requiring senior executives to retain a personal shareholding in the company which gives them exposure to share price movement and dividend policy well beyond the timeframe for traditional long-term incentive plans.
- A company that achieves less than 75% support for its remuneration report should be required to submit a revised remuneration policy at its next AGM.
- Greater alignment of interests between all aspects of the workforce by giving employees greater access to share save, profit participation and similar schemes (thereby reflecting their experience, performance and skills).
- Mandatory disclosure requirements which assist shareholders in their evaluation of quantum and alignment to corporate performance.

Responsibility for openness and transparency should not sit entirely on the companies and should extend to those who invest on behalf of their customers and clients. We believe our clients and those of other asset management firms should hold their managers to account in their delivery of these services, and transparency over voting and engagement activities brings this accountability into focus.

The UK Stewardship Code and the FCA regulations encourage asset managers to provide reporting on adherence to the Code, but there is still some way to go in creating the required transparency and accountability. We therefore support mandatory disclosure requirements for fund managers to provide their voting records and their use of proxy voting or voting advisory services which will be introduced through to implementation of the amendments to the Shareholder Rights Directive.

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