Written evidence from Glass Lewis (CGP0040)

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We would like to comment selectively on a few of the questions for which we feel we can add some value to the discussion.

Gender pay gap

Is the annual information related to pay required under the Equality Act 2010 sufficient? Should any further information be required?

We believe the information currently required is sufficient to identify those companies that are struggling to advance women to senior roles, which is pertinent to the apparent slowdown in appointments of women to boards and associated concerns regarding the relative paucity of the executive pipeline. However, we believe that requiring additional disclosure, in particular relating to junior appointments and the broader processes used in relation to hiring, promotions and talent development, would provide stakeholders with a more complete understanding of the company’s approach to the issue.

By way of an example, the level of disclosure of specific initiatives vs the use of boiler-plate language varies significantly across reports. Currently, many companies explain their pay gaps by pointing to the fact that there are more men in better paid senior roles, with the implication that balancing out the pipeline will, eventually, address this issue. We recognise the importance of a balanced pipeline, but note that gender pay gaps may persist throughout organisations, rather than just at the top. As such, we believe that requiring enhanced
disclosure, including breakdowns of gender representation (and pay) across all employee levels, would be appropriate.

What requirements, if any, should there be on companies to address gender pay gaps?

As discussed above, we believe that additional disclosure requirements are the best avenue for addressing gender pay gaps. Such information allows shareholders and other stakeholders to make more informed decisions when engaging company leadership on this topic.

Executive pay

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

The BEIS Committee's April 2017 report recommendations have influenced a variety of stakeholders.

Several recommendations were directed toward the FRC. Some of these have been included in proposed amendments to the UK Corporate Governance Code, including expanding the remit of remuneration committees to address pay and engagement throughout the wider workforce, and requiring that remuneration committee chairs have served at least twelve months on the committee before leading it. On the topic of shareholder voting, the BEIS Committee report suggested using binding shareholder votes and requiring mandatory remuneration committee chair resignation in cases where opposition is significant (which it defined at 25%). While the FRC has not proposed binding votes or mandatory resignation, pending changes to the UK Corporate Governance Code include enhanced requirements that companies publicly respond when opposition to any proposal is significant (defined as 20%).

Two BEIS Committee recommendations are not included in the pending Code changes: publication of pay ratios and moving away from long-term incentive plans toward deferred equity plans. The FRC has noted that it may revisit the issue of pay ratios after pending legislation is finalised. We have seen many "voluntarily" report pay ratios (BAE Systems, Man Goup & Rolls-Royce) and others, such as Hammerson and William Hill put forward their rationale for not disclosing in favour of waiting for a specific calculation method to be put forward.

The broader recommendation regarding incentive structures appears to have had a mixed reception throughout the market. Whereas the BEIS Committee called for no new LTIPs to be approved, to date during 2018, several dozen companies have proposed new LTIPs or amended/renewed existing LTIPs. In addition, most companies that had, during 2017, proposed plans that align with the BEIS recommendation for “a simpler structure based primarily on salary plus long-term equity” ultimately withdrew these proposals facing shareholder opposition. The
exception was Pets at Home Group plc which received relatively strong support for its RSU plan, which was structured to satisfy the criteria suggested by the Investment Association. In 2018 Weir Group proposed a RSP which received greater than 90% support this year, having previously proposed a RSP in 2016 which was not approved by shareholders. Notably, this year's RSP included a financial underpin and incentive limits represented a 50% decrease as per IA's recommendations.

Notably, the recommendation on incentive structures has stimulated significant debate and evaluation of this subject among corporate issuers, investors, consultants and service providers. While opinions remain divided, many investors would agree that a simplified incentive structure is not a "one-size-fits-all" approach to addressing pay gaps or misaligned incentives. Indeed, many market participants, including Glass Lewis, believe that performance-based long-term incentive plans can be an important and necessary vehicle for aligning executive interests with those of other stakeholders. Many companies have taken a cautious approach to consideration of the BEIS recommendation noting that simplified plans replacing LTIPs without appropriate safeguards or reductions in quantum may have the unintended consequence of guaranteeing large payouts that do not accurately reflect the value created by a company. In light of the ongoing debate over this issue, we would expect additional companies to adopt incentive structures that align with the BEIS recommendations; however, we would not expect wholesale adoption at this time.

With regard to the recommendation that bonuses be stretching and aligned with company objectives, many of the companies that we have analysed in 2018 to date have, as compared to prior years, provided additional disclosure explaining how these metrics relate to strategy.

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

In addition to the enhanced disclosure surrounding bonus metrics and targets we have seen an improvement in the disclosure provided by remuneration chair statements. In general, for 2018 the committee chair statements provide more detail as to the implementation in the past year, particularly around metric and target setting and shareholder engagement.

**What steps have been taken by Remuneration Committees and institutional investors to combat excessive pay in the last 12 months?**
Most companies that did not previously implement specified limits on equity awards to executives have now done so (e.g. TP ICAP). However, there are some notable exceptions (e.g. Safestore, Pendragon, ZPG plc).

A handful of companies have now implemented hard caps on the value of vested equity awards (e.g. Anglo American, Berkeley Group in 2017), which provide transparency and certainty as to the maximum potential headline figures of future pay outcomes. We have also seen the introduction of salary caps at Centrica plc, Aggreko plc (2018) & Hammerson plc, Spectris plc & Drax Group plc (2017).

We have witnessed an improvement in committee responsiveness and engagement. This may have been at least partly driven by the BEIS initiative which led to the Investment Association public register. Two particular examples are Persimmon and Weir Group, which responded meaningfully and publicly to shareholder opposition.

Institutional investors have increasingly voted against excessive pay packages, pressured boards to reduce or moderate pay levels, and stopped pay increases based on benchmarking exercises from coming into effect. Evidence of this can be found in a number of remuneration proposals that were not approved, withdrawn, or received a significant number of dissenting votes.

**What further measures should be considered?**

We believe that the most fruitful measures will be those that encourage greater transparency, standardise disclosure requirements (such as pay ratio calculations) and encourage board responsiveness to stakeholders in their organisations.

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