FTI Consulting Governance Event 2023

FTI Consulting hosted its seventh annual corporate governance event in Dublin on 12 October 2023, with speakers from some of the world's leading institutional investors and proxy advisors, Capital Group, Vanguard, Glass Lewis, and ISS. The discussion focussed on the key themes emanating from the 2023 AGM season and investors' evolving expectations around reporting, engagement and voting for the coming six months.

The event consisted of a keynote address from Vanguard, followed by a panel discussion with Capital Group, Vanguard, Glass Lewis, and ISS, and concluded with a reporting workshop from Glass Lewis. During the panel discussion, the corporate governance and stewardship representatives from Capital Group, Vanguard, Glass Lewis, and ISS each outlined their respective views on engagement and reporting and whether they were having the desired impact of enhancing governance and stewardship practices across capital markets. Each representative also provided additional insight and context into their organisation's approach to evaluating company practices regarding remuneration, board effectiveness, committee structures and the oversight of ESG risks and opportunities, among other issues.

While remuneration was inevitably a key focus – particularly against the backdrop of the cost-of-living crisis and the potential windfall gains from 2020 LTIPs – the panel also covered the independence and overall composition of boards and their committees, the competitiveness of the UK and Irish markets, whether governance and remuneration considerations are truly a barrier for companies looking to list in the market and how ESG factors are impacting proxy voting, if at all. Despite the differing views on some topics, it was clear from the panel discussion that companies' ability to provide clear and meaningful disclosure, alongside open shareholder engagement, is the benchmark standard for investors and proxy advisors. The workshop section of the event, which was delivered by Glass Lewis, brought to life much of the panel discussion, and provided real-life examples of what good reporting looks like.

Following the event, our governance team has set out six key takeaways for the period ahead:

Executive remuneration always matters

Changes to executive remuneration were under the microscope again in 2023, with any changes to remuneration being reviewed in the context of wider employee pay levels and cost-of-living crisis. With investors noting that, while quantum constitutes a key component of their review, the approach taken by boards and remuneration committees in defining pay practices is the most fundamental aspect of their analysis. With a significant focus from investors on the experience of a company's wider stakeholders, including through the cost-of-living lens, the panel noted the importance of understanding the remuneration committee's rationale for any salary increases, in particular. According to the panel, reporting on executive remuneration should provide detail into the merits of any changes to pay for executives, and provide context to the process by which the board reviews its approach to ensure the retention and motivation of talent across the entire organisation.

With LTIP awards granted in 2020 and 2021, during a period of capital market turbulence due the Covid-19 pandemic, vesting in 2023 and 2024, investors and proxy advisors noted their approaches to evaluating the potential for inflated vesting levels, known as 'windfall gains'. The panel recognised that, although the scrutiny on windfall gains became an important consideration in finalising votes and recommendations on remuneration reports, a number of remuneration committees did provide clear disclosure of their discussions and deliberations in annual reports.

As we enter 2024, the focus from investors and proxy advisors will remain on how effectively companies are justifying pay decisions and outcomes to the outside world. In particular, scrutiny will be on how companies are detailing the rationale for any changes and the input from shareholders through engagement and consultation.

Voting on directors is more than a checklist exercise

The panel recognised the concerns around election of director proposals being viewed as a checklist exercise – particularly in relation to diversity, overboarding and board skills. While these constitute important features of a strong board, its composition should be reviewed holistically and in the context of the company's structure and operations. One panellist specified that the independence of the board constitutes the starting point for any evaluation, after which everything else can be negotiable, reflecting the idea that the role of non-executive directors is ultimately to represent shareholders' interests. The panel debated whether reviewing board composition based on the achievement of specific diversity targets and overboarding thresholds constitutes the most appropriate approach to assessing board effectiveness. The panel also noted that reporting around the role of the board in the oversight of ESG has improved, in part driven by the requirements for TCFD reporting across companies in the UK. Unsurprisingly, 'overboarding' was discussed at length, with the panel accepting that the increased expectations of directors, which has driven tighter views on the acceptable number of board seats, may also result in increased director fees, but only when well justified. Ultimately, the goal is for boards to detail the merits of its composition and provide detail on how the skills and experiences it possesses support oversight of strategy and risk; while, in the event of any gaps in experience, how it plans to address them.

A company's ESG strategy should not be viewed in isolation

The panel shared their views that ESG-related risks should be viewed by the board with the same rigour as any other material financial risks, and that environmental and social targets should be incorporated into a company's wider business strategy. In this context, instead of replicating governance structures for environmental and social matters, companies should integrate these considerations into the well-functioning governance structures that are already in place.

The introduction of ESG metrics into executive remuneration structures could be reviewed through the same lens, in that these metrics should only be included if central to the business strategy, and not as a response to perceived shareholder expectations. On the topic of climate-related proposals, the panel pointed to the decrease in the number and support of say-on-climate proposals, and that holding companies accountable to their sustainability strategy goes far beyond say-on-climate and similar proposals. Instead, the focus should remain on board skills, accountability, and effective oversight.

Engagement and reporting are key to good governance

Reporting constitutes one of the biggest opportunities for companies to set out all the key actions, initiatives, and efforts of the business over the prior year. Robust and meaningful reporting provides investors and stakeholders with insight into the actions and outcomes of the companies' governance and strategy, and its alignment with shareholders' long-term interests. During the workshop, important tools to strengthen reporting were detailed, including: the usefulness of outcomes-based reporting and case studies, the narrative around key data points, and the benefits of signposting in the context of an increasingly complex reporting environment.

However, reporting on its own may not always provide the full picture and can be strongly enhanced through direct engagement with investors and proxy advisors. Engagement provides investors with the opportunity to build a better understanding of a company's approach. Companies can use engagement to bring reporting to life, directly detailing the merits of decisions on remuneration, governance and ESG. As the approach to engagement moves from being a transactional process, reserved for discussing contentious issues, to becoming an opportunity for companies and investors to stay connected, the panel invited companies to reach out on a more regular basis and not just once a year. The panel did, however, remind the audience that engagement does not always have to be a one-hour in person meeting, but it could be a short call, or even an email setting out a key change. The speakers noted the limited resources for more meaningful engagement during proxy season, and certain investors and proxy advisors' policies, which impede engagement after the publication of a company's notice of meeting.

'Comply-or-explain' versus 'comply-or-else'

Certain stakeholders have questioned whether the latest iteration of the UK Corporate Governance Code ('the UK Code'), which is currently being consulted on, is serving as it intended, with its overarching principles potentially being interpreted too strictly by investors, allowing little room for explanation as to the merits of a deviation. The panel noted that the UK Code constitutes a principles-based approach set out to provide guidance on how companies should approach key governance considerations, from a 'comply-or-explain' perspective. Indeed, the panellists detailed how a one-size approach to corporate governance is not desirable; however, whether this translates across the market and in the heat of AGM season is a different question. In support of its view, Glass Lewis referenced its proxy season review, noting that of 26 instances of 'non-compliance' with the UK Code on Chair tenure, it only recommended against the chair of the nomination committee in seven instances.[1]

Governance and the competitiveness of capital markets

In light of recent examples of UK and Irish companies taking up US-based listings, as well as the slowdown in the number of IPOs, the competitiveness of capital markets was a thread throughout discussions. The panel noted that the rationale for many companies listing in the US is not necessarily governance or remuneration-related and, instead, may reflect the geographic footprint of the business, access to a deeper pool of capital, a more comparable peer group, higher US valuations – or indeed a combination of all these factors. The panel and guests discussed the opportunity for the Irish market to distinguish itself more strategically in the post-Brexit environment, including through the potential for a separate Irish Governance Code. The speakers were firm though in their conviction about the strength of the UK Code, with issues related to interpretation as opposed to overarching aims.

The team at FTI Consulting

The focus on robust reporting and meaningful shareholder and proxy advisor engagement, should constitute a top priority for companies as preparations for the 2024 proxy season ramp up. FTI Consulting's Strategic Communications team brings together experienced corporate governance, ESG and communications professionals who have a deep understanding of the proxy advisory and stewardship landscape with a proven track record in helping companies shape better outcomes through effective reporting and engagement.

[1] Glass Lewis, 2023 UK Proxy Season Review, available at: https://www.glasslewis.com/webinars-and-events/

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