37

When Shareholders Have a "Say on Pay"

Shai Ganu

In recent years, against the backdrop of a sluggish global economy and depressed stock prices, the call from shareholders to regulate executive pay is becoming too loud to ignore.

Regulatory developments in Europe, Australia and North America giving shareholders greater oversight of executive pay and curbing bonuses in the financial services sector reflect a hardening of attitudes among politicians, investors and the general public.

This "Say on Pay" movement is now gaining ground in most of the advanced economies for shareholders to express their views regarding companies' executive remuneration practices.

THE SAY ON PAY VOTE

How Say on Pay works is typically by a voting exercise on remuneration-related issues at the company's annual general meeting.

Votes are cast either on the overall Remuneration Report (or Directors' Report), or on specific remuneration-related resolutions. The latter can range from the company's remuneration philosophy to the detailed remuneration packages and performance measures for named executives.

Shareholders and advisers are generally most active in ensuring that performance targets are sufficiently challenging to justify high levels of remuneration as well as ensuring that termination payments are not excessive.

Depending upon the jurisdiction, Say on Pay votes can be "advisory" or "binding".

In a binding vote system (which is enacted in the UK and several other EU countries), shareholders have a legally binding vote on remuneration outcomes for the year just completed, as well as the remuneration framework and targets for the forthcoming year.

In an advisory vote mandate (such as in the US, Canada and Germany), however, shareholders vote on remuneration-related resolutions, but the votes do not compel action on the part of the company. Instead, they allow shareholders to express their satisfaction or dissent regarding the company's remuneration decisions. In cases where companies receive a high "no" vote, it sends a strong signal to the company to make changes for the following year.

CONSIDERATIONS FOR SINGAPORE

Singapore is one of the few developed economies that do not have in place a Say on Pay mechanism for shareholders.

Remuneration disclosures are governed by the Code of Corporate Governance (the Code), which takes a principles-based approach to governance and disclosures. Publicly listed companies are expected to comply with the Code guidelines, or adequately explain the reasons otherwise.

However, the SID-SGX *Board of Directors Survey 2015* showed that 55 per cent of listed companies did not disclose the precise remuneration of each individual director and CEO as required by Guideline 9.2 of the Code. The explanations given in annual reports are usually about competitiveness and confidentiality.

The introduction of Say on Pay could potentially solve this problem and lead to better remuneration disclosures.

More importantly, remuneration committees and boards will be mindful of their pay strategies and would likely more carefully ensure that there is proper alignment between business performance and pay. Say on Pay can also lead to more effective engagement between companies and investors as companies seek to consult shareholders earlier in the pay-setting process.

It may also encourage companies to promote from within and focus more on succession planning.

On the other hand, the experience in other jurisdictions suggests that there are negative aspects and unintended consequences associated with Say on Pay.

Investors may need to spend more time analysing pay programmes. Shareholders may also increasingly rely more heavily on proxy advisory firms for voting on pay-related resolutions.

If the Say on Pay mechanism ends up being more prescriptive than it ought to be, it could reduce executive mobility or result in key executive talent moving to markets where pay is less tightly regulated.

Companies may also end up adopting "plain vanilla" or "off the shelf" executive remuneration plans, rather than designing plans best suited to their objectives just so that they do not deviate from market norms.

WHETHER OR WHEN

Say on Pay is without a doubt a trending movement in the corporate sphere. But the jury is still out on whether and when it will make its way to Singapore shores.

However, what should be important for remuneration committees to be cognisant of are the underlying sociopolitical concerns regarding inequality in pay and the perceived excessive levels of remuneration for senior executives that have led to the Say on Pay movement in the first place.

Remuneration committees should proactively ensure that these concerns are appropriately addressed in their design of remuneration schemes, and the approval of remuneration levels that are commensurate with company performance.

Meanwhile, boards are well advised to ensure that they fully comply with the Code on remuneration disclosures. If the poor level of compliance with this requirement continues, it may prompt regulators to do more in this area, perhaps even encouraging the institution of Say on Pay mechanisms. ■