The ‘shareholder spring’ is back and bigger than ever

Shareholder voting in the 2016 AGM season so far

For the past few years the media have been quick to print headlines proclaiming shareholder rebellions but 2016 is proving to be the toughest yet and in many cases the headlines reflect some real challenges for companies. There have already been several high-profile instances where companies have failed to gain sufficient levels of support from shareholders for resolutions relating to remuneration to be passed. We have also seen the first instance where a binding policy vote has failed to gain shareholder approval, leaving the company with no option but to continue with the existing policy.

Although we are only partway through the AGM season, there is already a clear sense that companies are finding it more of a challenge to justify their remuneration arrangements to shareholders. At this point in the season, proportionally fewer FTSE 100 companies have received ‘strong’ votes of at least 90% of votes cast in favour than ever before (74% compared to historical levels of 80-84%). In FTSE 250 companies the proportion of ‘strong’ votes currently stands at 76%, which is a similar level to that of the ‘shareholder spring’ of the 2012 season.

Retrospective disclosure of annual bonus targets

THE HOT TOPIC OF 2016?

Annual bonus target disclosure was anticipated to be a key area of shareholder scrutiny during the 2016 season, following guidance from the Investment Association in November 2015.

COMPANIES HAVE RESPONDED

For the most part companies appear to have responded to this focus and we are seeing a clear shift in market practice, moving towards more detailed disclosure around the performance targets used to determine bonus outcomes.

SHAREHOLDERS NOW EXPECT MORE

Proxy voting agencies have so far flagged retrospective bonus target disclosure as a concern more than any other remuneration issue. However, our analysis suggests that poor target disclosure alone is unlikely to cause a significant vote against, with just two instances where this appears to have been the key issue.

So what are the biggest concerns raised by shareholders?

Most companies would consider a vote of less than 80% to be a strong signal that remuneration arrangements are not acceptable to shareholders in their current form.

Of those FTSE All Share companies receiving votes of less than 80% so far in 2016, our analysis suggests investors have consistently raised similar issues in relation to remuneration reports and policies.

The table overleaf provides greater detail on the most challenging issues for companies this season. It is important to remember that there are often a number of issues contributing to the votes against.

A ‘no’ for restricted share awards?

This season one FTSE 250 company proposed a new remuneration policy that responded to the call for simpler remuneration arrangements which best suit the specific needs of the business. The new policy featured a restricted share plan under which long-term awards would be made without performance conditions alongside significantly smaller PSP awards.

Shareholders rejected this policy, primarily asserting that restricted share awards are not in line with market practice in the UK. This is interesting given that the Executive Remuneration Working Group’s Interim Report has indicated that the use of restricted share awards may be highlighted as a favourable option in the Group’s final recommendations. The outcome of this remuneration policy vote demonstrates that the Executive Remuneration Working Group have some work to do to convince investors that the simplification of remuneration arrangements should be achieved by the use of restricted shares.

Increases in quantum	Link between pay and performance	Pro-rating of incentives for leavers
Decisions that lead to significant increases to executive directors' total pay packages are a big concern for investors. Investors have raised concerns in relation to: • Significant increases in variable incentive opportunity. • Substantial salary increases, which have a knock-on effect on the size of the total package. • Granting exceptional awards. These issues are often exacerbated by targets which are lower than those set previously or are considered to be insufficiently stretching.	Investors are making it abundantly clear that they expect remuneration committees to exercise appropriate discretion in order to ensure that incentive outcomes and awards reflect the wider performance of the business and align with shareholder interests. Companies have faced a negative reaction for: • Exercising discretion that results in higher payouts for executives when original targets have been missed. • Adjusting targets resulting in larger payouts. • Failing to adjust large incentive awards and outcomes in the context of poor company performance.	Managing the remuneration arrangements of executive directors when they join and leave the company continues to be a highly sensitive area. For a number of the companies receiving low remuneration votes so far in 2016, the key issue for investors is a lack of pro-rating of incentive awards for outgoing executives. From a shareholder perspective this does not necessarily demonstrate an appropriate link between pay and performance.
Our analysis suggests that so far issues relating to quantum have been raised by proxy voting agencies as the key issue at 11 FTSE All Share companies that received votes of less than 80% in favour. These votes ranged from 51% to 79%.	Our analysis suggests that so far issues relating to the link between pay and performance have been raised by proxy voting agencies as the key issue at 6 FTSE All Share companies that received votes of less than 80% in favour. These votes ranged from 41% to 75%.	Our analysis suggests that so far pro-rating of incentives for leavers has been raised by proxy voting agencies as the key issue at 4 FTSE All Share companies that received votes of less than 80% in favour. These votes ranged from 58% to 78%.

Deloitte view

A review of the 2016 AGM season so far demonstrates the strength of feeling shareholders have around certain issues such as significant changes in quantum, termination and recruitment and the active use of remuneration committee discretion. These can all be sensitive issues with many factors to take into account, requiring a well informed and robust decision-making process.

There is currently a debate around the simplification of executive pay and whether a more holistic and tailored approach should be taken to ensure that remuneration arrangements are suited to the needs of the business rather than a 'one size fits all' approach. In our view a key issue in this debate is for shareholders, proxy services and companies to fully engage with one another when new arrangements are proposed. Companies should clearly articulate the business case for their proposals and shareholders should provide clear feedback in time for companies to modify proposals as part of the engagement process. Active engagement from both sides should ensure that all parties are able to make fully informed decisions and any issues are identified and hopefully resolved ahead of the publication of the annual report.

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