Local Authority Pension Fund Forum

LAPFF Newsletter

June 2003

LAPFF adopts tough policy on directors' pay

The Forum has agreed a wide-ranging series of best practice guidelines on boardroom pay, and has been assessing how far company remuneration reports comply with this policy. Where companies fall short, LAPFF is issuing 'Alerts' to members so they can consider a co-ordinated voting response.

Previously the Forum has had policies on particular aspects of remuneration such as share option scheme performance targets and on the length of directors' contracts. The decision to widen the Forum's approach and develop a more comprehensive policy follows this year's legal changes that require a shareholder vote on company remuneration reports at all listed companies.

The policy covers all the key aspects of directors' pay. On disclosure the Forum is calling for disclosure that goes beyond the legal minima particularly on valuation of share option awards, the relationship of boardroom pay with other employees and annual bonus targets.

The policy cautions against excessive salaries: "we encourage companies to pay at or below median for their sector, rather than paying above median which simply leads to an inevitable upwards spiral". The guidelines focus on the need for remuneration structures to be geared to performance: "Misalignment of pay and performance has the potential to set inappropriate incentives usually by rewarding executives regardless of performance...".

The Forum favours the use of performance targets that measure performance against competitors or which set targets higher than current market expectations. It also supports directors making a financial investment in a company before participating in option schemes. On contracts, which have proved the most controversial issue this proxy season, the Forum's policy backs notice periods of no more than one year and pre-determined compensation payments limited to no more than one year's salary.

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LAPFF director pay policy cont.

PIRC, LAPFF's research and engagement partner, is monitoring remuneration reports against this policy and has developed a unique scoring system to identify companies which breach the guidelines most seriously.

Since March, LAPFF members have been alerted to issues at 15 companies: British Vita, Reuters, Schroders, Aggregate Industries, Countrywide Assured, Provident Financial, Reckitt Benckiser, Spirax-Sarco, Xstrata, GlaxoSmithKline, Hilton, Novar, Tomkins, HSBC and Tesco. In all cases PIRC found that both performance targets for long term incentive schemes were inadequate compared to the level of potential payout and that directors' contracts were excessive.

LAPFF Deputy Chairman, Cllr John Saunders from Newham Superannuation Fund attended the AGM of GlaxoSmithKline and voiced the Forum's concerns.

Referring to the executive share option scheme's performance target of only real earnings per share growth of 3% a year, Cllr Saunders said."We would argue that this is an unambitious target - to say the least - for a global pharmaceuticals company. Dr Garnier [the CEO] was granted options worth 11 times his salary last year under this scheme. How can you justify this performance target? Does it not represent a clear example of providing huge potential rewards for achieving insipid performance?"

As has been widely reported, for the first time ever a majority of shareholders (51%) voted against the remuneration report at the company.

Forum supports US resolutions on carbon reporting

In a major development of international shareholder activism LAPFF agreed to support shareholder proposals at 10 US company AGMs designed to improve company reporting on carbon emissions.

The move came in the wake of an 18 month engagement campaign in the UK focused on persuading FTSE100 companies to step up reporting on greenhouse gas emissions (see below).

The Forum's March meeting agreed to recommend support for the various resolutions being proposed by the US CERES coalition relating to reporting on greenhouse gas emissions.CERES is a coalition of US institutional investors and environmental and advocacy groups, supported by investors with $300 billion in investments.

According to CERES, the votes at the various companies were generally the highest ever on these issues, with the results at the oil majors ChevronTexaco and ExxonMobil, and at power utilities TXU, GE and AEP being particularly noteworthy.

Companies with resolutions endorsed by LAPFF and respective voting levels were:

Citigroup	5.2%
Weyerhauser	7.7%
PG&E	9%
AEP	26.9%
GE	22.6%
TXU	24.2%
ChevronTexaco	32%
ExxonMobil	22%
SouthernCo	pending
GM	pending

Councillor Bob Sowman, LAPFF chairman and chairman of the West Yorkshire Pension Fund, said "We support the CERES coalition's role in moving the agenda of shareholder concern forward on global carbon emission reporting. Supporting the concerns of US institutional shareholders and others, through the CERES initiative is a natural next step. Reporting on greenhouse gas emissions reassures shareholders that companies are taking this important issue seriously."

Companies improve carbon reporting

The Local Authority Pension Fund Forum has found a significant improvement in company reporting on carbon emissions following a year-long engagement campaign. 54% of FTSE100 companies contacted by LAPFF had improved their reporting on greenhouse issues in line with government guidance, or have committed to doing so.

Among companies that have improved their reporting regimes are: BHP Billiton, BSkyB, Boots, Diageo, Dixons, EMI, GlaxoSmithkline, Granada, HSBC, ICI, Lloyds TSB, Marks & Spencer, Prudential and Safeway.

However, while the majority show some improvement, there is still some way to go before all companies disclose their carbon emissions fully in line with the guidelines. The Forum has found 38 FTSE100 companies where reporting progress can be improved. Of these, 14 use some government guidance but have no commitment to extend usage, 21 have improved general environmental reporting but do not use government guidelines on greenhouse gas emissions and three acknowledge climate change as an issue but do not report.

The Forum is continuing to raise this issue with companies and is participating with other institutional investor bodies in joint initiatives.

Dixons comes clean on overseas labour code

After three years of company meetings, correspondence and AGM attendance by the Forum, electrical retailer Dixons has finally published its policy relating to labour standards among its overseas suppliers.

The company has also indicated that it will start reporting on how the policy is being implemented and that it will be rolled out to cover other branded goods suppliers as well as its own-brand suppliers.

This move represents a major step forward as Dixons had been identified by the Forum as one of only two FTSE100 retailers without a published labour standards policy. While it claimed to have standards on issues such as child labour and health and safety to which suppliers had to comply, it had declined to disclose them previously.

Engagement and lobbying by the Forum (including the prospect of a shareholder resolution) and by other investment managers appears to have persuaded the company of the benefits of transparency.

The Forum is now working on a detailed study of how policies and codes of conduct are being implemented by major retailers.

Higgs and Smith Reports: LAPFF submissions

LAPFF has made full responses to the reports by Derek Higgs on non-executive directors and by the Smith Committee on the role of audit committees. The reports, published in January, propose major revisions to the Combined Code of Corporate Governance Best Practice.

The Higgs report in particular attracted considerable controversy from some company chairmen who claimed it would restrict their roles.

In its submission to the Financial Reporting Council (FRC), the body charged with implementing the reports, LAPFF strongly supported the role of senior independent director arguing that “We do not regard the post as divisive as there are a variety of roles already recognised within a unitary board. It is important that there are clear lines of communication between share-holders and directors and identifying a post with special responsibility for this is useful”.

The Forum also supported “the stronger emphasis...on independence issues and also the definition of independence”. The Higgs proposals on board appraisal, performance evaluation, induction, training and a more transparent nomination process were also welcomed.

New Forum executive and officer

Following an internal review last year, the Forum has established an Executive Committee to manage its strategy and operations. The Chairman remains Cllr Bob Sowman from the West Yorkshire Fund, with Cllr John Saunders from LB Newham as Deputy Chairman. Brian Bailey from West Midlands Pension Fund is the new Honorary Treasurer, with Stuart Imeson from West Yorkshire as the new Honorary Secretary. Other elected executive members are: Cllr Don Yates (Lancashire), Cllr Dan Wicksteed (Worcestershire) and Cllr Maureen Child (Edinbugh).

LAPFF has also appointed a new part-time officer, Keith Bray, former County Treasurer and well-known among many LA funds. Keith’s role will be to promote the work of the Forum more widely. PIRC will remain as the contracted provider of research and shareholder engagement services.

Date for your diary

Shareholder Activism:
Results and Prospects

8th Annual LAPFF Conference 10, 11, 12 December 2003,
Bournemouth Marriott Highcliff Hotel

Full programme and speakers to be announced
More details from Janice Hayward at PIRC 020 7247 2323 and www.lapfforum.org

LAPFF mission statement:

"LAPFF exists to promote the investment interests of local authority pension funds, and to maximise their influence as shareholders to promote corporate social responsibility and high standards of corporate governance amongst the companies in which they invest, commensurate with statutory regulations."

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