Local Authority Pension Fund Forum

LAPFF Newsletter

September 2002

Companies quizzed on carbon reporting

Climate change has become one of the central SRI concerns for instititutional investors following the USA's failure to ratify the Kyoto Protocol and increasingly extreme weather events in recent years. The Forum has been active on the question of company reporting.

Late last year LAPFF researched how well FTSE100 companies were following greenhouse gas reporting guidelines issued by the Department for the Environment, Food and Rural Affairs (DEFRA). The DEFRA guidelines contain eight minimum requirements for reporting including a description of the most important greenhouse gas emissions produced by the company and quantification of the most important greenhouse gas emissions produced in terms of absolute kilograms of carbon dioxide.

Results showed a low level of take-up. Only five companies reported according to the eight minimum requirements of the guidelines and 55 companies provided no disclosure at all which would satisfy any of the essential DEFRA reporting criteria. However, 40 companies did attempt to quantify their emissions of greenhouse gases.

Engagement with companies

Using these findings, in conjunction with the Environment Agency Pension Fund, LAPFF has been seeking explanations from companies and a commitment to provide fuller information in future.

After correspondence, so far 30 companies (35% of those contacted) have subsequently published a new report in line with DEFRA guidance or have committed themselves to using it in future. 16 companies state they intend to improve their environmental reporting but have not given an explicit commitment to using the DEFRA guidelines. A further 8 companies use alternative reporting guidance that the Forum regards as acceptable.

Only 7 companies have not yet committed themselves to further reporting on the issue including household names such as the Daily Mail & General Trust and Dixons. The Forum intends to continue to lobby on this vital issue.

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Progress seen on director notice periods

Lengthy directors’ contracts have come under fire from the Local Authority Pension Fund Forum as part of its shareholder action programme on corporate governance issues. Following a decision at the 2001 Forum annual meeting, LAPFF has been pushing companies to reduce notice periods to one year or less.

Lengthy notice periods have been one of the main reasons behind some substantial compensation payments made to departing directors, often after periods of underperformance or corporate disasters such as at Marconi.

At the beginning of the year LAPFF identified 123 companies from among the FTSE350 where there remained one or more directors with a rolling contract of longer than one year. Forum chairman, Councillor Bob Sowman, wrote to these companies pointing out that the Combined Code backed contracts of no longer than one year and seeking assurances “that all executive directors rolling contracts will be reduced to one year or less in the near future”. The letter also informed these companies that their response would be taken into consideration in determining the voting positions of LAPFF members.

Company responses

The results have been encouraging. A third of companies have reduced all their director contract periods since last year. This has been achieved through a combination of negotiated reductions with the directors concerned along with retirements and resignations of those directors who had longer notice periods. In total 84% of the companies contacted now have an ongoing policy for new appointments of no longer than one year notice periods. It can be expected therefore that the trend towards shorter rolling notice periods will continue due to natural wastage and as new appointments are made.

Although lengthy rolling notice periods may soon be a thing of the past, the broader issue of directors’ pay continues to create shareholder furore. New government regulations approved in July, however, will require all listed companies to seek shareholder approval for directors’ pay at each AGM, thereby giving shareholders an annual opportunity to vote on the issue for the first time, a move the Forum has championed vigorously.

LAPFF pushes for diversity among non-executives in Higgs enquiry response

US and UK corporate governance scandals over the past year have provoked a flurry of concern among regulators. Accountants and non-executives have both been in the firing line. In the UK, one of the government's first responses was to set up an enquiry into the role of non-executive directors under ex-UBS Warburg chief Dereck Higgs.

In its response to the enquiry, LAPFF expressed concerns about non-executives’ “independence, their background, their numbers, their calibre and the support they can draw upon”.

The Forum wants to see non-executives in the majority on boards and a more rigorous approach to defining independence, with full biographies available and new directors having to justify their contribution to the board when they are elected. LAPFF is especially concerned to see a *widening in the pool from which non-executives are drawn, with consideration given to candidates from other walks of life, not just with a business background. The current approach “both offends principles of equality of opportunity and also limits the experience and knowledge on which boards can draw” states the submission.*

Better appraisal and training for directors are also highlighted. The submission is available at www.lapfforum.org.

Selfridges challenged on option scheme

LAPFF members contributed to a 25% vote against a new executive share option scheme at Selfridges in May, after the Forum identified the scheme as having particularly weak performance targets. Under the proposed scheme, awards of up to 200% of salary could normally be made each year, with exceptional awards of beyond 300% of salary. All the options were to be exercisable for real earnings per share (EPS) growth of 3% a year over three years, rather than subject to a sliding scale of performance, as has become the norm for most new option schemes.

Councillor Bob Sowman, LAPFF chair and chair of the £5 billion West Yorkshire Pension Fund, said "As long term investors, pension funds want to see companies setting performance targets which only reward executives for superior performance. Not only is it hard to see the chosen target as tough, but it pays out on an all or nothing basis. Best practice is for schemes to phase payouts according to a performance scale".

Ahead of the meeting, the company stated that maximum award limits would go no higher than 300% of salary, but left the performance conditions unchanged. LAPFF attended the AGM and sought assurances that the targets would be reviewed.

The Forum has recently had a further meeting with Selfridges company chairman, Alun Cathcart. He has committed the company to reviewing its directors’ remuneration structure in the light of the obvious shareholder concern expressed at the meeting. The Forum has welcomed this response.

Labour standards: policy implementation is next challenge

LAPFF has shifted the emphasis of its long-standing labour standards campaign from the adoption of policies to looking at how effectively company policies are being implemented. The Forum started its activity on the issue three years ago by lobbying the listed retail sector over whether they had a policy covering overseas 'sweatshop' labour issues such as child workers, minimum wage, freedom of association and forced labour.

However, following the widespread adoption of such policies, the Forum has been looking at the issues surrounding implementation and has had detailed discussion with a number of major retail chains such as Sainsburys, Marks and Spencer and Safeway.

A seminar for Forum members with Sainsbury's was held in March to explore some of the practical difficulties involved.

Sainsbury has around 1500 suppliers, who, in turn, may have sub-contractors. Seasonal products may involve more suppliers still. Clearly it is physically impossible to audit compliance with the company's policy all through the supply chain, so their main efforts are on 'level 3' suppliers - international agents and pack-houses. Sainsbury is also using supplier self-assessments whereby suppliers are required to complete a questionnaire based on the company's code of conduct. Forum members had some criticisms over some of Sainsbury's policies and the scope of its activities, but they recognised that it is a complex process that cannot be undertaken quickly. Discussions continue with other retailers.

Dixons AGM

While most companies have disclosed their policies, a handful continue to play things close to their chest. Electrical retailer Dixons has assured the Forum that it has a policy and is rolling it out to suppliers, but has declined to publish the policy or to set targets for implementation. A further problem is that the policy covers only own-brand suppliers which account for only 20% of Dixons' sales.

Forum representatives attended the company's AGM on September 11 to seek commitments on whether the company would agree to extend its policy to cover branded goods and start reporting within a year.

The response at the AGM from outgoing chairman Sir Stanley Kalms was not encouraging, but the Forum remains hopeful that progress can be made before next year’s AGM without the need for further action.

Responsible Ownership: pension fund strategies for engagement

7th Annual LAPFF Conference 4, 5, 6 December 2002, Bournemouth

Speakers include: Paul Myners (author: Institutional Investment in the UK), Sir John Banham (chairman Whitbread plc), Bob Monks (founder ISS, Lens Inc), Terry Crossley (LGPU), Karina Litvack (Friends Ivory & Sime), Ed Mayo (New Economic Foundation), Paul Burke (Co-Operative Insurance Society), Colin Bridgnorth (Laxey Partners), Brian Myerson (Active Value Advisors), Deborah Allen (BAE Systems plc).

Plenary sessions on: The UK defence industry; corporate governance or corporate social responsibility?; the value of brokers’ research; shareholder activism, global public sector pension funds.

Workshops on: corporate corruption, shareholder engagement, democracy and the LGPS.

More details from Janice Hayward at the LAPFF Secretariat 020 7247 2323 and www.lapfforum.org

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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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