10 Minutes on…

2017 Annual General Meeting season - a fuss about nothing?

pwc

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Despite many media headlines predicting shareholder backlash against executive pay during the 2017 AGM season, as the season draws to a close, it appears that this may have been much ado about nothing. Voting outcomes do not demonstrate the shareholder backlash that we were expecting, with only 3 strikes in the ASX200 (and only one of those being in the ASX100).

In fact, over 80% of companies in the ASX200 received votes in favour of their remuneration reports in excess of 90%. The average vote 'Against' has dropped from 8.4% last year to 6.1% this year.

The positive change in voting outcomes may suggest that shareholder dissatisfaction over the last few years (particularly with the uptick in 'no' votes seen in the 2016 AGM season) has pressured companies into action and that resulting changes (either to frameworks, reward outcomes, or communications and disclosures) have been well-received.

In our October edition, we predicted that four key themes would play out this season:

1. ***Accountability*** reinforced through pay outcomes
2. Reasonableness of ***quantum***
3. Remuneration models that are ***customised*** to the company and disclosures that are ***simple***
4. ***Alignment*** with shareholders

These four principles have indeed been prominent in associated media commentary throughout the AGM season, and have been emphasised in explanations of 'Against' or caveated 'For' voting recommendations in many a proxy advisor report.

	2017**	2016
ASX100*		
% receiving a strike	1.3% (1 out of 74)	8.5% (7 out of 82)
Average % vote 'Against' Rem report	6.9%	8.4%
ASX200*		
% receiving a strike	2.0% (3 out of 148)	8.5% (14 out of 160)
Average % vote 'Against' Rem report	6.1%	8.4%

** results of AGMs held in the calendar year. ASX positions based on 3-month average market cap as at 30 September*
*** analysis based on companies who have had AGMs as at 8 December 2017.*

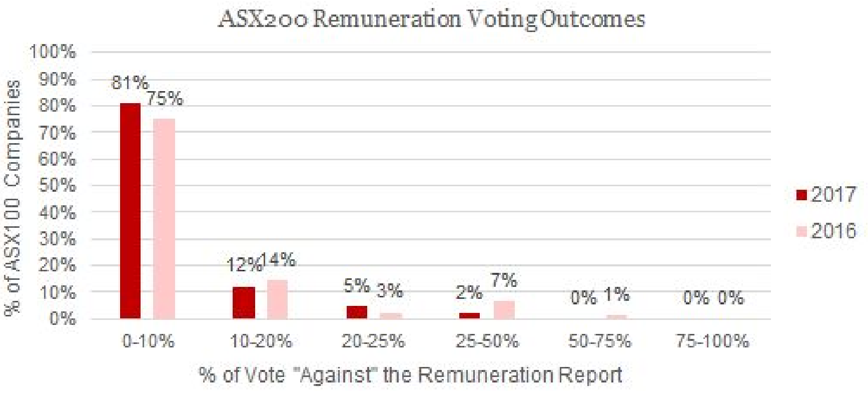
It is too early to tell whether the changes made to date are enough to restore public trust in executive pay. And whether such changes can start to address societal discontent around growing income inequality is another matter entirely. Regardless, the debate around fairness and the ethics of pay is likely to continue, with related regulations to be introduced in the UK and US next year, and so there is certainly more to be done. Companies should therefore look to build on the positive momentum and the lessons learnt from this AGM season as planning commences for 2018.

Summary of 2017 AGM season outcomes

Headlines were dominated by big dollar remuneration packages and predictions of shareholder backlash but this wasn't reflected in voting outcomes.

For those companies who received a strike last year, the most common changes were:

- more detailed disclosures of performance measures and targets;
- reduced STI maximum opportunities;
- changes to STI deferral practices such as the use of equity instruments rather than cast, introduction of malus / clawback;
- simplification (to an extent) of performance measures and rebalancing of weightings toward financial measures;
- moving from fair value to face value LTI allocation; and
- introduction of minimum shareholding requirements.



In 2017, where companies received a high 'against' vote, the main themes continue to be in line with concerns noted in previous years:

- Perceived **excessive quantum** in either fixed or variable pay, particularly when misaligned with shareholder outcomes;
- **Misalignment of performance measures,** particularly to long-term shareholder returns;
- **Poor disclosure** of performance metrics and/or targets; and
- Concerns around target setting and whether they are **appropriately stretching**, given resulting outcomes**.**

So has the 'heat' gone out of the pay debate?

We don't believe concern regarding executive pay has substantially dissipated. The 2017 AGM voting season indicates there are still key aspects of remuneration policy and practice that Remuneration Committees will need to stay on top of. So what has reduced the 'heat' this season?

1. Specific shareholder concerns tabled in 2016 have been addressed

All companies receiving a strike in the prior year have reviewed and introduced changes (to varying degrees) to their remuneration policy and/or disclosures to address shareholder concerns, resulting in positive voting outcomes.

2. The rationale for pay structures has been considered as much as the design itself

Companies are receiving support to implement bespoke arrangements, largely because in general, the rationale for change is strong, well-articulated and communicated.The 2017 AGM season provided evidence that shareholders can be open minded to change.

3. Demonstrated link between pay and performance with quantum remaining constrained

In general, there was a level of restraint demonstrated in the market this year, with fixed pay increases absent or moderate. There are still some concerns over total pay quantum in some cases, however it seems that companies' efforts in clarifying the pay and performance link is being recognised, as evidenced by the fact that even large variable payments have been supported when accompanied by strong performance.

4. Better sharemarket performance took (some?) focus off pay

A theory shared by some in the market is that shareholders tend to vote against remuneration reports as a protest in relation to disappointing returns.

The ASX200 delivered strong growth during 2017 - c.14% YTD as at 30 November 2017, however returns were also positive in 2016 (c.10% measured over the same period), a year in which we saw a significant uptick in strikes. So whilst strong financial returns is important to shareholders, it takes more than that to gain shareholders' votes on pay.

5. Proxy advisors 'on notice'

There is increasing pressure on proxy advisors globally, in the wake of recent criticisms, on the way they engage with listed companies and the quality of the inputs/analysis that support their voting recommendations.

As a result, we suspect that proxy advisors may have felt they were 'on notice' to some degree and consequently adopted a cautious approach to 'no' vote recommendations this season.

In aggregate, the statistics from this AGM season do not really justify the fuss it created. However, it is important to continue to recognise that there is widespread concern amongst the public and politicians about pay levels and practices as a whole.

So companies should continue to ask themselves the tough questions:

- *Are we adequately **making the case** for the pay executives are receiving?*
- *Are the **targets** set really **stretching** enough?*
- *What other **factors beyond financial** do we consider in determining pay outcome?*
- *Are pay designs really encouraging **long-term sustainable performance**?*
- *Are we clear enough on our **approach to fairness of pay** more broadly across our organisation?*
- *Are we **engaging early** with external **stakeholders** and **genuinely considering proxy advisor policies** and feedback as part of the consultation process?*

How can PwC help?

To have a deeper discussion about these issues, please contact:

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