

ALL PARTY PARLIAMENTARY CORPORATE GOVERNANCE GROUP
2015 ANNUAL DINNER – LONDON - WEDNESDAY, JULY 1, 2015

SPEECH BY GUY JUBB, HEAD OF GOVERNANCE & STEWARDSHIP,
STANDARD LIFE INVESTMENTS LTD

My Lords, Ladies and Gentlemen.

As a Scotsman in the Palace of Westminster it is of course not only a great pleasure to find myself sandwiched, so to speak, between parliamentarians of good repute but also a great temptation to give myself a round of applause before I have even started. But as a purveyor of good governance and stewardship, this Scotsman shall do his best to resist the temptation.

In preparing for tonight's very special annual dinner it occurred to me that there is a rather special bond of kinship between elected members of parliament and many of the fund managers who have signed up for stewardship. We all seek to represent the best interests of our constituents and clients respectively, transparent voting is a key performance indicator, and from time to time we get on our hind feet and speak what is on our minds – in your case, in the House, in my case in the body of the kirk that is known as the AGM. And sometimes people notice and sometimes they do not.

AGMs are an important part of a good steward's armoury but it is surprising – and disappointing - how few institutional investors pitch up to them. This year, I have spoken at two AGMs. One, as you may be aware, was WPP's, where I reflected our views on the governance risks – including executive pay - associated with Sorrellcentricity and succession planning – or rather the perceived lack of it. The other, of which you are probably unaware, was Royal Dutch Shell's in The Hague, where I quizzed the Board about a number of audit matters. If I had dressed as a polar bear or an arctic fox I might have had more media impact. But I didn't. That said, I am very confident our intervention had – and continues to have – impact with Shell's Board.

My purpose of mentioning these AGMs is to make very clear to you that there is more to corporate governance than just pay and rations in the boardroom. But executive pay is very important to us and our clients. The new binding vote, introduced at the behest of Parliament, has now been through its second AGM season, and the shareholder rights provided by the legislation and regulation have provided a framework of accountability that has been put to good use by investors – publicly and privately. Investors' resolve to stick to the approved pay policy at BG Group earlier this year, when it was seeking to recruit its new Chief Executive on terms that were outwith the approved policy, is a worthy testament to shareholders reining in remuneration and bringing boards to heel.

Despite these improved shareholder rights, I believe it is now generally accepted that there are still widespread problems with executive pay – quantum and inequality are manifest symptoms. It is worth remembering that the UK Corporate Governance Code states that that remuneration committees should have regard to pay and employment conditions elsewhere in the company when fulfilling their responsibilities but, in my experience, very few provide a convincing explanation of how they have done so. Remuneration committees need to do more to anchor movements in senior executives' pay – and not just the CEOs salary - to movements in pay throughout the company, so that they move in tandem – and are seen to move in tandem - during both the good years and the bad ones.

In this regard, I believe that the public and shareholder interests are aligned. Although the quantum may be the outcome, it is my belief that the complexity of remuneration policies lies at the root of much of the problem. There are generally too many components and too many performance conditions making it a challenge for even the seasoned governance

professional to see the wood from the trees. This is something the FRC could address – perhaps through a Governance & Stewardship Lab, building on its very successful Financial Reporting Lab, where innovative ideas to simplify executive pay arrangements can be discussed and incubated – and practical ways to move forward can be promoted as best practice.

So what else needs to be done? The first of two challenges to parliamentarians this evening is to promote the restoration of all-employee profit sharing schemes – or put another way John Lewis schemes. These were prevalent in the 1970s and 1980s, before LTIPs had been invented. They provided an alignment of interest from the top to the bottom of the organisation, they provided an alignment of pay and performance, and they were relatively simple and inclusive. Importantly in the context of this challenge, there were fiscal incentives, which made them popular for companies and employees alike. Parliamentarians, individually and collectively, have a role to play in getting this show on the road. Without fiscal incentives, I fear we are stuck in a remuneration rut.

As I said, there is much more to corporate governance than executive pay, so let me turn to the importance of high quality audits. When investing in a company and holding its board to account, investors need to be confident that the company's accounts show a true and fair view – and it is the role of the external auditor to attest to that.

So far, so good. It is generally understood that from time to time there will be audit failures – even chartered accountants aren't perfect – but it is not generally well understood that it is impossible for shareholders to sue auditors when there has been an alleged audit failure. Believe me, we have sought to do so several times but in every instance, learned counsel has drawn our attention to the Caparo judgement.

This is neither the time nor the place to debate the finer points of auditor liability but suffice it to say that the Caparo judgement by the House of Lords in 1990 determined that auditors do not owe a duty of care to existing or future shareholders. This has prevented our clients from taking negligent auditors to court. This situation is manifestly unfair and unsatisfactory. And surprisingly – perhaps – it is not very well known.

Therefore, my second challenge to parliamentarians this evening is to change the law to address the curse of Caparo. It is unrealistic to expect the judgement to be challenged by shareholders in the Supreme Court and a change in the law is needed. Justice demands no more and no less than the restoration of a level playing field between shareholders and auditors. I urge the parliamentarians here present to rise to this challenge – I believe you all have a duty to do so. Mike Everett and I would be more than happy to explain more fully our concerns about curse of Caparo over a glass of Compari.

So let me draw to a close. As a senior and seasoned member of the leadership team at Standard Life Investments I have a responsibility to champion the best interests of our clients. As a Scottish CA, I have an over-arching responsibility to uphold the public interest. These responsibilities are not mutually exclusive and serve to reinforce the importance of striving to do the right thing. And it is with this in mind that I have given some of you some homework this evening – to address Caparo and the incentives that may be needed to exorcise some of the demons of executive pay. In doing so, I hope you will get on and do it, get a good mark – and maybe even a gold star!

Ends

For further information please contact:

Yvonne Soulsby, Press Manager, Standard Life Investments, +44 (0) 131 245 3610.

Notes

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