

FTfm

# Key to pay restraint lies with boards



**Pauline Skypala**  
COMMENT

How much is too much when it comes to executive pay, and who should decide? There is much debate, particularly when it comes to banks, on what the top people are worth. Remuneration consultants have helped drive pay packages ever higher and remuneration committees are not generally noted for their restraint. Boards get their ideas about what is an appropriate level of pay from each other, according to governance experts.

Shareholders have revolted from time to time, but rarely go beyond voting against remuneration committee reports. They should be prepared to vote against the re-election of people to the remuneration committee, according to Co-operative Asset Management.

Token protests by a few shareholders will not achieve much, though. Investors need to act collectively, which is increasingly what they are doing. For example, the National Association of Pension Funds last week wrote to the chairmen of the FTSE 350 companies on the subject of remuneration policies. It talks of a "continued need for restraint and better alignment

with the long-term issues of shareholders", and says a review of accepted best practice is needed.

David Paterson, head of corporate governance at the NAPF, says shareholders must remain vigilant and make sure "boards are held to account for their pay policies".

Perhaps stung by a perception that pension funds have been among the "absentee landlords" excoriated by Treasury minister Lord Myners, the NAPF plans to use its collective voice more often, and be seen to do so.

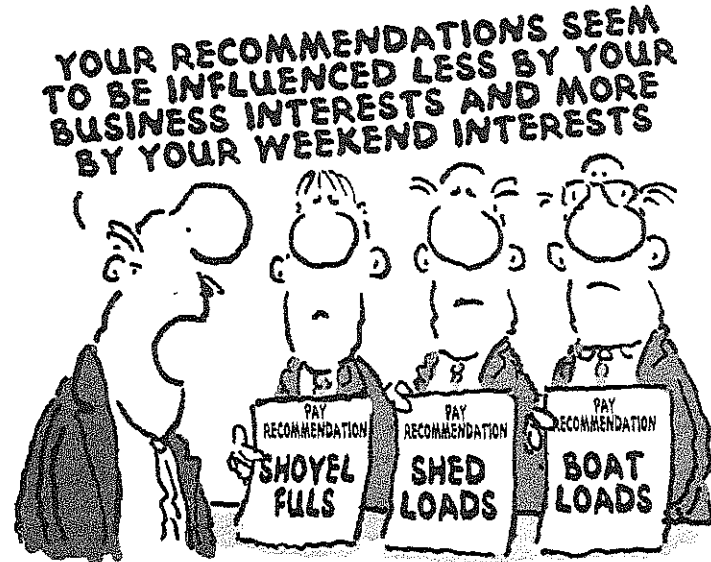
Investors generally do not want to dictate how and what executives should be paid. But they do want boards to ensure interests are aligned, and that profits are not going disproportionately to pay. Their main interest lies in making sure companies have effective boards in place. Unfortunately, this is no simple matter.

I asked Bill Crist what shareholders can do to make sure the right people are on the board. As chairman of Governance for Owners and former chairman of Calpers, the Californian pension scheme known for its shareholder activism, he is as likely to have the answer as anyone.

But he doesn't. "You've asked the question that if I had the answer to I would be famous."

Finding people with high integrity and independence of thought who are willing to sit on boards of directors is "a biggie", he said.

Stilpon Nestor of Nestor Advisors, a consultant on corporate governance, says the



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particular problem with boards of financial services companies was that they focused too much on the independence of board directors rather than their competence. The banks that performed the best had chairmen who were former chief executives or had banking experience.

He wants to see shareholder committees set up to hold bank boards to account on corporate

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governance issues. The problem with banks was not that interests were not aligned, according to Mr Nestor, as most top people at banks had big packages at risk, but that "the board and shareholders completely misunderstood the risks". The focus should be on "making the board wiser, not the shareholders".

Boardroom behaviours is the subject of a report by the Institute of Chartered Secretaries and Administrators, prepared to feed into Sir David Walker's report. It concludes that the lack of guidance on appropriate behaviours is a structural weakness that contributed to the severity of the credit crisis, and describes as "remarkable" the lack of any significant guidance in the

combined code that governs best practice for UK companies on the drivers of boardroom behaviours. The report identifies best practice boardroom behaviour as including: the appropriate deployment of knowledge, skills, experience and judgment; independent thinking; and the questioning of assumptions and established orthodoxy.

Seamus Gillen, senior adviser at ICSA, says: "The view was that the [comply and explain] model is not broken, the key is how it is implemented," which comes down to behaviour.

ICSA is working to change some behaviour through its Transparency in Governance Awards – winners to be announced this week. The awards, co-sponsored by Hermes Equity Ownership Services, focus on disclosure via annual reports.

"We are looking to encourage better disclosure so investors can be reassured there is a good board in place," says Mr Gillen.

The winners of the awards could include companies that have courted controversy, such as BAE Systems, which is shortlisted for several awards. Mr Gillen says such companies have a greater need to explain themselves.

The judging process found standards varied and FTSE 100 companies were not necessarily better than FTSE 250 companies.

Shareholders should take note of the winners and demand higher standards of the rest.

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