GOVERNANCE

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Women's role in solving the productivity puzzle

'Directors must consider which business metrics are most appropriate for identifying high performers and consider whether or not the ability to adhere to a traditional working pattern is the most important criteria at a time when productivity and the ability to innovate and generate results are becoming increasingly important.'

Alison Gill

Shareholder 'activism'

'Yet, when we look beyond these snappy headlines, we find not only has the concept of shareholder activism been hi-jacked by a small cadre of extremely wealthy private equity investors with large shareholdings to leverage but, more worryingly, the idea of increased board accountability is often just a polite synonym to describe rampant often wild short-termism in investment decision making.'

Gerry Brown

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News

Corporate ethics in a digital age

'While directors have to take account of AI and understand the role it is playing in their business, they do not need to be experts in technology to tackle relevant questions. Indeed, most of the challenges facing directors are more ethical and philosophical than technical', according to a recent Board Briefing published by the Institute of Business Ethics (IBE).

Corporate ethics in a digital age offers practical advice about how the ethical challenges of artificial intelligence (AI) can be addressed, looks at the expertise required in the boardroom and highlights nine challenges around the use of AI, suggesting questions for those in the boardroom to help address these challenges.

Making sure the board is in charge – Boards must remain in charge and not allow technology teams to take over simply because the directors do not fully understand the technologies used. They also need to understand how decisions involving AI are taken and the role of executive oversight. The use of technology presents opportunities as well as risks and boards should factor it into their strategic planning, both short- and long-term.

Sharing the benefits – Companies should share the benefits of new technology with all stakeholders – customers as well as employees. They need to ensure that the right skills are being developed and to think how existing skills can be adapted. Companies cannot however be expected to give away their competitive edge and innovative use of technology forms part of that.

'Boards need to ensure that it is always possible to override an AI decision when it is clearly wrong. It can be helpful to have a governance framework in place for AI, including checks and controls.'

Ensuring accountability – There must always be human accountability and in the corporate world this accountability rests with the board. Risk appetite is as important as risk management, including the amount of risk a board will take on and the steps taken to mitigate the risks. Boards need to ensure that it is always possible to override an AI decision when it is clearly wrong. It can be helpful to have a governance framework in place for AI, including checks and controls.

Avoiding bias – Inherent bias is an important issue for AI and can creep in, for example, through the nature of the data or data collection methods. The risk is that unconscious bias will become embedded in processes and that bias will become self-reinforcing. Companies that use AI have a responsibility to ensure that they are aware of the risk of bias and take steps to mitigate it.

Treating customers fairly – AI can enhance customer experience and outcomes. However, there is a risk that companies use AI to extract value from customers rather than delivering value to customers. Companies must remember, reinforced by GDPR, that individuals have rights over data processed about them and that the organisations processing the data have obligations.

Treating employees and contractors fairly – Boards need to be aware of the sensitivities of the workforce around introducing AI. Senior corporate leaders need to maintain dialogue with governments and other authorities to help promote a framework for dealing with the broader social consequences of AI. Companies also need to be careful about using AI as a tool of employee surveillance or being used to induce employees or contractors to adopt working practices they would otherwise reject.

Keeping data secure – Although cyber security breaches have become commonplace most organisations are not well prepared to defend themselves. Boards need to know: what data is held; policies in place regarding encryption; plans in place in case of a cyber attack and whether crisis management processes or business continuity plans have been tested; the safeguards in place; if senior management receive regular data security reports and regular reports on any lapses; and whether all staff receive data security training.

Codes of ethics are an important means of encouraging appropriate use of technology and can provide a secure framework for companies to make the most of opportunities. While overarching principles are good, codes need to be sufficiently granular to be of practical help to employees and need to be backed up by effective speak-up and whistle-blowing arrangements.

Boardroom expertise – Boards are accountable for what happens as a result of the application of technology to the business, however business experience, common sense and sound advice are more important for directors than technology expertise. That said, the appointment of a Chief Information Officer/Chief Technology Officer is very important. Responsibility for oversight and management of AI should also be embedded in executive remuneration schemes.

For the more information go to: https://bit.ly/2p8LqcN

This article is based on a Report written for the IBE by Peter Montagnon. Sadly, shortly after the Report was published, Peter died unexpectedly. Peter was a giant in the corporate governance world. He was enormously well-respected and will be sorely missed.

News

FTSE 100 corporate reporting trends 2019

'Now more than ever businesses need the trust of their stakeholders and society at large to prosper over the long term. However, only 6% of FTSE 100 companies provide specific examples of how stakeholders were considered in major decisions', according to a recent report by Black Sun.

The Report, *The Ecosystem of Authenticity*, analyses FTSE 100 corporate reporting trends and best practice and assesses how companies are responding to challenges they face in implementing the suite of legislative initiatives that take effect for companies with financial years beginning in or after January 2019 and changes within the reporting landscape. Analysis has found that there have been broad improvements in most areas, with more dramatic improvements around topics that are driven by the upcoming regulatory changes.

Six principles of trust

There is continued debate around the need to restore corporate trust and the Report breaks the theme of 'trust' into six key principles – Purpose, Culture, Stakeholders, Wider Value Creation, Diversity and Long-term Thinking – to encourage companies to embrace these principles in their thinking and communications, as well as covering the core building blocks of reporting.

Purpose

Company purpose focuses on what is most important, however only 47% describe what purpose means in practice, including providing tangible examples of how capabilities or even products support companies in fulfilling their purpose, with most struggling to evidence how strategic outcomes flow from purpose. The vast majority of the FTSE 100 is prepared for the upcoming reporting requirements with 72% now setting out their purpose, going beyond creating profit and shareholder value by also focusing on the value created for other stakeholders or society at large. This focus on purpose also extends to leadership statements where around a quarter of Chairs and CEOs discuss their purpose and just under a quarter of all FTSE 100 companies specifically provide a link between strategy and purpose, typically discussed in the setup to the strategy section.

Culture

Seventy-five per cent of companies set out their values and 6% provide a KPI relating to culture. However, reporting on culture has continued to plateau and the focus seems to be shifting slightly with companies increasingly discussing how culture contributes to value creation instead of just outlining how they prevent value being destroyed. Fifty-seven per cent of FTSE 100 companies talk about culture or values in the Chair's statement in the governance report, however, only 11% discuss progress in embedding a desired culture.

Stakeholders

Stakeholders have remained a major topic this year with almost all companies having some level of discussion on stakeholder engagement. Sixty-seven per cent of companies clearly identify their shareholder groups but only 6% provide specific examples of how the board has regard for stakeholders. There are also reassuring signs suggesting that stakeholder considerations are increasingly seen as crucial to operational and financial success. Ninety-eight per cent of companies do have some level of discussion on stakeholder engagement, with 21% outlining expectations for some of their key stakeholders, and 20% discuss stakeholders in relation to strategy.

Diversity

Narratives around diversity continue to improve: 41% of companies provide a detailed discussion of their diversity policy and 25% discuss their strategy for addressing the gender pay gap. Diversity policies are becoming more detailed and are increasingly encompassing the wider workforce. However, linkages between diversity within the wider workforce and strategy are rare, even when the business case is strong.

Value creation

Companies increasingly discuss the value they create for wider society: 68% provide a commitment to wider value creation and 14% provide information on relationships in their investment case. Sixty-seven per cent of companies include value creation outcomes in their business model and 40% discuss key revenue or profit drivers. There are a number of other typical content elements which together make up the value creation story in the annual report, including: strategy – 33% of companies include a link between strategy and culture or values; risk – 45% of companies make specific reference to particular principal risks in their viability statement; and governance – 61% of companies discuss the new Corporate Governance Code in the Chair's introduction to corporate governance.

Long-term thinking

Long-term thinking is the only way to create trust and, by extension, profit over the long-term. Uncertainty is affecting many of the typical measures of long-term thinking. However, many reports still provide discussions around future investment in new and existing capabilities, 35% of companies setting out forward-looking priorities for capital allocation and 26% providing a timeframe for their strategy. Companies are increasingly applying a longer-term lens to disclosure, discussing risks and opportunities stemming from increased global focus on sustainable development.

For more information go to: https://bit.ly/2SeE6tq

News

Internal Audit Code of Practice

A draft Code to strengthen corporate governance and help reduce the risk of further major corporate collapses has been launched for consultation. Published by the Chartered Institute of Internal Auditors (CIIA), the Internal Audit Code of Practice aims to create an internal audit industry standard and boost the status, standards, scope and skills of internal audit.

The draft Code of Practice contains 30 recommendations and offers guidance about raising internal audit performance to help businesses and other organisations protect their assets, reputation and sustainability and can be regarded as a benchmark of good practice against which organisations can assess their internal audit function. Recommendations contained within the Code are principles-based. They are written in the context of a reasonably-sized organisation operating in the private sector within the UK and Ireland. Smaller organisations, and branches of non-UK headquartered organisations in particular, might need to make some modifications to the detail, but all should comply with the principles.

Role and mandate of internal audit

The primary role of internal audit should be to help the board and executive management to protect the assets, reputation and sustainability of the organisation. It does this by assessing whether all significant risks are identified, appropriately reported and adequately controlled; and by challenging executive management to improve the effectiveness of governance, risk management and internal controls. The board, its committees and executive management should set the 'tone at the top' to ensure support for, and acceptance of, internal audit at all levels of the organisation.

Scope and priorities of internal audit

Internal audit's scope should be unrestricted and should include information presented to the board and its committees. In setting its scope, it should take into account business strategy; should form an independent view of whether the key risks to the organisation have been identified and assess how effectively these risks are being managed; and its work should be regularly reviewed to take account of new and emerging risks. In setting out its priorities and deciding where to carry out more detailed work, internal audit should focus on areas where it considers risks to be higher. Changes to the audit plan should be considered in light of internal audit's ongoing assessment of risk and material changes to internal audit plans should be approved by the audit committee.

Reporting results

Internal audit should be present at, and issue reports to, the appropriate governing bodies, including the board audit committee and any other board committees as appropriate. The nature of the reports will depend on the remits of the respective governing bodies.

Interaction with risk management, compliance and finance

Internal audit should include within its scope an assessment of the adequacy and effectiveness of the control functions. Informed judgement needs to be made as to what extent it is appropriate to take account of relevant work undertaken. Work such as risk management, compliance or finance, in either its risk assessment or in the determination of the level of audit testing required for the activities under review.

Independence and authority of internal audit

The chief internal auditor should be senior enough within the organisation to give them the appropriate standing, access and authority to challenge the executive. Subsidiary, branch and divisional heads of internal audit should also be of a seniority comparable to the senior management whose activities they are responsible for auditing. Internal audit should have the right to attend and observe all or part of executive committee meetings and any other key management decision-making fora and should have sufficient and timely access to key management information and records.

Resources

The chief internal auditor should ensure that the audit team has the skills, experience and expertise commensurate with the scale of operations and risks of the organisation and should provide the audit committee with a regular assessment of skills required and whether the internal audit budget is sufficient to recruit and retain staff or procure other resources with the expertise, experience and objectivity.

Quality assurance and improvement programme

Internal audit should maintain an up-to-date set of policies and procedures and performance and effectiveness measures for the internal audit function and should continuously improve these in light of industry developments. A quality assurance and improvement programme should be developed, the scope of which should include internal audit's understanding and identification of risk and control issues. The quality assurance work should be risk-based to cover the higher risks of the organisation and of the audit process and the results of the assessments should be presented directly to the audit committee at least annually.

The consultation period closes on Friday 11 October. Written responses to the draft Code can be submitted by email to iiapolicy@iia.org.uk. Full instructions are included in the consultation document.

To see the Consultation document go to: https://bit.ly/2ZZq9CI

Global News

Shareholder Rights Directive II

Rule changes relating to the revised Shareholder Rights Directive (EU) 2017/828 [1] (SRD II) have come into force. SRD II is an EU directive which sets out to strengthen the position of shareholders and to ensure that decisions are made for the long-term stability of a company. The changes relate to: the identification of shareholders; transmission of information; facilitation of the exercise of shareholders' rights; transparency of costs; public disclosure of information by institutional investors, asset managers, life insurers and proxy advisors; and remuneration of directors and related-party transactions.

Certain aspects of SRD II are directly implemented in EU Member States, including provisions intended to facilitate the exercise of voting rights by investors. Key aspects of SRD II that are not being directly implemented, and therefore require implementation in each EU Member State, are those concerning asset managers' and institutional investors' shareholder engagement policies.

In the UK, the FCA is amending its rules to implement SRD II and key elements of the rule changes are as follows:

- For asset managers and life insurers regulated by the FCA, new requirements regarding the public disclosure of their shareholder engagement policies and periodic public disclosure of the implementation of such policies. The engagement policy must be disclosed on the firm's website. The requirement will apply on a 'comply or explain' basis and if a firm does not comply with one or more requirements, it must publicly disclose, with a clear and reasoned explanation, why it has chosen not to do so.
- For life insurers regulated by the FCA, new requirements regarding the public disclosure of their equity investment strategy and their arrangements with asset managers they appoint. The information must be made available free of charge on the life insurer's website and updated on an annual basis. The requirement will apply on a 'comply or explain' basis.
- For asset managers regulated by the FCA, new requirements regarding the disclosure to asset owners of the manager's shareholder engagement activities. The FCA does not prescribe how these disclosures should be provided but does indicate that where the information is available publicly, the asset manager is not also required to provide the information directly to institutional investors.
- For UK companies with shares admitted on a regulated market, requirements regarding the disclosure and approvals required for related-party transactions.

The proposals only apply if the UK leaves the EU with a transition period. In the event there is no transition period, SRD II may still be relevant and the FCA will revise proposals at a later date.

Member States were required to transpose the majority of SRD II's requirements into national law by 10 June 2019 and have until September 2020 to transpose into national law measures relating to the identification of shareholders, transmission of information and facilitation of the exercise of shareholders rights.

New ESG disclosure guidelines for Abu Dhabi

The Abu Dhabi Securities Exchange (ADX) has issued new guidelines for listed companies on environmental, social and governance (ESG) disclosure, as part of its strategy to promote sustainability in the financial markets.

Sustainability reports provide the company's ESG disclosure content in one place and address information needs related to investors and other stakeholders, such as consumers and civil society.

ADX-listed companies are required to submit an independent report on sustainability, in line with Global Reporting Initiative standards. The criteria on which these reports are based are divided into three sets of 31 guiding principles for ESG.

According to the voluntary guidelines, companies must disclose critical ESG core issues through four phases:

First phase – disclosure. Companies should disclose critical ESG issues and identify all issues related to sustainability that may have a potential impact on its activities, products, services and relationships internally or externally.

Second phase – prioritisation. Companies should choose the most important topics to report on in accordance with the principles of relative importance and stakeholder inclusion.

Third phase – validation. Companies should assess the material aspects against the scope of the reports, the limits of each impact and the reporting period.

Fourth phase – review. Companies should carry out a review following the publication of the company report to prepare for the next reporting cycle.

The ADX will be holding workshops for all listed companies to clarify these criteria and to explain how to report and respond to queries from companies. Companies listed on the Exchange are expected to release these reports by the end of 2019.

Global News

Female representation in Japanese companies

The percentage of working-age women with jobs has reached a record high of nearly 70% in Japan, according to a report by the Japanese Internal Affairs and Communications Ministry. 69.6% of women between 15 and 64 held jobs in 2018, up 8.9 percentage points from 2012, reflecting the adoption of a policy of cultivating the power of women to drive the growth of the Japanese economy. However, the rate of participation in the labour force drops for women mainly in their 30s as they marry and have children.

There is widespread recognition that companies with female executives often show strong earnings and stock price performances, while corporate governance, risk management and innovation are positively affected by the diversity of opinion that women bring to management. However, the number of women in executive and managerial positions remains extremely low. Japan ranked 110th among 149 countries surveyed by the World Economic Forum in 2018 for gender equality, largely because of the lack of opportunities for promotion to managerial positions: women account for only 4.1% of board members at listed companies, well behind the Japanese Government target of raising the share of women in executive posts to 10% by 2020.

The 30% Club, founded in the UK in 2010 with the aim of increasing female representation on company boards and at senior management level, launched the 30% Club Japan in May 2019 and a target has been set of achieving 10% representation of women on the boards of TOPIX100 companies by 2020 and 30% by 2030. Institutional investors are also calling for increasing the number of female executives at companies in which they have equity stakes.

Tough new whistle-blowing laws

Australian companies must review how they deal with eligible whistle-blowers following legislative changes. The Treasury Laws Amendment (Enhancing Whistle-blower Protections) Act came into force on 1 July 2019 and introduces severe civil and criminal penalties for employers who breach the protections provided to eligible whistle-blowers. Maximum civil penalties for breaching the confidentiality of an eligible whistle-blower's identity or causing or threatening detriment to an eligible whistle-blower include: up to $1.05m for individuals (5,000 penalty units); and up to $10.5m for companies (50,000 penalty units), or 10% of the annual turnover (up to $525m or 5,000,000 penalty units).

The legislation increases those who can be eligible whistle-blowers to cover individuals currently or previously connected with a company and those who can be 'eligible recipients' of whistle-blower disclosures to include senior managers, directors and auditors and, in certain circumstances, journalists and politicians.

Stronger protection for whistle-blowers includes anonymity, increased immunities against prosecution and protection against detriment through victimisation. Whistle-blowers are no longer required to act in good faith to be protected (although they need to have reasonable grounds to suspect misconduct).

Whistle-blowers will be protected from disclosing information about matters beyond criminal breaches and new laws also allow for reporting of conduct which indicates systemic issues even if not illegal. Protections do not extend to disclosures about personal employment or workplace grievances.

From 1 January 2020, certain companies will be required to have a whistle-blower policy that complies with new s1317AI of the Corporations Act 2001. The policy must contain: protections available to whistle-blowers; how and to whom an individual can make a disclosure; how the company will support and protect whistle-blowers; how investigations into a disclosure will proceed; how the company will ensure fair treatment of employees mentioned in whistle-blower disclosures; and how the policy will be made available.

Good policies will also include scope to conduct investigations internally and externally, address client legal privilege and outline processes where a person subject to a disclosure is also authorised to receive the disclosure and a process to determine whether an eligible whistle-blower consents to be identified during an investigation.

The requirement to have a whistle-blower policy carries a $12,600 penalty for non-compliance and applies to: public companies; large proprietary companies; and registerable superannuation entities.

Staff training should include 'eligible recipients' (senior managers, officers and anyone else authorised by the company to receive disclosures from whistle-blowers) and all staff and should outline how the new whistle-blower regime works, the process for disclosing and investigating certain matters and also the protections provided to eligible whistle-blowers.

The new regime requires a thorough analysis of any existing whistle-blower procedures which are likely to need reworking or replacing, including ensuring that whistle-blowers' information is stored securely and complies with privacy laws.

Feature

Women's role in solving the productivity puzzle

Alison Gill argues that looking differently at the role of women in senior management and on the board can have a positive effect on productivity.

Every negative trend needs a point of crisis to drive real change. The productivity crisis is the tipping point needed to get more women on boards.

Britain's 'productivity puzzle' shows no sign of improving. There have been three consecutive quarterly drops in employee output, with the ONS suggesting that wages would be £5,000 higher on average if the productivity crisis were fixed.

While economists continue to puzzle over why greater employment and more people working longer hours is resulting in consistently less output per hour compared to all our major competitors, despite the economy's recovery from the 2008 financial crash, one thing is clear: companies with a significant number of senior female leaders are bucking the trend.

It's not just that companies in the top quartile for gender diversity are15% more likely to outperform their industry peers, research also shows that average employee productivity growth is higher for companies that employ three or more women at board level, compared to those that have just a single female director or none at all.

All of which means companies with greater female representation at board level are not only able to generate higher levels of productivity and profits, as measured by returns on equity, but also higher dividend payouts to investors.

You would think that with results such as these, companies would be clamouring to realise the business benefits associated with greater female representation. Unfortunately, despite the growing body of evidence that gender-diverse boards lead to productivity gains, this is not an argument that can be won by logic alone.

UK firms are set to fall short of government targets for increasing female representation on boards to 33% by the end of 2020 and top firms have been criticised by the chief executive of the Hamilton Alexander Review for taking a 'one and done' approach to appointing women onto boards. And a small number of FTSE companies have been found to be 'intentionally blocking progress' and 'turning a blind eye' to their lack of female leaders.

Why boards don't want more female directors

Despite the evidence of the business and productivity benefits that greater female representation at board level can generate, boards are failing to realise these benefits because there is a cognitive dissonance at play. Those in a position to allow more women to progress onto boards are either consciously, or unconsciously, blocking them because of deeply held beliefs that override the evidence before them.

Beliefs such as those recently expressed by FTSE 350 Chairs and CEOs to the Department for Business, Energy and Industrial Strategy, which included the notion that women are not able to understand the 'extremely complex' issues FTSE boards deal with and that most of them don't want the 'hassle or pressure' of sitting on the board.

These views cannot be overcome with equality targets or data alone, not least because even though the FTSE 100 is on track to ensure that at least a third of their board members are women by 2020, there is concern that these quotas are being filled by appointing female non-execs as 'outsiders' who can represent a 'woman's view' without giving them any real input. Or by bringing the heads of HR, communications, and other functions traditionally associated with women, into the board, without giving them a voice outside of their specialist areas.

Instead of ineffective gender targets, which are doing nothing to challenge the deeply held beliefs holding women back from attaining senior leadership positions, what's needed now is a way of making the consequences of clinging to these views clear. That's why the impact of the productivity crisis on business results might yet prove to be the tipping point that shatters the glass ceiling.

Challenging deeply held beliefs

Of all the beliefs holding women back, perhaps the most detrimental is the belief that women don't really want the top roles, because they are too invested in their families.

Not only does this assumption have no basis in reality, with research showing that individuals who identify highly with both work and family invest twice as much time in work (compared to a person who is highly identified only with one or the other). But the reality of motherhood and commitment are two different things. To suggest you can't be committed to anything if you have any other priorities is simply confusing the issue. Many successful male board directors have many competing demands on their time, without these causing others to question their dedication in the way that the commitment of working mothers is constantly viewed with suspicion.

Feature

There are many high-performing women in the workplace who are discriminated against for working flexibly or part-time, even though the reality is that they have often learned to become more focused and effective than those who have the 'luxury' of working late, precisely because of this time constraint. In fact, a large study has found that women at work are 10% more productive than men, despite being paid 18% less.

That we currently have a situation whereby an individual working late every night is perceived to be a 'better' and more 'committed' employee, than someone who can get everything done to leave work at 3pm every day, goes a long way to explaining why the UK produces less by the end of Friday than all its major competitors can produce by Thursday.

> 'Instead of making assumptions about whether or not women want to be included in boards, directors must talk to individuals to find out what they actually want.'

Allowing women to progress

Going forward, instead of assuming that women who have worked flexibly or part-time in the past must be uncommitted, and therefore unfit for the boardroom, directors must instead consider which business metrics are most appropriate for identifying high performers and consider whether or not the ability to adhere to a traditional working pattern is the most important criteria at a time when productivity and the ability to innovate and generate results are becoming increasingly important.

Instead of making assumptions about whether or not women want to be included in boards, directors must talk to individuals to find out what they actually want. They should also talk to their own families – because it's often only once someone holding deeply held views realises the extent to which their loved ones are also affected, and wants their daughter or sister to have choices, instead of being subjected to bias, that they will be able to finally update their beliefs.

At the same time, female executives sitting below board level, need to be developed to understand the workings of the board so they know what to expect and can be encouraged to gain relevant experience.

Women should be encouraged to seek out opportunities to sit on boards in their own right, or the boards of other organisations as a non-exec. This matters because only by broadening the pool of people who understand what it means to be a good board director will the pool of candidates become broad enough to allow more women to progress and be considered for the board.

Setting meaningful targets

Only by creating diversity targets based on the business benefits that women can bring to boards, instead of viewing this as some kind of tick-box exercise, will organisations be able to see beyond the 33% representation target set by the Hampton-Alexander Review.

Critical amongst these targets must be realising the productivity gains that greater female representation at board level can achieve. Senior female leaders not only have a valuable role to play in making organisations more flexible, agile and productive, they can also do this in a way that can reduce the stress and anxiety issues that poor work-life balance and unhealthy working patterns have already resulted in. Poor wellbeing is another factor driving low levels of productivity, with a major study sponsored by Mercer finding that the healthiest workplaces are able to save 10.6 days of productive time per employee by improving the health of their workforce.

Essential to realising these benefits is not only recognising the extent to which greater female representation can help to achieve this, but also putting in place clear strategies outlining what values and behaviours are needed to deliver this change. These strategies should be based on organisational data, root-cause analysis and change mindset action plans, with feedback loops incorporated, rather than more assumptions and beliefs.

At the same time, anyone who continues to undermine the appointment of more women at board level, be this by creating insufficient solutions, failing to take action or scaremongering, must also be dealt with. Because changing a system of male-domination and a particular style of leadership and working that has persisted for centuries will inevitably leave some people feeling threatened.

As is so often the case, it is the role of the Chair to assess the extent to which deeply held beliefs towards women reside within themselves and the board in general, so that they can objectively challenge any outdated assumptions and take stock of the business benefits that can be realised. Only by focusing on these benefits can they unite the board in wanting to realise the productivity and wellbeing advantages that more female leaders now have an essential role to play in creating.

Alison Gill is a behavioural psychologist, triple Olympian and CEO of Bvalco, a board evaluation consultancy focused on helping boards to become fit for the future. https://bvalco.com

Feature

Shareholder 'activism'

Gerry Brown looks at whether shareholder 'activism' is all it is cracked up to be or what people claim.

The founding tenet of shareholder democracy is that shareholders can apparently try to hold executive boards to account at Annual Meetings by virtue of their ability to vote or grumble about many aspects of company strategy from incentive plans to environmental, social and governance (ESG) matters.

> 'In broad brush terms, said "activism" tends traditionally to be economic or, recently, more exotic and ESG in emphasis.'

This principle is, of course, laudable but often only really – ultimately – an effective mechanism for dissent or query as function of the size of your shareholding. That said, boardroom anxiety about the impacts and effects of activism and so-called activist investors upon the share price or company strategy continues to set the corporate governance mood music and continues on its exponential rise as the one-size-fits-all panacea for holding wayward or recalcitrant executives to account.

If the definition of a drunk is someone who drinks the same amount as you but you don't like them, then so it is with investor activism as viewed from the boardroom. If you are okay with the changes proposed then executive teams can safely endorse activism as mechanism to improve corporate governance as well as influence or change board strategy. But, if you don't agree with any proposals with some serious shareholding weight behind them – for example, a minority shareholder wanting a seat on the board, a ritual sacking of Chairman or CEO over strategy or a fire-sale-cum-spin-off-of-non-core-business style disposal – then shouts about abuse of power quickly ring out in the media and board minutes.

In broad brush terms, said 'activism' tends traditionally to be economic or, recently, more exotic and ESG in emphasis. Whatever side you view this activism white or wholemeal bread to be buttered on, I am firmly of the opinion that complaints and statistics about such investor activism is little more than a recent popular myth, albeit an increasingly prevalent one.

But who exactly is putting around these myths about the effectiveness and power of either democracy or activism? I think we need look no further than investment banks research departments in search of real, imagined or spurious competitive advantage vis-à-vis the competition.

For example, the always thoughtful Matt Levine of Bloomberg reports in his *Money Matters* newsletter[1], 'JPMorgan Chase has launched a data analytics tool that aims to predict how investors agitating for change will influence other company shareholders, in the latest example of advisers using technology to help clients ward off activists. … JPMorgan has created a huge data set on previous activist situations at US-listed companies, and used that to build a profile of how various shareholders typically respond to individual activists. The system can isolate which shareholders are likely to support a given activists' approach, JPMorgan said, and which are likely to sell their stakes if a given activist joins a company's share register. The data are then cross-referenced against a client's shareholder base.

"This is all done with … available data," said Huw Richards, a former bond market banker who is in charge of digital initiatives at JPMorgan's investment banking division. The algorithm that connects different data sets is the project's "secret sauce", he added.'

Levine isn't the only sceptic about both activism and the data-analytics of self-interested advisers so also reports, 'Bill Anderson, head of Evercore's activism/raid defence business, said that although "statistical analyses on shareholder voting histories can be interesting, a company's relationships with their shareholders are much more important". He added: "I am concerned that companies – perhaps encouraged by bankers – over-focus on data, rather than the blocking-and-tackling of shareholder engagement."' The industry reverence of and for stats appears to suggest that Know Your Customer has nowadays fallen out of fashion in investment banking almost as much as it has at retail banking in favour of love for spreadsheets and algorithms.

In his recent book, *Boards That Dare* author Marc Stigter[2] repeatedly presses his activist panic button. 'As shareholder voices continue to get louder and as activists gain more access and exert more influence, reluctant boards can no longer ignore them. In the past five years, one company in two in the S&P 500 index of America's most valuable listed firms has had a big activist fund on its share register, and one in seven has been on the receiving end of an activist attack. Even though shareholder activists are a relatively small group, they've enjoyed a higher rate of asset growth than hedge funds and attracted new partnerships with traditional investors. As a result, they have both the capital and the leverage to continue engaging large cap companies, according to McKinsey & Company.'

Feature

If we get down and dirty with a deep dive into the latest global figures produced by Activist Insight[3] ('the definitive resource on activist investing and corporate governance'): from a UK perspective, the fanfare that greeted the uptick in so-called investor activism in this country to record and global leadership levels in Q1 2019 (with 17 UK companies 'facing public activist demands'), casual observers could be forgiven for thinking that shareholder democracy was alive and – more importantly – really kicking.

'That certainly could underpin the news that, despite the so-called "activism", three years later UK board related investor demands remain pretty much where they were in 2016 (49% then compared to 50%).'

Yet, when we look beyond these snappy headlines, we find not only has the concept of shareholder activism been hi-jacked by a small cadre of extremely wealthy private equity investors with large shareholdings to leverage. But, more worryingly, the idea of increased board accountability is often just a polite synonym to describe rampant often wild short-termism in investment decision-making.

Indeed, before we get carried away with the idea that the UK is at the forefront of some kind of corporate governance glasnost led by a militant shareholder democracy revolution that increasingly holds UK (or global) executive boards to account, we need to acknowledge that – according to the latest Q1 2019 figures from Activist Insight – public activist demands about both corporate governance (9%) and remuneration (7%) have crashed to all-time lows.

Obviously, it comes as no real surprise or news that private equity shareholders focus upon quick profits so have little duty of care towards matters such as diversity and inclusion, sustainability, reducing remuneration inequality or good corporate governance generally. It is also worth noting that from a global perspective, the first quarter 2019 was the quietist in activism terms since 2015. Rather than conclude that all the panic has been overblown, we must acknowledge the successful impact of public relations initiatives from cannier corporates to discuss, mitigate and resolve matters that itch and irk activist investors behind closed doors rather than virtue signalling them in a public forum.

That certainly could underpin the news that, despite the so-called 'activism', three years later UK board related investor demands remain pretty much where they were in 2016 (49% then compared to 50%).

As previously noted, actually moving the needle of dissatisfaction remains almost solely the prerogative of activists with seven figure investments rather than small ordinary shareholders. Even such shareholders aren't a guaranteed sure fire recipe for change: for example, Sherbourne Investors held $1.4bn of Barclays stock yet still failed to get their way with the board. Europe's biggest activist investors with serious strategic, board composition or governance aims in mind need to 'pay to play' to match their invariably short-termist ambitions with shareholdings often beyond the deepest pockets of individuals and pension funds alike.

Small UK investors continue to make the news, as well as signal their justifiable anger, via exercising their annual shareholder voting rights. This annual box-ticking led exercise in grass roots criticism mostly remains a charade, roughly equivalent to the effectiveness of repeatedly clicking on your Twitter like button, when it comes to making real changes to board level remuneration, environmental, social and governance issues as well as strategy.

More importantly, until shareholders can really hold UK executive boards to proper account, then we need to find other means to head off trouble at the pass. To my mind, this also requires effectively tapping into the already available non-executive talent pool. While we wait for the actions of shareholder democracy to catch up the florid claims, one place to start with immediate effect could be that UK executive boards need to commit to curtail their current widespread poor hiring practices.

Better non-executive recruitment is low-cost-high-return sensible housekeeping since it not only wards off most private equity activist shareholder interventions but it also immediately leverages the long-term value creation benefits truly Independent Directors deliver when they are allowed to hold executives to strategic account. Such free-minded non-execs are also able to provide the disinterested analysis and advice that might prevent, slow-down or mitigate the ongoing flow of often self-inflicted UK corporate scandals.

Gerry Brown is Chairman of Novaquest Capital Management and also the author of The Independent Director: The Non-Executive Director's Guide to Effective Board Presence (Palgrave Macmillan).

1 Matt Levine: 'Activism preparedness' (Money Stuff 22.07.19)
2 Marc Stigter: Boards That Dare (Bloomsbury, London, 2018), p.9
3 Activist Insight: 'Shareholder Activism in Q1 2019' (April 2019)

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