

LGIM's annual non-executive director event 2020



Introduction and welcome

We were delighted that so many Non-Executive Directors were able to join us for our fifth NED event, our first to have a truly global audience.



It's been an unusual and a disruptive year for all of us and the Coronavirus has forced many companies to change the way they operate, to look carefully at the skillsets of their board members, and to give a new level of priority to the welfare of their employees. Different data sets are emerging to help investors make sense of the shifting landscape. What's becoming clear is that the companies which for a long time have prioritised having high environmental, social and governance standards have fared better during the current crisis than peers which have not.

In this summary, we provide a brief overview of the main points from each session of our event. We meet hundreds of companies every year, but we can't meet everybody. By sharing our stewardship principles, rationale and implementation, as well as sharing our experience through our NED events, we aim to provide you with information and ideas to help you prepare your company for the future.



John Hoepfner
Stewardship & Sustainable
Investing, LGIMA



A new normal: how COVID-19 has changed the world

The COVID-19 pandemic has been incredibly challenging for many companies, and is likely to continue to be so. At LGIM, we recognise these challenges and we want to support you as company directors, doing your duties to help your firm navigate this new landscape.

As long-term shareholders, we've noticed that a number of themes that we've been discussing in these NED events over the past four years have been more important in 2020 than ever before. The need to challenge, support and find new ways of working has emphasised the need for diversity of thought, for people with the ideas and creativity to adapt your business for the future. The issue of 'overboarding' has also come to the fore: although seven board appointments might be a reflection of skill, do you have the time to help seven different companies through a crisis, all at the same time? Executive pay will also be a focus this year and we think it's vital that pay and rewards are aligned to

long-term results. Health and safety has been thrown into the spotlight: employees are companies' most important assets, and companies need to show that they are being looked after.

The conversation has moved beyond equities - credit investors are increasingly concerned about ESG factors and how they affect company valuations. Compared to ten years ago when conversations were about margins and saving on tax, we're now talking about employee welfare, social issues and companies paying their fair share. Even boards are working in different ways – the use of advisory boards, for example. We want to support you in finding the right people to make the best decisions for your business.

Employees want to work for great companies – we want you to work for a great company, and we want to invest in great companies. We want companies to do well, to make profits and be able to pay dividends, which are important to paying our clients' pensions. A more responsible form of capitalism, and LGIM's continued work to reduce red tape, are work for the long term. We are all part of the societies in which we operate, and LGIM is here to help you and your boards on this journey to transparency, accountability and adapting to the new normal.



Sacha Sadan
Director of Investment
Stewardship, LGIM

Engage for change: our 2021 plans

Broadening our conversation on diversity

Why diversity at board level is so important, and how NEDs can help tackle the 'S' of ESG.

2020 has seen a greater focus on diversity than ever before and in the corporate sphere, there is much work to be done. Of the S&P 500 companies in the US, 44 companies, or 8%, have no ethnic or racial diversity at board level; in the UK's FTSE 100 index, the number is much higher, at 36%. But how can companies move beyond reactionary platitudes and create real, positive change?

LGIM's five suggestions for **broadening diversity** are:

1. **Data:** ask for self-identification from employees at all levels so that you can report as accurately as possible – good data is essential for charting progress.
2. **Targets:** set out aspirational targets for ethnic diversity at your organisation – as the saying goes, what gets measured gets managed.
3. **Top-down:** buy-in from the top level of your organisation is essential.
4. **Talk and listen:** companies, leaders and boards must learn to be comfortable talking about the way in which race and ethnicity informs a person's experience and perspective. It is these different experiences that we must harness.
5. **Connect:** remember that ethnicity is part of a broader discussion about cognitive diversity – different ways of thinking and people who are different from each other are what will bring strength to a team.



LGIM's engagement strategy includes writing to the S&P 500 and the FTSE 100 companies whose board membership shows a total lack of ethnic diversity. We will be asking companies to have at least one non-Caucasian director on their board by the end of 2021, and from 2022 we will start voting against the Chair of the Board or of the Nomination Committee if there is still no ethnic diversity at board level. We believe transparency on issues such as diversity and inclusion are a broader reflection of a company's approach to governance, culture and risk management; following the pandemic, these will increasingly be areas of focus. Our aim is to have companies that are fully diverse and fit for the future.



Clare Payn
Senior Global ESG and Diversity
Manager, LGIM



The role of the board in tackling income inequality

Opening our eyes to income inequality and how all businesses can fight against it.

The events of this year have thrown a spotlight on the fact that many people who do the most important jobs in our society, from healthcare workers to cleaners, are often the least well-paid. Income inequality is not only structurally embedded within our society, but also appears to be worsening significantly – think of those statistics you read about high-flying company executives who by the first week of January have earned as much as their lowest employees will earn all year. Fears that the poorest in society will bear the brunt of the effects of the Coronavirus are sadly not only legitimate, but already being realised.

Income inequality differs within each country and can be improved or exacerbated by, for example, use of the minimum wage instead of a living wage, or regulations regarding healthcare and insurance. But individual companies can and should take action to improve the situation within their own firms and to make sure that those on the lowest rung are as well protected as those at the top of the ladder.

Some of **LGIM's suggestions** for helping to reduce income inequality in your organisation are:

1. Review your company's pay policies in light of a 'living wage'.
2. Look at data on how many of your lowest paid workers take up benefits on offer and assess how to make them more suitable and widely accessible to those who may need them most within your organisation.
3. Reduce where possible the use of insecure working practices such as 'zero hour contracts' and ensure all workers have contracts that offer a guaranteed number of hours each week, sick pay, and at least three weeks' notice of termination.
4. Assess what your company is doing to invest in the future generation of workers.



Angeli Benham

Senior Global ESG Manager, LGIM

ESG transparency: the responsibility of boards

As the stakes are raised, what can company boards do to improve the transparency of their ESG reporting?

Amid the growing consensus on the financial materiality of ESG issues, markets need to be able to price companies' ESG information accurately. We are only at the beginning of this journey, but the increasing breadth and availability of ESG data points means that more companies are being judged on what they do and do not disclose.

At LGIM, there are three broad actions we are taking regarding transparency of disclosures: the vote sanction, engagement at public policy level, and capital allocation. We use voting to hold boards to account, and we engage with policymakers across the world to help ensure disclosure standards and regulations are robust and consistent. And finally, our capital allocation decisions reflect our ultimate decision on whether we can continue to invest in a company.

So what can company boards do to improve their ESG transparency?

1. We expect ESG credentials to be disclosed in accordance with the guidance set out by the Sustainable Accounting Standards Board, and we encourage additional disclosure in line with the Global Reporting Initiative standards. Regarding climate change disclosure we would like to see alignment with the Taskforce on Climate-related Financial Disclosures (TCFD), the Climate Disclosure Standards Board (CDSB) and the CDP (formerly Carbon Disclosure Project).

2. In terms of how to disclose, while LGIM does not prescribe a particular form of reporting, we like to see evidence of ESG integration within a company's corporate vision and strategy, and to see ESG data that is accessible so that it can be extracted and analysed.
3. We encourage companies where possible to be proactive in having their ESG data verified by an independent assurance specialist, based on recognised standards.
4. Regarding ESG performance, boards should make sure that information held by third-party providers is accurate as the financial community increasingly relies on this data.

Most importantly, in addition to asking our investee companies to be transparent, we also apply these standards to ourselves. These discussions will continue into the future and for more information on our [approach to ESG and our expectations](#), please visit our [website](#).



Marion Plouhinec
Senior Global ESG Analyst,
LGIM



Avoiding the vote sanction

How LGIM helps companies better align their interests with investors.

We are long-term, constructive shareholders who support our investee holdings. We aim to improve market standards by working with companies and holding management to account for their decisions via our voting, as well as working with regulators and policymakers. We've noticed that in every AGM season, there are a few companies which make avoidable mistakes, incurring unnecessarily high numbers of 'against' votes. It is essential that the flow of information between investors and companies reaches all relevant parties, from investor relations to the company secretary and board members.

In times of crisis, ESG practices come to the fore. The COVID-19 pandemic has laid bare the difference between well-run companies that can weather the storm, and those that are likely to struggle. Such situations require strong, independent boards with diversity of thought and background, and board members who have enough time to devote themselves seriously to the tasks in hand. Companies which have received government support, have needed to raise capital, and/ or have had to make redundancies are likely to come under scrutiny as they plan for the future.



To help companies look at their decisions from an outsider's perspective, we summarise below some of the key points that LGIM and other investors will be looking at when casting their votes at your AGMs:

1. Board robustness: diversity, independence, division of CEO/Chair roles, directors with board positions at multiple companies.
2. Remuneration: keep it clear and simple, aligned with long-term performance, and ensure base salary increases and pension contributions are in line with the general workforce. If you are going against the grain, explain why.
3. Audit: length of tenure of your auditor, audit committee expertise, and audit versus non-audit fees.
4. Raising capital in COVID-19 times: is there a legitimate reason or are you just replenishing the 'war chest'?

We make our [voting policies publicly available](#), as do other investors, and these are important sources of information to be familiar with as you help your company plan for a stronger, more sustainable future.



Maria Larsson Ortino
Global ESG Manager, LGIM

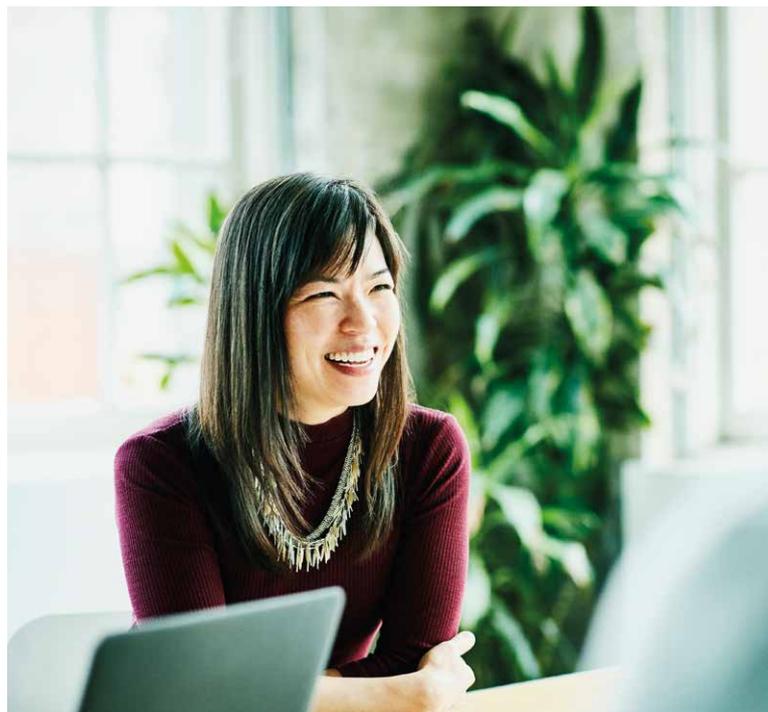
The future of effective engagement

Current interest in shareholder engagement is tremendous, propelled by governance codes, regulatory developments, and advocacy groups who tout these interactions as helping to work through well-known market challenges.

In our own experience, many of the direct company engagements have lacked the two-way exchange, candour and preparation to maximise their potential. In the live poll, 30% of our audience found most investor engagement calls were a waste time. That number is too high: the nature and purpose of engagement have to change – and they will.

We believe three main forces will drive this change: technology, data and novel collaboration models. All have the potential to improve the quality, speed and scale of engagement, particularly against a backdrop of evolving regulation.

1. **Technology:** from news bots automatically syndicating our voting stance to seeking feedback from investors on contentious votes, technology is the engine of the two-way conversation between companies and investors, making it possible to connect and analyse growing numbers of data sets.
2. **Data:** quality and transparency are quickly improving – standardisation is creating the foundation. We have different data strategies depending on objective – for example active strategies have more proprietary ESG elements, whereas our index and stewardship data seek to be ‘radically transparent’ all the way through to source data. We are publishing ESG scores (and, as of October, specific climate scores) for thousands of large listed companies, alongside methodologies used.



3. **Novel collaborations:** instead of relying on one-to-one calls and conversations, we are changing the way we interact, and are seeing an increase in collaborations between like-minded investors, working with companies and industry bodies around the world to raise ESG standards.

And finally, although regulation differences around the world can provide either headwinds or tailwinds, it’s important to ask who makes the decisions: is it the company, the state or is it feedback from investors? The tension between stakeholders has always been there, but the contradictions are becoming much clearer, particularly through social media. This dynamic will be crucial for all companies in shaping their pathway to a more sustainable future.



John Hoepfner
Stewardship & Sustainable Investing, LGIMA



Iancu Daramus
Senior Sustainability Analyst, LGIM

Net zero by 2050: what does it take?



Meryam Omi

Head of Sustainability and Responsible Investment Strategy, LGIM



Edward Bonham Carter

Senior Independent Director, Land Securities and Vice Chairman of Jupiter Fund Management plc

Q

What kind of conversations are you having about 'net zero targets'?

A

Land Securities was one of the first companies to sign up to the Paris-based climate agreement talks – I think it took the business about five years to get to a '2 degree world'. That seems a long time ago because we're now looking at a 1.5 degree world, followed by 'net zero'. To use the cliché, it's a journey: the board is fully committed. Our customers want this and we believe, as do many companies, that this is an absolutely necessary thing to do.

Q

Do some people think 'net zero' should be pushed aside for now?

A

Over the last five years, Land Securities has reduced its carbon footprint by over 40%. Half of that is from energy, moving away from coal. Other reductions have been made by making the buildings more efficient. But the big improvements will continue to be in terms of materials. We're just at the beginning of that, but I don't think there's a lack of commitment – I think COVID-19 is probably going to accelerate the demand for companies to respond to these trends.

Q

How do you reconcile the timeframe of business to the timeframe of individuals on the board, or executive pay?

A

There are no easy answers. The pressure on us all is how to think over the medium and long-term. If you're developing and building a new building, you need to have a lifecycle of five to ten years, if not longer. You have to have the courage to make decisions and judgments about what the world's going to look like – sustainability is going to be part of that. The average tenure of CEOs in the UK and the US is getting shorter. But I think the way to hold companies to account is to ask what is their progress, year-on-year. You can see disclosures in annual reports and they have to be more transparent.

Q

Are conversations on net zero or the climate agenda too 'new' to be on the agenda?

A

It's starting to come up – I think it's still relatively early days for a mainstream conversation. Many investors still think of their corporate governance teams and fund management teams as separate buckets. I think increasingly it should be one conversation not only about financials, but about the long-term issues that companies are facing, including net zero.

Ask the experts: Audience Q&A

Moderated by John Hoepfner, Stewardship & Sustainable Investing, LGIMA



Q: When do property companies need to start considering their Scope 3 emissions?

Meryam Omi: Scope 3 emissions relate to those from the supply chain and the use of property by their tenants. For the supply chain, it relates to construction of the buildings, what kind of materials are used, and how much carbon is involved in the process of making steel, cement and so forth. The simple answer is that property companies need to be thinking about this now, given the net zero goal of 2050. It's essential to start thinking about alternative materials and carbon capture, and to start to push this through the supply chains. It's also important to make tenants consider the implications of energy use. Talking to both sides is vital and thinking holistically, including about the impact upon society, will be really important.

Q: In some countries, for example Sweden, it's illegal to collect data on ethnicity, and in many companies around the world, there are employees who don't want to share information on their ethnicity. How do you handle this?

Clare Payn: So far, we have been looking primarily at the US and the UK, but we recognise that in many companies and other countries, we will need to take a more nuanced approach and incorporate qualitative research. There are a number of qualitative factors you can look at, such as policies and practices and initiatives, for example whether the company engages with any universities or higher education institutes to encourage graduate applications from a wider range of backgrounds. Even if you are unable to track your company's ethnicity and diversity through numbers (and this might be the case for many companies), there are ways that you can start to think about this and gather other information that you can use.

Q: In the UK, approximately 12% of the population is 'ethnically diverse'. Is this the right target for a UK company board?

Clare Payn: When coming up with targets for your company, it's important to reflect the society that you operate in – you need to look at your employees, your industry and your customer base, and set aspirational targets that are appropriate for your company. Diversity isn't about matching quotas – it's about finding the best people, and taking a sensible approach and timeframe that are appropriate for your company.

John Hoepfner: No stewardship team likes drawing red lines, but seeing zero diversity among board members is clearly unrepresentative. It sets a very low bar as a starting point for improvement!

Q: Please comment on LGIM's own ethnic diversity and statistics: how are you doing?

Sacha Sadan: We are delighted to answer your questions on LGIM! We are not perfect on diversity but we have done a lot of work and continue to do so. Our biggest board is chaired by an ethnic minority director, and we are looking carefully at replacements for board members who have had to step down. We have made great progress in increasing female representation in senior positions across LGIM and L&G. We are still on our journey, and we try to act in the same way as we ask of the companies in which we invest.

Q: Is LGIM comfortable with being made an insider if a company consults them on governance?

Sacha Sadan: If it really is a consultation and it is early on, we are able to be made insiders and have appropriate 'Chinese Walls' to be involved in the debates. Where it becomes frustrating for us is where we are told at 4:30pm the day before a public announcement, which isn't consultation, it's just being told a bit ahead of everyone else!



Q: How does your team evaluate heavy carbon use industries?

Meryam Omi: Next month (October) we will be publishing the latest version of our Climate Impact Pledge where you will be able to see all of our expectations in regards to addressing climate change. This will be available on our website and will summarise our expectations for each key sector in relation to the net zero target, recognising the challenges and opportunities for each. We will also explain what we expect in terms of policies and disclosures. We have been engaging for a number of years with oil and gas and mining companies who are going through an enormous energy transformation. We expect to see this built into their companies' strategies and articulated in their future proof plan. We will be looking for real evidence that the right conversations are taking place on the board, by reading through TCFD and CDP, in addition to our meetings. Through our pressure, we aim to steer companies into a sustainable direction – all companies, not just the carbon-heavy industries. The pressure is on and this conversation will continue!

Q: Do you worry that tougher requirements for stewardship in listed companies may encourage companies to delist, or not to list at all?

Sacha Sadan: We are stewards of our clients' capital and we run money on behalf of many of these companies – this might be your pension schemes! We want to do this well. But there are minimum standards you can and should expect for the people investing that money, and we don't regard these rules relating to, for example, audit committees, minimum directorships and premium listings as onerous. We want to have these minimum standards – we've seen too many examples of where it has gone wrong, and then you get regulations and governments stepping in with much tougher requirements than we would want, and we do push back when this happens (for example, on quotas). So we don't think current standards are onerous.

Q: What are your expectations for the role of Designated NED for Workforce Engagement? Would you want to engage with the person in this role?

Clare Payn: Yes, we would want to engage with that individual – it's important that the workforce is able to feed into the board via this role, and for this individual to be that voice at the very highest level. It's a key role.

Sacha Sadan: There was a huge clamour in the UK for employees to be heard on UK boards. We've tried hard to say it is up to each company to work with the version of this that they think is best and once they have decided how to manage this, we would expect to see evidence of how the employee voice has been factored into decisions.

John Hoepfner: Clare and I led a specific engagement exercise about workforce and culture and what elements of culture can be measured externally. We asked NEDs whether they'd walked through the halls and what the experience was like, and the level of detail that we received was a good signal. So it's good to share a story with your investors showing what you are actually doing.



Remarks from the Chair

All of us who are NEDs understand that we are on a journey. LGIM has been one of the leaders, but we will all have seen a significant change in attitudes: we recognise that companies are part of the broader community and see the impact that they have, which can be positive as well as negative.

From today, I would highlight two main challenges: the first is getting started on this journey. In a number of areas you will find that you don't yet have neat financial metrics, but you still have to make a start and work out ways to show the positive difference you are making. And the second challenge is being clear about the timelines for these changes.

The economic situation over the next few months and possibly years will be difficult and issues such as income inequality and executive pay will be examined. We need to remember that employees want to be proud of the companies that they work for.

NEDs are able to bring experience from a wide range of sectors – many of us have sat on many different boards and through this, we can bring the knowledge that there are people out there who have different and interesting ways of thinking about these challenges which may help your companies find the solution that will work for them. We have a huge part to play and our role is more interesting and arguably more important now than it has ever been before.



Lesley Knox

Chair of the LGIM (H) Board and a Group Board Non-Executive Director, LGIM

Contact us

For further information about LGIM, please visit lgim.com or contact your usual LGIM representative



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