NAPF

Securing the future of pensions

European Commission Consultation "Gender imbalance in corporate boards in the EU"

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About the NAPF

The NAPF is the leading voice of workplace pension provision in the UK. We represent some 1,200 pension schemes from all parts of the economy and 400 businesses providing essential services to the pensions industry. Ten million working people currently belong to NAPF member schemes, while around 5 million pensioners are receiving valuable retirement income from those schemes. NAPF member schemes hold assets of some £800 billion, and account for over one sixth of investment in the UK stock market. Our main objective is to ensure the security and sustainability of UK pensions.

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Executive Summary

- We believe there are several benefits associated with board diversity, particularly gender diversity, and understand and share the concern that low levels of women on boards can inhibit board effectiveness.

- It is important to ensure that any improvement in gender diversity does not come at the expense of skills and experience, and our view is that this is not a matter to be regulated.

- We do not believe that the debate about board diversity should be specifically limited to gender.

- We believe that companies should disclose their diversity policy, including the extent to which professional, international and gender diversity are considered.

- There is potential for shareholders to use their voting rights to encourage gender diversity.

- We believe that voluntary targets should be increased over time but that the key thing is a change in corporate culture and the development of an on-going pipeline to populate boards.

- Market driven initiatives, on a comply or explain basis, coupled with the reform of Corporate Governance Codes and the encouragement of responsible stewardship will in our view be the best way of achieving balanced and effective boards.

Response to individual questions

General Questions

(1) How effective is self-regulation by businesses to address the issue of gender imbalance in corporate boards in the EU?

We believe there are several benefits associated with board diversity, particularly gender diversity, and understand and share the concern that low levels of women on boards can inhibit board effectiveness. However, we believe it is important to ensure that any improvement in gender diversity does not come at the expense of skills, experience and broader diversity. Our view is that this is not a matter to be regulated; instead we believe that market instigated and based initiatives, including targets, underpinned by the principle of "comply or explain" is the most appropriate and effective method to achieve long term sustainable change.

Self regulation is proving effective but needs time to succeed.

Recent political, media and importantly market scrutiny issue has resulted in notable improvements in this area.

In the UK we have had the Lord Davies "Independent Review into Women on Boards"[1] which has focused boards' attention on gender diversity and the extensive media and market attention on the issue is encouraging boards to consider this issue and take action. We believe the resultant revisions to the UK Corporate Governance Code will go a good way to addressing the problem.

In our view self-regulation is the key to addressing the issue of balanced leadership. Many of the self-regulation mechanisms and proposals, such as the changes emanating from the Davies Report, are still very new. As such they should be allowed to become embedded and for companies to be given the opportunity to adapt to and embrace them. Importantly, to truly address the issue in a sustainable fashion, companies need the time to be able to nurture their potential female executives, developing them into effective leaders.

Research conducted by the Cranfield School of Management on the first anniversary of the Lord Davies' review revealed a significant move in a positive direction[2]. If the current pace of change continues almost 30% of directors could be women by 2015 and almost 40% by 2020. It is sensible to allow the opportunity for this change to continue in the first instance.

Quotas would be self-defeating

We are not supportive of mandatory quotas for the proportion of women on boards, as we are concerned that it could lead to a simple 'box-ticking' approach at the expense of board and company performance.

Mandatory quotas are blunt, unsophisticated instruments which address the symptoms of an issue as opposed to solving the root cause. We favour a more sustainable solution whereby chairmen engage in setting and achieving voluntary measureable targets.

[1] http://www.bis.gov.uk/assets/biscore/business-law/docs/w/11-745-women-on-boards.pdf
[2] http://www.som.cranfield.ac.uk/som/ftse

In Norway, from 2004, companies were mandated to have 40% women directors (the average proportion at the time in Norway was 9%). Subsequent evidence indicates that the introduction of quotas actually undermined shareholder value[3]. Research found: "Significant decreases in operating performance and higher costs as a result of the imposition of the quota. These results are consistent with boards of directors that lack sufficient experience to act as capable advisors." The introduction of the quota also led to a large number of companies de-listing from the Norwegian stock exchange.

The EU should adopt a consistent approach to corporate governance

The wider corporate governance debates taking place at present at EU level, including those considering issues such as the composition, objectives and limits on the number of board directorships individuals can hold are framed as "comply or explain" requirements; this issue could also be treated effectively in this way and result in a consistent EU approach to governance issues.

Diversity is broader than gender

We do not believe that the debate about board diversity should be specifically limited to gender, instead boards should encompass a balance of skills, experience, independence and knowledge of the company, considerations should include professional, international and gender diversity.

(2) What additional action (self-regulatory/regulatory) should be taken to address the issue of gender imbalance in corporate boards in the EU?

We believe that recent self-regulatory action is proving effective but needs time to succeed. We have outlined a number of potential actions below.

Target setting & reporting

We agree with the Davies Review recommendation that companies voluntarily set and disclose their approach to diversity. We also believe that companies should disclose in their Annual Report and Accounts the company's diversity policy; including the extent to which professional, international and gender diversity are considered.

The importance of gender diversity has been emphasised in the past year and investors now expect boards to set out an explicit policy for achieving a greater degree of diversity than has been the practice in the past, as such stronger scrutiny of Board policy regarding director appointments and succession can be expected.

This approach of target setting and reporting could be replicated at an EU level.

Shareholder influence

Through this fuller and more open disclosure the shareholders of companies can apply more pressure on companies if needed to act in a responsible and balanced way.

The NAPF believes that there is a potential for shareholders to use their voting rights to encourage gender diversity, and our Corporate Governance Policy and Voting Guidelines currently ask that boards explain to shareholders what steps they are taking to bring diversity to their boardroom.

[3] The Changing of the Boards: The Impact on Firm Valuation of Mandated Female Board Representation Kenneth R. Ahern and Amy Dittmar, University of Michigan, Ross School of Business May 20, 2011

Where there is no statement on a company's diversity policy, shareholders may choose to vote against the election of a director – who in the UK are now up for re-election each year. We intend to update our guidelines later this year to reflect recent changes (which we welcome) to the UK Corporate Governance Code. We are also assessing how we can assist our members in holding their asset managers to account on key issues such as diversity.

A formal and transparent procedure for appointing new directors

We believe there should be a formal and transparent procedure for appointing new directors to the board and this should encompass a balance of skills, experience, independence and knowledge of the company. The search for board candidates should give due consideration to the benefits of diversity on the board.

(3) In your view, would an increased presence of women on company boards bring <u>economic benefits</u>, and which ones?

Yes we think more balanced leadership will bring economic benefits. As mentioned above this is not just gender balance but also all other factors that allows board members to represent and understand their customers and workforce.

There is a growing body of evidence to support this. In addition to the findings in the Commission's report, reports from McKinsey[4][5], The Economist[6] and Ernst & Young[7] show a positive correlation between women in management positions (and throughout the workforce) and a rise in economic performance of those companies.

(4) Which <u>objectives</u> (e.g. 20%, 30%, 40%, 60%) should be defined for the share of the underrepresented sex on company boards and for which <u>timeframe</u>? Should these objectives be <u>binding</u> or a <u>recommendation</u>? Why?

We believe that increases should be both incremental and non-binding for the reasons cited above.

We believe that voluntary targets should be increased over time but that the key thing is a change in corporate culture and the development of an on-going pipeline to populate boards. Thus we support voluntary reporting on a "comply or explain" basis as set out above.

(5) Which <u>companies</u> (e.g. publicly listed / from a certain size) should be covered by such an initiative?

We believe that all listed companies should be encouraged to address the issue of balanced leadership. Market led targets on a "comply or explain" basis will allow all companies to show progress in this area.

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[4] http://www.mckinsey.com/locations/swiss/news_publications/pdf/women_matter_2010_4.pdf

[5] "Women Matter: gender diversity, a corporate performance driver", McKinsey & Company, 2007.

[6] http://www.economist.com/node/21539928

[7] http://www.ey.com/Publication/vwLUAssets/Mixed_Leadership/$FILE/Mixed%20Leadership%202012.pdf

SMEs and non-listed companies should also be encouraged to make public their targets.

(6) Which boards/board members (executive / non-executive) should be covered by such an initiative?

The main board, as a whole, of all publicly listed companies should seek to have a balanced composition. Particular attention should be paid to developing women into executive roles. Most women on boards currently tend to be non-executive directors. Of particular concern to shareholders, including pension funds, is the independence of NEDs, succession planning, evaluation and re-election.

(7) Should there be any sanctions applied to companies which do not meet the objectives? Should there be any exception for not reaching the objectives?

We believe that any initiative should be market led and based on the “comply or explain” principle. This will mean that the market will sanction companies that do not meet their stated objectives.

Companies who are committed to increasing balanced leadership should also apply pressure on their suppliers and partners to take action.