GUIDANCE PAPER

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EFFECTIVE STAKEHOLDER ENGAGEMENT WITHIN THE CONTEXT OF REMUNERATION

Introduction

The King Subcommittee on Remuneration has identified a few concerns regarding the application of Principle 14 in the King IV Report on Corporate Governance in South Africa 2016[1]. One of these concerns is the perceived lack of effective stakeholder engagement between stakeholders and organisations on the matter of remuneration. Ineffective stakeholder engagement could be because of stakeholder apathy or ineffective interventions by organisations to create platforms for constructive dialogue with stakeholders.

Context setting

Executive pay has never been more of a dilemma than in 2021, in the wake of the devastating impacts caused by the Covid-19 pandemic which has put the spotlight firmly on the extreme levels of social and economic inequalities in so many countries. The pandemic has sent a clear message that social issues can trigger significant financial risks and threaten organisational sustainability in an unimaginable way. Although many executives have taken short-term salary cuts and forfeited short-term incentives in recognition of hardship suffered by employees and communities, these are largely symbolic steps; governing bodies have the arduous task of finding the right balance between reward outcomes, financial and non-financial organisational performance and impacts on all stakeholders, over the next few years. This balance includes working through the moral dilemma of awarding justified high incentives in recognition of exceptional performance rendering outstanding results to shareholders during this exceptionally difficult period in the world's history, when at the same time, there is so much poverty and unemployment. Governing bodies and executives are at a crossroads facing opportunities to rebalance the world.

Stakeholder interests need to be determined and trade-offs must be made between achieving multiple desirable objectives including the balancing act between an increased focus on sustainability, achieved through a combination of financial and non-financial measures such as environment, social and governance (ESG) matters. It is widely documented that organisations which consider key stakeholder interests in their strategy and business plans are more likely to produce long-term, multi-faceted sustainable growth[2]. There is increasing pressure from proxy houses, asset managers, community groups and NGOs towards organisations to focus on reducing their environmental impact disclose how they have integrated ESG matters into executive remuneration design. The World Economic Forum (WEF), in September 2020, published a report on CEOs of 120 companies in the International Business Council (IBC) titled "Measuring Stakeholder Capitalism: Towards Common Metrics and Consistent Reporting of Sustainable Value Creation" suggesting 21 'core' and 34 'expanded' metrics in the categories of principles of governance, planet, people and prosperity[3]. The purpose of this initiative by the IBC and the WEF was to develop guidelines on how organisations could demonstrate how they are serving the interests of a broad group of stakeholders, beyond investors – this is where the engagement with stakeholders starts.

Purpose of this paper

This paper aims to address the matter of apparent ineffective stakeholder engagement and to provide more guidance to governing bodies and remuneration committees for enhancing dialogue with key stakeholders. This guidance is based on the premise that stakeholders are responsibly responding to the calls for engagement with organisations.

[1] The King IV Report on Corporate Governance for South Africa 2016
https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/684B68A7-B768-465C-8214-E3A007F15A5A/IoDSA_King_IV_Report_-_WebVersion.pdf
[2] Harvard Law School on Corporate Governance: ESG and Executive Remuneration – Disconnect or convergence
https://corpgov.law.harvard.edu/
[3] www.weforum/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf

King IV is premised on the stakeholder inclusive model whereby the governing body should consider and balance the legitimate and reasonable needs, interests, and expectations of all stakeholders in the best interests of the organisation. Stakeholder inclusivity is described in King IV[1] as "there is an independent relationship between the organisation and its stakeholders, and the organisation's ability to create value for itself depends on its ability to create value for others. An organisation becomes attuned to the opportunities and challenges posed by the triple context in which it operates by having regard to the needs, interests and expectations of material stakeholders. When using the six capitals model as an alternative lens, it is evident that each of the forms of capital has one or more stakeholders with an interest in it."

Stakeholders therefore have an obligation towards ensuring that the organisation acts as a responsible citizen and they should engage responsibly with the organisation to exercise their legitimate rights and expectations ensuring sustainable value creation for all.[4] By following the stakeholder-inclusive approach, the governing body ensures that the interests of the providers of capital, are balanced with the interests of all sources and providers of value creation including social and relationship capital[1].

The only stakeholder that has a formal and well-understood mechanism for engaging with organisations are shareholders who have the legal right to vote on resolutions at the Annual General Meeting ("AGM"). Thus, organisations should not have to ask shareholders for their input – the mechanism is already there for them to use it. Institutional shareholders should be encouraged to use these mechanisms.

Contrary to this, other stakeholders do not have formal and well-understood channels for engaging with organisations on a regular basis unless organisations create these channels (such as establishing employee or customer forums or climate change dialogue platforms). Important stakeholders such as suppliers, customers, and communities are usually too diverse and disorganised to effectively challenge organisations on issues that affect them. Because of this, these stakeholders generally must wait for the organisation to make the first move (which many leading organisations already do).

Thus, the obligation to meaningfully engage with stakeholders lies more with organisations than with stakeholders.

This paper should be read together with King IV and its related Remuneration Guidance Notes, and relevant legislation, including, but not limited to, the Companies Act, 2008, as amended, the JSE Limited Listings Requirements, and International Financial Reporting Standards.

What Is a Stakeholder?

A stakeholder is a party that has an interest in an organisation and can either affect or be affected by the decisions taken by or performance of the organisation. The primary stakeholders in a typical corporation are its shareholders, employees, financiers, customers, and suppliers. However, with the increasing attention on corporate social responsibility, the concept has been extended to include communities, governments, and trade associations.[5] The term "stakeholder" appears 150 times in the King IV report, which shows how important the concept has become. King IV states that an organisation "can no longer be seen as existing in its own narrow universe (or society) of internal stakeholders or resources needed to create value, as it also operates in, and forms part of general society". In this view, the licensor of an organisation is not just those individuals and entities within its narrowly defined value chain, but society as a whole."

[4] Guidance for Remuneration Committees: The Remuneration Policy https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/57F28684-0FFA-4C46-9AD9-EBE3A3DFB101/Paper_2_The_Remuneration_Policy.docx.pdf
[5] https://www.investopedia.com/terms/s/stakeholder.asp

The AA1000 AccountAbility Stakeholder Engagement Standard[6] defines stakeholders as "… those groups who affect and/or could be affected by an organisation's activities, products or services, and associated performance. This does not include all those who may have knowledge of or views about the organisation. Organisations will have many stakeholders, each with distinct types and levels of involvement, and often with diverse and sometimes conflicting interests and concerns." Stakeholder Engagement is defined as "… the process used by an organisation to engage relevant stakeholders for a purpose to achieve accepted outcomes."[7]

The quality of stakeholder relationships indicates how effectively an organisation can strike a balance between the needs, interests and expectations of all stakeholders when making its decisions[1].

Why are Stakeholders relevant in the context of remuneration?

Executive remuneration has become a complicated and controversial topic resulting in the potential for multiple reputational risks. Therefore, the preparation and composition of a comprehensive remuneration policy are increasingly important for governing bodies and remuneration committees.

In terms of Principle 14 of the King IV Report on Corporate Governance for South Africa 2016[8] ("King IV"), the governing body should ensure that the organisation remunerates fairly, responsibly, and transparently to promote the achievement of strategic objectives and positive outcomes in the short, medium, and long term. One of the recommended practices under Principle 14 of King IV, requires the governing body who assumes responsibility for remuneration, mostly referred to as the Remuneration Committee, to set the direction for how remuneration should be addressed and approached on an organisation-wide basis, through the articulation of a remuneration policy. King IV recommends that the governing body should ensure that remuneration is used as an instrument to create value sustainably within the economic, social, and environmental contexts within which the organisation operates for the benefit of all stakeholders.

Furthermore, Principle 14, stipulates the minimum requirements of the remuneration policy and the implementation report to be voted on in the form of two non-binding resolutions. According to King IV, the remuneration policy should *inter alia* address the following[9]: what the consequences would be if more than 25% of votes cast on the policy and the implementation report are not in favour of these two non-binding resolutions. The policy should stipulate which measures the governing body commits to take if either of these resolutions does not achieve supporting votes of at least 75%.

In addition, Principle 14 recommends that when more than 25% of votes were cast against one of these two non-binding resolutions, the following be included in the remuneration policy, also disclosed in the background statement of the remuneration report:

- with whom the organisation engaged,
- the manner and form of engagement to ascertain the reasons for the dissenting votes; and
- the nature of steps taken to address legitimate and reasonable objections and concerns.

[6] AA1000 AccountAbility Stakeholder Engagement Standard (2015) https://www.accountability.org/standards/aa1000-stakeholder-engagement-standard
[7] https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/ZA_StakeholderEngagement_04042014.pdf
[8] https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/684B68A7-B768-465C-8214-E3A007F15A5A/IoDSA_King_IV_Report_-_WebVersion.pdf
[9] The IoDSA's Remuneration Committee Forum has previously published in-depth guidance on the requirements of remuneration policy: Paper 2 -The Remuneration Policy https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/57F28684-0FFA-4C46-9AD9-EBE3A3DFB101/Paper_2_The_Remuneration_Policy.docx.pdf

In June 2017, the JSE Limited amended its Listings Requirements by requiring issuers to, in the future, table their remuneration policies and remuneration reports annually to shareholders at the AGM for non-binding advisory votes (Paragraph 3.84 (k) of the JSE Listings Requirements).[10]

The Companies Act, 71 of 2008 ("Companies Act"), requires that the fees of non-executive directors of companies must be submitted to a special resolution approved by shareholders within the previous two years as is required by the Companies Act.

Although Principle 14 only refers to shareholders, the broader stakeholder group is not unimportant for the purposes of remuneration. Although it would be impractical for all stakeholders to express a view on the remuneration policy and the implementation report, one could argue that the intention of this requirement, in the context of the stakeholder inclusive model, would be for the governing body to be encouraged to have constructive dialogue between and amongst stakeholders and the governing body on matters of mutual interest, ensuring value creation for all.

Strengthening governance, culture, remuneration, and accountability is a collaborative effort by stakeholders, regulators, and the governing body. King IV encourages the debate on executive remuneration beyond the design of executive remuneration packages to include the justification of the link between remuneration, value creation, and key performance indicators within the social, economic and environmental context.[11]

King IV furthermore states that "directors owe their duties to the organisation and the organisation alone … the organisation is represented by several interests and these include the interests of shareholders, employees, consumers, the community, and the environment. Thus, requiring directors to act in good faith in the interest of the 'organisation' cannot nowadays mean other than a blend of these interests…". Despite the validity of this statement, organisations are faced with the following challenges in this context:

- understanding the needs and expectations of their various stakeholders;
- understanding how to address and satisfy the often-competing needs and expectations of different stakeholders (e.g. do we create more employee value or more customer value? Do we increase our profits or reduce our impact on the environment?).;
- how to satisfy these requirements in the short- and medium-term business plans; and
- understanding the link between the different forms of stakeholder value and the "interests of the organisation".

Linking ESG matters to remuneration is becomingly increasingly important for various stakeholders and the pressure is mounting on remuneration committees to disclose how this is done. Objective setting in incentive plans, is a useful catalyst to ensure the required focus on ESG related matters. How this is to be done, depends on every organisation, its value drivers, purpose statement and culture. The same attention and time spent on financial metrics, should be allocated to the setting of non-financial metrics, measuring progress, communicating targets and outcomes, and disclosing this information to stakeholders.

[10] JSE Listings requirements; www.jse.co.za
[11] King IV Remuneration Governance https://www2.deloitte.com/content/dam/Deloitte/za/Documents/governance-risk-compliance/za_Deloitte_KingIV_Remuneration_Governance_01032017.pdf

Stakeholder Apathy

Stakeholder apathy is also referred to as “silent or passive stakeholders”; it is the opposite of stakeholder activism. Stakeholder apathy can present in many forms; some examples are:

- Environmental and community groups not raising alarm bells when industrial organisations pollute rivers.
- Unions being silent on outrageous pay-outs to non-performing executives when employees are retrenched.
- Investors not voting against remuneration resolutions when there is a clear disconnect between the organisation’s performance, investor value created and executive incentive outcomes.
- Shareholders voting for remuneration policies where incentive plans only reward financial performance with no reference to ESG matters.
- Consumers buying products manufactured by organisations well known for unethical practices.
- Shareholders “blindly” following the recommendations posted by proxy advisor organisations without reading and understanding the rationale for such recommendations.
- Non-responsiveness to organisational calls for engagement.
- Shareholders not informing organisations whether they voted for or against a resolution.
- Not allocating qualified or knowledgeable analysts to remuneration matters.
- Not ensuring the recruitment and appointment of suitably qualified or experienced executives and non-executive directors.
- Etc.

It has been well covered in literature over the past few years that at the heart of it, many of the problems identified in many corporate failures, were because of governance, culture, and leadership lapses and blunders – which went past stakeholders without raising red flags about these matters. Admittingly, poor outcomes are often the product of many small decisions, rather than one major decision, making it harder to pinpoint when and where things went wrong and who should be held accountable. However, there is a clear need for organisations to enhance their approach to issues of governance, culture, remuneration, and accountability (“GCRA”) and for stakeholders to make it their business to understand what is going on in organisations.[12]

For purposes of this paper, the most prevalent stakeholders who could be accused of apathy are shareholders and institutional investors who invest funds on behalf of Pension and other Savings Funds and ordinary citizens. Although the norm for many institutional investors has been to become more active and even radical in their roles as shareholders (and there are numerous examples of these radical and active shareholders of listed organisations performing at shareholder meetings), there is still a view (and most recently raised by the JSE Ltd) that shareholders are still too apathetic. Indeed, shareholders have been accused of being 'asleep' which could have contributed to the financial services crisis in 2008 – 2009. Had there been closer scrutiny of management at the time, reward, and credit-granting practices, the global economic collapse could potentially have been prevented – this requires shareholders to fully embrace their Stewardship role. "The notion of "stewardship," in relation to institutional shareholders, can be "defined as the process through which [institutional] shareholders, directors, and others seek to

[12] https://aicd.organisationdirectors.com.au/membership/organisation-director-magazine/2020-back-editions/april/stakeholder-engagement-can-get-remuneration-back-on-track

influence organisations in the direction of long-term, sustainable performance that derives from contributing to human progress and the wellbeing of the environment and society"[13]

From a holistic perspective, stewardship expects shareholders to not only act in their own interest but also the interests of the organisation and all other stakeholders including society at large. Indeed, the point of an asymmetric relationship in terms of access of information between investors and the governing body must be made which often could lead to shareholders not being able to raise risks or concerns timeously if they have not had access to the required information.

The Code for Responsible Investing in South Africa ("the CRISA Code")[14], sets out in detail the responsibilities of institutional investors in South Africa.

There are many reasons why shareholders could be or (perceived to be as) apathetic *inter alia*:

- Not believing that a vote on a *non-binding* resolution will make any difference i.e. they may be voting if it was a binding resolution.
- Smaller or retain shareholders believing that *nothing will change* as a result of their vote.
- *Insufficient resources, capacity, or knowledge* to do a detailed review of financial statements and hold directors accountable.
- Shareholders believe that governing bodies *are appointed to oversee the management of organisations*, and they should get on with it and if not, be removed.
- General *lack of interest* in shareholder matters/engagements.
- *Asymmetry of information* to shareholders who do not have enough insight into organisation affairs, to enable them to conduct a reasonable evaluation.

In the meantime, the absence of the shareholder vote both at and outside the shareholder meetings leads to just more regulations being crafted worldwide.

There are however also shareholders who do take their roles as stewards very seriously, who do take the time to spend several hours labouring through financial statements, attending shareholder meetings, and casting their vote. One of the biggest problems that organisations however have, is that there is no requirement in South Africa, for shareholders to inform them, or to publicly state how they voted in respect of shareholder resolutions. In the absence thereof, organisations do not know how to reach out to these shareholders to start an effective debate.

It also needs to be stated though that there are scenarios where stakeholders have been very active, but they have been met with resistant members of governing bodies, and all their efforts have resulted in zero to little change – this could be a problem of management apathy rather than stakeholder apathy.

Effective engagement with stakeholders on the remuneration policy[15] - a proposed way forward

The stakeholder inclusive model, emphasised in King IV, calls for organisations to consider the legitimate expectations of all their stakeholders. Stakeholder inclusivity means that the board considers all

[13] Institutional Shareholders as Stewards: Toward a New Conception of Corporate Governance https://core.ac.uk/download/pdf/228596919.pdf
[14] https://cdn.ymaws.com/www.iodsa.co.za/resource/resmgr/crisa/crisa_19_july_2011.pdf

[15] Paper 2: The Remuneration Policy https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/57F28684-0FFA-4C46-9AD9-EBE3A3DFB101/Remuneration_Policy_December_2013_FINAL.pdf

stakeholders, and not only shareholders, as adding value to decision making in the best interest of the organisation, whilst considering holistic sustainability of the organisation. However, this is a balancing act: too much shareholder involvement will hinder effective governance whilst too little shareholder involvement will increase the risk of misunderstanding and surprises.

The trade-offs between the various stakeholders should be made on a case-by-case basis, to serve the best interests of the organisation and the stakeholders. Even when agreement cannot be reached, seriously considering an investor's view will help to gain support for its remuneration policy.

This, however, is easier said than done.

What is being done to address the needs of all stakeholder groups? For organisations that have not already identified their stakeholders, Burchman and Emanuel (2019)[16] suggest the following three steps:

- ***Identify key stakeholders and their interests:*** What do stakeholders need and expect so they give the organisation, in return, what it needs to create long-term value? What value proposition should be created for each?
- ***Resolve trade-offs:*** What are the organisation's highest priorities, and which stakeholders can support them? What will the organisation do, and what won't it do?
- ***Create accountability for achieving priorities:*** How do you focus and align the efforts of executives through goal setting and reward structures?

Clarity of roles may assist with the engagement process.

The governing body's primary governance role and responsibilities as defined in King IV[17] include:

- steering and setting the strategic direction with regard to the organisation's strategy and the way in which specific governance areas are to be approached, addressed and conducted;
- Approves policy and planning that give effect to the strategy and the set direction;
- Ensures accountability for organisational performance by means of, among others, reporting and disclosure; and
- Oversees and monitors implementation and execution by management (i.e. holds management accountable for operational performance).

Based on the strategy set by the governing body, *management* develops the strategy, formulates the policy and the operational plans which are approved by the governing body.

Shareholders own the organisation, and they appoint the directors who serve on the governing body (Board).

The responsibility of the *remuneration committee* is to ensure an effective remuneration policy is approved and implemented as developed and proposed by management. By implication, the remuneration committee is also responsible for defending an effective remuneration policy.

The responsibility of the *shareholder* is to hold governing bodies accountable to perform their duties as envisaged in the Companies Act and to have them removed from the governing body if they do not act in the best interests of the organisation and its stakeholders. The responsibility of the shareholder is to act

[16] https://corpgov.law.harvard.edu/2019/10/08/a-stakeholder-approach-and-executive-compensation/
October, 8, 2019

[17] The King IV Report on Corporate Governance for South Africa 2016

as a responsible investor and vote on the remuneration policy and other resolutions on an informed basis, at the AGM.

Effective engagement requires the participation of the governing body and the shareholder. In the context of remuneration, the shareholder must be willing to disclose their votes on resolutions and respond to organisation's invitations to engage. Governing bodies, on the other hand, must be open to engage with shareholders and be willing to hear their views – even though it would probably be impossible to meet the often-conflicting demands of all stakeholders simultaneously. This should also not be the goal – the aim should be to encourage constructive debate between the parties on matters of disagreement to ensure that all parties understand and respect each other's views.

The next section of this paper provides guidance for governing bodies and remuneration committees on how to effectively engage with stakeholders/shareholders on remuneration specifically and is included as guidance for these bodies to improve the quality of dialogue between organisations and their stakeholders.

THE NEED FOR ENGAGEMENT

Both globally and locally, remuneration is drawing more attention at AGMs than in the past. This is due to a combination of factors:

- Shareholders, often via asset managers, proxy or shareholder advisory firms or other intermediaries or agents, are expected to exercise their voice at the AGM with the introduction of the annual non-binding vote on the remuneration policy.
- The introduction of the CRISA Code, effective from 1 February 2012. Institutional shareholders have some responsibility for ensuring that an effective remuneration governance framework exists in the organisations they invest in. In this regard, proxy voting is an essential governance tool for investment professionals to act as good stewards of their clients' assets.
- Institutional investors are increasingly transparent on their voting decisions, and the reasons behind them.
- One of the five CRISA Code principles requires institutional investors to be transparent about their investment and corporate governance policies.
- Increasingly, institutional investors will not hesitate to withdraw their support for the remuneration policy if they see a problem or a lack of alignment between reward outcomes and performance against strategic objectives which should include ESG KPIs. It is therefore necessary to understand the rationale for their decisions. Asset managers inherently want to protect their clients' interests and the value of their investments and in this regard are becoming increasingly interested in the governance of remuneration – specifically as remuneration aligns to organisational performance. Asset managers want to understand the role of the governing body in overseeing management and they want to play a role in helping to develop and implement the policies that do this.
- Any dissent at the AGM on pay practices and policies is aired in the media more than ever before. Misunderstandings on remuneration and damage to reputation can be avoided by proactive engagement before the AGM.
- High-performing organisations are more advanced in building strong relationships with their stakeholders. Building stakeholder confidence, in general, is a key driver of competitive success, and this is built through engagement.

If more than 25% of votes cast are against the non-binding resolution on the remuneration policy and/or the implementation report, the governing body should record, in its remuneration policy, the steps taken to engage with shareholders on this matter. This engagement should provide for taking steps in good faith and with the best reasonable effort to achieve an engagement process to ascertain the reasons for the dissenting votes, and to appropriately address legitimate and reasonable objections and concerns raised, which may include amending the remuneration policy, clarifying, or adjusting remuneration governance and/or processes.[18]

In addition, in the following year's remuneration report, feedback of such engagements and the measures taken to address the legitimate concerns should be disclosed. The following section focuses on how to improve engagement with shareholders specifically about the remuneration policy and the implementation report.

PLANNING FOR SHAREHOLDER INVOLVEMENT

A remuneration report alone is not sufficient to effectively explain the remuneration policy and the effectiveness of its implementation to ensure shareholder support. Stakeholder relations should also not be confined to the AGM.

A strategy for engaging shareholders on the remuneration agenda throughout the year should be developed on the following guidelines:

- Aligned with the remuneration committee's work plan, an annual calendar should be developed outlining when and how many times to engage throughout the year with shareholders and, potentially, shareholder advisory bodies.
- A high level of support on the remuneration policy in the previous year is no guarantee of receiving high support again in the current year. Proxy advisory firms change their voting policies, for example, on the methodology for determining peer groups. This creates uncertainty and therefore requires proactive ongoing management throughout the year.
- The more changes being introduced to the remuneration policy, the earlier the engagement should take place relative to the AGM and the release of the remuneration report.

WHO

Know your stakeholders

KPMG has, on the basis of core principles set out in "The Stakeholder Voice in Board Decision Making" proposed useful questions for boards to consider:[19]

a) Has the board identified its key stakeholders?

b) Has the board determined which stakeholders they should engage with, as opposed to management?

c) When evaluating board effectiveness and the appointment of new directors, is the required stakeholder expertise present in the boardroom?

d) Is the training programme offered to directors adequate to address the variety of matters raised by stakeholders?

e) Are the board's decision-making processes adequate to give sufficient consideration to matters raised by key stakeholders and also the most adequate manner to provide stakeholders with feedback on matters raised?

Successful engagement is focused, without being exclusive. The remuneration committee should identify and prioritise which shareholders and advisors should be contacted. In cases where there are many shareholders, in the context of remuneration, the remuneration committee could focus on those that have

[18] King IV Recommended Practice 38

[19] KPMG stakeholder engagement 2018: www. assets.kpmg/content/dam/kpmg/uk/pdf/2018/07/stakeholder-engagement-10-questions.pdf

the largest shareholding and the most vocal shareholders on remuneration governance issues; however, engagement with shareholders should not be exclusively with the large shareholders or the most vocal ones. At the same time, the remuneration committee should be open to engaging with all shareholders. This will assist to ensure that a full range of perspectives on the remuneration issues are effectively considered. The management of stakeholder risk as an integral part of the organisation wide risk management process, is critical particularly when matters become contentious.

Allocate responsibilities

Has the governing body identified directors and if required, members of management, who could engage with investors and other relevant stakeholders on remuneration matters?

While most stakeholders are comfortable engaging with management, provided the message is conveyed to the governing body, they often prefer to involve the governing body or committee members or more importantly the remuneration committee chair, as management is inevitably conflicted. Involving committee members will also help build investor trust and confidence in the committee and governing body decisions. Therefore, typically, the remuneration committee chair should be capable of handling these shareholder engagements being supported by management.

HOW

Develop a process

Stakeholder dialogue should include a holistic approach where all matters on investor relations including organisational results, strategy, governance, and remuneration could be included. Alternatively, particularly if remuneration policy changes are needed, separate engagements could be arranged on remuneration only. The process for engagement should include how feedback is given to stakeholders post the engagement. This should be well set out in the comprehensive remuneration policy included in the remuneration report which could also be perceived as a way of reaching out to stakeholders in a 'passive' form of engagement.

WHAT

Develop the messages and materials to tell the right story in the right way. Key messages should focus on:

- Business strategy and stakeholder alignment;
- Links between remuneration outcomes, which will tend to focus more on variable pay, and medium to long term financial and non-financial performance;
- Areas where the remuneration committee has applied its discretion (up or down) and rationale for these decisions;
- Acknowledge any prior year issues and reasons why certain suggestions by stakeholders were not implemented; and
- The rationale for any policy changes in the current year and those proposed for the next year.

PRACTICAL CONSIDERATIONS

Consider the following:

- Allow stakeholders sufficient time to prepare, and if necessary, engage with the organisation before the AGM;
- Ensure that the remuneration committee's annual work plan and terms of reference are robust. The remuneration report should communicate how it followed the work plan and the terms of reference as this will make evident the nature and extent of the work done;

- Read the proxy voting guidelines of the asset managers and proxy advisors, which are now increasingly available on their websites;
- When dealing with asset managers, know that it is possible that one party deals with the proxy voting aspects and another with the engagement aspects. The party leading the engagement may not always be aware of how the votes are cast;
- Respond to stakeholder correspondence in a timely manner;
- Sharing targets, forecasts and other market-sensitive information likely to affect the price will need to be managed with care and within the parameters of the JSE Listings Requirements;
- Consider including in the annual remuneration report a summary of key concerns raised by stakeholders in the past year and the remuneration committee's response to addressing these. This would include a response to the voting outcomes of the prior year; setting out any changes made to the remuneration framework and the rationale for their decisions made; and
- Just as significant effort is required to explain the rationale for the remuneration approach to external stakeholders, the same is required for internal stakeholders, primarily the organisation's employees. The effectiveness of incentive plans and their internal credibility depend on participants' understanding, supporting, and valuing of the incentive schemes and knowing what is required of them to deliver suitable pay-outs.

"Investors have a distinct role in relation to executive remuneration. Investors have a fiduciary responsibility as well as a strong economic interest in remuneration. No aspect of corporate governance touches as many drivers in terms of performance, risk, and incentive, or is ultimately more critical to the long-term alignment of interests. However, investors are not, typically, insiders and in almost all cases are not in a position to dictate executive remuneration practices." [20]

Acknowledgment

This Guidance Paper was drafted with the assistance of subject matter experts serving on the King Committee's Subcommittee on Remuneration and the IoDSA Remuneration Committee Forum.

[20] ICGN Guidance on Executive Remuneration, 2012; https://www.icgn.org/sites/default/files/ICGN_Exec_Rem_Guidance_2012.pdf