Spotlight on director-investor engagement

Board perspectives

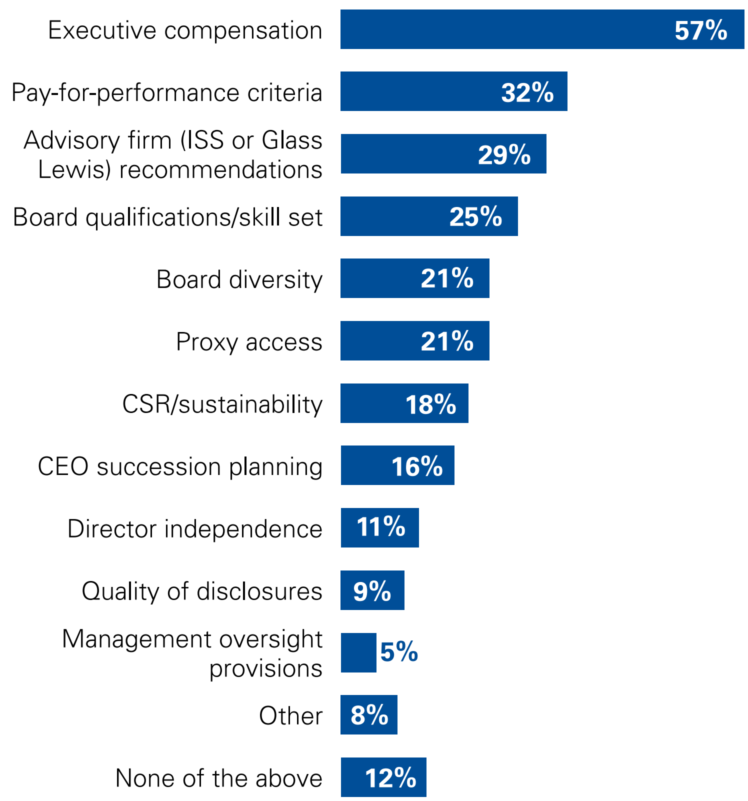
In the current environment, the question that corporate boards should be asking with respect to shareholder engagement is no longer if, but how. Engagement with the company's significant shareholders is becoming the new normal, rather than the exception. Given heightened investor expectations for transparency in governance and oversight, having a well-executed plan for communicating the company's story and gauging investor sentiment on key issues is critical. It is also increasingly important that the entire board knows what that plan is and what role the directors may play.

"When things go wrong, investors get one vote, and that's on directors," said Stephen Brown, Senior Advisor, KPMG Board Leadership Center. Brown and Lopa Zielinski, currently deputy corporate secretary at HSBC in North America, both former governance leaders for a major institutional investor, joined Faye Wattleton, managing director at Alvarez & Marsal and director on several public and private company boards, for a panel discussion on communications between shareholders and boards. The discussion, moderated by Susan Angele, also a senior advisor with the KPMG Board Leadership Center, took place during the WomenCorporateDirectors 2017 Global Institute in New York in May.

The panel discussed the corporate governance issues most often raised by institutional investors, offered examples of engagement scenarios that boards could face, and provided tips for engagement.

Notably, activist hedge funds are not the only investor demographic driving the need for engagement. "[More traditional institutional investors] are becoming much more active, whether it's on board composition issues, company performance, or social responsibility issues, they are all over it, and they're starting to use their votes more and more to drive the change that they want to see," said Angele. These investors include state and local pension funds, not-for-profit foundations, and university endowments.

Corporate governance issues most often raised by investment professionals



Source: Rivel Research Group, Corporate Secretary Flashpoint: Institutional Investor Engagement, March 2016

Data from Rivel Research Group ranked executive compensation, pay-for-performance criteria, advisory firm recommendations, board qualifications and skills, board diversity, proxy access and corporate social responsibility/sustainability as the issues raised most often by institutional investors.

According to Brown, investors have three main factors on which to evaluate companies and directors: price, personnel, and processes. "Information on the first two is easy to get, but on board processes, investors have very limited information. If your company has good processes, it's important to explain it to investors to help to demonstrate board competence."

Wattleton added, "Investors want to know that there is rigor in the [board's] process—not only on why you got there, but how you got there."

Zielinski emphasized that investors are not interested in a repetition of the company's public disclosure. "They're looking for companies to articulate the underlying philosophies behind your story," she said. "How does this support your strategy? How is this going to be sustainable? They want a deeper conversation."

Four key takeaways emerged from the discussion:

1. Engagement is the new normal. To understand how directors are carrying out their fiduciary duties, investors want and expect to hear from board members. While there is no one "right" way to engage, there are plenty of poor ways to do it—such as not preparing or waiting until a crisis erupts.

2. Know the plan. Directors should ask management for details of the company's engagement plan as well as the role they may play. What issues will the company engage with investors on, who will be involved, and when will engagement occur?

3. Execution is key. Substance and style matter. The board should understand the depth of the company's investor relations capabilities as well any third-party resources available. Does the company have the appropriate chain of command and protocols in place to ensure that the board receives the critical engagement information it needs? Mock engagement exercises may be useful.

4. Understand investor concerns. Investors' governance policies and concerns may vary widely. The board and management should be informed on the governance concerns and views of the company's most significant shareholders and should be prepared to discuss the company's position on those issues and the rationale behind it. It is important to gauge the sentiment of the company's largest investors ahead of governance changes, particularly on issues that shareholders have expressed concerns about. Shareholder proposals serve as a bellwether of the issues that investors are focused on, even when they do not receive majority shareholder support. The board should understand the implications of opposing proposals from large or influential shareholders.

About the KPMG Board Leadership Center

The KPMG Board Leadership Center champions outstanding governance to help drive long-term corporate value and enhance investor confidence. Through an array of programs and perspectives—including KPMG's Audit Committee Institute, the WomenCorporateDirectors Foundation, and more—the Center engages with directors and business leaders to help articulate their challenges and promote continuous improvement of public- and private-company governance. Drawing on insights from KPMG professionals and governance experts worldwide, the Center delivers practical thought leadership—on risk and strategy, talent and technology, globalization and compliance, financial reporting and audit quality, and more—all through a board lens. Learn more at kpmg.com/blc.

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