



## **Corporate Governance in Switzerland**

-

**Who decides, who takes responsibility?**

**SWIPRA Corporate Governance Survey 2018**

Zurich, November 7, 2018



## SWIPRA Corporate Governance Survey 2018

- 6<sup>th</sup> SWIPRA Corporate Governance Survey
  - SPI® companies representing approx. 77% of total index market cap
  - Swiss and international institutional investors, representing approx. EUR 17.3tn assets under management or approx. 26% of global equity investments
- Survey covers developments in governance in the Swiss market and includes views on current topics
- Scientifically-founded market analysis of investors' and corporate issuers' views over 6 years
- In cooperation with researchers at the DBF (UZH)



# SWIPRA Corporate Governance Survey

## Key findings of the past



- |      |   |
|------|---|
| 2013 | Status quo and perspectives of corporate governance in Switzerland  |
| 2014 | After the Ordinance against Excessive Compensation  |
| 2015 | Market discipline and regulation  |
| 2016 | Corporate governance between globalization, shareholder activism and proxy advisors                       |
| 2017 | Governance Activism – The increasing importance of corporate governance in fund managers' decision making |
| 2018 | Who decides, who takes responsibility?  |



## SWIPRA Corporate Governance Survey 2018

➤ Special thanks to our partners

Georgeson



lemongrass communications

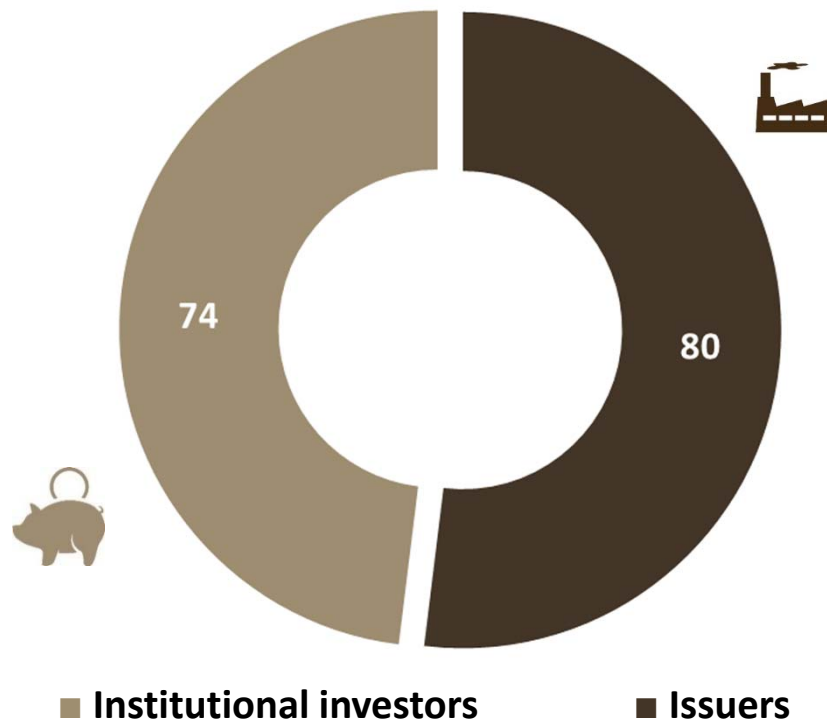
**FINANZ** und  
**WIRTSCHAFT**





# SWIPRA Corporate Governance Survey 2018

## Participants



Issuers: 80

Asset and Fund Managers: 44

Pension Funds: 30

#CH / Non-CH: ca.  $\frac{2}{3}$  :  $\frac{1}{3}$

A total of 154 participants filled out the survey, representing more than 77% of the SPI market cap and 26% of global equity AuM.



## Plan for this presentation

- Key results
- Proxy advisors: changing role
- Engagements: further gaining importance
- Board independence: the holy grail for investors
- Board succession and director selection: diverging views
- Corporate social responsibility: room for improvement
- Remuneration: challenge to link goals, culture and incentives
- Summary and outlook



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## Key results (I/III)

### ➤ **Proxy advisors: changing role**

- Issuers and investors have diverging views regarding proxy advisors' diligence
- Proxy advisors' role is changing, from voting advice to standardized data
- Investors' own analyses reduce direct impact of proxy advisors on AGM outcomes (SWIPRA AGM Analysis 2018)

### ➤ **Engagements: further gaining importance**

- Engagements create value through better mutual understanding between board of directors and investors
- Higher duty of care standards for investors and a more differentiated view on governance continue to increase the importance of engagements
- Engagements complement standard disclosure and ensure governance-related decisions can be taken diligently by investors and issuers





## Key results (II/III)

- **Board independence: the holy grail for investors**
  - A functioning governance framework requires an independent board
  - Independence is a prerequisite to gain investors' confidence in the board's work
  - Investors view independence criteria as most critical when assessing proposed board members in AGM elections
  
- **Board succession and director selection: diverging views**
  - Succession planning necessity for issuers' stable long-term development
  - Little information on succession planning and differing views on director selection criteria further increase investors' focus on board elections
  - Board succession and director selection generally seen as the chairman's responsibility, but shareholders increasingly influence this decision



## Key results (III/III)

- **Corporate social responsibility: room for improvement**
  - Shareholders want companies to live up to higher CSR standards
  - CSR and related disclosure of Swiss-listed companies generally viewed critically
  - Demand for broader reflection of CSR targets in compensation systems
  
- **Remuneration: challenge to link goals, culture and incentives**
  - Diverging views between issuers and investors on how to reward qualitative performance (non-financial) goals
  - Besides quantitative targets, qualitative performance metrics are considered as impactful in achieving long-term strategic goals
  - Limited disclosure on qualitative metrics by issuers impair their suitability as performance metric



## Plan for this presentation

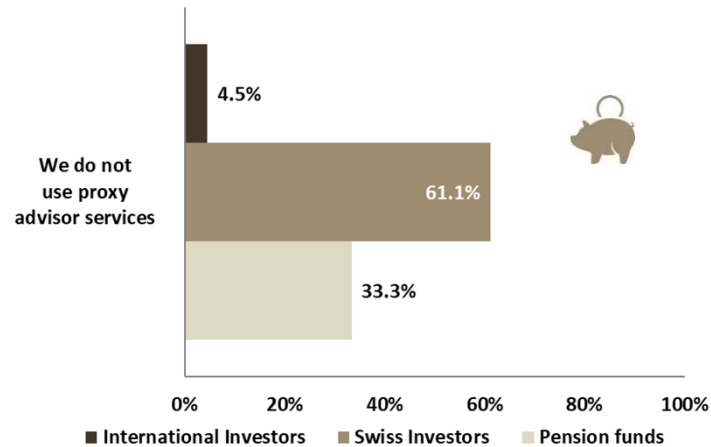
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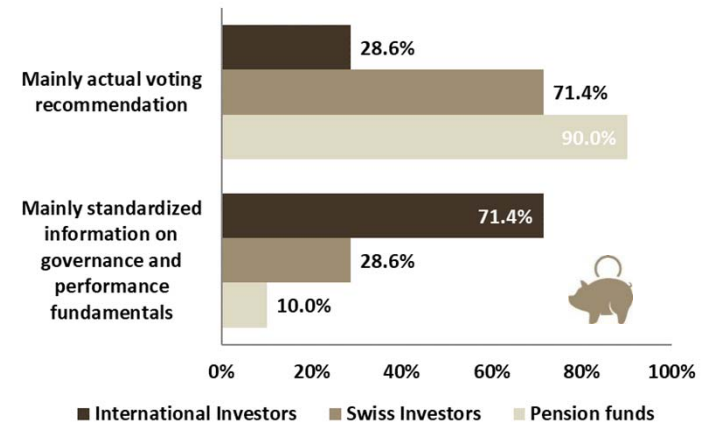
## Proxy advisors (I)

### Use of proxy advisor services

**Investors using proxy advisor services**  
Survey 2018



**Requested proxy advisor services**  
Survey 2018



- Swiss investors and pension funds less likely than international investors to purchase proxy advisor services, mainly interested in actual voting recommendations
- 71.4% of international investors use proxy advisor data mainly for comparability of governance frameworks across issuers (as basis for own analysis)
- Individual analysis allows investors to set own priorities when taking voting decisions

Question: For your organization, what is the main purpose for purchasing services of proxy advisors?  
[left] Fraction not using services; [right] Services requested by those working with proxy advisors

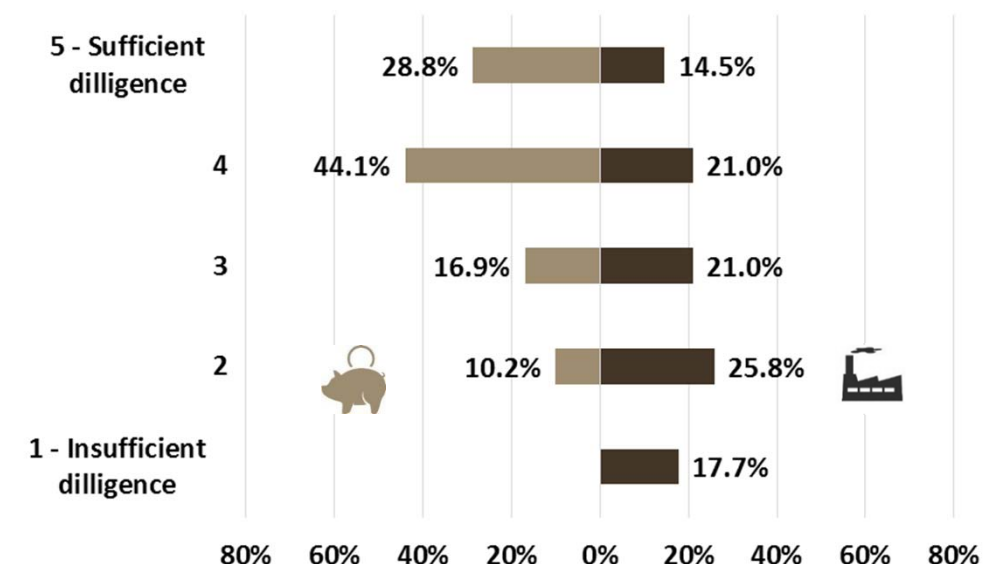


## Proxy advisors (II)

### Diligence in data analysis

#### Proxy advisors' diligence in developing voting recommendations

Survey 2018



	Pension funds	CH asset managers	Int. asset managers
5 - Sufficient diligence	52.0%	14.3%	10.0%
4	28.0%	42.9%	65.0%
3	16.0%	28.6%	10.0%
2	4.0%	14.3%	15.0%
1 - Insufficient diligence	0.0%	0.0%	0.0%

- 35.5% of the issuers believe that proxy advisors are diligent enough when assessing information
- 72.9% of the investors state that proxy advisors are diligent enough in their analysis
- Investors trust proxy advisors, but increasingly deviate from their recommendations

Question: Do proxy advisors exercise sufficient diligence in evaluating company information when deriving proxy voting recommendations?



## Implications: Proxy advisors

- The work of proxy advisors is controversial: they are an essential player in the stewardship process, but their role and level of impact are changing
- In the SWIPRA Survey 2015, 60% of the investors and 57% of the issuers stated that proxy advisors' direct impact on AGM voting outcomes increased as a result of the Ordinance against Excessive Compensation
- The SWIPRA Survey 2018 now reveals that large investors are relying less on proxy advisors' voting recommendations, but rather conduct their own proxy analysis

**What is the future role of proxy advisors in stewardship?**



## Plan for this presentation

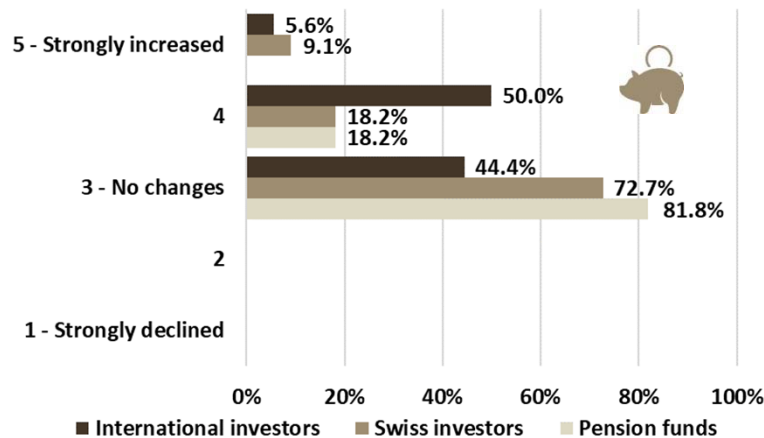
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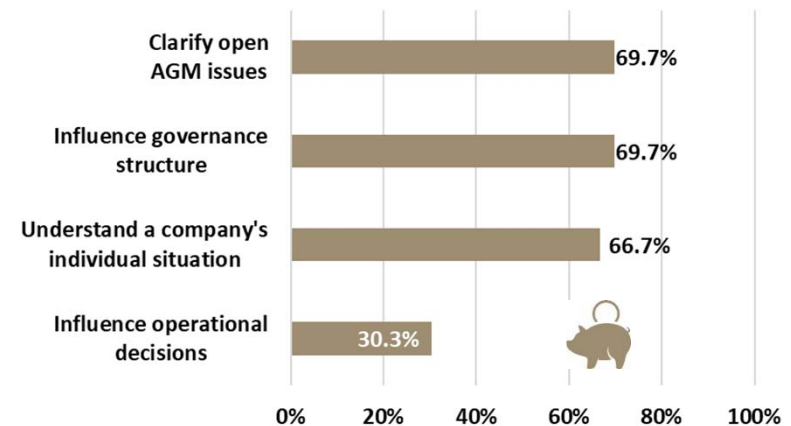
## Engagements (I)

Increasing importance

### Number of engagements with portfolio companies Survey 2017



### Purpose of engagements Survey 2017 (Investors (strongly) agreeing)



- The SWIPRA Survey 2015 already indicated engagements to become more important as a result of additional shareholder rights (OaEC)
- In the SWIPRA Survey 2017, 55.6% of the international investors stated that the number of meetings with Swiss-listed issuers had increased compared to previous years
- Investors use engagements to better understand their portfolio companies' individual governance frameworks

Questions: [left] How have the engagements (direct interaction) with your portfolio companies developed compared to the previous years?; [right] If you engage with companies, what role do you see in this direct interaction?

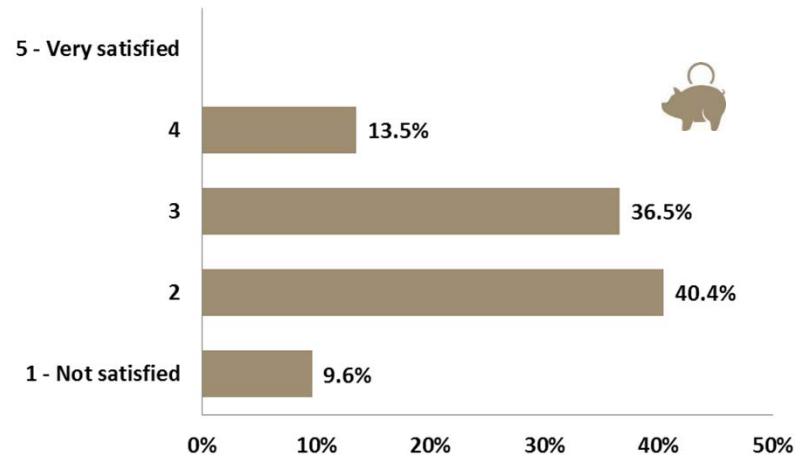




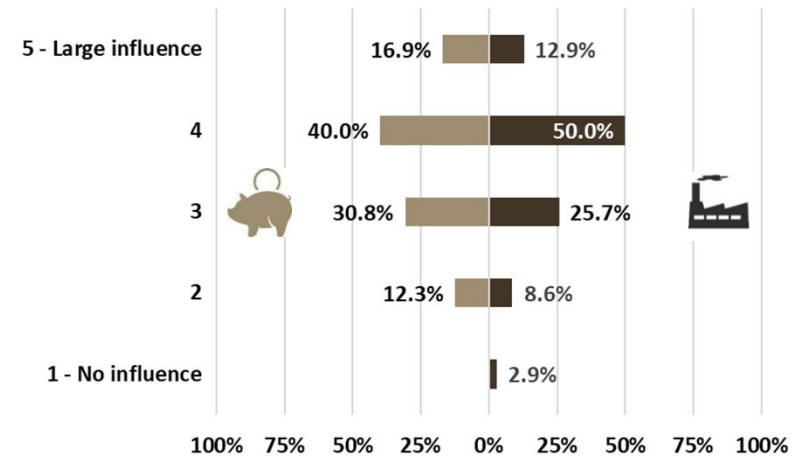
## Engagements (II)

### Complementing disclosure

#### Satisfaction with pay for performance disclosure Survey 2018



#### Spill-over of standards and regulation Survey 2018



- Survey shows that key engagement topic during the AGM season 2018 was compensation
- 50.0% of the investors were not satisfied with the information provided by issuers on pay for performance, up from 40.0% in 2017
- 56.9% of the investors and 62.9% of the issuers believe developments in governance standards abroad, e.g., SRD II, will have a (large) influence on Swiss-listed issuers

Questions: [left] How satisfied were you with the information provided on the comparison of achieved performance targets and the payout of variable compensation elements (pay for performance) during the AGM season 2018 in Switzerland? [right] How do you assess the influence of international governance standards, in particular from the EU, the UK and the US, on the assessment of the general meeting agenda items of Swiss-listed companies?

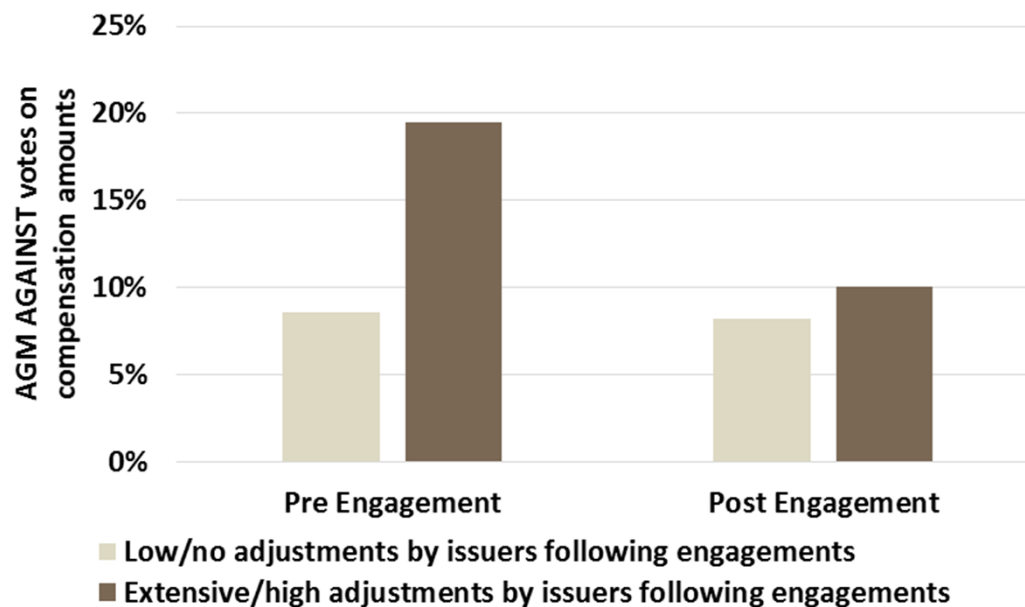


## Engagements (III)

### Benefits of engagements

#### Impact of engagements on voting outcome

SWIPRA Survey 2017



- In the SWIPRA Survey 2017, 61.9% of the issuers stated that engagements generally increase investors' support at AGMs
- Issuers engaging with investors and making adjustments thereafter were able to reduce AGAINST votes on compensation amounts to almost half

The graph is based on a question in the corporate governance survey 2017 that asked issuers whether they made adjustments following engagements and what the key topic of their engagements was. The graph compares the AGM outcomes in 2016 (pre) to 2017 (post) for identifiable companies participating in the survey and which indicated that compensation amounts were the key engagements topic. The light/dark brown bars sort these companies according to whether or not they made adjustments following engagements in the year prior to the AGM 2017.



## Implications: Engagements

- Engagements complement issuers' regular disclosures and are especially helpful to clarify non-standardized, company-specific items, particularly compensation
- Shareholders continue to base their voting decisions on the data or the recommendations provided by proxy advisors if issuers are not engaging (in line with findings of the SWIPRA Survey 2017)
- Investors' sustained discontent with compensation-related disclosure, combined with disclosure standards spilling over from abroad, will further increase the importance of engagements

**Is there diligent governance without engagements?**



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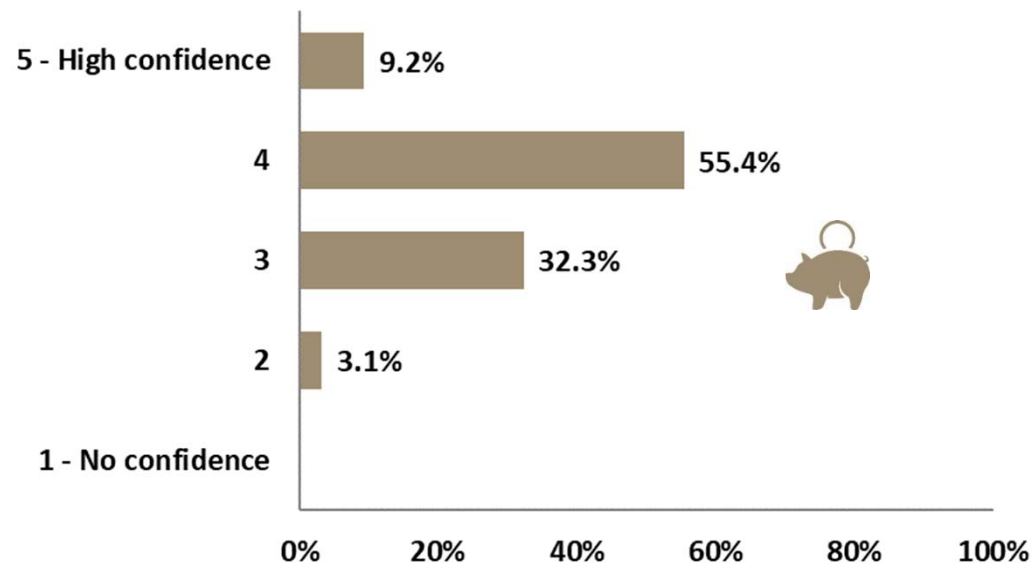


# Board independence (I)

## Confidence

### Confidence in boards of Swiss-listed companies

Survey 2018



- Engagements help issuers to build trust and confidence with investors
- 64.6% of the investors have (high) confidence in the boards of Swiss companies
- This is consistent with overall high approval rates in AGM board elections

	Pension funds	CH asset managers	Int. asset managers
5 - High confidence	13.3%	11.1%	0.0%
4	63.3%	44.4%	52.9%
3	20.0%	44.4%	41.2%
2	3.3%	0.0%	5.9%
1 - No confidence	0.0%	0.0%	0.0%

Question: Do you generally have confidence in the work of the board of directors in Switzerland?

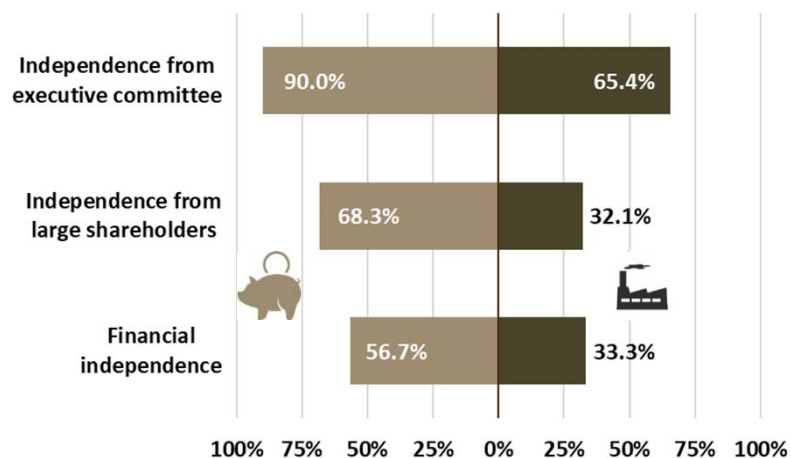


## Board independence (II)

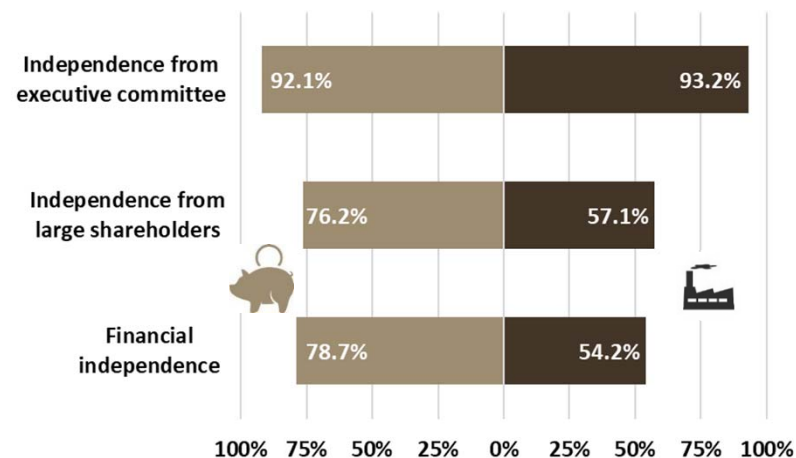
### Importance of independence criteria

#### Assessing board candidates independence – Items considered (very) relevant

Survey 2016



Survey 2018



- Investors confidence in the board is linked to perception of the board's independence
- Significant increase of issuers considering board's independence (very) relevant:
  - From 65.4% in 2016 to 93.3% 2018 for independence from executive committee
  - From 32.1% to 57.1% in 2018 for independence from large shareholder(s)
- Investors consider a director's financial independence more relevant than two years ago

Questions: [investors] Please indicate the relevance of the following factors in evaluating a proposed candidate for the board of directors in a company listed in Switzerland;  
[issuers] Please indicate the relevance of the following factors for selecting a candidate for the board of directors of your company.

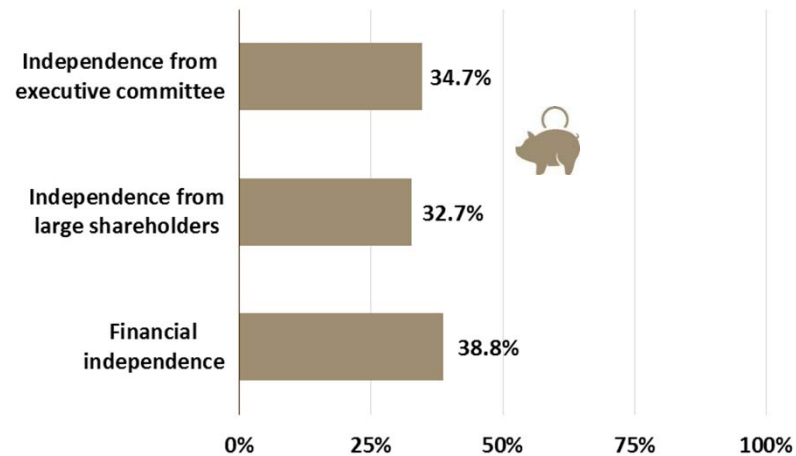


## Board independence (III)

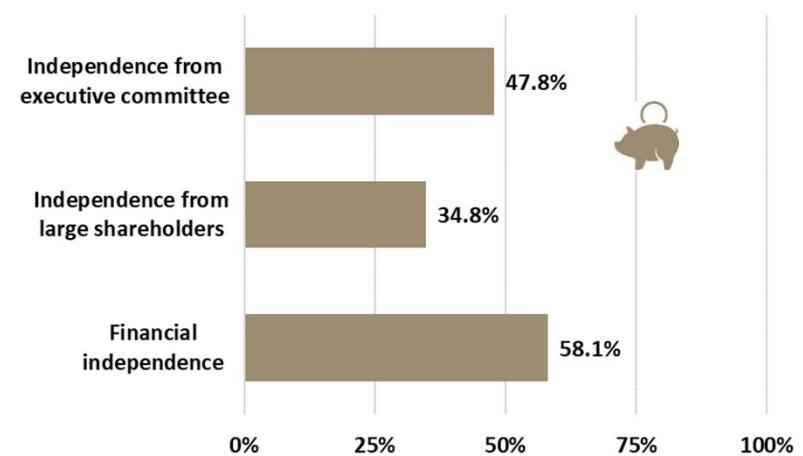
Disclosure regarding independence criteria

### Quality of disclosure on board candidates – Items considered not/little satisfied

Survey 2016



Survey 2018



- Fraction of investors not or little satisfied with disclosure related to individual board members' independence from the executive committee increased from 34.7% in 2016 to 47.8% in 2018
- Similarly, fraction of investors not or little satisfied with disclosure of individual board members' financial independence increased from 38.8% in 2016 to 58.1% in 2018

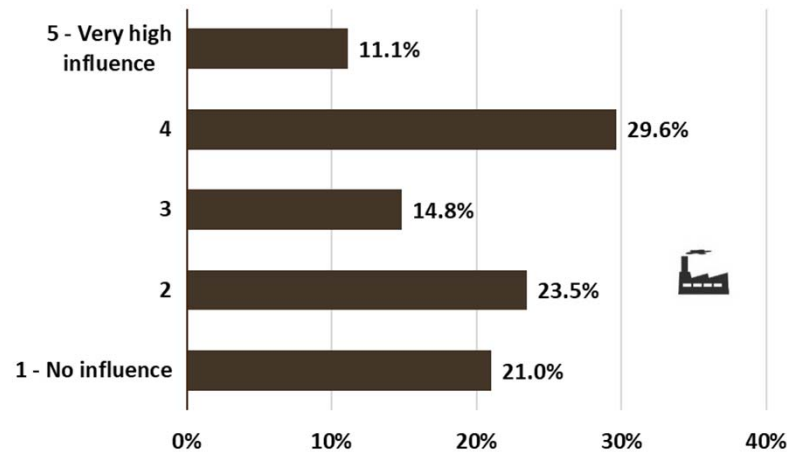
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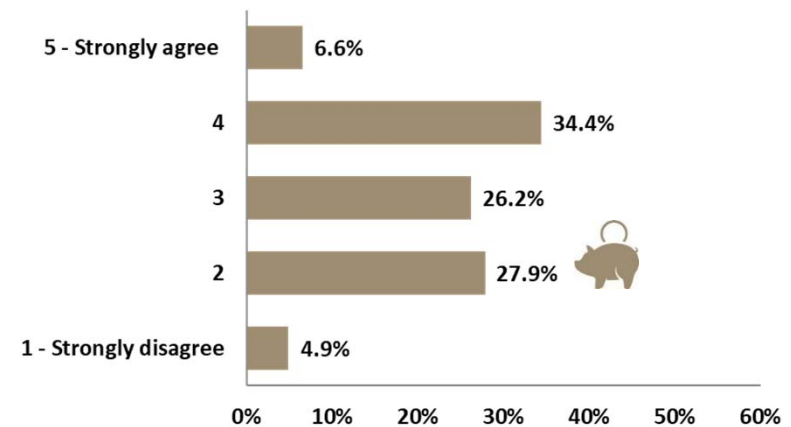
## Board independence (IV)

### Large shareholder independence

**Impact of shareholder structure on board decisions**  
Survey 2016



**Worse disclosure in large shareholder companies**  
Survey 2018



- Large investors may impact the governance of a company in several ways
- 44.5% of the issuers in the SWIPRA Survey 2016 stated that shareholder structure has no or little influence on decision making process of the board
- 41% of the investors consider disclosure quality lower in companies with a large shareholder

Questions: [left] What influence does the shareholder structure (e.g., existence of a large shareholder) have in the decision making process of the board of directors of your company?; [right] How do you assess the following statement: "Companies with one or more large shareholder(s) (blockholder/s) generally have a less meaningful disclosure than companies without anchor shareholders" ?



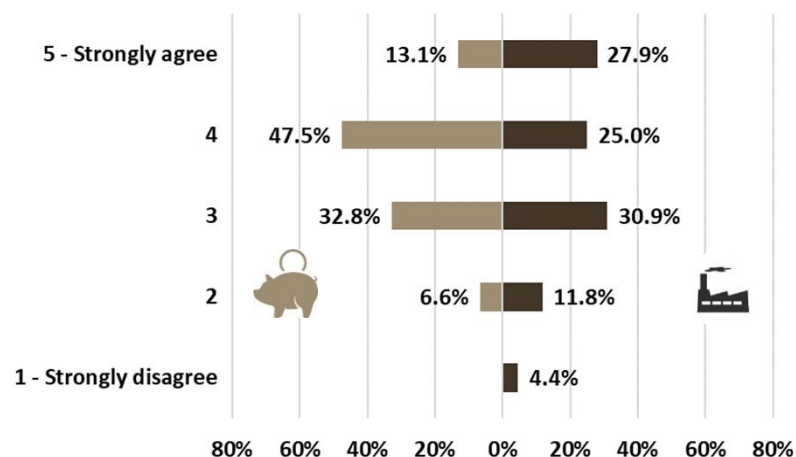


# Board independence (V)

## Advantages and concerns of full-time chairmen

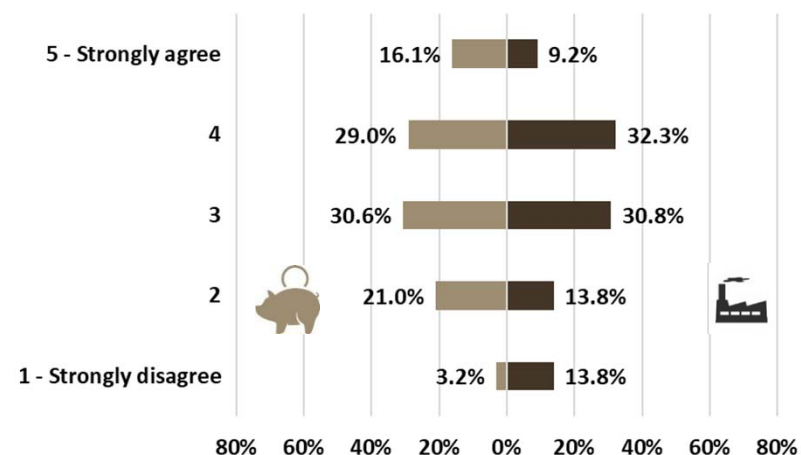
### Stronger monitoring by full-time chair

Survey 2018



### Less independence of full-time chair

Survey 2018



- Workload of the board of directors and particularly its chairman increased
- 61.6% of investors and 52.9% of issuers believe full-time chairmen are better monitors and 45.1% of all investors (69.6% of Swiss investors) and 54.4% of issuers believe full-time chairmen have better capabilities to take strategic decisions
- 45.1% of investors and 41.5% of issuers believe that full-time chairmen are less independent

Questions: How do you generally assess a full-time chairman of the board of directors? [left] Full-time chairmen of the board of directors can generally better monitor the work of the executive committee; [right] Full-time chairmen of the board of directors are generally less independent.

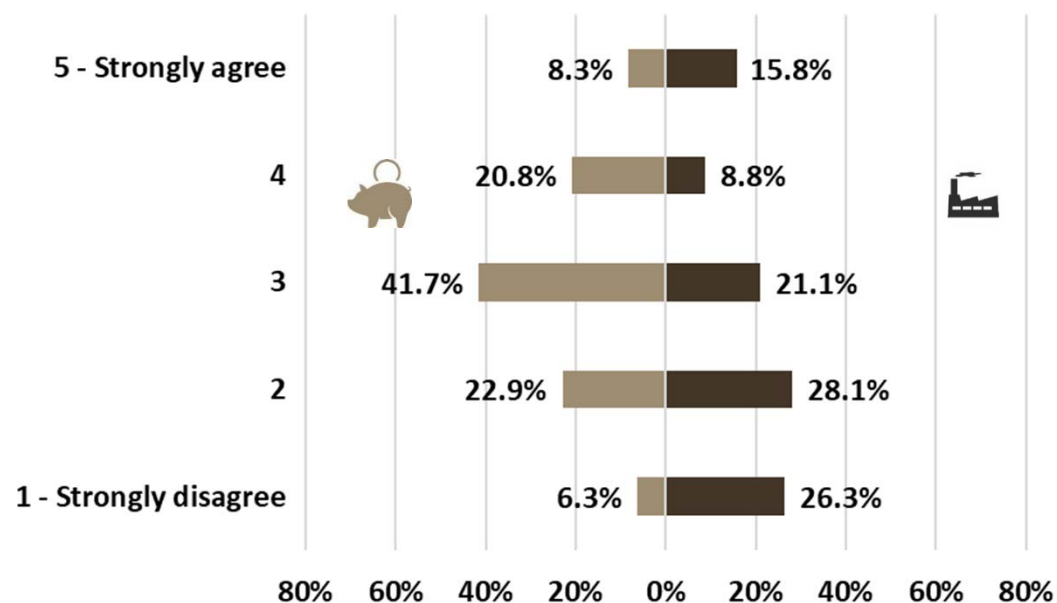


## Board independence (VI)

Concerns regarding full-time chairmen

### Support of full-time chairmen

Survey 2018



- Only 29.1% of investors and 24.6% of issuers generally support full-time chairmen mandates
- Benefits of a full-time chairman, better monitoring and decision making, seem not to outweigh “costs” of perceived lower board independence

Question: How do you generally assess a full-time chairman of the board of directors? - We generally support full-time chairman mandates



## Implications: Board independence

- Boards of Swiss-listed companies enjoy a high level of confidence
- Shareholders closely link confidence in a board with the perception of a board's independence
- Importance of a board's independence from management and the company's large shareholder(s) has attracted broad attention amongst issuers only recently
- Issuers and investors alike consider a chairman's general independence more important than the potential benefits of a full-time mandate

**Can board members be expected to take full responsibility of a company's development, but not be involved too closely with it?**



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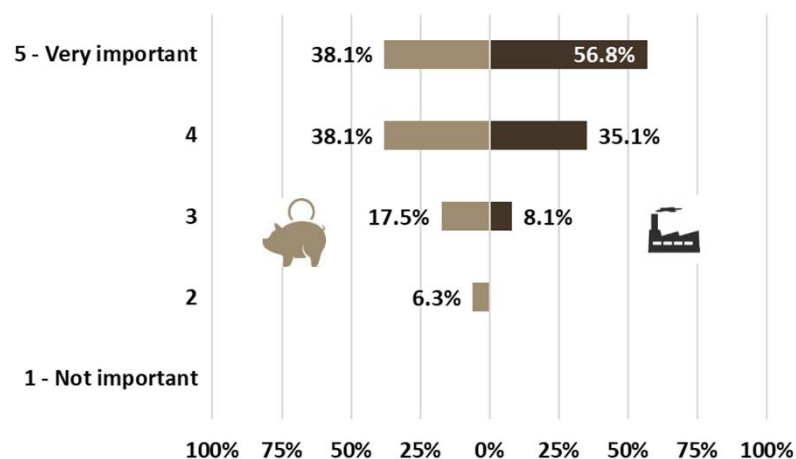


# Board succession and director selection (I)

## Succession planning

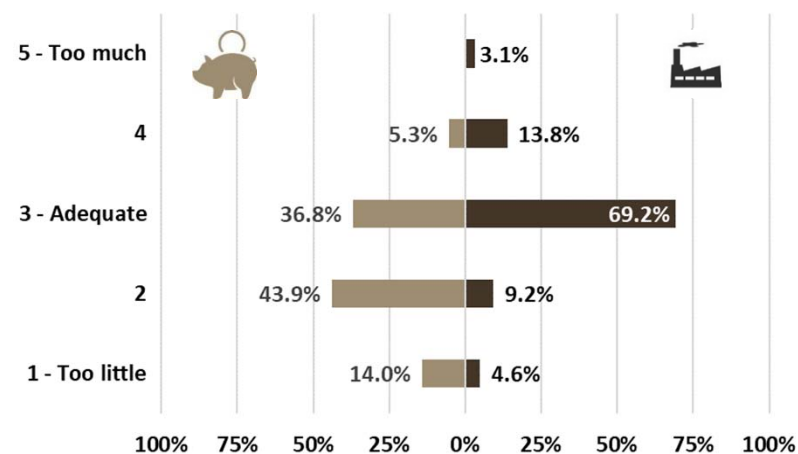
### Importance of succession planning

Survey 2018



### Adequacy of disclosure on succession planning

Survey 2018



- In the SWIPRA Surveys 2015 and 2016, board elections were considered key value drivers for a company's long-term value creation
- 76.2% of investors and 91.9% of issuers consider succession planning (very) important
- Clear gap in perception: 69.2% of issuers consider information on succession as adequate, whereas 57.9% of investors consider it insufficient

Questions: [left ] How important is succession planning in the following bodies of a company? – Board of directors; [right] How do you generally assess the disclosure on succession planning in the following bodies of a company? – Board of directors

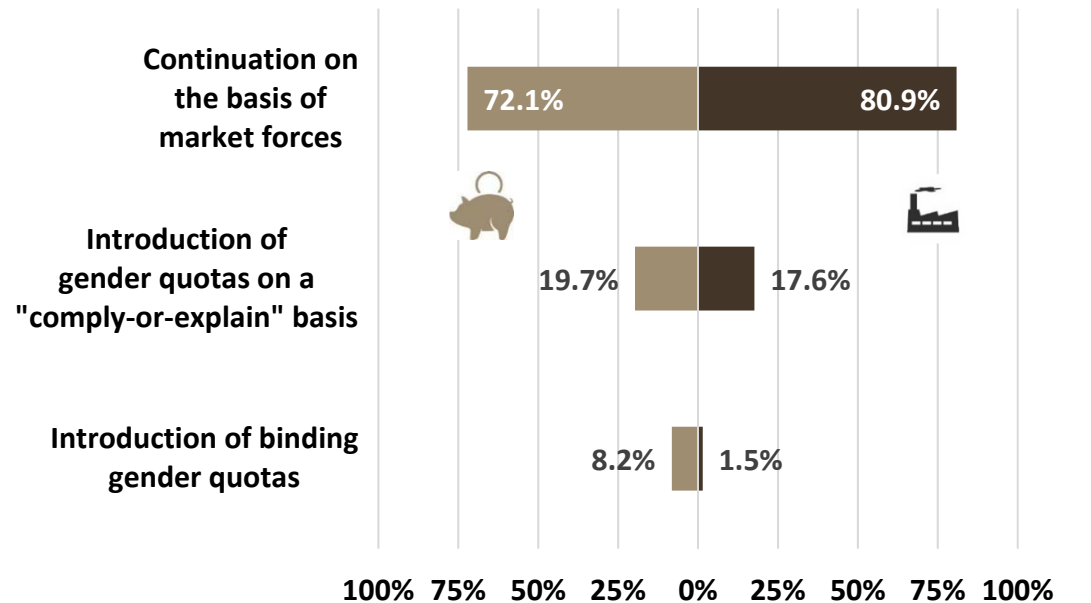


# Board succession and director selection (II)

## Personal diversity and regulation

### Policy on gender representation

Survey 2018



- Difference between investor preferences for personal diversity on boards is also reflected in considerations of regulatory approaches
- 40% of international investors prefer some kind of board gender quota, only 24% of Swiss investors agree
- Vast majority of market participants continues to be against a gender quota

	Pension funds	CH asset managers	Int. asset managers
Continuation of the current development on the basis of market forces	78.6%	72.2%	60.0%
Introduction of gender quotas on a "comply-or-explain" basis	17.9%	22.2%	20.0%
Introduction of binding gender quotas	3.6%	5.6%	20.0%

Question: In your opinion, how should the gender representation issue in board of directors be approached going forward?

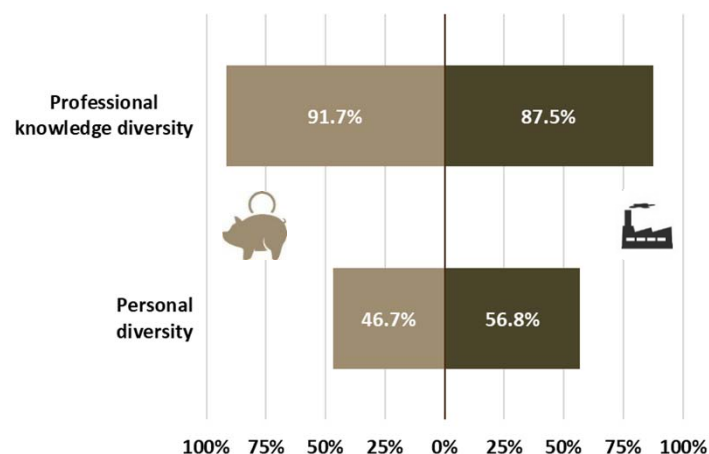


# Board succession and director selection (III)

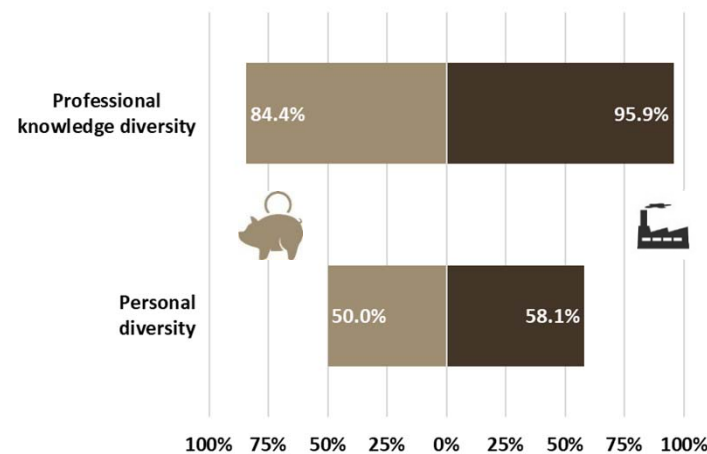
## Diversity as selection criterion

### Assessing board candidates – what is relevant? - Items considered (very) relevant

Survey 2016



Survey 2018



- Share of investors considering knowledge diversity (very) relevant decreased from 91.7% in 2016 to 84.4% and increased for issuers from 87.5% to 95.9%
- Personal diversity (e.g., origin, gender, age, ethnos, etc.) overall unchanged, but relevant to 77.7% of international investors (68.8% in 2016), compared to 27.8% of Swiss asset managers (38.6% in 2016)

2018	Pension funds	CH asset managers	Int. asset managers
5 - Very relevant	21.4%	11.1%	33.3%
4	25.0%	16.7%	44.4%
3	21.4%	55.6%	16.7%
2	21.4%	11.1%	5.6%
1 - Not relevant	10.7%	5.6%	0.0%

Question: Please indicate the relevance of the following factors in evaluating a proposed candidate for the board of directors of a Swiss-listed company.

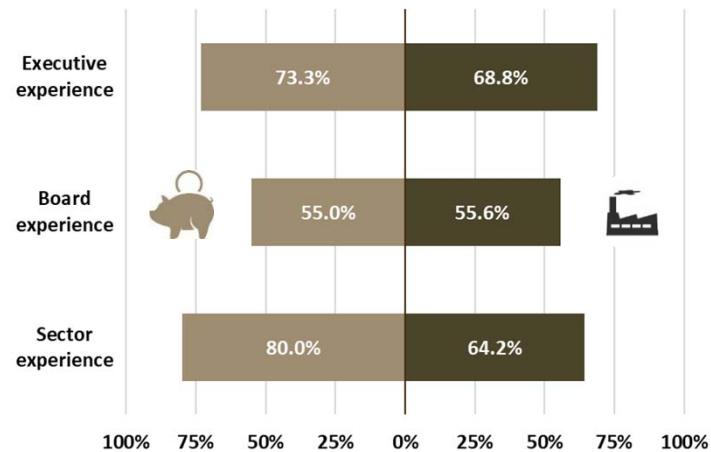


# Board succession and director selection (IV)

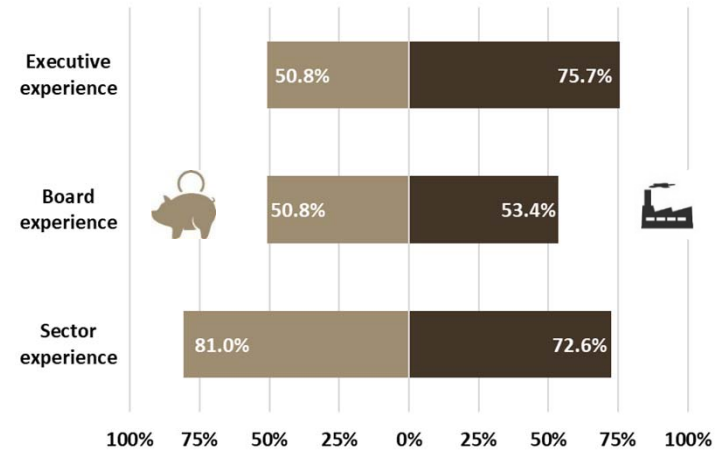
## Experience as selection criterion

### Assessing board candidates – what is relevant? - Items considered (very) relevant

Survey 2016



Survey 2018



- 50.8% of investors consider executive experience (very) relevant (down from 73.3% in 2016), compared to 75.7% of issuers (up from 68.8% in 2016)
- Board experience is considered (very) relevant by 53.4% of issuers and 50.8% of investors overall, though less than 25% of international investors share this opinion
- 81.0% of investors perceive professional industry experience (very) relevant, assigning it a relatively higher priority than board or executive experience

Question: Please indicate the relevance of the following factors in evaluating a proposed candidate for the board of directors of a Swiss-listed company.





## Implications: Board succession and selection

- Understanding board composition and succession planning is highly relevant for shareholders to better appreciate the development and long-term value creation of their investee companies
- Issuers' disclosure on succession planning and director selection generally limited, but would be important to bridge gap in understanding between investors and issuers
- Investors pressure towards more diversity on boards of Swiss-listed issuers has increased (SWIPRA AGM Analysis 2018) and is mainly driven by large international investors

**How should a chairman solicit views of shareholders  
on board succession and director selection?**



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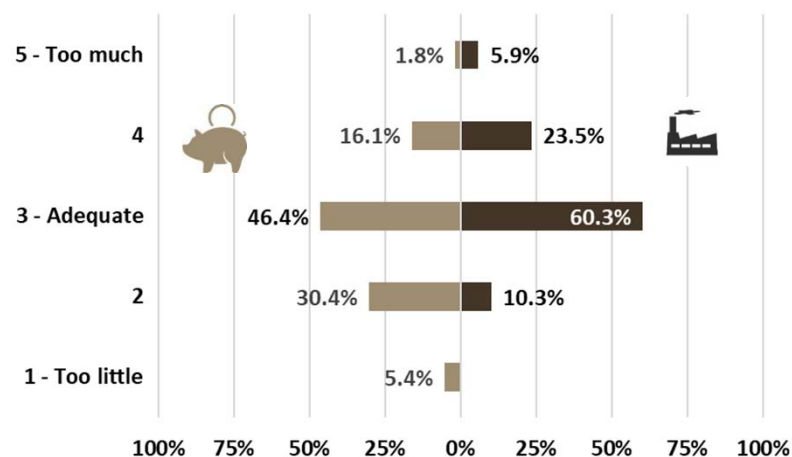


# Corporate social responsibility (I)

Accountability for CSR

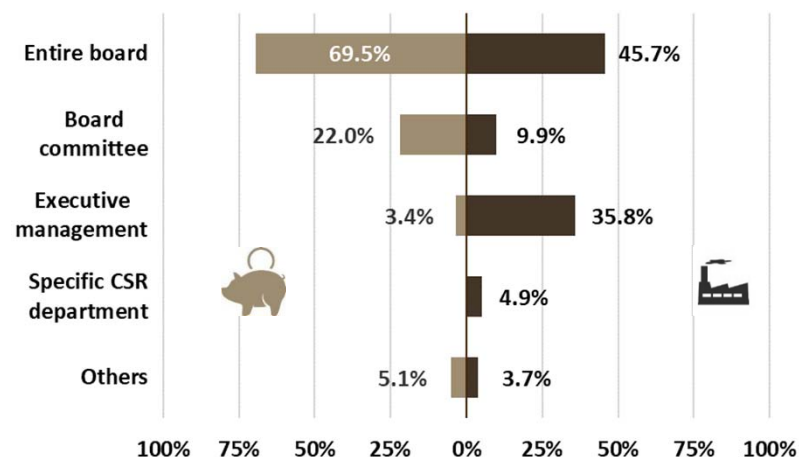
## CSR in Swiss-listed companies

Survey 2018



## CSR responsibility within the company

Survey 2016



	Pension funds	CH asset managers	Int. asset managers
5 - Too much	0.0%	5.9%	0.0%
4	16.7%	17.6%	13.3%
3 - Adequate	50.0%	52.9%	33.3%
2	25.0%	17.6%	53.3%
1 - Too little	8.3%	5.9%	0.0%

- 35.8% of all investors and 53.3% of international investors consider Swiss-listed companies' CSR not sufficient. Only 10.3% of the issuers share this view.
- Focus on boards as 69.5% of the investors in the SWIPRA Survey 2016 considered the board in the lead to define a company's CSR strategy

Questions: [left] In your opinion, to what extent do Swiss-listed companies assume their corporate social responsibility? [right] Investors: In your opinion, who should be in charge of defining the corporate social responsibility strategy in a company? Issuers: Who is in charge of defining the corporate social responsibility strategy in your company?

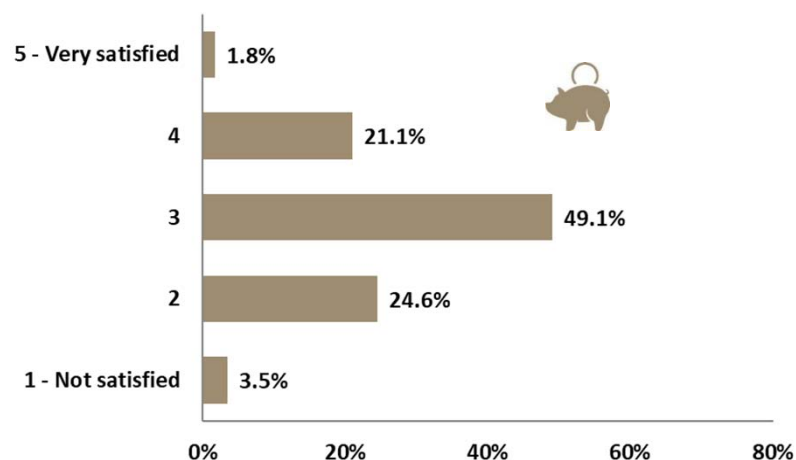


# Corporate social responsibility (II)

## CSR disclosure and audit

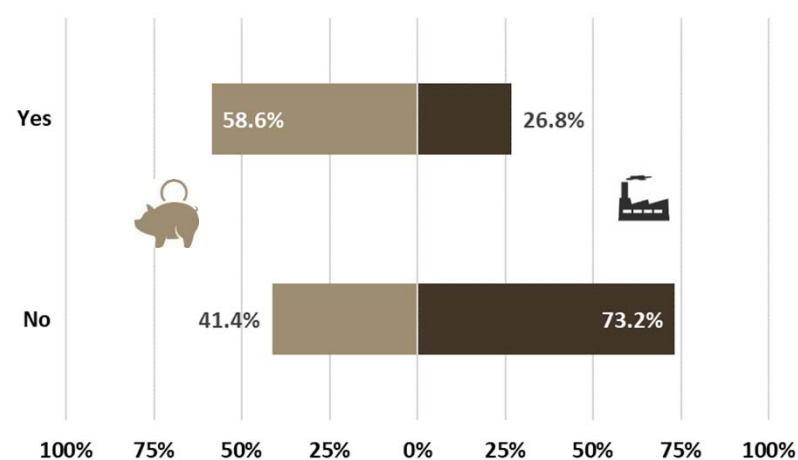
### Meaningfulness of CSR disclosure

Survey 2018



### Audit of CSR reports

Survey 2018



	Pension funds	CH asset managers	Int. asset managers
5 - Very satisfied	4.2%	0.0%	0.0%
4	20.8%	29.4%	12.5%
3	50.0%	52.9%	43.8%
2	25.0%	11.8%	37.5%
1 - Not satisfied	0.0%	5.9%	6.3%

- 22.9% of investors overall and only 12.5% of international investors satisfied with CSR disclosure
- 58.6% of investors overall and 80.0% of international investors want external auditor to review CSR reports
- 73.2% of issuers do not consider external reviews on audit reports as necessary

Questions: [left] In your opinion, do (non-financial) corporate social responsibility targets receive sufficient weight in the determination of variable remuneration? [right] Should the external auditor also review a company's corporate social responsibility reporting?

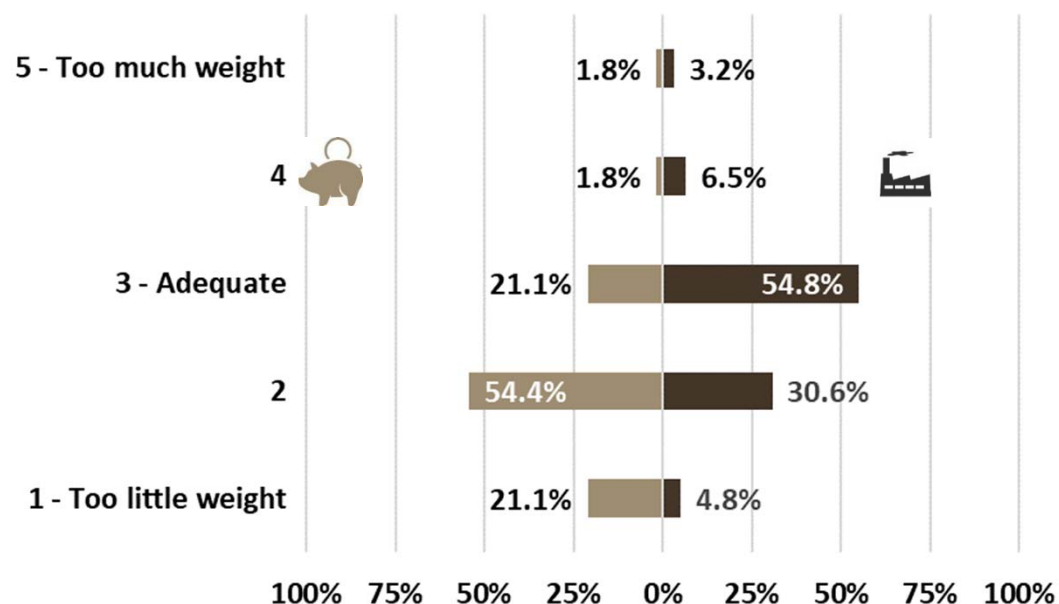


# Corporate social responsibility (III)

## CSR and compensation

### CSR targets in variable compensation plans

Survey 2018



- 75.5% of the investors believe CSR targets receive too little weight in compensation systems
- 87.0% of Swiss pension funds consider weight of CSR targets in compensation systems too low
- 64.6% of issuers believe CSR targets are reflected adequately (or even too strongly)

	Pension funds	CH asset managers	Int. asset managers
5 – Too much weight	4.3%	0.0%	0.0%
4	4.3%	0.0%	0.0%
3 – Adequate weight	4.3%	43.8%	22.2%
2	60.9%	43.8%	55.6%
1 – Too little weight	26.1%	12.5%	22.2%

Question: In your opinion, do (non-financial) corporate social responsibility targets receive sufficient weight in the determination of variable remuneration?



## Implications: Corporate social responsibility

- CSR is becoming a more important topic for investors who will challenge the board on an increasingly broad range of topics and request a more meaningful and comprehensive disclosure
- The link between variable compensation and CSR is considered insufficient by investors, raising questions about the substance of CSR strategies
- High CSR standards help issuers to build investors' trust, which is particularly valuable in crisis situations

**What are concrete ways in which CSR elements can be credibly incorporated in strategy and compensation design?**



## Plan for this presentation

- Key results
- Proxy advisors: changing role
- Engagements: further gaining importance
- Board independence: the holy grail for investors
- Board succession and director selection: diverging views
- Corporate social responsibility: room for improvement
- **Remuneration: challenge to link goals, culture and incentives**
- Summary and outlook



# Remuneration (I)

## Disclosure

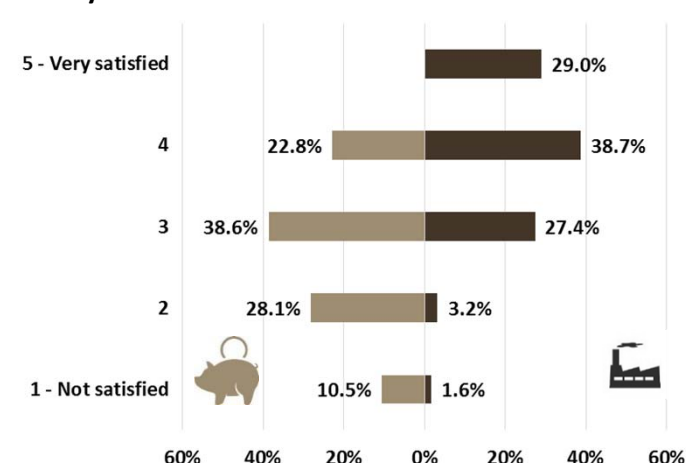
### Disclosure of *qualitative* targets

Survey 2018



### Disclosure of *quantitative* targets

Survey 2018



- Qualitative (non-financial) performance metrics are difficult to trace for investors
- Substantial gap between investors' and issuers' perception: 72.7% of investors not satisfied with the disclosure of qualitative targets, 83.3% of issuers believe disclosure is sufficient
- Compared to *qualitative* targets, investors perceive disclosure quality of *quantitative* targets better, though none of the investors is very satisfied

Questions: How satisfied are you with the general disclosure of compensation-related performance measures? [left] Qualitative targets (e.g. achievement of strategic targets, compliance, etc.); [right] Quantitative targets (e.g. EPS, EBIT, etc.)



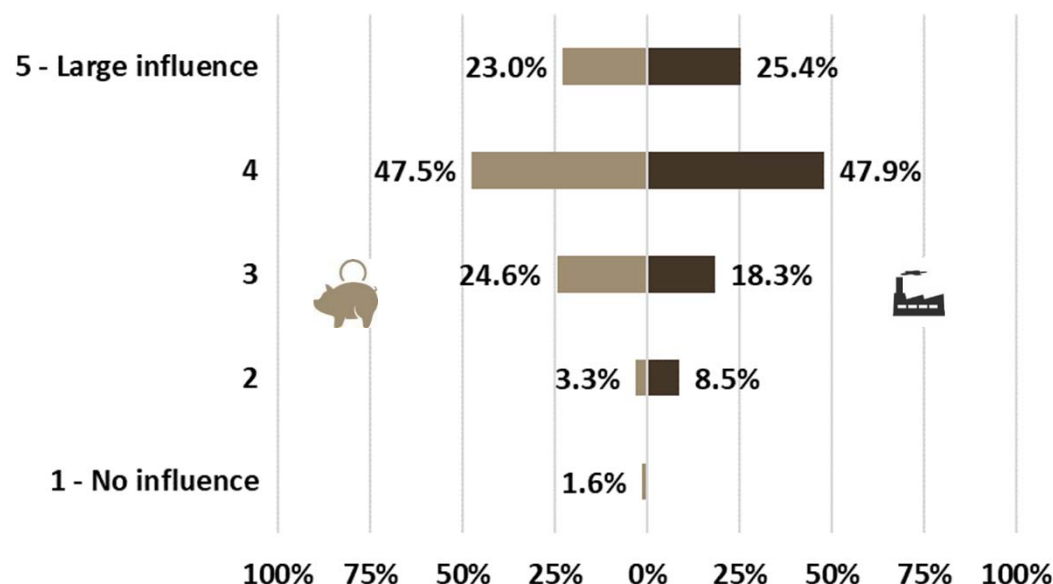


# Remuneration (II)

## Suitability of qualitative targets

### Impact of qualitative performance targets on long-term target achievement

Survey 2018



- 70.5% of investors and 73.3% of issuers believe qualitative performance measures support reaching long-term strategic targets
- Failing in qualitative targets, e.g., compliance systems, may lead to significant negative value impact
- Guide short-term behavior with qualitative targets to maximize long-term value

	Pension funds	CH asset managers	Int. asset managers
5 - Large influence	33.3%	6.3%	22.2%
4	33.3%	75.0%	44.4%
3	29.6%	12.5%	27.8%
2	0.0%	6.3%	5.6%
1 - No influence	3.7%	0.0%	0.0%

Question: To what extent do qualitative performance targets in compensation systems (e.g. ethical conduct, functioning compliance, functioning risk management, etc.) support the achievement of a company's long-term strategic targets?

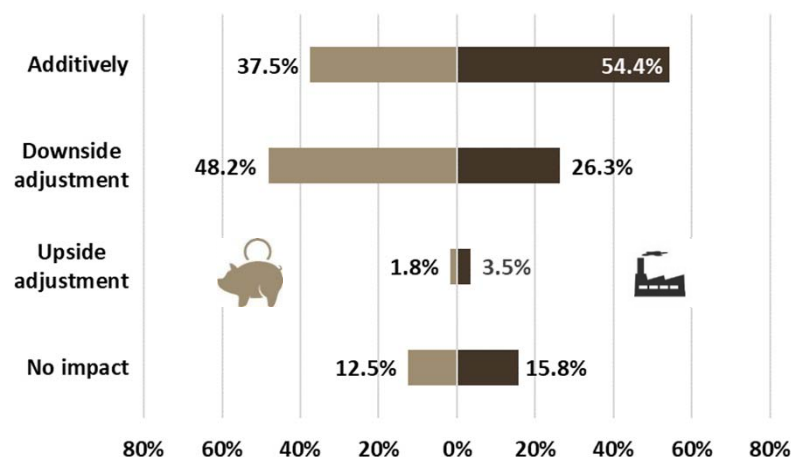


## Remuneration (III)

### Impact of qualitative targets

#### Impact of achievement of *qualitative* targets on short-term bonus

Survey 2018



- Investors and issuers ambiguous about impact of qualitative targets on short-term bonus
- 54.4% of issuers believe they should be treated similarly to financial targets
- 48.2% of investors believe underachievement should lead to downward adjustment, only 1.8% believe it should lead to upside adjustment

**Additively** to the financial targets (weighted average of financial and qualitative target achievement levels).

If the qualitative targets were achieved, the short-term variable remuneration based on financial targets achievement levels should be reduced (i.e., **downside adjustment**).

If the qualitative targets were not achieved, the short-term variable remuneration based on financial targets achievement levels should be increased (i.e., **upside adjustment**).

The achievement of qualitative targets should have **no impact** on the short-term variable remuneration.

	Pension funds	CH asset managers	Int. asset managers
Additively	36.0%	20.0%	56.3%
Downside adjustment	44.0%	60.0%	43.8%
Upside adjustment	0.0%	6.7%	0.0%
No impact	20.0%	13.3%	0.0%

Question: To what extent should the achievement of qualitative targets (e.g., ethical behavior, functioning compliance, working risk management, etc.) influence the level of short-term variable remuneration?



## Implications: Remuneration

- Qualitative performance metrics considered useful by issuers and investors alike, but their use in variable compensation plans is highly controversial
- Despite perceived benefits of qualitative metrics, achievements difficult to reconcile for investors on basis of available disclosure
- A downward adjustment of regular bonuses in case qualitative targets are not achieved provide strong incentives for management to fulfill these targets

**Can qualitative performance metrics provide the desired long-term incentives while remaining meaningful and traceable for investors?**



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## Summary and outlook

More distinct and differentiated analyses by investors will result in requests for a more comprehensive and meaningful disclosure by issuers.

Investors face an increasing demand for transparency regarding their approach to careful stewardship.

Addressing these challenges efficiently and constructively requires regular engagements between the board of directors and investors.



## Further scope of the SWIPRA Survey 2018

Some of the additional questions covered by the survey:

### **Regulation**

- Are minority shareholders sufficiently protected?
- Where does the market see a need for action?

### **Auditors**

- What is the market's perception of the external auditor's independence?
- To what extent are external audits used to assess the adequacy of compliance management systems?

### **Payout**

- Are payout levels of Swiss-listed companies sustainable?
- Do payout decisions impact variable compensation?



## Notes



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