

Written evidence from EEF, the manufacturers' organisation (CGV0142)

1. EEF, the manufacturers' organisation, is the voice of manufacturing in the UK, representing all aspects of the manufacturing sector including engineering, aviation, defence, oil and gas, food and chemicals. Representing some 20,000 members employing almost one million workers, EEF members operate in the UK, Europe and throughout the world in a dynamic and highly competitive environment.
2. EEF members comprise of a spectrum of different undertaking, from large multi-nationals to small family owned businesses. Overwhelmingly they are mindful of their legal and ethical duties to their shareholders, customers, workers and wider society. Long before the advent of auto-enrolment, they invested in workplace pensions, and more than three times as many manufacturers invest in apprenticeships than businesses in the economy as a whole. The backdrop to our submission therefore is a manufacturing sector that is already providing a high level of corporate responsibility in areas of pay, corporate governance and board representation.
3. Below we set out in greater detail our evidence to the committee, but in summary we have no evidence from the extensive surveys with our members and the resultant public reports that there is an evidence-based case for further UK legislation. The UK already has a robust system of regulation coupled with a record of success where non-legislative initiatives have been used.
4. This inquiry comes at an historic time for UK businesses. The impending exit from the European Union casts a shadow over businesses who trade with the EU. Over 50% of UK exports into the EU come from the manufacturing sector. Until the UK has secured its future trading relationship not just with the EU, but globally, we believe that to the greatest extent possible, stability in all other areas of business practice should be maintained. Legislation should therefore be contained solely to areas where there is a clear evidence base for immediate intervention. The EEF reports which we have cited here do not suggest that this test has been met. In addition, the UK Government has stretching targets for the reduction of the cost and burden of regulation on business, made all the more important by its various statements that the UK should, in the future, increase its global trade footprint. Success in meeting these ambitions, which are necessary for shareholders, workers and consumers, will depend on the UK's wider industrial strategy. Corporate governance will form an element of this, and therefore needs to support wider industrial goals and not be seen in isolation.
5. This is not to say that more cannot be done to improve the UK corporate governance acquis, but that the tools used should be proportionate. Whilst not explicit, the underlying objectives of the inquiry seem to be centred on larger companies which comprise of, perhaps, the FTSE 350. There is even within publicly listed companies a considerable variety of types of businesses and even more so when private companies are also considered. Attempting to universally apply principles to large multi-nationals and larger SMEs is unrealistic and potentially damaging, but that principles can be established and good practice spread. Much of this is already embedded in business

practice, but some businesses can benefit from change which we believe should be incremental and positive. Legislation is by contrast slow and can be perceived negatively.

Director duties

6. The 2006 Companies Act was the largest single piece of UK legislation at the time. It largely codified the already established duties of directors and was followed by extensive training given to directors. It therefore served as a useful catalyst for the improvement of the visibility of the obligations of directors, and in our experience directors responded to this as a result, becoming better aware of their duties.
 7. Section 172 of the 2006 Act already provides a platform for the obligations of directors which is difficult to substantially improve upon. In effect, it requires the promotion of the success of the entity in the long term, with a series of factors for the director to have regard to whilst discharging a fiduciary duty. We do not believe that section 172 is in itself deficient, or that the world in which businesses, consumers, workers and other stakeholders operate is so different today that the 2006 Act requires amendment.
 8. There is however a credible case for refreshing the work which was done by corporates in the aftermath of the 2006 Act, that is ensuring that all directors of all incorporated undertakings know what their duties are and what their legal obligations are. This process will be different depending upon the size and nature of the undertaking, and the largest undertakings already ensure that there is a comprehensive process in place to achieve this, but this is we believe an example of where the best corporate practice can achieve greater traction by demonstrating good practice to all corporations.
 9. In addition, since 2006, companies of different sizes have been required to comply, or will shortly need to comply, with a range of new measures which will cumulatively further improve corporate transparency and drive ever greater compliance with the duties under the 2006 Act. Gender pay reporting, modern slavery reporting and corporate social responsibility reporting all add to the transparency of businesses subject to the new requirements and place further obligations on directors.
 10. In summary then, the 2006 Act already provides a robust set of obligations for directors, but that improvements in awareness and transparency can be achieved by revising the approach of many companies adopted after the obligations came into force, by training and the spreading of good practice to companies of all size.
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Executive pay

11. The total reward received by executives can only be justified by their continuing performance. Very high reward can only be justified by exceptional, sustained and

transparent performance. Pay processes themselves must be transparent and subject to accountability, else they will lack confidence. Applying these principles in practice will ensure that executive pay is seen as a reward for long term success and not business as usual.

12. Larger EEF members typically rely on remuneration committees to set executive pay, with pay at the highest level decided upon within terms set by shareholders. The key link in any discussion of pay, whether executive or other, is that pay is seen as a reward for achievement. This achievement needs to be transparent, else executive pay will be construed negatively. Performance must therefore be transparent and the process of reward by be overseen and subject to accountability.
13. In any incorporated undertaking, the ultimate owners are the shareholders. They should therefore be the final arbiter of pay and reward. Shareholders already have an advisory role on pay and more recently a binding vote on the remuneration policy for Directors. With this background, we do not believe that further legislative intervention can, at this time, achieve more than the processes already in place. Furthermore, the UK must be able to attract the best talent at the highest level globally, which may at times require a reward package which can compete with other corporate entities, which may be outside the UK. In the same way that other sectors need to be able to compete for the best global talent, UK businesses need to be able to attract and retain the world's best business leaders. This is not to say that their reward should not comply with the principles outlined above, but that now, and even more so in the future, the UK will be globally focussed economy competing for the best global leaders.
14. The paragraphs above have been directed at the largest UK corporates. In keeping with our views on the duties of directors, there is good practice that can be spread down the corporate chain. Larger SMEs are in a wholly different category to publicly listed corporates, but their practice is a useful corporate steer. Perhaps too little has been done to raise awareness of and propagate principles of good practice already adopted by the largest corporates, and there is more we believe that can be achieved in this space.

Composition of boards

Diversity on boards

15. EEF members have already demonstrated the efforts which they have made to improve the diversity of their own boards. There is a clear message from manufacturers that boards comprised of diverse individuals make better decisions. The only issue which we will address here is how this is already being achieved.

16. EEF has published three *Women in Manufacturing* reports (2013, 2014, and 2015) to track the progress of FTSE companies against the Lord Davies target to increase the number of female representation on boards. The final of these three reports, published in 2015, when the Lord Davies target was to be achieved, showed significant progress. Our 2015 report found that for the second year running every FTSE 100 manufacturer had at least one female director on their board – with women accounting for 23% of total board seats (up from 21st on the previous year). Moreover, 25% of all new board appointments in FTSE 100 manufacturers are now going to women.¹
17. There are still challenges. While growth is seen in non-executive roles, female share of executive directorships in FTSE 100 manufacturers remained static in the final year of our reporting at 8%. But represents a long-term challenge and requires addressing the barriers to getting more women into our industry, starting at a grass-roots level.
18. The demographics of an average EEF member company is 85% male and 15%. Therefore it is vital we encourage more women into industry.² Moreover, only 14% of engineering and technology graduates are female, only 8.2% of engineering professionals are female and even more concerning just 3.1% of engineering apprentices are female.³ If we are to tackle the number of female executive directors in our industry, we must tackle the grass-roots problems first.
19. In EEF's recent report, *An Up-Skill Battle*, we found that manufacturers of all sizes and across all sectors are offering flexible working as a means to attract and retain the best female talent. Many manufacturers also continue to offer enhanced maternity packages, with enhanced maternity pay and back to work bonuses in a bid to incentivise highly skilled women into, and then back into the workforce. However, even with the introduction of shared parental leave, women still take primary caring responsibilities and career breaks. The cost of childcare is commonly cited as a key area of concern for women, with women staying at home instead of returning to work.⁴
20. Furthermore, manufacturers continue to report that they simply do not receive the same volume of applications from females, particularly at entry level, as they do from their male counterparts. Part of this can be explained by the choices made by young women in school. This issue is now new and programmes and initiatives are currently in place to overcome this, but it won't happen overnight. EEF itself continues to promote women in manufacturing.⁵

Worker representation on boards

21. Some global EEF members already have workers represented on their boards at some level. Their experience of this is positive; that the voice of workers improve accumulated

¹ EEF, *Women in Manufacturing* (2015) Available at <https://www.eef.org.uk/resources-and-knowledge/research-and-intelligence/industry-reports/women-in-manufacturing-2015>

² EEF Skills Survey 2015-16

³ Figures from Women In Science and Engineering (WISE).

⁴ EEF, *An up-skill battle* (2016) available at: <https://www.eef.org.uk/resources-and-knowledge/research-and-intelligence/industry-reports/skills-report-2016>

⁵ <https://www.eef.org.uk/campaigning/campaigns-and-issues/current-campaigns/women-in-manufacturing>

board knowledge and is an aid to workforce communication. There is, however, no evidence amongst the EEF members we have consulted that it is the requirement to include a worker on a corporate board that has in itself caused these positive results.

22. EEF members already use a spectrum of ways to engage with their workforce. Amongst EEF members, this has long been embedded business practice and is not a new development. EEF's report, *Flexibility in the Modern Manufacturing Workplace*, highlighted this. Manufacturers can only achieve the flexibility they need through cooperation with their employees. They embed this cooperation into their business strategy through a number of channels, including employee engagement and reward. Four-fifths of manufacturers say that the nature of the cooperative relationship between management and the workforce has helped them to achieve the flexibility their business needs to fulfil their growth ambitions.⁶
23. Employers recognise that they need strategies to engage the workforce, and the importance of employees and employers working together in both good times and bad. This was best demonstrated during the last recession, where many manufactures worked with employees and their representatives to help keep companies afloat and were therefore able to reduce the need for job losses and to help retain key skills. Manufacturers continue to see their approach to engaging their employees, people management and communication as a core component of their overall business strategy.
24. Strong engagement brings many direct business benefits, from higher productivity to reduced absences. But, EEF members have achieved this largely without any legislation requiring this, and some anecdotal evidence suggests that in larger SMEs workers have. There is no evidence from our surveys or consultations with our members that further legislation would help in promoting the employee voice, if indeed that is what the concept of workers on boards is intended to achieve. Whilst we therefore firmly support strong employer-worker engagement, we do not support statutory intervention to require all, or a cohort, of companies to appoint a worker to their board. Furthermore, we do not support any dismantling of the UK corporate structure in order to achieve this objective. There is no evidence that the UK's unitary structure is ineffective and to change it would divert resources which will be needed in the coming years to deal with other possible corporate changes.
25. In discussion with our members, it has been clear that any single structure for requiring workers to be represented on UK corporate boards would result in considerable difficulties for many. Ironically, legislative intervention risks penalising businesses that already have established structures for engaging their workforces, as these may need to be dismantled to comply with any new legislation. Where, for example, an EEF member already has a worker representative, this may not conform to a new model. The worker, who may be experienced, trained and successful, may then need to be removed. Smaller companies who use worker consultative committees may be left with little practical option other than to disband them, and former workers, who are often retained by members after they leave the businesses, may become disenfranchised. Questions around elections, nominations, term of appointments, conflicting duties, proportions of

⁶ EEF, *Flexibility in a modern manufacturing workplace* (2011) available upon request

board members and who to appoint would all need to be addressed under a statutory system.

26. What has been clear in the discussions with our members is the variety of ways in which a company can ensure that they both engage their workforce and give effect to a strong employee voice. There is no common platform which we identified and there was a widespread view that long lasting relationships would be lost if government legislated over ground already covered.
27. We therefore believe that rather than attempting to devise a statutory platform, agile enough to deal with the issues we raise in the paragraphs above, more could be achieved in a shorter timeframe by an initiative similar to that following the intervention of Lord Davies in the area of women on boards. Government and parliamentarians should allow a space for EEF and other leading business organisations to make the case for and promote the representation of workers in a variety of forms, with no single statutory option for all to follow. In the same way as the work of Lord Davies drove change over a realistic time period, businesses can be nudged to follow existing good practice, by ensuring the need to provide a platform for the voice of their workers is firmly on the corporate agenda, without specifying a precise single-option to achieve this.

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