June 2016

the inside track #32

Highlighting CSR Issues of the moment

Getting more Social!

Over the past few years, the ESG focus has been very much on E for environment. This is perhaps unsurprising given the amount of media attention and legislation, both internationally and nationally, with the Paris UN Climate Change summit in December, the EU's ESOS audits requiring completion for December and the UK's ongoing Carbon Reduction Commitment.

But now we are seeing more of a focus on S for Social in ESG – at least in the UK. This started first with the Modern Slavery Act, the first statement of which will be required for UK companies for the year ending 31st March. This has built upon the UN's Ruggie Framework. Now, we are also seeing the requirement for gender pay gap reporting by UK organisations.

The statutory requirement for gender gap reporting was established in clause 147 of the Small Business, Enterprise and Employment Act 2015 (SBEE). This referred to "regulations under s.78 of the Equality Act 2010 (gender pay gap information) for the purpose of requiring companies to publish information showing whether there are differences in the pay of male and female employees." Section 78 envisaged regulations requiring employers of more than 250 employees to publish gender pay information. However, the government never introduced any regulations, preferring instead to focus on a voluntary scheme (the Think, Act, Report Initiative).

The statutory requirement was put in place by Liberal Democrats because of the poor levels of voluntary reporting - only 270 employers are involved in the Think, Act, Report Initiative, compared to 7,000 companies with over 250 employers in the UK. Of those, only five signed up to publish their gender pay gaps (one of which was PwC).

The draft regulations were published in February and the Government consultation ended on 11 March 2016. Based on these proposed regulations employers (private, public and voluntary with over 250 employees) are required to publish their:

- **Gender pay gaps**
- **The quartiles of their pay distribution**
- **Gender bonus gap**

For gender pay gap purposes, pay includes basic pay, paid leave, maternity pay, sick pay, area allowances, shift premium pay, bonus pay and allowances. Employers must publish their overall mean and median gender pay gaps (which are seen as complementary indicators). These pay rates are based on the calculation of an hourly pay rate for each relevant employee. In addition, employers will be required to report on the number of men and women in each quartile of their pay distribution.

For gender bonus gap, this covers bonus payments paid including profit share, commissions, productivity, performance and other bonus or incentive pay, piecework and commission, LTIP and cash equivalent value of shares.

For gender bonus gap information, employers must publish the difference between the mean bonus payments paid to those men and women eligible for bonuses and to publish the proportion of eligible male and female employees.

Employers are required to calculate this information for a specific period around April 2017. Then 18 months after commencement they are required to publish this information for the first time and must then publish annually thereafter. Publication includes a written statement (signed by a senior executive) confirming that the information is accurate (which must accompany the required information). The information must be provided on their searchable UK website that is accessible to employees and the public and retain it online for three years.

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The trigger point for gender pay gap reporting is for all organisations with more than 250 employees – this covers those in the private and voluntary sectors as well as the public sector. This is less stringent than the trigger for Modern Slavery statements which is for all companies with more than £35m turnover. As such it is less burdensome than the modern slavery reporting.

However, the devil is in the detail, and assuming the draft regulations are adopted relatively untouched, then there is a great deal of detail!

For example, organisations have to include within their pay gap reporting allowances such as those for cars paid through the payroll, on call and standby allowances, clothing, first aider or fire warden allowances. However, there is no requirement to include overtime, expenses, the value of salary sacrifice schemes, benefits in kind, redundancy pay or tax credits within the hourly rate reporting. Then the average pay rate is based on the calculation of an hourly pay rate for each relevant employee.

In addition, there is the question around the capability of the HR systems within an organisation. If the organisation is a single entity, then there may be few problems in calculating the mean and median pay rates. However, the challenges become greater the more entities within an organisation – and as a result the likelihood is that the HR systems may also multiply. If so, the challenges of calculating the median rate will be greater (although calculating the mean rate is less challenging). The use of a median pay rate is not unknown. Those companies that provide information for the Dow Jones Sustainability Index will be aware that the requirement to report on this measure has been required for several years. There are likely to be similar calculating issues in multi entity organisations in determining those employees eligible for bonus payments.

However, the real challenges will arise in terms of managing the reputation issues from publication. These will be particularly onerous if the proposal regulation that organisation must upload their information to a government sponsored website is carried through into the final statutory instrument. If so, then the risk will be for observers to group together organisations in similar sectors and comparing and contrasting the information without being able to put the information in the context of the organisation's structure or operating methods. However, it is worth bearing in mind that the Modern Slavery statement was also intended to be put on a government website for comparison purposes, but this was dropped before it became a statutory instrument.

It is important to stress that at this stage, gender pay gap reporting is only for UK based employees in large organisations. These employees are defined as "relevant employees who work in Great Britain and whose contract is governed by UK legislation". For those organisations that operate internationally, the task of collating pay gap information across their entire organisation would be a mammoth task, due largely to the fact that most HR systems focus on the needs of their country based reporting rather than pan national. However, given the way in which the EU seems to be viewing UK company reporting as being best practice (as is the case with the EU's Directive on corporate disclosure of non financial and diversity information), then organisations operating across the EU should consider such reporting being required within the EU over the next five years. If that is the case then the draft regulation's statement that the Secretary of State will review the burden of these regulations within five years may be worthless.

If you would like to know more about Asesoria Group's activities in general or The Virtuous Circle's work with clients on these topics and other CSR issues, and would like an objective and impartial view, contact: Melissa Kittermaster or Tony Hoskins via melissa.kittermaster@asesoria-group.com.