BIS | Department for Business Innovation & Skills

ENTERPRISE & REGULATORY REFORM BILL: Directors' Pay

Main purpose and benefits of legislation:
There is broad consensus that something must be done to address the disconnect between directors' pay and company performance. The CBI, IoD, ABI, NAPF, institutional investors and company bosses recognise that action needs to be taken so that rewards reflect genuine success and not mediocrity or failure.
It is not Government's role to micro-manage company pay but there are things we can do to address what is a clear market failure and to ensure the right governance framework is in place.

Experience of the existing advisory vote on pay has shown that it has had limited impact - companies don't have to take action, even where a large number of shareholders are unhappy and pay has continued to rise sharply.

The ERR Bill will give shareholders of UK quoted companies a **binding vote** on directors' pay policy. This will encourage shareholders to use their vote and companies to take notice.

Alongside this and through secondary legislation, the Government is **boosting transparency** so that what people are paid is clear and easily understood. The Government is also working with responsible business and investors to **promote good practice** in setting pay.

These are the most comprehensive reforms of the governance of directors' pay in almost a decade. They will encourage better engagement between companies and their owners and will give shareholders the tools to promote a stronger and clearer link between pay and performance.

It should still be possible for people to be rewarded for good performance but shareholders will have more power to prevent rewards for mediocrity or failure.

Background:

In March the Government published a consultation on a new shareholder voting model, including:

- A binding vote on future pay policy;
- An advisory vote on how pay policy was implemented in the past year; and
- A binding vote on any exit payments of more than one year's base salary.

The consultation also asked whether companies should have to get support from a larger proportion of shareholders when agreeing pay policy. The consultation closed on 27 April.

On 20 June, after carefully considering the responses and engaging extensively with a wide range of stakeholders, the Government announced its final policy package. This includes:

- A binding vote for shareholders on a company's pay policy including their approach to exit payments. This will happen annually unless companies choose to leave their pay policy unchanged; in which case the vote will happen as a minimum, every three years.
- A company will only be able to make remuneration payments and exit payments within the limits that have been approved by a majority of shareholders.
- When a director leaves, the company will have to promptly publish a statement of payments the director has received.
- Shareholders will get, as now, an annual advisory vote on how the approved policy is being implemented, including actual sums paid in the previous year.
- If a company fails the advisory vote they will need to put the pay policy back to shareholders the following year for re-approval in a binding vote.
- In addition, the Government supports calls from stakeholders that where a substantial minority of shareholders vote against, companies should have to respond and say what they will do to address shareholder concerns.

On 27 June the Government tabled clauses to be included in the Enterprise and Regulatory Reform Bill which would implement this package, These were accepted during committee stage in the House of Commons.

At the same time, the Government published draft regulations setting out the required content and format of directors' remuneration reports. These will replace the existing regulations and require companies to be much clearer about how much directors are paid and how this relates to performance. The Government invited comments on the draft regulations up to 26 September and will now consider the responses before bringing forward a final version in early 2013 when Parliament will have an opportunity to scrutinise the detail.

These legislative reforms will sit alongside the Government's existing initiatives to increase the diversity of boards and board committees and encourage employees to be more engaged in company decisions.

Key facts:

- The average total remuneration of FTSE100 CEOs has seen over a four-fold increase in the period 1998-2010. This is faster than the increase in the FTSE100 index, retail prices or average remuneration levels across all employees for the same period.[1]
- According to Manifest statistics, median total remuneration awarded to FTSE100 CEOs went up 12% in 2010/11, while average employee earnings rose just 2.3% in 2011.
- In 1998, FTSE100 CEOs earned on average 47 times the amount earned by the average employee; by 2010 this had risen to 120 times.

1 Manifest/ MM&K, The Executive Director Total Remuneration Survey 2011, May 2011