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100 Group of Finance Directors (The Hundred Group)

The Hundred Group
of Finance Directors

Investor Relations and Markets Committee

By email: executive.pay@bis.gsi.gov.uk

Mr Barry Walker
Department of Business, Innovation and Skills
1 Victoria Street
London SW1H 0ET

26 September 2012

Dear Mr Walker

Directors' pay: Consultation on revised remuneration reporting regulations

We welcome the opportunity to contribute further on the proposed changes to executive remuneration reporting. We recognise the need for simplification and change to the remuneration report in order to assist users of Annual Reports and to increase transparency in reporting executive pay.

Who we are

The Hundred Group represents the views of the finance directors of FTSE 100 and several large UK private companies. Our member companies represent almost 90% of the market capitalisation of the FTSE 100, collectively employing over 7% of the UK workforce and in 2011, paid, or generated, taxes equivalent to 13% of total UK Government receipts. Our overall aim is to promote the competitiveness of the UK for UK businesses, particularly in the areas of tax, reporting, pensions, regulation, capital markets and corporate governance.

Our views

The issue of executive compensation continues to be a hot topic for many media commentators and some members of the general public, particularly in the current tough economic environment, when it is believed that some executives have received unjustified levels of pay, when the results of their company in the current year have been poor. Whilst this is sometimes simplistic and overlooks achievement under long term incentive plan criteria which are now vesting, we agree that clearer remuneration reporting could help increase understanding of the relationships between pay and company performance, both long and short term.

We agree that executive remuneration reporting needs to be revised and we believe that the overarching principle should be the need to have reporting that is clear, concise and easily understandable, free from any unnecessary disclosures and that can be applied in a consistent manner to assist comparison between companies and individuals.

Our main concern with the proposed legislation is that the proposals should be clearer, especially with regard to what information should be included in the summary statement. We believe that confusion could lead to increased disclosures to ensure that prepares comply with the legislation 'by default'. We are opposed to any additional disclosure that does not have a clear purpose, and we fear that the legislation, as currently drafted, will not provide the necessary level of guidance to avoid unnecessary disclosure, clutter and duplication in the Annual Report. Our view is that remuneration reports have become too long due to the extensive disclosure requirements which already exist. We hope that these proposals will replace rather than add to existing disclosure requirements. We also recommend that guidance should be offered to remuneration committees to encourage them to consider what is material disclosure so that reports remained succinct and clearer.

We are supportive of the proposed disclosures for long term incentive plans "LTIPs", but highlight that the proposed disclosures for the cost of LTIPs and pensions are not aligned with international accounting standards and will therefore lead to different amounts being reported in the remuneration report and the accounts. We believe that one of the key parts of the Annual Report is consistency and this could be reduced by these proposals, although on balance we understand why a "value settled" approach has been selected.

We disagree with the proposal to automatically use the "HMRC methodology", involving a multiplier of 20 to calculate a director's pension liability in a defined benefit pension scheme, as we believe this methodology is flawed, can give non-intuitive results and outcomes which do not reflect specific scheme rules, thus reducing the real comparability of pension related values, even between co-directors who are often in different schemes from one another. We do not believe that this methodology produces reporting that is clear, comparable and understandable. We would prefer to use either IAS19 or the cash equivalent transfer value method instead, as we believe these approaches give a more accurate liability at the reporting date. We feel the "HMRC methodology" would be better positioned as a fall- back method, in the event that more accurate methods were not viable.

We support the proposal to align the UKLA Listing Rules with the revised legislation and see this as a good step towards removing current duplication and subtle variances in reporting.

We have taken this opportunity to answer some of the consultation questions raised (see the appendix to this letter), but believe that the Financial Reporting Lab's report 'A single figure for remuneration' provides a good basis for remuneration reporting. We also highlight our previous response to you on 27 April 2012 on your consultation on enhanced shareholder voting rights.

Yours sincerely

Robin Freestone
Chairman
Hundred Group: Investor Relations and Markets Committee

Annex: Our view on specific questions raised in the BIS consultation paper

We have chosen not to respond to all questions raised in the consultation paper, instead focussing on the ones we consider most significant to our members.

3. The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We support any disclosure that presents complicated information in a clear and concise manner. We believe that the illustrative disclosure included in Annex A of the consultation paper achieves this aim.

4. The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We agree that the proposed approach is a practical and informative approach, however we also note a couple of specific issues.

In keeping with our desire for reduced, focussed disclosure, we believe that a summary rather than the detail of all existing contractual provisions relating to directors' remuneration should be sufficient in the policy report.

We also note that the illustrative graph on page 18 of the consultation document is, as currently presented, likely to confuse preparers. Our main concern is that there appears to be a significant variance in the quantum of the example base salary, which, in our experience, remains broadly constant regardless of the other variable elements of pay.

Whilst presenting a large amount of information in graphical format is often a helpful way to convey key points, we believe that this and the other proposals in the draft legislation could lead to a plethora of graphs, especially if companies have a large number of directors. We recommend clarification that this graph should not need to be applied to non-executive directors, the vast majority of which are not subject to any variability in remuneration.

5. The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We support the Government's proposals and recommend that an explanation of contractual rights should also be given if valuable to the users understanding.

6. The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We disagree with the proposal to report on how a company has sought employee views as we don't currently see enough guidance on how this can be done effectively to represent the views of a meaningful population of employees within our member's companies. As we represent a large number of companies with a significant international presence, we also believe that the disclosure of the ratio between CEO pay and the median earnings of the workforce is misleading. The inclusion of this ratio would not, in our view, add anything to users understanding of directors' remuneration, nor would it be directly comparable to any other company falling within the amended disclosure requirements due to the large variances in geographic reach and workforce distribution of each FTSE 350 company.

7. The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

We acknowledge that there is no simple way to communicate remuneration in a single figure, but we are not convinced that the approach set out in the table on page 24 meets the objectives of this legislation. We appreciate the Government's desire to reflect actual pay rather than potential pay for a particular reporting period, however we note that this is contrary to accounting principles. Under the proposals, the treatment of both LTIP and pension reporting does not accord with applicable accounting standards and will result in different amounts being shown in the remuneration report and the accounts.

The disclosure of amounts paid for LTIP awards with performance conditions that end in the year is likely to lead to certain years where the remuneration disclosed is significantly higher than the preceding or subsequent years. This could cause more public disquiet about the levels of executive compensation than a model which reflects the potential amounts accrued each year over the life of an LTIP scheme. We recognise that the Financial Reporting Lab proposed this "paid" approach as the solution that satisfies most interest groups and therefore we would accept this disclosure model, but would suggest that the Government ensures that the implications of such disclosures have been considered fully.

If the Government remains committed to showing remuneration on a "paid", rather than an accrued basis, we reiterate our view that this needs to be explained with a "one number: two drivers" approach, with clarity on how the elements of remuneration related to long term performance are aligned with Company performance.

8. The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We believe that valuing the benefit of a defined benefit pension scheme should be done using IAS19 (or the existing cash equivalent transfer value method), as this calculation is based on current market conditions and provides the most accurate calculation of any benefit at the reporting date. Whilst the calculation methodology may be complex, it will have already been calculated for each director as part of the IAS19 disclosures in the notes to the Annual Report and we believe using two differing calculation methodologies to calculate the same benefit would lead to confusion.

The HMRC method seems flawed, as the annual allowance methodology is extremely complex and may give non-intuitive results, dependent on the specific wording of scheme rules. This means that the results will not be comparable between directors who are members of different schemes, which is often the case. This would seem at odds with the Government's desire for clarity of reporting.

Should the Government reject using the IAS19 calculation methodology, we would recommend further definition of the 'HMRC method' and we believe that using a multiplier of 20 to this calculation is a very arbitrary and approximate way of calculating the pension benefit for a director that takes no account of whether there is a spouse's pension, pension increases, early retirement benefit, or even how old the member is. The single figure disclosure is designed to be as accurate as possible (with auditors significantly reducing their level of materiality to audit these numbers down to the nearest thousand or less), therefore introducing this approximation for pension benefits seems counter to the overall aim of this legislation.

We would prefer to see the HMRC methodology as a fall back, only to be used if other more precise methods weren't viable. We'd support the need to disclose the methodology adopted which should be consistently applied.

9. The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Yes. We agree with this approach, as clawbacks can significantly alter the total remuneration a director receives in any one year.

10. The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We believe in certain circumstances it could be commercially sensitive to disclose details of performance against very precise company metrics which may not have been disclosed elsewhere, depending on what metrics have been used to set director's remuneration. However, providing a blanket exemption could lead to abuse unless clear guidelines are also issued. We recommend that criteria are set for when the exemption can be taken as well as requiring an explanation for why metrics have not been disclosed.

11. Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We agree with the principle that additional information may be needed to supplement the single figure where a director has defined benefit pension benefits. However, we do not think that the current proposals provide sufficient clarity as to what is proposed. Is the accrued benefit to be calculated as if the member remained in service until their normal pension age, or as if they had left at the end of the year? How is the additional early retirement benefit to be calculated, given that the actual annual figure is unlikely to change, but rather the date from which it is paid? Further clarification of the disclosures required is needed.

13. The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We welcome any simplification in reporting requirements and would be supportive of any alignment between the Companies Act and the Listing Rules to ensure clear disclosure requirements for directors' interests.

14. The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We do not believe that this disclosure is useful for a two reasons. Firstly, using total shareholder return as a proxy for company performance is a very crude assumption and, whilst it may be appropriate for many companies, it is likely that some CEOs are remunerated on other measures such as increased market share. Therefore, if this disclosure is retained in the final legislation, we would recommend that companies should be allowed to choose an appropriate alternative benchmark, as long as the reason for choosing the benchmark (if not TSR) is disclosed and it is consistently reported. Secondly, we believe the use of CEO pay alone is also a crude assumption and would recommend using total director or key management personnel pay, which would be more appropriate.

We accept that over a ten year period there will be years in which pay will 'spike' when one CEO leaves and another joins, and we note that it is often companies which are struggling to increase shareholder return that may change CEOs more regularly than more stable companies, meaning that the comparison would be even more misaligned.

Finally, we are unsure what guidance will be given when dealing with companies that have substantial change, such as demerger during the ten year period. We presume the 'newco' will only have a short period to report, however should the legacy company show the TSR and CEO pay for the original combined group prior to demerger or carve out the return to shareholders and what the executive in charge of the demerged operations was paid for the period prior to demerger? Further guidance on this would be welcome.

15. The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We do not believe that it is necessary to expand the scope of the audit to other areas of the remuneration report and agree that the specific numbers highlighted are the most appropriate ones that should be audited. As much of the remuneration report relates to statements of policy, we do not see any criteria which would be able to be appropriately verified by the auditor. We note that, whilst no explicit audit opinion is given on the other parts of the remuneration report, auditors are required to read all sections of the Annual Report and to highlight any misstatements or inconsistencies when compared to the audited financial statements.

ACCA

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

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Department of Business, Innovation and Skills
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Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
✓	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

The Government is seeking to make the reporting of directors' remuneration more transparent, to increase shareholder engagement, and thereby to restore the link between pay and performance.

ACCA agrees that the disclosures and enhanced shareholder voting rights, set out in the proposed Regulations, represent progress in achieving the above objectives. Companies will, however, need to remain mindful of the key principle in the Government's proposals that the information provided to shareholders should be, and should remain, understandable (which will also achieve the aim of year-to-year consistency). The increasing complexity in remuneration reporting in recent years is not chiefly due to statutory Regulations. One factor is the increasing complexity in remuneration structures themselves, and we have previously stated that simpler structures would, in general, be desirable (in our response in November 2011 to the Discussion Paper on Executive Remuneration, dated September 2011 ["our November 2011 response"]).

Our November 2011 response also drew attention to broader factors which are essential if the proposed Regulations are to have the effects intended. These include the need for shareholders and non-Executive Directors to have (and continue to have) a challenging mind-set on issues such as pay, and a reduction in short-termism (for example, by increasing the typical vesting period for incentive schemes).

We also have the following comments in relation to individual areas of the proposed Regulations:

Regulation 2: we agree that the Government should not prescribe the contents of the summary to be given by the chairman of the remuneration committee. We do believe that guidance should be issued which lays down principles for determining the information which will be of most use to investors. We have previously commented on the need for remuneration committees to demonstrate regard for the company's wider interests (in our November 2011 response, and our response in April 2012 to the Consultation on enhanced Shareholder Voting Rights, dated March 2012).

Reg. 6.(c)(iii): for money purchase pension schemes, the single figure for remuneration would include the additional value achieved in the year only where the company has not made a contribution to the scheme during the year. We disagree with this provision, both in respect of its inclusion in the remuneration figure, and the idea that such a disclosure would only be required when no company contribution is made. We note that Section 10(2) requires the annual disclosure of the accrued benefits under a defined benefit scheme, and believe that any disclosure of the value of a money purchase scheme should be on the same basis.

Reg. 13.(2): we support the ten-year maximum time period to be covered by the line graph. We would also recommend provision for accompanying narrative disclosures of any significant matters affecting the reported data. There may be notable changes during a ten-year period, both in a company's industry or the wider economy, and for a company individually (such as the effects of a restructuring).

Reg. 15.(2):particular emphasis is placed on advice given to the remuneration committee by a director who was not a member of it. We believe that at least equal emphasis should be placed on the involvement of external remuneration consultants.

Reg. 16(c): in the context of reporting when there has been substantial shareholder dissent, it would be helpful for "substantial" to be clarified with, for example, an indicative percentage of the total votes cast / exercisable.

Reg. 24 (relative importance of spend on pay); and
Reg. 30 (percentage increase in CEO pay compared to employees):

These concern the reporting of actual historical data. Consequently, they would be better-placed within Part 3 (Report relating to the Financial Year) than Part 4 (The Policy Part).
Furthermore, the terms "profit" and "previous years" in Reg. 24 need to be more precisely defined. There are several reported measures of profit in the financial statements of listed companies. With respect to "previous years", a three-year period could be stipulated, for example, which would be consistent with the maximum period of time between votes on pay policy.

Similarly, to avoid potential confusion, it would be helpful if the term "face value" for longer-term incentive rewards were to be more precisely defined (Reg. 12.(b) (iii)).

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

ACCA agrees that any additional costs incurred in implementing the new Regulations should not represent a burden for companies, especially after the first year of implementation. The proposed regulations are a replacement for the existing ones, rather than an addition to them, and companies should be able to extract readily from their accounting records most of the information to be disclosed. Furthermore, as a general principle, we believe that Regulations should seek to avoid adding undue complexity to corporate reporting. If a company is not already compiling internally some of the information required by the proposed Regulations, we support, on the grounds of good practice, the fact that it will now need to do so.

Additional costs would be minimised, and possibly avoided altogether, if companies took the opportunity, when making the changes, to adopt a straightforward reporting style which continues to avoid unnecessary additional disclosures. As mentioned in our response to Question 1, this more straightforward style would also benefit the users of the financial statements, and consequently the matter would be worth mentioning in the guidance issued by the Government to accompany the Regulations.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We agree that it is not practical for the Regulations to prescribe specific disclosures, suitable for all types of company, in respect of the table which explains pay policy (Part 4 of the proposed Regulations).

Whereas the report on remuneration actually earned (Part 3) should have content which is as precise as is practically possible, the policy section's main function should be to explain and justify to shareholders the structure of remuneration, and how this incentivises the directors to contribute to the long-term success of the company.

Companies' circumstances vary, and they need to be able to decide how best to report remuneration policy in a manner which is most informative to shareholders. We believe that the content of the proposed Regulations sets out adequately the framework in which companies may do this.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

ACCA mainly agrees with the Government's proposals on these matters. Whilst there is a potential separate concern that service contracts are in fact proving difficult for shareholders to access (as reported in the consultation document), it will in any case be informative for the provisions therein relating to remuneration to be additionally disclosed each year within the Remuneration Report.

The statement on scenarios in graphical form needs to be supplemented by an explanation of why total remuneration has under-performed or out-performed target in the reporting period, and whether this outcome is different from the trend in recent years. Shareholders need to be aware if, for example, actual remuneration typically exceeds the expected amount, as this may indicate that targets (and consequently, what they have been expecting the directors to earn) are being set artificially low. Alternatively, there may have been an impact from external factors not within the control of the directors.

A similar set of explanations would be advisable to accompany the reported percentage changes in profits, dividends and total remuneration in the period.

As set out in our response to Question 1 above, we believe that Regulations relating to the disclosure of actual (historical) data should be placed in Part 3 rather than Part 4 of the proposed Regulations.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We agree with the general principles in Regulation 26 concerning how termination payments will be calculated, such as how each element of the payment is calculated, and how performance will be taken into account.

Regulation 26.(b) requires the company to state whether the calculation of termination payments will distinguish between types of leaver and the circumstances of leaving. In view of the concerns over perceived "rewards for failure", it would be helpful for companies to explain their policy decision more fully here. For example, shareholders would normally expect confirmation that the exit payment will be lower if a director chooses to leave before the end of the term of the service contract.

We note that the statement will not be individualised (para. 51 of the Consultation Document). Whilst the policy for termination payments will be more understandable when it sets out its provisions generally, rather than at much more length by director, it may be desirable (and in order) for shareholders to agree that specific terms may apply to individual directors, reflecting their particular role and what is expected of them. In this case, these specific terms should be reported (and explained) as individual amendments to the general policy.

It is also proposed that companies disclose details of any contractual provision agreed before the introduction of the Regulations that could impact on a termination payment. As exit payments are a potentially controversial matter, it would be informative for shareholders if the company were also required to explain why any contractual provision pre-dating the introduction of the Regulations would now be precluded from service contracts.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

ACCA supports the inclusion of this statement within the policy part of the remuneration report. Employees are stakeholders, and may also be the holders, individually, of small proportions of shares in the company. To provide balance, it would be helpful for the company to explain why it did not seek employee views on the remuneration policy. Companies may either have no consultation procedures, or may consult employees on other matters which in turn, do inform the discussions of pay policy by the remuneration committee.

This same section of the Regulations (no. 30.(1)) requires a comparison of the increase in salary of the Chief Executive Officer with that of employees generally (or a group of employees, if considered more relevant). As set out in our response to Question 14 below, we would question whether the CEO alone should be used for comparison, as opposed to a wider group of directors.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We believe that the table set out on page 24 of the Consultation Document does set out principles consistent with the intention set out above.

ACCA also supports the view that a single total figure of remuneration for each director, suitably analysed, will assist the understanding by the users of the financial statements of the rewards provided during the financial year.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

ACCA agrees that the reported amount for defined benefit schemes in the Remuneration Report should be based on the value to the director, rather than the cost to the company. Consequently, IAS 19 would not be as suitable a basis for this particular disclosure as it is for the cost to the company disclosed in the statutory financial statements.

The use of HMRC methodology is practical, as it has the advantage of being readily understood and straightforward to apply. We view this is an important consideration in making the Remuneration Report itself, with its many components, as readily understandable as possible. However, directors will be interested in and - motivated by – the value of their pension fund as determined under other methods. For individuals, it is likely that transfer value will be the key measure here.

The above raises the question of how to reconcile the need for practicality and relevance in the disclosure of the value of defined benefit pension schemes. One way in which this could be achieved involves retaining the proposed HMRC method for the amount to be reported in the single figure. This could then be supplemented by a narrative statement that the transfer value, to which individual directors will probably have regard, is likely to be *x* times higher than the HMRC value, but is not included in the single figure for remuneration, as it is subject to volatility which is not caused by the performance of the director.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that claw-back should be reported within the single remuneration figure, as it is a component of total remuneration (albeit a deduction).

However, we do disagree with the proposal that no further disclosure should be required concerning the claw-back (leaving companies a choice as to whether to disclose the circumstances, as set out in para. 73 of the Consultation Document). In view of concerns about the extent of “rewards for failure”, claw-back is likely to attract similar levels of shareholder interest as termination payments (on which we have submitted our views in our response to Question 5 above). Furthermore, whilst claw-back amounts may be smaller than exit payments, they may indicate underperformance or even misconduct, which shareholders would particularly need to be made aware of.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We believe that, in order to improve transparency around directors’ remuneration, particularly the element which is variable, it is necessary to explain how the pay achieved compares to the company’s performance.

It would not be possible or desirable to specify levels of detail which would, for every company, achieve a balance between commercial confidentiality and adequate disclosure to shareholders. We would not therefore propose changes to the general reporting requirements proposed by the Government.

Companies already have to disclose potentially sensitive information, such as an indication of their future prospects. There can be a tendency to adopt vague wording, in order to avoid revealing more than is absolutely necessary. However, in the case of pay, shareholders are able to secure adequate disclosure thorough having the ultimate sanction of rejecting the report on pay in their advisory vote.

It is also likely that measurement criteria and reward mechanisms are similar throughout companies in a particular industry, as norms develop and companies compete. In this respect, commercial sensitivity is unlikely to present a major issue for companies.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We believe that the proposed requirements will mean that sufficient information is disclosed concerning accrued pension benefits. In particular, the requirements cover information relevant to shareholders (such as the pension receivable if a director was eligible to retire at the accounting date). They also do not prescribe excessive disclosures, which in the relatively complex areas such as defined benefit pension schemes, are likely to be counter-productive for shareholders.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We agree that it is practical to disclose at face value the scheme interests awarded to directors during the reporting year. An expected value is less clear, due to the assumptions which would have to be both applied and explained.

However, it is important that shareholders are fully aware that face value is not the amount which will eventually be received. The additional disclosures which are proposed go some way to explaining this (such as the maximum award). These additional disclosures could be linked with an explanation of how they work in practice. Preferably, this explanation would be accompanied by information on how actual outcomes have differed from face value in the past, and the factors involved.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

The simplified reporting requirements should save some costs, which would help to offset some of the additional costs of complying with the proposed Regulations (although, as set out in our response to Question 2, we do not believe that these additional costs should be burdensome for companies).

The information disclosed on remuneration will indicate how directors' interests have changed during the year. When reporting year-end interests as well, we believe that comparative figures alongside the year-end ones will also be of assistance to shareholders.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

In the Remuneration Report, any proxy for company performance needs to be both relevant to shareholders, and readily understood. We agree that total shareholder return is a measure which meets these criteria.

There is no explanation why the remuneration of only one director (albeit the Chief Executive Officer) is to be plotted in the graph against the company-wide total figure of shareholder return. It may be more appropriate if, for example, the figure of total remuneration of all executive directors (at least) was used instead. This would be consistent with the rest of the Remuneration Report, which does otherwise provide information about all of the directors, rather than focussing on individual directors.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

The focus of a statutory audit is principally on actual historical figures. Sections of the Annual Report which are more discursive and / or forward-looking are not as conducive to cost-effective, evidence-based auditing, but are read by the auditor for consistency with the view given by the audited financial statements. An example of the latter would be the summary of the Remuneration Report given by the chairman of the Remuneration Committee

(Section 2. of the proposed Regulations).

In view of the above, ACCA agrees that the scope of the statutory audit of the Remuneration Report should be those matters set out in Sections 3 to 12 of the proposed Regulations. The reporting elsewhere, such as the comparison of overall pay and performance (Section 13), is similar to the type of information in the Annual Report which is read by the statutory auditor, but not otherwise subject to detailed audit procedures.

Al R Saneie

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

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Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
Name: A R SANEIE	Organisation:
Email: [redacted]	Address: [redacted] [redacted]

I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
X	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

The policy is a right one and well overdue, but the solutions proposed are complicated and over elaborate. The solution lies within simplicity which in turn means less open to manipulation and interpretation. As we have seen on many occasions it is where policy and framework is open to interpretation when problems occur. It is good idea to change the rules and the structures of reporting on remunerations but somehow we have lost the plot within its details. The aim should not be to set a new framework that is developed further out of the existing framework. The aim should be to totally dismantle the existing structures that have obviously failed and instead develop new frameworks, by thinking quite out of the box. For example - Is a share option at all necessary when the levels of pay are so obviously high!! - Exit Options – why - Unfunded pension schemes – Why And so on. A simple equation/figure which takes into account a certain number of parameters is in my opinion the best way forward and least open to abuse. The answer is in simplicity. These parameters, over the financial year, include The change in the share price, The annual profit, The level of dividend and market capitalisation, existing pay and so on. By reporting on these figures and publishing the consequential remunerations, this report can be concluded in two pages and therefore has every chance of actually being read by all that are interested. It is important to control unrealistic pay demands at the top of the organisation by ensuring that the single multiplier figure applies consistently across the whole of the organisation. Instead of just motivating the CEO/directors we would make the whole of the workforce motivated.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Costs will be minimal if the system is simple to implement and simple to monitor.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

The table of key elements of remuneration must be disclosed to provide transparency and therefore less prone to abuse and misrepresentation.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

There should not be a case for different remuneration based on different scenarios. This is again adding another layer of complexity on pay structures. The aim should be to say if the organisation does well(according to the key elements), then everyone within the organisation would be rewarded the same percentage increment.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

There must be a correlation between different levels of pay depending on rank and responsibility. One useful method would be to have a multiplier of the average pay within the organisation and apply that to the board. This will greatly enhance the clarity of the way pay is calculated.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

Companies do not involve employees views on remuneration policy. However under my proposals, remunerations will be universal within the company as determined by the key financial elements and it is a good idea to publish that within the report for the shareholders approval.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

Yes

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Yes at 75%.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

It will not be commercially sensitive as performance of key figures are already within the public domain in accounts and market updates.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

Yes it should and in any case pension benefits of directors need to be streamlined drastically. This should particularly apply to non executives.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

There are far too many perks and that is exactly what is making the system unmanageable in terms of due diligence and oversight. A directors pay and some pension contribution should be all that is on offer. These are not particularly gifted or clever people. If there were, we would not be in this situation. Many have multiple directorships and part time. They should not be so pampered..

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

As above. Simplify

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

Please refer to question 1

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

A simplified set of figure would be easier to audit. Any figures announced by organisations should be subject to detailed audits. It is important that auditors should be made liable for their work.

Aon Hewitt

BIS Consultation
Date: 26 September 2012
Prepared for: BIS
Prepared by: Aon Hewitt

Directors' Pay - consultation on revised remuneration reporting regulations

Introduction

Aon Hewitt is pleased to submit its response to the above consultation.

By way of background, Aon Hewitt is a global company providing human resource consulting and outsourcing solutions with more than 29,000 professionals in 90 countries.

Our comments below focus on those aspects of the consultation which relate to pension benefits. We have some significant concerns about these proposals as outlined below.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We note that the FRC Lab report of June 2012 considered a number of approaches to the methodology for placing a value on Directors' pension accrual, and did not reach any clear conclusion. There were advantages and disadvantages of the differing approaches (see the FRC report for details) and no consensus on the best approach was reached.

We are therefore surprised that the government is proposing use of the HMRC methodology with little discussion of the advantages and disadvantages.

We are also concerned at the confusion between the HMRC methodologies for testing total benefits against the Lifetime Allowance and for testing one year's benefit accrual against the Annual Allowance. For example, paragraph 67 refers to the use of the HMRC methodology for assessing lifetime limits, whereas note 20 to this paragraph and following paragraphs refer to Annual Allowance methods. This does not reassure us that the proposals have been well thought through.

We acknowledge that multiplying pension accrual (net of inflation) by 20 appears to be the simplest and most easily understood of the methods. However, as has been identified during protracted exchanges between the pensions industry and HMRC about the calculation on the Pension Input Amount for the purpose of Annual Allowance, calculations of the amount of pension accrual under the HMRC rules can give anomalous results. We feel that it is unlikely that the audience consulted by the FRC Lab would have been aware of these complications. (We have not yet reached the first deadline for the reporting of Pension Input Amounts to scheme members.) It is therefore likely that this audience believed that the HMRC rules would lead to more consistency between companies than is likely to be the case.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach cont/…?

For example, the references in the HMRC rules to the pension payable at the year end *on the assumption that the director's age is equal to his or her retirement age* gives rise to some odd deemed accrual patterns. For example, for schemes where the rules provide a 2/3 pension at normal retirement age, with the pension on early withdrawal calculated as this rated down by completed service over potential service, the HMRC rules define the whole pension as being accrued on the day of joining the pension scheme (due to the reference to treating the calculation as being done as if the employee's age is equal to the normal retirement age). If adopted, this could lead to the whole pension accrual as being treated as before the date of being appointed a director, with no accrual while a director. Is this really sensible?

Enhancement of pension on early retirement, for example by eliminating the reduction normally applied to reflect early payment, would be treated as having no value under the HMRC methodology. (The pension is worth more by being paid early, even if the amount of pension has not increased.) **The value of the enhancement of pensions on exit/retirement seems to be exactly the kind of material information which investors would want to be reported.** For example for schemes where early retirement reductions are not applied it is not unusual for this to lead to an increase in the value of a pension of 20%, so for some Directors this would be worth millions of pounds and should be allowed for.

As noted in the consultation paper, the application of the HMRC methodology to non-UK pension plans, with different provisions relating to inflation protection etc is likely to produce values for disclosure that may bear little resemblance to the actual value of those benefits. We would also note that similar issues apply in UK schemes, where different schemes have very different pension increases in deferment, pension increases in payment, Normal Retirement Ages, early retirement policies, spouse's pensions etc. These difference in the value of these different pension benefits would be ignored in the simple approach being suggested.

We would therefore recommend placing a value on the benefits accrued based on either the transfer value or pension accounting assumptions, in line with IAS 24 (consideration of whether to allow for future salary growth and generous early retirement terms will also be required). We acknowledge that the resulting value can vary from one year to the next as market yields change. However, this variation reflects real changes in the cost of providing the benefits, so should not be seen as a problem with these approaches. **We would strongly recommend requiring disclosure of:**

- **the value of the increase in accrued benefits (net of inflation) NOT**
- **the value of the benefit at the year end less the value of the benefit at the beginning of the year.**

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Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach cont/…?

This is because under the second approach the figure reflects the change in the value of the benefit already accrued at the beginning of the year due to the change in market yields, as well as due to the increase over the year in the amount of the benefits. It is including the impact on the value of assumption changes over the year that can make the amounts reported volatile and difficult to explain and understand. This is avoided under the first approach (which is that already adopted under the Listing Rules).

In the light of our views that the requirements should not be based on the HMRC methodology built into the draft Regulations, we have not reviewed these draft Regulations in detail. However, we would flag the following comments (which will not be comprehensive) which occurred to us on a brief scan:

- the provisions do not cater for cash balance plans
- the cross-reference imports a multiplier of 16, not 20 - which appears not to be what is intended
- although the consultation paper only refers to placing a value on unfunded as well as on funded benefits, we suspect you would want a value to be placed on funded non-registered benefits as well as on unfunded non-registered benefits
- the HMRC methodology places a nil value on benefits in both unfunded schemes and in funded but non-registered schemes – which appears not to be what is intended
- the HMRC methodology which is cross-referenced relates to the increase in accrued benefits over the pension input period (as defined for each pension arrangement) ending in the relevant tax year; there may be different pension input periods for the various pension arrangements for a particular individual; if pension input period end dates are amended, one tax year can pick up the pension input from more than one pension input period from an arrangement – this does not seem appropriate for inclusion in a comprehensive remuneration figure in respect of the company's financial year.
- the cross-reference to 7(4)(a) in 7(5) appears to be wrong

We would also suggest clarifying the requirements where an individual becomes a director part way through the company's financial year or steps down part way through the year, including the requirements in relation to benefits accrued before becoming a director and after stepping down as a director. Is the accrual during the year before/after becoming a director excluded? In relation to increases in pensionable pay on becoming a director and/or while a director, is the impact on the benefit accrued before becoming a director included as well as the impact on the benefit accrued while a director? Is the value based on financial conditions at the year end or at the date of ceasing to be a director?

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Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach cont/…?

Above all, we believe that it is vital that the government and the Stock Exchange work together to reach agreement on a consistent framework for placing a value on and for disclosure of Directors' pension accrual. The current inconsistencies between the requirements under the Companies Act and under the Listing Rules generate unnecessary costs, unnecessarily lengthy disclosures, and serve to confuse readers.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We agree that the value attributed to the final salary pension accrued by a director will not provide as complete a picture of the director's pension scheme accrual as will the contribution paid to a money purchase pension scheme. However, we do not think disclosure of the year end pension amount provides sufficient information. A large year end pension could reflect pension accrual over many years before becoming a director, or it could reflect a rapid rate of accrual over the last year or two. We believe that the disclosure should be extended to require disclosure of the increase in the accrued pension over the year (net of inflation*) in addition to disclosure of the year end pension. (*The inflation figure used should be consistent with that used in valuing the pension accrual.)

We note that this would be consistent with the current Listing Rules. More generally, as noted in relation to Question 8 above, we believe it is important that the requirements of the Companies Act and of the Listing Rules should be consistent in relation to both the valuation of pension accrual and the disclosures required.

The disclosure should be required for all defined benefit pension rights (where defined benefit pension rights are everything that is not a pure money purchase pension scheme), not just for final salary pensions.

We recognise that the reference to the pension payable at the year end on the assumption that the director's age is equal to his or her retirement age matches the basis on which the consultation paper proposes that a value is attributed to the pension. However, as discussed above under Question 8, this will lead to anomalous results, with the disclosed pension in some cases far higher than that to which the director would actually be entitled on withdrawal or early retirement. In these cases, there would appear to be no increase in the pension from one year to the next other than that due to salary linking. We therefore believe that the pension amount disclosed should be that payable on withdrawal. Disclosure also of the normal pension age would also be helpful.

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Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors cont/…?	We recognise that the reference to the pension payable at the year end on the assumption that the director's age is equal to his or her retirement age matches the basis on which the consultation paper proposes that a value is attributed to the pension. However, as discussed above under Question 8, this will lead to anomalous results, with the disclosed pension in some cases far higher than that to which the director would actually be entitled on withdrawal or early retirement. In these cases, there would appear to be no increase in the pension from one year to the next other than that due to salary linking. We therefore believe that the pension amount disclosed should be that payable on withdrawal. Disclosure also of the normal pension age would also be helpful. The reference to the "*value of the additional benefit*" payable on early retirement could be misleading. In general, payment of a reduced pension on early retirement would be expected to provide the same value to the director as the accrued pension payable at normal pension age. Disclosure should therefore be required of any entitlement or practice of paying early retirement pensions before normal pension age with no reduction for early payment or a reduction that is lower than the cost neutral reduction, as well as of any additional pension payable on early retirement. It is not clear whether your comments at paragraph 80 were intended to require such disclosure.

Association of British Insurers

Association of British Insurers

Department for Business, Innovation, and Skills

Directors' Pay: Consultation on revised remuneration reporting regulations

The ABI's Response

Introduction

The UK Insurance Industry

The UK insurance industry is the third largest in the world and the largest in Europe. It is a vital part of the UK economy, managing investments amounting to 26% of the UK's total net worth and contributing £10.4 billion in taxes to the Government. Employing over 290,000 people in the UK alone, the insurance industry is also one of this country's major exporters, with 28% of its net premium income coming from overseas business.

Insurance helps individuals and businesses protect themselves against the everyday risks they face, enabling people to own homes, travel overseas, provide for a financially secure future and run businesses. Insurance underpins a healthy and prosperous society, enabling businesses and individuals to thrive, safe in the knowledge that problems can be handled and risks carefully managed. Every day, our members pay out £147 million in benefits to pensioners and long-term savers as well as £60 million in general insurance claims.

The ABI

The ABI is the voice of insurance, representing the general insurance, protection, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 300 members, accounting for some 90% of premiums in the UK.

The ABI's role is to:

- Be the voice of the UK insurance industry, leading debate and speaking up for insurers.

- Represent the UK insurance industry to government, regulators and policy makers in the UK, EU and internationally, driving effective public policy and regulation.

- Advocate high standards of customer service within the industry and provide useful information to the public about insurance.

- Promote the benefits of insurance to the government, regulators, policy makers and the public.

Main Comments

The ABI is supportive of the Government's policy objective to give shareholders more influence on executive pay and allow them to make informed voting decisions. We believe that these draft regulations meet the Government's aims. They will give shareholders more information to ensure that the remuneration policy is aligned with the company's strategy and that there is an appropriate link between pay and performance. This will help shareholders make fully informed voting decisions on remuneration matters.

However, we are concerned that the proposals could encourage boiler plate or legalistic disclosures. Investors believe that, at present, the most informative reporting is the narrative aspects of the remuneration report, where the Remuneration Committee articulates the Company's remuneration strategy, why the Committee has chosen the approach it has and why its decisions are in the best interests of the Company and shareholders.

We are supportive of the general approach and the majority of the proposals made by the Government, but we have provided some suggestions which will allow shareholders to get the most out of the new Remuneration Reports. We believe that the regulations should require the Policy Table to be disclosed annually, even if it is not subject to the binding vote. This will make it easier for shareholders to locate the policy currently in force and allow them to make a judgement on how it has been implemented. Our Members believe that the Distribution Table should be moved to the Implementation Report, so that shareholders can put the Committee's decisions on variable remuneration into context on an annual basis. Finally we believe that the proposed Scenario Analysis could be improved if the Government prescribed the method currently used by, for example, Tate & Lyle. Their disclosures provide monetary values and percentage of salary at each level of performance for each element of pay. We believe that this approach is more helpful than a bar chart and gives a more useful portrayal of likely pay-outs under each element of pay and at each level of performance.

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

It is not the role of Investors to micromanage companies. It is the role of the Board and the Remuneration Committee to set the remuneration policy and make decisions on what individuals should be paid. Shareholders expect the Remuneration Committee to protect and promote their interests in setting executive remuneration and to scrutinise but not micro-manage this important part of the Non-Executive Directors' responsibilities.

The ABI is supportive of the Government's policy objective to give shareholders more influence on executive pay by making informed voting decisions. We believe that these draft regulations meet the Government's aims. They will give shareholders more information to ensure that the remuneration policy is aligned with the company's strategy and that there is an appropriate link between pay and performance. This will help shareholders make fully informed voting decisions on remuneration matters. The draft regulations will provide additional information for all listed companies on a consistent basis. This will mean that the overall level of reporting should improve with all companies providing this type of information rather than the best reporters only.

The consultation documents states that some remuneration reports are lengthy and complex, with facts and figures buried. Whilst we agree with this to a certain degree and that increased consistency will be beneficial, we are concerned that the proposals could encourage boiler plate or legalistic disclosures. Investors believe that the most informative reporting at present is the narrative aspects of the remuneration report, where the Remuneration Committee clearly articulate the Company's remuneration strategy, why the Committee have chosen the approach they have and why their decisions are in the best interests of the Company and shareholders. Whilst we recognise that regulation on reporting can only do so much, investors have a role in outlining the disclosure which they require. Members want to ensure that the new reporting requirements result in meaningful and enlightened disclosures for shareholders rather than being seen as a compliance exercise by companies. In addition, investors are wary that the new reporting requirements will lead to the establishment of a new industry to help in the production of Remuneration Reports. This would not be beneficial to investors.

Under the current regulations, there is a requirement for the Company to outline the overall remuneration policy. We believe that it would be beneficial to include some comments on the Committee's overall remuneration policy (and not just the individual elements as outlined in the policy table) within the Remuneration Committee Chairman's statement. For example, some companies currently outline what is their remuneration philosophy, what are the key aims and objectives of the remuneration policy, how it is linked to the business strategy and how the overall package is positioned compared to the Company's peers.

We recommend these arrangements be subject to a full review after three years to ensure that the reporting requirements put in place are promoting the right behaviours and providing the right information for shareholders.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

We agree with the consultation that the majority of information required in the policy table under the legislation is already contained in the Remuneration Reports of the companies who are seen as the best reporters. There may be some costs to put it into the new format. Some companies may argue that there will be a significant cost of implementation; this may be because they are not currently providing this information. But, as noted above, the provision of the information will be a benefit to shareholders to allow them to make informed voting decisions.

For almost all companies, the requirements on service contracts, exit payments and the distribution table are new requirements with very few, if any, companies actually providing these disclosures at present. We do not, however, see how these additional requirements will lead to a significant cost to companies.

Some companies, particularly smaller companies, have informed us that they believe that the new regulations will require them to get extra advice from remuneration consultants to ensure that their policy report meets the legislation and the needs of investors. While we can understand that some companies will want to ensure that they are providing the right disclosures under the new legislation, by either engaging remuneration consultants or consulting with their largest shareholders, we do not believe that this will lead to significant on-going costs for companies.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

As stated previously, it is not for the Government or Investors to micromanage companies. It is the role of the Board and the Remuneration Committee to set the remuneration policy and make decisions on what individuals should be paid. We consider that it is not the role of the Government to prescribe the level of detail to be outlined in the table. This will be for shareholders and companies to decide, but shareholders will want sufficient detail to ensure that policy is appropriate, whilst ensuring the company has sufficient flexibility for companies to attract and retain talent. This balance of disclosure needs to be worked out between shareholders and companies and may differ between companies. The ABI is committed to moving the debate forward and proposes to provide guidance to companies on what our members, as significant investors, will expect under the new reporting requirements. This will ensure that investors are getting the right level of detail to make informed voting decisions.

Members have a number of suggestions which they believe will improve the draft requirements to the benefit of shareholders:

1) Currently the legislation requires companies only to disclose this table in years when they are putting the Policy Report to a vote (at least once every three years). We believe that there would be considerable benefit in requiring companies to put this table in the Remuneration Report each year; this will mean that shareholders will be able quickly to locate the current policy in operation. This should not create an additional burden for companies, but that it will be beneficial for investors to know the exact policy which is currently in force. It would also be informative to shareholders for companies to disclose the scenario analysis and distribution chart on an annual basis. These disclosures will aid shareholders’ understanding of the policy and outcomes, improving disclosure on the relationship between pay and performance over time.

2) We believe that if the Company is putting the Policy Report to a vote, then it should be required to explicitly state if the existing policy is being changed and why. This will mean that shareholders will get a clear understanding of the proposed changes and why they are being proposed. This will be helpful for shareholders to assess if the changes in the policy are appropriate. The draft regulations require the Policy Table to include any changes to policy. Members are concerned that the disclosures in this table will not give the level of detail they require to make an informed voting decision.

3) Members believe that companies should be required to outline the policy that they have for the recruitment of new Directors. This may include the provision of exceptional grant levels under the long term incentives on recruitment, the treatment of any recruitment awards, particularly what performance conditions would be attached, and how the Committee will calculate the size of such awards based on the forfeiture of awards from a previous employer.

4) The majority of companies currently disclose both the performance metrics and actual performance conditions used under the long term incentive schemes. The current drafting of the regulations does not require actual long term incentive performance conditions to be disclosed in the Policy Table. There is a concern that this could lead to less disclosure by some companies and we are concerned that current best practice could be lost.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Investors believe that there could be benefit in requiring additional information on service contracts. Currently, disclosures are mostly of a boiler plate nature, confirming that the contracts do not provide notice periods greater than twelve months and any special circumstances on change of control or specific provisions on termination. The requirement to provide details of any contractual payments under the service contract will be of particular importance, given that any payments will have to be in accordance with the Remuneration Policy agreed by shareholders. These disclosures will help shareholders to ensure that there is no payment for failure.

We support the requirement for the distribution table and feel that it would be helpful to put executive remuneration into the appropriate context of the change in profit, pay generally and dividends. We think that this table would be better represented in the Implementation Report, as this will put into context the decision the Committee has made on variable remuneration during the year under review. If it is included in the Policy Report, it will only be required when the Company's remuneration policy is put to the binding vote, once every three years. Investors believe that this information should be disclosed annually.

Whilst we believe that the scenario analysis will be useful, we do not think the proposed chart is the most appropriate. The most informative disclosure we have seen on scenarios is the approach taken by Tate & Lyle. Which provides both monetary amounts and percentage of salary at below threshold, threshold, mid-range and stretch – see the attached table. We believe that this approach is more helpful than a bar chart and gives a more useful portrayal of likely pay-outs under each element of pay and at each level of performance. Members believe that it would be informative to outline the performance required to achieve on target and maximum, within these disclosures.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We strongly believe that there should be improved disclosure on executive contracts, including contractual terms on exit and the Remuneration Committee's policy on exit payments. This is critical if the policy is to be comprehensive and to tackle payment for failure.

We believe that the proposed disclosures cover the appropriate information. However, the key requirement for investors is understanding how the Committee will categorise departing Executives as either a good or bad leaver. This should include an explicit definition of what a good and bad leaver is. Disclosure on the resulting treatment of each element of pay under both types of leaver situations is also important, but we believe that the proposed requirements are appropriate.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

Investors expect companies to ensure they have a well-motivated and engaged workforce. The Board and Remuneration Committee should be conscious of any disparity in treatment of employees compared to the Executive Directors, for example in pension provision, and the impact their remuneration decisions for the Executive Directors have on the general workforce. Each Company is different and will have workforces which differ in terms of size, geographical spread and diversity. We do not believe that there is any merit in specifying requirements on employee engagement. Of more interest to shareholders is how changes in the basic salary of the Executives compare to changes in the workforce more generally. In recent years, shareholders have been monitoring the link between executive wage inflation and the increase in salaries elsewhere in the Group.

Therefore we welcome the proposals for setting remuneration policies within the wider employee context but do not believe that there is a case for requiring for all companies to consult with employees. If individual companies believe that it is valuable in ensuring a motivated and engaged workforce then shareholders would welcome this.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

The ABI were consulted and provided significant input to the FRC Reporting Lab project and report into the single figure. We are supportive of the approach proposed by the Government in the consultation document. We believe that the consistent and standard approach outlined in the consultation document will mean that investors will be able to get an understanding of the amounts received by directors in one particular year. The important aspect is that every company takes on this consistent approach year on year, which will mean that we have a figure which can be used across companies and within the same company year on year.

We believe that the most important aspect is for companies to explain the amounts being paid under each element of pay, why the payment is merited and why the Committee has taken the decisions it has. The approach outlined is the appropriate method for calculation and has been agreed following a consultation with major investors and companies.

We note that the regulations do not explicitly require the inclusion in the single figure of some irregular payments and any deductions (such as clawback). It is important to ensure that all payments or deductions (that related to that financial year) are accounted for in the single figure. These may include: recruitment awards (either in cash or shares), compensation for loss of office, discretionary bonuses etc.

The Company should be required to disclose the single figure for the previous financial year as well as for the financial year being reported on. Additional disclosure should be required if a previous year's single figure is being restated for any reason or the clawback of previous awards received has been triggered.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

This was subject to the FRC Financial Reporting Lab consultation and there was significant debate about the right approach. We believe that the HMRC-style multiplier and applying a 20 times multiple should give a reasonable estimate of the value of the increase in the Defined Benefit pension benefit, deliver comparability across different companies and avoid extraneous noise. It is therefore the ABI's preferred approach.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We believe that clawback should be reported in the Director's Remuneration Report but not included in the single figure, unless it relates to awards vesting in the financial year being reported on. It is likely that clawback will relate to performance in previous reporting periods, whereas the single figure will show payment for performance in the current period. Therefore, the disclosures on remuneration for the current financial period will be reduced as a result of the implementation of clawback. It is more beneficial to know what is being paid in the current period without being reduced by the implementation of clawback in previous years.

We believe that the single figure for the current year should not be amended. But the clawback amount should be required to be disclosed separately. As outlined in our response to question 7, the previous year's single figure which includes the award which has been subject to clawback should be restated. There should be supporting disclosures on the reasons for and outcomes of the use of clawback.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

ABI members have always been firm believers that the performance measures and conditions should be disclosed, if there are issues over commercial sensitivities then they should be disclosed retrospectively. Outlined below are the relevant parts of the ABI's Principles of Remuneration:

> *Annual bonuses should exist to reward contribution to the business during the year above the level expected for being in receipt of a salary……The measurements chosen should be quantifiable and the targets chosen should be set at the start of the year. The performance measures and targets should be publicly disclosed. If the targets are considered to be commercially sensitive they should be disclosed retrospectively.*
>
> *Long-term incentives exist to reward the successful implementation of strategy and the creation of shareholder value over a period appropriate to the strategic objectives of the company. Performance measures and vesting conditions should be fully explained and be clearly linked to the achievement of appropriately challenging financial performance which will lead to enhancement of shareholder value. The definition and calculation of any performance measurement should be clearly disclosed.*
>
> *Shareholders believe that companies should clearly disclose and justify the performance measures chosen and the related targets. Where consideration of commercial confidentiality may prevent a fuller disclosure of specific short-term targets at the start of the performance period, shareholders expect to be informed of the main performance parameters, both corporate and personal, for the financial year being reported on.*
>
> *Following payment of the bonus, shareholders will expect to see a full analysis in the Remuneration Report of the extent to which the relevant targets were actually met.*

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We acknowledge that the defined benefit pension benefit included in the single figure (using the 20 times HMRC approach) will give an indication of the pension benefit provided to the executives. However, we believe that there is merit in requiring companies to disclose fully the defined benefit pension benefits which the executives will receive. This will ensure that shareholders have full details on the benefits, accrual rates, any provision for early retirement etc. which Executive Directors can receive under the relevant pension scheme.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We are supportive of the approach to disclose scheme interests at face value. We believe that this is a more meaningful and transparent disclosure than using an expected value. Under expected value, shareholders rarely are informed of the underlying assumptions or estimates used to calculate the expected value. Disclosing grants on a face value basis is more comparable and is the means that most companies disclose their grant size.

It is best practice for companies to report the level of their award on a face value basis and the ABI principles reflect this.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

There is merit in requiring companies to outline the Remuneration Committee's policy on share ownership requirements and if the individual directors have met that requirement. It will be useful to shareholders if the company disclose the monetary value of the shares the executives hold at the year end, based on the share price at that time. There may also be benefit in requiring companies to provide further information on what approach the Committee is taking to ensure that the requirements will be met, going forward.

Shareholders find the current disclosures on outstanding share awards useful, particularly, the details on the date of grant, share price at time of grant and under which scheme awards were made. Members want to ensure that the details in these tables are not lost.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We agree that the current TSR chart provides limited benefit.

There are a number of different performance measures which could be chosen and some will be more appropriate for some companies and their strategies than others. TSR is seen by some investors as a general proxy for a Company's performance and its perception in the market. There may be benefits to showing the correlation between TSR performance and CEO pay to see if there is a disconnect between pay and performance. Most investors will carry out their own analysis of the link between pay and performance based on the performance measures, which they consider to be the most important based on the individual circumstances of the company. The measure of CEO pay should be the single figure. If the company has had more than one Chief Executive during the 10 year performance period, the chart should be annotated to provide this information.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We are supportive of the proposed approach.

Association of Consulting Actuaries

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26 September 2012

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
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Dear Mr Walker

DIRECTORS' PAY: REVISED REMUNERATION REPORTING REGULATIONS

I am writing on behalf of the Association of Consulting Actuaries (ACA) in response to the consultation paper issued in June 2012 containing proposed changes to theremuneration reporting regulations.

Members of the ACA provide advice to thousands of pension schemes, including most of the country's largest schemes. Members of the Association are all qualified actuaries and are subject to the Actuaries' Code of the Institute and Faculty of Actuaries. Advice given to clients is independent and impartial. ACA members include the scheme actuaries to schemes covering the majority of members of defined benefit pension schemes.

The ACA is the representative body for consulting actuaries, whilst the Institute and Faculty of Actuaries is the professional body.

We have limited our responses to the questions relating to the disclosure of directors' pension arrangements. Our detailed response is set out in the appendix to this letter.

Overall we are concerned at three levels:

- We believe that a cash-equivalent based system is the best approach to providing appropriate information to shareholders about defined benefit pensions; but that the current system should be reformed by making it consistent with the approach that has been used for many years under the Listing Rules. It should not be replaced by the HMRC methodology which is inappropriate for the purpose and will substantially mislead shareholders.

  We expand upon this in our answer to Question 8.

- We believe that the policy process by which you arrived at putting forward the HMRC methodology is flawed.

  The Lab Project report by the Financial Reporting Council shows that companies did not want the HMRC methodology used at all. They were split between two methods that seek to place a realistic and market-related value on the pension accrued during the year. It seems strange that a completely arbitrary approach is being proposed because the companies could not decide which of the other two methods to champion. In addition the supposed advantages of the HMRC methodology put forwards by the investor group have not been properly tested. The HMRC methodology will not deliver a figure that relates to the benefit received by the individual. So whilst this approach could be designed so that it is applied "consistently across all companies" it would be at the price of a complete masking of differences in the benefits that are accruing. We say more about this in our answer to Question 8.

  We would have liked to have been involved in the pre-consultation. It is not clear to us whether any pension industry bodies were invited to participate.

- If you do decide to use the HMRC methodology, we would be very concerned with the proposed way in which the policy intention is to be delivered.

  The regulations as drafted seem unworkable as a means by which to determine the pension values to report. This is primarily because there is an inadequate cross-referencing to the Annual Allowance methodology set out in the Finance Act 2004.We expand upon this in our answer to Question 1.

  If you do decide to adopt the HMRC methodology, the Pensions Taxation Committee of the ACA would like to work with you on the actual implementation to minimise distortions and unintended consequences that are likely to follow from simple cross-referencing to what is already a very complex method to apply in practice and which has generated a great deal of correspondence with HMRC, a lot of which remains on-going.

We hope that you find our comments of assistance and would be happy to discuss them further if that is helpful. You can contact me on 020 7432 6635 (david.everett@lcp.uk.com) or my colleague Karen Goldschmidt (chair of the ACA Pensions Taxation Committee) on 020 7432 6622 (karen.goldschmidt@lcp.uk.com).

Yours sincerely

David Everett

David Everett
Chairman
ACA Pension Schemes Committee

Sent by e-mail to executive.pay@bis.gsi.gov.uk

APPENDIX: ACA RESPONSES TO SPECIFIC QUESTIONS

We have only addressed questions 1, 8 and 11, being the questions that directly relate to pensions but we address 8 and 11 first given their importance.

***Question 8**: The Government proposes the application of the HMRC methodology towork out the value of defined benefit pension schemes. Is this a practical andinformative approach?*

Our view is emphatically that using the HMRC methodology is not informative in the context of the aim of the disclosure, and has practical problems too. We address this question in two parts – by looking at the difficulties with the current system, which could be easily addressed, and noting the advantages of such a modified cash equivalent based system; and then commenting on the HMRC methodology.

The current cash equivalent-based system should be reformed – not replaced

We do not see that a valid case has been made for a move away from a system based on valuing the increase in the director's pension benefit over the year using a cash equivalent transfer value basis. The reported debate on the matter was inconclusive.

A cash equivalent is the best available way of encapsulating the quality of benefits deliverable as well as their amount; of identifying changes to those qualities; and of identifying the value of enhancements such as early retirement on generous terms.

A cash equivalent value does move with investment markets so can be volatile, but the same can be said about the valuation of other components of a director's remuneration. For example, the value of long term incentive plans is to be based on the market value of the shares at the relevant date, or an estimate of totalmarket value if not yet vested. These figures are likely to be as volatile as or more volatile than pension cash equivalents based on market interest rates.

Where we would like to see a change is in the way in which the cash equivalent approach is applied. Currently there are unnecessary inconsistencies between the Large Companies Regulations and the Listing Rules (even though both are “cash equivalent - based” methods), which has resulted in the need for confusing dual disclosures to date. The approach used by the Listing Rules makes better sense and fulfils the intended purpose. Under it the cash equivalent (less director’s contributions) at the year end of the increase in accrued benefits (excluding inflation) is disclosed, whereas under the Large Companies Regulations the cash equivalent at the beginning of the year and the director’s contributions are subtracted from the cash equivalent at the end of the year. In other words the Large Companies Regulations require “the difference in valuation between that at the end of the year and that at the start of the year”, whilst the Listing Rules require “the valuation, at one time, of the increase in benefit entitlement over the year”.

The Large Companies Regulations will generallyproduce an inappropriately bigger figure than the Listing Rules due to the unwinding of the discount rate (in the end year figure) used to determine cash equivalents as well as not excluding the impact of inflation. Both exclusions are anomalous in our view in the context of understanding the remuneration delivered “for” the year – the first being essentially a charge for getting older even where there is absolutely no change in the amount of benefit dueon ultimate retirement.

The Large Companies Regulations can also lead to anomalies due tochanges in financial conditions/transfer value bases between year ends. Negative figures can typically be generated, if for example, giltyields rise during the year (by contrast the fall in gilt yields in recent years have resulted in disclosed pension costs that are too high). The Listing Rules by contrast use one consistent basis – the end year one – to place a value on the benefit accrued during the year and so do not suffer from these distortions.

The Large Companies Regulations also fail to allow for the offsetting of any transfers-in received during the year, or for benefit payments during the year of retirement. The Large Companies Regulations also do not contain the (desirable) statement that reductions in transfer values due to scheme under-funding should be ignored. The Listing Rules do.

We think that all these long-standing failings in theLarge Companies Regulations should and can simply be addressed by a move to the cash equivalent approach already established in the Listing Rules.

Overall this provides a method that best reflects the quality of benefit (and improvements in those); and is already in place so is relatively easy to continue.

We acknowledge that it is not “perfect” for the purpose. Some disadvantages include: inconsistencies in valuations due to the different assumptions used by different schemes (noting that these are set by the trustees of the scheme, not the company); changes in market conditions and member’s age donot change the benefits awarded, but the cost of the benefits does change; and in deciding between this approach and say the IAS19-based approach, there is the underlying issue of the purpose of the disclosures.

However, the advantages strongly outweigh the disadvantages, especially as compared to the new inconsistencies that would be introduced by the HMRC methodology.

The HMRC methodology is neither informative nor practical as a basis for disclosure of pension costs

We have a number of concerns with the HMRC methodology, all important and material.

A single multiplier masks the quality of the benefits

We were surprised by the proposal to use asingle multiplier (whether 16:1 or, as proposed, 20:1) to place a value on defined benefit pension rights.

(In passing we cannot see any detailed rationale within the consultation paper as to why 20:1 should have been chosen over 16:1 (the latter being used for Annual Allowance testing of defined benefit pension accrual).)

This seemsan extreme approach, given that the different possible components of pension design may lead to a very different value of the benefit to the director, and a very different cost to the company. For example:

- a pension paid from 60 may cost 30% more than the same amount paid from 65;
- a pension which carries the right to 5% increases a year once in payment may cost 30% more than a pension carrying 2.5% (or in line with Consumer Price Inflation if lower) increases;
- a pension carrying a spouse's pension entitlement on death may cost 20% more than a pension carrying none.

Compounding these three, it is possible for one director to be disclosed as entitled to pension benefits that have the same value as those of another director, when the actual value of one could be twice the value of the other. The difference could be more extreme if the director's age was taken into account – the value of an amount of pension to be paid to a 40 year old is significantly lower than the value to a 50 year old.We do not think that this quantum of error would be acceptable in valuing other director's benefits, such as share schemes, and we do not think it is appropriate for pensions either.

As identified in the consultation document, the issue can be more pronounced if non-UK pension arrangements are brought into the frame, where pension design can be more diverse.

The HMRC methodology(because of the use of the single factor, and other reasons) also ignores advantageous value when early pension is drawn – we address this later – and also if the terms for exchange of pension for lump sum are generous.

It is proposed that the fixed factor is applied to the deemed accrued retirement benefit calculated using the HMRC methodology. We have considerable concerns with this as you will see from the following.

The HMRC methodology is not simple to apply

The Consultation document states (para 68) that "This methodology also has the benefit of being an accepted and comparable methodology that is easy to calculate". Clearly,a methodology on which tax is based should be "easy" or at least unambiguous to follow.

But in practice theAnnual Allowance tax law was substantially changed with new provision inthe Finance Act 2011; and the parts left unchanged from the 2006 legislation had little use before because few individuals reached the old £200,000+ Annual Allowance. The interaction of the current legislation with scheme rules and typical benefit designs is only now emerging and is proving to bevery complex. HMRC have had to issue much guidance. More than a year after its enactment (so one tax year impacted and not yet past the reporting deadlines), answers to central queries are still awaited from HMRC; and answered queries have shown up unexpected answers, as well as someunintended elements to the legislation which are being addressed in some way in the Finance Act 2013 and regulations. Other issues may arise as the Annual Allowance legislation is tested further. Even with the HMRC guidance, legal advice can be needed to interpret the positionfor an individual.

The HMRC methodology was not designed for directors' disclosures

The Annual Allowance tax law is designed to achieve a certain tax behaviour and consequent tax take. To a large extent this was to discourage tax deductible pension contributions beyond £50,000 pa and not necessarily to tax any excess on a "fair" evaluation (hence for example the adoption of a simplified single multiplier, and some other points raised below). HM Treasury found this acceptable for tax purposes but it is inappropriate as a basis for disclosure.

The HMRC methodology can give unnatural results and result in different disclosures for identical benefits

It is concerning that the outcome can be "unnatural", sometimes depending solely on how scheme rules are worded or structured. An accrual fraction expressed as 1/60thsper year of service might have to be read differently as one expressed effectively as 1/40ths x 2/3rds. An individual who to all intents and purposes is accruing additional pension in respect of service might be treated as no longer accruing pension, or accruing substantially more than is the case. The numbers emerging can be different for individuals who for all real purposes build up the same benefits.This does not happen for the simpler scales; but it can happen particularly in relation to a certain type of wording of a benefit promise that is not an uncommon one for defined benefit promises to senior executives. The differences can be substantial. More on this can be found in HMRC's guidance (particularly at RPSM06107035 and also RPSM06107100).

Trustees' decisions can result in different disclosures for identical benefits

In connection with (4) – and the precise wording in the rules mattering –HMRC acknowledge in their guidance (at RPSM06107035),that Annual Allowance figures could also changeif *trustees "change the wording of their rules expressing accrual* ***(without such a rule change actually affecting the benefit due to be paid)*** *for certain members".*

There are other waysthat numbers may depend on trustees' decisions for a scheme (for example a decision by trustees on "arrangements" for tax purposes, effectively the "units" by which pension tax calculations are broken up for a particular member of a scheme).The Trustees' decisions can mean that the numbers emerging can be different for individuals who are building up precisely the same benefits in different schemes.

Additional work will be required

It might have been argued that if this type of calculation already has to be done for an individual by a scheme, the approach can use these calculations and hence save work. We disagree. The financial year will often not correspond to the period (Pension Input Period) over which a director's Annual Allowance figures have to be calculated (which can, as well as causing extra work, introduce extra complexities); and for those directors who may not have input over the Annual Allowance there may now be a requirement for exact calculations when an approximate test was all that was needed to ensure that an Annual Allowance charge was not payable.

The approach is at odds with accounting disclosures

We also draw to your attention an accounting standard IAS 24 (Related Party Disclosures), where related parties include key management personnel. The IAS 24 requirements are quite vague in the detail but are broadly that compensation provided to key management is disclosed in accordance with IAS 19 and IFRS 2 (Share-based Payment) as appropriate. The HMRC methodology is at odds with the requirements of IAS 24 which means companies would report two quite different figures which supposedly represent the same pension accrual – ie. the cost to the company is calculated in line with the principles of IAS 19, yet the value received by the director uses a broad brush factor of 20.
However we do note that our preferred approach (cash equivalent based) would also be at odds.

***Question 11**: Will the Government's proposed disclosure requirements on pensions leadto reporting of sufficient information on the benefits received by directors?*

1. We do not understand yourintended policy on accrued pension disclosure

We found the wording of paragraph 80 of the consultation paper, and Regulation 10(2) of the draft regulations, very confusing. We think that the wording is trying to say that the directors' remuneration report should include information for each director similar to what is required by the current regulations.We suggest a reversion to the wording which appears in the current legislation and for you to go on to define what you mean by "accrued benefit" – for example is it the leaver benefit had the member left at the end of the year, assuming that the individual will then draw the benefit at normal retirement date but ignoring any revaluation due in the interim?

And in fact we think that the normal retirement date reference should be to the earliest age at which the individual has a right to draw all retirement benefit from the scheme without reduction for age – which might be called"normal pension age" although this is not a generically defined term.

We have assumed that the intention in this section was to state the benefit due, not a valuation; but this is not total clear from the drafting.

We note that, for the reasons to be given in our answer to Question 1 below, this accrued pension (which seems the appropriate disclosure) may well be very different from the "HMRC methodology pension" and hence on which "value" was based.

We do not understand how to undertake the early retirement disclosure, in the context of the proposed HMRC methodology

We now turn to Regulation 10(3). This says that the report should state "The total value of any additional benefit that will become receivable to a director in the event that thatdirector retires early". It is not clear what to do, particularly in the context of using the HMRC methodology. For example:

- How exactly is the additional benefit determined?

- How should any additional benefit be valued? By using the 20:1 factor?
- What early retirement date is being assumed? A notional one at the end of the year, or the earliest possible one not earlier than this?
- Is the early retirement date the earliest at which the director can go without company consent?

If the cash equivalent methodology were maintained (modified as suggested), these confusions could be resolved. The cash equivalent valuation would already reflect the earliest age that an individual can draw benefits unreduced ("normal pension age"); and that age could be explicitly disclosed. To the extent that extra value might be delivered were the individual to retire even earlier (eg by promised generous factors), this could be shown by the improvement in the total cash equivalent were the individual to retire immediately (or such later age allowed for earliest retirement not on grounds of illhealth).

Question 1*: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document*

We address this question in the context of the proposals relating to pensions.

We mainly focus our comments on Regulation 6(c) and whether it achieves a mechanism that fulfils your proposed policy (which we don't support – see above) and whether it can be used unambiguously.

The draft uses shortcuts to try to pick out certain but not all parts of the tax law. If it is to avoid brand new questions – and achieve the aim that was stated within the consultation of using a defined objective measure – we would have expected the drafting to be picking up the tax law more directly along the lines of the following:

> *[replacing 6(c) (ii-iv)]: The total figure for items (ii) and (iii) of column "c" , for Company Year Y is to be calculated as the sum across relevant schemes of:*
>
> *what would be the Pension Input Amounts under Finance Act 2004 Sections229 to 237for the individual, for a Pension Input Period that starts with the Company Year start (or the start of service as a Director if later) and ends with the Company Year end;*
>
> *except that references in that legislation to "16" should be read as "20";*
> *and references in 230 (1) and (3) and in 234 (1) to (3) to "increases" should be to "increases or decreases".*
>
> *less:*
>
> *The sum of the relievable contributions made by the individual to the schemeduring the Company Year;*

And where the scheme does not normally fall under the provisions of the Finance Act 2004 (for example unfunded employer-financed retirement benefit schemes), the calculation of Pension Input Amount is to be done as though it did so.

We are not sure why a different approach was chosen, but some examples of where the above structure would work but the current drafting causes difficulties include the following:

- As written the legislation does not deal with cash balance benefits (or if it does so by default under the header "money purchase benefits", does so incorrectly by reflecting employer contributions paid rather than the benefit promised).

  (In fact the terms "money purchase benefit" and "defined benefit" are undefined in this legislation. If it is intended to use the HMRC methodology, the tax law terminology needs to be directly referenced and used: that is "cash balance", "other money purchase" – which is the traditional idea of money purchase, "defined benefit" and "hybrid". The term "money purchase benefit" encompasses both the first two.)

- Hybrid arrangements are dealt with differentlyunder the Annual Allowancetax law approach methodology to that proposed in the Regulation 34(2) definition so this causes ambiguity in requiring the use of the "HMRC methodology".

- Regulations 6(c)(ii) and (iii) (applying to appropriate money purchase schemes - see first point above) look to the contributions "paid" sowould overlook contributions assignedto the individual from funds already within the scheme.

- Individual's own paid contributions are treated correctly in relation to the money purchase arrangements (they are ignored) but incorrectly for defined benefit (they should be netted off the increase the in value of the benefit).

- As drafted, only increases in the value of defined benefit or cash balance benefits are reflected, with decreases set to nil. Disclosure should acknowledge decreases.

- There is use of the terms "capitalised" (undefined) and "rights would be used to provide a lump sum" which we think are meant to mean the same thing, but neither term is clear.

We note that in the above we have assumed that the reference in the current draft solely to Section 234 of the Finance Act 2004 was intended implicitly to pick up all the adjustments in provisions in 235-236A, which are essential.

We have not had time to consider how death benefits or benefits granted for retirement on grounds of severe ill-heath should be treated; but we note that the HMRC methodology would generally reset values to zero.

It should be noted (whether explicitly in our structure, or implicitly in the draft by virtue of how it aims to use tax legislation), that:

- Tax law may change, sometimes retrospectively – and each time that happens it may be appropriate that such changes need consideration for whether and how it should be interpreted for the disclosure context.

- Pension Input Amount calculations in the registered pension scheme may depend on specific decisions that the scheme trustees need to make (for example about "arrangement" structure) that may have not yet been made (and in the absence of decisions at a time, may be later made with retrospective effect). For example with unfunded employer-financed retirement benefit schemes the wording shown above might need "and as if all defined benefits were provided under one arrangement, ditto all cash balance benefits".

- While it appears necessary to impose the "Pension Input Period" definition, it might have some unexpected impacts (for example bringing into the figures a pension increase that would normally be excluded).

We hope that there is no question of this methodology applying for current or past years. If so there needs to be special provision to override calls on "straddle PIPs" and other transitional features.

With the uncertainty of what the aim is, we have not been able to do further analysis.

For Regulation 10(2), our response above to your Question 11 is indicative of areas of uncertainty from the drafting, again with our analysis limited because of uncertainty of the intention. We also note that the phrase "has become entitled" here is confusing, because under HMRC legislation this has a specific meaning(broadly "benefit has come into payment", which is clearly not the intent here.

Response by:

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26 September 2012

Association of Investment Companies

aic

The Association of Investment Companies

Directors' pay: consultation on revised remuneration reporting regulations

Submission from The Association of Investment Companies (AIC)

The Association of Investment Companies (AIC) represents approximately 350 closed-ended investment companies with assets under management of around £80 billion. The AIC's members include UK investment trusts, Venture Capital Trusts (VCTs) and non-EU companies.

Investment companies are a type of collective investment fund whose shares are traded on public markets. The vast majority of our members are listed on the London Stock Exchange.

Investment companies have boards of directors whose duty it is to govern the company to secure the best possible shareholder returns. They comply with various company law, Listing Rules and other transparency requirements. Their constitutional obligations are also determined by a dedicated framework set out in the company's Articles of Association. The directors are appointed by and answerable to the shareholders.

Many investment companies appoint external fund managers to deliver the day-to-day activities of the company. When this is the case the board is often composed exclusively of non-executive directors (NEDs). They therefore do not adopt remuneration structures which have stimulated the current concern over executive pay.

Remuneration agreements for investment company NEDs tend not to have significant variable elements. Trust Associates produce an annual survey which details the levels of investment company NED fees from the 205 investment companies in their database. The most recent survey produced the following average figures:

Role	Average Pay	Range
Chairman	£30,289[1]	£5,000 to £75,000
Audit Chairman	£23,751	£5,000 to £52,000
Director	£20,896	£5,000 to £45,000

For VCTs, which are a type of small investment company with a market cap of only a few tens of millions of pounds, the figures are lower:

Role	Average Pay	Range
Chairman	£21,351	£15,000 to £45,000
Audit Chairman	£16,471	£8,000 to £31,000
Director	£16,180	£8,000 to £31,000

[1] Chairmen paid over £100,000 have been excluded as their pay reflects additional factors unique to that company.

Many investment companies already have strong controls on director's pay through a limit on the aggregate level of their pay in their Articles of Association. The aggregate figure set out in the investment company's Articles of Association rarely exceeds £500,000 annually and is usually much lower. Few companies actual aggregate pay totals get close to the £500,000 limit (a consequence of the relatively low directors' remuneration fees already listed). Any changes to the limit in the Articles of Association could only be made with shareholder approval.

Investment companies do not offer excessive remuneration packages to their directors. Historically the level of remuneration has not raised concern amongst shareholders or created perverse incentives in relation to risk or a general escalation of board fees.

The AIC recognises the concerns which have stimulated the current proposals. However, we are also clear that matters of corporate governance should concentrate on issues which represent the key concerns of shareholders and a significant governance risk. Requiring additional disclosures where such considerations do not exist risks creating longer annual reports which suffer from a "boilerplate" format rather than helpful disclosures. Requiring additional annual resolutions at AGMs threatens to distract shareholders from other important concerns.

The Government should be wary of imposing burdens on companies who do not pay excessive fees and otherwise have shareholder agreed limits on remuneration in place.

The AIC therefore **recommends** that, where a company's Articles of Association limit the aggregate annual pay to all directors to under a set level, which would be defined in the legislation, they would be exempt from all additional requirements.

The AIC **recommends** that this level be at least £1 million a year. This aggregate figure is well below the levels of individual remuneration which has stimulated the current concerns. This level would deliver the Government's objective and focus the new proposals on the practices which cause concern.

If a £1 million limit is not deemed suitable, the AIC **recommends** that a lower level of either £750,000 or £500,000 be adopted.

This approach will also deliver the Government's objective of ensuring a strong role for shareholders in setting remuneration amounts and preventing an automatic ratcheting upwards of rewards. Shareholders already have a binding vote to approve the Articles of Association, along with any subsequent changes. The AIC's recommendation will therefore not impact the level of engagement of shareholders of these companies on the issue of executive remuneration. It will however prevent an unnecessary regulatory burden and Government micro-management of companies who are not the cause of concern about the unchecked growth in executive pay.

Where a company meets this requirement, the AIC **recommends** that the statement required in the Directors' Remuneration Report should note the limits set out in the

Articles of Association. No additional disclosures should be required. Specifically the AIC **recommends** they should not have to publish a policy or implementation report as currently proposed.

The AIC recommends that companies with the required limits in their Articles of Association should not be obliged to have regular shareholder votes on their remuneration policy. Of course, any further changes to the Articles of Association would have to be voted on

This approach in its entirety would deliver the necessary protection against excessive pay and associated risks which have caused concerns, whilst delivering a proportionate outcome for other listed companies. Increases in pay will also be controlled because of existing requirements in relation to the Articles of Association.

Policy Report

Question 1: The Government seeks comments on ho w well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

The AIC **recommends** that, where a company's Articles of Association limit the total aggregate annual pay to all Directors to a statutory limit (ideally £1 million) they should not be subject to the additional proposed disclosures, and the associated votes as proposed in this consultation.

If this approach is accepted, the current text of the draft regulations would need to be amended to deliver the AIC's recommendation. The AIC would be pleased to provide input on this drafting if its policy recommendations were accepted.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

There will inevitably be costs attached to the revised reporting regulations.

This is an unnecessary burden upon companies who have measures in place, through their Articles of Association, to limit aggregate director remuneration to a relatively low level.

This is why the AIC **recommends** an exemption from the additional disclosures recommended and the associated votes when a company's Articles of Association limit the total aggregate annual pay to all directors to under £1 million.

By taking this approach the Government would avoid imposing an unnecessary and disproportionate compliance cost.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

The AIC has no specific comments on this question.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

The AIC has no specific comments on this question.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

The AIC has no specific comments on this question.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

Most investment companies are managed by an external fund management group and therefore employ no executive or other staff.

If any company without staff is included in the proposals, it must be acceptable to note this situation, without any obligation to seek views on the remuneration policy.

<u>Implementation Report</u>

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

The AIC has no specific comments on this question.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The AIC has no specific comments on this question.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

The AIC has no specific comments on this question.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

The AIC has no specific comments on this question.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

The AIC has no specific comments on this question.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

The AIC has no specific comments on this question.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

The AIC has no specific comments on this question.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

The AIC agrees that publishing a performance graph demonstrating total shareholder return (TSR) over the previous five years in comparison to peer group companies is of limited use to shareholders.

Also, the current disclosure requirements impose unnecessary costs on companies. Many companies, including investment companies, comply with the requirement to compare shareholder return with a "broad equity market index" by providing performance data of a FTSE index, for example the FTSE 100 or the FTSE All

Share. This necessitates purchasing relevant data which can cost thousands of pounds.

Removing the requirement to present the current performance graph in the Directors' Remuneration Report would represent a significant cost saving to businesses.

That said, the AIC **recommends** that the proposed requirement to include a graph linking executive pay with total shareholder return (TSR) be dropped. This is an overly simplified format given the myriad factors that affect TSR. We are sceptical of the value of implying a causal relationship between TSR and the chief executive's pay and are unconvinced that this disclosure provides useful information to shareholders.

If the graph is to be included, where a company's Articles of Association limit the total aggregate annual pay to all Directors to a statutory limit (ideally £1 million), the AIC **recommends** that it should not be required to make any of the additional proposed disclosures, including this graph.

The AIC **recommends** that closed ended investment companies (defined as those subject to Chapter 15 of the Listing Rules) which are required to make the additional disclosures under these regulations, should be excluded from the specific requirement to produce this graph. The unique nature of investment company operations, where the company is seeking to deliver portfolio returns in relation to a published investment policy, means the case for the assumed causal links between executive pay and TSR is even weaker than for trading companies.

If these recommendations are not accepted, and investment companies are to be included in the requirement to report TSR against executive pay, then the disclosures should be tailored to suit situations where these companies have no executive directors. The AIC **recommends** that in the absence of any executive directors, a company should be able to report (i.e. prepare the required graphs) using the highest paid director's remuneration as the comparator. This will make the disclosure deliverable by the sector.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

The AIC has no specific comments on this question.

August 2012

To discuss the issues raised in this paper please contact:

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Association of Pension Lawyers

Association of Pension Lawyers

By email to executive.pay@bis.gsi.gov.uk
Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET

Date 26 September 2012 Our Ref CXC Your Ref

Dear Mr Walker,

Directors' Pay: Consultation on revised remuneration reporting regulations

A. Introduction

1. The Association of Pension Lawyers ("**APL**") is a not-for-profit organisation whose members comprise over 1,000 UK lawyers, including most of the leading practitioners in the field, who specialise in providing legal advice on pensions to sponsors and trustees of pension funds and others, including the largest pension funds in the UK. Its purposes include promoting awareness of the importance of the role of law in the provision of pensions and to make representations to other organisations or governments on matters of interest to APL members.

2. This report has been prepared by the Legislative and Parliamentary Sub-Committee of the APL.

3. **APL has limited its response to pensions-related aspects of the consultation questions. The APL response does not address those aspects of the consultation paper which deal with wider remuneration issues.**

4. **There is at least one situation, discussed in section C3 below, in which the proposals could mean that shareholders receive materially misleading information about a director's pension accrual which (a) seems to us undesirable from the perspective of the company and the director concerned and (b) will result in misleading comparisons as between different companies.**

B. Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

See comments at Appendix A.

Please reply to

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One Bunhill Row
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EC1Y 8YY

APL website: www.apl.org.uk

C. **<u>Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?</u>**

1. The "HMRC method" for valuing defined benefits places under Section 234 of the Finance Act 2004 places a notional current value on a future benefit at a particular point in time. The value is calculated by applying statutory valuation assumptions as follows:

   - the person becomes entitled to the benefit at the relevant point in time,
   - the person has (at the point in time in question) reached the age that must have been reached so as to avoid any reduction in benefits on account of age (so there is no reduction in benefits for early payment), and
   - the person is in good health (so there is no increase in benefits for ill health).

2. Although this methodology may appear to be a simple method of calculating the value of a defined benefit and be readily comparable, in practice:

   2.1 there are areas of considerable difficulty in interpreting how the statutory valuation assumptions should apply to the diverse range of legacy defined benefit promises (see example at **3.** below),

   2.2 the valuation assumptions can produce different results depending on how a particular pension benefit promise has been worded, so that the resulting figure is not comparable as between the defined benefit scheme of one company and another (see examples at **3.** and **4.** below), and

   2.3 the value produced can depend on the arrangement structure adopted by the scheme, so that the resulting figure is not comparable as between the defined benefit scheme of one company and another (see examples at **5.** and **6.** below).

3. There are a number of different ways that the same defined benefit promise might have been expressed. For example, a benefit promise may be framed as "2/3 of final pensionable salary at normal retirement date" with a reduction factor applied if the person leaves service ahead of that time. HMRC's view is that, because of the assumption made about age and as, apart from the valuation assumptions, the scheme rules are to be applied by reference to the member's then current active status, under Section 234 of the Finance Act 2004 the whole of that 2/3 benefit is treated as accruing in the first year of service. In subsequent years only the increase in final pensionable pay will feed into the Section 234 calculations. If the benefit had instead been expressed as accruing at a fraction of final pensionable salary for each year of service (so 1/30ths if on joining the scheme the member had 20 years of potential service to normal retirement date), the benefit would instead be valued under Section 234 as 1/30th accruing each year. See HMRC's guidance on "non-uniform accrual scales" at RPSM06107035 for further information on this point.

   Comment: The member would in fact be entitled to the same rate of pension accrual whichever way the benefit promise was expressed. However, HMRC's interpretation of the Section 234 calculation means that the value placed on that benefit using the "HMRC method" will be very different, depending on the precise wording in the scheme rules. "Non-uniform accrual" type promises were historically quite common for top executives. The ongoing true defined benefit accrual for those individuals could be, on an ongoing basis assuming the original promise was given some time ago, significantly under-reported using the "HMRC method" (for 2/3 type promises), or, where the benefit is expressed as accruing at a particular rate with a maximum number of years service, over-reported in years before that maximum service is reached. Using the HMRC methodology, it would be difficult for shareholders to compare the value of pension benefits from one company to another, as the values will depend on the way that the benefit has been expressed.

4. A further example of a problem with HMRC practice is that there is a floor of nil even when the calculations produce a negative value. This would, if applicable, be misleading in the context of reporting pension value received by the individual to shareholders. See paragraph 7 of the section entitled paragraph 7(4) in the Appendix.

5. The concept of an "arrangement" is a tax construct and is key to making calculations under Section 234, but there is no "default" position under the legislation for analysing an arrangement structure. HMRC view this as a matter of scheme construction. However, schemes will typically have been set up without consideration being given to the point as the arrangement concept was only introduced in 2006 and only had wide spread practical relevance once the annual allowance reduced to £50,000 in 2011. A scheme's arrangement structure can determine whether there is an "input" under Section 234, or the size of the input. For example, in a "career average re-valued earnings" ("**CARE**") scheme (which is a type of defined benefit scheme) if it can be determined that there are separate arrangements for each year of service, depending on the scheme rules at 14th October, 2010, there is the possibility of accessing a nil value for past years' accrual (using the deferred member exception at Section 234(5B)) (see RPSM06107260). The "value" of benefits receivable from one CARE scheme to another as calculated under Section 234 may therefore not be directly comparable.

6. Similar points arise where a scheme provides for tranches of benefit with different retirement ages (as is common following equalisation of retirement ages for men and women). In periods of service after the first retirement age is reached the value of the benefit accrued will depend on whether the tranches of benefits are structured as in the same or separate arrangements (see the examples at RPSM06107176).

7. A further point to note regarding the "HMRC method" is that no value is placed on discretionary benefits, even where the normal practice under the pension scheme is to exercise the discretionary power to deliver benefit in a certain way, so the value of that benefit is not recognised under the "HMRC method" until that discretion is actually exercised.

Conclusion

8. There are, therefore, some significant difficulties in practice in using the "HMRC method" under Section 234 of the Finance Act 2004 to value defined benefits, and the results produced may not be consistent between schemes. It would be preferable to use a methodology for valuing defined benefits that produces more consistent results and which does not under or over report the true accrual rate of particular types of benefit promise.

9. On the assumption that BIS is keen to have a flat-rate factor for capitalisation in order to aid comparison between companies and to avoid undue fluctuations from year to year, we would suggest adapting the proposal so as to keep the 20:1 factor but to apply it to a much simpler methodology than the HMRC methodology. This would need a small amount of work and no doubt engagement with the actuarial profession but it seems to us to be preferable and in practice simpler for businesses

to operate and simpler for shareholders and others to understand than using the complicated HMRC methodology.

10. **We would also point out that there will be potential confusion in the disclosure requirements by both (i) requiring the single total figure of remuneration number to include the value of the pension earned in the year in question and (ii) separately the total pension entitlements unless, from year to year, (ii) increases exactly by (i) – it would be sensible to scenario test the valuation method to ensure that this is likely to be the case.**

11. **There are further detailed comments relating to the "HMRC method" in Appendix A.**

D. **<u>Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?</u>**

1. It is proposed to require disclosure of:

- the aggregate of the contributions to money purchase schemes and the increased value for defined benefit schemes (and unfunded money purchase type schemes) in a year, and

- the value of the total accrued benefit under each defined benefit scheme, assuming the member retired at the end of the year and (it appears, but this is not altogether clear) that the member has reached normal retirement date at that date, and

- the value of any additional defined benefit if the member retires early.

2. **If accrued defined benefits are to be reported, to avoid confusion, the basis on which they are calculated should be consistent with the basis on which the annual increase is calculated. It is not clear that the current drafting delivers this – see comment at C.10. above.**

3. **It is not practical to report the "value" of any additional benefit if the member retires early, as the value is likely to vary depending on how early the member retires, and may depend on the circumstances in which the member retires.** Also, the "HMRC method" uses a single flat capitalisation factor so does not capture the benefit of permitting a benefit to be taken early without actuarial reduction or with "soft" reduction terms.

4. **It would be preferable to require a description to be given of any favourable mechanism which would apply on early retirement.** For example, report that there is no reduction in benefit if the director retires after age 60, whereas other members have to retire early with reduction, and indicate the reduction factor that would be disapplied.

Yours sincerely,

Charles Cameron
Chair
Legislative & Parliamentary Sub-Committee

Appendix A

References to paragraphs are to the numbered paragraphs in the proposed substituted Schedule 8 set out at paragraph 3 of the draft Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2012.

Paragraph 5(c) *Only relevant if HMRC method is used*

1. The Finance Act 2004 distinguishes between 3 different types of benefit each of which has a different calculation methodology for valuing "inputs" for annual allowance purposes. (This is the valuation method it is proposed should be used as the "HMRC method"). Paragraph 5(c) only caters for 2 of these benefit types ("other" money purchase schemes, where the benefits are calculated wholly by reference to payments into the scheme, and defined benefit schemes). The Finance Act 2004 also identifies a third type of scheme which is also defined as a money purchase scheme but provides cash balance benefits (i.e. benefits the rate or amount of which is calculated by reference to an amount available for the provision of benefits calculated otherwise than wholly by reference to payments made). Provision should be made for valuation of cash balance benefits to be dealt with separately since it is not the contributions in which are counted under the Finance Act 2004, but the increased value of benefit. However, the methodology for valuing this type of money purchase benefit under Section 230 of the Finance Act 2004 differs from the methodology for valuing defined benefits under Section 234.

2. A single scheme may provide both defined benefit rights and money purchase rights for the same member. For example a scheme may have an AVC money purchase section, or a scheme may have provided defined benefits for a member up to a certain point in time with that section having closed and the member being provided with benefits under a money purchase section of the same scheme for later periods of service. The definition of "defined benefit scheme" (see **paragraph 33(1))** needs to be refined to reflect this. The Finance Act 2004 uses the concept of "arrangements" which may be a useful drafting device to follow in this context.

Paragraph 6 *Only relevant if HMRC method is used*

1. **Paragraph 6(c)(ii)**

   This paragraph provides for reporting the cash value of money purchase contributions paid or payable by the Company for a financial year. It appears there could be double counting if a contribution was due in one year but paid in the following year as it would have to be reported as payable in year one and then as actually paid in year two.

   Typically under a money purchase scheme, death benefits will be provided partly on a money purchase basis and partly on a defined benefit basis. We note that this benefit feature would be excluded under **paragraph 34(3)** in determining whether a scheme is a money purchase scheme. However when measuring the contributions attributable to a particular member for money purchase purposes all the contributions paid in respect of member under the scheme will be counted in (including any contributions used to fund defined benefit death benefits, for example by insurance). However if a company chooses to provide death benefits separately, either through a separate defined benefit registered scheme or via a non-registered insured scheme, the cost of providing those benefits will not be included in the pension column headed "c" of the "single total figure table", as death benefits are not measured using the "HMRC method". As these are not taxable benefits they will also not be included in the column headed "b" and they do not appear to be included anywhere else in the table. Whilst these amounts are unlikely to be a significant proportion of an individual's remuneration, this is another area in which there is a lack of comparability as the proposals currently stand from one company to another, depending on how pension and risk benefits are structured.

2. **Paragraph 6(c)(iii)**

   The only circumstance in which we can envisage that a money purchase scheme would be established under which no contributions were paid in a year would be in the unusual case of a non-registered unfunded money purchase scheme. Presumably the intention is that the increase in value should be measured over the financial year, whilst under the "HMRC method" values are measured over pension input periods (see **3.** below). The "HMRC method" does not apply to non-registered schemes, so they do not have pension input periods in any event. The references to Section 234 of the Finance Act 2004 in **paragraph 7(4)** would require appropriate modification to measure the increase over the financial year.

3. **Paragraph 6(c)(iv)**

The "HMRC method" envisages calculating pension increases over the course of a "pension input period" ending in a tax year as selected by the scheme administrator. Presumably the intention would be to instead measure the increase in value of the defined benefit during the financial year. The references to Section 234 of the Finance Act 2004 in **paragraph 7(4)** would require appropriate modification to achieve this.

The words "rate of the" should be added between the words "annual" and "pension".

<u>**Paragraph 7(4) ("HMRC method")** ***Only relevant if HMRC method is used***</u>

1. This refers to the amount of increase in the *"value of the **lump sum** that the individual is entitled to under the pension scheme"*. In fact under Section 234 what is valued is the amount of any *"increase in the value of the **individual's rights** under the arrangement"* which itself is split out into increases in pension rights and increases in any stand-alone right to lump sum. This structure should be reflected in the drafting of paragraph 7(4).

2. Only Section 234 of Part 4 of the Finance Act 2004 is referred to.

3. Is it intentional that the uprating of the opening value under Section 235 (by the increase in the CPI) is excluded for these purposes? The uprating is meant to give an increase in value above an inflation measure, and so reflect the "real" increase in value.

3. Is it intended to exclude the adjustments at Section 236 and 236A?

4. The adjustments at Section 236(2) to (5) aim to strip out from the valuation of the benefit increase those changes in benefit amount which are due to transfers in or out from other pension schemes, and also to deal with pension debits and credits. Presumably the intention would be to remove these from the calculations for the purpose of reporting remuneration since they do not represent additional (or decreased) accrued value due to service.

4. The adjustment at Section 236(8) and the adjustment at 236A are anti-avoidance provisions. They are intended to prevent artificial reductions in the value produced by the calculations under Section 234 either due to surrender of benefits in return for something that is not measured under Section 234 or by value being delivered through pension increases after retirement, rather than an increase of benefits during service. Presumably both these adjustments should in fact be included for present purposes.

5. Section 236(8A) and (8B) deal with calculations in a year in which benefits crystallise. How is it intended that the calculations made for the purposes of reporting remuneration should be made in a year in which benefits crystallise? One of the consequences of using the "HMRC method" is that (but for Sections 236(8A) and 8(B)) if benefits are fully crystallised under Section 234 during a calculation period, a nil benefit ensues at the end of the calculation period. Under Sections 236(8A) and (8B) if there is a benefit crystallisation, the actual value of the benefits crystallised is included in the calculation. The result of this is that if benefits are enhanced at retirement, that enhancement is captured in the valuation. However, if the benefits are paid early with a "soft" reduction for early payment, the value of that soft reduction is not captured by this valuation method.

6. Section 236(8C) and (8D) deal with the situation where a member's increased benefits exceed the annual allowance and the annual allowance charge has been met by the pension scheme under the "scheme pays" provisions of the Finance Act 2004. In years before retirement, the

consequent reduction to scheme benefit is added back to the calculation. If these provisions are not included then the total pension value reported for the individual who elects for scheme pays through the scheme would be less than the equivalent for an individual who chose to meet their own annual allowance charge from their own resources.

7. Under Section 234, only increases in the value of an individual's rights are recorded. If in any particular year the calculations would produce a negative value (for example, if the individual retires early, Section 236(8A) and (8B) apply (see **5.** above) and the benefit is in fact reduced for early payment), the amount recorded is nil. Adopting this approach would be misleading in the context of reporting the pension value received by the individual to shareholders.

Paragraph 10

1. **Paragraph 10(2)**
The words *"right to which he has become entitled"* in a pensions context usually means that the individual has a right to **payment** of those benefits. Presumably the intention here is to identify the rights that have **accrued to** the member in respect of qualifying service.
The term *"the **details** of the person's accrued benefits under the scheme"* is used. Presumably the intention is to identify the **value** of the person's accrued benefits.
Presumably the intention here is to identify the value of the benefits that would be payable if the member were entitled to immediate payment of benefits and the member had reached the age at which benefits would be paid without reduction. This is not what the drafting currently says.
The term "*normal retirement date*" is not used in the Finance Act 2004 and is not a defined term in pensions legislation. The concept used in the Finance Act 2004 is to identify the earliest age at which there is an entitlement to benefits without reduction on account of age.
Is it intended to require the value of death benefits to be reported here? These are not reported for defined benefit schemes in the single total figure of remuneration under paragraph 5 and 7 (see comment on **paragraph 6(c)(ii)** above). See also comment on definition of "**pension scheme**" under **paragraph 33** below.

2. **Paragraph 10(3).** See **D.3** and **D.4** of our note, responding to Question 11.

3. **Paragraphs 10(2) and (3).** There is no provision for determining how the value of the accrued rights and early retirement rights are to be valued.

4. **Paragraph 10(4).** How is the relative weight and of each type of benefit to be determined? It is the value as determined under paragraphs 5 and 7 compared to the total sum reported in column "c" of the single total figure table?

Paragraph 19(c)

It is unclear what is meant by the *"maximum potential value"* in the context of a defined benefit promise. As there are additional provisions dealing with total pension entitlements under paragraph 10, perhaps defined benefit promises should be excluded from this requirement.

Paragraph 24(1)(c)

1. It is unclear whether the overall expenditure on pay referred to at paragraph 24(1)(c) is intended to refer to the pay for the entire workforce or only pay for the directors.

2. It is unclear whether pay is intended to only include cash benefits or also the cost of providing pensions. The method of accounting for the cost of pension benefits for the purposes of the accounts of the company will be different from the "HMRC method" used for the purposes of the directors' remuneration report so in the context of pensions the comparison may not be useful.

Paragraph 33

1. Definition of "**defined benefit scheme**" – see comments on **Regulation 5(c)** above.

2. Definition of "**emoluments**". UK pension schemes, whether registered or non-registered, should include a non-assignment clause which means that the company contribution paid or treated as paid in respect of an individual under such schemes will not count as emoluments for tax purposes in any event.

2. Definition of "**money purchase scheme**". There is no definition of "money purchase benefits". What definition is it intended to use? The definition in Finance Act 2004 (which would appear to be the appropriate definition for these purposes if the "HMRC method" is used) differs from the definition currently included in Schedule 8 of the Large and Medium Sized Companies and Groups (Accounts and Reports) Regulations 2008.

3. Definition of "**pension scheme**". Presumably subparagraph (a) should refer to schemes "*operated **by or** on behalf of the company*".

4. Definition of "**pension scheme**". The definition of "retirement benefit scheme" under Section 150(1) of the Finance Act 2004 includes death benefit only schemes. This definition is used in paragraph 10 and therefore would require the value of such schemes to be reported. (See also comments on **paragraph 10(2)** above.)

5. Definition of "**retirement benefits**". Section 612(1) of the Income and Corporation Taxes Act 1988 has been repealed. However, this remains the most appropriate definition of "retirement benefits" as the definition of "relevant benefits" in Section 393(B) of ITEPA 2003 excludes benefits such as pensions and certain benefits under non-UK schemes. (The definition is used at **paragraph 7(3)(c)** to ensure that schemes providing such benefits do not fall within the column headed (e) in the single total figure of remuneration - awards under schemes).

<u>Paragraph 34</u>

1. **Paragraph 34(2)** gives guidance to companies as to how to value benefits that include an underpin on the basis that the company can view whichever outturn appears more likely at the end of the relevant financial year. We support this non-prescriptive approach.

2. **Paragraph 34(3).** *"Death in service"* benefits provided by the scheme are to be disregarded when determining the type of scheme However there may be circumstances in which death benefits other than death in service benefits may be provided on a different basis from the main retirement benefits. The words "in service" should be removed.

Aviva Investors Global Services Ltd

AVIVA INVESTORS

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
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26th September 2012

Executive.pay@bis.gsi.gov.uk

Dear Barry,

Thank you for the opportunity to respond to the consultation on the proposed remuneration reporting regulations. This response is on behalf of Aviva Investors, which is the global asset management business of Aviva plc and currently manages assets in the region of £270 billion (as of December 2011).

We are pleased by the outcome of the proposals and believe BIS has done an excellent job in identifying and aggregating all the various strands of remuneration into a cohesive approach for the future. There are one or two suggestions we would like to make in relation to the regulations which we believe will further improve transparency and accountability of companies to their stakeholders.

While the regulations are crucial to produce the right disclosures, it is the industry and shareholder guidelines that support the regulations and the future behaviour of shareholders in holding companies to account that will determine the success of these regulations going forward. Therefore, we believe there should be a continued focus on how shareholders are playing their role in this area of governance.

These regulations have given the industry a unique opportunity to re-think pay practices and has given us room for more innovative thinking, we would suggest that BIS revisit the area of remuneration again in 3 years to assess whether pay practices are moving in the right direction (before poor practices become embedded) and whether the regulations are working. We very much hope that these regulations will be enough to improve poor pay arrangements.

Environmental, social and governance disclosures:

- One area that has not been discussed so far is the question of environmental, social and governance disclosures. As part of our corporate responsibility agenda and in support for a longer term approach by companies and investors, we believe this would be an appropriate time to ask companies to say what environmental, social and governance performance conditions they have incorporated into their pay arrangements. If they have not included ESG metrics companies should explain why not. This request does not require companies to incorporate ESG metrics, it only asks them if they have and if not, why not. This is in keeping with existing ABI guidelines which state:

With regard to the Board, the company should state in its remuneration report:

1. Whether the remuneration committee is able to consider corporate performance on ESG issues when setting remuneration of executive directors. If the report states that the committee has no such discretion, then a reason should be provided for its absence.

2. Whether the remuneration committee has ensured that the incentive structure for senior management does not raise ESG risks by inadvertently motivating irresponsible behaviour.

Our answers to the consultation questions are as follows:

Background

1. **The government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.**

- We believe that the regulations largely address the areas which are required to meet the policy objectives of the consultation document. The answers we give to the rest of the questions will highlight areas where, in our view, further improvements may be made.

- It is not clear that the regulations will lead to more concise reporting but we hope that over time this will resolve itself. We are also concerned that some reporting may become boiler-plate, especially in the Policy Part, where we are struggling to find the right balance between sufficient information for shareholders and sufficient flexibility for companies to deal with exceptional circumstances.

- We have already seen attempts by companies to simplify their own plans and the trend is moving to much longer performance periods which we welcome.

- We are also not clear at this time as to how remuneration reporting will fit into the new narrative reporting structure. We maintain our strong view that both governance and remuneration should be part of the Strategic Report as both these issues pose risks to companies' future wellbeing.

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2. **What costs will companies face in adjusting to these revised reporting regulations?**

- This question is best answered by companies. However, as much of the information which is requested should already be available, we would not expect this disclosure to be excessively costly, with costs reducing after the first year.

- For smaller companies, paying for advice on how to comply with the regulations may be comparatively greater but even so, it would be surprising if this would lead to unreasonable levels of ongoing costs.

Policy Report

3. The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach? (Annex A)

- Yes, we believe this is the right approach so that companies can decide for themselves what is appropriate to disclose and this approach will give companies flexibility to improve their disclosures. However, the table needs to be well supported by explanations and justifications. There needs to be sufficient detail so that shareholders are able to work out whether they are happy with the parameters of pay policies.

- The wording in Part 4, The Policy Part 19 (d) says that performance ‘metrics’ should be disclosed. We would add that the ‘targets’ attached to the metrics should be disclosed too.

- Changes to policy in the table should be supported by explanations as to why it was changed.

- Disclosures on pensions in the table should be supported by details on transfer values, accrual rates, length of service, normal retirement dates, enhancement facilities and how they differ from pension arrangements for employees. In 2010, the NAPF and LAPFF produced a paper on pensions disclosure which are a good guide to the disclosures required.

- It would be helpful if linkages to companies' strategic KPIs were explained, preferably in the table but the narrative should explain how the chosen metrics for incentives support the company's strategy.

- The regulations make no comment about recruitment policies. We believe these are significantly important payments that can be made without reference to performance conditions. Therefore, we would include policy on recruitment into the mix of what should be disclosed.

- Where companies do not disclose performance targets (although they should always disclose the measures) e.g. if they are deemed too sensitive, this section should explain when they will provide further information so that shareholders can assess whether the payouts are reasonable and appropriate.

- Lastly, we believe that this table should be in every year's Annual Accounts (not just in the year when the policy is being voted on) so readers know what policy companies are working to.

4. **The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details**.

- Yes, we would like to see all these disclosures.

Service contracts:

- The information on service contracts would be extremely helpful. All areas of potential payments agreed on appointment or at any later date should be disclosed. Disclosures should also be specific enough for shareholders to know what will be paid out on termination of contracts. For example, if it's a 12 month contract, disclosures should state whether the agreed payment is 12 months basic salary or salary plus benefits, pensions and incentives etc so shareholders can calculate the potential amount.

Distribution statement:

- We are very supportive of the distribution statement as this will identify pay vs dividends vs profits. However, we believe this information belongs best in the implementation part of the report as shareholders would be more interested to see the actual division of profit rather than an anticipated one. This information should therefore reflect the actual division between profits, dividends and pay and should also be given in monetary amounts.

- There should be consistency in the profit number used over time. Once a company chooses which profit number they wish to use, they should be consistent in their use so that the comparisons over the years are also consistent.

- In addition (1) pay should be separated between board pay and pay for the rest of the employees and (2) on top of the percentages disclosed these should be supported by monetary amounts as well. We believe that over time, this will help stakeholders identify the trajectory of pay versus investment in the company versus shareholder returns.

- On top of these mandatory elements, companies should feel free to include other key elements of distribution that may be of particular importance to their sector. For example, if pharmaceutical companies wish to disclose how much they have put aside for research and development into their pipeline, this would be a welcome addition. Over time, shareholders should be able to see whether the focus of companies is on the longer term by apportioning their payments towards areas that promote the business over the long term.

Scenario analysis:

- We are supportive of scenario analysis but we are not convinced that the chart is sufficiently illuminating on its own. We prefer the Tate & Lyle table which puts the payments for below threshold, at threshold, mid-range and at stretch, into context with performance. Monetary amounts are given and explained together with the performance conditions and targets required to achieve each scenario. To have all this in one place would be of great benefit.

5 The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

- Yes, we believe the information in the proposed regulations is appropriate. In addition, companies should also explain their approach to mitigation of payments in the event of an exit.

- The disclosures should clarify the circumstances under which the director left. It would be helpful if companies clarified, at the outset, what a good/bad leaver scenario would look like. We understand that these are difficult and sensitive times but we believe that such transparency would be likely to tip the balance towards the board in a helpful way.

6. **The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy**

- We agree that despite current regulations, remuneration reports do not provide meaningful information. We agree that reports should be much more specific about pay policy for the wider organisation and how this has impacted on the decisions taken by the remuneration committee. We believe that it is good practice to seek the views of employees on the remuneration policy, both as it applies to them as well as within the firm more generally.

- We would have liked companies to be required to seek employee views without prescribing how companies might want to do this. We can see that in some situations it may be difficult for global companies with many thousands of employees to do this easily but we hope that companies are already communicating with their workforce on a regular basis on many issues so this should not be too problematic. However, it would be helpful for companies to say that they have not consulted rather than keep silent.

Implementation Report:

7. **The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?**

- Yes, we are supportive of this approach. We recognise that it is not perfect but, for the moment, we believe that it gives shareholders a consistent methodology to compare across companies and within companies over time. Companies should provide context for the numbers that emerge from these calculations especially if they believe the prescribed methodology is not appropriate for them (both if they appear too large or if they appear too little)

- There should, in any case, be sufficient narrative to explain the amounts being paid under each element, why it is merited and why the remuneration committee has taken the decisions it has taken.

- Companies should put last year's figures (for each component) next to the current one so readers can tell, at a glance, what the changes have been and what the change in the overall single figure has been.

- We would suggest that there is an additional column in the implementation table which would indicate exceptional payments made/amounts clawed back, that is NOT part of the normal policy for the year in question. This links in to our answer to question 9 (whether clawbacks should be part of the single figure) where our view is that it should not be, as otherwise, we would not be comparing like with like over the years. However, we need to record the clawback and any discretionary payments made over and above the normal policy, so we propose there should be a final column which will itemise any additional payments made (e.g. recruitment payments) or amounts clawed back.

8. The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

- Yes, we believe this is the best approach for dealing with very complicated calculations. However, if companies believe that the figure does not accurately reflect the right amount whether upwards or downwards, they should explain what they think the more accurate figure might be.

9. The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

- We believe that clawback should be reported but not as part of the single figure. We have suggested in question 7 above that there should be a separate column in the table (shown as Annex A) to reflect any unusual deductions and additions that have been made.

10. The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

- Wherever possible we prefer performance metrics and targets to be disclosed. Having said that, it is common practice not to disclose performance targets for bonuses but companies have increased the amount of bonuses so significantly that we no longer think such potentially large payments should be predicated on metrics and targets that are not disclosed to shareholders.

* We do not believe metrics are ever commercially sensitive whereas the actual targets might be. Where this is the case, we would expect companies to disclose retrospectively (the year after) the targets set, the performance achieved against target and the resulting payment so that these payments can be justified.

* Where companies still feel they are unable to do so, then I believe Shareholder Guidelines need to be toughened up so that the maximum amount that can be earned through performance that is not disclosed is a set figure, say, 100% of salary or a set number of shares. All other incentives should be awarded under more transparent arrangements. This is beyond the scope of this consultation. However, companies should understand that this may preclude some shareholders from supporting their pay arrangements.

11. Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

* As in question 3 above, the disclosure requirements as itemised in the NAPF/LAPFF paper should accompany the single pension figure. It may be that the information will have to be individualised to account for the different arrangements companies have for individuals.

12. The government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

* Yes, we believe this approach is more transparent and less prone to manipulation than an expected value number.

13. The Government proposes to simplify the reporting requirements regarding directors interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

* In addition to the proposed requirements it would be helpful to have (1) the monetary value of the shares and share options owned and (2) shares held in trusts (3) confirm there are no hedging arrangements.

14. The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay

are the best proxies for company performance and pay? If not, what measures would be more appropriate?

- Yes, we agree this graph would be useful. It is a 10 year graph which is a sufficient length of time to cover cycles and TSR is a good proxy for long term performance. There is a case for using board pay but as it's the CEO's pay that normally creates the concern, we believe it is appropriate to plot the graph against the CEO's pay. An alternative would be to use the highest paid director where the CEO is not the highest paid.

- We believe that companies ought to produce the 10 year graph from the beginning. Otherwise, a significant amount of time will have passed before shareholders get the benefit of this graph.

- Companies should be encouraged to plot other information on to the graph. For example, they may want to plot the achievement of strategic financial targets such as ROCE or the movement of average employee pay.

- Where there has been a change of CEO, companies can explain any unusual CEO pay movements through the narrative that accompanies the graph. Companies would probably also want to justify the link between CEO pay and TSR performance.

15. The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

Provision of advice:

- On the provision of advice, we believe that additional information could be required of remuneration consultants (or any other advisers e.g. lawyers) that will give some context as to whether the advisers are independent. For example, the total fees on remuneration committee advice and other work for the company, fees for the given client as a percentage of total firm fees and other professional or personal relationships with the board of directors and executives. See PwC's, July 2012 paper 'More disclosure on executive pay, draft regulation published on remuneration reporting disclosure'

Shareholder context:

- We strongly agree that companies should disclose how their shareholders voted in the previous shareholder meeting (covering votes against, abstentions and votes for) and how shareholder views have been taken into account. Our experience is that it is not always easy to get the information on voting outcomes so this disclosure would be very welcome.

- We think it is important that companies disclose the voting outcome, substantive reasons for concern and what action the company has taken in response. This should be backed up by the FRC who should make it best practice for companies to make a public statement about what it will do once it has received significant votes against.

- The follow through i.e. what companies are doing in response to the vote will encourage better engagement on remuneration issues on the most contentious cases.

Assurance:

- In addition to the list of items for assurance, we would suggest that any recruitment payments should also be audited.

Thank you once again for the opportunity to respond to the consultation on the proposed remuneration reporting regulations.

Yours sincerely,

Steve Waygood
Chief Responsible Investment Officer
Aviva Investors
1 Poultry
London
EC2R 8EJ

Baillie Gifford & Co

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
✓	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Greater clarity and improved transparency on executive remuneration, particularly with regards to pay for performance, appears to be one of the main objectives of the policy. There is a lot of detail provided in the draft regulations in Annex B, and therefore it is difficult to imagine what the revised remuneration reports will look like in future. To the extent that the revised reporting regulations encourage more consistency between companies' remuneration reports and increased simplicity, we hope that future remuneration reports will be easier to read for investors. This should hopefully result in improved disclosure on realised pay (what fixed and variable remuneration – short and long term – executives have actually received during the year) and make pay for performance easier to assess. It should also hopefully facilitate engagement between companies and investors.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

We think that the costs should be minimal although there may be additional fees to remuneration consultants in the first year as companies restructure their remuneration reports and consider what degree of flexibility they require in their remuneration policies. Many companies already disclose most of the data and information which is attached at Annex B in their current remuneration reports. We think that the main costs for companies will be restructuring and reordering the data and information in their current remuneration reports so that it complies with the revised reporting regulations.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

Yes, we agree that companies should have the flexibility to decide what they want to disclose in the table for each element of remuneration. We would however prefer to see concise disclosures from companies, which improve investors' understanding of the remuneration policy (including pay for performance and how it is integrated into the business strategy) particularly if there is more detail disclosed elsewhere in the remuneration report on each element of remuneration. Ideally the table should serve as a useful reference point for investors to get a good understanding of the remuneration policy. It would also be beneficial for investors if companies improved their disclosure

on the different tax rules within incentive schemes. We have seen instances where the tax incurred by the executives is capital gains tax rather than income tax. Whilst this is clearly of benefit to participants, it is not always clear how this impacts the company's tax expense.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Yes. In our experience however estimating what remuneration directors will receive according to the level of performance achieved, particularly for long-term incentives, is difficult and largely depends on the share price performance. Companies should therefore disclose fully what their assumptions are regarding share price growth alongside their chart on total remuneration opportunity.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

The level of Remuneration Committee discretion over exit payments, where appropriate, would be useful additional information.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We agree with the decision not to require companies to disclose the ratio between the pay of the CEO and the median earnings of the companies' employees, because like the Government we think that this would be misleading.

The requirement to take the pay of employees into account as disclosed on page 20 of the consultation document is very different to actually seeking employee views on pay. We believe that it is unnecessary to require companies to make a statement on whether they have sought employee views on the remuneration policy. The differential and relationship between executive and employee pay varies significantly between companies and industries and largely depends on the employee base and relative skills of the workforce. This statement would in most instances be of limited use to investors. Instead of introducing a prescriptive disclosure rule it should be left to the discretion of each individual company to decide if making such a statement is appropriate for their business.

In our experience from being consulted by companies on executive remuneration, an increasing number of remuneration committees are taking into account the salary increases for employees when considering the executive directors' salary increases. We believe that this is an increasingly important consideration for remuneration committees and something we expect to see more of.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We agree that a single total figure which shows remuneration actually received by the executives will be both easier to understand and facilitate a proper assessment of pay for performance. We would however prefer to see separate columns showing the value from exercised options and vested shares (i.e. what value has actually been realised or received during the year) and what becomes receivable (i.e. an estimated value) during the year. This would make it easier to measure the correlation between realised pay and performance.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

Since this appears to be the simplest and least volatile method of calculating the value of defined benefit pension schemes, we agree that this is a practical approach.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Yes, we agree that claw-backs should be included within the single figure.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We believe that in most instances it should not be commercially sensitive for companies to disclose retrospectively details of their performance against metrics within their annual bonus (and LTIP where appropriate). Although the vast majority of US companies provide very detailed retrospective disclosure of their performance against metrics in their annual bonuses, most companies in the UK don't, although we have seen some signs of improvement in recent years (we estimate that about 15 to 20% of UK companies now provide this information). Whilst we understand that disclosing targets in advance might be deemed as commercially sensitive, we are less convinced when a similar explanation is given for retrospective disclosure.

Since full disclosure of performance against metrics is essential for investors to assess pay for performance and the robustness of the performance targets, we think that if companies continue to have a degree of flexibility then they should provide a detailed explanation when they don't publish performance against metrics retrospectively.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We agree that the additional information proposed by the Government should improve investors' understanding of the potential benefits.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Yes, however as highlighted on page 29 (paragraph 84) of the consultation, companies will need to provide detailed disclosure of the vesting percentages for different levels of performance. We agree that expected values are often misleading and based on a number of unclear and opaque assumptions, which are of limited use to investors.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We agree with the Government's proposals which should provide clarity on the share ownership requirements and the status of directors' holdings of shares and options, and any conditions attached. It would also be beneficial for investors if companies were required to disclose if they have a policy on directors' hedging their share and option positions. Some companies disclose that this is prohibited however disclosure on this area is currently very limited in the UK.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We have mixed views on how useful a TSR graph is for investors as a proxy for management performance. Share price performance can be influenced by external economic factors which are essentially outwith management control (e.g. a commodities boom) therefore it is important to be mindful of any short-term volatility on the share price. A TSR graph is only of use to investors where it is relative to a suitable comparator group which includes a company's main competitors (where possible) and over a sufficiently long period of time (5 to 10 years).

Companies should have discretion to include other KPIs if this provides a more useful and meaningful illustration of pay for performance.

In addition, comparing total directors' pay to performance would be of benefit to investors.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We agree that auditing these numbers should give investors confidence that the remuneration report is free from material error.

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13 September 2012

Our ref: JR/BLC/BIS consultation

Email: James.Roberts@bdo.co.uk

Dear Barry

Directors' Pay - Consultation on revised remuneration reporting regulations

We are pleased to have the opportunity to comment on the above consultation issued by the Department for Business Innovation & Skills. As we noted in our response to the 2011 consultation on narrative reporting including directors remuneration, our overall view is that financial reporting within annual reports has become overly complex and is in need of simplification to enable user understanding. This can be enhanced by improvements within the narrative element of corporate reporting and by removal of outdated boilerplate disclosures. Indeed the current consultation notes that "remuneration reports have become increasingly lengthy and complex" and that "there needs to be "access to better quality and more concise information about pay".

The consultation notes that the Government will work with the UK Listing Authority to consider whether the requirements of the Listing Rules need to be reviewed. We believe that this is a necessity. If the Government wishes to succeed in its aim to simplify company reporting it is imperative that an exercise is carried out to compare, contrast and rationalise the current rules from various sources.

One of the key aims of the proposal is to introduce a single figure of payments made to directors. We remain unsure of the value of a single cumulative figure as it contains so many elements of remuneration which are variable in their calculation and contain an element of valuation. For example, including the value of long-term incentives in full on vesting may be confusing as they may have been granted three or more years before vesting and have depended on the company's performance over the full vesting period. We believe the single figure will oversimplify a complex number and could lead to erroneous and misleading comparisons.

We have set out our responses to the specific questions raised in the consultation below.

1. **The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document**

   The Government's intentions are to increase transparency in pay reporting, to give shareholders more power so they can hold companies to account and to promote good practice. There appears to be a view that the remuneration of directors in the largest listed companies is excessive and a combination of transparency and greater power for shareholders will make it more difficult for companies to increase directors' pay in the

future. Companies have run the risk of damage to their reputation and the press has campaigned against the excesses in general and vigorously against some companies in particular.

On the other hand, an increasing number of shares are held by investors whose aim is to make profits in the short term from buying and selling shares, not by investors who have a long term interest in the growth of the companies. The proportion of listed companies' shares held by insurance companies and pension funds has fallen dramatically over the last 20 years. These short-term investors appear to be less interested in directors' remuneration.

As well as aiming to deliver greater transparency, the draft regulations demand a consistent approach and are even more prescriptive that the old regulations in what must be disclosed and the format of the disclosure.

We believe the "single total figure table" may be less transparent than the existing disclosure rules for the following reasons:

a) The proposed regulation appears to omit any requirement for comparative information. There is currently a requirement to compare this year's total by director with the previous year's total (paragraph 7(2) of the existing Directors' Remuneration Report requirements in SI 2008/410).

b) The variable pay will largely be in the form of shares. Simply providing a cash figure showing the value of awards that are awarded and vest in the same period may mean very little (Column "d" and regulation 6(d) of the proposed regulations). We would prefer an option similar to that in paragraph 6(e) of the proposed regulations (relating to column "e") computing the value as a function of the number of shares, the proportion of the award that vests and the share price.

c) The value of long-term incentives received in a year may be confusing because the amount received will be the amount that has vested from awards actually granted three or more years ago. The benefit from those awards will depend on the Company's performance over the full vesting period.

On the other hand, at present, the share option table shows options exercised during the year (paragraph 9 of the existing Directors' Remuneration Report requirements in SI 2008/410). Once an option has vested, it is up to the individual to chose when they exercise an option. Showing the value vesting in a year may be a fairer method of showing the value of an award.

Greater clarity is required in respect of the "performance conditions" referred to in respect of columns "c" and "d". The existing Directors' Remuneration Report requirements in defining long term incentives schemes (paragraph 11(5)) refer to <u>one or more qualifying conditions with respect to service or performance</u>. It is unclear how service conditions are applied in the proposed regulations which only refer to final vesting being determined as a result of the achievement of performance conditions in the period being reported on (proposed paragraph 5(e)) and omit any reference to services. The proposed regulations refer to situations where full vesting is not achieved at the date of the remuneration report (proposed paragraph 6(e) (iii)). These seem to be mutually exclusive situations. For example, the consultation notes at paragraph 63 "within a 2012 report, the variable element of pay included within the single figure would be the bonus awarded for 2012 performance (even if that bonus has been deferred) and long term awards that cover periods where 2012 is the last financial year of the performance cycle." Consider a long term award that was granted based on the profits for the three years 2010 to 2012 but was only payable if the director remained in employment through to the date in 2013 when the award was finalised. Is that to be included in 2012 or in 2013 when the award finally vests and all qualifying conditions (service and performance) are met?

It would be useful to see some historic examples of the comparison of performance and pay graph (proposed regulation 13). Given the relatively short tenure of chief executives, we suspect that the total pay will fluctuate enormously. A new chief executive is likely to have significantly lower total pay in the first two years until his first award of long-term incentives vests. On year three, his total pay could then jump up.

The requirement to show shares of which the director is the legal owner (proposed regulation 14) will not necessarily deliver clarity. A director could have shares held by a nominee (such as a broker) or in an ISA. Also, as noted at 13 below, it is unclear whether the disclosure is restricted to shares and options awarded in respect of qualifying services or whether it is also to include those share and options that a director has acquired in the market or as a shareholder.

We have already referred to the earlier consultation on narrative reporting. This consultation notes that the government intends that all changes to the reporting framework should take place at the same time. Some of the provisions in these regulations (for example, changes in profits, dividends and overall expenditure) may overlap with requirements of those other regulations. It is important that companies are not forced to duplicate information and therefore increase the complexity of annual reports.

The consultation notes that the Government will work with the UK Listing Authority to consider whether the requirements of the Listing Rules need to be reviewed. We believe that consideration should be given to removing most of the detailed disclosures in Listing Rule 9.8.8 and inserting a requirement to disclose the information required by the relevant paragraphs of Schedule 8 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410). Such an approach is already taken in DTR 7.2.6. This would also maintain a level playing field between UK companies and an overseas company with a premium listing.

There is no reference to Schedule 5 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410). This currently includes provision relating to directors remuneration for all companies including quoted companies. We believe the requirements for quoted companies should all sit within Schedule 8. There are differences in the requirements between the two schedules.

We also note that certain disclosures in the existing Schedule 8 have been omitted from the proposed Schedule 8. We have already commented on the lack of a requirement for a comparative. We also note that the proposed Schedule 8 omits disclosure of sums paid to third parties in respect of a director's services (paragraph 16 of the current Schedule 8) and only requires disclosure of compensation for loss of office for those persons who served as directors in the period and not compensation for those who served as directors in a prior period (paragraph 15 of the current Schedule 8).

2. **What costs will companies face in adjusting to these revised reporting regulations?**

The cost will vary from company to company depending on the complexity of its arrangements and the extent to which work is done internally or with outside guidance. We anticipate additional costs in the following areas:

- articulating the remuneration policy in a way that fits with the future policy table required by Part 4;
- re-writing the remuneration report to satisfy the requirements of Part 3;
- calculation of the numbers for the table required by para 3, particularly for column "e";
- cross checking the report to confirm it complies with the new regulations, the Listing Rules and the Corporate Governance Code.

We expect that the majority of the costs will be one-off costs in the first year.

3. **The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?**

This question addresses the Future Policy Table. Such a table could lead to a much greater degree of uniformity in reporting policies relating to directors' remuneration. It will help people who use the accounts to compare the policies of different companies. It remains to be seen how much flexibility companies will include in their policy statement.

4. **The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.**

The proposed regulation 21 requires "a statement setting out all the provisions that relate to remuneration contained in the directors' service contracts". This could introduce unnecessary and additional length and complexity. As the consultation notes such contracts are available for inspection. If the intention is merely to make the details more easily available there could be a requirement to reproduce extracts on the company's website. The Government should avoid a knee jerk reaction of simply adding further lengthy disclosures to the annual report. Alternatively the company could summarise the main provisions of the contracts. If this is the intent behind regulation 21 it needs to be reworded.

The usefulness of the reporting and the "Total Remuneration Opportunity" chart (illustrated on page 18 of the consultation) will depend on the quality of the predictions.

As we noted in the previous consultation, typical performance criteria are complex and the decision as to whether an individual meets or exceeds targets is a subjective one made by the remuneration committee. It would be difficult to distil this process down into concise and meaningful disclosure.

If we assume that a significant percentage of the total remuneration for reaching stretch targets will be in the form of shares, how much will those shares be worth?

We can see from, for example, defined contribution pension statements that there can be a big difference between projections and what actually happens. Share prices as a whole have fluctuated but are lower now than they were 12 years ago. Is it safe to predict an increase in share prices for the next, say, three years for the purposes of this chart?

The example in the consultation document illustrates how difficult it is to prepare such a table. Wouldn't it be reasonable to assume that the salary that can be earned will be the same in monetary rather than percentage terms, or almost the same, for below target, on target and maximum performance? Wouldn't you expect the percentage of the whole represented by LTIPs to be much higher for maximum performance and zero for below target performance?

It is also unclear what is meant by Total Remuneration Opportunity for the purpose of proposed regulation 22. Is this meant to be an annualised amount, the amount receivable in the next financial year or something else?

In practice, we believe this chart will require supplementary guidance. As noted in the consultation, such guidance should be in place before these proposals take effect.

5. **The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.**

Some indication of the extent to which exit payments are at the discretion of the company would be useful.

6. **The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.**

We do not see a benefit in seeking the views of employees on the remuneration policy. If there is a requirement to include a statement on whether and how a company sought employee views, this could lead to companies feeling obliged to consult employees, whether this is of benefit or not.

7. **The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?**

Care must be taken that amounts are not included twice. For example, should deferred bonuses be included at the beginning or the end of the deferral period?

There is a mixture of past and future pay in the table: salary will have been paid in the year; a bonus will generally be paid after the end of the year; deferred amounts could be paid some time later. There will also be LTIP payments that relate to awards made several years earlier but that vest in the following year based on performance conditions achieved in the year in question.

These problems arise because, as noted in 1 above, it is unclear how service conditions are applied in the proposed regulations. If a long term award was granted based on say the profits for the three years 2010 to 2012 but was only payable if the director remained in employment through to the date in 2013 when the award was finalised is that long term award to be included in 2012 or when it finally vests and all qualifying conditions (service and performance) are met at the end of the service period in 2013?

8. **The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?**

While there may be occasional anomalies as highlighted in the consultation document, the application of the HMRC methodology will provide a consistent approach.

The proposed method of applying a factor of 20 to the pension has the important merit of simplicity. However, it makes no allowance for the fact that the pension at the start of the year would be expected to increase (for example by inflation) and therefore would give a misleading and overstated value of the true increase in pension value over the year. This would be the case even given the reduced upper limit of £50,000 pa on increases to pensions qualifying for tax relief in approved schemes, particularly for members with long past pensionable service. A simple way of overcoming this would be to increase the accrued pension at the start of the year by inflation, deducting that from the accrued pension at the end of the year, and applying the factor of 20 to the resulting increase.

9. **The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?**

Yes. But it is not clear from the proposed regulations how this is to be achieved.

10. **The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?**

The answer to this question depends on the performance conditions. Conditions such as earnings per share and total shareholder return are transparent and readily available. Other targets, such as profits or achievement of commercial milestones could be more sensitive. We would encourage some flexibility along the lines of "comply or explain" in the Corporate Governance Code.

11. **Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?**

Given the rules on annual pension limits, we do not consider pensions to be the most significant element of total remuneration. This was more of an issue when the annual limit on pension contributions was over £200,000.

Our preference would be to show at the start and end of the year, the accrued pension and the pension that could be taken on early retirement (if over age 55). This would show both the magnitude of the pension entitlement and also whether any preferential early retirement terms apply.

12. **The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?**

We believe that a face value approach could be more practical and informative than the projected value approach as it would appear to require less estimation of future movements. The actual value received will be reported later in any case as part of the single total number. However, we note that there is no definition or explanation within the proposed regulations of what the "face value" is meant to represent.

13. **The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.**

We welcome any true simplification of reporting requirements. The existing, more detailed disclosures (Schedule 8, regulation 9 and 12) also require disclosure of share based awards that have been granted but are subject to performance conditions before vesting. The proposed disclosure may assist in highlighting that a proportion of those share based awards may never vest.

The current disclosures in schedule 8 relate to share options and interests under Long term incentive schemes received in respect of qualifying services. The proposed regulation 14 does not appear to restrict the disclosures of shares and rights to shares to those received in respect of qualifying services.

Listing Rule 9.8.6 requires disclosure of changes in the interests of each director that have occurred between the end of the period under review and a date not more than one month prior to the date of the notice of the annual general meeting.

The proposed regulation 14 refers to shares of which the director is the legal owner. This will not necessarily deliver clarity. A director could have shares held by a nominee (such as a broker) or in an ISA.

14. **The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?**

We are not convinced that the graph will be useful. We have reservations about total shareholder return (TSR) as a measure of performance. There are many outside factors that influence share price. At least the current requirement to show a company's TSR relative to a relevant index allows the reader to take a view as to the impact of market fluctuations.

Having said that, we recognise that long-term investors are interested in achieving a good total return over an extended period.

The CEO's pay may be linked to key performance indicators that are not reflected in TSR or that affect TSR in different periods.

It would be useful to see some historic examples of the comparison of performance and pay graph (proposed regulation 13). Given the relatively short tenure of chief executives, we suspect that the total pay will fluctuate enormously. A new chief executive is likely to have significantly lower total pay in the first two years until his first award of long-term incentives vests. On year three, his total pay could then jump up.

If the government's concern is that executives are overpaid we believe that the cultural makeup of a company and its board is likely to be more important in setting remuneration that is a fair reward than further disclosures. Further disclosures will tend towards the boiler plate and we believe that consultation with major shareholders is likely to be more effective in putting the brakes on inappropriate remuneration policies.

15. **The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?**

No.

We would be very happy to discuss our response to this consultation with you should you require. Please contact James Roberts, Partner (on 01293591000 or at james.roberts@bdo.co.uk) or David Ogden, Director (on 02078933216 or at david.ogden@bdo.co.uk) should this be the case.

Yours sincerely

James Roberts
Partner
For and on behalf of BDO LLP

BG Group plc

BG GROUP PLC

EXECUTIVE PAY

RESPONSE TO CONSULTATION ON REVISED REMUNERATION REPORTING REGULATIONS ISSUED BY THE DEPARTMENT FOR BUSINESS INNOVATION & SKILLS IN JUNE 2012

About You	
Name: **BG Group plc**	**Organisation:** **BG Group plc**
Email: *Please send any correspondence to the Company Secretary, Steve Allen, steve.allen@bg-group.com*	**Address:** *100 Thames Valley Park Drive* *Reading* *Berkshire, RG6 1PT*

I am responding on behalf of (please tick):	
√	**Quoted company**
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other

QUESTIONS

1. ***The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.***

We have a number of comments on how well the Draft Regulations give effect to the policy set out in the Consultation Document. As these are detailed and lengthy we have set out them out at Appendix 1A below.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

There will undoubtedly be additional costs associated with adjusting to the revised regulations. This is expected to be largely in connection with advice regarding ensuring appropriate compliance with the regulations and to a lesser extent costs associated with the production of a new format remuneration report.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We are supportive of the use of a tabular approach, as we believe this will aid shareholder understanding.

We are also supportive of the proposal that the precise content of the table beyond the headings and outline content at Annex A will not be prescribed and instead be an area for the Company to agree with its shareholders. We would like to achieve a balance between providing our shareholders with sufficient information to understand our remuneration policy, but retain enough flexibility for us to operate our business and anticipate and respond to business situations in a timely manner.

The Consultation Document indicates (paragraph 38) that this policy table will only be required when the remuneration policy is subject to a binding shareholder vote, which could only be every three years. We consider that this table is important to understanding the remuneration policy and helps facilitate the readers' understanding of the implementation report. We would suggest consideration be given to requiring the publication of this table each year, even when the remuneration policy is not being subject to a vote.

We are supportive of the inclusion of narrative explanations of why performance metrics for variable pay have been chosen. We are pleased that the consultation document indicates that performance metrics will not be expected to be disclosed if doing so would harm shareholders interests. The current Draft Regulations do not however, include such a "carve-out". For complete clarity on this issue we would very much welcome the inclusion of such a carve-out within the final regulations.

We are supportive of the inclusion of a narrative explanation of whether (and if so why) the remuneration policy for Executive Directors differs from that for other employees.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Service contracts

The Consultation Document and Draft Regulations require the disclosure of all provisions relating to remuneration contained in the directors' service contracts.

Whilst we are uncertain of the benefits of this additional reporting requirement, we do not consider it to be too onerous. However, we would note that this requirement is likely to lengthen the report somewhat. We would therefore welcome a provision allowing companies to provide a link to the relevant provisions instead. Alternatively, perhaps companies could be required to disclose only fundamental remuneration provisions (such as those on salary, bonus and share plan awards) and not those on more minor benefits.

Scenario analysis

We are generally supportive of this disclosure and consider that this will be more useful than the current requirements to disclose the balance of fixed and variable pay.

The calculation of reward outcomes at threshold, maximum and below threshold will require companies to make various assumptions. For example, what share price assumptions should be used under each scenario. Whilst we agree that it is appropriate that valuation methodologies are not prescribed by the Regulations, we do believe, however, that it would be best practice for disclosure of the assumptions used to be made. This would allow the scenario analysis to be as transparent as possible to shareholders and other stakeholders.

Relative importance of spend on pay

We are not supportive of this additional disclosure as we do not believe it would aid shareholders' understanding of executive remuneration and its relationship to corporate performance.

The overall expenditure of pay by a company can change for a number of reasons not related to shareholder value creation. For example a company choosing to bring "in-house" work previously undertaken by contractors may increase its total pay cost, with a relatively neutral impact on profits and dividends. The opposite would of course apply if operations previously undertaken "in-house" were outsourced. In addition, our view is that it will be difficult for shareholders to draw comparisons between different companies based on this disclosure, given the huge variations in the make-up of different companies' workforces.

If the Government considers numbers must be reported we consider absolute spend, rather than change in spend, should be included. We would also ask the Government to clarify how many "previous years" are expected to be covered.

As the Government will be aware this information is already disclosed in other places in the annual report and therefore if stakeholders are interested in this information they can find it elsewhere in the report.

Frequency of reporting

As currently drafted, all the information it is proposed is reported under Question 4 above is only required to be produced when the Remuneration Policy is subject to a binding vote, which may be only every three years. We are not convinced that this is helpful. We would suggest the scenario analysis and information on service contracts is provided annually for information to aid users understanding of the remuneration report.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

It is unclear to us whether the requirements in connection with "exit payments" relates to situations where a director's service contract is terminated early and without due notice, or relates to all forms of cessation even where due notice is given. The table on page 19 of the Consultation Document and paragraph 26 of the Draft Regulations suggest it is all forms of cessation for which exit payment policy must be defined. We would be grateful for your clarification.

As set out in our response to the March 2012 consultation where an executive director's contract is terminated early and without due notice, the exit is often commercially sensitive and it is necessary to agree terms quickly (which may involve the exercise of discretionary powers by the remuneration committee) and move forward. We therefore consider it is important for companies to have sufficient flexibility to draft their policy on exit payments in a way which allows them to react appropriately and in the best interests of shareholders in the event such a circumstance arose.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We have severe reservations that this requirement will provide useful information and add value for shareholders and other users of the accounts.

BG Group is a global organisation with operations in over 25 countries. Whilst we operate formal employee surveys on a global basis, seeking feedback on a variety of matters, including views on their own pay and benefits; consultation on the broad principles of our remuneration policy is not a matter we would ordinarily consult with our employees on. In our view it is for the management and leadership of the Company to set the remuneration strategy and policy (and in the case of the executive remuneration, this would be the Remuneration Committee), in the same way as other aspects of our corporate strategy.

Results of our employee surveys are of course shared with the Remuneration Committee. We also spend considerable time briefing our Remuneration Committee on reward and benefit practices throughout the organisation to ensure they understand the remuneration arrangements for the wider employee population and how executive arrangements compare to these.

We would recommend that paragraphs 28 and 29 are removed from the Draft Regulations.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We are supportive of the reporting of a single total figure for remuneration for each executive, provided it is calculated on a consistent basis. We believe this will aid shareholder's understanding of reward, particularly in relation to the performance of the business during the year and aid comparison with peer companies.

The proposed methodology put forward for calculating the single figure seems straightforward and we agree it should give effect to the Government's intention. Our detailed comments on how the Draft Regulations give effect to this are set out in our response to Question 1 above. In the interests of brevity we have not repeated them in full. However we have the following summary observations:

- **Bonus-** As set out in our responses to Q1, we would be grateful for clarification as to where it is intended any non-performance related cash payments, or cash awards not under the bonus scheme, which are awarded for example to incoming executives in recruitment situations should be reported;

- **LTIP** –As set out in our response to Q1 we consider it would be helpful to distinguish between LTIP awards made in recruitment/retention situations and normal ongoing annual awards; and
- **Comparative data –** We believe it would be helpful to shareholders if there was also a requirement to report prior year comparative data for each of the amounts reported.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The proposed approach has the benefit of simplicity and ease of calculation. However we would ask you to note that it does have limitations and may materially over or under estimate the value of benefit accrual in certain situations.

In addition in utilising the methodology in s.234 of the Finance Act 2004 (which is referred to in the Draft Regulations) for these purposes it was not clear to us which inflation figure would be used to uplift the opening pension value. The relevant part of the Finance Act 2004 defines this as the "percentage (if any) by which the consumer prices index for the September before the start of the tax year is higher than it was for the previous September" but it is not clear how this should be translated into a situation where the period in question is a financial reporting period rather than a tax year. Although we have no specific recommendations in this regard, we believe that additional guidance is needed in the regulations to ensure that the methodology is applied consistently and, more specifically, that the same inflation figure is used by companies that have the same reporting period.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that any amounts clawed back should be included in the single figure where the amount being clawed back has been included in the figure for a previous year. Disclosures, however, should clearly distinguish between what has been paid and what has been clawed back perhaps by reporting the clawed back amount as a separate item.

The current Draft Regulations do not appear to incorporate this provision. We would recommend Paragraph 5 of the Draft Regulations be extended to incorporate this. Consideration would need to be given to the basis on which clawed back amounts should be disclosed particularly if the amounts clawed back are in respect of share based awards which may have subsequently increased or decreased in value. Provided that disclosure is not commercially sensitive we would also suggest that where appropriate, details of the reason for the application of any claw back should also be reported.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We are generally supportive of the requirement for companies to provide clear details of the level of payout or vesting under incentive plans and as far as possible what performance was achieved to support this. BG Group already provides comprehensive details in respect of its Long Term Incentive Plan, where the metrics used are not commercially sensitive and are externally verifiable.

We do have concerns about the publication of specific performance against individual metrics for our annual incentive plan. Annual incentive plans are by their name designed to motivate executives over the short term. Targets set are almost always commercially and operationally sensitive and we would not be supportive of the introduction of regulation which required detailed and extensive disclosure. Such an approach could potentially harm shareholders' interests.

In respect of commercially sensitive targets, such as those for our annual incentive plan, we would be comfortable reporting;

- What the performance conditions are and the relative weighting of each;
- Performance achieved for each condition, in terms of was it below threshold, between threshold and target, at target, between target and maximum, or at maximum;
- Whether the Remuneration Committee exercised discretion in arriving at award outcomes and the reasons for any discretion applied; and
- The resulting level of award (this will be included in the single figure).

We would recommend Paragraph 8 of the Draft Regulations be amended to reflect this. We would also recommend the Draft Regulations be expanded to include a specific statement making clear companies will not be expected to disclose commercially sensitive information.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We support the proposed disclosures on pensions. However it is not clear from the Consultation Document whether the Listing Rule requirements would continue to apply (Listing Rules paragraph 9.8.8R (12)). If not, then we consider that it is important that the additional detail on pensions set out in the Listing Rules (see below for a summary) continues to be disclosed and the Draft Regulations are amended to reflect this.

- The rate of accrual.
- The accrued benefits at the start of the year, as well as at the end.
- The transfer value of the accrued benefits at the start and end of the year. This provides an indication of the total cost of the pension to the company.

We understand the desire to simplify the report, but believe the above provides valuable information for shareholders in assessing the total pension benefit.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We are supportive of the proposal to report scheme interests awarded during the year at face value, provided that the requirement currently included at paragraph 12 (v) of the Draft Regulations to report the percentage which will vest at threshold performance is retained. We would also recommend extending the requirement to also show the value vesting at threshold performance (based on share price at grant).

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We are concerned that the Draft Regulations may remove information that is vital for understanding the outstanding awards held by executives.

The proposed aggregation of all outstanding awards into a single figure significantly restricts the information shareholders can currently obtain from the remuneration report. Without looking back through historical annual reports, the user is not able to establish, in relation to awards which neither vested or were granted in the year, for example:

- Under which plans the outstanding awards/options have been granted;
- When these awards/options are due to vest; and
- The exercise price for any share options (and therefore whether they are 'in the money' or not).

This information is currently found in the LTIP/share options tables in the DRR and is a requirement of the Listing Rules as well as Schedule 8.

For each separate outstanding award we would propose the following information is presented;

- Number of shares or options awarded;
- The date of award;
- The date of vesting;
- The share price/exercise price at the date of award; and
- Details of performance conditions attached to awards where they differ from the stated policy.

It is not clear from the consultation document whether the Listing Rule requirements would continue to apply (Listing Rules paragraph 9.8.8R (2 - 6)).

We would suggest that this lack of "snapshot" of information relating to all outstanding awards/options is addressed through some redrafting of regulation 14, along the lines of the suggestions above. In addition, there would seem to be some overlap between regulation 14 as currently drafted and Listing Rules 9.8.6R (1) and (2) (which require disclosure of information reported by companies under the Disclosure and Transparency Rules) which we would also like to see addressed.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We agree that it is important a summary of historic shareholder value creation relative to executive reward is presented to shareholders in an easy to use form. A graph is probably the best way of achieving this.

We also agree that total shareholder return (TSR) is probably the most objective, verifiable, measure of shareholder value creation (although it can be influenced by factors often outside of management's control) and that presentation of CEO pay rather than some form of Board average or Board Total is the most appropriate, given differences in sizes of Boards and distortions created by averaging. We would however welcome clarification that companies may add other measures, in addition to TSR, to the graph, if thought appropriate. We would also welcome clarification as to the method of calculating the measure of CEO pay in previous years – will companies be expected to produce a "single figure", on the same basis as the single figure proposed under the regulations, for previous years?

We do question whether it may be more appropriate to present the graph over a five year rather than 10 year period. This time period being more consistent with; (i) the typical tenure of a CEO; (ii) periods over which organisations typically monitor and present historic financial performance (for example 5 year financial summaries; review of financial performance and tracking of KPIs in our ARA; (iii) the period for which detailed business strategies are set and planned; and (iv) periods over which incentive arrangements typically operate (very few run for their full ten years – many are reviewed between 6 and 8 years and sometimes more often).

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We agree that the areas set out above should all be subject to audit.

Other comments

In addition to our response to the detailed questions above we also have the following comments:

Payments to former directors

Under the current reporting regulations companies are required to disclose “significant payments for former directors”. We assume this requirement will be maintained within the listing rules or included in the revised reporting regulations.

BG Group's response to Question 1 of the June Consultation Document

1. ***The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.***

Draft Regulations
Part 2 - Summary Statement
This states
"2. The directors' remuneration report must contain a statement by the director who fulfils the role of chairman of the remuneration committee summarising the contents of the report."

Paragraph 23 of the Consultation Document indicates that the purpose of the letter is intended to "summarise the key messages on remuneration and the context in which decisions have been taken".

This is inconsistent. We would suggest that the Draft Regulations be amended to reflect the Consultation Document.

Part 3 – Single total figure of remuneration
3
We understand the need for clarity and consistency of reporting. However the proposed format of the table and limited number of columns is relatively narrow (being broadly Salary (a), Benefits and Dividends (b), Pension (c), Annual Bonus (d), Long Term Incentive (e) and Total (f)). Presenting information in this way may result in shareholders having less information in tabular form than is currently the case. For example BG Group currently sets out details of the amount of annual bonus, payable in cash and that which is deferred in its remuneration table in separate columns. Similarly where cash based annual incentives or long term incentives are provided under different plans or in recruitment/retention situations, we consider it may aid shareholder understanding if these could be presented in separate columns. We would ask that consideration be given to incorporating this flexibility. This may also serve to avoid the extensive use of footnotes to the table.

Part 3 – Single total figure of remuneration
5
The current drafting implies that only salaries and fees should be reported in respect of "qualifying services" (see paragraph 5(a)). We assume that the intention is that all elements of reward reported under each of the headings (a) to (e) inclusive of the remuneration table should be in respect of "qualifying services".

We would suggest that paragraph 5 be amended to reflect this. We believe this could be achieved by moving the words "in respect of qualifying services" to after "the sums" in the opening sentence so it reads:

"In the table in paragraph 4 the sums, in respect of qualifying services, that are required to be set out in the columns are-"

Part 3 – Single total figure of remuneration
5 (d)
The first sentence of this section refers to “money or other assets awarded ***in the*** reporting period...in respect of achievement of performance conditions ***that relate to that period***”.

We assume this section is designed to capture annual bonus amounts awarded in respect of the financial reporting period. In practice annual bonus amounts reported for a financial year are the bonuses which relate to performance in that year. Whilst accrued for in the financial statements they are actually determined and awarded after the end of the financial year.

To clarify we would suggest the wording be amended to, for example;
“money or other assets awarded ***in relation to the*** reporting period...in respect of achievement of performance conditions ***that relate to that period***”.

We would also observe that currently the amounts reported in column (d) are limited to amounts received or receivable which have performance conditions attached. Whilst obviously remuneration committees are concerned to ensure as far as possible remuneration packages awarded to incoming executives in hiring situations are consistent with the company’s remuneration policy, it can on occasion be commercially necessary to compensate an incoming executive in cash for part or all of the annual bonus lost at his/her previous employer. Is it the intention that such payments would also be reported in column (d), or if not in column (d) where is it intended they are reported?

5d(i) and (ii)
In general we found both these paragraphs a little confusing, particularly as the words “awards” and “payments” appeared to be used synonymously, when we are not sure that was the intention. We would recommend the wording of both these paragraphs is reviewed.

We also consider it would be helpful to clarify what is meant by “performance conditions” and “vesting” and include both in the interpretation section.

Part 3 – Single total figure of remuneration
5 (e)
Again as mentioned above, (in connection with 5 (d)) we consider it would be helpful to clarify the terms “performance condition” and “vesting”.

We also feel it would be useful to refer to performance periods – being the period over which the performance condition is measured (as performance is not always measured over financial years but from grant to vesting). We assume the intention is to report the value of long term incentive awards which vest in respect of performance periods ending in the year being reported on, even where the actual vesting takes place in the following year?

In addition, the reference in 5(e)(ii) to "awards granted under schemes" appears to suggest that awards granted during the year should be included in the single figure. We understand that this is not BIS' intention and note that if correct, there would be significant overlap between this and the requirements in Regulation 12. Therefore we would suggest that 5(e)(ii) begins "the final value is…".

Part 3 – Single total figure of remuneration
6(d)
It is clear that annual bonuses subject to deferral must be included in 5(d). We assume that they should also be included if they are subject to claw back. If this is the case, we would suggest that "and/or subject to claw back" is added after "amounts deferred" in 6(d).

Part 3 – Single total figure of remuneration
6 (e) (ii)
Whilst the use of market value options has declined, we believe that in arriving at (XYZ) the exercise price of any share options should be deducted from the market value of the shares at the date of vesting. Whilst this is referenced below in (e) (iv), it may be helpful to explicitly refer to (e) (iii) being subject to (e) (iv).

Part 3 – Single total figure of remuneration
6 (e) (iv)
This paragraph states that where share options have been included in the single figure the amount shown should be net of the amount the individual was required to pay to purchase the share.
As options may not have been exercised and many are exercised under "Sell to cover" type arrangements we would suggest amending to "the amount the individual is required to pay to purchase the shares".

Definitions applicable to the table
7(2)
It is unclear what is intended here. Is the intention benefits received in advance of a director commencing qualifying service are to be treated as having been provided on the first day of commencement of qualifying service, or first day of employment, as these may be different? Also, we assume that 7(2) is only intended to cover benefits paid in respect of qualifying services and would therefore suggest adding this specifically.

Variable pay – additional disclosures
8 (2)
This paragraph refers to "shares". We assume the intention is that disclosure is wider than just share based payments. Consideration should be given to replacing the word "shares" with "amounts".

If the intention is for the disclosure to extend to performance conditions, for example for annual bonus awards then we have concern over the level of detail expected to be reported in respect of each performance condition under 8(2). Performance conditions and levels of threshold, target and maximums set for annual bonus arrangements are frequently commercially sensitive and it would not be in the interests of the Company and its shareholders to report on them in detail. We have set out in our response to Draft Consultation Question 10 below the detail we would envisage reporting for commercially sensitive performance metrics. We would recommend the drafting of paragraph 8 be amended to reflect this and to include a specific carve out for commercially sensitive information.

Variable pay – additional disclosures
8(3)
This paragraph suggests that where any discretion exists in respect of an award, whether or not such discretion has been exercised should be explained. We are concerned that the current drafting of 8(3) is wider than intended. By their nature, such awards include various discretions and we would assume that such discretions only need to be explained if they have actually been exercised. We are concerned that if all discretions must be explained, even if not exercised, additional length would be added to the report without being helpful to shareholders. Our view is therefore that the drafting of 8(2) should be narrowed to require explanation only of a discretion which has actually been exercised.

Loss of office payments
11
It is not clear from the current drafting whether the disclosure is intended to also include details of the treatment of vested and unvested share awards when a director ceases to hold office and employment. As you are aware, some share awards may subsist following cessation of office/employment and vest at a later date.

If the intention is to include such share awards, this could be clarified by adding an additional paragraph stating:

"(e) the treatment of any outstanding incentive awards that vest on or following the termination of office"

In addition, we assume that under 11(d), companies are only required to explain any discretion that has actually been exercised (also see above in relation to 8(2)). If so, we would suggest amending 11(d) to read "if discretion allowed for within the policy on exit payments was exercised, the outcome of such exercise".

Variable pay awarded during the financial year where the value will be determined according to the achievement of performance condition in future periods
12

In respect of the information set out under 12 (b) we believe some expansion of the information which should be disclosed is required. Specifically where awards are granted over shares in the Company details of (i) the number of shares over which the award is granted and (ii) the market value of a share at the date of grant should be disclosed. Similarly if the awards over shares are made in the form of share options the option exercise price should be disclosed.

We would also recommend:

- The text of 12(b) (iii) and (iv) should be expanded to make it clear that the face value of the award and maximum values at vesting should be calculated using the market value of the asset or shares awarded at the date of grant of the relevant award. That is we assume the intention is that any potential future share price appreciation /depreciation from the date of grant to vesting is ignored when calculating the maximum value on vesting; and
- The requirements under 12(b)(v) to show percentage vesting at threshold be extended so that the value (using share price at the date of grant) vesting at threshold is also shown. In this way we believe shareholders will get a more representative picture of values (in current terms) which may be received if an award vests.

Two minor drafting points:

- "scheme interest" is not defined; and

- (vi) and (v) are mis-numbered.

Consideration by the directors of matters relating to directors' remuneration
15 (c) (i) (iii)

Paragraph (95) of the Consultation Document indicates that for each consultant providing advice to the Remuneration Committee the "total cost of advice on remuneration and basis on which they are paid" should be reported.

The current Draft Regulations at paragraph 15 appear to extend this requirement to also disclose fees for "any other services". This is inconsistent with the Consultation Document.

We would recommend this is clarified. In order to ensure the Draft Regulations reflect the Consultation Document our preference would be for the requirement to disclose fees for any other services be removed.

BHP Billiton

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26 September 2012

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
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BY EMAIL: executive.pay@bis.gsi.gov.uk

Dear Mr Walker

I am pleased to provide a brief response from BHP Billiton to BIS's consultation paper on *Directors' Pay: Revised Remuneration Reporting Regulations*.

We support the general thrust of the proposals and were pleased to have the opportunity to work with the Financial Reporting Lab project to determine how the new single figure should be calculated and disclosed. In addition we look forward to working with government and shareholders to help ensure that the changes have a lasting impact.

We also support the desire to reduce the length of the Remuneration Report by removing information that may not add to the overall quality of disclosures from a shareholder/user perspective. However, because we are dual listed, there is a high chance that while the UK regime looks to make reporting simpler, the necessity for us to report against the Australian regulations as well as the UK regime may mean that retail and institutional investors see no material change in our Remuneration Report. (Given our ADR programs we also need to stay across U.S. governance developments.)

There are specific areas where we (like other companies, shareholders and other stakeholders) might prefer a slightly different approach in the detail. There is one particular example we wish to highlight. The Australian Federal Treasury is currently considering introducing a 'single figure' disclosure requirement (usually referred to as 'actual pay' or 'realised pay' in Australia). However, the way in which the Australian proposal deals with the reporting of equity awards (short-term and long-term) for any particular reporting year differs materially from that in the BIS consultation proposals.

If the UK and Australia were to continue down their respective paths, we are in danger of having to report more than one single figure. Based on the current proposals, we would need to disclose two different single figure disclosures, as well as a third figure in the 'statutory' remuneration table which is currently required under the Australian Corporations Act. This would of course be potentially confusing for users of our Remuneration Report. Given the governance issues around remuneration between the UK and Australia, alignment in approaches would be desirable if at all possible. We have engaged with the Australian bodies to ensure they appreciate the proposed UK approach, and would consider it appropriate and prudent that BIS does likewise if it hasn't already.

Our other comment relates to several aspects of the consultation proposals. Companies use a wide range of remuneration structures. There are valid business reasons for doing so – different industries have different product cycles, for example, and executive pay should reflect these different circumstances. In our view disclosure requirements should be crafted with this in mind. We therefore favour less rather than more prescription when it comes to disclosing the key elements of remuneration and information about pay policy (question 3), exit payments policy (question 5), the obtaining of employee views (question 6) and performance against metrics (question 10). A related comment is that condensing complex information into tables and graphs is useful for clarity and comparison. However, there is some risk that this will come at the expense of a fuller understanding of the particular circumstances impacting performance.

We would be very happy to discuss this further with you.

Yours sincerely,

Sir John Buchanan
Chairman, Remuneration Committee

cc Richard Carter, Director, Business Environment, Department for Business, Innovation and Skills
Gemma Peck, Policy Manager, Executive Remuneration, Department for Business, Innovation and Skills

Brussels European Employee Relations Group

BEERG

Comments on the Revised Remuneration Reporting Regulations

Introduction

- The Brussels European Employee Relations Group **(BEERG)** provides a forum for European employee relations specialists and in-company employment lawyers to discuss issues of mutual concern, including Directors' remuneration on which they may advise their employers. We now have over 60 major transnational corporations in membership.

- A substantial number of these companies are incorporated in the UK or have a controlling interest in businesses so incorporated, and as a result have a direct interest in the proposed revisions to the remuneration reporting Regulations.

- A group of our members had an opportunity to review the proposed revisions to the Remuneration Reporting Regulations and the accompanying consultation document at a meeting in London in July. The comments below reflect that discussion.

- The consultation document seeks views on the central question of how well the draft Regulations give effect to the policy set out in the consultation document; it then asks about the costs of adjusting to the Regulations; and 13 further questions are posed on the general practicability and effectiveness of most of the specific extensions or changes to the reporting requirements.

Effectiveness

- There appear to be two closely linked objectives of the proposed legislation:
    1. to address "failures in the governance of directors' pay"; i.e. to tackle what the Secretary of State describes as " a disconnect between pay and performance in large UK listed companies"; and
    2. to provide shareholders with "the clear, high quality information they need to monitor and engage with companies".

- In other words, the Government looks to better informed shareholders to exercise their voting powers, to address the perceived failures, including via: a new, binding vote on remuneration policy; and revised advisory voting powers on the implementation of that policy which will necessitate a review of the policy itself where shareholders have expressed their dissatisfaction with its implementation.

- Shareholders already possess considerable influence over Directors tenure and their remuneration where they choose to exert it, as the well-publicized examples of what has been called a "Shareholder Spring" this year have demonstrated. The new regulations would assist them further in understanding Directors' pay and holding the Board and its Remuneration Committee to account for Directors' remuneration and exit packages. It will empower the owners to rein in excessive behaviour; but it will remain a matter for their discretion as to when and how they utilize it. Not every example of behavior that attracts public controversy will be caught. We agree, however, that this "shareholder empowerment" is the appropriate approach to take.

- We also note that the impact will be broader than on UK listed companies; rather, as the Impact Assessment indicates, it will apply to all companies incorporated in the UK and listed on a main stock exchange in the UK, US or an EEA state.

Costs

- There were no serious concerns about the costs of reporting in the proposed manner. We note, however, that the policy report element introduces new requirements which will involve some additional work. The extra work involved will be lessened if, as the consultation paper anticipates, policy reports need only be developed once every three years. Note, however, our concerns set out in further comments below regarding relatively minor adjustments on 'policy' issues, unless suitable wording proves to be applicable through the promised guidance. Otherwise, the new requirements may lead to an obligation to revise the policy report and obtain the necessary endorsement from shareholders annually.

Other questions

- We have no detailed comment to offer on the other questions raised. The specific proposals to which they refer appear generally to be designed to deliver fuller information on Directors' remuneration in a timely and comprehensible way to shareholders. No matter how carefully the individual provisions are worded, it is to be expected that those who wish to provide more generous remuneration to attract or retain key talent will find ways of bypassing such provisions, possibly by appointing key executives to roles that do not strictly qualify as Directorships.

- Ultimately, much will depend on the will of shareholders to supervise and intervene; the new proposals should assist them where they wish to do so.

Further comments

- The Implementation report attempts to link actual pay of Directors to actual performance. In this context, we believe that the appropriate measure of actual pay should be at vesting (in the case of restricted stock or performance shares), or exercise (in the case of stock options). Otherwise, fluctuations in share price until the time when the compensation is certain could change the value dramatically (e.g. compare the value of stock-based incentives in July 2008 with December 2008).

- The Policy report is a major development. It is intended as a forward looking document, setting out all the elements of a company's policy for Directors' remuneration in the upcoming period and the factors taken into account in setting it. The Consultation Document, however, states that, when it comes to the elements in this report that set out
    - percentage change of profits, dividends and overall spend on pay;
    - the metrics used; and
    - the comparison of % rise in workforce pay with CEO's,

  the data which must be provided in the Policy report will refer to actual numbers for the preceding period, rather than a forecast. This is an important clarification that needs to be reflected fully in the documentation introducing and accompanying the revised Regulations. It would be quite impractical, as well as potentially disruptive and damaging to the business and the livelihoods of all its employees, to require forecasts on these points.

- We understand the rationale for attempting to show how total pay for the CEO is moving and how that compares to pay movements elsewhere in the Company over the long term. However, it is important to set such comparisons in context. The total pay bill will be affected by ongoing restructuring, including divestments, outsourcing and acquisitions which will inevitably impact the labour or skill intensity of the mix. It is not unusual in these circumstances for the pay of each worker employed at the end of a reporting year to have risen by more than the average earnings index compared to that worker's pay the previous year, though the average pay level across the workforce may have gone down. Similarly, pay for any group possessing key skills must always be related to market demand rather than tied to the general movements for the majority in any given period; and that applies particularly at CEO level. In addition, where the majority of CEO compensation comprises long-term incentives aimed at ensuring successful strategies, rather than the settled and certain pay packages of other workers, the true value of that remuneration will be tentative and unclear, and cannot be accurately determined in the year of grant. These considerations need to be clearly expressed in the proposed guidance accompanying the Regulation, to guard against the media and others making simplistic analyses which lead to false and damaging conclusions.

- We note that the example policy table offered anticipates providing the target, in terms of the percentage of salary in respect of bonus, as well as the potential maximum. We think that this is a useful indicator, and not only for the bonus element, as it demonstrates the intentions of the Remuneration Committee in terms of their expectations against the target performance of the company. However, the Regulations (19(c)) focus only on the 'maximum potential value', which is likely to be misleading as its achievement will normally depend on delivering truly exceptional company performance, well beyond reasonable expectations.

- We appreciate that the purpose of having separate policy and implementation reports is to give shareholders access to better quality and more concise information about pay, and particularly how it links to performance, so that they can better hold the Board to account. The consultation document anticipates that the policy may be set for up to 3 years, and possibly longer if re-endorsed by the shareholders, with the annual implementation report allowing for checks of outcomes against that policy. We believe this makes sense. However, there will need to be some flexibility and provision for discretion. Pay plans tend to be revised annually in response to market and competitive conditions. There must be more scope for this than is currently allowed within the Regulations, otherwise a binding vote will be needed every year, which all parties agree is not desirable. For example, a business that runs Long-Term Incentive Plans on a rolling basis may amend or refine the format for the next 3-5 year tranche from one year to another, while retaining a close link between pay and performance; this should not automatically necessitate a new binding vote on a new policy report each year.

- The consultation document contains a welcome acknowledgement that the Regulations "will need to be supplemented by clear guidance on the level and type of information that should be reported". It goes on to say that this should

    1. be jointly agreed by the business and investor communities;
    2. act as a "gold standard" of remuneration reporting; and
    3. be in place before these proposals take effect

  This raises important questions about how this guidance will be developed and what opportunities there will be for companies to contribute, in the context of Regulations that are not yet finalized but which are expected to take effect as soon as autumn of next year. The guidance will be needed well in advance of that date.

  There will also need to be clarification regarding the status of this guidance. There is an important distinction between 'best practice' guidance that companies may aspire to, and a code of practice with the backing of statute or a regulatory body, to which they may be held as an obligation by their shareholders or by regulatory authorities. Since we understand the government's main objective to be empowering shareholders, we would expect this guidance to replace or at least be compatible, and not conflict, with advice being developed by the investment community, such as the Association of British Insurers.

  The US experience suggests that, from the outset, the aim should be to make such guidance as clear and succinct on what is to be disclosed, and how; otherwise legalistic rather than practical responses will result and the objectives of the Regulation will be badly served.

- As the consultation document notes, there is further separate but related activity within the Financial Reporting Council as it revises the Corporate Governance Code. The BIS has also commissioned Lord Kay's Review of UK Equity Markets and Long-term Decision Making, published on 23 July, which looks at the establishment of the right incentives, including on directors' remuneration, at Chapter 11. We note that he warns against "the provision of large quantities of data, much of which is of little value to users.[1]" Less closely connected, but also relevant is Lord Hutton's Review of Fair Pay in the Public Sector.

[1] The Kay review of UK Equity Markets and Long-Term Decision Making: Executive Summary, paragraph xi

- As far as possible, we need consistent guidance on what is required and expected in respect of Directors' remuneration – what it should cover, how it should be established and the responsibility of and towards shareholders. We look to BIS to ensure that whatever is established now will provide a firm and lasting framework within which business and shareholders can work.

- As we have noted, the impact of the proposed Regulations will be broader than those firms incorporated in the UK that are UK-listed. As the Secretary of State has noted in the House, the US has already revised its reporting requirements; other countries are also reviewing their reporting requirements, and EU-wide provisions are a possibility. We would urge that experience elsewhere and plans in other jurisdictions, particularly across Europe, should be studied, with a view to creating the most practical and effective arrangements before the Regulations and Guidance are finalised.

- We understand that the new requirements are currently intended to come into effect from October 2013. That date, of course, is provisional and dependent on the Parliamentary process. Whatever the initial date for bringing in the new requirements, there will be an inevitable disconnect in many companies during the first year between the new policy report and the implementation report covering the previous 12 months: their first implementation report will refer to a period before any relevant policy report existed.

- We believe that it is important that a clear timetable for introducing the new requirements is provided. This should ensure that both the final Regulations and the promised guidance are available at least 4 months and preferably not less than 6 months in advance of the Regulations coming into effect in order to allow companies to develop compliant policies. The Regulations should allow for a transitional interval of not less than 15 months before the obligations in respect of assessing the implementation report against a policy report come into effect. Transitional guidance will be needed to assist Boards and their remuneration committees in managing through this period. The transitional arrangements must also be clearly explained to shareholders and commentators at the outset and again throughout this period, in order to guard against unrealistic short-term expectations about the impact of the new regulatory regime. Otherwise unreasonable and unnecessary damage may be done to the reputation, value and prospects of major businesses at a time of continuing economic difficulty; and the new rules are likely to be wrongly criticized or dismissed for lacking impact.

Center on Executive Compensation

Center On Executive Compensation

September 26, 2012

VIA EMAIL

Barry Walker
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RE: Center On Executive Compensation Comments on the Revised Remuneration Reporting Regulations

Dear Mr. Walker:

The Center On Executive Compensation ("Center") is pleased to submit comments on the Department of Business, Innovation and Skills' proposed revisions to the Remuneration Reporting Regulations. The Center is a U.S.-based research and advocacy organization that seeks to provide a principles-based approach to executive compensation policy from the perspective of the senior human resource officers of leading companies. Headquartered in Washington, DC, the Center is a division of HR Policy Association, which represents the chief human resource officers of over 335 large companies, and the Center's 100 subscribing companies are HR Policy members who represent a broad-cross-section of industries. While most Center Subscribers are headquartered and listed in the United States, a large proportion has a significant presence in the U.K. and European markets.

The Center's primary purpose in commenting on the proposed changes is to give our perspective on the impact of expanded executive remuneration disclosure requirements, based upon changes that have been made in the United States since 2006, and to urge that those experiences and the experiences of other countries be factored into the development of the final regulations. Because the market for executives extends beyond any one country's border and is truly now a global market, the Center's comments also urge the BIS to ensure that enhanced transparency – which is a desirable end -- does not inadvertently affect the ability of companies to attract or retain senior talent.

The Center strongly supports clearer disclosure of director remuneration that will truly foster greater investor understanding of whether pay and performance are aligned at a particular company. While there are a number of approaches to achieve this end, the Center supports disclosure of a comparison of realized pay to actual performance rather than estimates of potential payouts. The Center also believes that it is important to ensure that disclosure does not encroach on the flexibility of companies to determine how pay should be delivered, or impact their ability to recruit and retain employees.

In addition, there should be a balance between the quality and quantity of disclosure. Expanded remuneration disclosure in the United States has generated widespread criticism by investors and companies alike that the disclosures have become too long and in many cases may have effectively reduced transparency by making it difficult for investors to find information they are seeking. Practices are improving, but length continues to be an issue. In response to investor requests, companies have begun to include executive summaries at the front of their disclosures to allow investors to identify key issues and prioritize where to spend their time. Although the proposed letter from the chair of the remuneration committee appears to be such a summary, the Center urges the BIS to implement revised regulations that minimize unnecessary information in disclosures to allow an effective and efficient flow of information. For example, the proposed increase of disclosure about the wider employee context of director remuneration calls for companies to disclose the comparison metrics taken into account (if any) and how they were taken into account, along with the percentage increase in pay of the workforce and the percentage increase in pay of the CEO. Because the pay levels of employees at all levels of a company are typically determined based upon the skills required, the market for that talent and the overall importance to the company, there is a significant question regarding whether this information would be useful to investors in making investment decisions.

Another concern when making the decision to increase disclosure requirements is that significant expertise will need to be developed within the government in order to understand and implement the new regulations. In the U.S., when new and expanded disclosure regulations were implemented in 2007, the staff of the U.S. Securities and Exchange Commission reviewed a random set of roughly 300 company disclosures for compliance and issued comment letters to them. It was quickly discovered that the SEC professional staff, while experienced in other aspects of corporate disclosure, were not sufficiently familiar with corporate pay regimes or compensation disclosures. Since 2007, great strides have been made, but the initial communications led to considerable frustration on the parts of companies and regulators. Finally, the expansion of disclosure requirements in the U.S., Canada and Australia give the U.K. a body of experience from which to work, and the Center urges that these examples be used as the final regulations are developed and implemented.

The proposed revisions to the regulations highlight the focus of the “shareholder spring” on greater accountability for pay regimes in the U.K., it is important to understand that the market for senior director talent is increasingly global in scope. The regulations should be careful to focus on greater transparency rather than regulating the structure or amount of compensation, so that U.K.-listed businesses are not negatively impacted within the global market for talent. Companies are increasingly reaching across continents to secure the best executive talent. Emerging markets such as China, Brazil and India, which are experiencing a shortage of qualified executives, can support highly competitive pay packages to attract top talent from around the world, including from companies based in the West. The Center urges BIS to consider the impact this battle for talent might have on companies hampered by requirements which make it difficult for them to remain competitive with regard to pay design and delivery for directors.

Some data help put this point into perspective. A 2010 Korn/Ferry survey of global executive mobility reported that 82 percent of executives said they were willing to relocate to a different region, state or country, and more than half said they had already accepted an international assignment.[1] A recent talent mapping study by executive career site Experteer showed that U.K. executives are particularly willing to move – 26 percent of senior professionals

[1] Korn/Ferry, The Executive Quiz (2010), http://ir.kornferry.com/phoenix.zhtml?c=100800&p=irol-newsArticle&ID=1420936&highlight.

changing jobs between 2010 and 2011 chose to work in a new country, compared to Germany where the figure was only seven percent.[2] To the extent overly prescriptive disclosure requirements prevent U.K.-listed employers from retaining their executive talent, inability to compete could impact the competitiveness of UK employers and perhaps lead to a talent drain into more business-friendly markets.

Further evidence of the market for talent comes from leading global management consulting firm Booz & Co.'s 2011 annual global study of worldwide CEO succession patterns, which noted that CEO turnover is on the rise again, largely due to the improving economy in many parts of the world. More than 20 percent of incoming CEOs came from outside the company (up from just 14% in 2007) reflecting a wider net being cast by companies to obtain CEOs with experience in multiple regions. The report also noted that the number of companies based in emerging markets has more than doubled, rising from 10% in 2006 to 25% in 2011, while the number of companies headquartered in Western Europe dropped from 26% to 19%.[3] These emerging markets are experiencing a chronic shortage of executive talent and are willing to pay to obtain it.

In sum, the Center believes that greater transparency is worthwhile and should be adopted, but that the impact on global competitiveness should be factored into the development of the regulations.

Conclusion

The Center On Executive Compensation appreciates the opportunity to comment on the proposed revisions to the Remuneration Reporting Regulations. Please do not hesitate to contact me at tbartl@execcomp.org if you have any questions about our comments or would like to discuss them further.

Sincerely,

Timothy J. Bartl
President

[2] Experteer, OMIS Research, Talent Mapping (2011), http://www.experteer.co.uk/about/press_release/european-executive-talent-movement.
[3] Booz & Company, CEO Succession Report, 4 (2011),http://www.booz.com/media/uploads/BoozCo_CEO-Succession-Study-2011_Extended-Study-Report.pdf.

Chartered Institute of Management Accountants, The

Chartered Institute of
Management Accountants

26 September 2012

Mr Barry Walker
Department of Business, Innovation and Skills
1 Victoria Street
London
SW1H 0ET

via email : Executive.pay@bis.gsi.gov.uk

Dear Mr Walker

Directors' Pay: Consultation on Revised Remuneration Reporting Regulations

The Chartered Institute of Management Accountants (CIMA) welcomes this consultation on the reporting of executive remuneration as we believe effective reporting of directors' pay and its link to the achievement of strategic objectives is a prerequisite for the promotion of resilient, robust and successful businesses that will help to create long term growth.

We support the government in its intention not to micromanage the incentive policies of organisations. There is a significant risk to the competiveness of businesses if mechanisms that determine or limit executive pay are imposed artificially especially if such regulations were introduced unilaterally by either individual countries or regional authorities. The quantum of directors' pay should be decided by market forces but for the market to work effectively then appropriate information needs to be reported effectively. It is our view that these draft regulations provide a comprehensive and balanced regulatory response to the reporting of executive pay and we encourage investors and other stakeholders to actively engage with companies on the basis of the information that will be provided.

We would like to emphasise the importance of the covering letter from the Chairman of the Remuneration Committee that the draft regulations propose will preface the remuneration report. In particular we encourage the chairmen to personally engage with this process. The most effective letters that we have seen in this area are written in a personal style balancing readability with the necessary remuneration content.

Question 14 refers to the draft requirement for a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. The consultation paper asks, inter alia, whether this graph would be useful and if so, whether CEO pay is the best comparator. We agree that this information is useful. We suggest that trend information regarding the percentage relationship between pay and total shareholder return would also be useful. In respect to the question as to whether CEO pay is the best comparator we would prefer that total directors' pay is used. This preference is based on a number of factors :

- As discussed in the consultation paper, the average tenure of CEO's is less than ten years and so a graph using CEO pay is likely to cover a number of Chief Executives;
- It is the board under the executive leadership of the CEO that drives performance; and
- Using total directors' pay further encourages collective board responsibility which we support and is one of the elements underpinning the recent BIS narrative reporting proposals.

We agree with the Government that these draft regulations provide an effective framework within which companies and shareholders can set, agree and implement pay policy and further that they will need to be supplemented by clear guidance on the level of detail and type of information that should be reported. The consultation paper envisages that this guidance should be jointly agreed by the business and investor communities and we encourage these parties to actively engage in this debate which we suggest would be most effectively held under the auspices of the FRC's Financial Reporting Lab.

We would be pleased to discuss with you any aspect of this letter that you may wish to raise with us.

For and on behalf of CIMA

CHARLES TILLEY
Chief Executive

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INVESTORS IN PEOPLE

Chartered Secretaries Australia (CSA)

CHARTERED SECRETARIES AUSTRALIA

Leaders in governance

12 September 2012

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Dear Mr Walker

Directors' pay: revised remuneration reporting regulations

Chartered Secretaries Australia (CSA) is the peak body for over 7,000 governance and risk professionals in Australia. It is the leading independent authority on best practice in board and organisational governance and risk management. Our accredited and internationally recognised education and training offerings are focused on giving governance and risk practitioners the skills they need to improve their organisations' performance. Our Members are all involved in governance, corporate administration and have a thorough working knowledge of the operations of the financial markets, the needs of investors and the corporations law.

We welcome the opportunity to comment on the consultation paper, *Directors' pay: revised remuneration reporting regulations* (the paper). CSA is interested in this issue because any reform in the United Kingdom (UK) will affect UK/Australia dual-listed companies and we are also conscious of the increasing convergence of regulation globally. This submission is considered relevant as earlier consultation papers referenced the changes in law relating to executive remuneration that have been introduced in Australia.

CSA believes that shareholders should have the capacity to hold directors accountable for their decisions on remuneration, as well as other decisions affecting the performance of a company. We support in principle proposals that aim to ensure that robust governance arrangements are in place to ensure director accountability when setting executive remuneration. Notwithstanding this, we have taken the opportunity to point to the practical implications of some of the proposals.

Our comments on the consultation questions follow.

Yours sincerely

Tim Sheehy

Tim Sheehy
CHIEF EXECUTIVE

General comments

CSA notes that there are practical implications that require attention in order for the regulations to be practically and feasibly implemented.

- The implications of a binding shareholder vote on remuneration policy remains problematic for companies in relation to executive directors who have not yet been appointed, particularly those from other jurisdictions. For example, a proposed CEO may be a Canadian, and seeking a contract with Canadian terms outside of the approved remuneration policy. This candidate is the best person for the role, as the board has conducted an international search and subjected all candidates to a due diligence process and informed consideration. It is not in shareholders' interests for the candidate to be rejected, due to the remuneration policy.
- If the legislation is too prescriptive, it will not be able to accommodate circumstances as they arise. There is no provision for directors to make retention payments to key staff at the times when they may be most needed, that is, when the company is experiencing difficulties or subject to a takeover and key people need to be retained.
- CSA recommends that some form of flexibility be granted to the board to act in the best interests of the company in relation to remuneration structures.
- Transition payments have not been accommodated in the draft regulations. Any reform to apply a binding vote to remuneration policy needs to take account of long-term contracts that have been in place for some time. Although legislation can override an employment contract, we strongly recommend that the principle at law of legislation not taking retrospective effect should operate. Any new law should apply to new contracts only.
- If the remuneration policy is rejected by shareholders, the existing remuneration policy will continue to apply. This policy may be one that has also caused shareholder disquiet. Shareholders would therefore remain upset with the board in relation to its remuneration decisions, with no means of breaking the deadlock. CSA notes that the annual election of directors under the 'comply or explain' provisions of the UK Combined Code applies only to the FTSE300.
- The principles on which the determination of exit payments will be made should exclude those matters that apply to the length of service generally, such as accrued annual leave; accrued long service leave; sick leave (to the extent that it can be cashed out); bona fide redundancy payments made in accordance with a policy applicable to all employees of the company; pension/superannuation (contributions and payouts); deferred bonuses (that is, already earned with no further performance condition); insurance payments (for example, if the person leaves because they are disabled or have died); and other applicable entitlements applicable in the UK and globally. The global issue is important — the UK is not the only jurisdiction in which FTSE companies employ and pay executives. These are accrued entitlements of the individual and should not be bundled together with 'rewards for failure'. It should be absolutely clear in the regulations that the person can be paid these legal and other entitlements upon termination and without waiting for the shareholder vote on the remuneration policy.
- Companies will still need to report against the Accounting Standards. The proposed method of reporting remuneration will not match that required by the Accounting Standards, which could give rise to confusion and lack of comparability.

CSA is concerned with the impact of the proposed new regulations on dual-listed companies, as the proposed regulations conflict at times with existing legislation in this jurisdiction. Such conflict is likely to create difficulties for dual-listed entities in complying with the law in both jurisdictions. For example, we note that the proposed disclosure requirements on pensions cannot be applied absolutely to dual-listed entities, given that they will employ directors who do not have payments made into such pension schemes. For example, both BHP Billiton and Rio Tinto make payments for executive directors into Australian superannuation funds, which is a statutory obligation under Australian law. Any changes to UK regulation need to take account of the existing statutory obligations of other jurisdictions.

We also note that the paper refers to directors, which term captures both executive and non-executive directors. However, the regulations will only apply to executive directors in Australia.

1. Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

CSA's comments on aspects of the draft regulations are set out in our responses to later questions.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

There will be additional costs of compliance in any company, but dual-listed entities will bear further additional costs. They already report in two (or three) jurisdictions and will now need to also align two different reporting frameworks. Such alignment and reporting will demand an allocation of resources above and beyond that contemplated in an entity listed only in the UK.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

CSA supports the introduction of a table setting out the key elements of remuneration and supporting information on the pay policy. Our comments on particular aspects of the disclosure requirements are set out in our responses to later questions.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

While requiring disclosure of the percentage change in profit, dividends and overall expenditure on pay sounds feasible in theory, in practice pay may not be tied to company performance in a particular year. For example, long-term incentives (LTIs) may be over a three-year period and the pay results therefore may not be directly related to performance results in the year of their award. In such circumstances it is therefore not possible to make a direct comparison of the spend on pay with company performance and disclosure under these terms could be misleading.

CSA supports boards having to scenario test the remuneration directors would receive according to different circumstances. However, CSA is of the view that disclosure of the best-case scenario could be read by the media and shareholders as a 'given', with scant attention paid to disclosure of the worst-case scenario. CSA recommends a disclosure requirement that provides shareholders with sufficient information on which to base their voting decision (that is, negative and positive impact statements) rather than disclosure of the absolute best-case and worst-case scenario, that is, a ‘target’ or ‘expected’ outcome rather than a best or worst-case scenario.

Question 5: The Government proposes that a company’s statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

CSA members agree with the introduction of a disclosure requirement setting out how the company determines exit payments. When exit payments are made during or following a period of poor company performance, shareholders perceive this as ‘reward for failure’.

However, there is a wide variety of circumstances that may result in an exit payment. Commonly accepted bona fide payments can be made for:

- retirement (for example, accrued pension entitlements)
- resignation (for example, accrued annual leave entitlements)
- redundancy (for example, redundancy payments as per a company policy)
- death (for example, a death benefit payable by the company, insurer or pension fund to the person’s estate).

CSA strongly believes that payments of those ordinary-course entitlements that accrue according to length of service and that would apply broadly to employees within a company should be expressly excluded from any disclosure requirement as to how the company determines exit payments. In other words, they should be excluded from a requirement for shareholder approval.

For example, if a senior executive is made redundant after working for a company for 20 years and has accrued annual and long service leave, that executive is entitled to a reasonable redundancy payment together with the payout of that accrued leave.
CSA recommends strongly that the disclosure requirement for how the company determines exit payments specifically exclude certain legal and other entitlements including:

- pension/superannuation (contributions and payouts)
- accrued annual leave entitlements
- accrued sick leave entitlements
- long service leave entitlements
- ‘bona fide’ redundancy payments limited to redundancy payments which apply to the executive in the same way as they apply to the company’s employees generally
- deferred bonuses (that is, already earned with no further performance condition)
- insurance payouts (for example, if the person leaves because they are disabled or died), and
- other applicable entitlements applicable in the UK and globally. The global issue is important — the United Kingdom is not the only jurisdiction in which FTSE companies employ and pay executives.

CSA notes that this issue was dealt with in Australia appropriately and as we have recommended.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

The financial interest in a company rests primarily with the shareholders, although the interests of creditors, employees and the broader community are also important. CSA is of the view that boards would be wise to take into account the views of its employees on remuneration.

However, CSA does not support a requirement for companies to expressly set out in the remuneration report details of communications between the board, management and employees on remuneration policy. CSA is concerned that such an obligation could elevate the concerns of employees over those of shareholders. We note that shareholders' concerns are neither sought nor described under these proposals.

In addition, CSA has doubts that the resulting disclosures would be particularly meaningful and is concerned that they may be more likely to cause more internal difficulties than benefits. Bland statements that a company has consulted with employees will not be particularly enlightening for readers of the report. Lengthy disclosures of discussions held will add to the length of the report without necessarily adding any particular clarity. One can imagine that any such disclosures would immediately be met with internal debate along the lines of: 'Which employees in particular did the company consult? Would the outcomes have been different if other employees had been consulted? How many different groups of employees should a company consult and in which jurisdictions?'Which unions were consulted?

CSA notes that it is relatively common for large numbers of employees to already 'have a say' in their capacity as shareholders. Many listed companies have broad-based employee share plans, giving participating employees the right to express their views on the company's remuneration framework by voting on the remuneration report as shareholders.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

CSA supports a single total figure to aid shareholder consideration of the remuneration policy. CSA also supports the findings of the *Lab project report: A single figure for remuneration*, which the UK Government has referred to in preparing its proposals.

We note that it is important to ensure that double counting never occurs between years.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

CSA is of the view that it is for UK stakeholders to comment on this proposal.

Notwithstanding this, CSA does note that companies may employ people who are not awarded benefits through such pension schemes. For example, the executive directors of dual-listed entities BHP Billiton and Rio Tinto are paid under the statutory superannuation scheme operating in Australia. CSA recommends that any regulation of disclosure requirements needs to accommodate differences such as this.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

CSA is of the view that the clawback of executive remuneration is best dealt with in the employment contract between an executive and the company, with directors accountable for their decision through disclosure to their shareholders whether such contractual arrangements are in place. CSA therefore supports the proposal that clawback should be recorded as part of the single figure if it occurs, with an accompanying explanation as to its occurrence.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

CSA has some concerns with this proposal. Although CSA supports disclosure of the performance hurdles selected by a company, upfront detailed disclosure of internal hurdles may cause commercial difficulties for companies. It is unreasonable to assume that external hurdles (such as total shareholder return) will be the best metrics for all companies. Companies should be free to choose the metrics that best suit their circumstances, which will change over time. In CSA's view, the emphasis on 'detailed disclosure' should occur at the end of the performance/testing cycle, when the long-term incentive has vested/lapsed. At the end of the long-term incentive cycle the commercial sensitivities should have passed, and shareholders are most interested in remuneration outcomes *vis a vis* company performance.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

CSA is of the view that it is for UK stakeholders to comment on this proposal.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

CSA notes that, in Australia, the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations* recommend that non-executive directors not participate in performance-based equity incentive schemes designed for the remuneration of executives. CSA is of the view that it is for UK stakeholders to comment on this proposal.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

CSA strongly supports the simplification of reporting requirements and hopes that the proposed new regulations will indeed lead to such simplification. However, CSA notes that it may be useful to set a threshold for such reporting, given that the directors' holdings in large companies are likely to be immaterial, with no capacity to influence voting control, compared to those in companies where directors could hold substantial shareholdings. Such a threshold could be five per cent.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

CSA notes that total shareholder return may not be the metric employed by all companies as a proxy for company performance. CSA does not support regulation prescribing the metrics that companies should use. For example, in the property industry, returning money to shareholders may not be in their best interests as they need to maintain capital in the buildings. The mining industry is a long-term business and total shareholder return would not always equate to executive performance.

CSA also notes that it is unlikely that total shareholder return will be used as a metric over one year. It is more likely that it would be used over a five-year period.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

CSA supports an audit of the single figure, as this provides a level of assurance that should give comfort to shareholders.

Corporate Governance Committee Share Plan Lawyers

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September 2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
The Corporate Governance Committee Share Plan Lawyers Jonathan Fenn, Slaughter and May Louise Whitewright, Hogan Lovells International LLP Jocelyn Mitchell, Freshfields Bruckhaus Deringer LLP Nicholas Stretch, CMS Cameron McKenna LLP Paul Randall, Ashurst LLP Robin Tremaine, Clifford Chance LLP Mahesh Varia, Travers Smith LLP Nick Janmohamed, Speechley Bircham LLP	Lawyer or accountant Lawyer Lawyer Lawyer Lawyer Lawyer Lawyer Lawyer Lawyer
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Introduction

This response form is sent on behalf of Share Plan Lawyers ("SPL"). SPL was originally formed approximately 25 years ago by lawyers in law firms in London whose main practice is employee share plans. It has nearly 300 members representing more than 60 law firms and a number of specialist practitioners. Our members include senior lawyers from all the major London law firms and most major regional firms in the UK.

The main purpose of SPL is to meet, consult with and make representations to the Government and other institutions involved in taxation, corporate and other regulatory issues in relation to employee share plans.

Members of SPL are responsible for the drafting of share plans for a large number of quoted companies and for advising those companies on the content of their remuneration reports. We will, therefore, be closely involved in the actions which quoted companies take to comply with the proposed legislation, once enacted. (Given SPL's role, we have not answered questions within this consultation response form which relate to pensions.)

Generally

As a preliminary observation we should mention that, once again, we are struggling to determine the purpose of the proposed legislation from a legal and commercial, as distinct from a political, point of view. There is a concern that the current legislation (itself introduced in similar circumstances) results in over-complex reporting by companies which shareholders have difficulty understanding. It is not clear to us whether, while the new legislation will certainly provide for lengthier disclosure than under the current legislation, that additional material will be more useful to shareholders and other stakeholders.

Appendix 1 to this response form contains a preliminary summary of comments from our members on the detail of the draft regulations. Appendix 1 also contains our comments regarding the relevant sections of the draft Enterprise and Regulatory Reform Bill. We think it would be very helpful to have a meeting to discuss our comments with you, particularly on the detail of the draft regulations since there are complex issues to resolve. We are particularly concerned about how the transitional and grandfathering provisions will operate.

Please contact jonathan.fenn@slaughterandmay.com (telephone number 020 7090 5025) to arrange a meeting with the Corporate Governance Committee of SPL.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Companies will face substantial costs in adjusting to these revised reporting regulations. We do not agree with the statement at paragraph 27 of the consultation paper that the costs will not be significant. There will be significant additional legal and consulting costs when the provisions are introduced. (We are already seeing this in questions from our clients) and additional ongoing costs for companies, particularly in relation to external advisors, such as lawyers, remuneration consultants, public relations advisors and auditors.

We think the proposed changes in the way companies report on executive remuneration and the binding vote will affect companies more profoundly than when the current Directors' Remuneration Report Regulations were introduced. Companies have experienced a significant increase in costs from that time.

There will also be costs for companies in gathering the information required to comply with the revised reporting regulations. The preparation of the annual report is already a detailed and time-consuming exercise. Existing material will have to be reviewed, reorganised and substantially augmented. Paragraph 27 of the consultation paper states that the Government believes that *"the majority of the information that companies will need to report as a result of this consultation is already readily available"*. We disagree. We believe that there will be significant costs involved in gathering the information and that this information will not necessarily be readily available. For example, under paragraph 13 of the draft regulations, companies will need to gather information on a different basis than under the current regulations on performance and pay for ten financial years up to the relevant financial year.

We have assumed that companies should not need to negotiate the amendment of service contracts as part of the implementation of the new regulations. However, we would welcome the opportunity to discuss this aspect in particular. If this assumption is incorrect and the grandfathering provisions are not adequate, companies would incur significant costs/face additional practical difficulties as we have already pointed out in our previous submissions.

Although compliance costs for the first time may be higher than those for following years, there will undoubtedly be an overall increase in the continuing costs to quoted companies. This increase in costs is likely to affect smaller quoted companies more than larger companies.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We agree that it would be informative to have a table setting out the key elements of remuneration and supporting information on the pay policy. As mentioned in paragraph 42 of the consultation paper, this is already in line with how many quoted companies already present an overview of the structure of directors' remuneration to ensure shareholders are given helpful and clear information. We think it is appropriate that the Government will not propose prescribed specific disclosures for each element of pay.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

In our view, this is not a practicable and informative approach. It is likely to result in much longer reports with little additional benefit to shareholders.

Reporting requirements on service contracts

Under paragraph 21 of the draft regulations, a company must set out *"all the provisions that relate to remuneration contained in the directors' service contracts"*. This will have a significant impact on the length and complexity of the remuneration report and will not necessarily provide investors and shareholders with more meaningful information. Shareholders are only interested in the material elements – not, for example in the detail of holiday or sickness pay so we think some sort of materiality threshold ought to apply here to reduce the need to disclose a lot of irrelevant information.

All directors' service contracts are on display and can be reviewed by shareholders at any time. Furthermore, the existing rules already require disclosure of information relating to service contracts. We find the reference in paragraph 46 of the consultation paper to shareholders having found it difficult to get hold of service contracts baffling, given that companies are required to make these contracts available under s.228 of the Companies Act 2006. It seems odd to rely on some respondents saying they have encountered difficulties to justify introducing longer disclosure in the remuneration report when shareholders should simply be able to review the relevant document.

The point could be dealt with entirely and far more simply by companies being required to put the service contract on display on their website.

Relationship between service contracts and other remuneration arrangements, remuneration receivable in different schemes etc

We believe there may be a misunderstanding relating to the structure of service contracts and the overall provision of remuneration for directors. The normal position is that employee share plans, bonus arrangements (and pension arrangements) will involve discretion of the company, or, often, of independent trustees ("Trustees"), and there will be a range of payments which can be made under these plans depending on performance. The terms would generally not be covered in a director's service contract. It may not be possible to say what directors may receive in different scenarios where this is subject to discretion. This is particularly important in the context of Question 5. Companies will need to ensure that neither the discretion of the Board (or Remuneration Committee) nor Trustees' discretion is fettered.

Any long term incentive plans (cash or shares) ("LTIPs") for main board directors or any other share plan in which directors may participate will have been approved by shareholders when they were adopted as required under the Listing Rules. The plan rules will have been made available for shareholders and a summary of the main terms of the LTIP or other share plan sent to shareholders. The summary will set out key terms, including the maximum award that can be made to individuals as required under the Listing Rules. (If there were concerns over information available rather than including more information in the report which has already been approved by shareholders. The Company could retain the relevant plan summary as provided to shareholders on its website.)

Interaction between shareholder approval for plans and on policy

We are particularly concerned about the interaction between the binding vote with the shareholder approval of LTIPs and other share plans. The binding vote on policy should not affect the operation of plans in accordance with arrangements previously approved by shareholders. For example, most LTIPs and other share plans will contain a limit on annual grants usually expressed as a percentage of salary (for example, 150% of salary). The limit could not be exceeded without shareholder approval. It will need to be clear that payments made pursuant to rights treated as in accordance with an approved policy will be "consistent" with that approved policy even if the policy has subsequently changed. This is particularly important in the transition to the new regime.

It appears that a payment under a share plan is still subject to the new regime even if the plan has been separately approved by shareholders. (That may make sense where the plan has only been approved in principle and the level of awards needs to comply with the approved remuneration policy from time to time. However, what is the position on good leaver provisions? Do they need to be included specifically in the remuneration policy if awards are to be allowed to vest when someone leaves employment or will it be enough that the good leaver provisions were approved when the plan rules were approved? We think it should be the latter. There should be some level of certainty and as long as a company operates within the confines of the plan previously approved by shareholders it should not be subject to further and ongoing shareholder approval.

The draft provisions are drafted very widely, so, again, investors and shareholders may end up being provided with a significant amount of additional information, which is neither practical for the companies nor particularly helpful for shareholders and, as we understand it, is not the intention of the new regulations. For example, in paragraph 24 of the draft regulations, quoted companies must report the percentage changes in various figures *"in the reporting period compared to previous years".* It is not clear how many previous years companies will need to use for the comparison. In addition, what is meant by *"overall expenditure on pay (as a whole)"*? Does this relate to only to directors? What does "pay" mean for these purposes?

We think that a requirement to show percentage change in profit, dividends and overall expenditure on pay in the reporting period is particularly unhelpful. It may be possible for companies to produce a headline figure but year on year this is likely to need considerable explanation because profit, dividends etc will fluctuate for many different reasons. The difficulties are clear from the current drafting which is at best confusing and imprecise.

Further comments are set out in the Appendix on the drafting of these sections.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

It is likely that a significant proportion of payments made to directors on termination will not be a termination payment under a service contract but will relate to the exercise of discretion (either by the company (through the Board (or Remuneration Committee as appropriate)) or by independent Trustees) under employee share plans, bonus arrangements and pension arrangements.

It is important to have such discretions both in the varied circumstances of departure and in relation to the application of performance targets. It is not appropriate to legislate in advance for a situation that has not yet occurred. Shareholders are, in our experience, generally supportive of such discretions.

As set out in Appendix 1 to this response form, we are concerned that setting out the principles on which the determination of the exit payment will be made could cause significant legal issues for companies as it will either need to be very vague (and, therefore, of limited/no use to shareholders or other stakeholders) or if it specific it could be viewed as fettering the discretion of the Company or of Trustees. As mentioned in the response to question 4 above, employee share plans are often operated by the independent Trustees of employee benefit trusts. A company could not state in a report that no payments will be made under an LTIP where the Trustees have discretion as to whether and to what extent an award vests. This would potentially fetter the Trustees' discretion and also give rise potentially to tax issues for the Trustees (and, therefore, ultimately, additional costs for the company). This should be a matter for the Trustees, not for the company.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We agree with the view in paragraph 55 of the consultation paper that there should not be a statutory duty for companies to consult their employees on pay issues.

We have concerns about this proposal. There is a risk that companies may be perceived to be "non-compliant" if they do not consult employees even though there is no statutory obligation to do so. Companies with an international workforce may not want to seek the views of their employees on pay issues, especially as the approach may quite properly be different in each relevant jurisdiction.

It is true that there will be some companies which will already have employee consultation committees and so will not be significantly impacted by this. However, for companies which do not have such a committee, dealing with the perception of non-compliance will be costly. There may also be issues potentially for some companies with ensuring confidentiality.

We also note that paragraph 28 of the draft regulations does not require companies to report the results of any discussions. Is the intention that the results should be reported? In which case the best practice guidelines should include some guidance on how to report this information.

We are also not convinced that providing the percentage increase in pay of the workforce and the percentage increase in pay of the CEO would be useful for investors and shareholders especially for international companies whose workforce may be largely overseas or in a number of different jurisdictions where pay rates move differently. Comparisons may also be affected by currency movements. The more prescriptive the legislation is made, the more explanation companies will need to provide.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We do not believe that it will be useful for shareholders to disclose a single total figure which includes share awards under LTIPs and other share plans and share options. At present the remuneration of directors is already shown broken down between different categories of remuneration, including salary, bonus and benefits, with separate tables showing pension and share plan entitlements (Part 3 of Schedule 8 to the Large & Medium-sized Companies & Groups (Accounts & Reports) Regulations 2008).

Showing a single cumulative figure dealing with all categories of remuneration is likely to produce figures which are not comparable between companies and are impossible to interpret without fuller explanation. Without fuller explanation companies will be concerned that the single figure ignores the main point that any number will be based on a fluctuating value in the hands of the recipient. Therefore, it is likely that quoted companies will include footnotes to explain the figures, which will increase, not reduce, the complexity of the remuneration report. Even if footnotes or further explanation is provided companies are likely to spend considerable amounts of time dealing with the outfall of having to produce a single figure based on an asset with a fluctuating value. Inevitably a company's costs will increase. Once again, there is also the risk that investors and the press will focus unduly on the single figure as it provides a convenient "sound bite" and is likely to result in simplistic and possibly damaging press analysis. It seems to us that the disclosures which are currently required already provide investors with sufficient information in relation to grants under share plans to directors to enable them to calculate a value of such awards based on the share price **at any point in time** not just at an arbitrary point which may not properly reflect value to the individual.

Option value

We have a particular concern in relation to the share option value calculation (described in paragraph 71 of the consultation paper) because the option will not necessarily be exercised when it vests, so the director may not receive any (or a much lower) value from the share option depending on subsequent share price fluctuations until exercise. The director may also be prevented from exercising their option, eg because of close periods under the Model Code. There is a good argument to provide that the reporting for share options should occur in the reporting year when the option is exercised rather than at the point of vesting. This would better match the accuracy of the reporting for share awards where the reporting will reflect better the value actually received.

The value of options (and other forms of share awards) was debated at length some years ago in the light of proposed changes to accounting rules on the disclosure of directors' share options. The eventual conclusion of the Urgent Issues Task Force, published in UITP Abstract 10 in September 1994, refers to the "practical difficulties of attributing a meaningful estimated money value to an option at the date of grant, and differing views on whether and if so how to apportion any benefit over time". As a result, the UITF simply required that relevant factual information be provided, such as market price information at the year end and at the date of exercise. From this shareholders can assess for themselves the actual or potential gains which a participant may realise from such rights.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We have no comments to make in response to this question.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We note that in paragraph 73, the Government refers to *"formal claw-back"* and distinguishes it from malus but companies sometimes describe malus provisions as claw-back, so we suggest that malus and claw-back are explained in the guidelines. Claw-back is often most relevant in cases involving former employees. The single figure for a former employee may not need to be included in the table because the former employee may not have served as a director of the company at any time in the relevant financial year. Practically, therefore, it may be difficult for companies to comply.

As the Government accepts in paragraph 73, companies may choose to explain why claw-back is operated over a particular award. The most practical way of including this information is in footnotes to the table, which seems at odds with the policy objective of making remuneration reports less complex and easier for shareholders to understand.

In our view, any discussion about claw-back should be considered in the wider context of the Financial Reporting review into whether claw-back should be a UK Corporate Governance Code requirement, so that there is a consistent approach for quoted companies.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Shareholders already receive information under the current regulations on vesting of awards and the extent to which performance targets have been met. Increasing the amount of information would, however, be difficult and commercially sensitive according to the views expressed by our clients. Ultimately, disclosing highly commercially sensitive information could be to the detriment of shareholders, rather than to their benefit. We have already had concerns on this point made to us by a number of listed companies.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We have no comments to make in response to this question.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

In our view, it is not a practical and informative approach to disclose scheme interests at face value. The current rules, which provide that the number of shares must be recorded (along with other relevant information in relation to share options awards under LTIPs and share awards under other share plans) is more informative for shareholders and investors. It is not clear why the proposed disclosure is regarded as better than the current regime in this respect and it is likely to be misleading.

For example, "face value" is not defined in the draft regulations nor is it clear when the face value should be measured – is it the date of the award or the end of the reporting year? We assume face value relates to the market value of the underlying shares at the date of the award/end of reporting year. If so, it does not provide investors and shareholders with useful information, because the relevant point in time is when the award vests or the options are exercised rather than the date of grant. For a "market-value" share option, if face value is the market value of the shares at the date of grant less the exercise price, we would expect the face value to be zero.

In addition, "scheme interest" is not defined in the draft regulations, unlike in the current regulations (paragraph 11(4)) which separates out share options and awards under LTIPs. It is also unclear what paragraph 12(b)(iv) of the draft regulations is intended to cover.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We believe that the current provisions in Schedule 8 which require quoted companies to disclose detailed information on directors' interests at the beginning and end of the financial year for share options and LTIP awards are clearer and of more value to shareholders and investors than the proposed simplification. This is an example where there will be unnecessary costs to companies to comply with the new regime when the existing provisions work well. Again the Government should be wary of discarding provisions which work well, provide the necessary information and which companies understand, simply to satisfy political perception. We also have specific points on the drafting of paragraph 14 of the draft regulations (please see Appendix 1).

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We have no views on whether total shareholder return and CEO pay are the best proxies for company performance and pay respectively. We are not aware that there has been pressure from investors for this type of information. We believe such a graph would do little, if anything, to make the disclosures in the report more comprehensible to shareholders and, as such, is not likely to add value. It is more likely to provide material for sensationalist headlines which are unlikely to be helpful to the company or shareholders. We suggest that companies should be free to choose the performance measure which they consider appropriate and explain why they have chosen it.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We have no comment on whether there are any other sections of the report that should be subject to audit. However, companies take their statutory responsibilities very seriously regardless of whether that information is audited or not. If a significant section of the report is subject to audit, this will significantly increase the administrative burden and costs for companies (see our response to Question 2 above). The consultation paper states, at paragraph 97, that *"the Government recognises that audit is also a costly process for companies"* so we would urge the Government to limit the sections of the report that are subject to audit.

DIRECTORS' PAY: CONSULTATION ON REVISED REPORTING REGULATIONS – SHARE PLAN LAWYERS' RESPONSE - APPENDIX 1

Comments on draft Schedule 8 to the Large and Medium-sized Companies and Groups (accounts and Reports) Regulations 2008

GENERALLY

- We commented in our earlier submission that the Government would need to ensure with the UKLA that the definitions in the proposed legislation and the Listing Rules must be capable of operating together. Any inconsistency between the two sets of rules will be very unhelpful for companies trying to comply with new legislation (see comments on paragraphs 5 and 6).
- A number of definitions have been used (sensibly) from the existing legislation. We suggest that all definitions are taken into Part 6 for ease of reference even where expressed as specific to a paragraph so that they may easily be found. All the definitions need to be checked for usage throughout the draft schedule for consistency.
- There are likely to be further comments on the draft legislation once a number of points made have been resolved.

1. **PARAGRAPH 1 – PART 1 – INTRODUCTORY**

Paragraph 1(3) allows the policy part of the report to be found on "the company's website or other place". It seems to us that it ought simply to be available on the company's website. The intention here is that the report should be easily accessible. If a company is able to have it available only at its registered office or other remote location, it is more difficult for stakeholders to be able to access the policy. All companies to which the regulations are subject will have a website.

2. **PARAGRAPH 2 – PART 2 – SUMMARY STATEMENT**

We strongly recommend removing paragraph 2. Although it is very common for companies to have a statement by the Remuneration Committee chairman, and companies may well wish to have a user-friendly introduction to the report, we do not think such an introduction should be required by the legislation. The requirement that this introduction "summarises" the contents of the report means that there would be a degree of compulsory repetition - because companies will be advised that summarising the contents of the report means that all the material points need to be covered in the Introduction. This also raises the issue of what would be regarded as an adequate summary. This would seem to be a pointless requirement given that the report is itself a summary.

3. **PARAGRAPHS 5, 6 AND 7 – PART 3 – REPORT RELATING TO THE FINANCIAL YEAR IN RESPECT OF WHICH THE REPORT IS REQUIRED TO BE MADE – SINGLE TOTAL FIGURE OF REMUNERATION**

3.1 Paragraph 5 contains a number of **key** references which **must** be resolved in the next draft and must be synchronised with the definitions in the Listing Rules from which they are derived.

Use of terms long term incentives, "Scheme" etc

For example, there is a reference in paragraph 5(b)(ii) to "long term incentives". This reference does not appear anywhere else. We think it should refer to "vesting period of scheme interests". The existing regulations contain a definition of "long term incentive scheme" which has been used in the draft legislation in paragraph 7(3) but has been changed to "Scheme" instead of "long term incentive scheme". However, in paragraph 33(1) in the definition of "emoluments" there is a reference in paragraph (c)(iii) to "long term incentive scheme". There are clearly references to "scheme" in paragraph 5(e) which should be to "Schemes" (ie meaning long term incentive schemes). We suggest you:

(a) revert to the reference in the current legislation to "long term incentive scheme" not "Scheme". The definition used in the draft regulations is for a long term incentive scheme. You will need to consider whether the definition needs to be expanded (or use a separate definition) to include schemes with no performance conditions to cater for awards under schemes as referred to in paragraph 5(e)(ii) (which are not subject to performance targets and so are not long term incentives within the meaning of the definition used in the draft legislation);

(b) include a definition of "scheme interest" using the existing definition in the current legislation (see paragraph 11 of Schedule 8 to CA 2006);

(c) include a definition of "vest" (used in paragraph 6(e)(ii) in the draft regulations but not defined) using the existing definition in the current legislation (see paragraph 11 of Schedule 8);

(d) ensure that you review the Listing Rules and, for example, include the full definition of long term incentive scheme and a definition of "deferred bonus" which would presumably help with paragraph 6(d) in the draft regulations.

3.2 **Paragraph 5**

(a) Why is paragraph 5(b)(ii) limited to cash dividends? It should presumably include stock (or other) dividends as well.

(b) Paragraph 5(d) is oddly expressed. It refers to money or assets awarded <u>in</u> the reporting period as a result of achieving performance conditions that relate to that period. Normally any award (for example a simple cash bonus) would be made following the end of the reporting period, once the results for that reporting period were available. They will not have been awarded <u>in</u> the period. It would be better if the reference was to awards made “in respect of” the relevant reporting period? That would then tie in better with paragraph 36.

(c) In paragraph 5(d)(i) the words “(or shortly thereafter)” are unclear. To what are they intended to relate? Performance conditions will almost invariably relate to a reporting period. Does it refer to the date of determination?

(d) In relation to paragraph 5 generally, it would make sense to specify that amounts should appear in one only of columns (a) to (e). (There are a number of items which could fall into more than one column and the requirement is that sums must be set out in the columns. This requires an additional paragraph in the legislation to avoid the need for companies to include extensive footnotes.)

3.3 **Paragraph 6**

(a) In paragraph 6(b) there is reference to “taxable value” in the context of a dividend. Is this intended to mean the value of the dividend actually received in cash terms or the dividend plus the associated tax credit? The dividend income for tax purposes is the dividend received plus the tax credit. We think it would be desirable to make this clear.

(b) Paragraph 6(d) must be clarified. Presumably the intention is that where a cash payment is made (whether an immediate cash payment or a deferred cash payment) then that cash amount should be shown (i.e. for example, there should not be an attempt to show an equivalent value, for example by applying a discounted cashflow). However, where what is delivered is other assets then there should be a reference to the amounts determined by the Company to be the value of those assets at the time of award. Care will need to be taken with deferred awards which may be in the form of options or other types of share award or by reference to other investments and how they will fit within the table.

(c) Paragraph 6(e)(ii) is overly complex. It would be simpler to refer to the number of shares or share options that vest multiplied by the value of the relevant shares at the date of vesting. Introducing references to percentages seem unnecessary and does not work if there have been changes to the company's share capital such as a sub-division or consolidation of shares since the awards were granted (so the original number of shares is irrelevant). To that value should then be added the amount of any accrued cash dividend received at the time of vesting or the value of any additional shares delivered in place of dividend. (However, please note our comments on share options in the response to Question 7.)

3.4 Paragraph 7

(a) In paragraph 7(1) (definition of "Benefits") it might be helpful here to provide that paragraph 7(b) does not refer to any emoluments that are included within paragraphs 5(c) to 5(e) - presumably those paragraphs should take precedence over paragraph 7(b).

(b) Paragraph 7(2) provides that benefits received in advance of a director commencing qualifying services are to be treated as received on the first day of the contract. Where a director ceases qualifying services during a year but does not receive payment until after the end of that year, should that payment be shown in the year in which qualifying services ceased (i.e. treated in a similar way) or in relation to the subsequent year? We presume that paragraph 36 is intended to have the effect that it should be shown in respect of the former year. This needs to be clarified.

4. PARAGRAPHS 8 AND 9 – PART 3 – VARIABLE PAY ADDITIONAL DISCLOSURES

4.1 Paragraph 8

(a) The additional disclosures in relation to variable pay will give many companies significant problems. Paragraphs 8(2)(a) and (b) require "details" of performance conditions and of the target set when the performance condition was agreed. Very often performance conditions relate in whole or in part to confidential internal performance measures. Having to disclose "details" will cause real problems with confidentiality. This point has already been made to us by a number of our corporate clients. This wording should be softened - perhaps to require a description of the nature of the performance targets applied and an **indication** of performance against them, to avoid requiring disclosure of sensitive material. We would stress that this point was made in relation to the previous legislation when it was introduced as well in previous submissions on the current proposal. It is also possible that any greater detail could lead to the risk of companies having to consider profit forecast issues.

(b) There is a reference in paragraph 8(1) to "interest". Should this be to "scheme interest" which as noted above has not been defined?

4.2 **Paragraph 9**

Paragraph 9 should require the company to state whether there is deferral in cash or "other assets" to tie in with the wording used in paragraph 5(d). Clearly the deferral could be in something which is not cash or shares.

5. **PARAGRAPH 11 – PART 3 – LOSS OF OFFICE PAYMENTS**

In paragraph 11 it is not clear why there is a difference between compensation for loss of office, where explanation of how the payment was calculated is required, and any other payments (where no such explanation is needed). This is relevant given our comments on paragraph 33(2) (see below).

6. **PARAGRAPH 12 – PART 3 – VARIABLE PAY AWARDED DURING THE FINANCIAL YEAR WHERE THE VALUE WILL BE DELIVERED ACCORDING TO THE ACHIEVEMENT OF PERFORMANCE CONDITIONS IN FUTURE PERIODS**

6.1 In paragraph 12 it would be helpful if the regulations could explain what is meant in 12(b)(iii) by the "face value" of an award. Most people would understand that if an individual is being given a grant of shares, which were only received if certain conditions were achieved, that the value of the shares at the time of grant would be the "face value". However, what would be the face value of an option grant? Is it intended to be the value of the shares subject to an option or, where an amount is payable on exercise of the option, is it the difference between the value of the shares at the time of grant and the amount to be paid?

6.2 It is not clear when the face value should be measured – is it at the date of the award or at the end of the reporting year?

6.3 In paragraph 12(b)(iv), where the scheme interest is structured as an option (as is very common) it would not be possible to give a maximum value at the time of vesting because the actual value to an option holder will depend on the value of a share at exercise.

6.4 As already noted above, the term "scheme interest" is not defined, unlike in the current regulations (paragraph 11(4)) which separate out share options and awards under LTIPs.

7. **PARAGRAPH 13 – PART 3 – COMPARISON OF OVERALL PERFORMANCE AND PAY**

In paragraph 13 there is a requirement for a company to provide a line graph showing the total shareholder return for the previous 10 financial years. In order for it to be possible to calculate TSR this requirement should only relate to periods when the company was in fact listed. (So, in the same way as the regulations try to do for companies with less than ten financial years, the period for the line graph should be shortened.) We also consider that a 10 year period imposes a disproportionate administrative burden on companies; we suggest a five year period is used instead.

8. **PARAGRAPH 14 – PART 3 – STATEMENT OF DIRECTORS' SHAREHOLDINGS**

8.1 Should the title refer to interests in shares as well?

8.2 It is not clear whether paragraph 14(b) only relates to vested share awards and share options or to both vested and unvested share awards and share options.

8.3 Paragraph 14 requires the remuneration report to list a total number of shares and share options "of which the director is the legal owner". The reference to a legal owner looks like a mistake. This disclosure should pick up shares which are owned by the director but which are registered in the name of a nominee. Presumably the reference should be to shares of which the director is the "beneficial" owner. The paragraph should be separated out to make clear that what must be disclosed are shares beneficially owned, shares under option or shares held under any other form of award. It may be better to consider reviewing the reference to scheme interest and then using terminology consistently.

9. PARAGRAPH 15 – PART 3 – CONSIDERATION BY THE DIRECTORS OF MATTERS RELATING TO DIRECTORS' REMUNERATION

Paragraph 15(1)(b) requires details to be given of persons who provided advice to the remuneration committee on their consideration of any matter relating to the directors' remuneration. This is very widely drawn at the moment so that it would potentially require disclosure of information that is of very limited value and is likely to be misunderstood. For example it would be common currently for not only the company's remuneration consultants to be named in the remuneration report but also perhaps the company's corporate lawyers. The advice which the corporate lawyers have provided to the remuneration committee might be as simple as explaining how the terms of the company's share schemes work in the event of a director leaving service or the Committee's legal obligations as to disclosure. Paragraph 15(c)(iii) would appear to require not simply a disclosure of the fee charged for that advice (which might be small) but also a disclosure of the fees charged for other legal services provided during the relevant financial year and the basis (whatever that means) on which fees were charged. For a large corporate that may lead to a disclosure which is entirely unhelpful to shareholders - perhaps on the following lines:

> *"XYZ LLP provided legal advice to the remuneration committee on the terms of the Company's share incentive schemes. A fee of £2,500 (plus VAT) was paid for that advice, based on the time spent by XYZ LLP and the nature of the advice provided.*
>
> *In addition XYZ LLP provided legal services to the Company and other members of the Company's group during the year in relation to a variety of corporate advisory, transactional and litigation matters. Total fees paid to XYZ LLP by the Company and other members of the Company's group during the period were £2,790,500 (plus VAT). Fees were charged on different bases in relation to different matters, depending on the nature of the work involved and all the relevant circumstances."*

We would suggest that this disclosure would be of little value to shareholders or other stakeholders. Obtaining meaningful figures might itself be a significant exercise, particularly where a number of members of a corporate group instruct lawyers independently and the "basis" for fees would often vary from matter to matter.

It is not clear that the wording "materially assisted" will help to limit what is described. Is this an objective or subjective test? The remuneration committee may have taken advice which cost a great deal but which did not "materially assist".

What is the policy intention of paragraph 15? What is it intended to achieve?

We strongly recommend that this requirement is withdrawn. It does not serve the primary purpose of the proposed legislation which is to boost transparency so that what people are paid is clear and easily understood.

10. **PARAGRAPH 16 – PART 3 – STATEMENT OF SHAREHOLDER VOTING**

In paragraph 16 there is a requirement for there to be disclosure "where known to the company, of the reasons for [the shareholder vote against]". The difficulty with this requirement is that the directors may know what some shareholders have said about their reason for voting against the resolution but they will not know why others did. Those reasons will be different and may well be contradictory and inconsistent. In that situation one may end up with a lengthy but extremely unhelpful disclosure. We do not see any problem with an obligation to disclose actions taken by the directors in response to the shareholder vote against but a summary of reasons expressed by some shareholders is extremely unhelpful.

The likely outcome is that it will curtail helpful dialogue between a company and its shareholders with shareholders reluctant to give reasons for votes against or even to explain that they may vote against the resolution.

11. **PARAGRAPH 17 – PART 4 – THE POLICY PART**

11.1 Paragraph 17 of the draft regulations state that the directors' remuneration report must identify the date on which the policy report takes effect. That date may be the start of a financial year or some other date. Paragraph 17 only provides that a start date must be stated; it does not regulate what that date is.

Companies may choose a start date which precedes the AGM and that causes problems with awards made between the start date and the AGM which would have to be made conditional in some way on the vote being passed. A company may choose as the start date the first day of the next financial year but that seems a long way off - the company's position may have changed by then. The safest course may be to choose the date of the AGM as the start date. Perhaps this should be covered in the guidance – although companies should still have the freedom to choose.

11.2 If a company has a binding vote at the AGM in 2014 for a policy starting on 1 January 2015, presumably the policy which applies for the rest of 2014 is the one approved under the advisory vote in 2013. This is not clear. It would be helpful to discuss transitional arrangements in this context as soon as possible.

12. **PARAGRAPHS 19 AND 20 – PART 4 – FUTURE POLICY TABLE**

12.1 **Paragraph 19**

Paragraph 19(d) requires disclosure of the performance metrics which are to be used. Reference to specific performance metrics will give rise to problems for many companies with sensitive information - performance metrics set in relation to annual bonus arrangements in particular will often quite properly be specifically designed to deal with specific short-term business targets for that company. As referred to in our comments in relation to paragraph 8 of the draft regulations (paragraph 4.1 above), companies will be very reluctant to release anything which they feel could damage their business – nor should they be forced to make such disclosures.

There needs to be clarity in relation to, for example, "maximum potential value" in paragraph 19(c).

12.2 **Paragraph 20**

In paragraph 20(b) some words appear to be missing.

13. **PARAGRAPH 21 – PART 4 – SERVICE CONTRACTS**

13.1 We believe that this paragraph should not be contained in Part 4 (the Policy Part) because it is a factual matter, rather than a policy matter. If it remains in the policy section and the binding vote on policy is not achieved, this may potentially bring into question the validity of existing contractual terms which would be inappropriate and unhelpful.

13.2 Paragraph 21 requires statements of <u>all</u> the provisions that relate to remuneration contained in directors' service contracts. This could well be a very lengthy disclosure, since it would require describing the provisions relating to salary, benefits, pension, life insurance, company car etc as well as the terms on which benefits are payable on termination in different circumstances. For a company with a number of executive directors this is likely to lead to a lengthy disclosure. This detail is unlikely to be of interest to most shareholders but will substantially increase the length of the remuneration report. If the concern is that the current obligations to have directors' service contracts available for inspection by shareholders have made it difficult for shareholders to access this information, would it not be more sensible to impose a requirement on companies to make copies of the directors' service agreements available on their website? That deals with the availability of the information to shareholders and ensures that the minority of shareholders who are interested can obtain the full details without unnecessarily extending the report.

14. **PARAGRAPH 22 – PART 4 – SCENARIOS**

14.1 What does "threshold" mean?

14.2 The drafting does not appear to achieve the intention that the maximum remuneration which could be achieved is displayed in graphical form. Paragraph 22 requires a graphical representation. However the drafting seems to assume that there will only be one threshold set of performance criteria. It may well be that different performance metrics will apply to different benefits. The threshold at which amounts will be payable under an annual bonus, for example, may well be different from a long term incentive arrangement. This is likely to require companies to produce many different graphics to illustrate different thresholds.

15. **PARAGRAPH 24 – PART 4 – RELATIVE IMPORTANCE OF SPEND ON PAY**

15.1 Paragraph 24 ought to appear in Part 3 of the regulations - since it is simply a report on historic movements - not relating to future policy. In any event we are not entirely clear what is meant in paragraph 24 by "profit". The accounts of many companies will have different calculations of profit - does this mean profit before or after tax, for example?

15.2 Paragraph 24(1) requires quoted companies to report the percentage changes in various figures "in the reporting period compared to previous years". It is not clear how many years this is intended to go back.

15.3 What is meant by "overall expenditure on pay (as a whole)"? Does this relate only to directors? Does it refer to all employees globally? What does pay mean for these purposes?

16. **PARAGRAPHS 25 AND 26 – PART 4 – EXIT PAYMENT POLICY**

16.1 The term "termination payment" is not defined, so it is not clear what it is intended to include.

16.2 Paragraphs 25 and 26 of the draft regulations use inconsistent terminology. Paragraph 25 refers to an obligation to "summarise and explain the company's policy". Paragraph 26 then requires the report to "state the policy". That suggests that, in the latter case, the policy must be set out without explanation. The paragraph 25 approach seems to us to meet the policy intention rather better. Companies may be concerned that this inconsistency could lead to the potential for shareholders to bring an action against them.

17. **PARAGRAPHS 27-30 – PART 4 – STATEMENT OF CONSIDERATION OF CONDITIONS ELSEWHERE IN COMPANY AND GROUP**

17.1 The heading should not include "elsewhere".

17.2 The references to "group" and what is contained within the "group" seem unclear. Should the reference be to "subsidiary undertakings, not "undertakings"? Contrast with the definition of "qualifying services".

17.3 The obligation to report consultations with employees is likely to impose considerable pressure on global companies to consult with their worldwide workforce on issues not previously consulted where local employers do not consult on similar issues. This regulation will effectively become extra-territorial. This provision should be deleted and referred to the Financial Reporting Council for consideration.

18. **PARAGRAPH 32 – PART 5 – PROVISIONS OF THE REPORT WHICH ARE SUBJECT TO AUDIT**

This should refer to the "information specified in paragraphs 3-9 etc is subject to audit" rather than "the following paragraphs are subject to audit".

19. **PARAGRAPH 33 – PART 6 – INTERPRETATION AND SUPPLEMENTARY**

Paragraph 33(2) is different from the equivalent provision in Section 215(1) Companies Act 2006. In particular, limb (d) of paragraph 33(2) deals only with a situation where retirement is occasioned by a "breach of the person's contract with the company". Limb (d) of Section 215(1) is not so limited. This is relevant in the case of termination of a director's employment because very often that termination will be effected in a way that is not a breach of the contract - for example by a contractual payment in lieu of notice. This would not, therefore, be picked up by limb (d) of paragraph 33(2). We suggest that the definition of compensation for loss of office should track Section 215(1) of the Companies Act 2006 more closely.

<u>Comments on provisions relating to payments to directors of quoted company in the draft Enterprise and Regulatory Reform Bill</u>

20. **KEY DEFINITIONS (DRAFT SECTION 226A(1) COMPANIES ACT 2006)**

The definition of remuneration payment appears to apply only to payments made in relation to the office of director not to payments made as an employee so would technically exclude most of an executive director's pay and benefits. This would negate the Government's intentions. This needs to be clarified.

21. **REMUNERATION PAYMENTS (DRAFT SECTION 226B COMPANIES ACT 2006)**

Draft section 226B does not appear to cover remuneration payments by Trustees (in contrast to draft section 226C). The guidance needs to make clear when a remuneration payment is made. For example, in relation to a share option or award, is it at the time of exercise or vesting rather than at grant?

22. **THE TRANSITIONAL PROVISIONS (DRAFT SECTION 64 OF THE ENTERPRISE AND REGULATORY REFORM BILL)**

22.1 If there is a requirement to make a payment under an agreement or obligation entered into before 27 June 2012, the new regime will not apply. When does a "requirement" arise, particularly where benefits are discretionary? In the case of a share option or award, is it when it is granted? What if there is a wide discretion to cancel an award or claw it back (i.e. not just for misconduct or misstatement, for example). Does that negate the "requirement" to make the payment, particularly where that power could be exercised if the binding vote was lost? Will guidance cover this?

22.2 As drafted, it seems that any modification of a service agreement will "re-date" it under the transitional provisions. This should be limited to modifications of the provisions relating to remuneration or payments for loss of office or, at the very least, material amendments to any part.

23. **HOLDING UNAUTHORISED PAYMENTS ON TRUST (DRAFT SECTION 226E COMPANIES ACT 2006)**

There may be practical problems with the trust arrangement introduced in the Bill, for example if money has been paid to the trustees of a pension fund. How would it be recovered?

24. **DAMAGES AWARDS AND PAYMENTS IN SETTLEMENT OF EMPLOYMENT CLAIMS**

24.1 The legislation does not provide a safe harbour for any damages award or a payment in settlement of a claim. It seems a strange result that shareholders could prevent a company paying damages awarded by a court or tribunal to a director simply by not approving the payment or an applicable policy.

24.2 S.220 CA 2006 would not apply to payment for loss of office to a director of a quoted company (see s.63(4) of the Bill). The new s.215(5) is strangely drafted because as currently drafted it provides that nothing "in this section" - i.e. s.215 - shall apply to payments for loss of office to a director of a quoted company. However, s.215 is relevant to defining what a payment for loss of office is (see new s.226A(1) which defines payment for loss of office by reference to Chapter 4, i.e s.215) so if s.215 does not apply it is not obvious what is a payment for loss of office.

24.3 This may also cause issues where a UK plc director is employed by an overseas subsidiary which is subject to local employment laws that require certain payments to be made to employees on termination of employment. The overseas subsidiary would have a legal obligation to make the payment and yet it would need to be approved by UK plc shareholders as part of the policy - what would be the result if shareholders refused to approve?

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24 September 2012

Dear Sir

Deloitte response to the Directors' Pay consultation on revised remuneration reporting regulations

Our response to the Consultation is based on the collective experiences of our team over a period of more than 20 years. Deloitte is a member of the Remuneration Consultants group.

Transparency and dialogue

We believe that the roots of good pay governance lie in transparent reporting of executive remuneration arrangements as well as a strong level of dialogue between shareholders and companies. In general, we consider that the proposed revised remuneration reporting regulations will provide shareholders with clearer and more helpful information which should improve the understanding of the dynamic between pay and performance. We do however have reservations with regards to some proposed disclosures and we have commented on these in the detailed responses to your questions.

Policy report information included only once every three years

As the regulations are currently drafted, companies may only be required to put their remuneration policy to a binding vote to shareholders once every three years. The information included in the policy report may therefore only appear once every three years. While we appreciate the desire to streamline company reporting, we believe that it is important that shareholders see this information each year even if a company is not required to have a formal vote on their remuneration policy.

Interaction with listing rules

A significant area of uncertainty is the interaction of these new regulations with the Listing Rules. If no changes are made to the Listing Rules there will be a requirement to report information in different ways. Notwithstanding this, we believe there are some aspects of the **current** regulations that are not included in the **proposed** regulations that should be retained either in the new regulations or as part of the Listing Rules. It is not clear, for example, whether the existing requirements with regards to pension disclosure or outstanding share interests would remain. It would therefore be helpful to get clarification and alignment between the Listing Rules and remuneration report regulations.

Deloitte.

We have set out in our "other comments" section following question 15 those disclosures that are currently required by the Listing Rules which we think are important to retain, ideally as part of these regulations.

We believe the best outcomes are achieved when companies and shareholders are encouraged to enter into open and transparent dialogue on pay. While we often see constructive dialogue this is not always the case and we would therefore support any further measures which encourage active engagement from both parties.

Our thoughts on the specific questions raised in the document and some other areas raised in the consultation are attached. If you have any questions or comments, please contact Carol Arrowsmith (020 7007 2969) or Stephen Cahill (020 7303 8801).

Yours faithfully,

Deloitte LLP

Deloitte.

Directors' Pay: consultation on revised reporting regulations

Name of respondent

Deloitte LLP

Please state whether you are responding as an individual or representing the views of an organisation by ticking the appropriate box below:

	Business or business representative organisation
	Investor or investor representative organisation
	Government or regulator
	Lawyer
✓	Remuneration consultant
✓	Other professional advisor
	Trade union or employee organisation
	Individual
	Other (please describe)

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Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Regulation	Comment
Part 1 - Introduction (2)	Para 1(2) refers to Section 439A of the Companies Act 2006. We do not think that such a provision currently exists.
Part 2 - Summary Statement 2. The directors' remuneration report must contain a statement by the director who fulfils the role of chairman of the remuneration committee summarising the contents of the report	As set out in the Consultation Document at (23), the purpose of the letter is intended to "summarise the key messages on remuneration and the context in which decisions have been taken". This is somewhat different from simply "summarising the contents of the report". We would suggest that the regulations be amended to reflect the Consultation Document as follows: "2. The directors' remuneration report must contain a statement by the director who fulfils the role of chairman of the remuneration committee summarising ~~the contents of the report~~ the key messages on remuneration and the context in which decisions have been taken"
Part 3 – Single total figure of remuneration 4. The form of the table required by paragraph 3...	In the current draft regulations the columns on the single total figure tables are headed a, b, c, d, e etc. We think this might be confusing and our suggestion would be that a, b, c, d etc be replaced by Salary, Benefits and Dividends, Pension, Annual incentive, Long-term incentive, Total, with appropriate definitions. If the titles a, b, c, d, e are retained then we think that it would be useful to include headings in addition to the letters in the draft regulations to aid clarity (with wording to say that it is for interpretation purposes only and not part of the formal regulations). In addition, we believe that there should be flexibility for companies to provide additional columns where appropriate. This would be helpful for example where a company operates more than one form of long-term incentive award in order to show the value of each in separate columns. We also consider that it would be helpful to be able to separate recruitment awards or dividends from other forms of benefits.
Part 3 – Single total figure of remuneration **5(a)**	As currently drafted, only salary and fees are specifically defined as being in respect of "qualifying services" (see paragraph 5(a)).

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	We suggest that Paragraph 5 should be clarified so that **all** forms of remuneration must specifically be in respect of qualifying services before they are included in the single figure.
Part 3 – Single total figure of remuneration 5 (d)	This paragraph refers to "money or other assets awarded in the reporting period..." In practice, bonuses are not awarded during the financial year as bonus decisions and the actual payment are made after the year end. We would suggest rewording as follows: "money or other assets awarded <u>in respect of</u> the reporting period..." In addition, we believe that the word "awarded" in paragraph 5(d) should be defined in the legislation to avoid confusion.
Part 3 – Single total figure of remuneration 5 (d) and 5 (e)	The drafting of these paragraphs are unclear and could be further clarified.
Part 3 – Single total figure of remuneration 5 (e) (i)	The regulations assume that all performance is always assessed over financial years. In some cases performance is assessed from award to vesting. We would therefore suggest rewording (e)(i) as follows: "final vesting is determined as a result of the achievement of performance conditions that end in the year being reported on <u>(or shortly after).</u>" Some companies may operate plans where awards are subject to performance conditions over a set period e.g. three years but with awards only being released to participants at a later date, perhaps after a further year or two years. The release of these shares may be subject to a company meeting an underpin performance condition (e.g. EPS growth must be positive). It is unclear in the legislation when these awards would be included in the single number. Presumably the intention is that company make a reasonable decision based on their commercial circumstances? If such awards were included in the single figure and then subsequently were not delivered to

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	participants, it would be necessary to show the value as a negative in the single number as with clawback.
Part 3 – Single total figure of remuneration 6 (e) (iii)	This paragraph states that the "value of the benefit will be calculated on the basis of an average market value over the last quarter of the financial year". The consultation document states that a three month average should be used (p71). For most companies this should be the same period, however, for companies where the financial year is not a full calendar year (e.g. retailers) these periods might not be exactly the same. Either approach is considered appropriate but clarity should be provided.
Part 3 – Single total figure of remuneration 6 (e) (iv)	This paragraph states that where share options have been included in the single figure the amount shown should be net of the exercise price. We would recommend amending the wording as follows: "was or will be required to pay to purchase" This reflects that share options may be included in the single number before they have actually been exercised.
Definitions applicable in the table 7(4)	This paragraph defined the "HMRC method". In doing so it refers to s234 Part 4 of the Finance Act 2004. In our view it would be better to replicate this section in the regulations rather than refer to the FA 2004. This will provide more clarity for the reader.
Definitions applicable in the table 7(5)	This section refers to 7(4)(a) which does not exist. We assume this should just read 7(4)?
Variable pay – additional disclosures 8 (2)	This paragraph refers to "any shares...". We do not believe that the intention is to limit this disclosure to just share based payments. We would therefore suggest replacing the word shares with "variable remuneration".
Loss of office payments 11	We are not clear whether it is the intention that this disclosure should include details of the treatment of share awards when a director ceases employment. In particular, some share awards may continue

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	following cessation and vest at a later date (i.e. the "normal" vesting date). If this is the intention we do not believe that the current drafting captures this as these are not usually considered to fall into the category of "compensation for loss of office". This could be clarified by adding an additional paragraph stating: "(e) the treatment of any outstanding incentive awards that vest on or following cessation".
Variable pay awarded during the financial year where the value will be determined according to the achievement of performance condition in future periods **12**	In addition to the information outlined in paragraph 12. We also believe that the following information should be disclosed: • The number of shares awarded • The share price on the date of award • The option exercise price if awards are made in the form of share options
	Although the value of awards granted without performance conditions will be included in the single number in the year in which they are granted we believe that the details required under paragraph 12 should also be required for such shares. This section title would therefore be amended to: "Variable pay awarded during the financial year where the value will be determined according to the achievement of performance and / or service conditions in future periods."
Comparison of overall performance and pay **13**	Our understanding is that this chart would only need to be calculated from the year in which the company became a "quoted company". This is not clear from the current drafting and should be clarified. Will the first financial year for the purpose of this chart be the financial year for which this legislation comes into force or is a chart of look back over the previous ten years? .
Consideration by the directors of matters relating to directors' remuneration **15 (c) (i) (iii)**	Paragraph (95) of the consultation asks for the "total cost of advice on remuneration and basis on which they are paid". Under the current draft regulations the requirement

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	is to disclose fees for "any other services" see paragraph 15 (c) (iii). This is not included in the consultation document. In order to give effect to the consultation document we would suggest deleting the words "any other services" referred to in paragraph 15 (c) (iii) as follows: (c)(iii) the amount of fee or other charge paid by the company to that person for the provision of the advice or services referred to in (b) ~~and the other services referred to in (c)(i)~~ and the basis on which it was charged.
Part 5 **Provision of the report which are subject to audit** **32(2)**	This paragraph states that Paragraphs 3 – 9 and 10 – 12 are subject to audit. We would suggested amending this to: Paragraphs 3 – 12 are subject to audit.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

[Intentionally left blank]

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We agree that requiring companies to present information in the form of a table is a clear and informative approach.

We also agree that it should be for shareholders and companies to establish the appropriate level of detail to be included in this table, rather than this being an area for regulation. In particular, there will need to be a balance between providing shareholders with sufficient information to understand the remuneration policy, whilst providing flexibility for companies to react to commercial circumstances. We would expect this to be a matter of best practice that will develop over time.

Under the current regulations this policy table will only be required when a company puts its remuneration policy to a binding shareholder vote, which could only be every three years. Given that this table is key to understanding a company's remuneration policy and provides the context for the implementation report, we believe that the Government should consider requiring companies to publish this table each year, even if they are not putting their remuneration policy to a binding vote. We believe that this approach will be significantly more useful for shareholders.

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We agree that it is helpful to supplement this table with a narrative explanation of the rationale for the selection of performance measures and how the remuneration policy for executive directors relates to the policy in place for the wider employee population.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Service contracts

Under current legislation companies are already required to disclose the notice period and termination provisions in respect of executive contracts which are the key areas of interest for shareholders. Extending the disclosure requirements to include "all provisions that relate to remuneration" should therefore not be particularly onerous for companies – although we do acknowledge that the circumstances around individual departures can differ which may introduce complexity.

We believe, as with the policy disclosure, that there will be a role for companies and shareholders to develop best practice guidelines to establish the appropriate level of detail for this disclosure.

Scenario analysis

We believe that this disclosure will be more useful than the current requirements to disclose the balance of fixed and variable pay.

Companies will need to consider the assumptions used in this analysis carefully to ensure that it is an appropriate reflection of each of the individual scenarios, for example, what share price assumptions should be used under each scenario. Given that different assumptions are likely to be appropriate for different companies, we agree that the methodology should not be prescribed by the Government. We do believe, however, that it would be best practice for companies to disclose the assumptions used to make this as transparent as possible for shareholders and other stakeholders. This will enable stakeholders to take a view of the appropriateness of the assumptions used for each individual company.

This information is currently included in the remuneration policy section of the report. Given that companies need only submit a policy to shareholders once every three years, this information may not be disclosed each year. In our view, it would be more helpful to have this information disclosed each year given that, for example, incumbents and award levels (within the stated policy) may vary.

Relative importance of spend on pay

We do not believe that this disclosure would add value for shareholders. It is unclear how information relating to the change in the total level of pay helps shareholders better understand the dynamic of the relationship between executive pay and performance. Total pay of an organisation can change for a number of reasons which may not necessarily be related to shareholder value creation, for example, currency exchange, corporate acquisition / disposal or a company opting to outsource some of its production / services would reduce its total pay cost.

If numbers are included, we believe absolute spend, rather than change in spend, should be included. We note however that this information is already disclosed in the annual report.

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For companies in sectors where profits vary significantly depending on external circumstances but employment costs are more fixed, these numbers are likely to have little meaning and are unlikely to be useful to shareholders.

The regulations state that "Profit" shall have the same meaning as is relevant in respect of the preparation of the accounts of the Company. There are a number of different definitions of profit within the accounts and therefore it is not clear which number should be used and further clarity should be provided.

If this requirement is included, as it relates to historical data, we believe it should be included in the implementation report.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We agree that this disclosure will be useful and in our view the proposed regulations cover the right areas of detail.

Situations around exits are varied and companies will need to have the ability to draft their policy on exit provisions with sufficient flexibility to ensure that they can react appropriately and in the interests of shareholders in the prevailing commercial circumstances.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We do not agree that it is necessary for companies to consult with employees on remuneration policy for executive directors in order to develop an appropriate remuneration policy that is both equitable throughout the organisation and creates alignment with shareholder value. We would also observe that many companies operate across many countries and with complex organisational structures and this kind of consultation would be practically very difficult to implement.

We do, however, believe that the remuneration committee should spend more time understanding the remuneration arrangements for the wider employee population to understand how executive arrangements compare to these. As part of this there could be a role for companies to ask employees about their views on their own arrangements in order to gain information to enhance the impact and retention values of these throughout the organisation. A number of companies already include this in their employee engagement surveys. We consider that it would be good practice for the finding of these surveys to be shared (where they are not already) with the Remuneration Committee. Companies should also be encouraged to articulate these findings in the DRR. However, we do not believe that this is a matter for legislation but more for best practice.

On this basis we would suggest that paragraphs 28 and 29 are removed from the regulations with paragraph 27 being retained.

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Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We believe that a single figure, calculated on a consistent basis for all companies, will provide useful information for shareholders, particularly when considered in the context of information regarding the performance of the business during the relevant period.

We agree that the proposed methodology for calculating the single figure is a sensible approach and that it gives effect to the Government's intention, subject to the comments below:

- **Comparative data -** In addition to providing a single number for the financial year being reported on (broken down into its component parts) we also believe that companies should be required to include the total single number for the prior year as well i.e. a comparative figure to show how the total compensation for each individual has changed year on year. This could easily be achieved through an additional column to the table.

- **LTIP** – The disclosure implies that pay from all LTIPs should be disclosed together. Companies may operate more than one LTIP arrangement and we believe that it would be helpful if the requirement is to disclose the payout from each plan separately but under one overall LTIP heading. For example:

PSP	Share options	Value builder plan	Total LTIP
£500k	£60k	£10k	£570k

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We support this proposal as we believe that this approach is by and large simple and reasonable. While we acknowledge that this approach is not necessarily ideal in all circumstances (e.g. international pensions) we believe the benefit of simplicity outweighs this concern.

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Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that any amounts clawed back (including any deferred shares where malus was applied and these shares did not vest) should be included in the single figure where the amount being clawed back has been included in the figure for a previous year or included in the single figure in another column for this year. Disclosures, however, should make it clear what has been paid and what has been clawed back as a separate item. For example:

Salary	Benefits	Bonus	LTIP	Total (pre-clawback)	Amount clawed back from previously disclosed amounts	Total
£500k	£10k	£250k	£150k	£910k	(£50k)	£860k

Paragraph 5 of the regulations would need to be extended to incorporate this provision and consideration would need to be given to the basis on which clawed back amounts should be disclosed. We would suggested that amounts "clawed back" are included in the year that the clawback occurs based on the original value that was included in the single figure. This will allow for a like for like comparison of the number year on year. It should also become best practice to include details on the reason for the application of clawback.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We support the requirement for companies to provide clear details of the level of payout or vesting under short and long-term incentive plans and what performance was achieved to support this. We believe that Remuneration Committees have a responsibility to evaluate the outturns against the "formulae" but also to consider payouts in the round to ensure that they are appropriate in the context of overall performance and value added for shareholders. It is important that the Committee has this flexibility to do this and that where such discretion is exercised that this is fully justified to shareholders.

We have concerns around a blanket requirement for companies to disclose the full details of the performance metrics **set**, given the potential commercial sensitivities of this approach. We believe this approach could ultimately be detrimental to the interests of shareholders.

This concern is primarily in relation to annual bonus payments, although in some cases may also apply to long-term plans.

Where targets are commercially sensitive, we believe that the disclosure requirements for the year in which the bonus is in respect of should be:

- What the performance measures were and the relative importance of each.
- For each measure, how the company performed against the targets set for that condition (e.g. were they below threshold / at threshold / on-target / above target / outstanding), and, unless commercially

sensitive, what the actual performance was (e.g. profit growth of £xm). There will be some performance targets where performance is not otherwise externally disclosed and we do not believe that in these instances actual performance should be disclosed.

- Where the committee had discretion, how it exercised that discretion.

- The resulting level of award (this will be included in the single figure).

Paragraph 8 of the regulations would need to be amended if this suggestion is adopted.

We not believe that the exact form of such disclosures is a matter for legislation. We have set out an example of what we believe is good disclosure in this area. The exact target performance range is not included but shareholders get a clear indication of where performance falls for each measure.

Measures	**Weighting**	**Performance**			
		Below	*Threshold*	*Target*	*Stretch*
Measure 1	X%				♦
Measure 2	X%	♦			
Measure 3	X%		♦		
Measure 4	X%			♦	
Measure 5	X%			♦	
Measure 6	X%		♦		

We believe that this level of information would be a significant step forward from the current levels of disclosure and would be sufficient for shareholders to assess whether the basis of awards is reasonable in the context of performance achieved.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We support the proposed disclosures on pensions, however we would suggest that companies should also be required to disclose, for individuals participating in defined benefit plans:

- The rate of accrual.

- The accrued benefits at the start of the year, as well as at the end. Although the single figure will include the deemed value of the increase in the accrued benefit in the year, for completeness, we think the start as well as the end position should also be shown.

- The transfer value of the accrued benefits at the start and end of the year. We think this information is important as it provides an indication of the total cost of the pension to the company. We understand the desire to simplify the report, but believe this provides a key piece of information for shareholders in assessing the total benefit to the executive of the pension.

It is not clear from the consultation document whether the Listing Rule requirements would continue to apply (Listing Rules paragraph 9.8.8R(12)). If not, then we believe that it is important that the additional detail on pensions set out above continue to be disclosed.

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Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We agree that showing awards at face value is the most informative approach for readers of the report. The alternative approach of using expected values is overly complex and relies heavily on the particular assumptions made by each company.

As noted, some companies operate plans where the maximum level of vesting is more than 100% and therefore the 'face value' may understate the true value of the award. Under the draft legislation this would be dealt with by the inclusion of a column showing the maximum value at vesting. This information is important for shareholders and we agree that this is a sensible way of dealing with it.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We appreciate the desire to simplify the information on directors' interests, however we are concerned that the draft legislation removes information that is vital for understanding the outstanding awards held by executives.

Our primary concern is around the aggregation of all outstanding awards which remain subject to time and/or performance into a single figure. This means that, without looking back through historical annual reports, the reader is not able to ascertain, for example:

- What plans the shares relate to.
- When these awards are due to vest.
- The exercise price for any share options (and therefore whether they are 'in the money' or not).

This information is currently found in the share interests tables in the DRR and is a requirement of the Listing Rules as well as Schedule 8.

We consider that the following information should be included for each separate outstanding award:

- Number of shares or options awarded
- The date of award
- The date of vesting
- For options the date on which the option expires
- The exercise price and the share price at the date of award
- Details of performance conditions attached to awards where they differ from the stated policy.

It is not clear from the consultation document whether the Listing Rule requirements would continue to apply (Listing Rules paragraph 9.8.8R(2 - 6)).

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Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We agree that it is important that the remuneration report effectively communicates how the level of remuneration delivered relates to the value that has been added for shareholders, however, we question whether the proposed chart is too blunt an approach to do this effectively.

We understand the rationale for the use of total shareholder return as the measure of company performance - it is easily comparable between companies and does ultimately reflect the value that shareholders receive. The challenge with TSR is that it is influenced by factors outside of management's control making a comparison with payouts challenging. Remuneration is made up of a number of different components including fixed pay and bonus which is often based on short-term financial performance as well as long term incentives and therefore payouts are based on a combination of different performance periods. A comparison with an annual TSR might therefore not be fully relevant..

Notwithstanding the above comments, based on the current proposals we would make the following observations:

- We expect that some companies may choose to supplement TSR with other measures (such as underlying profit) which they may consider to be more relevant for them.
- We agree that CEO pay should be used, rather than a total or average of all directors, the alternative approach would make year on year comparisons meaningless given that the number of individual directors on the board can change from year and to year.
- It should be noted, however, that not all companies have a CEO either on a permanent or an interim basis. In this circumstance, companies should have the flexibility to determine which director should be included in the chart - highest paid director might be an appropriate choice.
- It is not clear whether the first financial year for the purpose of this chart be the financial year for which this legislation comes into force or is a chart of look back over the previous ten years. In our view for simplicity it would be better if this chart was forward looking from the date of implementation..
- The graph should cover a five year period, rather than the ten year period proposed. The rationale for this is that five years is more closely aligned to the typical tenure of a CEO and would better reflect the current remuneration committee's decisions around pay. We believe that a chart based on five year TSR and CEO pay would be a more meaningful addition to the annual disclosures. .

Question 15: The Government proposes that the single figure, details of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We agree that the areas set out above should all be subject to audit.

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Other comments

In addition to our response to the detailed questions above we also have the following comments:

Interaction with the Listing Rules

As set out in our covering letter, a significant area of uncertainty is the interaction of these new regulations with the Listing Rules. If no changes are made to the Listing Rules there will be a requirement to report information in different ways. Notwithstanding this, we believe there are some aspects of the current regulations that are not included in the proposed regulations that should be retained either in the new regulations or as part of the Listing Rules. These are:

Listing rule reference	Information captured	Why this is useful
LR 9.8.6(1)	Directors' interests (i.e. shares of which the director is the legal owner) at the end of the period under review and "at a date not more than one month prior to the date of the notice of the annual general meeting"	This is a more detailed requirement than that set out in 14 (b) of the draft regulations and captures whether there have been share sales following the year end.
LR 9.8.6(6)	A statement as to whether the company has complied with all the relevant provisions of the UK Corporate Governance Code, and if not, the reasons for any non-compliance.	This forms the heart of the UK corporate governance system of 'comply or explain'.
LR 9.8.8(2)(b)	The total remuneration for each director for the period under review and for the corresponding period.	As set out in our response to Question 7, we believe that companies should continue to be required to show the total single figure for the prior year. This comparative enables shareholders to understand how the total compensation for each individual has changed year on year.
LR 9.8.8(2)(c)	Payments to former directors	This is an important requirement as it allows shareholders to see potentially valuable payments made to directors made after they leave the board. This requirement should be maintained within the listing rules or it should be included in the revised reporting regulations.
LR 9.8.8(2-6)	Tables of outstanding long-term share or share option awards	As set out in our response to Question 13, we are concerned that the draft legislation over simplifies the information on outstanding share

		awards that is vital for shareholders to understand the awards made. See our earlier response for more details.
LR 9.8.8(12)	Details of defined benefit schemes	As set out in our response to Question 11, we suggest that companies continue to be required to disclose additional information for individuals participating in defined benefit plans, in order for shareholders to understand the total benefit for the individual and cost to the company. See our earlier response for more details.

Remuneration Consultant fees

We continue to believe that it is not appropriate to require companies to disclose fees paid to remuneration consultants. We understand the potential conflict of interest concerns that may arise, however, simply requiring the fees paid to consultants to be disclosed only focuses on one narrow part of the issue.

It is unclear to us what conclusion shareholders should draw from knowing how much was spent on advice. Companies should not be discouraged from seeking external independent advice as this often enhances the quality of committee decision making.

We believe that potential conflicts of interest are best managed via governance of consultants (through the Remuneration Consultants Group) and the consultant selection process. The SEC recently issued Listing Standards for Compensation Committees that requires compensation committees to consider certain factors when appointing advisors. These factors are:

- Whether the compensation consulting company employing the compensation adviser is providing any other services to the company
- How much the compensation consulting company who employs the compensation adviser has received in fees from the company, as a percentage of that person's total revenue
- What policies and procedures have been adopted by the compensation consulting company employing the compensation adviser to prevent conflicts of interest
- Whether the compensation adviser has any business or personal relationship with a member of the compensation committee
- Whether the compensation adviser owns any stock of the company, and
- Whether the compensation adviser or the person employing the adviser has any business or personal relationship with an executive officer of the issuer.

While we do not believe it is necessary to regulate on the factors that need to be considered when appointing advisors, we do believe that it would be useful to issue some guidance on the factors that ought to be considered when selecting advisors, and suggest that companies could disclose information about how advisors were selected, as well as why they are considered independent, and the processes advisors have in place to minimise conflict of interest and how on-going independence is monitored. This information would complement requirements to disclosure the nature of services provided.

Finally, we believe it is important that details of all parties that have provided advice to the Committee which has materially assisted in making a decision about executive remuneration should be disclosed in the remuneration report (including company brokers, lawyers and other advisors) even where this advice is provided free of charge. In our experience, this does not always happen.

Exit payments

In the BIS Secretary's statement on the 20th June 2012, it was noted that it would be a requirement that when a director leaves, a company will have to publish a statement promptly, setting out exactly what the director has received on exit. This requirement is not included in the draft regulations – how is it intended that this requirement will be enacted and from what date will it apply from?

EIRIS

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
X	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

The draft regulations appear to successfully give effect to the policy set out in the consultation document.

We note that the Government does not propose to prescribe (beyond general headings) the types of pay of the specific disclosures that are required for each element of pay. We would therefore support the creation of best practice guidance (as mentioned in paragraph 43 of the consultation).

Particularly with the policy objective of encouraging companies "to be proactive in designing long term pay policy that is clearly linked to the company's strategy and which is acceptable to shareholders" there could be guidance that gives examples of the types of metrics that could be considered as best practice when measuring long term performance. Such guidance could give examples for section 19(a) of the draft regulations, which covers short and long-term strategic objectives of the company (or group) within the elements of the directors' remuneration package in the table in the directors' remuneration report.

EIRIS would suggest that best practice guidance could refer to consideration of environmental, social and governance metrics as criteria for measuring long-term financial corporate performance.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Given the existing length of remuneration reports, we imagine that the costs associated with revised reporting requirements should not result in a significant change in cost for the reporting organisations.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

This is a practical and informative approach. We understand the need to increase transparency whilst allowing for flexibility by the company.

We support the creation of best practice guidance (as mentioned in paragraph 43 of the consultation).

Particularly with the policy objective of encouraging companies “to be proactive in designing long term pay policy that is clearly linked to the company’s strategy and which is acceptable to shareholders” there could be guidance that gives examples of best practice metrics for consideration when measuring long term performance. Such guidance could refer back to section 19(a) of the draft regulations, which covers short and long-term strategic objectives of the company (or group) within the elements of the directors’ remuneration package in the directors’ remuneration report table.

In any best practice guidance, we would strongly urge the Government to encourage companies to consider extra financial elements, such as consideration of environmental, social and governance metrics for measuring long-term financial corporate performance, in particular when these are financially material to the long-term business strategy and likely success of a company. An increasing number of investors such as those who are signatories to the UN Principles for Responsible Investment are actively seeking the implementation of such metrics.

As an example of best practice reporting, the Global Reporting Initiative is currently consulting on its revised guidelines for corporate reporting. Its reporting guidelines are used by thousands of companies globally including many in the UK. In the draft guidelines, disclosure 64 encourages companies to disclose:

“If performance-related pay is used, describe how performance criteria in the remuneration policy relate to employees’ economic, environmental, and social objectives for the reporting period and the period ahead. Break down the information by governance body, senior executives, and all other employees. Include all applicable types of compensation used by the organisation such as salary, bonuses, stock awards, option awards, and all others.”

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We support this approach as it encourages greater transparency.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

No comment

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

EIRIS supports the Government's proposal for the policy part of the remuneration report to include such a statement.

However, we would suggest that those organisations that answer negatively in response to the statement's question of "whether" such a company sought employee views on the remuneration, should be required to additionally explain why they did not seek such views on the remuneration policy.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We support the items included in the table. The table helps to breakdown how the remuneration figures are calculated. We also support the intention to create a single total figure.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

No comment

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Transparency about a company's policies on remuneration claw-back would be helpful, so we support this approach.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

There is a fine line to be achieved between how much information investors need access to in order to effectively judge whether performance measures are challenging enough and applied correctly, and commercial sensitivity.

We would suggest that at the very least shareholders need to know whether or not core performance targets have been met; as without this information shareholders will find it difficult to understand how well the company has performed and therefore whether remuneration rates are/were justified.

EIRIS would also propose the inclusion of an additional reference to consideration of environmental, social and governance metrics in the table relating to long-term incentives:

- "If any environmental, social or governance metrics are included in the performance conditions for the company
  - If yes, how these environmental, social or governance metrics have been included in performance conditions
  - If no, why environmental, social or governance metrics have not been included in performance conditions"

We would strongly urge the Government to encourage companies to disclose in the details about performance against conditions for annual bonus and LTIP contained in the single figure table companies, whether and how consideration of environmental, social and governance metrics for measuring long-term financial corporate performance, were included.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

No comment

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We support this approach.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

No comment

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

Total shareholder return and CEO pay are not necessarily the only proxies investors may wish to consider for company performance and pay levels. When a company's share price is high, that may not necessarily equate to a good, or even best practice, policy on remuneration for the CEO or other employees.

However, we recognise that having a simple graph showing total shareholder return against CEO pay would nonetheless be a clear piece of information for investors. The Government may wish to proceed with this, but indicate that total shareholder return may not necessarily equate to best practice on pay and investors may need to look further into company information to find this out.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

EIRIS would recommend that the whole remuneration report is subject to audit. We are in favour of meaningful, measurable and verifiable data in the report. It is essential that this is properly verified. External auditing brings credibility, greater accountability and transparency to the reporting process.

If non-financial information was to be included in any remuneration report and therefore audited by auditors, auditors' liability and responsibility would need to be defined (similarly to financial auditors).

Auditors reports should also not be limited to only stating if what has been audited is true, but also making suggestions for improvement in scope, detail and the quality of reporting. This would provide an extra layer of reassurance for report users, and encourage best practice.

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Directors' Pay: Revised Remuneration Reporting Regulations Consultation

Response from the Employment Lawyers Association

24 September 2012

Directors' Pay: Revised Remuneration Reporting Regulations Consultation

Response from the Employment Lawyers Association

Introduction

The Employment Lawyers Association ("**ELA**") is a non-political group of specialists in the field of employment law and includes those who represent employees and employers in the Courts and Employment Tribunals. It is therefore not ELA's role to comment on the political merits or otherwise of proposed legislation, rather to make observations from a legal standpoint. ELA's Legislative and Policy Committee is made up of both Barristers and Solicitors who meet regularly for a number of purposes including to consider and respond to proposed new legislation.

An ELA sub-committee responded to the Shareholder Voting Rights Consultation in April 2012. A new sub-committee was set up by the Legislative and Policy Committee of the ELA under the joint chairmanship of Clare Fletcher of Slaughter and May and Julian Roskill of Slater & Gordon (formerly Russell Jones & Walker) to consider and comment on the Directors' Pay: Revised Remuneration Reporting Regulations Consultation. Its report is set out below. A full list of the members of the sub-committee is annexed to the report.

ELA intends only to address certain of the questions posed by the consultation paper, as set out in Part A below, focussing on the practical experience and expertise of its members, who represent both plcs and directors. ELA’s comments are also limited to issues of employment law, and do not encompass those aspects of the consultation paper which deal with pensions and share schemes. This response is primarily directed towards the drafting of the proposed draft Regulations, which are set out in Annex B of the consultation paper. ELA’s comments on these Regulations are set out in Part B of this document.

Part A: Response to the consultation questions

1. The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

See Part B

3. The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

See section 1.1(A) of Part B

4. The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

See sections 1.2 and 1.3 of Part B

5. The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

See section 1.5 of Part B

7. The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

See section 2.1(B) of Part B

10. The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

See sections 1.1(B) and 2.1(C) of Part B

14. The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

See section 2.3 of Part B

Part B: Comments on the proposed draft Regulations

Note: "Section X" refers to the numbered sections within the body of the consultation document. "Paragraph X" refers to paragraphs of the draft new Regulations.

General comments

- There are a number of instances (set out in detail below) where the drafting of the Regulations is inconsistent and/or unclear.

- The drafting of the Regulations will also need to be amended (as set out below) to tie in with the provisions of the Enterprise and Regulatory Reform Bill which propose a new Chapter 4A of the Companies Act 2006 (CA 2006) governing executive remuneration.

- Sections 8, 30 and 31 make it clear that there will be guidance to accompany the Regulations, but this has not yet been published. The following paragraphs set out some suggestions for areas which could be usefully covered in the guidance. ELA is also conscious that guidance on related issues is currently being produced or updated by other regulatory bodies, including the Financial Reporting Council (in relation to the UK Corporate Governance Code) and the UK Listing Authority (in relation to the Listing Rules). It would be helpful if the guidance to accompany the Regulations takes into account (and is consistent with) this related guidance.

1. Policy part of the report

1.1 Future pay policy table

(A) **Comment**: Paragraphs 18-20 do not prescribe in any detail the form or content of the future pay policy table. Section 43 makes it clear that it is intended that the content of the table will largely be dictated by guidance. This appears to allow companies to set a wide framework for pay policy within this table, and give them the flexibility to make a range of remuneration arrangements whilst remaining within the approved policy. This is a welcome approach from the companies' perspective, as it allows them to formulate a pay policy which is appropriate for their sector as well as their individual circumstances.

That said, ELA's view is that in many cases companies will need to seek annual approval of their remuneration policy (as opposed to triennial approval), under the proposed new section 439A CA 2006. This is due to requirements such as that in paragraph 19(c) to set out the maximum potential value of each element of the remuneration package.

Suggestion: ELA agrees with the Government's approach of leaving the detailed content of the future pay policy table to guidance rather than setting it out in the Regulations.

However, ELA suggests that there should be some link between the elements included in this table and the definition of "remuneration payment" in the proposed new section 226A(1) CA 2006.

(B) **Comment**: Paragraphs 20(b) and (c) require an explanation of why performance conditions on variable pay were (or were not) chosen. ELA agrees with the statement (at Section 44) that the Government does not expect companies to be forced to disclose performance metrics, where to do so would harm shareholder interests. However, this statement is not included in the Regulations. ELA's concern is that reference to specific performance conditions could give rise to problems for many companies as regards sensitive information.

Suggestion: It would be helpful if the statement at Section 44 was reflected in the Regulations, so that the Regulations explicitly provide that companies need not disclose specific performance conditions where to do so would involve disclosure of commercially sensitive information, or otherwise harm shareholder interests.

1.2 Service contracts

Comment: Paragraph 21 requires a statement setting out all contractual provisions that relates to directors' remuneration. This has the potential to make the report very lengthy, since it would require describing the provisions relating to salary, benefits, pension, and other benefits, as well as the terms on which benefits are payable on termination in different circumstances, for each director. ELA's view is that this could jeopardise the Government's objective of making remuneration reports more concise and transparent and enabling shareholders to more easily locate the information which they find most helpful. The new disclosures would also be of limited additional benefit, given the existing requirement on companies to have directors' service contracts available for inspection by shareholders (under sections 228 and 229 CA 2006).

Suggestion: ELA considers that the Government's objectives could be better met if Paragraph 21 were removed, or amended so that it is confined to the terms governing the fundamental components of remuneration which are likely to be of most interest to shareholders. Alternatively, the existing provisions of sections 228 and 229 CA 2006 could be strengthened to ensure that shareholders have ready access to directors' service contracts.

1.3 Graph of performance scenarios

Comment: Paragraph 22 assumes that there will be a single threshold set for performance conditions. In practice, there may be multiple thresholds within one element of variable remuneration. There may also be different thresholds for different elements of variable remuneration. Therefore, ELA's view is that Paragraph 22 will require companies to produce numerous different graphs, to illustrate the various different thresholds which apply to each element of variable remuneration.

Further, it is not clear how the operation of malus/clawback provisions would be accommodated within the graph. ELA assumes that this information would in fact be provided as a note to the graphs.

Suggestion: It would be helpful if the guidance on Paragraph 22 confirms the approach which companies are obliged to take in respect of the above issues.

1.4 Relative importance of spend on pay

Comment: Paragraph 24 requires disclosure of the percentage change "compared to previous years". It is not clear for which (and how many) years this comparison must be made.

In addition, it is not clear whether the "overall expenditure on pay" in Paragraph 24(c) is limited to directors' pay, as opposed to pay for the entire workforce.

Finally, it is not clear how the "pay" in Paragraph 24(c) should be calculated (for example, whether it is limited to base salaries, or should also include other elements of remuneration such as bonus, benefits and pension)

Suggestion: It would be helpful if Paragraph 4 is amended to clarify the above issues. ELA suggests that Paragraph 4 should be amended as follows (a) the comparison that should be required is with the previous year only; (b) the "overall expenditure on pay" in Paragraph 24(c) should be limited to directors' pay; and (c) "pay" should be calculated as the single total figure for remuneration as set out in Paragraph 3.

1.5 Exit payment policy

(A) **Comment**: Paragraph 25 applies to, amongst other things, "termination payments". This concept is not defined in the Regulations, but seems to be limited to contractual payments, by the wording of Paragraph 25(b). It is not clear why the concept of "termination payment" has been used in Paragraph 25, and a separate definition of "compensation in respect of loss of office" is used in Paragraph 33(2) (in relation to the implementation part of the report). Further, both these concepts/definitions are different to the definition of "payment for loss of office" in the proposed new section 226A(1) CA 2006. ELA's concern is that this creates significant uncertainty and inconsistency in relation to what companies' obligations are to disclose exit/termination/compensation for loss of office payments to shareholders.

Suggestion: ELA suggests that paragraph 25 should use the same definition of "payment for loss of office" as the definition which is used in the new provisions of the CA 2006.

However, it is also ELA's view that there is a fundamental problem with the proposed new section 226A(1) CA 2006, insofar as it is not consistent with the current provisions in Chapter 4 CA 2006 (sections 215-222 CA 2006). Although the section 226A(1) definition incorporates the section 215 definition, it does not incorporate the exceptions in the remaining provisions of Chapter 4 (notably, in section 220 CA 2006, where a payment is made in good faith in discharge of an existing legal obligation, by way of damages for breach of such an obligation, by way of settlement or compromise of any claim arising in connection with the termination of office or employment, or by way of pension in respect of past services). ELA suggests that the section 226A(1) definition should be amended to incorporate these exceptions and make it consistent with the current Chapter 4 provisions.

ELA is aware that other concerns with the proposed new Chapter 4A CA 2006 are being raised by other respondents to this consultation. This response on behalf of ELA does not seek to repeat those concerns. However, members of the working party would be happy to discuss and give their views on those concerns, if representatives of the Government would find this useful.

(B) **Comment**: Paragraph 26 requires an explanation of how "termination payments" will be determined. It is not clear what this will require companies to disclose as regards the exercise of discretion. ELA agrees with the principle that companies should be required to disclose where discretion exists. However, ELA's view is that it would be impractical for companies to be required to explain how discretion will be exercised in certain circumstances, and that this would be contrary to the very nature of discretion. ELA notes that this form of obligation is explicitly included in Paragraph 11(d), but has not been included in Paragraph 26.

Suggestion: It would be useful if the guidance on Paragraph 26 confirms the approach which companies are required to take as regards discretion, and that this is as outlined above.

(C) **Comment**: Paragraph 26(d) applies to contractual provisions on exit payments agreed prior to the commencement of the Regulations. This contrasts with the transitional provisions for the new Chapter 4A CA 2006, which exempt any contractual provisions which arise before 27 June 2012 (unless that provision has since been modified or renewed) (see clause 64 of the Enterprise and Regulatory Reform Bill). ELA's concern is that this creates significant uncertainty and inconsistency in the approach to pre-existing contractual agreements.

Suggestion: ELA suggests that Paragraph 26(d) should adopt the same date in respect of pre-existing contractual agreements as the transitional provisions for the new Chapter 4A CA 2006.

1.6 Statement of consideration of conditions elsewhere in company and group:

Comment: ELA's view is that the requirement in Paragraph 30(1) to disclose the percentage increase in pay of the workforce, as against the percentage increase in pay of the CEO, may involve the same problems which prevented the Government pursuing its plan to require disclosure of the ratio between the pay of the CEO and median earnings of the organisation's workforce (as set out in Sections 53 and 54, i.e. firm-specific factors such as workforce composition and main country of operation obscuring meaningful comparison between companies). The option for directors to choose a comparator group rather than using the whole workforce may help to alleviate these issues, although it may also allow a choice of comparator group which puts the directors' remuneration in the most favourable light (for example, by choosing the management level immediately below the board, where remuneration levels are likely to be comparable to (or in some cases, even higher than) than those at board level).

Suggestion: ELA agrees that the option for directors to choose a comparator group for the purposes of Paragraph 30(1) provides useful flexibility. However ELA also suggests that it would be helpful if Paragraph 30(1) permits the disclosure of the increases as being within a range, as opposed to a specific percentage.

2. Implementation part of the report

2.1 Single total figure of remuneration:

(A) **Comment**: ELA's view is that, in Paragraph 5, there are some amounts which could fall within more than one of columns (a) to (e). There is therefore a risk of duplication or uncertainty about how the table should be completed.

Suggestion: ELA suggests that paragraph 5 should be amended to provide for amounts to only appear in one of columns (a) to (e).

(B) **Comment:** The drafting of Paragraph 5(d) requires disclosure of remuneration "awarded in the reporting period" as a result of the achievement of performance conditions that relate to that period. In the experience of ELA's members, this does not accord with usual practice, which would be to award remuneration shortly after the end of the period in which the performance conditions have been satisfied.

Suggestion: ELA suggests that Paragraph 5(d) is amended to require disclosure of remuneration which is "awarded for" the reporting period, rather than that which is "awarded in" the reporting period.

(C) **Comment**: Paragraph 8 requires additional disclosures about performance conditions attaching to variable remuneration within the single total figure of remuneration. Paragraph 8(2)(c) requires the company to disclose, for each performance condition, how the company performed against the targets set for that condition. ELA notes that it does not, however, specify that the same will apply for individual performance against individual performance conditions.

In addition, Paragraph 8(2)(a) requires "details" of performance conditions and of the target set when the performance condition was agreed. Although Section 78 makes it clear that the Government does not expect Paragraph 8 to require companies to disclosure performance metrics where doing so would harm shareholder interests, this is not codified in the Regulations. This is the same issue that is outlined in 1.1(B) above.

Suggestion: ELA suggests that either the wording of Paragraph 8(2)(c), or the guidance on that Paragraph, should clarify whether disclosure of performance against individual performance conditions is required. The suggestion made at 1.1(B) above is also repeated here.

2.2 Loss of office payments:

Comment: Paragraph 11 requires the company to disclose any "compensation for loss of office", as defined in Paragraph 33(2). This definition is different from the definition of "payment for loss of office" in the proposed new section 226A(1) CA 2006. As noted in 1.5(A) above, it is also different from the concept of "termination payments" used in Paragraph 25 (in relation to the policy part of the report). It is not clear why these different definitions have been used. ELA's concern is that this creates significant uncertainty and inconsistency in relation to what companies' obligations are to disclose exit/termination/compensation for loss of office payments to shareholders.

Suggestion: ELA suggests that paragraph 11 should use the same definition of "payment for loss of office" as the definition which is used in the new provisions of the CA 2006 (and in Paragraph 25).

2.3 Comparison of overall performance and pay:

Comment: Paragraph 13 currently provides for a comparison of company performance against the pay of the CEO. However, ELA agrees with the suggestion in Section 91 that the figure for total directors' pay should be used, instead of the pay of the CEO. In ELA's view, this would give a better overall picture of executive pay versus company performance.

Further, Paragraph 13 requires that the comparison be conducted over the previous 10 years. This could create a significant administrative burden for companies, in performing the calculation under Paragraph 3 for such a long period. ELA is also not convinced that a 10 year period is necessary to produce a meaningful comparison.

Suggestion: ELA suggests that the approach set out in Section 91 should be adopted, and the figure for total directors' pay should be used in Paragraph 13 instead of the pay of the CEO. However, ELA recognises that there may need to be a distinction made for this purpose between executive and non-executive directors (whose remuneration packages usually vary significantly). ELA therefore suggests that Paragraph 13 should require the graph to show total pay for executive directors only. Alternatively, Paragraph 13 should require the graph to show one line for total executive directors' pay, and a separate line for total non-executive directors' pay.

ELA also suggests that the comparison under Paragraph 13 should be conducted over the previous 5 years, instead of the previous 10 years. In ELA's view, a 5 year comparison would still produce a meaningful comparison, while imposing a reduced administrative burden on companies. A 5 year period would also accord with the period required for the performance graph under Regulation 5(1) of the current version of the Regulations.

Members of ELA Working Party

Co-Chairs:

Clare Fletcher, Slaughter and May

Julian Roskill, Slater & Gordon (formerly Russell Jones & Walker)

Working party:

Paul Harrison, Baker & McKenzie LLP

Sinead Hall, BG Group Plc

Jean Lovett, Linklaters LLP

Clare Peake, Linklaters LLP

Caroline Stroud, Freshfields Bruckhaus Deringer LLP

Andrew Taggart, Herbert Smith LLP

Alistair Woodland, Clifford Chance LLP

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26 September 2012

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Dear Mr Walker

Directors' pay

Ernst & Young LLP welcomes the opportunity to comment on *Revised remuneration reporting regulations, June 2012* ("the Consultation").

We support the Government's aim to improve remuneration reporting in the UK, and to this end we have replied to earlier consultations and a discussion paper issued by BIS (i.e., *The future of narrative reporting, October 2010, Discussion on remuneration, December 2011*, and *The future of narrative reporting, December 2011.*)

It is important that shareholders can access clear and reliable information on remuneration, to help inform their views on the performance of their companies and those who lead them. Regulation can help in this regard, but it must not develop to the extent that it dictates remuneration structures or quantum, otherwise companies will be restricted from tailoring their remuneration arrangements to support their individual business strategies.

That said, regulation needs to be clearly drafted to help keep remuneration reports comparable. Accordingly, we have provided detailed comments on the draft regulations in the Consultation response form (attached) which in our view would clarify the requirements. We have provided additional notes as well, appended to the form.

We also encourage the Government to publish guidance on the implementation of the regulations as soon as possible, before the regulations are implemented. This should help to ensure the remuneration requirements are interpreted by all concerned - including company stakeholders and external auditors - in the most consistent way possible, in readiness for the effective date. It would also be helpful if this could be done to coincide with the launch of the new UK narrative reporting framework.

We would be pleased to discuss our views with BIS, and for the avoidance of any doubt our response to this Consultation is not confidential. We wish BIS every success in developing this important regulation, and we look forward to reviewing related guidance in due course.

Yours sincerely

Robert Overend
Audit Compliance Principal and Professional Practice Director
Ernst & Young LLP
United Kingdom

BIS | Department for Business Innovation & Skills

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

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Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
X	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

In general, we consider that the draft regulations contribute to the policy objectives set out in the Secretary of State's Foreword to the Consultation. However, as the Government acknowledges in the Consultation, it is a matter for companies to design and implement pay policies that suit their organisations and for investors to hold them to account, and we agree that lasting reform is dependent on both business and investors maintaining active engagement and adopting good practice on pay. The final regulations can ultimately only facilitate this process.

We set out our responses to the specific consultation questions in the relevant sections of this response form, with further drafting issues raised in additional notes appended to this form. . However, we have some observations of principle on other parts of the proposals which are set out below.

Interaction with the strategic report/summary financial statements

In its Narrative Reporting Consultation (September 2011) the Government proposed that the Strategic Report would include key remuneration information. However, paragraph 33 of the Consultation states that although the directors' remuneration report remains a legally required report, 'this does not preclude companies from including information about remuneration anywhere else in annual reports'. This suggests that there will not be a mandatory requirement to include key remuneration information in the Strategic Report.

The original Narrative Reporting Consultation proposals also implied that the Strategic Report could be used as a summary financial statement. Under existing company law, a summary financial statement must include the prescribed summary information on directors' remuneration. If it is still proposed that quoted companies can send out a summary financial statement based on the Strategic Report, the Government should consider, in finalising its Narrative Reporting proposals, whether and if so, what key remuneration information should be included in that summary financial statement.

Development of non-mandatory guidance

In paragraph 30 of the Consultation, the Government highlights that the draft regulations will 'need to be supplemented by clear guidance on the level of detail and type of information that should be reported.' We have a number of concerns over the clarity of drafting, including, in particular, how and when certain common features of directors' remuneration should be reported in the analysis by element of the single figure for directors' remuneration (required by paragraph 5 of the draft regulations). We give a number of examples in our response to Q7. While we consider that the drafting of the regulations needs to be clarified, we also strongly support the issuance of implementation guidance which, inter alia, could address the treatment of common features of directors' remuneration, in order to enable a consistent interpretation to develop.

It would be appropriate if this guidance reflects the input of both companies and investors, similar to the guidance produced by the Financial Reporting Lab in support of BIS's proposal for a single remuneration figure. It would be helpful if such guidance were to be developed in conjunction with other guidance (e.g. to support Government proposals on narrative reporting). In order to give companies time to prepare remuneration reports under the regime, we believe that guidance should be in place as soon as possible after the regulations have been passed by Parliament, particularly as the proposed effective date for the changes is periods ending after October 2013.

Specific disclosures

We are not convinced that every disclosure proposed in the draft regulations will provide meaningful information to support the Government's policy objectives. For example, the various disclosures of percentage increases in pay and profits in a particular year may be distorted by specific factors that are not representative of long-term linkages between pay and performance. (See appendix).

Certain disclosures included in the existing Schedule 8 of SI 2008/410 should be retained. In particular, we would support retention of roll-forward tables for LTIP and share option schemes. There is limited information required in the draft regulations (except for an overall table on directors' interests in shares) on the existence of awards under such schemes made in previous years (where these have not met the final performance conditions in the current financial year). This detracts from a proper assessment of the remuneration packages of directors and the linkages between pay and performance. (See our response to Q12).

In addition, we note that the disclosures of compensation for past directors and sums paid to third parties in respect of directors' services, currently in paragraphs 15 and 16 of Schedule 8 have been removed. We disagree with their removal. We concur with the removal of disclosure of excess retirement benefits of directors and past directors, currently in paragraph 14 of Schedule 8.

We are also concerned that no comparative information appears to be required for the single total remuneration by director. In our view, it would be informative to have this available in total (and for each element) in the previous year. This would also help put into context the "lumpiness" of certain variable elements of pay.

Compensation for loss of office

One of the changes made in the draft regulations (compared to existing Schedule 8) is to report exit payments separately from the table making up the single figure of remuneration. Paragraph 33(2) of the draft regulations states that 'references in this Schedule to compensation [for loss of office] include benefits otherwise than in cash; and in relation to such compensation references in this Schedule to its amount are to the estimated money value of the benefit'. This gives rise to various isues.

Firstly, the boundary between what amounts are reported under paragraph 5 as part of the single remuneration figure, and what amounts are reported under paragraph 11 as compensation for loss of office is unclear. Under the related requirements of the Enterprise and Regulatory Reform Bill, exit payments must be computed in accordance with the approved policy (subject to any transitional requirements set out in the Enterprise and Regulatory Reform Bill, once enacted). An exit is likely to give rise to an early pay out of amounts due under 'schemes' (e.g. long term incentive plans/share options) or even annual (and deferred) performance bonuses which have not legally vested as at the date of exit.

For awards where all qualifying performance conditions have been met, or awards with no performance conditions (even if there are remaining qualifying conditions), the value of the award as measured under the draft regulations may have been reported as part of the single remuneration figure in the current or previous period. However, if the director has not met the further service or other qualifying conditions, the amount of award which vests on exit may be scaled back. Other awards may not have yet met the normal performance conditions (which would have applied if the director had not left) and therefore would not have been previously reported. This should be clarified in the draft regulations and/or related implementation guidance.

Secondly, the measurement requirement in paragraph 33(2) used for compensation for loss of office could differ from that used for computing elements of the single remuneration figure in paragraph 5 of the draft regulations. An example is an enhancement made to a pension provision, or where the terms of the exit payment policy determine how many share options can be exercised (if the normal service and performance conditions have not otherwise been met). It is not clear that this is intended and it may be appropriate that further requirements on how to compute compensation for loss of office is included and at what date it is measured.

Thirdly, often exit packages provide for mitigation, e.g. payments will cease if the director secures new employment. In such cases, some companies will currently report the full amount as compensation for loss of office whereas others may report the payments as they become receivable (as if the director obtains alternative employment, these amounts will not be paid). Under existing Schedule 8, such payments will be reported in any event as payments to former directors (if not reported as compensation for loss of office). However, the Government should consider clarifying the treatment of contingent payments in the draft regulations (and other exit payment statements).

Under the amendments made to sections 226E of the Companies Act 2006 in the Enterprise and Regulatory Reform Bill, amounts paid which are in contravention of the approved (remuneration or exit) policy (subject to transitional rules) are held by the director on trust. The interaction of this requirement and paragraph 35(2) which implies that 'sums to be accounted for the company or any of its subsidiary undertakings etc.' are excluded from the amounts shown under the draft regulations could give rise to a lack of clarity as to what is reported as remuneration. It is important that the directors' remuneration report discloses what directors have received as remuneration (even if not in accordance with the approved remuneration policy). This is quite different from not disclosing as remuneration, say, a season ticket loan repayable by the director.

Interaction with the Listing Rules

The remuneration disclosures in LR 9.8.8R relate to premium listed UK companies (which would also be quoted companies under the Companies Act 2006). At present, there is a degree of overlap of the disclosures in LR 9.8.8R (but also some conflict) with Schedule 8. The proposed disclosures in the draft regulations also differ in a number of respects from, and do not include all disclosures required by, LR 9.8.8R. It would simplify matters if the disclosures if the draft regulations are acceptable to the UK Listing Authority. However, if this is not the case, we are concerned that the additional disclosures needed to comply with both company law (as set out in the draft regulations) and the current requirements of LR 9.8.8R (over and above the company law requirements) are likely to be more extensive than is currently the case.

Interaction with Schedule 5 to SI 2008/410

At present, quoted companies additionally have to comply with paragraph 1 of Schedule 5 to SI 2008/410 in the financial statements. Most quoted companies are IFRS reporters and therefore comply with IAS 24 key management personnel compensation. However, these disclosures are not necessarily comparable with the statutory directors' remuneration disclosures, as they reflect compensation for key management personnel (which may not equate to the board of the directors) and the categories and bases of measurement of the elements of compensation vary from those required under company law.

As most of the information required on remuneration by Schedule 5 is already included in the directors' remuneration report, some companies currently cross refer to the latter from the financial statements, adding any additional disclosures required by Schedule 5, e.g. gains on exercise on share options (with comparatives).

Under the draft regulations, there will be differences between the total remuneration (as computed under the two schedules, particularly in relation to pensions, LTIP schemes and share options). To have to additionally comply with Schedule 5 could be both a burden and confusing to investors who may now be seeing three sets of total pay information.

Provided the Government is satisfied that Schedule 8 provides sufficient information on directors' remuneration (and subject to retaining any minimum requirements of European Accounting Directives), we would recommend that quoted companies do not additionally need to comply with paragraph 1 of Schedule 5. However, the issue with IAS 24 still remains, and unless the statutory directors' remuneration disclosures are revised to reflect the requirements of IAS 24, the incomparability of these two disclosures will remain.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Costs involved in adjusting to the revised regulations will vary by company. This question is therefore best answered by companies, but we would expect BIS to have some idea of what these costs might be, as part of the impact assessment process for these new requirements.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We agree with the Government's proposed approach not to prescribe the specific disclosures required for each element of pay. However, we stress the importance of introducing guidance to help companies present high quality information that clearly sets out the linkage between pay structures and strategy and long-term performance.

As we emphasised in our response to the earlier consultation on narrative reporting, we believe that a "one-size-fits-all" approach is challenging as company pay policies and the interests and needs of stakeholders vary. Allowing companies to tailor disclosures by a certain extent is a practicable approach.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Overall, we believe that reporting requirements should only be introduced if they provide information which users of remuneration reports: a) want and need; b) but cannot find or access.

Service contracts
We do not believe that requiring companies to disclose "all" contractual provisions relating to directors' remuneration would lead to any additional benefits for shareholders.

Instead, we believe that a requirement for companies to provide a detailed summary of the provisions relating to remuneration contained in the directors' service contracts should suffice.

Scenarios

While graphical representation of remuneration outcomes expected under different outcomes has the potential to provide meaningful information, we consider that the requirements are unclear and that expected pay outcomes may not be comparable across companies.

For example, the terms – 'threshold', and 'below threshold' are not defined and even if these were to be defined, this may be interpreted differently by different companies. Therefore, it is important that companies are required to set out clearly the approach to determining the threshold and below threshold levels. In addition, the wording is unclear as to what elements are to be included, how they are to be measured and over what period (particularly for LTIP schemes covering several performance periods).

The Enterprise and Regulatory Reform Bill specifies that a resolution to approve the first policy report must be approved at the accounts meeting held in the first financial year, which begins after the coming into force of the Act (likely 1 October 2013) or at an earlier general meeting. The policy described in the Policy Part may, therefore, not relate to remuneration commencing in a financial year.

An interpretation of the requirements is that the graphical disclosure should relate to the outcomes for all elements of remuneration awarded, under the policy described in the Policy Part. This would include the ultimate expected outcome of LTIP awards with performance conditions granted in the financial year to which the Policy Part first relates (or other relevant period – although what this would be, is unclear) and be measured consistently with the requirements for the elements of the 'single total remuneration figure' for each director. The draft regulations do not, however, contain detailed requirements which could lead to diverse interpretations.

Complexities in remuneration packages, e.g. agreeing to make new grants of share awards each year over a multiyear period, could lead to particular interpretational difficulties. In addition, it would not be possible to easily check expected with actual outcomes as the remuneration disclosed in the Implementation Report relates to LTIPs whose performance conditions were met in the financial year (which may have been granted many years previously).

We would advise that, if this disclosure is retained, the wording is clarified and 'road-tested' to establish that it is operational and meets the policy objective.

Relative importance of the spend on pay

We do not believe that setting out the percentage change in total pay (or total directors' pay, if this is what is intended) relative to changes in profit and dividends in the reporting year is a practical way of showing the relationship between pay and company performance.

The reasons are outlined below:

- Pay outcomes in a reporting period are not always aligned, in terms of timing, to profit and dividend results of that period. For example, LTIPs with relative performance measures can still pay out even where company profits have declined.

- Profit, dividends and overall expenditure on pay can vary significantly, due to one-off events and circumstances. We believe that year-on-year variability would limit the relevance of the proposed disclosures in assessing either linkages of long-term pay and performance, or how profits earned are disbursed between pay and investors.

- In addition, the wording is unclear in that it does not define:

    - the measure of profit to be used;

    - dividends (e.g. are these dividends on ordinary equity shares, or dividends for each class of share - including shares classified as liabilities where the finance costs may, in certain circumstances, be deducted from profits?) and

    - overall expenditure on pay (does this refer to total directors' pay, total employees' pay- and if so - what is the treatment of subcontractors etc - and does it include all elements of employee benefits, including items like share-based payments?).

- We also consider that paragraph 24(c) should refer to 'the accounts of the company *(or where the company is a parent company and group accounts are prepared, the group accounts)'*. This is because the percentage changes disclosed are supposed to be consistent with the definitions used in respect of the preparation of the accounts.

- Moreover, if the relevant information is readily available from the financial statements, we question the added value of providing these metrics in the directors' remuneration report.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We believe the disclosures proposed in the draft regulations will facilitate greater shareholder understanding on exit payment policy, although the requirements could include 'how, or in what way' the company will distinguish between types of leaver and the circumstances under which a director left, and also the limits of remuneration committee discretion allowed for within the policy.

We note, however, that the disclosures set out in paragraph 26(a) to (d) are not necessarily exhaustive as the main requirement is to 'state the policy on which the determination of the termination payment will be made'. The Enterprise and Regulatory Reform Bill requires exit payments to be computed in accordance with the approved policy (subject to any transitional requirements). Failure to do so will mean the director holds the sums on trust for the company or for any other person making the payment (and any director who authorised the payment by a company is jointly and severally liable to indemnify the company making the payment for any loss resulting from it). Companies, in conjunction with their legal advisers, therefore will need to be satisfied that the level of disclosure provided on exit policies in the Policy Part is appropriate.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We support the Government's view that there should not be a statutory duty for companies to consult their employees on pay issues, and that the views of the wider organisation (if consultation could be effective) may provide an important perspective. However, we are concerned that there may be a negative perception of companies which state that they have not consulted with employees, and that some companies face far greater challenges in implementing effective employee consultations compared with others. This concern could lead to a proliferation of boilerplate disclosures, or partial employee consultations which may not be effective in achieving the policy objectives.

It is also important to recognise that the practicability of effective employee consultation will be influenced by wider factors such as the industry within which a company operates, the structure of the organisation, the global nature of its workforce and the extent to which employee representative groups already exist.

Equipping employees with the knowledge to provide meaningful views is not a straightforward exercise. At a very basic level, employee representatives would need to be informed on wider business issues and how such issues impact the company's remuneration policies. Further, employees would need to understand the intricacies of their company's remuneration structures. There is also the issue of how employees assess information on remuneration policy to arrive at a view point.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We do not believe that the specific disclosures in the draft regulations for paragraphs 5(d) and (e) clearly give effect to the Government's intentions as reflected in the Consultation.

Performance conditions versus service conditions

The draft regulations (see, for example, the definition of 'scheme' in paragraph 7) distinguish between performance conditions and service conditions. Performance conditions are not specifically defined under the draft regulations or under existing Schedule 8. The concept of performance conditions has caused interpretational difficulties in IFRS 2 (and is the subject of a recent Improvements Exposure Draft). While it may not be necessarily appropriate to mirror the definitions in IFRS 2 in the regulations, consideration should be given to explaining what is meant by 'performance conditions'.

In particular, it is important to clarify whether awards should be reported in the year of grant, if subject only to service conditions – and in the year the last performance conditions for vesting are met (even if there are other qualifying conditions such as service conditions which have not yet been met). This appears to be the effect of the drafting, but it is not clear whether this was the intention. Further application guidance on this issue would be valuable in the non-mandatory guidance discussed above.

The focus on whether performance conditions (rather than whether service or other 'non-vesting' conditions) are met and the measurement criteria in paragraph 6 of the draft regulations inevitably mean that the actual value of the awards earned by the directors on vesting may differ from that reported under the draft regulations.

Distinction between paragraphs 5(d) and 5(e)

The wording used in paragraphs 5(d) and 5(e) is convoluted and reference to the Consultation is needed to determine what might be the Government's intention in distinguishing between these categories.

The table on p24 of the Consultation clarifies that 5(d) should capture the 'full bonus awarded in relation to the performance year'. The table, however, is unclear whether this is intended to capture deferred bonuses which are subject to further service conditions for vesting, rather than simply delayed payment. We assume that the intention with paragraph 5(d) captures annual bonuses (including deferred bonuses subject to service conditions). This would be consistent with the conclusions set out in the Financial Reporting Lab report 'A single figure for remuneration'.

By contrast, the table clarifies that paragraph 5(e) is intended to include LTIP awards (or 'schemes') with performance conditions over more than one performance period, once the performance conditions in the final performance year are met - and hence will reflect actual (or 'an estimate of actual outcome', if the performance conditions are met in the financial year but final vesting is post year end).

The table also states that 'where there are no further performance conditions for long term incentives, awards granted relate to current performance year'. This implies that a long term incentive scheme with say, solely a three year service condition, would be reported in the financial year that the award is conditionally granted. This is confirmed by the drafting of paragraph 5(e) but would mean accelerated reporting of such awards in the year conditionally granted, compared to the current Schedule 5.1(1)(b) and (c) requirements to disclose gains on exercise of share options (and amounts received or receivable under LTIPs).

Distinction between paragraphs 5(d) and 5(e) - Problem scenarios

As drafted, there is potential for a 'deferred bonus' subject to a service condition to meet both the definition of 5(d) and 5(e)(ii). In addition, it is not clear how a 'sign on' or a 'stay on' bonus is awarded, if a director meets a requirement to stay for a period which is met within the same financial year. This is neither clearly salary nor is it an award as a result of achievement of *performance conditions* under 5(d) nor is it a 'scheme' under 5(e).

To take another example, would the value of share options awarded to directors under a three year SAYE scheme be viewed as reportable under 5(e)(ii) in the year the share options are conditionally granted, as the remaining conditions are 'service conditions' or 'non-vesting conditions' (such as continuing to save) that do not relate to performance?

Distinction between paragraphs 5(d) and 5(e) – Potential drafting suggestions

Paragraph 5(d) includes the phrase 'money or other assets *awarded* in the reporting period as a result of the achievement of performance conditions that relate to that period'. Annual and deferred bonuses may not be actually awarded until the following period, once the remuneration committee has approved them. Moreover, the exceptions in 5(d)(i) refer to 'payments' whereas awards can meet the qualifying performance conditions before they are paid. The reference in paragraph 5(d)(i) to 'final vesting is determined as a result of the achievement of performance conditions relating to the year being reported on (or shortly thereafter)' also lacks clarity. In paragraph 5(e)(ii), should it read 'where the final *vesting* (i.e. rather than value) is not dependent on the achievement of performance conditions'?

We acknowledge that it is difficult to draft wording to capture the government's intention here. As illustrated above, it would be sensible to 'road-test' wording against common remuneration scenarios to see whether the requirements meet the intended objective. This may be an area that non-mandatory guidance could explore with guidance on the principles and illustrative examples.

Some suggested wording which presumes that paragraph 5(d) represents all annual bonuses (and deferred performance bonuses including service conditions only) relating to the financial year is set out below for consideration. This is based in part on the definition in Schedule 8.7 of SI 2008/410 and the definition of 'deferred bonus' included in the FSA's Listing Rules.

'(d) the total amount of bonuses paid to or receivable by the person in respect of qualifying services subject to qualifying conditions in respect of service and/or performance in a period not exceeding the length of the financial year, notwithstanding that the bonus may, subject only to service conditions [or other qualifying conditions which are not performance conditions] be receivable by the person after the end of the period to which the bonus award relates.

(e) awards of money or other assets (including shares and share options) made under schemes (as defined in paragraph 7 below) where:

> (i) the award under the scheme (as defined in paragraph 7 below) includes qualifying conditions in respect of performance conditions covering more than one financial year and final vesting due to fulfilling the performance conditions is determined in the year being reported on. This includes awards which remain subject only to service conditions [or other qualifying conditions which are not performance conditions].
>
> (ii) awards granted under schemes (as defined in paragraph 7 below)

in the financial year, where final vesting is not dependent on the achievement of performance conditions. This excludes bonuses reportable under (d).'

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We agree that the Government's proposal to apply the HMRC methodology is a practical and informative approach. The use of the HMRC methodology to value DB benefits is clear and (in the pensions world at least) is a universally understood and simple approach. Using the HMRC methodology would enable pension benefits across companies to be valued using a consistent basis. This will aid comparisons between companies and hence transparency.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

The answer to this question depends on the type of claw-back applied, and how the Government would like these arrangements to be reported.

There are two types of claw-back: (1) claw-back of deferred remuneration ('malus'); and (2) claw-back of actual remuneration paid. Both types of claw-back are quite distinct from each other.

Paragraph 73 of the Consultation indicates that cases of malus will appear as a reduced LTIP value to a director (presumably on the basis that the percentage vesting under paragraph 6(e)(ii) of the draft regulations would be based on the knowledge, as at the time of approving the remuneration report). Paragraph 73 also indicates that 'In cases of formal claw-back, where moneys are retrieved following misstatement or misconduct, it is consistent with the approach set out here that this is also disclosed as part of the single figure' but acknowledges that 'companies may choose to set out the circumstances and factors that affected the decision in its supporting disclosures'.

Unfortunately, it is not clear from the Consultation or the draft regulations how each of these types of claw-backs would be recorded for the purposes of the single figure. It is also not obvious from the draft regulations that the effects of claw-back or malus are intended to be reflected in the single remuneration figure nor how this should be done.

The effects of claw-back or malus, since the previous remuneration report was approved, should be reported in the next directors' remuneration report issued after they occur – but should be distinguished separately as a prior year adjustment from the single remuneration figure, where the remuneration of that director is reported in the financial year.

However, in many cases, claw-back or malus would relate to former directors. Unlike Schedule 8 or the Listing Rules, the draft regulations do not contain requirements for disclosure of payments to former directors. We consider this is an important disclosure which should not be omitted. See our comments on specific disclosures in response to Q1.

We note that practice and guidance around remuneration claw-back is still developing. We believe that there must be further experience and understanding on this issue to ensure the reporting of claw-back is practical and informative for shareholders. We note that the FRC intends to consult on extending the UK Corporate Governance Code's existing provisions on claw-back arrangements.

Awards with no performance conditions

A similar issue may occur when awards which are not subject to performance conditions could fail to vest, e.g. due to not meeting any service conditions. As discussed in our comments in response to Q7, it appears that such awards under LTIP schemes are reported in full under paragraph 5(e) in the year of grant. Paragraph 5 appears to include no requirements to disclose subsequent failures to vest – which could lead to an overstatement of the remuneration figure. If the wording was amended to permit adjustments for items which subsequently fail to vest, we consider that such amounts should be separately identified as 'prior year adjustments'. In addition, there would need to be guidance on the amounts at which 'failures to vest' were reported (as share-based remuneration would have been reported at a different amount in the remuneration report when granted, compared to the value of the shares foregone on failing to meet the service condition).

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We believe that any disclosure regarding *full* details of performance against metrics could potentially be commercially sensitive. There may be a case for flexibility to provide an appropriate balance between providing fuller information for investors on the achievement of performance metrics for variable pay (and on the extent to which discretion has been used, where such metrics are not met), and providing protection to companies from disclosing commercially sensitive information. However, we believe that how such a balance might best be achieved is best answered by companies and investors.

If an exemption was given in certain circumstances, the Government should consider requiring companies using such an exemption to disclose use of the exemption, giving an indication of the nature of the performance conditions not disclosed, and the reasons why commercially sensitive.

We note, however, that the drafting of paragraph 8 is also unclear and is unlikely to meet the government's intended objectives. In particular, an annual bonus (and potentially a deferred annual performance bonus, depending on how paragraph 7(3)(a) is interpreted) would not be a 'scheme' (as defined in paragraph 7). Consequently, it is unclear whether any of the 'relevant details' in paragraph 8(2) are required at all for annual or deferred annual performance bonuses. This seems, however, unlikely to be the intention.

This is important as potentially there is more sensitivity over annual performance objectives (which can often be personal as well as company/group performance based) as opposed to those in LTIP schemes (e.g. TSR and earnings per share performance).

It is also unclear what, if any, information will be reported under paragraph 8(2) for LTIP scheme interests awarded which are not subject to performance conditions (such as SAYE schemes or LTIPs with only three year service conditions).

(See Appendix).

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

Our view is that the proposed disclosures are appropriate in respect of the disclosure of benefits accrued over the accounting year, however no absolute value of the benefits is provided, which is in contrast to the current disclosures.

The lack of a current value of the benefits appears to be minor, given that it is the change in benefits, ie cost of benefit accrual over the year, which is of most importance. Also, in future years, all new directors' benefits will be able to be calculated by simply adding up the accrual over previous years' accounts, meaning that the lack of a disclosed value will have little impact.

Regarding paragraph 10(3), in respect of the disclosure of early retirement benefits, the regulations are unclear. Are the proposals looking for the enhancement cost of any early retirement benefits to be disclosed in the year in which a director takes early retirement? The wording is not at all clear.

It is also unclear from paragraph 10(3) how the early retirement benefits are to be valued. Are they to be valued using the HMRC method and an annuity rate of 20 - in which case the disclosure would only show the value of additional benefits and would in fact show a reduction in value where there is an early retirement reduction applied. This would also hide what is often the most significant increase in value on early retirement which is the waiving of the early retirement factor.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Disclosure of face values

No. We do not believe that disclosing scheme interests at face value is practical, nor is it informative.

The face value of scheme interests does not reflect the real value of the grant to a director and can therefore, mislead the reader. It is also unclear how 'face value' is defined in the draft regulations. For example, what is the face value of options to acquire shares at an exercise price which is equal to the current market price at grant date?

Although the Government recognises that supporting disclosures are necessary, we believe that face values would nevertheless be mistakenly represented to the public as take home pay, whereas they may not represent expected performance and cover performance over a number of years.

We note that paragraph 12 of existing Schedule 8 could provide a basis for providing sufficient information to compute 'face values of awards' because it requires 'details of scheme interests' to be given, with further details required for share awards made such as the number of shares and market price and performance conditions.

If the existing requirements in paragraph 12 were supplemented with similar details for share option awards (which are currently set out in paragraphs 9(c) and (e) of Schedule 8) and additional information was provided on 'threshold vesting percentages' (once appropriately defined), this would either directly meet most of the disclosure requirements set out in paragraph 12 of the draft regulations or enable the required amounts to be easily ascertained.

Retention of roll-forward tables (or similar) for LTIPs and share options

The existing Schedule 8 disclosures of roll-forward tables for share options and LTIP scheme interests (and supporting information) have been removed in the draft regulations. The Listing Rules also require similar roll-forward tables and therefore if these are proposed to be removed, it would be important that this was also acceptable to the UK Listing Authority.

Under the draft regulations, detailed information will only be available in respect of awards of scheme interests (i.e. LTIPs and share option awards with service/performance covering more than one period) in the current financial year (in paragraph 12) and in the period that amounts become 'receivable' (under paragraph 8). See Appendix and response to Q10.

In our view, the draft regulations give little insight into the *overall* remuneration package that has been made available to the director. We consider that the existing roll-forward tables provide more useful information as to the existence of all awards and their status (e.g. exercise dates, dates when scheme interests would vest or not), with additional details for new awards and vested scheme interests or share options exercised in the financial year (as referred to above).

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We welcome any simplification of existing reporting requirements and agree it is important that this disclosure should be consistent with the disclosure requirements under LR 9.8.6R. Since only premium listed companies (admitted to the FSA's Official List) are subject to LR 9.8.6R, and not all 'quoted companies' are 'premium listed companies', we acknowledge that there is a role for statutory disclosures of directors' interests, if this is considered important information, even if similar disclosures are already in the Listing Rules.

However, we believe the costs and benefits, together with the practicability, of this approach would be best answered by companies. Please also refer to our response to Q12 in respect of arguments for retaining roll-forward tables for share options and LTIP awards.

We note that there clearly are differences in what is required under the draft regulations and under the Listing Rules. For example, the disclosure in paragraph 14(a) of share ownership requirements is not required under the Listing Rules. Clearly, the analysis in paragraph 14 (b) would differ to that required under the Listing Rules (which might capture other financial instruments over shares). Information on conditional awards would usually be separately disclosed under the Listing Rules and existing Schedule 8 requirements for roll-forward of share options and LTIP interests.

We note also that the details required under paragraph 14(b) would be required for directors at any time in the financial year (but paragraph 14(b) does not specify the date at which interests are given, e.g. is it year end for all directors, even those not in position as at year end?). By contrast, LR 9.8.6R relates only to directors as at the year end. The Listing Rules also require disclosure of directors' interests at year end, together with changes to the directors' interests since the financial year end, or an appropriate nil statement.

We are not convinced that the definition in paragraph 35(3) of the draft regulations would be sufficient to require the directors' interests in share and share options reported under paragraph 14 of the draft regulations to include the interests of directors' connected persons (and bodies corporate controlled by directors). If paragraph 14 is retained, it is important that this is made clear.

We also note that there appear to be no requirements to give comparatives. While we note that the Listing Rules do not specify inclusion of comparative disclosures, many companies do give this information. We consider it would be appropriate for the disclosure, if retained, to include the interests at the beginning of the financial year, or the date of appointment of the director (if later). This is particularly important if the Government does not retain disclosures on roll-forwards of share options and scheme interests. See our response to Q12.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We do not believe that a graph which plots total shareholder return (TSR) against CEO pay would be a useful proxy for the relationship between pay and company performance.

As we have noted in our comments in response to question [6], pay outcomes in a reporting period are not always aligned to financial performance of the period. Executive remuneration is structured such that directors often receive incentive plan payments in respect of multiple performance years. This misalignment renders the comparison between CEO pay and total shareholder return somewhat meaningless. While other measures, such as total executive director pay or total board pay may be less volatile than CEO pay, this underlying concern would remain.

The example provided in the consultation document tracks TSR against executive pay over a 10-year period. However, this appears to disregard the following issues:

- Over the course of a 10-year period, it is inevitable that there would be CEO turnover. The pay packages of CEOs can significantly vary depending on business needs over time. In addition, the structure of boards and executive management committees (and the role and responsibility taken by the Chairman, e.g. some boards have an executive Chairman) can vary significantly across companies or indeed over time for the same company. Therefore, a comparison between CEO pay and performance across different companies would also be unlikely to be meaningful. We also note that there may be a burden in computing pay information for a 10 year period on the basis of the methodology set out in paragraph 3 of the draft regulations.

- TSR is influenced by wider organisational and external factors (e.g. merger and acquisition activity, sector-specific downturn etc). These issues may or may not be reflected in the CEO's pay package or alternatively there may be misalignment in terms of timeframe.

As the Government has noted, finding a suitable proxy to show the link between pay and performance is very difficult. However, taking into account the above issues, TSR is not a suitable proxy to illustrate the link in a meaningful way.

We do not believe there is a single metric that should be used to compare pay and company performance. We believe that package of disclosures proposed by the Government will increase transparency regarding the link between pay and company performance. However, this may be an area where best practice may evolve.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

The performance metrics should not be included in the audit. This is because these metrics might include non-financial information, which would vary significantly in scope, presentation and detail between companies. It would not be possible to apply the rigour and professional standards expected of a statutory audit to information such as this.

We do not believe there are any other sections of the remuneration report that should be subject to audit.

Appendix – other drafting points

Other issues concerning the drafting

In the comments below, italicised sections are potential drafting suggestions, except where the context is otherwise clear.

Paragraph 5

Qualifying services

In the draft regulations, 'in respect of qualifying services' is included in paragraph 5(a) for salary and fees, in the definitions in paragraph 7 for benefits reported in paragraph 5(b)(i), and not referred to at all in relation to paragraphs 5(b) (ii) and 5(c) to 5(e). This lack of consistency could lead to confusion as to what is required – particularly for directors serving only part of the financial year - and as to whether it has a different scope to the current requirements. We recommend that the definition of each category is reviewed to ensure it meets the intended requirements. We also recommend that these definitions are 'road-tested' by reference to common elements of remuneration.

We note that particular care will be needed when clarifying this point for each element of remuneration. For example, there are currently different scopes in relation to the share options and pension benefits included under paragraphs 1(b), (d) and 2(2) of Schedule 5 compared to paragraphs 8(4) and 13(2) of Schedule 8 to SI 2008/410.

One particular issue that gives rise to this different scope is that directors may have been granted options prior to becoming a director. Under the draft regulations, share options are defined as 'rights to acquire shares'. These would appear to be disclosable (in the period of grant if there are no performance conditions, or in the period when the performance conditions are met) under paragraph 5(e) if they are awards under 'schemes' (as defined in paragraph 7).

The awards would be disclosable under paragraph 5(d) if awarded in the reporting period subject to performance conditions relating to that period which were achieved. Share options granted in respect of the appointment of directors would also be included. However, directors may have share options granted originally while they were only employees (i.e. prior to board appointment), but subject to continuing service conditions which might continue while a director. It is not clear whether such awards would be excluded from the remuneration in paragraph 5(e)(ii) of the draft regulations or not.

Many defined benefit pensions are closed to future accrual, and so do not accrue further benefits relating to providing qualifying services. Such schemes are reportable under Schedule 8 (and the Listing Rules) provided *any* of the benefits accrued in relation to qualifying services, but not under paragraph 2(2) of Schedule 5.

We note that the additional information on pension schemes required in paragraph 10 of the draft regulations refers to 'rights under a pension scheme that is a defined benefit scheme in relation to the person and any of those rights are rights to which he has become entitled in respect of qualifying services of his' (i.e. the scope is consistent with paragraph 11(2) of Schedule 8). If this is the intention, we suggest paragraph 5(c) clarifies that it is 'all pension related benefits *relating to rights under a pension scheme that is a defined benefit scheme in relation to the person and any of those rights are rights to which he has become entitled in respect of qualifying services of his'*.

<u>Paragraph 5</u>

In the table in paragraph 4, the sums that are required to be set out *for the relevant financial year:*

(a)..... the total amount of salary and fees *paid to or receivable by the person* in respect of qualifying services.

(b) (i) *all benefits* (NB paragraph 6(b) already specifies these are measured at 'taxable value') (ii) A distinction is drawn between cash dividend received on shares and awards of additional 'dividend shares' as part of the scheme interest (usually subject to the same performance conditions as the original shares). However, it is not entirely clear how a cash dividend which is accrued on the shares in the relevant financial year but is only payable at the end of the scheme (if the service requirement is met) would be treated.

Would this be an award under (b)(ii) or (e)(ii) reported in the financial year? What if dividend shares were awarded in relation to the financial year and were either immediately vested or vested subject only to service conditions (or qualifying conditions which are not performance conditions). Would this be an award under (e)(ii) and would this be reported in the year that the dividend shares were conditionally awarded?

(c) ... all pension related benefits *relating to rights under a pension scheme that is a defined benefit scheme in relation to the person and any of those rights are rights to which he has become entitled in respect of qualifying services of his* - See comments relating to specifying which pension schemes are to be included under 'qualifying services' above.

(d) and (e) – See comments in response to Q7 above.

<u>Paragraph 6</u>

In our view, the measurement methods described in paragraph 6 are not clearly articulated.

Paragraph 36(1) states that 'amounts shown for any financial year are the sums receivable in that year (whenever paid) or in the case of sums not receivable in respect of that year, the sums paid during that year'. This is a key principle underlying disclosures under existing Schedule 8. However, the disclosure requirements in paragraph 5 appear to require early reporting of amounts before they become 'receivable' (e.g. before completion of remaining service conditions). In addition, the measurement methods described in paragraph 6 sometimes refer to 'paid to or receivable', and paragraph 7(1)(b) refers to 'received'. Paragraph 5(d) and (e) (and related requirements in paragraph 6) refer to 'awarded'. There is potential for inconsistency and confusion.

Clearly, if the intention is that amounts are considered reportable once performance (rather than service) conditions have been met, this will need to be made clear in the definitions used (as this would differ from the current Schedule 8 requirements which would report a 3 year LTIP with only a service condition as amounts received or receivable under LTIPs only once the service period was completed).

We set out detailed comments on each element of remuneration disclosed under paragraph 5 below.

(a) - Not clear why this refers only to cash – in principle, salary could be paid in other forms, e.g. shares

(b) - Reference to 'taxable value' may be applicable to the measurement of items in (b) (i). It is unclear why 'taxable value' is the appropriate measurement method for items in (b) (ii).

(d) - It is common for deferred annual performance awards to be given in the form of shares as well as cash. Therefore, this needs to specify how the cash equivalent is measured, e.g. at what date is the cash equivalent determined (and clarify that there is no discounting, if this is the intention).

(e)(i) As awards under schemes could be reported while still subject to service conditions, it may be relevant to explain that this should be computed as an undiscounted amount (if this is the intention).

While (e)(i) refers to a monetary award, some awards payable in shares are shares to a given value (which may be determined by performance conditions), based on the market price at a given date. It is unclear how the value to be included in respect of such awards are to be determined as the methodology in (e)(ii) and (iii) is more suited to a share award where the number of shares is fixed once the performance conditions are met.

(e) (ii) and (iii) - It is necessary to explain how and when a best estimate is arrived at in terms of the number of shares (as well as the market values to be used).

(e)(ii)(XY) - Should this refer to 'the amount of accrued dividend received in the *form of additional shares or share options?*

(e)(ii) and (iii) - The term 'vesting' needs to be clarified as it appears that (e) will include awards subject to remaining qualifying conditions which are not performance conditions and therefore have not actually vested.

(e)(iv) - Instead of referring to 'the cash amounts the individual was required to pay to purchase the share', why does this not refer to using 'amount' as defined in paragraph 33 of the draft regulations and applying that to the number of share options arrived at in (XY)? It would make more sense if (e)(iv) was integrated into (e)(ii)(XYZ).

Paragraph 7

Paragraph 34(1) includes an important paragraph (currently in paragraph 18(1) of existing Schedule 8) in respect of emoluments and share options granted in respect of a person accepting office. The wording of this paragraph needs to be reviewed, in conjunction with the new requirements of paragraph 5 so that it is clear that paragraph 5 will capture all awards made in respect of accepting office.

Paragraph 7(1)(b) – Is the reference to 'other than salary' correct – as there are many other benefits which are emoluments but which are not salary? This refers to the definition of emoluments (see separate comments) which may not be well aligned with the items now disclosed in the single remuneration figure under paragraph 5.

Paragraph 7(3) – We consider that 'scheme interest' should also be defined.

Paragraph 7(5) – This should read for the purposes of paragraph *7(4)*.....

Paragraph 8

(1) – This refers to 'the relevant details (see sub-paragraph (2)) of any award that has become receivable in respect of the interest'. It is not clear what 'receivable' means and when it occurs – as items are reportable under paragraphs 5(d) or 5(e) once performance conditions (but not service conditions) have been met.

(1) and (2) - It is unclear what 'interest' (or 'scheme interest' in paragraph 8(2) means (as it is not defined).

(2) -The reference to 'shares' is too narrow (as a 'scheme' as defined in paragraph 7(3) could include share options, shares, money or other assets).

(2)(b) - It is important to clarify at what date the 'value of the award achievable' is measured.

(2)(b) and (c) - The draft regulations are unclear whether this level of detail is required for personal performance objectives as well as company/group performance objectives. Reference to 'how the *company* performed' in paragraph 8(2)(c) is also likely to be inadequate – since objectives could well refer to the company, the group as a whole, particular undertakings within the group or even divisions or product lines. Therefore, a better description to capture what is required should be included.

Paragraph 10

Paragraph 10(3) – The total value of any additional benefit *under a pension scheme falling under (2)* that will become receivable to a director in the event that the director retires early...

Paragraph 10(4) – Where a person has rights under more than one type of benefit identified in column "c" of the table in paragraph 4, *each type of pension benefit* and the relative weighting of each type of benefit.

Paragraph 11

The definition of 'benefit' in paragraph 7 is specifically in respect of the disclosures in paragraph 5(b), i.e. the benefits element of the single remuneration figure. Paragraph 33(2) which addresses compensation for loss of office refers to 'benefits otherwise than in cash' and states these are included at 'the estimated money value of the benefit'. However, use of the term 'benefits' may confuse.

See also comments in response to Q1. There is scope for more guidance on how compensation for loss of office should be computed.

Paragraph 12

Paragraph 12(b) refers to 'scheme interest' and paragraph 12(b) (v) refers to 'threshold performance', neither of which have been defined. The current definition of 'scheme interest' in paragraph 11(4) of Schedule 8 is that 'in relation to a person, means an interest under a long-term incentive scheme that is an interest in respect of which assets may become receivable under the scheme in respect of qualifying services of the person' . While this definition could be adapted for inclusion in the draft regulations, it would need to make clear that the reference to 'assets' includes share options (which it does not under the existing Schedule 8, as these are separately reported).

In addition, in paragraph 12(b)(v), the reference to 'if not set out elsewhere in the report' should be deleted, as the Policy Part may not be prepared each year (and so may not be available in the same document) and it may add confusion as to what is auditable or not.

See our comments in response to Q12.

Paragraph 13

See our comments in response to Q14.

Paragraph 14

See our comments in response to Q15.

Paragraph 16

Paragraph 16(c) - It is important to define 'substantial shareholder votes against the resolution' as this could be interpreted differently by different companies. We note that the FRC (see PN 364) intends to consult on 'whether companies should engage with shareholders and report to the market in the event that they fail to obtain at least a substantial majority in support of a resolution on remuneration'. It would be appropriate for any definition to be consistent with any changes made to the FRC UK Corporate Governance Code, although it is expected that changes to the latter would have a later implementation date.

Paragraph 19

Paragraph 19(a) - This should explain when information is given for the group, i.e. presumably where the company is a parent company (consistent with paragraph 30).

Paragraph 20

Paragraph 20(b) should state 'explain why any *qualifying conditions which* are performance conditions were chosen'.

Paragraphs 21 and 22 and 24

See our comments in response to Q4.

Paragraph 26

See our comments in response to Q5.

Paragraph 30

For the reasons also set out in our responses to Q4 and Q14, we are concerned that disclosure of the percentage increase in CEO pay compared to employees pay generally, will not provide meaningful information for the company or for comparisons with other quoted companies. Over a single year, a CEO's pay may diverge from total employee pay for reasons not necessarily representing of a longer period (e.g. a new appointment, payout on a multi-year long term incentive scheme).

We also note that the computation of pay is not defined in paragraph 30. In addition, the ability for companies to determine an appropriate comparator group (albeit disclosing reasons) could give very different comparisons, depending on the group chosen. We note that there would be additional costs in obtaining the relevant information for this disclosure. If it is done on a basis comparable with paragraph 5, it may be difficult to obtain particularly employee data on that basis.

Paragraph 30(2) should state 'Where the company is a parent company, the statement shall refer to *the employees of* the group and not the company.

<u>Interpretation and supplementary in Part 6</u>

<u>Paragraph 33</u>

There appear to be redundant definitions in paragraph 33. These currently include the definition of 'amount' for a gain on exercise of a share option (but see our comments on paragraph 6(e) above) and 'company contributions' in relation to pension schemes. In many cases, these definitions do not fit well with the concept of a single remuneration figure and the measurement methods in paragraph 6.

The definition of 'emoluments' is only referred to in paragraph 7(b) and 34(1) of the draft regulations. In addition, paragraph (b) of the definition of emoluments also makes no sense. It will be important to ensure the definition makes sense and is appropriately integrated in the context of the draft regulations. See above comments on these paragraphs.

<u>Paragraph 35</u>

Under the amendments made to sections 226E of the Companies Act 2006 in the Enterprise and Regulatory Reform Bill, amounts paid which are in contravention of the approved policy (subject to transitional rules) are held by the director on trust. The interaction of this requirement and paragraph 35(2) could give rise to a lack of clarity as to what is reported as remuneration. It is important that the directors' remuneration report discloses what directors have received as remuneration (even if not in accordance with the remuneration policy). This is quite different from not disclosing as remuneration, say, a season ticket loan repayable by the director.

<u>Paragraph 36(1)</u> – See comments in our response to Q7 above.

<u>Paragraph 36(2)</u> - It would be helpful if paragraph 36(2) could clarify in which categories amounts previously not reported because they were liable to be accounted for to the company etc. or taxable benefits which become chargeable to UK tax, should be reported (and separately distinguished) or whether these are intended to be disclosed as a footnote rather than included within the single remuneration figure for the year.

Experian plc

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
✓	**Quoted company**
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

No comment – we believe that it is more appropriate for legal firms who are being included in the consultation to feed back on the draft regulations.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

While much of the information required by the revised regulations is already reported on, reconfiguring the remuneration report so that it complies with the new legislation will inevitably incur costs; both in the form of time from internal company resources and fees from external advisers (e.g. lawyers, remuneration consultants and auditors). There will also be increased costs of holding shareholder meetings if and where seeking additional approval from shareholders is required.

However, whilst we appreciate that the initial transition costs may be high these should then reduce in future years. We would note, however, that the on-going audit costs will likely be higher as the auditors will be required to sign-off on more / more complex information than they currently do.

We would also point out that the increased complexities of these proposals increase the costs and complexity of doing business in the UK and are at odds with the Government's aim of simplification and reduction of red-tape and costs.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

The information required in the proposed table is largely contained in our current Remuneration Report. Therefore this should not be onerous to produce. We welcome the non-prescriptive nature of the disclosure as this will give flexibility to companies to provide information to shareholders in a way which is appropriate for their own remuneration structures, and should prove informative for users of the report.

However, it is to be expected that, initially at least, the level of detail disclosed will vary by company and shareholders will have a role to play in helping shape best practice in this area.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

While much of the information proposed by the revised regulations is already available in our annual report and accounts, the new proposed format will make this information more readily available to users of the accounts.

However, in terms of the reporting requirements for service contracts, this will increase the length of the Remuneration Report and in any event, the provisions may require much lengthier disclosure to put them into context. We believe that the current level of disclosure is sufficient and that a link to a Company website giving access to the full provisions would provide the necessary transparency and practicality.

In addition it is questionable how much value the proposed disclosure of change in profit, dividends and expenditure on pay will add. It is difficult to see how this will help shareholders to understand the link between pay and performance as overall pay spend may vary for reasons not linked to performance (e.g. could reduce if a significant area is outsourced). We would question whether this disclosure would be better placed in the implementation report as it is a statement of fact about the reporting period, rather than a statement of policy.

The most onerous disclosure to comply with is the one regarding remuneration under various performance scenarios. Our concern with this proposal is that there will not be any consistency in the assumptions made by companies when preparing this disclosure. As significant elements of directors' pay are delivered in shares, the value realised is highly dependent on movements in share price. Differing assumptions on share price growth under the various performance scenarios would have a marked impact on the amounts disclosed. This would make comparisons between companies (which will inevitably be done by shareholders, other users of the accounts and the media) meaningless and therefore not informative. A similar situation would arise if expected value methodologies were used to value the share based elements of the package.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

There is no further information we would suggest including, but would note that companies need to be allowed a high degree of flexibility in their exit policies to deal with the wide variety of circumstances under which a director may leave a business.

We would also note that companies will need the flexibility to honour the terms and conditions of existing service contracts which may conflict with best practice.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

It is difficult to see how such a disclosure would be helpful to users of the remuneration report. We note that the Government does not believe that companies should have a statutory requirement to consult their employees on pay issues but our concern is that the proposal will have the same effect as, if a company states that it does not seek the views of its employees, this could be perceived negatively (e.g. by shareholders or the media). However we struggle to see the value, or appropriateness, in canvassing employee views on executive remuneration. We have c 17,000 located in over 40 countries so the cost of consulting all of them would be significant and it is difficult to see what useful insights a Remuneration Committee could gain from an employee survey on Directors' pay.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Yes, we believe the proposed methodology would achieve this with the exception of awards granted without performance conditions which have to be recognised in full in the year of grant. We believe that it would be more appropriate for these to be recognised at the time of vesting in line with other long-term awards.

However, given the current level of disclosure in our Remuneration Report, we do not believe the extra disclosure is necessary.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

If the Government believes that this is a necessary requirement then this approach is simple, consistent across companies and is therefore practical to adopt.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

If the Government believes that the single figure is a necessary requirement then we would agree that any claw-back applied should form part of the single figure and this is a practical way for claw-back to be disclosed.

Where there is a commercial sensitivity surrounding the use of claw-back we would think it appropriate that companies be excused from disclosing those sensitivities (clearly companies would state that they had withheld information on this basis to avoid abuse).

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Annual bonus targets are likely to be more commercially sensitive than those applying to long-term incentives. It is our view that companies should retain the right to not specifically disclose performance against these targets.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We agree that the proposed disclosures on pensions will provide sufficient information although it would be helpful to companies if these requirements were aligned with those of the UK Listing Rules.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We agree that this approach is practical to comply with and is informative for users. This will provide a consistent approach across companies which would not be the case if, for example, expected values were used.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

The simplification of reporting of directors' interests is welcomed. As this is a simplified reporting arrangement we do not believe there will be additional costs involved (other than those incurred in initially transitioning to the new format as mentioned in Question 2).

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

While we understand the desire to illustrate a link between pay and performance we do not believe that a graph such as the one proposed will achieve this especially without a considerable amount of explanation.

There are often time lags between performance and the payments made as a result and total shareholder return does not always reflect company performance – TSR is obviously influenced by external factors outside of the company's control and may, for example, fall significantly even if the company's profit growth has been strong.

We also have concerns about the inconsistency that would arise, and so the amount of explanation required, in including pay of a number of chief executives over the proposed 10 year period. A shorter time period would be preferable and more relevant.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

This proposal is likely to increase the audit fees for UK businesses which is at odds with the Government's aim of reducing costs and simplifying the UK business environment.

We don't believe that any further sections of the report should be subject to audit.

GC100 Group, The

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
London
SW1H 0ET

26 September 2012

By e-mail to executive.pay@bis.gsi.gov.uk
Cc: Richard Carter and Gemma Peck, BIS

Dear Mr Walker

Consultation on Revised Remuneration Reporting Regulations

The GC100 welcomes the opportunity to respond to the recent consultation paper issued by the Department of Business Innovation and Skills on revised reporting regulations in relation to directors' pay. The GC100 is the association for the general counsel and company secretaries of companies in the UK FTSE 100. There are currently over 120 members of the group, representing some 80 companies. Please note, as a matter of formality, that the views expressed in this letter do not necessarily reflect those of each and every individual member of the GC100 or their employing companies.

As you are aware, over the past few months, we have been in discussion with Richard Carter and colleagues reviewing the practicalities of implementing some of the proposals set out in the consultation paper. We do not propose to reiterate all the points we have discussed, as we believe that they have been well understood. We remain willing to continue work constructively with BIS in these matters.

General Points

Before reviewing the specific questions in the consultation paper, we have the following general comments to make:

- We believe that the revised remuneration reporting regulations as now proposed are, by and large, workable for companies. They are a practical alternative to some of the earlier recommendations and we welcome the aim to cut down on some of the detail, and focus on more concise and comprehensible reports on remuneration.

- The implementation of the proposals needs to be seen in the light of the fact that many of the UK-listed companies that will be subject to them are international or global in nature. Their executive directors will typically be employed on service contracts in other jurisdictions where employment practices differ. In some cases, particularly the provision of pension benefits by the employer, the regulations as proposed will lead to some anomalous disclosures and make meaningful comparisons difficult and therefore subject to misinterpretation. (See response to question 8).

- We have previously expressed a concern that shareholders should not be put in a position of micromanaging the companies in which they own shares. Equally, boards need to be able to rely on the trust placed in them by shareholders. That relationship of trust also imposes upon shareholders a duty to take their responsibilities towards the company in which they invest seriously and to engage constructively with boards in order to help sustain a focus on long term value creation. This is in part being addressed by the Stewardship Code; but we believe that the introduction of these regulations and the continued focus on the need for transparency in company's affairs places an even greater burden on shareholders. Accordingly and for this purpose, we would emphasise that the determination and assessment of performance by executives against commercial and financial targets is a matter that is best left to the members of the remuneration committee.

- We would recommend that greater clarity is provided on the information to be provided in the annual report and accounts. We understand that this is being addressed in the ongoing review of narrative reporting but would highlight that this draft legislation includes or excludes information which is currently required by the UK Corporate Governance Code, the FSA's Listing Rules and IFRS reporting requirements.

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

- Whilst we feel the draft regulations do give effect to the policy set out in the consultation document, we believe additional clarification is required to support the framework within which companies can agree and implement their own remuneration policy. We would therefore support BIS's call for guidance to be developed by companies and shareholders in this area and as you aware, the GC100 is working with a group of major investors to develop such guidance for consideration by BIS.

- Overall, the draft regulations appear to meet the Government's objective of creating a two-part remuneration report. There are some points to consider on the draft regulations as follows:

    - In the comparison of overall performance and pay provisions (paragraph 13), it is not clear if the ten year "relevant period" period starts when the new requirements come into force or whether this is a backward-looking disclosure over the last ten years. As set out in our response to question 14, we see little value in tracking these measures retrospectively.

    - Paragraph 14 on directors' shareholdings includes the total number of shares and share options of which the director is the legal (beneficial) owner. Whilst simpler and more concise reporting is to be welcomed, it may be appropriate to include some further information under these provisions to assist shareholders' understanding of these disclosures, for example, including option prices and vesting dates for share awards where appropriate.

    - In relation to the resolutions to approve the policy and implementation report,

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paragraph 16 requires disclosure, in respect of the votes cast, of the number of votes for, against and abstentions. We are concerned that the legislation is requiring disclosure of an 'abstention' which is not a vote in law and may further blur the distinction between an actual vote – whether for or against a particular resolution - and a shareholder's decision not to vote for various reasons. If the intention is that such disclosure is required, we would suggest that the legislation should follow the wording of the UK Corporate Governance Code and refer to 'votes withheld' and make it clear that such votes are not a vote in law.

- Part 4 (para 24), includes the 'Relative importance of spend on pay'. This relates to the percentage change in profit, dividends and overall expenditure on pay in the reporting period compared to previous years. This is currently included in the forward-looking Policy Report and shareholders may only see this information once every three years. Would this disclosure not sit better as part of the Implementation Report requirements?

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Adjusting to these new reporting regulations will place a significant burden on business. We anticipate that the costs associated with these proposed changes will be very high for corporates, particularly 2013 to 2015 as we get up to speed with the new requirements. The first votes on remuneration policy will be in 2014, with implementation reports against that policy in 2015 although some companies may seek to report against the new requirements earlier. This effectively means a three year transition period. Typically, there will be a number of people in our company secretarial, human resources and communications teams who will be involved in drafting the Policy Report for submission to shareholders and, thereafter, the Implementation Report regarding that policy.

We conservatively estimate that collectively each company will need at least 100 man hours to absorb and implement the changes. In addition, we believe that remuneration committees will need to take further advice from remuneration advisers, lawyers and auditors over and above existing requirements. Additional or lengthened remuneration committee meetings and briefings are likely to be required to ensure that boards and remuneration committee members fully understand the new requirements. We also anticipate that there will be a requirement for greater engagement with shareholders not only ahead of the Annual General Meeting but throughout the year in order to educate and help shareholders understand the new approach to determining and disclosing executive remuneration. This will inevitably take up more management time and incur travel and associated costs for remuneration committee members.

As a very rough estimate, we would estimate that transition to the new regulations could cost each FTSE100 between £100,000 and £250,000 in management time and additional advice, although some companies within the GC100 are already estimating significantly higher costs. As well as the costs of adjusting to the revised reporting regulations, there will be increased on-going costs, particularly for those companies where the vote on either the Policy Report or the Implementation Report has failed. Considerable management time and external advice will needed in analysing the vote and ascertaining which shareholders voted against and then engaging with those shareholders to understand which aspects of the report they did not support and then preparing and publishing an

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explanatory statement.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We support the introduction of the remuneration table. It is a practice that is already being followed by many companies. We would strongly support the joint development of guidance and, as BIS is already aware, we are currently working with major investors to develop such guidance for consideration by BIS. We would however emphasise that such guidance should be seen as such, so long as it is apparent from the table how each element supports the achievement of the company's strategy, the potential value and the performance metrics associated with remuneration packages. We recommend that the guidance that is issued makes it apparent that it should be for companies to construct their tables in a way they think fit and explain why that is appropriate for their particular circumstances. The final form of the proposals should, in our view, embrace this principle.

Whilst we agree that the use of the table within the Policy Report is likely to succeed in providing an easy at-a-glance summary of the key elements of remuneration, our expectation is that the explanations of each element and the rationale for selecting particular performance measures will result in reports that are just as lengthy as at present.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We recognise that the proposed reporting requirements using different scenarios to show how much remuneration directors would receive might be regarded as logical in providing useful information for investors. However, we are not convinced that this really is the case. Detailed scenarios will involve a lot more work for companies in disclosing potential outcomes for awards made under many plans and could be regarded as additional clutter, when the aim is for more concise reports. Showing three scenarios for a good, bad and average year is too simplistic as it is unlikely that all performance measures governing various different plans and arrangements will all move in the same direction at the same time. The proposals assume all companies identify a threshold level of performance which may not always be the case. We are currently working with major investors to develop guidelines for useful yet concise disclosures.

We also recognise that portraying this diagrammatically in a chart could be useful. We do however have some reservations about the chart given on page 18 of the consultation paper. In particular, we note that whatever the performance, the salary would remain the same and it would be the variable elements of pay that would go up or down depending on performance. In a successful year, the base salary would form a smaller proportion of the whole and bonuses and LTIPs would be higher. The different elements of variable pay are likely to be driven off different measures and therefore their relative percentages are also likely to change in different scenarios.

We appreciate the desire to view remuneration within the broader context. However, the

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proposed use of the same comparability measures (profits and dividends) will not be appropriate for all companies across all sectors. Shareholders invest in different companies and in different sectors for differing reasons. Some investors look for share price growth, whilst others will look for dividend yield. Requiring all companies to disclose the same measures appears to enable comparison across companies but will not in fact be comparing like with like. Importantly, setting out overall spend on pay in a reporting period relative to the percentage change in profit and dividends is of questionable benefit for investors and is more likely than not to feed misinformation amongst less informed investors, media and other commentators.

Further, an unintended consequence of requiring reporting of percentage change in profit and dividends alongside overall spend on pay would be to “reward” (from a disclosure perspective) companies that cut the workforce as a way of increasing profitability. An alternative would be for companies to be provided with the flexibility to determine their own reporting methodology for this purpose, e.g., the use of share price growth, dividends, profits, earnings per share etc and therefore permitting companies to uses two or three of the measures which are most appropriate to their particular circumstances. This allows sectoral differences over longer time periods to be more fairly reflected when comparing performance against total spend on pay. In addition, we do not believe that it is appropriate that such disclosure is made in the policy part of the remuneration report.

Question 5: The Government proposes that a company’s statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

The proposal in the proposed regulations that a description of the exit payments payable under different scenarios be included as part of the Policy Report, is far more practical and workable than some of the earlier proposals requiring a shareholder vote at the time of a termination. We do however see this as an area which could well lead to fairly extensive disclosure by companies. Caution is required if we are to cut the clutter. In line with the guidance that we proposed to develop with the investment community for this purpose, we would expect the policy on exit payments to be drafted broadly in order to retain the remuneration committee’s ability to exercise their discretion. This is probably another example of where companies and investors should develop some joint guidance to determine the type of information that would be useful for investors but will not lead to excessively lengthy or complex disclosures.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We note that the current proposals relating to employees’ views on remuneration are more practical than some of the earlier proposals which would have been unworkable, particularly for very large companies with an international workforce. However, we still feel that ascertaining employee views on executive director remuneration will be a practical challenge and of questionable benefit, i.e. what is the advantage and for which set of stakeholders of a statement to the effect that employee views on the remuneration policy have been solicited? Many large companies conduct employee surveys on a regular basis, and could include an additional question on director remuneration. It is however hard to think how such a question could be framed so as to elicit meaningful responses, particularly in large, internationally diverse organisations, where the link between worker

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and director may be remote and global remuneration practices may vary considerably. We would also note that not all companies conduct employee surveys and this will be an additional regulatory burden for them.

We also have some concerns that asking employees about their views on executive remuneration raises expectations that employees might play a more significant role in influencing executive pay than would be the case.

We would expect that this provision would be on a "comply or explain" basis and that companies should be free to explain, where applicable, if it is impractical to ascertain employee views on remuneration.

In terms of the related disclosure on the percentage increase in pay of the workforce against the percentage increase in pay of the CEO, it is not clear from the draft regulations whether this relates to salary or total pay for the CEO. The structure of total pay for a CEO will typically have a much larger variable element that will only be earned dependent on performance, making comparison with the wider workforce more difficult. Further given the cultural and geographic spread of the employee base of many international companies, any comparison between the pay of the CEO with the earnings of the organisation's workforce would not be practical or relevant.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

We believe that the description in the table relating to the single figure accurately defines the governments' intention that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The HMRC methodology is somewhat "crude" and may not cater for the many international companies that employ executive directors in different countries, often with local pension arrangements which can vary from country to country. The HMRC methodology may well not be appropriate in these circumstances and may give an anomalous figure. A more refined approach may be to adopt the transfer value of the increase in accrued benefit, given that there is a range of different retirement ages and benefit structures.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We are not sure exactly how this is proposed to work and suspect that the inclusion of a figure for claw-back in the single figure could lead to double-counting in certain circumstances. It will depend on exactly how claw-back is applied by the reporting company and companies may well adopt different practices when applying claw back. Whilst recognising the importance of transparency regarding claw-back, we do not believe

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that it should form part of the single figure and would suggest that it be subject to a separate disclosure. Companies' remuneration committees are best placed to review the application of claw-back provisions on a case by case basis. This will necessarily require these committees to have the discretion to determine what is appropriate in particular circumstances and, if considered appropriate in material situations, to discuss this with key shareholders.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We are very concerned that full disclosure of performance against metrics brings with it a very real risk of disclosure of commercially-sensitive information and possible price sensitive information being mandated. It is our view that the detail in paragraph 77 of the consultation document goes far beyond what most companies would be comfortable to release into the public domain, particularly in relation to annual plans. Whilst companies are willing to disclose at a high level the performance conditions and their relative importance, disclosure of the precise target for each performance condition is understandably commercially sensitive, particularly if the target was set at the beginning of a year and may well be one stage within a longer term plan.

We would point out that the numbers within the remuneration report are audited and presume that this will continue to be the case under the new reporting requirements for the Policy Report and the Implementation Report. The audit is independent confirmation that the amounts paid out or the number of awards vested is in accordance with the performance targets.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

Subject to the caveat that the disclosure requirement would be projection of pension entitlement, the proposals appear satisfactory.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We would advocate an approach that includes disclosure both at face value and on an expected value basis. The face value alone may lead to misleading disclosure, namely remuneration levels that will only rarely materialise in practice.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We welcome simplification of disclosure in this area. However, we question whether the disclosure of directors' total shareholdings is of value, given that these details have already been disclosed to the market through RNS announcements as shares are bought and sold or awards and options are granted and exercised. We would also point out that it is often the case that these details in the remuneration report are out of date by the time the report is printed, as awards are often made shortly after sign-off, and awards made in previous

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years vest at this time.

We would suggest that there should be a requirement to maintain and update this information on corporate websites, so that shareholders are able to review the most up to date figures rather than using out of date figures form the annual report. We would not suggest replicating the full Register of Directors' Interests as this can be very complex, particularly where numerous current and former share plans are involved, with many vesting or lapsing points. We would therefore suggest that the total number of shares held and awards or options outstanding could be sufficient.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

It is difficult to find the perfect measure for comparison purposes between director pay and company performance and no single measure will please everyone. TSR is, in our members' views, as good as any other measure and, importantly, it provides a clear, simple and transparent reference point for relative as opposed to absolute performance.

We understand the rationale for tracking pay against performance going forward. However, we see little value in tracking these measures retrospectively. A graph showing performance in the past 10 years, when there were different CEOs, board, chairmen, members of the remuneration committee policies and strategies does not sit naturally either with a policy looking forward to remuneration in the years to come or with a policy describing how remuneration policy was implemented in the past 12 months. It does not seem right that a decision taken by a former remuneration committee relating to a former CEO say in year two should be subject to a shareholder vote eight years later.

Rather than solely focussing on TSR, allowing companies some degree of additional flexibility, for example comparing performance against CEO pay based on the company's strategic measures or the CEO's objectives for that period, may provide a more meaningful comparison.

We also note that this graph will throw up some anomalies in cases (the majority) where there have been a number of CEOs in the period, particularly where a new CEO may well have share awards in the early years that do not vest until later. There is also a concern that a very good CEO may come into their own when market conditions are difficult. A CEO comparator matrix may therefore give a misleading impression that the CEO is being "rewarded for failure".

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We believe that these items detailed in paragraph 97 of the consultation paper and reflected in paragraph 32 of the draft regulations attached in Annex B are the appropriate items to be audited. The audit of these figures will give shareholders added assurance in cases where detailed disclosures cannot be given due to commercial sensitivities.

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We would welcome the opportunity to discuss these points with BIS in greater detail.

Yours sincerely,

Grant Dawson
Group General Counsel and Company Secretary, Centrica plc
Chairman of the GC100
For and on behalf of the GC100

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Gerrit Aronson

Response to:

Directors' Pay: consultation on revised reporting regulations.

NOTE: The views expressed are the personal perspectives of Gerrit Aronson and do not necessarily reflect those of the organisations that have engaged him.
September 2012

Please return completed forms to:

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About You	
Name: **Gerrit Aronson**	**Organisation:** **Independent Advisor to Boards**
Email: [redacted]	**Address:**

I am responding on behalf of myself	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Lawyer or accountant
Independent Advisor to BP, Electrolux and Autoliv Remuneration Committees	**Other (e.g. consultant or private individual)**

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Generally speaking the draft regulations do a good job of giving effect to the policy and also eliminate some of the ‘clutter’ of existing DRR regulations.

A number of the sections are particularly positive in terms of relevancy, clarity and encouraging the right kind and level of engagement with shareholders. These include the pay policy table, exit payments, the single figure table, and the definitions that have been provided for these (with a few minor modifications as explained later)

There are a few elements of the draft regulations that are however irrelevant to dangerous and should be changed or eliminated. These include the detail requirements for sections on comparison of overall company performance and pay, relative importance of the spend on pay, provision of advice, and employee context. These sections are counterproductive to the spirit and intent of the policy.

Finally there is some confusion that arises because the policy applies to ‘All Directors’. It is clear that the prime focus is on Executive Directors but the required inclusion of Non-Executive Directors to be equally represented is somewhat cumbersome. This is not insurmountable but it probably means reports will be longer than useful because of the need to give added explanation to the largely uncontroversial Non Executive pay policy.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Clearly there will be added costs including staff costs to prepare and adapt the new reporting requirements as well as significant audit and legal costs. But while not immaterial in an absolute sense, these costs are manageable for the FTSE 100 size of companies. Smaller companies will feel the cost impact more.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

Yes, both practical and informative. A policy table is a positive change, requiring companies to summarize key points of policy in a way that investors can understand. Definitions as set out make sense for ‘operation’, ‘opportunity’ and ‘performance metrics’ for each element of pay. Only change suggested is to leave off ‘purpose’. This will add little value (it should be rather obvious), will be largely motherhood (eg ‘support long-term shareholder value creation’ etc), and take up valuable space that can better be used for the other explanations.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Principle of setting out what remuneration directors can receive in different scenarios is a good one but some minor modifications on detail may be appropriate. Max scenario is clear and what everyone wants to know. ‘Threshold’ will be interpreted differently and so potentially misleading. A better definition may be ‘meeting plan’. Similarly ‘Below Target’ is ambiguous (how much below?). A better definition may be ‘Minimum’ that reflects what is guaranteed.

The relative importance of spend on top exec pay versus dividends and profits is irrelevant, misleading and dangerous. Short-term changes in profit are unlikely to correlate appropriately with top exec pay. Business cycles and circumstances vary greatly; economic cycles have differential impact on profits. As an example short-term oil company profits are driven more by oil price than by executive performance. If oil price increased significantly, resulting in a large rise in profits, it does not follow that that should justify a large increase in pay. Trying to provide a formulaic link between the two risks perverse incentives for Remuneration Committees.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

A sound concept. It is appropriate to set out what remuneration directors can receive on departing, but methodology, as set out is probably a distraction. Three scenarios are too complex and the maximum is really all people care about. Principles are however very important as there are almost always legitimate individual circumstances that arise with top exec departures. These need to be explained and justified against some pre-established principles.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

It is legitimate for a Remuneration Committee to have to comment on how increases and conditions throughout the company were considered in arriving at pay decisions for top execs. But the detail requirements suggested are an intrusion on proper governance and potentially destabilising to companies. Requiring publication of percent increases for groups or suggesting some sort of employee surveying on the topic is confusing and open to manipulation by companies if required to comply. For example for a global company of 100,000 employees, whom do you compare to, who gets surveyed? Publication of some information (eg salary increases for some employee groups) could be harmful to employee relations. It is all easily manipulated in order to look good while missing the real point.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Very well. Good definitions and methodology for clarifying what execs actually received (with exception of pension number – see below) Very helpful for investors to get the total picture and the bottom line.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

Any methodology for pensions value has pros and cons – important thing is to define one that everyone uses.

HMRC methodology works fine, in this regard, for UK plans but major issues with DB pension plans outside the UK that have significantly lower value (eg not inflation proof, no survivor benefits etc). Alternative may be to use the HMRC methodology for UK based schemes but an 'equivalent' for foreign schemes (justified by actuarial/audit support)

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Should be OK – if it was counted in earlier disclosures then in principle it is appropriate to deduct it if 'clawed back'. Only risk is double counting or subtracting.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Concept is good – companies should explain how performance against metrics justifies pay awarded. But trying to make this process formulaic is dangerous and counterproductive.

First, the commercially sensitive issue will lead companies to avoid meaningful metrics because of reporting requirements.

Second, judgement is an important part of Remuneration Committee assessment and should not be micro managed by putting too much emphasis on formulas that may or may not show well externally.

Finally investors form their own views of performance, irrespective of the metrics the company sets and have their own (and often different) compasses against which to judge arguments from Remuneration Committees.

Absolutely, companies should explain - but the dialogue is what's important and they should be left to explain the way they think is best.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

.Should do a good job of it.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Max is OK and what investors want to know. Threshold level is misleading and open to interpretation – just adds clutter with little added value. Better information to add would be the history of payouts under the respective plans – ie what % actually vested for say each of the last 5 years.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

Important thing is consistent definitions and no duplication. Current 'Directors Interests' requirement seems broader to include family members, trusts etc. Also would be good if US reporting requirements were aligned with UK ones for this purpose.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

Sounds very rational but, as with current TSR graph requirement, is largely meaningless. TSR and CEO performance do not correlate in a meaningful way. Business cycles, CEO tenure, unexpected problems or windfalls etc mean most comparisons will be irrelevant or misleading. More importantly, investors have much better, more rigorous ways of assessing performance and judging the appropriateness of pay in the company's circumstances. Perversely, such a requirement could even provide an incentive for companies to overpay when short term TSR graph looks good.

The section on advisor disclosure is equally erroneous. It is a good idea to require Remuneration Committees to explain their level of independence and how they manage that. But to use amount of advisor fees as a proxy for independence is misleading and dangerous. It is irrelevant to real independence (what is the right level that should be paid? Is more better?). It will be counterproductive to the intent.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

Good idea but costly for companies – audit companies are probably delighted and their partners pay will get a good boost. Shame the comparisons the government makes do not seem to include partner pay at audit companies, law firms, investment banks.

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Executive Pay Discussion Paper
Business Environment
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28 November 2011

Dear Sirs

We welcome the opportunity to comment on the BIS discussion paper on Executive Remuneration. GKN's views are as follows:

Introduction

We wholeheartedly agree with the Government's desire for the UK to be a magnet for attracting and retaining the best talent, and to create a business culture that promotes sustainable growth and rewards long term success.

However, we do not believe that the way to measure the success or otherwise of UK plc remuneration policies is to apply a read across from the median CEO pay to the performance of the FTSE 100 index. With certain exceptions, CEOs invested tremendous efforts in steering their companies through the turbulent market conditions of the last few years. At the same time many CEOs voluntarily took significant reductions in remuneration. Without this level of performance and commitment many more companies would have ceased operations resulting in thousands more job losses. Despite their efforts, and due to external factors beyond their control, the FTSE 100 index fell considerably. To use this backdrop as a basis to explain a dysfunctional market in executive pay is in our view far too simplistic.

The focus should be on ensuring, in the light of all factors, that directors' remuneration is not excessive, is clearly aligned to the company's strategic objectives and rewards performance which may, dependent upon the circumstances, be excellent financial results or, at the other end of the spectrum, survival. Generally, this means encouraging companies to adopt remuneration schemes with a strong element linked to longer term performance – more than the three years that typifies many schemes today.

Improving transparency

We note the proposals on narrative reporting contained within the separate consultation paper published by BIS, and in particular the proposals relating to remuneration disclosure. We have commented on these separately as part of our response to that paper.

Role of shareholders

Q1 Would a binding vote on remuneration improve shareholders' ability to hold companies to account on pay and performance?

Our view is that the advisory vote works well in practice. Companies take very seriously material votes against the remuneration report as well as material abstentions. They take time to understand shareholder concerns and make adjustments to their remuneration policies and practices. Through this process of engagement, coupled with the use of the advisory vote, shareholders are able to hold companies to account on remuneration matters. We strongly believe that this process should not be changed.

There are also a number of practical difficulties that would arise from a binding vote: How would companies determine which aspect of the directors' remuneration shareholders were voting against? How should they react to this? How would a company reconcile requiring directors to pay back remuneration with the legal position under their contracts? Such an approach would also be open to abuse by activist shareholders.

In our view more emphasis should be given to encouraging quality engagement between companies and their shareholders such that remuneration committees determine policy and practice in the knowledge of and taking into account the views of those shareholders.

Q2 Are there any further measures that could be taken to prevent payments for failure?

The current regulatory system, supported by the UK governance environment, should be adequate to ensure that inappropriate payments are not made, but we reiterate that for this to be wholly successful companies and shareholders should engage in meaningful dialogue to ensure understanding on both sides of what is and is not acceptable.

Q3 What would be the advantages and disadvantages of requiring companies to include shareholder representatives on nominations committees?

We can see only disadvantages in this approach. In order to play a full part in the deliberations of a nominations committee, a committee member needs to have a deep understanding of the strategic and operational challenges facing a company. This almost inevitably at some point in time will involve price sensitive knowledge which if an investor was privy to would make him an insider and bar him from dealing in a company's shares.

There is also an issue with regard to the selection of an appropriate shareholder representative: Who would select the shareholder? Does he represent the views of all shareholders and, if so, how does he reconcile conflicting views which will inevitably exist? Given that he will be one of a number of members of the committee and could be outvoted what is the true value of his presence on the committee? His views could just as easily be obtained by the company through informal means.

We reiterate that provided there is quality dialogue between a company and its shareholders such artificial measures as this should be unnecessary.

Role of Remuneration Committees

Q4 Would there be benefits from having independent remuneration committee members with a diverse range of professional backgrounds and what would be the risks and practical implications of any such measures?

As stated above, we do not believe it to be either practical or appropriate for non-board members to be members of the remuneration committee. It is widely accepted that the remuneration of directors should be linked to a company's strategic objectives and certain aspects, such as short term incentives, will be linked to specific financial targets. In these circumstances it is almost inevitable that the committee will consider matters of a price sensitive nature. In addition, independence is brought to bear in committee discussions through advice provided by remuneration consultants. This, together with an appropriate composition of non-executive directors usually provides adequate independence of thought.

Q5 Is there a need for stronger guidance on membership of remuneration committees to prevent conflict of interests arising?

There are sufficient checks and balances currently in place to prevent conflicts of interest impeding independence of directors.

Q6 Would there be benefit from requiring companies to include employee representatives on remuneration committees and what would be the risks and practical implications of any such measures?

We do not support employee representatives as members of remuneration committees for reasons similar to those articulated in response to question 3 above. There is also an issue of selecting an employee who has the requisite skills and who can represent the views of all employees, particularly in a company with global operations. The UK Corporate Governance Code already requires remuneration committees, in making decisions, to be sensitive to pay and employment conditions elsewhere in the company.

Q7 What would be the costs and benefits of an employee vote on remuneration proposals?

We fail to see any benefits of an employee advisory vote on remuneration. It would be time consuming, extremely costly for companies with a large global employee base and could produce potentially divisive and damaging results should employees vote against proposals. Also, in practical terms, it is unclear what a company would be required to do if employees and shareholders voted differently.

Q8 Will an increase in transparency over the use of remuneration consultants help prevent conflict of interest or is there a need for stronger guidance or regulation in this area?

Given the relatively small amounts paid to remuneration consultants, when compared for example to audit fees, we consider disclosure of fees unnecessary, however if it is considered that this would contribute to transparency we would not oppose it.

What is more helpful is disclosure of other services provided by the consultants to the company. This, coupled with consultants adherence to the Remuneration Consultants' Code, should be adequate disclosure.

Structure of remuneration

Q9 Could the link between pay and performance be improved by companies choosing more appropriate measures of performance?

It is important that appropriate measures of performance are chosen by remuneration committees to ensure that directors are incentivised to deliver strong financial performance and the longer term strategic objectives. The fact that more companies are moving away from traditional EPS and TSR measures to measures that are specific to the company's requirements is evidence that the trend is towards more focused arrangements that support a strong link between pay and performance. This trend should be supported.

Q10 Should companies be encouraged to defer a large proportion of pay over more than three years?

This approach should certainly be considered by remuneration committees but its relevance will depend on the business model of the individual company. For companies in which success is determined by reference to long term contracts this approach could usefully form part of the remuneration arrangements.

Q11 Should companies be encouraged to reduce the frequency with which long term incentive plans and other elements of remuneration are reviewed? What would be the benefits and challenges of doing this?

We agree that it is unhelpful for companies to change remuneration arrangements too frequently. Executives need clear incentive targets that are closely aligned to strategy and, just as a well-run company does not change its strategy too frequently neither should it change its incentive arrangements too frequently. However, to survive and grow a company's strategy will constantly evolve and incentives arrangements will need to evolve alongside and reflect its strategic objectives.

Q12 Would radically simpler models of remuneration which rely on a directors' level of share ownership to incentivise them to boost share value, more effectively align directors with the interests of shareholders?

Whilst we are supportive of avoiding overly complex incentive arrangements, to suggest that directors be incentivised solely on the basis of share price is a retrograde step.

Share ownership is an integral part of the way in which long term incentives are already structured, through delivery in the form of shares, and additionally most companies also impose a shareholding requirement on directors. The fact that vesting of long term incentive awards is dependent upon performance measures aligned to strategy, as well as their value on vesting being determined by share value, is a positive addition that outweighs any complexity in the schemes.

It should be noted in this context that investors often own shares in a quoted company for far shorter periods than executives remain in their posts, and we need to ensure that the shorter term time horizons of many investors do not override the longer term focus of executive management and their boards.

Q13 Are there other ways in which remuneration could be simplified?

Whilst remuneration committees should always strive to avoid complexity in remuneration arrangements to avoid obscuring the incentive message, a certain degree of complexity is an inevitable consequence of aligning directors' and shareholders' interests.

Q14 Should all companies be required to put in place claw back mechanisms?

We would support this provided it is limited to cases of fraud, misrepresentation etc and that it can be achieved successfully in practical terms and with due regard for any legal requirements.

<u>Promoting Good Practice</u>

Q15 What is the best way of co-ordinating research on executive pay?

Whilst there is a vast amount of data already available from various research bodies, institutional shareholder organisations, academic bodies etc, we could see some benefit from a body which had an overarching, co-ordinating role provided that this body was both independent and apolitical.

Yours faithfully

Judith Felton
<u>Company Secretary</u>

Glass Lewis

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
X (Proxy advisor)	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

N/A

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

N/A

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

While Glass Lewis believes companies should be free to provide the best disclosure as they determine makes sense for company, establishing some disclosure standards would facilitate easier comparisons among companies by shareholders.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Glass Lewis believes that the proposed disclosure requirements would be practical and informative. Further, Glass Lewis believes that disclosing the percentage change in profit, dividends and pay spend over a longer period would benefit shareholders by providing greater context and illustrating the company's historical practices. In addition an extended reporting period would help align this disclosure with the standard performance/holding period for many awards.

Further, Glass Lewis believes that the provisions of executive service contracts relating to exit payments are of paramount importance to shareholders, as discussed in our response to Question 5 below.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

Shareholders face significant challenges in evaluating executives' exit payments since companies often fail to provide a clear rationale for the remuneration paid to executives upon departure. In many cases, payments that appear to be triggered by employment termination are made despite the executive apparently stepping down voluntarily. Glass Lewis recognises that in some cases, the circumstances surrounding an executive departure may be sensitive, and the committee may therefore have to weigh contractual entitlements against potential liabilities; however, absent clear explanation shareholders may have difficulty reconciling the committee's stated principles regarding exit payments with the actual payments made.

While some companies condition the payment of large severance payments on actual termination of employment following a merger or similar corporate transaction, some make such payments even when the executives are still employed by the surviving entity. Information regarding these payment triggers and whether there are more than one is therefore very useful. Glass Lewis believes companies should disclose the principles governing service contracts and exit payments so that shareholders may review the appropriateness of the selected trigger for the executive exit payments.

Moreover, we believe all post-merger service agreements between executives of the target company and the acquiring company should be disclosed. Disclosure would illustrate potential conflicts between the best interests of the executives and shareholders if the prospect of a large exit payment influenced the executive's decision to advocate selling the target company.

Furthermore, we note the Government's intention that "exit payments will be subject to shareholder approval as part of the new binding pay vote on remuneration policy and, where relevant, the existing binding vote on share plans." True shareholder sentiment on exit payments is necessarily more evident in the vote results of a separate proposal, not bundled with a broader vote on remuneration policy. Including the vote on exit payments/provisions in the binding remuneration vote would create anomalous situations where a majority of shareholders support a remuneration policy but, if the exit payments/provisions were subject to a separate vote, the same shareholders would vote against the exit payment/provision.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

N/A

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

N/A

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

N/A

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

While Glass Lewis concurs that the single figure should reflect the claw-back, any use of claw-back should be clearly identified and explained in the table/footnotes, and the amount clawed-back disclosed.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Transparent disclosure of performance metrics/targets is essential for shareholders to assess whether the incentive is appropriately aligned with the company's strategy, and stretching relative to potential payouts. When performance targets are fully disclosed, independently verifiable, and aligned with the company's disclosed strategy/KPIs, shareholders are generally able to make this assessment without significant additional explanation. However when targets are not disclosed, are subject to opaque evaluations or adjustments, or do not align with disclosed strategy/KPIs, it is far more difficult for shareholders to assess whether they are appropriate. As such, in cases when targets are not fully disclosed, additional narrative disclosure requirements would strongly benefit shareholders, thereby encouraging companies to increase transparency.

We recognise that there are circumstances when full disclosure may be commercially sensitive. Nonetheless, shareholders still require sufficient disclosure to assess whether the incentive is appropriate and stretching. While not optimal, retroactive disclosure provides shareholders with some means of making this assessment, and specifically, the targets and actual performance should be disclosed retroactively. If this information remains commercially sensitive following the period in question, shareholders should reasonably expect a high level of explanation as to how vesting outcomes reflect overall performance, and of the committee's methodology in setting targets (including some effort to express the targets in less sensitive terms—for example, in relation to previous targets/performance under the same metric).

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

N/A

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Glass Lewis believes using the face value of awards provides a clearer and more comparable valuation than an "expected value" based on assumptions that may vary company to company. However, we believe that shareholders would benefit if this information were supplemented by historical vesting levels of awards made under the same plan and targets.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

Augmenting the current disclosure of directors' beneficial interests at the beginning and end of the reporting year with the number of shares subject to deferral and subject to performance conditions, as the Government has proposed, would benefit shareholders by providing a more comprehensive view of the directors' interests.

However, we note that proposed requirements on disclosure of variable pay (Draft Regulations, 12) only appear to apply to awards granted during the most recent financial year. The current practice of disclosing itemised details of all outstanding share awards for each director benefits shareholders by providing reference for past grant and target levels, and historical context for the current policy. This reference use is particularly beneficial given year-to-year changes in grant levels and targets, and the high occurrence of outsized "one-off" awards. The additional reporting burden on companies from disclosing multi-year grants is outweighed by the benefit to shareholders to be able to make more informed remuneration evaluations.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We consider the proposed method useful and appropriate since it would facilitate a transparent and comparable view into the correlation between remuneration and performance. Given that the number of executives may fluctuate within a company, particularly over the ten-year period proposed, CEO spend should generally serve as a more effective proxy than total executive spend. However, this should not preclude the company from displaying other performance metrics that may be more relevant to the company and its industry. Nor should it preclude the company from providing a separate line in the graph plotting total executive remuneration.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

Just as shareholders rely on the integrity of audited financial statements in making investment decisions, they rely on the integrity of the remuneration disclosure in making voting decisions on the approval of the remuneration report and, potentially, the election of the members of the remuneration committee and other directors. Therefore, it is essential the remuneration information be correct.

Since certain aspects of the remuneration information would be subject to audit as proposed, an audit of additional components would entail minimal additional costs. In particular, Glass Lewis believes that given the shareholder interest in evaluating outstanding variable pay awards and the performance-to-date or estimated vesting levels for outstanding awards, these are areas that would benefit from additional verification through auditing.

GlaxoSmithKline plc

Directors' Pay: consultation on revised reporting regulations. Response form.

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About You	
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I am responding on behalf of (please tick):	
X	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

We are very supportive of the desire to further improve remuneration reporting and of the new proposals in so far as they seek to raise the bar. We commend Dr Cable and BIS for their work in preparing the new regulations. We agree that remuneration reporting should be simplified and standardised as much as possible, but are mindful that latitude should be given to enable companies to differentiate themselves.

Having reviewed the proposed regulations we believe that there is one main change that would significantly contribute towards improving the introduction and operation of the new regulations and would alleviate anxiety on both the part of shareholders and companies.

The current proposal envisages a high level Policy Report which would be approved every three years (or sooner when changes are proposed) and an Implementation Report, to explain how the Policy was implemented for the reported year.

This leaves a potential gap in companies providing and shareholders getting comfort on how the high level Policy is proposed to be implemented for the following year. We consider this information important for shareholders.

We would therefore propose that the regulations be enhanced to require the following format:

- **A high level Policy Report** – subject to a binding vote every three years or when a material change is proposed.
- **An Implementation Report, split into two sections** – subject to a non-binding vote:

    A. Implementation of the Policy for the reported year

    and

    B. Proposed implementation of the Policy for the year ahead.

This would ensure that Remuneration Committees were able to communicate in advance how they planned to implement their approved high level Policy and shareholders would have the reassurance of seeing in advance what is planned.

Changing the Policy Report to provide this information on an annual basis could trigger the need for a binding vote on an annual basis, depending on the definition of a material change.

We would also suggest that companies should include the Policy Report in their Annual Report every year, even though it would not be the subject of a binding vote. This would save shareholders time in having to keep referring back to the Annual Report or our website to check against the approved Policy Report. It would, however, not result in achieving a cost saving to companies.

Finally, although we do not entirely agree that the CEO pay comparison graph is helpful, we would suggest that CEO pay comparison graph would be more meaningful if it initially required companies to show data for the previous five financial years. It could then build to a ten year picture, as envisaged by the current draft regulations. We would also suggest that interpretation of the graph could be assisted by annotating the line plotting the pay for CEOs over time to indicate any changes in CEO.

Please note that we have not provided drafting comments on the proposed regulations in respect of the above suggestions.

We believe certain aspects of the draft regulations require further clarification. Our suggestions are set out below:

Part 3, Section 6(e)(ii) should be clarified by the addition of the wording set out below:

(e) for column "e", either—

(i) the cash value of any monetary award or

(ii) the value of any shares or share options awarded, calculated by—

(X) multiplying the original number of shares granted by the percentage that will vest based on current year performance (or best estimate)

(XY) adding to the total arrived at in (X) the amount of accrued reinvested dividend shares received

(XYZ) multiplying the total arrived at in (XY) by the market value of shares at the date of vesting

Part 3, Section 15(b) and (c) require any person who has advised the company on remuneration matters to be named in the remuneration report. Where the adviser to the committee to be named in accordance with this section is acting on behalf of a firm, we believe that the regulations should be clarified to confirm that a company may name the firm itself rather than any individual(s) employed by that firm in its remuneration reports, or that the company should otherwise be able to seek an exemption from naming the individual(s) on the same grounds as those set out in section 506 Companies Act 2006 in respect of naming senior statutory auditors in the company's financial statements.

The following typographical correction should also be made to this section:

(b) state whether any person **or firm** ~~who~~ provided to the committee advice, or services, that materially assisted the committee in their consideration of any such matter;

(c) in the case of any person **or firm** named under paragraph (b), who is not a director of the company, state—

(i) the nature of any other services that that person has provided to the company during the relevant financial year;

(ii) by whom that person was appointed, whether or not by the committee and how they were selected;

(iii) the amount of fee or other charge paid by the company to that person for the provision of the advice or services referred to in (b) and the other services referred to in (c)(i) and the basis on which it was charged.

Part 3, Section 16(c) should provide further guidance concerning the Government's view of what constitutes a "significant shareholder vote" against a resolution.

We do not believe that requiring companies to adopt the tabular presentation format for setting out future remuneration policy, as envisaged by Part 4, Sections 18 to 20, will lead to the production of meaningful and informative disclosure. This could be remedied by the proposal set out above to include a "*Proposed implementation of Policy for the year ahead*" section in the Implementation Report.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

The costs associated with adjusting to these revised regulations include both the increased man hours required in preparing and responding to the new requirements as they are phased in over two or three years, as well as the financial cost of professional advice from lawyers and remuneration consultants required to ensure full compliance.

There are also likely to be increases in audit fees and associated management time as auditors adjust to the new requirements.

It is likely that Boards and Remuneration Committees will expend additional time in the first year or two following the introduction of the regulations as they adjust to the new format and requirements. They will undoubtedly wish to ensure that the Policy Report adequately reflects the remuneration policy that they have established to ensure that executives are rewarded fairly and are truly incentivised to achieve pay for performance.

Companies will also wish to ensure that they consult with their shareholders on the high level Policy they set out. GSK already conducts an annual governance and remuneration meeting with shareholders which provides invaluable feedback and guidance to the Board and Remuneration

Committee. The number of companies seeking to engage with shareholders will increase. A positive, but this will undoubtedly place a pressure on shareholders time.

Other incidental costs may include marginally increased printing and distribution costs. However, these are not likely to be significant.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

Please see our answer to question 1.

No. We strongly recommend the introduction of an addition to the Implementation Report to enable companies to set out for shareholders how they propose to implement the Policy in the year ahead. Otherwise we believe the high level Policy Report will be deemed by shareholders as too high level.

Based on the current proposal it would be inappropriate to include such detail in the Policy Report as any changes year on year could trigger the requirement for another binding shareholder vote before they could be implemented.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Yes. We believe that the proposed framework for reporting on directors' service contracts is clear, and would represent a useful and informative approach for shareholders.

We understand the perceived benefits of reporting what remuneration directors can receive in different scenarios, although we would approach such disclosure with caution.

Any requirement to provide estimates of potential future remuneration must inevitably involve making a number of assumptions, and may not reflect elements of remuneration for which it is not possible or reasonable to make an estimate, such as the value of reinvested dividends on long-term incentive plan awards. Accordingly, any such disclosure will need to make explicit that it is an indicative estimate provided solely for illustrative purposes, and is neither a guarantee of, nor cap on, the level of remuneration which may be received by a director upon achievement of threshold or maximum performance.

Similarly, the various assumptions upon which the calculations have been predicated should be set out in full, particularly where conditions for assessing threshold and maximum performance are different for the various elements of directors' variable remuneration.

We believe that additional factors should be considered when assessing the relative importance of the company's spend on pay. Although changes in profit and dividends are one indicator of company performance, a significant proportion of the variable remuneration of our directors is subject to business related performance conditions and measurement of relative total shareholder return (TSR). We believe that including TSR with these measures, which also takes into account factors such as share price appreciation and other returns to shareholders in the form of share buybacks is a more appropriate measure of company performance against which to assess spend on pay. However, we recognise that this measure may not be appropriate for other companies, so this requirement is unlikely to lead to meaningfully comparable disclosure between companies in different sectors or industries.

In any event we believe that this comparison should compare company performance measures against the company's spend on pay for its directors and senior management only. We believe that this would be more meaningful.

It is also worth noting that Total pay for an organisation can change for a number of reasons which may not necessarily be related to shareholder value creation, for example, currency exchange, corporate acquisition or disposal, or a company opting to outsource some of its production services would reduce its total pay cost. If numbers are to be included we believe that the absolute spend rather than the change in spend, should be included. Alternatively it may be preferable to focus on directors and senior management pay.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We support the introduction of a broad, principles based approach to calculating exit payments for outgoing directors, and agree with the Government that it would not be appropriate to mandate a specific mechanism. We support the principle that the company's remuneration committee, acting within the scope of such a policy, should retain discretion to decide an appropriate exit package quickly for an outgoing director, taking into account the circumstances under which a director leaves, the director's performance up to that time and the changing needs of the business.

We believe that in circumstances where a departure of an executive could result in significant competitive harm to a company it is appropriate to mandate that the executive should not be required to seek work to mitigate his loss.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

The remuneration committee, acting in the best interest of the company's shareholders, is already required to have regard, among other things, to the wider workforce in carrying out its duties. We firmly believe that it is important that decisions concerning the remuneration of executives should be taken in the context of the policies and practices in place for the wider workforce.

However, for large international complex businesses like ours with over 95,000 employees in over 100 countries, it would be extremely difficult to facilitate a detailed and truly representative process to gauge the views of all employees on the company's remuneration policy. The practical implications of ensuring that the Remuneration Committee is aware of the views of all of the company's employees would make this proposal administratively unworkable.

GSK currently undertakes, on a regular basis, employee satisfaction surveys. We believe that these may be a more appropriate vehicle for the remuneration committee to understand employees' views, and agree that this approach should be discussed in full in the remuneration report.

Since 2010 companies have been required to disclose how the pay and employment conditions of employees in listed companies have been taken into account when determining directors' remuneration. We think companies could provide further information in the implementation report (e.g. in relation to overall planned salary increases), but the key point is that the remuneration committee is presented with relevant facts.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Please see our specific comments on this point in Question 1 above.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

No, we do not believe that this is an appropriate solution.

We understand that shareholders are concerned at the possible manipulation of remuneration packages by payments into pension funds. We believe that this could be clearly addressed by providing clearer guidelines on pension disclosure. Furthermore, Remuneration Committees could also provide an explanation of how they reference pension arrangements in their benchmarking process.

However, adding what would be an arbitrary pension valuation into a summary of payments actually made or received by an executive will create a misleading impression of the total value of the package actually received by the executive.

The Government should be keen to encourage both companies to provide adequate pension provision and for employees to take up pension arrangements. We believe this disclosure will create an overinflated value of a remuneration package which is to all intents and purposes meaningless. It will also likely draw fire from the media, unnecessarily.

We remain concerned that the value attributable to defined benefit pension schemes is not easily measurable and not an appropriate element to be combined into "the single figure".

However, to the extent that it will be required to be included in the single total figure of remuneration, we do not believe that the HMRC methodology should be used. We would favour disclosing the transfer value of the change in accrued benefit, net of inflation, relating to the year being reported on. Alternatively, if such a methodology is not be considered appropriate, we believe that applying the valuation methodology set out in International Accounting Standard 19 (IAS19) would be preferable to the HMRC methodology, and that such methodology should be applied consistently to all applicable pension valuations and calculations throughout the company's annual report.

We would further encourage the Government to work with the Financial Services Authority to ensure that pensions' disclosures, and disclosures pertaining to executive remuneration more generally, are harmonised between the requirements of these regulations and the Listing Rules.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We believe that the purpose of the single figure should be to demonstrate clearly the amount of remuneration actually received by each director (for which reason we continue to believe that inclusion of pension benefit accrued during the year is not an appropriate element to be included).

Accordingly, we would expect that the amounts shown in respect of bonus, vested LTIs and other elements of remuneration subject to clawback would be shown net of any amount already clawed back, and would not be shown as a separate item in the single total figure of remuneration.

In practice, the likelihood is that if the company exercises its right to clawback it would be reflected in a reduced or nil bonus and failure of awards to vest or grants to be made.

A separate disclosure or reconciliation may be provided to show the effect or quantum of any amount(s) of remuneration clawed back, although the reasons for applying such clawback may be commercially sensitive and Remuneration Committees should retain discretion to determine whether or not to disclose these specifically. We are also mindful that there may be legal restrictions or it might prejudice ongoing litigation to publish details of individual clawback arrangements. However, as far as reasonably possible, this disclosure should be provided or the Committee should give an explanation as to why it has not been provided.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Due to the commercially sensitive nature of certain performance measures and metrics, GSK does not publish all targets during the relevant performance period due to the risk of competitive harm. The Company has undertaken in all instances to publish full details of the targets, and how they have been met, once the performance period to which they relate has ended and to give an indication of how they have been achieved during the performance period.

Disclosures in the remuneration report relating to vested LTIs are audited, so shareholders should have assurance that the amounts of awards vested are correct.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

No. We do not believe this disclosure will aid understanding.

Please refer to our answer to question 8. The basis of valuation of pension benefit for inclusion of "the single figure" should be consistent with the accounting methodology applied to the calculation and disclosure of pension benefits elsewhere in the Report, and aligned with the requirements of the UKLA's Listing Rules.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Yes, we are supportive of this proposal.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We support the simplification of approach to disclosing directors' interests, and agree that it should not be necessary to repeat information relating to directors' holdings to the extent that these have been disclosed elsewhere in the report. We realise however, that this will require careful drafting to avoid confusion.

Care must be taken in disclosing directors' share ownership requirements, particularly in the absence of specific guidelines concerning the format that such disclosure should take, as these disclosures will not necessarily be comparable between companies.

Furthermore, care should be taken when disclosing whether share ownership requirements have been met, particularly as the absence of guidelines or recommendations for the appropriate level of share ownership for a director or the length of service of a particular director will have a direct impact on whether or not such requirements have been met.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph

would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

No. Subject to our comments in response to question 4 above, we are unsure of the value that this graph would add in addition to the comparisons required. We suggest that these two requirements could be neatly combined and disclosed as a single table or graph together, plotting company performance (measured by TSR) against total CEO pay and total pay for the company as a whole.

Given that CEOs change and their remuneration will vary based on their skills and experience, the chart could be misleading unless appropriately annotated. Please see our suggestions in question 1.

We would also suggest that the table should initially show remuneration for the last 5 years and then build to 10 years.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We would suggest that the information on the total shareholdings of directors and their share ownership requirements should also be subject to audit.

Graham Phillips

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
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I do not wish my response to remain confidential.

About You	
Name: GRAHAM PHILLIPS	**Organisation:**
Email: [redacted]	**Address:** [redacted]

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	Quoted company
	Other company
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	Investor representative organisation

	Non governmental organisation
	Trade Union
	Lawyer or accountant
X	**Other (e.g. consultant or private individual)**

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

I have carefully examined the draft regulations, which seem to appropriately reflect the policy approach outlined in the Consultation Document.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

I have no evidence to doubt the comment in paragraph 2.7 of the Consultation Document that any costs will be significant.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

I appreciate the Government does not want to micro-manage companies. However the approach proposed in paragraphs 40 -44 of the Consultation Document is somewhat generalised. There is therefore a risk that this generalised approach will blunt the cutting edge of the proposals, and not represent much of an advance on the current system. The bullet points in paragraph 41 of the Consultation Document are fine. Annex A is also mainly satisfactory (though the % figures quoted in the “Opportunity” column (Long Term Incentive Plan row) seem somewhat high and a 200% maximum would be appropriate.) Paragraph 42, last sentence, refers to companies that already adopt best practice. It would be helpful to identify a number of these companies by name.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

The Government approach is generally helpful practical and informative. However, the approach would be even better if the Government was to propose a standard methodology for calculating pay in the scenarios referred to in paragraph 48 of the Consultation Document.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

I support the Government proposals on exit payments. It seems Especially unjust if Directors who leave "under a cloud" take substantial exit payments.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

I consider that it helpful if the Government was to introduce a requirement that individual companies have to disclose the ratio between the pay of the Chief Executive, and the median earnings of the organisations workforce. This could easily be done, and could be a helpful influence on curbing excessive executive pay.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

I support the approach of the Government here. I especially welcome the proposal that there is to be a set methodology for the calculation of the single total figure of remuneration.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

Yes

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Yes. I especially agree with the statements in paragraph 73 of the Consultation Document about claw-back needing to be transparent.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

I appreciate there is a balance to be struck between protecting commercial confidentiality, and ensuring that reports are specific enough to allow meaningful accountability to shareholders. However if all the companies are equally required to publish full details of performance against metrics then there may be an approximation of a level playing field for companies?

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

I am not entirely convinced by the reasoning outlined in paragraph 81 of the Consultation Document.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Yes

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

There would be a particular benefit if reports were sent out the shareholdings of Directors that are subject to performance conditions (paragraph 87(c) of the Consultation Document refers.)

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

Such a graph would be extremely useful. I agree that the total shareholder return and CEO pay are the best proxies for company performance and pay.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

I agree that it is not necessary for every part of the report to be audited. I also agree with the sections that the Government proposes should be subject to audit. However I would also add:

- Total shareholders of directors (all elements included within the box (especially (c)) in paragraph 87of the Consultation Document.

Grant Thornton UK LLP

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

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Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
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Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

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I am responding on behalf of (please tick):	
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Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

We make the following observations on the draft regulations attached at Annex B to the consultation paper:

Paragraph 6.(c).(iii) requires inclusion for money purchase pension schemes of the additional value achieved in the year within the single figure of remuneration only where a contribution has not been made by the company during the year. It is not clear, however, why such a distinction is made for remuneration reporting purposes. We note, therefore, that it may be more appropriate to harmonise the reporting of defined contribution schemes with those set out for defined benefit pension schemes in paragraph 10 of the draft regulations.

Paragraph 7(5) states "for the purposes of 7(4)(a) as it applies to paragraph 6(c)(iii)…" There does not, however appear to be a paragraph 7(4)(a).

We note the requirement in paragraph 13(b) that for the purposes of the line graph that the relevant period is 10 years. We note, however, that it would be helpful for a commentary to explain any significant matters affecting the reported data that would be required to interpret it correctly.

Paragraph 15(2) appears to place particular emphasis on advice given to the remuneration committee by a director who was not a member of it. In our view, equal emphasis should be given to any party, internal or external, who is giving advice to the remuneration committee to enable them to discharge their duties. In addition we note that "person" according to the Interpretation Act 1978 includes bodies of persons corporate and unincorporate.

Paragraph 16(c) requires certain information to be reported in the event of there being substantial shareholder votes against the resolutions specified in paragraphs 16(a) and (b). In this context, it would be helpful to define what is meant by the term "substantial" to enable consistent application of the regulations.

Paragraph 24 requires the remuneration report to set out the percentage changes in profit, dividends and overall expenditure on pay in the reporting period compared to previous years. However, it is not clear either what comparative period is meant by previous years or by overall expenditure on pay. In the context of overall expenditure on pay, is it intended to mean the change in the single figure for directors' remuneration or, say, total payroll costs incurred.

Furthermore, the consultation paper suggests that this information should be reported each year. However, this will not be required where a company does not have to include the policy part in its directors' remuneration report for a particular year. It may, therefore, be necessary to include these requirements within the requirements of Part 3 of the draft regulations.

In addition, paragraph 24 (2) refers to the phrase "profit" which is a vague term, especially in the context of financial statements prepared under IFRS. In this context, it may be more helpful to define the line item in the primary statement that should be used such as "profit (loss) on ordinary activities after tax" in the context of UK GAAP accounts and profit (loss) after tax for accounts prepared in accordance with IFRS. Furthermore, it is not clear whether the measure used should be that reported in a parent company's accounts or those in its consolidated accounts from the term used (emphasis added) "..shall have the same meaning as is relevant in respect of the preparation of the **accounts of the company.**"

Paragraph 30 requires specified information to be given concerning the percentage increase in pay of any director fulfilling the role of chief executive officer and that of all the employees generally. As noted above, if it is intended that this information should be provided annually then it may also be necessary to consider including this requirement within Part 3 of the draft regulations.

Paragraph 32 could be simplified by stating that the information contained within paragraphs 3 to 12 are subject to audit.

We also note that, in the first year of implementation of the new regulations, it may be beneficial for users if a reconciliation was given between the single figure of remuneration reported under the new regulations and the various components of remuneration reported under the previous regulations.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

We note that companies may incur some additional costs in complying with the new reporting regulations, some of which will be of a one-off nature in the first year of applying the new reporting requirements and others will be on-going incremental costs such as additional audit costs arising from potential scope changes introduced by the regulations.

We do not, however, expect the overall additional costs incurred by companies to be substantial and also note that clear and timely guidance, as proposed, should help to reduce these incremental costs.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We are supportive of a principles based approach to reporting and consider that Part 4 of the proposed regulations relating to pay policy is consistent with this.

Companies need the flexibility to decide how to communicate with their stakeholders in a meaningful manner and the draft regulations sets out the framework to report information relating to directors' remuneration.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We are generally supportive of the proposals contained in the draft regulations.

The reporting of scenarios in a graphical form should be supplemented with a narrative disclosure explaining the reasons for remuneration being either above or below threshold in the reporting period together with a comparison to previous years as this would enable shareholders to understand whether the targets set were, in fact, sufficiently stretching for management to achieve.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We are broadly supportive of the provisions set out in paragraph 26 concerning how termination payments will be made.

Paragraph 26(b) requires a company to explain whether it will distinguish between types of leaver or the circumstances under which a director left. In the light of the concern over perceived "payments for failure", it would be helpful for companies to state explicitly the approach they expect to adopt.

We note that the information required by paragraph 26 is not required to be individualised. However, it may be necessary to agree specific terms with individual directors reflecting their roles and expectations of them. In such cases, companies should report this information as individual exceptions to the general policy applied so that shareholders can give their approval to the arrangements made.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We support the Government's proposals in this area. In this context, we note that employees are stakeholders and some may also be shareholders as well. Therefore, to provide a balanced report on directors' remuneration, it would be helpful information for users to understand why employees' views on the directors' remuneration policy were not sought.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We consider that the table set out on page 24 of the Consultation Paper generally sets out the principles of reporting a single measure of directors' remuneration. We note, however, that it may provide more meaningful information to include the "claw back" of remuneration within a separate column in the table.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We agree with the general principle that the amount reported for defined benefit pension schemes should be based on the value of the benefit to the director rather than the cost of the provision of the benefit to the company. We note that the use of the HMRC methodology may be a practicable solution. We are not persuaded, however, that the number reported will provide any meaningful information other than being a raw comparator against other companies. In addition, as noted in our response to question 1, we recommend that a similar methodology is applied to determine the value of defined contribution pension arrangements.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that the amount clawed back during the year should be reported as part of the single figure of directors' remuneration.

We do not, however, agree that no further disclosure relating to amounts clawed back should be given as implied by paragraph 73 of the Consultation Paper.

We consider that any amount that has been clawed back will be of interest to shareholders together with the reasons for doing so. In this context, we note that amounts clawed back should be separately identified, as referred to in response to question 7 above, in the proposed table.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We consider that it will be important for companies to explain clearly the amounts of variable pay that have been earned in the context of the company's performance for a particular reporting period. They will need to explain their performance against the key metrics used to determine the amounts of variable pay earned by the directors.

However, given the difficulty to achieve through regulation the balance between commercial sensitivity and the provision of useful information to shareholders we do not propose any changes to the general reporting requirements set out in the Consultation Paper.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We do not have any substantive comments in response to this question.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We are generally supportive of the approach proposed. We do note, however, that the amount reported may bear little relation to the benefit they ultimately receive and, therefore, this should be made clear to shareholders in the remuneration report.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We do not have any substantive comments in response to this question other than to recommend that comparative information should also be disclosed.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We agree, in principle, that any proxy for company performance needs to be both relevant to shareholders and easily understood. In this context, total shareholder return appears to be a measure that meets these characteristics.

However, there is no explanation given in the Consultation Paper as to why it is that the remuneration of the CEO should be plotted against total shareholders' return. In the light of this, it may be more appropriate for total directors' remuneration, which is the emphasis of the report, or at least total executive directors' remuneration to be reported in proposed graph.

If, however, the Government continues to proceed with this requirement it will be important to provide clear guidance on how to deal with a change in the appointment of the CEO during the reporting period when determining the measure of remuneration that should be used in the graph.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We do not have any substantive comments in response to this question.

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27 September 2012

Introduction

We welcome the reforms set out in the consultation which we believe will help to provide the tools for investors to engage more meaningfully on remuneration. We believe that executive remuneration at many companies does not align executives' interests as well as it should with their long-term owners.

Inevitably, some of our comments may be more appropriately be included within emerging best practice. However, above all, we believe that there should be a level playing field between UK and overseas domiciled listed companies.

Question 1: the Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

We have confined our remarks to the substance of the consultation rather than the drafting of the regulations.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

We believe that companies are best placed to answer. We would point out that many such costs should be non-recurring and we do not believe that they will be significant as a proportion of turnover for the largest companies. However, the additional cost, including opportunity cost, of the change will fall disproportionally on smaller listed companies. Whilst we welcome the change as far as the largest companies are concerned, this is more of an issue for smaller companies, particularly those outside the FTSE 350.

Notwithstanding these remarks, we believe that the changes should encourage greater and more effective shareholder engagement on remuneration policy and practice. Over time, we believe that this should improve alignment to our clients' interests and result in better practice, where pay is better aligned to long-term owners' interests. This in turn should help to improve the long-term sustained value arising from our clients' part ownership.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We believe that there is merit in a table that describes the key elements of remuneration and the company's remuneration policy behind the payment, not least because it should aid finding the relevant disclosures and comparability. We agree that that the Government should not prescribe the nature of disclosures as each company has a unique business model and therefore should have a different remuneration policy which in turn should drive different disclosure.

We also note that if companies wish to include exceptional circumstances as part of their policies they should be clear within this table as to what those exceptional circumstances are.

4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

The most important change in relation to service contracts would be to make them available for scrutiny by shareholders more readily. We do not understand why such contracts cannot be made readily available electronically. That companies are unwilling to make these contracts available in such a way fuels our concern that they may often contain provisions that many investors would find troubling.

Nevertheless, it would be helpful to see the key points of the service contract, most sensibly within the table described in question 3 against each element of pay. It would also be helpful to have a provision that allowed for all material elements of the service contract and incentive scheme rules to be disclosed either in the remuneration report or on the company's website. In particular, all termination provisions should be in this table or at least cross referenced in it and easily found.

In relation to the requirement that the company set out the change in profit and dividends together with the total expenditure on pay we have some concerns. Which profit figure? Will it be audited? Is profit the best measure for all companies? Free cash flow may be a more appropriate figure to use in some companies. If profit is used, we believe that audited distributable profits would be a good figure to use. We believe that UK and other tax payments should also be included in the split of payments so that investors can understand better the contribution made by companies in this way.

Depending on business model, the total pay figure will vary between companies even those within the same industry. We are not sure that it will actually reveal anything useful or that is not fairly readily calculable. This figure may be better achieved via cross reference or hyperlink to the company website, particularly in the context of cutting clutter within annual reports.

We believe, instead, that there should be analysis of remuneration against the chosen key performance indicators of the board, even if these are not used directly as performance targets in remuneration schemes. If the company is demonstrably not performing well against its chosen KPIs, we would expect there to be a correlation to pay and if there is not, the reasons should be explained. If KPIs have changed this should be noted and it should be clear which KPIs are audited and which are not. Limiting the analysis merely to profit and dividend may provide a false analysis and lead to focus on short term profit and cash return at the expense of long-term investment in the business.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We agree that this is an important exercise. However, most leavers are neither fully good nor bad leavers and the reasons for them leaving are often somewhat grey. Companies should therefore also explain their approach in relation to leavers whose contracts are settled other than in the case of bad leavers. As well as enforcing, explicitly, the duty of the leaver to mitigate losses to the company, companies must be more alive to the risks of overpaying executives when they leave the company. And so how the nominations committee and the remuneration committee work together, including at the time of recruitment, to minimise this risk is important to understand.

As well as the general principles, companies should disclose any exceptions within individual service contracts to those principles and when the individual service contracts were last reviewed.

We would also note that the scheme rules for LTIPs and other share based payments should be made easily available on the company website as these will influence the range of options available to the remuneration committee.

When any executive director leaves the company, the remuneration committee must explain clearly any payments made on departure, the reasons for them, any departure from the provisions of the service contract and the extent to which they have used their discretion, either to reduce or increase the payments.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We believe that such a requirement will help remuneration committees to consider important issues such as whether their policy articulates the appropriate tone from the top and how the pay policy cascades down through the organisation. We believe that it is not just important to seek employee views but to explain the final policy and practice to employees. We would suggest that the government adds this requirement.

We have heard suggestions that this is an impractical requirement but we believe that vehicles such as use of the company intranet, employee surveys, town hall meetings and employee consultation forums and trade unions can all be used to communicate with staff: other messages are communicated in this way so why not use them to explain pay?

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

We believe that the proposals should go further than described. The FRC's Reporting Lab's proposal included an additional column for additional information and explanations and we would welcome this.

We also question whether it may be possible to include this information in the table relating to the policy (see Question 3). It would also be helpful to see comparative figures for previous years and so the table showing historic pay and relative TSR (Question 14) should ideally be presented in close proximity to the table.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We believe that this is the best available option.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that claw-back should be included within the calculation of the single figure and the associated disclosures around it. We also believe that the committee chair's introductory remarks to the remuneration report should draw attention to any such action and the reasons for it.

We would further add that it would be a very helpful disclosure for the remuneration report to state whether claw back or malus provisions were used and/or how the committee used its discretion when assessing the payments made during the year. This would especially be the case in circumstances where there had been an incident during the year that prima facie would suggest that variable remuneration should be adjusted.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We do not expect companies to publish information that might damage them commercially. However, we also expect companies to be candid about performance, metrics and performance against targets.

We do not believe that it would be damaging commercially to publish retrospective information on the extent to which targets have been met if those targets cannot be published in advance. However, we do believe that the metrics should be published so that shareholders are able to judge their appropriateness and be cognisant of changes.

We have heard that companies are considering changing their metrics because their chosen KPIs are so commercially sensitive or would reveal price sensitive information. As part of the wider debate around remuneration, of which this consultation forms part, we believe that companies need to provide practical examples of where they believe that there are commercial risks in disclosure. Investors can then begin to have a dialogue with companies about how to find a solution. As yet, we have not become aware of a scheme where publishing the targets and performance against them retrospectively would be damaging.

We would be seriously concerned if companies chose to change KPIs without attempting to resolve this issue with investors.

We would further add that KPIs should normally only change if there has been a change in strategy and this would be likely to result in a material change to the policy which should in turn be put to shareholder vote.

Whilst we can see that unthoughtful extrapolation from the previous year's data into sell-side analyst's models for the current year may lead to difficulties for some companies but this will most likely be in cases when companies are not communicating effectively or where remuneration practice is egregious. Again, we do not wish to damage companies but do not see that companies with good practice have grounds for significant fears: let us debate these fears openly.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors.

We believe that the remuneration report should be clear on how directors' arrangements differ from other members of staff. We believe that it is important for boards to explain to shareholders why there are differences, if there are differences, and further believe that both seeking employee views on these differences and explaining the reasons for them to employees (see question 6) is also very important.

In particular, we are increasingly concerned by directors frequently enjoying pension arrangements that are far more generous than those of other employees. Where pension arrangements differ for directors companies must explain the reasons for these differences.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Yes. We believe that this is appropriate for the reasons that the consultation states. Companies will still be free to explain what they expect the actual vesting value to be. We would also welcome companies explaining why they believe that the targets that they have chosen are stretching.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

The disclosure must make clear all encumbrances or lien over the shares together with any hedges and similar arrangements. Otherwise, we are in agreement with the disclosures.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful. If so do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We believe that this would be a useful tool and that serious readers of annual reports would understand the potential shortcomings of the chosen metrics.

We believe that the proposed report would be hugely strengthened and linked to the forward looking policy by indicating the target performance anticipated for the next three years.

There has been some discussion about boards becoming non-executive in nature, akin to German supervisory boards, to arbitrage the proposed reforms in this consultation. We would therefore suggest that this graph should be published whether or not the CEO is on the board.

We would add that perhaps the graph could be strengthened by showing how each individual element of pay contributed to the overall total, though this requirement might best be achieved via emerging best practice guidance.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We believe that the report should explicitly state which KPIs chosen as performance metrics are audited and which are not. If the metrics are not audited the remuneration committee should describe how it assures itself of their integrity.

Other remarks:

We note that one of the most high profile votes against a company's remuneration report this year was at WPP which is not domiciled in the UK. We therefore urge the government to ensure that the UKLA requires, via the Listing Rules, similar standards for all companies listing in London in relation to remuneration disclosure.

It is conceivable that the additional scrutiny over the CEO's pay might lead to executives not wishing to be on the board and the de facto emergence of supervisory boards with the attendant governance issues that they might bring. We also note that in some companies there are individuals who are more highly paid than the CEO. It may be appropriate therefore to show the pay of the top five highest paid in the table discussed in question 14.

High Pay Centre

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
Name: Deborah Hargreaves	Organisation: High Pay Centre
Email:deborahhargreaves@gmail.com	Address: CAN Mezzanine, 32-36 Loman St, London SE1 OEH

I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
X	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Costs should not be onerous as companies have most of this information already available. An additional cost will be incurred in consulting the workforce, but this is such a valuable addition to the disclosure regime that it should not be omitted on cost grounds.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

A table is helpful, but each element of remuneration should be clear. There needs to be a specific amount detailed for the maximum potential value of pay awards in monetary terms.

Companies should disclose key performance indicators that relate to pay awards.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Companies should make directors' service contracts available, in line with best practice. Contracts should also be in line with the company's agreed remuneration policy, subjected to a binding shareholder vote.

A chart of total remuneration opportunity to show remuneration committee expectations around pay awards is a useful way of displaying this information.

When disclosing profit, dividends and overall expenditure on pay, it is important that some absolute numbers are attached to these requirements rather than just percentage changes. This will help shareholders make meaningful judgements on how the company is allocating resources. Also it would be useful to publish figures extending over a number of years rather than just for one year. A figure for expenditure on boardroom pay should be published alongside one for the rest of the workforce.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

A company should be required to publish the extent of exit payments it will pay. Companies should also consider the length of directors' contracts and therefore size of exit payments with a view to reducing them more into line with notice periods required by the rest of the workforce.

Companies should also be required to disclose the level of golden hellos that they are prepared to pay, particularly if they are prepared to buy executives out of existing retention bonuses.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

The High Pay Centre believes that publication of the ratio between chief executive's pay and the workforce average would be informative. Meaningful comparisons could be made between companies in the same sector. In addition, big changes to the pay ratio from one year to the next would prompt some more searching questions by investors.

Companies should be required to consult all employees on directors' remuneration. This should cover all aspects of remuneration, not just salary. This could be done by a vote extended to the entire workforce, or through consultation with employees representing the workforce. If the company holds a vote, it should be required to publish the results of the vote in the remuneration report.
The High Pay Centre believes that effective communication with the workforce could be achieved by appointing an employee to the main board or remuneration committee.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

The single figure for pay received is an important element of these reforms. It is crucial to measure all elements that will pay out in a particular year. The table representing disclosures required is comprehensive as long as all incentive plans that vest in that year are captured.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The HMRC methodology for calculating pension values is likely to represent a lower value than would be the case if a transfer value, for example, was used. Directors' pensions are an extremely valuable part of their whole package and the only really meaningful way to value them is to include a transfer value even if it fluctuates.

Directors' pensions should also be compared with employee retirement benefits. For example, what percentage of salary is paid into the director's pension compared to that paid into employee pensions.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Clawback is an important development in remuneration policy. So far, it has been most applicable to financial services companies where risk-taking may jeopardise returns in future. However, there are plenty of examples where it might apply to other companies.

Environmental damage by company negligence, for example, may require clawback from an executive's package. Similarly, safety issues at the company, tobacco companies supressing research into the dangers of smoking, nuclear power plants being built in the wrong place, such as at Fukushima.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Key performance indicators are used to measure company strategy. These should also be included in bonus targets. At the moment, bonus targets can consist of completely different measures and are often not fully disclosed due to commercial confidentiality.

Shareholders suggest that performance targets are sometimes changed by the company if they look like not being met so that bonuses are achievable. If key performance indicators were also used as bonus targets, there would be a closer alignment between pay and performance. Targets would also be easier to understand.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

Companies should be required to disclose details of DB pension schemes including value of contributions in that year, accrual rates, size of overall pension pot, directors' retirement ages and any additional benefits that become due on retirement.

Numbers of directors in the directors' pension scheme should be published alongside numbers of employees included in different types of company schemes (including those closed to new entrants). The company should disclose the value of contributions it makes on behalf of the workforce into pension schemes.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

Disclosing incentive awards (that have not yet paid out) at face value is the only way to achieve any consistency of disclosure since expected values rely on models where inputs may vary.

It is important that incentive awards include clear performance criteria and companies should look at using key performance indicators for both strategy and remuneration, as previously mentioned.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

Simplification is to be welcomed for any aspect of remuneration.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

Total shareholder return as a proxy for company performance is a blunt tool. It would be best practice for companies also to track executive pay against other key performance measures.

Executive pay (total package) should also be plotted against employee pay.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

No

Hymans Robertson LLP

Director's Pay

HYMANS ROBERTSON'S RESPONSE TO THE DEPARTMENT FOR BUSINESS, INNOVATION & SKILLS' CONSULTATION ON REVISED REMUNERATION REPORTING REGULATIONS

In June 2012 the Department for Business, Innovation & Skills (BIS) published a consultation paper proposing changes to the statutory rules about disclosure of directors' remuneration. We have responded only to those aspects of the proposals connected with pension provision: specifically, our comments relate to consultation questions 8 and 11.

Hymans Robertson's Views

The proposal to base defined benefit pension scheme disclosures upon HMRC's annual allowance rules will elicit Pavlovian snorts from those who are familiar with the legislation in question. Nevertheless, it has some features that recommend it. It is relatively simple (superficially). It should, in theory, facilitate easy comparison between companies. It provides mechanisms for adjustments that take account of inflation, as well as mid-year events such as transfers, pension sharing on divorce, etc., and as such has a level of sophistication above that of the current Companies Act requirements.

It resolves to some extent the existing incompatibilities between the current Companies Act disclosures and those under the FSA's Listing Rules. The Companies Act legislation requires comparison of the director's cash equivalent transfer values (CETVs) from one year to the next, whereas the Listing Rules entail the calculation of a CETV of the increase in the directors' pension during the year. To complicate matters further, the increase measured by the Listing Rules value is net of inflation, whereas no such allowance is currently made in the Companies Act disclosures.

The annual allowance calculation is, somewhat like the Listing Rules disclosure, a measure of the increase in the director's accrued benefit. That information can be lost in the noise created by changes in market conditions if one simply compares successive years' transfer values.

As HMRC and the pensions industry has learned, however, the annual allowance calculations can be far from simple in some cases. HMRC has already published (and reviewed, and re-published) dozens of pages of guidance on the annual allowance legislation, and yet there many problems that remain to be dealt with; indeed, the 2012 Budget document confirms that further legislative amendments are required to make the rules work as intended. It is not clear from the draft Amendments Regulations how far companies would be expected to follow the annual allowance rules. As matters stand at present, we cannot recommend the adoption of the '*HMRC method*'.

The possibility of a review of the Listing Rules, mentioned in the consultation document, is welcome. We strongly recommend that the statutory and FSA requirements are harmonized; or, better yet, that one or the other is eliminated entirely, on grounds of redundancy.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The reference to section 234 of the *Finance Act 2004* as an explanation of the '*HMRC method*' is inadequate. Paragraph 7(4) of the substitute Schedule 8 refers to '*the increase in the value of the lump sum that the individual is entitled to*'. This seems to correspond to the '*pension input amount*' in section 234, the calculation of which encompasses both pension and lump sum entitlements. The use of 'lump sum' in a way that is inconsistent with section 234 may lead to confusion.

It is unclear whether and to what extent the '*HMRC method*' is intended to take into account the adjustments to the '*pension input amount*' calculation required by other sections of the *Finance Act 2004*. Differences in interpretation could lead to inconsistency in reporting practices from company to company.

The proposed substitute Schedule 8 appears to lack a definition of '*money purchase benefits*'. (It may be relevant to note at this point that the tax legislation considers a '*cash balance benefit*' to be a sub-category of '*money purchase benefit*' (see section 152 of the *Finance Act 2004*). It appears that for directors' remuneration disclosure purposes a cash balance benefit may be a form of defined benefit.)

The reference to '*7(4)(a)*' in paragraph 7(5) of the substitute Schedule is nonsensical.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

For the reasons given above, it is unclear whether the information reported would be consistent from company to company , and whether this would in turn limit shareholders' ability to exert more leverage on executive pay.

Enquiries

If you have any comments on this response, please address them to Paul Maclean, whose contact details are set out below.

Postal address: Paul Maclean
Research Consultant
Hymans Robertson LLP
20 Waterloo Street

BIS | Department for Business Innovation & Skills

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

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About You	
Name: Paul Maclean	Organisation: Hymans Robertson
Email: paul.maclean@hymans.co.uk	Address: 20 Waterloo Street, Glasgow, G2 6DB

I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
✓	Other (e.g. consultant or private individual)

Questions

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The annual allowance calculation is, somewhat like the Listing Rules disclosure, a measure of the increase in the director's accrued benefit. That information can be lost in the noise created by changes in market conditions if one simply compares successive years' transfer values.

As HMRC and the pensions industry has learned, however, the annual allowance calculations can be far from simple in some cases. HMRC has already published (and reviewed, and re-published) dozens of pages of guidance on the annual allowance legislation, and yet there many problems that remain to be dealt with; indeed, the 2012 Budget document confirms that further legislative amendments are required to make the rules work as intended. It is not clear from the draft Amendments Regulations how far companies would be expected to follow the annual allowance rules. As matters stand at present, we cannot recommend the adoption of the '*HMRC method*'.

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It is unclear whether and to what extent the '*HMRC method*' is intended to take into account the adjustments to the '*pension input amount*' calculation required by other sections of the *Finance Act 2004*. Differences in interpretation could lead to inconsistency in reporting practices from company to company.

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Institute and Faculty of Actuaries, The

The Actuarial Profession
making financial sense of the future

Consultation Response

Department for Business, Innovation and Skills

Consultation on the Draft Regulations Determining what Companies must Disclose in Pay Reports

28 September 2012

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

The Actuarial Profession
making financial sense of the future

Barry Walker
Executive Pay Consultation
Department for Business, Innovation and Skills
1 Victoria Street
London
SW1H 0ET

28 September 2012

Dear Barry

Consultation on revised remuneration reporting regulations

The Institute and Faculty of Actuaries welcomes the opportunity to comment on the proposals set out in the above consultation.

In this response we have concentrated on the aspects of the proposals that relate to the calculation of the remuneration disclosures related to pension benefits. Accordingly, the points we wish to make are as follows:

Question 1

The reference in regulation 7(5) to regulation 7(4)(a) does not appear to be correct.

The legislative reference to the HMRC calculation method is to the calculations underpinning the "annual allowance" test; as part of this calculation the pension entitlement at the start of a reporting period is uprated by inflation before comparison with the end year entitlement. Whilst we do not disagree with this approach (and it is consistent with existing reporting requirements) the consultation paper is silent on this point and refers to the "lifetime allowance" method.

The HMRC methodology which is cross-referenced relates to the increase in accrued benefits over the pension input period (as defined for each pension arrangement) ending in the relevant tax year. There may be different pension input periods for the various pension arrangements for a particular individual; if pension input period end dates are amended, one tax year can pick up the pension input from more than one pension input period from an arrangement. This does not seem appropriate for inclusion in a comprehensive remuneration figure in respect of the company's financial year.

We would also question whether the cross-reference to the HMRC method sufficiently well defines the calculation required in all cases, as problems have arisen with application of the HMRC regime (for instance where members are promised a 2/3rds pension if active at retirement).

The proposed regulations do not cater for cash balance plans or hybrid schemes – we note that the sections in Part 4 of FA2004 dealing with these types of arrangement are separate from the HMRC method (for defined benefit schemes) that is cross-referenced by these regulations.

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www.actuaries.org.uk

Question 2

We do not believe that the reporting costs in relation to the pension components of the disclosures will be significantly different to those incurred for companies subject to the Listing Rules. However costs may increase for those companies currently subject only to Companies Act requirements.

Questions 3 and 11

We believe that disclosure of the pension accrued during the year (net of inflation) as well as the accrued pension at the end of the year would aid understanding (and should apply to all defined benefit arrangements, not just final salary schemes).

In terms of early retirement, the reference to the *additional* pension payable may not capture the full picture. In general, payment of a reduced pension on early retirement would be expected to provide the same value to the director as the accrued pension payable at normal retirement age. Disclosure should therefore be required of any entitlement or practice of paying early retirement pensions before normal retirement age with no reduction for early payment or a reduction that is lower than the cost-neutral reduction, as well as of any additional pension payable on early retirement.

Question 8

We agree with the 3 possible approaches as set out in paragraph 67, namely the “HMRC method”, IAS19 and transfer values.

Both of the IAS19 and transfer value methods could be argued for, on grounds of consistency with the reported costs to the company and the amount the member could take as an immediate settlement from the scheme respectively. Whilst these measures will lead to different valuation factors from year to year reflecting market conditions, the degree of volatility would be reduced if it is the value of the increase in benefit each year (net of inflation) that is disclosed (as in the Listing Rules) rather than the difference between the values of the total benefit at the beginning and end of the year (as in the current Companies Act requirement). A further relevant point is that both methods rely on actuarial assumptions which (although subject in both cases to guidance) are set by the company (in the case of IAS19) or the Trustees of the scheme (in the case of transfer values). In the context of company reporting the use of IAS19 assumptions would therefore seem more relevant; whilst these assumptions do vary between companies the differences are less pronounced than for transfer values and the assumptions do not depend on factors such as the scheme’s investment strategy.

The proposed “HMRC method” with a fixed valuation factor of 20 would certainly be more straightforward to calculate from a valuation perspective (but see our comments under Question 1 above); however the use of a fixed factor ignores elements of actuarial value such as different levels of pension increases, spouse’s pensions, retirement age – as well as the age (and therefore true funding costs) of the member concerned. These drawbacks of the fixed factor approach may actually impair (rather than enhance) comparability between different companies and individuals.

Finally, we note the comment in paragraph 36 to the effect that the Government will work with the UK Listing Authority to consider whether the requirements of the Listing Rules need to be reviewed. We would further ask whether the general Companies Act reporting requirements should also be brought into a general review in an attempt to achieve consistency in pensions reporting across all UK companies.

We hope that the above will be helpful but if you have any questions, or would like to discuss any aspect of our response further, then please do not hesitate to contact us.

Yours sincerely,

Martin Lowes
Chair of the Pensions Consultations Sub-Committee
The Institute and Faculty of Actuaries

Institute of Chartered Accountants in England and Wales, The

28 September 2012

Our ref: ICAEW Rep 143/12

Barry Walker
Department of Business, Innovation and Skills
1 Victoria Street
London
SW1H 0ET

By email: Executive.pay@bis.gsi.gov.uk

Dear Mr Walker

Directors' Pay: Revised Remuneration Reporting Regulations

ICAEW is pleased to respond to your request for comments on *Directors' Pay: Revised Remuneration Reporting Regulations*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

Jo Iwasaki ACA
Head of Corporate Governance

T +44 (0)20 7920 8786
E jo.iwasaki@icaew.com

ICAEW REP 143/12

ICAEW REPRESENTATION

DIRECTORS' PAY: REVISED REMUNERATION REPORTING REGULATIONS

Memorandum of comment submitted in September 2012 by ICAEW, in response to Department of Business, Innovation and Skills consultation paper Directors' Pay: Revised Remuneration Reporting Regulations published in June 2012

Contents **Paragraph**

INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation paper *Directors' Pay: Revised Remuneration Reporting Regulations* published by Department of Business, Innovation and Skills on 27 June 2012, a copy of which is available from this link.

WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 138,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

4. This response reflects consultation with the ICAEW Corporate Governance Committee which includes representatives from the business and investment communities. The Committee is responsible for ICAEW policy on corporate governance issues and related submissions to regulators and other external bodies. The response also reflects input from the ICAEW Financial Reporting and Audit and Assurance Faculties and Business Law Committee.

MAJOR POINTS

5. It is important that companies provide clear and accessible information about remuneration to enable shareholders to scrutinise and challenge where appropriate (see ICAEW REP 111/11, our response to the Government discussion paper *Executive Remuneration* published in September 2011). We have also strongly supported the launch of the FRC's Financial Reporting Lab and contributed to the development of its project report on a single figure for remuneration. We however believe that initiatives to produce a single remuneration figure should be supported by efforts to ensure that underlying components of the single figure are also recognised and measured in as simple and understandable a way as possible.

6. The Directors' Remuneration Report Regulations originally introduced in 2002 have undoubtedly provided a useful starting point in assisting users of annual reports. However, there are criticisms today that more extensive pay disclosure has led to a 'ratcheting up' of directors' pay; conversely there is evidence that suggests otherwise. We suggested in our previous response on executive pay that there should be research, to help establish definitively whether the benefits of increased disclosure in terms of improved performance have outweighed potential ratcheting.

7. Another criticism of the current disclosure regime is its complexity which can obscure key messages. We believe that the revision of the remuneration reporting framework provides a great opportunity for the Government to inject clarity into remuneration reporting, and we note that there are potentially useful disclosures: for example consideration of remuneration in multiple scenarios and the services received from remuneration consultants and the related fees paid to them. However, we must also be mindful that regulations including this proposal would not be a substitute for good governance and best practice reporting.

8. We believe that pay should reflect the value the director becomes entitled to in relation to the performance for the year. Although some improvements have been made, we believe that this could be further enhanced in the proposed Regulations. In order to develop a meaningful reporting framework for a single figure disclosure, it is important to be clear how the three key features of this figure (page 22) are applied in practice. This is particularly relevant in terms of recognising and measuring benefits for which entitlement and receipt do not fit into a single reporting period: namely claw back arrangements, pension entitlements and long term incentives. We set out our concerns and views in our response below to your specific questions concerning these areas.

9. We encourage the Government to introduce a review clause into any new legislation, so that after three years there is an in-depth review to ensure that the adopted solution is having the appropriate impact and there are no adverse, unintended consequences of its operation. The Government should also demonstrate its commitment to better regulation by addressing points made in this letter about complexity in the drafting of these Regulations.

OTHER COMMENTS

The proposed legislation should be clearer

10. Remuneration reports are currently complex and hard to understand and compare, even for those experienced in using remuneration data. We support the Government's objective to develop a single total figure for individual directors' remuneration provided that it is clear, consistent and meaningful as to what is to be disclosed and the basis to be used for recognition and measurement. Furthermore, to help facilitate effective and consistent implementation of the requirements, the Regulations need to be drafted in an unambiguous manner and the guidance that the consultation calls for must be published in time for initial adoption. Our detailed comments are set out in the Appendix.

How remuneration reports fit with other reports and minimise duplication

11. The purpose of the remuneration report is to help shareholders' decision-making over their annual advisory vote on the implementation of pay policy. It is therefore important that the proposed Regulations should enable shareholders to have comprehensive, easily understandable information on remuneration which is different from increasing clutter.

12. It is therefore important to consider the role of the remuneration report within the context of the future reporting framework. In due course, there might be a strategic report, a remuneration report and an annual directors' statement in addition to the financial statements and it is unclear how these fit together to complement each other and benefit shareholders. Although remuneration reporting is considered to be a higher priority by the Government, we do need to understand the full picture of the future reporting framework, especially as it is stated that 'the Government intends that all changes to the reporting framework should take place at the same time (paragraph 34 of the Consultation).'

13. A practical example of potential inconsistency or duplication is the requirement to produce a summary statement from the Chairman of the Remuneration Committee setting out key messages on remuneration and the context in which decisions have been taken (paragraph 23 of the Consultation and paragraph 2, Part 2 of the draft Regulations). It seems that this might be located within both the remuneration report and the strategic report which may lead to duplication or inconsistent practice.

The content of the summary statements is unclear

14. It is unclear what information should be present in the summary statement. While the consultation observes that many companies already produce a statement from the chairman of the remuneration committee, these statements often do not cover the full scope of the remuneration report. It would be helpful if paragraph 2, Part 2 of the draft Regulations were reworded to set out the type of information sought in the summary statement, for example: *The directors' remuneration report must contain a statement by the director who fulfils the role of chairman of the remuneration committee setting out significant decisions taken in developing and applying the remuneration policy and the context in which decisions have been taken*. This may be supplemented by further guidance in the explanatory note. In this way, prescription may be avoided while providing a useful navigation aid for shareholders.

Support for aligning Listing Rules with the revised Regulation

15. In paragraph 36 of the Consultation the Government states that it will work with UKLA to consider whether the Listing Rules need to be reviewed. Rather than duplicating requirements, we suggest that Listing Rules should refer to relevant sections and Schedules of the Companies Act 2006 so that quoted companies not covered by UK Company Law are subject to an equivalent reporting regime.

Different schedules of the Regulation should be applied as appropriate

16. The Regulations are intended to revoke and replace Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) and replace the existing disclosure requirements. Our understanding is, however, that Schedule 5 will continue to require aggregate disclosure of information about the benefits of directors of quoted companies.

17. We strongly suggest that either Schedule 5 should apply only to companies not within the scope of Schedule 8 or that the requirements should be aligned. Differences between the aggregate requirements for unquoted companies and for companies within the scope of Schedule 8 should be eliminated as far as practicable to improve the overall quality of the regulations.

18. Currently, there is no proposal to exempt quoted companies from Schedule 5. However, if quoted companies complied with Schedule 8 while Schedule 5 applied to unquoted companies, this would simplify the regime. Schedule 5 requires different disclosures in respect of certain elements of the pay package from those required in the directors' remuneration report; it would be good to remove this inconsistency. Furthermore, Schedule 8 defines 'emoluments' in a similar but not identical way to 'remuneration' in Schedule 5. These differences in definitions and disclosure requirements between the two Schedules will therefore continue to cause complexity and confusion for both preparers and users of information.

19. Finally, some disclosures included in existing Schedule 8 should remain as they would be useful in the proposed Schedule 8. For example, in the proposed Schedule 8, disclosure of payments for loss of office applies only to persons who have served as directors of the company at any time during the year. The existing Schedule 8 requires disclosure of awards made to any person who has or previously had been a director of the company, thus including payments made in the year following the retirement of a director. Similarly, the proposed revised Schedule 8 should include 'sums paid to third parties in respect of a director's services'.

Transitional arrangements

20. Transitional arrangements should be clearly explained in a relevant statutory instrument that introduces the binding votes so that companies fully understand the effect of decisions that take place subsequent to the proposed Regulation coming into effect. The Enterprise & Regulatory Reform Act provides transitional arrangements and these could be useful in the context of this Regulations. Relevant illustrations would be helpful, such as:

- a situation where the vote on the policy part does not happen until the following AGM at which the vote gets rejected; and
- what would happen to payments made to directors in the period from the new Regulations coming into force until the vote is cast.

RESPONSES TO SPECIFIC QUESTIONS/POINTS

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

21. As noted above, the draft Regulations need to be clearer and it must be possible to read them as a stand-alone document. Currently they are written in a manner that is difficult to understand without referring to the consultation document. Please also see our drafting suggestions as appended. This will also help the government to draw out the mismatches between the consultation document and the draft regulations as the two are not aligned in places.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

22. We do not collect specific information to be able to respond to this question with precise figures. However, it would be inappropriate to assume in the impact assessment that a number of requirements are already best practice and therefore there will be no additional cost at all from them. Given that these are new requirements, there will be many companies for which these proposals do not represent current practice and may well add cost.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

23. Yes, it would be a practical and informative approach. However, for effective application, key concepts need to be clearly defined. For example, there should be a definition for ‘performance metrics’ preferably linking the achievement of strategy and pay.

24. Annex A is presented as a mock-up policy table setting out all the elements of remuneration. While it is useful to have a required format presented visually, the illustrative wording could be more specific to give insight into how strategic goals have been advanced by the performance as measured by the KPIs. There is also a risk of companies copying similar words into their own reports if the table remains generic.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

25. Yes, we believe that it is a practical and informative approach. We have however detailed comments.

26. The proposal in paragraph 46 of the Consultation and paragraph 21, Part 4 of the draft Regulations requires 'all existing contractual provisions that relate to directors' remuneration' to be included in the policy report. This disclosure may become lengthy and complex. We suggest that a summary or explanation could be sufficient and equally useful.

27. The illustrative graph between paragraphs 47 and 48 of the Consultation is misleading as it is. For example, base salary usually is expected to remain relatively static across the three scenarios, while the variable elements such as bonuses would vary although not necessarily in direct proportion. Yet the graph appears to suggest that the ‘fixed’ elements would in fact vary in line with performance along with other variable elements of pay. This makes the comparison difficult or even misleading. Percentages shown appear to be distorted. If a similar graph is to be produced in guidance material to the final Regulations, it should be thoroughly reviewed.

28. Paragraph 49 of the Consultation and paragraph 24, Part 4 of the draft Regulations discuss reporting of percentage changes in profit, dividends and the overall pay. While paragraph

24(2), Part 4 of the draft Regulations states that these terms have the same meaning as in the statutory accounts, it would be clearer to state that these are consistent with IFRS as that is familiar to companies to which the Regulations apply. Furthermore, it would be useful to have further clarification, as to:

- profit: this should be profit after taxation, as this is the only profit measure that will be consistently found in IFRS based financial statements; and
- overall expenditure on pay: this should include all expenditure including finance cost, share-based and other non-financial pay, amounts earned under long term incentive plans (LTIPs), the cost of pension commitments measured in accordance with IAS 19, and employment taxes such as NICs.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

29. We support the disclosure of the principles on which future contracts are to be entered into or future exit payments negotiated. However, the proposed level of disclosure does appear rather prescriptive. It is by no means certain that real exit agreements will be structured in the way envisaged by the proposed disclosure as they will usually be bespoke arrangements. It would be better for the disclosure to be more flexible to allow relevant factors to be disclosed to suit the individual agreements a company has in place. We would also support the disclosure of any exit payments actually made and the rationale for such payments.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

30. Good management should be sensitive to the broad environment within which the company operates and seek views on a range of issues including remuneration policy when making important decisions. In this context, employee views will often be taken into consideration.

31. We do not believe any prescription in this area is required and current requirements are likely to lead to a misleading or boilerplate disclosure. For example, In terms of the disclosure in paragraph 30(1), Part 4 of the draft Regulations, factors such as exchange or local inflation rates can potentially distort comparison. On the other hand, the option to identify an appropriate comparator group is easy to manipulate. If the information is to be meaningful and not subject to abuse, further consideration will be required.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

32. No. We believe that the Government's intention is that the single figure should reflect the value the director becomes entitled to unconditionally in relation to the performance for the year. However, the wording of the Regulations is not entirely clear and we are concerned how the requirements will be implemented. This is particularly relevant where performance and the vesting of the award relate to periods that are not coterminous.

33. For example, bonus vested shortly after the reporting year end based on the performance during the year would be included within the single figure of the subsequent year. Another example may be that in a case of a long term incentive plan that runs over several years, the entire amount would be recognised and disclosed in the final year when vesting takes place. If so, the proposed approach would not help investors to see a fair picture of reward that facilitates a stronger link between pay and long term performance. The one-off nature of disclosure of amounts awarded in the reporting year may prompt companies to disclose pro forma numbers showing the spread over the period of accrual as otherwise the numbers may be distorted by the timing of performance obligations. If a major concern of the Government is 'short-termism' it would be better to have visibility over the value of a long term incentive plan that accrues in the year.

34. The Government may wish to consider the inclusion of a table or figure that illustrates how the value of long-term benefits changes over the year. These values can vary significantly and an appreciation of such variation is important to understanding the nature of remuneration arrangements.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

35. Our preferred approach is to use the transfer value, which measures the value of pension benefits to the director: in other words, the amount it saved him or her in the year from paying to buy an equivalent pension in the market. We also see the benefit of using the HMRC methodology for its simplicity and consistent applicability, although the proposed use of a multiplier of 20 is somewhat arbitrary and may be subject to challenge.

36. For these purposes, we do not support an IAS 19 based measurement of pension benefit. It would be measuring the cost to the company rather than the benefit to the director. Further, discount rates are subject to volatility which, while useful in understanding the risks pertaining to a defined benefit pension scheme, would have little meaningful connection with an individual executive's remuneration in the year.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

37. Claw-back arrangements can have a significant impact on the overall figure and it is appropriate to reflect the effects of any claw-back in the single figure of the reporting period when this occurs. The conditionality this reflects is clearly significant to an understanding of the link between pay, performance and the personal risk a director bears. It should be noted that in some cases rights of claw-back may defer the vesting of rights to remuneration, which in turn will cause deferral of the accounting charge.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

38. Yes, it could be commercially sensitive to require companies to publish full details of performance metrics and the provision of an exemption may be sensible. However, there should be some criteria for when the exemption might be taken and a requirement to explain why such a metric is not disclosed. Otherwise this flexibility may be abused.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

39. Yes, it appears reasonable.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

40. Yes, they should continue to be disclosed. We support the use of face value provided that the term 'face value' is clearly defined in the proposed Regulations to enable consistent calculation. We suggest that if the award made is equity based it should refer to the market value at the reporting date. If the market value is not readily available, it should be calculated according to an appropriate model, such as proxy market value.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

41. Provided that user needs are satisfied, we support the reporting requirements regarding directors' interests being simplified.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

42. In principle we are supportive of the use of a graph to give shareholders an 'at a glance' view of how well pay compares with performance. It is important however that the readers of the report are reminded that a single figure is unlikely to give the whole picture of how executives are remunerated. Indeed, CEO (or equivalent) pay based on a long-term success of the business such as increases in market share and customer loyalty or technological breakthroughs may look disproportionate unless readers appreciate that Total shareholder return (TSR) would take time to reflect these types of success. However, we note that the benefit of using CEO pay lies in its simplicity in contrast with, for example, an aggregate figure of total pay for directors which can fluctuate easily according to the number of persons included.

43. TSR alone may not be an appropriate measure to compare CEO pay. This is because changes in general market conditions significantly affect TSR: the same rise in CEO pay would look understated in a bull market where TSR is expected to rise compared to the same rise in a bear market where TSR is likely to be depressed. It would therefore be useful to incorporate in the graph a measure to mark company TSR against the stock market as a whole, such as FTSE 100 TSR.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

44. No. While the audit could be extended to the disclosures proposed in paragraph 14, there is no evidence of companies erroneously reporting such information and therefore the cost of such assurance is likely to outweigh the benefit; in any case all that the auditor could do would be to check the information to the disclosures made to the company under DTR 3 as they would not be able to directly confirm shareholdings with directors, nor to demand nominees disclose who they were acting for. The remaining sections of the report are mostly forward-looking statements of policy, and there would be no objective criteria against which to verify such statements. They will, however, be read by the auditor in accordance with his or her duty under International Standard on Auditing (UK and Ireland) 720 and therefore, whilst the auditor will not be required to verify the information contained in the report, the auditor will be required to take action if they become aware of an apparent misstatement or inconsistency with the audited financial statements.

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APPENDIX

Detailed drafting comments

- Part 6 defines terms that do not appear to be used in the other parts of the regulation. For example, 'emoluments' which includes bonuses as well as sums paid by way of expense allowances and 'compensation' which includes benefits paid otherwise than in cash which are the estimated money value of the benefit. However, disclosure is required of 'all taxable benefits' which appears to be an undefined component of emoluments which includes both sums paid by way of expense allowances and the estimated money value of benefits paid otherwise in cash. We would like the term clearly defined. Also it appears to imply that benefits that are not taxable are exempt from disclosure requirements and this point needs to be clarified.

- It is unclear whether paragraph 5(b) (ii), Part 3 applies to amounts that do not remain within a share plan such as those that are re-invested in additional shares or otherwise only received at vesting. It is not clear why only dividends are disclosed and not, for example, interest received on a scheme that involves a loan rather than shares. We question whether these amounts should be aggregated with taxable benefits or included with the long term incentive plans to which they relate.

- Paragraphs 5(d) and (e), Part 3 seems unduly complex. We are not clear, for example, if year 1 is the reporting period, whether the bonus relating to performance (and presumably service) in year 1 but actually awarded and paid in year 2 when the results from year 1 are known should be included in year 1 since it was not in fact awarded in the reporting period.

- Paragraph 6(c) (ii), Part 3 may result in double counting for a pension contribution that was disclosed in year 1 because it was payable in respect of year 1 and then paid in year 2. The drafting should be clarified to avoid this interpretation.

- Paragraphs 5(e) and 7(3), Part 3 refer to schemes with service or performance conditions that cannot be fulfilled within a single financial year. The definitions of service and performance conditions have been subject to much interpretation where they are used in IFRS 2. If the intention that these terms should be interpreted as they would be in IFRS, a question may arise when an amount should be disclosed if it is payable under a scheme that is determined based on performance over a 3 year period to year 3 but vesting or actual payment is deferred to year 4 and subject to a service condition. It may be that the intention of paragraph 6(d) is that the disclosure should be made in year 3, but it is not clear that 'deferred' relates to a final payment subject to service conditions. Some schemes have conditions that are not clearly service or performance related, for example SAYE schemes require that the employee makes regular payments into a savings scheme. We would like some clear explanation.

- The calculation required by section 6(e) (ii), Part 3 is confusing. It appears to aggregate a number of shares with a cash amount of dividends received and then multiply this total by the market value of the shares (XY). Since this relates to vesting of an award that relates to performance over more than one year, it may be better for the number of shares to be estimated based on cumulative performance, rather than performance in the current year (unless the scheme vests over time). Presumably the idea is that any dividends that result in additional shares awarded should be included in the calculation, but this seems to imply that dividends already disclosed in 5(b) (ii) would be counted twice before they are multiplied by the market value of shares (XYZ).

- Please explain what is meant by 'full vesting' in paragraph 6(e)(iii), Part 3 and how the requirement would be applied where an award has partially vested so at least part of the value can be determined based on the market values at particular date(s).

- The reference to paragraph 7(4) (a), Part 3 of the draft Regulations in paragraph 7(5) should be to paragraph 7(4).

- In some cases performance conditions for share and other schemes may not relate only to the performance of the company. 'Company' should include a division, a subsidiary or possibly the parent depending on which the director works for. In addition, the performance condition could relate to an individual financial or non-financial objective, for example based on exhibiting certain behaviours. This may have implications for confidentiality.

- Please clarify whether the 'person's accrued benefits' in paragraph 10(2), Part 3 of the draft Regulations is intended to be the same as accrued benefits in Schedule 5 paragraph 2 which applies only to unquoted companies because the description is similar but not identical. It is unclear if disclosure is required if benefit receivable by a director would be reduced in the event that the director retires early.

- Presumably the analysis required in paragraph 11(a), Part 3 of the draft Regulations is that set out in paragraph 5, which could be usefully clarified by defining 'element.'

- It is not clear what is meant by 'threshold performance' in paragraph 12(b) (v), Part 3 of the draft Regulations.

- Where the data have not been collected using the definitions and requirements of the Regulations in the past, we suggest that there should be suitable transitional provisions for 10 year performance and pay graph rather than to require all companies to cover full 10 years in the first year of implementation.

- It is unclear what else is necessary to constitute a 'fair method' in accordance with paragraph 13(4), Part 3 of the draft Regulations other than following the required assumptions.

- The point in time at which the number of shares held by a director (or a former director) is not included in paragraph 14(b), Part 3 of the draft Regulations. Presumably this is either at the year-end or the date of resignation, but this should be clarified. It should also be clarified how uncertainties about the number of shares subject to performance conditions or conditions other than performance conditions should be addressed.

- Paragraph 16(c), Part 3 should define 'substantial.'

- Expressions such as 'the last policy part' in paragraphs 19(e) and 'performance conditions pay' in 20(b), Part 4 need to be explained.

- If a company has multiple, long term incentive plans which will vest in different years, it is unclear how paragraph 22, Part 4 of the draft Regulations should be applied, ie, over what future period should the company set its remuneration expectations, particularly if they are likely to be different for different years.

Institute of Chartered Accountants of Scotland

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September 2012

Please return completed forms to:

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET
020 7215 3930
executive.pay@bis.gsi.gov.uk

Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
✓ **(Professional body for accountants)**	**Other (e.g. consultant or private individual)**

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

We support the drive for greater simplicity, consistency and comparability. Overall, our view is that a balance should be struck between what has to be included in the two reports and the exact content, and how it should be presented. These proposals tend to stray too far into a prescriptive approach. We strongly believe that the focus for legislation is best at the principles level and the FRC is the best placed (and credible) body to manage the detailed application and adherence by companies through supplementary guidance. Specific examples where a less prescriptive approach is advised are highlighted in our response such as question 4 (identifying factors to compare directors pay), question 6 (employee views), question 10 (performance metrics) and question 14 (comparisons with total shareholder return).

We suggest the approach to a single total figure should also respect the following in addition to the three key features[1]:

i) Ensures consistency of disclosure with published accounts for transparency and good practice
ii) Represents the cost to the company at the financial reporting date, being of interest to shareholders, rather than benefit to the employee which may be out with the reported period and more subjective
iii) Represents the in-year costs rather than a mix of annual and cumulative amounts.

Single total figure

We agree that the scope should include all those who served as a director in the period. It should be clarified that this should include temporary appointments and those acting up.

Salary & fees
We suggest adding “allowances” for completeness to the definitions table and to legislation (Part 3(5)(a)). An example is a housing allowance paid on top of basic salary.

Benefits
For completeness, the definition should include both cash and non-cash benefits paid in respect of the director’s employment, not included within other columns. In addition, where the company/ pension fund is picking up an additional tax liability (which would normally be a personal tax liability) this should form part of the single remuneration figures. This would provide a more complete figure for the cost to the employer.

[1] Consultation paper paragraph 61

Bonuses
The legislation at Part 3 (6)(d) should be expanded to include preferred valuation method if non-cash payments.

LTIP/share awards
The proposal to calculate a current market value for equity awards does not match the cost of the award with the period that the director renders service (nor reflect the risk of the award to the director). Furthermore, it could potentially give the wrong impression of remuneration and performance. For example, if a director is awarded options in year 1 worth £100, and by the time they vest in year 3 they are worth £200; this would hopefully reflect the fact that the directors have done a good job at managing the company over three years, rather than just the fact that they had received options worth £200 in year 3.

The approach would also result in inconsistency between the remuneration report and the accounts which would be difficult to explain in a clear manner. For consistency with disclosure methods in the published accounts, we suggest that the grant-date fair value approach is a more meaningful approach to determining the 'cost to the company' of awarding shares/options, at the point they are granted (IFRS 2).

Observations on the draft legislation
In the legislation for LTIP/ schemes Part 3 (6)(e), the calculation in (ii) & (iii) shows inconsistencies, being market value of shares at the date of vesting for XYZ or average market value of the last quarter if not vested for XYZ. It would be clearer to maintain a single approach and maintain consistency with the disclosure of share values in the accounts.

Secondly, paragraph (iii) appears to be a subset of (ii). If this is the case, it would be clearer to write (ii) "(*XYZ) multiplying the total arrived at in (XY) by the market value of shares at the date of vesting OR ~~(iii)~~ for the purposes of the calculation in subsection (XYZ) where full vesting is not achieved by the date on which the remuneration report is signed off…*"

It would also be relevant to include a statement explaining any conditions around the retention/ sale of shares.

Pension

The BIS proposal mixes methodologies for the pension benefits amount in the Single Figure Table by including company contributions for money purchase (or defined contribution "DC") schemes and value of benefit achieved for defined benefit (DB) schemes. This is confusing and likely to create distortions in the final remuneration figure for directors on different schemes. Additional narrative would be required to explain to readers the implications of the different pension schemes on the single total figure.

For consistency and to provide a more meaningful figure, we believe that the approach for both DC and DB schemes for the Single Figure table should be harmonised. The starting objective should be that the figure represents the cost to the employer, rather than benefit to the employee (being the principle noted in our response to Q1). As such, only the employer contributions for all relevant pension schemes should be recorded in the Single Figure Table.

The inclusion of the accrued in-year values only represents the benefit to those Directors on DB schemes so it is not only inconsistent across schemes, but inconsistent in terms of the purpose of the single figure (to show actual pay). Any disclosure of DB in-year values for Directors would sit more logically out with the Single Figure Table, in a separate note. However this would be a bit one-sided as Directors on DC schemes do not have this additional disclosure.

As a comparison, whilst other public sector accounts show a pension benefit / transfer value (see footnotes 2[2] and 4), these are represented in a separate table and are not trying to fit a meaningful Single Total Figure. The local government DB scheme disclosures notably include in-year pension contributions.

We believe that for a meaningful pensions figure within the Single Figure Table only employer contributions for all pension schemes should be included. This would reduce complexity, improve comparability and remove the need for a more complex (HMRC) valuation methodology.

Definitions should cover all the different types of pension schemes for clarity. Further guidance including scenarios and examples would provide clarity.

Observations on the draft legislation
The draft legislation Part 3(6)(c)(ii) notes that measurement includes company contributions for the relevant financial year or payments made by the company in that year for another financial year. This appears to mix payments for different financial years which risks overstating the annual single total figure and is inconsistent with the measurement approach of other headings. Further clarification is required.

Exit payments
This figure should form part of this table and the single total figure, where applicable. This would enhance completeness better than a separate disclosure[3] and would be consistent with presentation in the published accounts of other sectors[4].

To reduce duplication, a statement at the foot of the Single Total Figure table

[2] http://www.scotland.gov.uk/Publications/2011/09/29132216/0
[3] Consultation paper paragraph 59
[4] http://www.scotland.gov.uk/Resource/Doc/1070/0116807.pdf

should confirm whether the exit payment has been calculated according to the Policy[5]. We are not convinced that a further break down of the amount is required if the Policy section adequately explains how this has been calculated. A simple total could then be more easily included within the Single Total Figure table.

Areas requiring further information

Exit payments – the policy and payments made refer to different scenarios and how performance is taken into account. Further guidance is required on the types (including early retirements, ill-health, dismissal, redundancy etc.) and application of exit policies in different scenarios, with good practice examples to help ensure that the level of detail and consistency of approach are made clear for the purposes of reporting and interpretation.

The legislation does not state how the governance process for the binding and advisory votes will interplay with the regulatory challenges which have changed remuneration policies of companies over the last few years. As an example, the implementation of the FSA Remuneration Code in 2010 meant that banks had to react quickly to update their remuneration policies and approach, and implement the new regulatory landscape within weeks of the regulations being published. All this happened prior to the next Annual General Meeting. How these types of activities are addressed in the future and how this would impact on the timing of the votes and the specifics that need to be disclosed, has not been made clear in the consultation document. This requires further review and provision of clear guidance.

Other areas where guidance would help to improve understanding, consistency and ensure an appropriate level of detail:

i) Scenarios, sample disclosures/ good practice examples, especially for performance, differences in performance versus financial years, pensions, LTIPs, variable pay and exit payments (examples of detailed scenarios for a different sector are available at footnote 4),
ii) How to treat adjustments and explanatory notes (this should be consistent with the accruals concept as used in the financial statements and minimise under and over statement of current period pay),
iii) Clear and precise methodology for calculation of the single sum disclosures with examples,
iv) Disclosures on advisers to the Remuneration Committee. Not all use external advisers. Further guidance should help to clarify the exact content and description of the disclosure including the type of fees and services which would fall under the scope of the reporting and how it is determined, those who are advisors to the Committee versus advisors of the Company when the outcome is used to provide information to be provided to the Committee,

[5] Consultation paper paragraph 25/26 of draft legislation

v) HMRC methodology (see also our response to question 8),
vi) Interplay with other regulatory challenges.

Additional clarification on the following would assist:
vii) A director may choose to pay AVCs out of his salary, this is a personal choice and should not need to be disclosed (as his salary is already shown),
viii) Confirm that accrued benefits relate only to the company scheme (and not other schemes the individual may be a member of either privately or through previous employers).

In conjunction with greater disclosure of actual pay, the Policy Report needs to help focus greater attention and control (including shareholder approval) on negotiation of contracts to control against unjustified pay ratcheting.

Finally, the scope of implementation is left open for companies to come to their own decision as to whether to adopt any/all of the proposals prior to the legislation being enacted in October 2013 which may provide certain levels of confusion/inconsistencies, particularly if areas requiring further guidance and clarification are not resolved before the main period of reporting (being H1, 2013).

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

We agree with the assessment by BIS that there are some quoted companies already adopting much of these disclosures on a voluntary basis for whom work will be to refine their disclosures rather than introducing completely new material.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We agree with this approach.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Introducing disclosures on remuneration opportunity in different scenarios is useful however there are some practical issues to consider for more effective implementation. We support the intention to compare pay to performance but have concerns that the particular benchmarks proposed and annual percentage movements can risk focusing on short term measures and changes which is inconsistent with current thinking on the benefits of a longer term view of performance and remuneration[6].

In addition, directors pay in the year could be affected by many variables besides just "profit" if there is a balanced scorecard approach to bonuses. Flexibility and discretion is required to provide more meaningful comparisons. Another scenario could be if pay includes LTIP's which may vest due to an excellent performance over two years and a modest one in year three. The director would receive a large pay figure as a result of the vesting which compares to a modest profit growth figure in year 3 and will need explanation.

Our preference is that the legislation is not prescriptive in its identification of appropriate performance benchmarks but a responsibility is placed on the Board to identify their own most appropriate benchmarks for directors' remuneration to demonstrate alignment with performance and fairness. A narrative explanation would help provide further meaning and context.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We agree with this. Further guidance is required as noted in the response to question 1.

[6] See Kay Report page 13, recommendation 15.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

The proposal to include a statement of how employee pay and conditions were taken into account supports the principle of fairness[7]. However, the main thrust of proposals for employee consultation and comparison metrics[8] has failed consultation so the residual proposals of extra narrative if a company has voluntarily done something similar, is adding clutter to the report. This is likely to lead to boiler plate responses and not adding much value.

Improvements already noted in the consultation paper should provide a more effective structure to encourage a greater focus on fairness, in particular greater transparency and disclosures, explaining differences in the payment policy between directors and employees, comparisons with pay and performance and the shareholder vote (views from a group who are in a position to compare performance with remuneration as well as having the responsibility).

The responsibility for a remuneration policy rests with the Remuneration Committee, who are structured to include independent non executives. Employees are not independent. They may however, also be shareholders and can contribute views using that route.

Although we appreciate the intention for proposals in paragraph 28 and 29, there is insufficient evidence around its effectiveness and as such, should not be included in the legislation. Our preferred approach would be for the Remuneration Committee to explain how it ensures balance, fairness and alignment with performance in its remuneration policy; and in the implementation report, to demonstrate that this has been achieved. Any further employee comparison (such as pay medians) or engagement should be on a voluntary basis.

The proposal to show the percentage increase in pay of the CEO to wider employees[9] is valid for those working in the same country and subject to the same inflationary conditions however, it is likely to encounter difficulties for companies working internationally so some flexibility is welcome.

The focus on CEOs suggests that they are the highest remunerated but this is not always the case. In recognition of this, some organisations voluntarily provide details of the most highly paid in the organisation if not the CEO or board member. There is a precedent for this in Scottish local authorities[10]

[7] Paragraph 27 in the draft legislation
[8] Paragraph 28,29 in the draft legislation
[9] Paragraph 30 in the draft legislation
[10] http://www.legislation.gov.uk/ssi/2011/64/pdfs/ssi_20110064_en.pdf

whose Remuneration Reports include (the equivalent of) directors as well as those earning above a certain threshold (by name and post). There is also a table of general disclosure by pay band of the aggregate numbers of staff earning above a certain threshold.

Some quoted companies include these additional disclosures on a voluntary basis[11]. Examples include RBS[12] and HSBC[13] (8 highest paid senior executives by number). We believe it is not unreasonable to extend disclosure to this group in the Remuneration Report for transparency and consistency. Disclosure of post (as a minimum) would be more informative than number. Voluntary disclosures are also provided for bands (HSBC). Guidance could help disseminate best practice and generate greater consistency and transparency of this group across quoted companies.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Yes, subject to concerns noted in our response to question 1.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The intention to minimise volatility is appreciated, albeit the approach is inconsistent with how other organisations report pension benefits[14] and methodologies used for valuation in the published accounts which could reduce transparency.

Although this method may provide a useful first order approximation, buy-out costs vary with age and expected mortality as well as annuity rates (which vary annually with gilt yields, quantitative easing etc.). Consistency and neutrality should not be substituted for a prudent estimate of the full in-year cost, including past benefit revaluation. Overall we are not sufficiently

[11] as proposed by the HM Treasury consultation paper in December 2011 (http://www.hm-treasury.gov.uk/consult_merlin_remuneration_disclosure.htm)
[12] http://www.investors.rbs.com/download/report/Annual_Report_2011.pdf
[13] http://www.hsbc.com/1/content/assets/investor_relations/hsbc2011ara0.pdf
[14] http://www.scotland.gov.uk/Resource/Doc/1070/0116807.pdf & http://www.legislation.gov.uk/ssi/2011/64/pdfs/ssi_20110064_en.pdf

persuaded that this provides a meaningful number for users and meets the objective of a true and fair view. This is of particular concern given the proposal for the pension entitlements figure to be subject to audit.

One of the implications of the HMRC method is that the Remuneration Report would also require additional narrative notes to explain any significant/ unusual movements which may arise say when annual allowances are exceeded and contributions not paid (draft legislation Part 3 (6)(c)(iii)&(iv)).

Further information in the consultation paper on the HMRC method would have been helpful. Some ambiguity was noted which needs clarified. For example, the relevant legislation (s234 of Part 4 of the Finance Act 2004) uses a multiplier of 10 (which has been updated to 16). A separate calculation would therefore be required for tax purposes if a different multiplier of 20 is required to calculate the pension benefit.

Secondly, the definition of the HMRC method per the proposed regulations suggests that it is to be used to calculate in-year increases (if any) to a lump sum entitlement. However elsewhere in the proposed regulations there is a suggestion that this is used to determine increases in pension entitlement acquired in the year. Finally, if the method is to be used to determine the lump sum, it is not clear how this is possible as in the formulae the lump sum is a ‘given’ not a figure to be calculated.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

This is a sensible approach to avoid over stating remuneration. The amount should be separately disclosed and explained. This needs to be clearer in the legislation Part 3 (section on single total figure of remuneration) to be consistent with the consultation paper paragraph 73.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We support the intention to link directors’ pay and directors’ performance more clearly, however there are concerns that this is a commercially sensitive area and in practice, one of the unintended consequences could be to change the metrics to focus on less sensitive areas of the business. To get round this, disclosures could be maintained at a more general level. By moving towards a binding vote on the remuneration policy, major shareholders should be able to get the details they need through private discussions with the company (or threaten to vote against).

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

No, please see our response to question 1.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We support the expected value methodology on the grounds that this is what the company anticipates the director will receive. We appreciate that the calculation of this value requires a number of assumptions to be made but we believe this to be better than a value which is not reflective of what the company expects the director to receive. These assumptions could also be disclosed and supported by narrative explanation.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We support efforts to align with the Listing Rules.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We have concerns over the requirement for Total Shareholder Return (TSR) as a metric for all quoted companies. Not all companies are valued on earnings; some such as house builders and utilities use assets, others may use return on capital employed (ROCE) or sales as a key performance measure. In addition a company's strategy can change in 5-10 years so the metric may need to change to keep pace. We would prefer a company to select its own most appropriate metric to measure company performance. This should combine short and longer term

measures and form some sort of triangulation of the comparison. The proposed legislation is too prescriptive which risks generating disclosures that are not a fair reflection of company performance.

See our response to question 6 on the focus on CEOs.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

Accountability for the Remuneration Policy and Report and sign-off arrangements should be clarified and formalised (for example including responsibilities to select appropriate performance benchmarks and achieving fairness).

Investment Management Association, The

Investment Management Association

28 September 2012

executive.pay@bis.gsi.gov.uk

Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET

Dear Mr Walker

DIRECTORS' PAY: CONSULTATION ON REVISED REMUNERATION REPORTING REGULATIONS

IMA represents the asset management industry operating in the UK. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of £4.2 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (for example, pensions and life funds), private client accounts and a wide range of pooled investment vehicles. In particular, the Annual IMA Asset Management Survey shows that IMA members managed holdings amounting to around 34% of the domestic equity market.

In managing assets for both retail and institutional investors, IMA members are major investors in companies whose securities are traded on regulated markets. How the executive directors of those companies are incentivised can be an important driver of company behaviour and we recognise measures are needed to address excesses in executive directors' remuneration. Currently many remuneration reports can be complex such that it can be difficult to interpret them and make meaningful comparisons. We therefore welcome this consultation in seeking to improve transparency so that a company's future pay policy is clear and easily understood, and that there is a clearer link between pay and a company's strategic objectives and performance. We set out in the attached our answers to the questions raised and our key points below.

- The regulations are complex and certain of our members consider that the prescriptive nature of the proposals mean that there is a risk that remuneration reports will become even longer and include more boiler plate and standardised language. Much of the detail should be contained in guidance and we support this being developed by the FRC. It would also be helpful if BIS undertook to review disclosures after a suitable timeframe, say two or three years, to see whether the policy objective sought has been achieved (question 1).

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- Certain additions should be made to the table of the key elements of pay policy such as: the policy on the remuneration of new executive director recruits, including those from overseas; the extent to which ESG considerations are taken into account in setting pay policy; and, given the sensitivity, the policy on disclosing performance targets achieved in the implementation report. Moreover, given that an individual director's remuneration varies according to their particular responsibilities, there should be a separate table for each executive director and the tables should be disclosed every year – even when remuneration policy has not changed and is not subject to a vote so that investors can continue to review the situation (question 3).

- The policy report looks forward and is subject to a binding vote. The implementation report looks backward on how the policy was effected in practice and is subject to an advisory vote. However, this distinction is not necessarily followed in the detail. For example, it is proposed that the relative spend on remuneration, profit and dividend, and the percentage increase in the pay of the work force and the CEO are included the policy report. It would be more meaningful if these were included in the implementation report in that they relate to the past (questions 4 and 6).

- Consistency is essential in reporting a single figure for each director's remuneration which should be accompanied by narrative that explains its components and how it has developed. In the figure, long term incentive plans should only be recognised in the final year in that reflecting the amount the director becomes entitled to for the year would involve assumptions and predictions as to, for example, the vesting rate and/or share price, such that the disclosures may not relate to how much the director finally receives. In addition, a further column should be added to the table for exceptional items such as, for example, claw back and recruitment fees paid (question 7).

- The outcome of the Government's consultation on narrative reporting is awaited. It is important that any revised remuneration reports fit within any new framework and that any disclosures of a company's objectives and measures of performance are consistent throughout.

Please contact me if you would like clarification on any of the points in this letter or if you would like to discuss any issues further.

Yours sincerely

Liz Murrall
Director, Corporate Governance and Reporting

IMA's ANSWERS TO THE QUESTIONS RAISED

IMA's answers to the questions raised are as set out below.

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

It is proposed that the remuneration report is in two parts. First, a policy report which looks forward on all elements of the remuneration policy and the key factors to be taken into account. This is subject to a binding vote. Secondly, a report on how the policy was implemented in the last financial year together with actual payments and the link between pay and performance. This is subject to an advisory vote.

IMA considers that clearly setting out the remuneration policy and then how that policy has been implemented will help investors hold companies to account. However, the regulations are complex and and certain of our members consider that the prescriptive nature of the proposals mean that there is a risk that remuneration reports will become even longer and include more boiler plate and standardised language. Much of the detail should be contained in guidance and we support this being developed by the FRC[1]. It would also be helpful if BIS undertook to review disclosures after a suitable timeframe, say two or three years, to see whether the policy objective sought has been achieved.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

This is a question for preparers of financial statements.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

IMA welcomes the introduction of a table which sets out the key elements and supporting information on pay policy. This should help improve comparability between companies. We believe companies should have flexibility in reporting the key elements in that these should be entity specific and not 'boiler plate'. Thus it is important that the table is accompanied by narrative that puts it into context. There are also certain other matters that are not noted in the consultation or the draft Regulations that investors would value as set out below.

- The policy towards the remuneration of new executive director recruits, including the approach to buying out existing packages. There may be particular considerations in relation to overseas recruits in terms of buying out benefits, such as school fees, and any transfer costs.

- The extent to which the company takes ESG (environmental, social and governance) issues into account when setting its remuneration policy.

- Whilst a company's policy the achievement of performance targets in advance would be helpful, there may be commercial sensitivities around such disclosures. Thus at a minimum, companies should set out their policy on disclosing performance targets

[1] Paragraph 30

achieved retrospectively in the implementation report or not disclosing as the case may be.

In addition, the example table does not differentiate between individual directors. How an individual executive director's remuneration relates to his/her performance and the time frame over which it is measured may vary according to their particular responsibilities. We consider there should be a separate table for each executive director and that the Regulations should make this clear.

Lastly, it appears that in years where there is no material change in the policy and the policy is not subject to a vote, then companies would not be required to include the table in their report. We consider that this information is valuable every year and should be required to be disclosed.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

IMA welcomes more transparency on the relative importance of the spend on remuneration, profit and dividends. However, as drafted this is to be contained in the policy report which is forward looking and subject to a binding shareholder vote. Essentially we consider that this relates to the past and should be disclosed in the implementation report.

It is proposed that the "percentage change" in the reporting period is disclosed[2]. We consider the relative proportion of each should be disclosed - the relative change could disguise the fact that remuneration is a disproportionate amount of the total. It is also important that the type of profit is clarified, i.e. gross profit, operating profit or profit after tax, such that the proportions are comparable year on year. Our preference is that it should be operating profit to reflect better that which represents what the management and directors have done with the resource entrusted to them.

In addition, in the graph of "total remuneration opportunity" the base salary as well as the other components of remuneration appear to vary in line with the target achievements. We do not consider base pay would vary in this way.

Lastly, investors would welcome more transparency around directors' service contracts and the remuneration an individual is entitled to and disclosure of "all existing contractual provisions that relate to directors' remuneration[3]" in the policy report. However, such contracts can be long and detailed and it is important that such disclosures are targeted. It would also help investors accessing service contracts if they were made available on a company's web site.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

[2] Paragraph 49

[3] Paragraph 46

IMA's ANSWERS TO THE QUESTIONS RAISED

IMA agrees that companies should set out the principles on which exit payments are determined and that this should be part of the policy report. We had concerns about the basis of the original proposals that exit payments were to be subject to an annual binding vote[4]. The proposals outlined cover the main principles in determining exit payments. It would also be helpful for the company to disclose their policy on exit payments in relation to the different types of leaver or the circumstances under which a director left. However, we recognise companies are likely to want to be allowed a certain amount of discretion in this area in terms of disclosing the implementation of that policy.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

IMA supports companies seeking employees' views on the executive pay policy, but it has challenges and we agree that companies should not have a statutory duty to consult. Whilst the remuneration committee should take account of the views of the wider organisation, we do not consider a company should be required to state whether, and if so how, it sought employee views on its remuneration policy. This would be likely to result in standardised reporting in that the process is likely to be generic. We do not consider the same could be said of the engagement with shareholders, particularly in view of the binding vote, and thus support the proposal that the report should state how shareholder views were taken into account.

The proposals require the percentage increase in the pay of the workforce and that of the CEO are disclosed. We welcome this but consider it would best be included in the implementation report in that it relates to the past and for ease of comparison, should only address the UK work force.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

The single figure for each director's remuneration should be accompanied by narrative that explains the various components that make up that figure and how it has developed over time. Consistency in how each component is measured is essential to ensuring comparability, not only year on year for a particular company but also between companies.

As noted in the Financial Reporting Lab's project in this area[5] the intention is that the single figure includes remuneration receivable as a result of the achievement of conditions relating to performance in the reporting year and where the performance cycle is longer than a year, it includes remuneration in the last year of the cycle. Thus long term incentive plans would only be recognised in the final year when it is know with some certainty what the directors will receive. We support this in that to reflect the amount the director becomes entitled to for their performance for the year would involve assumptions and predictions as to, for example, the vesting rate and/or share price, such that the disclosures may not relate to how much the director finally receives. However, it is important that in simplifying

[4] http://www.investmentfunds.org.uk/assets/files/consultations/2012/20120427-bisexecutivepay.pdf

[5] http://www.frc.org.uk/News-and-Events/FRC-Press/Press/2012/June/Financial-Reporting-Council-publishes-report-on-A.aspx

this that alongside the table, disclosures are given on amounts awarded that will vest in the future.

We also consider a further column should be added for exceptional items such as, for example, claw back and recruitment fees paid in that these shod be separately identified for each director.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

IMA supports the application of the HMRC methodology to work out the value of defined benefit pension schemes on the basis that this measures the actual benefit to the individual as opposed to the cost to the company. In this context, different terminology to "HMRC methodology" needs to be used in any final legislation should this approach be adopted. In addition, the paper states that IAS 19 uses 'market based' valuations[6]. Whilst that is true for the assets funding the scheme, the pension obligation is determined using an actuarial valuation method.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We understand there are differences of opinion with regard to the valuation of LTIPs when the performance criteria have been satisfied in the period but the shares awarded have yet to vest at the reporting date. However, for users it is important that the details are comparable and as such, companies should use the same measurement methods which are clearly explained in the note. In this context, clawback arrangements can have a significant impact on the single figure for remuneration and it is appropriate that they are reflected.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

IMA supports the reporting of additional information in this area and the proposed disclosures[7] but would not expect commercial confidentiality to be compromised. Hence, high level disclosure, for example, percentages of targets achieved as opposed to those set could be an acceptable compromise. In this context, paragraph 19(d) of the draft Regulation states that "what performance metrics, if any, are used, the relative weighting of each and the period of time over which they are measured" the following should be reported. It needs to be clear that this should be on a comply or explain basis – see answer to Question 3.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

See answer to Question 8 with regard to defined benefit schemes. IMA agrees with the proposals for other types of scheme outlined. The disclosures should separate the amounts

[6] paragraph 67

[7] Paragraph 77

into types of pension to enable users to understand the different benefits of each. We also agree with the proposal to disclose any additional benefit that would become receivable by a director were they to retire early.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

IMA supports the continuing disclosure of information on scheme interests awarded in the current year under long term incentive plans and that face value is preferable to expected value in that the latter requires the use of assumptions. We agree that in the case of the former the awards disclosed may be higher than those that are received but consider this would be addressed by requiring the disclosure of the percentage of the award that would vest at threshold performance.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

IMA supports simplification but would welcome more consistency in reporting in this area in that this can vary. We consider directors' interests should be valued at the current market price.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measure would be more appropriate?

IMA supports CEO remuneration being compared to total shareholder return. However, we recognise that certain small companies may find it difficult to identify this figure for the last ten years and thus it would be helpful if initially companies were required to give details for the last five years and build up to ten years. In addition, as the CEO can change within this period, the graph should clearly indicate where this has happened.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

IMA believes that there will be sufficient audit assurance if the single figure, performance against metrics, total pension entitlements, exit payments made and detail on variable pay are subject to audit. We are not aware that companies make errors in reporting such information and the rest of the report mainly relates to the forward looking policy which it would be difficult to verify objectively.

Johnson Matthey plc

BIS | Department for Business Innovation & Skills

Directors' Pay: consultation on revised reporting regulations. Response form.

The closing date for this consultation is 26 September2012

Please return completed forms to:

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Department of Business, Innovation and Skills
1 Victoria Street
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020 7215 3930
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Confidentiality & Data Protection

In the interests of transparency, the Department may choose to publish the responses to this consultation. **Please state clearly if you wish your response to remain confidential.**

Please note also that information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

About You	
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I am responding on behalf of (please tick):	
tick	Quoted company
	Other company
	Investor or investment manager
	Business representative organisation
	Investor representative organisation
	Non governmental organisation
	Trade Union
	Lawyer or accountant
	Other (e.g. consultant or private individual)

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Most companies will react in the appropriate spirit and seek to provide a clear and transparent response in line with the final policy. However, the nature of the subject and the complexities therein mean that it is difficult to cater for every nuance and particular set of circumstances within the written regulations. We assume that the ultimate arbiter will continue to be the shareholder, rather than the court of law, and under the new regulations, the shareholders have enough firepower to ensure proper compliance. Therefore, in that spirit, the draft regulations seem to fit the policy objective.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

The new regulations will require further internal analysis and preparation in order for companies to be fully compliant in 2014. A degree of consultant support is likely to be required to assist in the process, and there will be some further auditing work. Therefore, there will be extra costs associated with the new regulations.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

This question applies to the 'policy' side of the Rem Report. In general, this is a practical and informative approach, and has been followed in our

Remuneration Report this year. As with the answer to question 1, it is difficult to write into regulation the exact data required for every category. Responsible firms will present the data in a clear format, and well informed shareholders will make a judgement.

There may be some tricky parts requiring best estimates, such as 'pension opportunity' which may depend on an as-yet-to-be-determined succeeding years pay rise.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

In terms of pay policy, it is possible to provide information on base, threshold, on target and maximum earnings, under different scenarios. Some performance targets will remain confidential, which will render some of the information difficult to interpret. It seems a reasonable goal for shareholders to understand what the maximum level of remuneration will be, and what performance is required to achieve it.

There will be some difficulties in quantifying maximum levels of some items, where the quantum is related to share price or salary increase, and various explanatory footnotes may be required.

However, the biggest difficulties with this proposal may lie in the difficulties associated with amending service contracts, under circumstances of major company events, such as mergers, acquisitions, fundamental market events etc. It seems unlikely that every company event can be foreseen, and as yet, it is difficult to discern the room for flexibility in the regulations and policy.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

On first inspection, this sounds reasonable. The normal terms of a service contract may be disclosed, which cater for early termination, and these would represent a normal maximum.

It seems unlikely that all departure scenarios can be envisaged under policy, and the key part for disclosure will be the maximum available under the terms of the service contract.

However, it is feasible that legal issues such as alleged discrimination could arise within a company which require that a compromise is sought, which could exceed the service contract amount. Is it the case that companies will lose the ability to make a compromise outside of the normal terms of a service contract?

It seems likely that companies will seek as broad a latitude as is possible in writing termination terms into the remuneration policy.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

It should be expected that a Remuneration Committee should take into account the wage policies and awards for the global employees of the company, when setting Remuneration Policy and quantum.
However, Board level remuneration is not necessarily a good subject on which to elicit employee views. In the case of a global multi-national company, it is not clear which views should be sought, how they should be gathered, or how they should be used.

Independent members of a Remuneration Committee will be fully aware of the relevant factors, such as the performance of the company, the market for UK pay settlements, the performance of the individual directors and the relevant benchmarks. Based on this full knowledge, and mindful of the new shareholder voting rights, they are likely to come up with the right answers. It is not clear how employee views would be a critical factor in this, and the eliciting and use or non-use of those views is likely to be a an aggravating and divisive factor in the company. It is also not helpful to be required to state that ‘employees were not consulted’. The Remuneration Committee are the right group to balance such factors, and the owners are the right group to have the

final say.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Subject to a consistent definition of this number, this is a valid approach. For a company with a straightforward and transparent Remuneration Policy, it is not too difficult to assemble and report on the information required.

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

The HMRC calculation (which is basically the Annual Allowance calculation with a multiplication factor of 20 rather than 16) has the benefit of simplicity, but does not reflect the true cost to the company. However, the alternative, using the existing CETV approach with IAS19 assumptions is likely to cause large swings in the single figure calculation, and therefore obscure the original purpose. In that sense, this simple calculation may be the best and most informative figure for shareholders.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

It seems reasonable to expect that where claw-back has occurred, that the quantum and reason are explained separately.

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

Whilst most routine performance measures such as EPS, TSR and profitability targets can be safely retrospectively disclosed, there are some targets which might betray a specific and ongoing strategic objective which could be commercially sensitive, for example in the areas of M&A or R&D.

Therefore it may be difficult to require full publication of all details. Again, shareholders will retain the mandatory and advisory votes and will therefore make judgements regarding the adequacy of disclosure.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

The proposals would adequately cover all the benefits pertaining to the remuneration of our Directors

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

This section seems to be a repetition of information covered in the Policy Section. The additional requirement to declare awards at face value is misleading (as face value requires maximum performance) and adds no further information to shareholders.

Equally, it would be difficult to reflect the alternative 'fair value' as this would require a disclosure of detailed forward expectations (eg EPS expectations) and would therefore be commercially sensitive.

We would conclude that a properly written policy section adequately discloses face value awards.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

No particular comment, this seems to be standard information, and there are no particular costs.

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

This measure seems to take the myriad complex circumstances that face a CEO and Board, and implies that the simple rules of thumb for determining CEO pay are profitability and general stock market conditions.

This measure takes no account of difficulties of markets, dismisses any long term contributions, and renders short term performance as the key determinant.

The appropriate measures are to follow the company closely, read the Annual Report, and make a judgement, expressed through the binding vote on policy, and advisory vote on pay, as to whether remuneration is appropriate to company performance.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

No particular comment. We would expect to have audited all the relevant numerical data in the Remuneration Report.

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28th September 2012

Dear Mr Walker

DIRECTORS' PAY: CONSULTATION ON REVISED REMUNERATION REPORTING REGULATIONS

This submission is made on behalf of Jupiter Asset Management Limited (Jupiter). Jupiter manages assets for a range of institutional and private investors. It is a subsidiary of Jupiter Fund Management plc and manages both segregated and pooled pension funds, charities and assets for investment companies. It also acts as Investment Adviser for the Jupiter range of unit trusts and SICAVs.

Jupiter seeks to invest in companies that are well managed and demonstrate a high standard of corporate conduct, responsibility and governance, thereby creating an appropriate culture in which to enhance long-term shareholder value. We think it is vital to promote a clear link between executive remuneration and company performance. Shareholders should be empowered to hold companies to account on this matter. Not only is this commensurate with good market practice, it goes hand in hand with ensuring the responsible investment of our clients' funds.

We are pleased to have the opportunity to comment on the package of measures set out by the Government to address weaknesses in the corporate governance framework for executive remuneration. We understand that the Government's objective is to provide shareholders with clear and accessible information about remuneration and, in particular, the link between reward and performance.

We also believe that the introduction of a binding vote on remuneration policy will encourage greater dialogue between companies and their investors. We are therefore pleased to see the requirement that the future policy report sets out how shareholder views were taken into account in setting remuneration policy and that a similar shareholder context is provided in the implementation report (ie how shareholders voted at the previous year's AGM, the reasons for significant dissent where known and any action taken by the remuneration committee in response).

Other key points are highlighted below:

- It is proposed that the remuneration report is in two parts. First, a policy report which looks forward on all elements of the remuneration policy and the key factors to be taken into account. This is subject to a binding vote at least every three years. Secondly, a report on how the policy was implemented in the last financial year together with actual payments and the link between pay and performance. This is subject to an advisory vote.

  We believe that clearly setting out the remuneration policy and then how that policy has been implemented will help investors hold companies to account. However, given the complexity of the regulations, we support guidance being developed on the level of detail and type of information to be disclosed.

  It would also be helpful if BIS undertook to review disclosures after a suitable timeframe, perhaps three years, to see whether the policy objective sought has been achieved.

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

- We welcome the introduction of a table which will improve comparison between companies. Whilst the exact format of the table is not stipulated, we believe that the following key elements of pay policy should be added to the detailed requirements for its content:

  - the policy on the remuneration of new executive director recruits, including those from overseas;
  - the extent to which environmental, social and governance (ESG) considerations are taken into account in setting pay policy; and
  - the policy on disclosing performance targets achieved in the implementation report.

  We also believe that a separate table for each executive director would be helpful where they have different performance requirements and/or remuneration structures, and that these tables should be disclosed every year, even if not subject to a vote.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

- Disclosure of the percentage change in profit, dividends and overall expenditure in pay is included in the policy report. This also applies to the percentage increase in the pay of the work force and the CEO as set out in question 6. It would be more meaningful if these were included in the implementation report as they relate to the past.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

- Consistency is essential in reporting a single figure for each director's remuneration which should be accompanied by narrative that explains its components and how it has developed. We welcome the proposals put forward by the Department of Business, Innovation and Skills as developed by the Financial Reporting Council's Reporting Lab, which disclose remuneration when it is earned rather than when it is awarded.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

- We agree with the Government that there should not be any statutory requirement on companies to obtain employee views on the remuneration policy. Accordingly, it does not seem appropriate to require companies to include a statement on whether or not employee views have been sought on the remuneration policy. We do not see any benefit in a requirement for such a statement.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

- Finally, we are still waiting for the outcome of the Government's consultation on narrative reporting. It is important that any revised remuneration reports fit within any new framework and that any disclosures of a company's objectives and measures of performance are consistent throughout.

Please contact me if you would like clarification on any of the points in this letter or if you would like to discuss any issues further.

Yours sincerely

Emma Howard Boyd.

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Mr Barry Walker
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Our ref tc/815

1 October 2012

Dear Sir

Directors' Pay

We welcome the opportunity to respond to the Consultation Paper *'Directors' Pay'*. We share the Government's concern that in some companies there is, or at least appears to be, a disconnect, between executive pay and long-term corporate performance; and we believe that boosting transparency so that what directors are paid is clear and easily understood is part of the remedy for any failings in the corporate governance framework for executive remuneration.

To understand properly the link between pay and performance, it is fundamental that pay should reflect the value the director becomes entitled to in relation to the performance for the year. This is particularly relevant in terms of recognising and measuring benefits for which entitlement and receipt do not fit into a single reporting period such as pension entitlements and long-term incentives. In our view, there are three main issues that need addressing. The first question is what is it that is to be measured – the value at the date the 'award' is granted (the 'day- 1 replacement value') or the value crystallised when all performance (and service) conditions have been met (the 'end point achieved value')? The second question is whether one is measuring the cost to the company or the benefit to the director? Lastly, how does remuneration gets allocated across time?

We agree with the Government's proposal that, as regards the Directors' Remuneration Report, the disclosure should address the benefit to the director rather than the cost to the company. However, we believe the Government should re-appraise the proposal for disclosing 'pay' using 'end point achieved value' measures in the year of meeting the conditions and whether there is a solid consensus for it among shareholders and companies. While the Government's proposal is certainly pragmatic, it does have the disadvantage of reporting a (potentially) large figure in a single year when in fact it is in respect of several past years also. If, however, there is a consensus for this pragmatic approach then we should not object to it.

With respect to pension entitlements, we note that the proposed approach – the HMRC methodology for calculating the benefit arising from pension promises – is inconsistent with the view that the single figure should address the benefit to each director. We believe that the transfer value is the appropriate measure of the benefit to the director i.e. the amount that the director would have to have paid to an insurance company to acquire pension rights equivalent to the increase in the benefit entitlement that year.

Finally, notwithstanding our concerns regarding the substance of the proposed disclosures set out above, we believe that elements of the draft regulations lack clarity. Definitions are not provided in all cases and the terminology is sometimes inconsistent – some terms seemingly carried over from the existing and rather complex Schedule 8 of the Large and Medium sized Companies and Groups (Accounts and Reports) Regulations 2008 whereas others have been newly drafted. We also note that paragraph 72 refers to the need of potential 'best practice guidance ' regarding the disclosure of the amounts once an award has vested which seems to indicate that the Government has concerns that the requirements are not clear. Consequently, we believe that the government should take a fresh look at how the (eventual) policy is implemented in the regulations and grasp the opportunity to re-draft in clear unambiguous terms. The end result would be easier application by companies and more consistent reporting across companies to the benefit of shareholders.

* * *

Our detailed arguments on the points set out in this covering letter are addressed in Appendix 1 – "Disclosing directors' remuneration – the challenges". Our comments on the specific questions raised in the Consultation Paper are set out in Appendix 2 and our comments on other matters are set out in Appendix 3. A table of inconsistencies in terminology and clarity issues is set out in Appendix 4.

We hope that our comments prove to be useful and we welcome an on-going dialogue as the Government's thinking continues to develop and evolve. Please do not hesitate to contact David Matthews (020 7311 8572) or Tim Copnell (020 7694 8082) should you wish to discuss any of the points raised in this response.

Yours faithfully

KPMG LLP

KPMG LLP

Appendix 1

Disclosing directors' remuneration – the challenges

The measurement of remuneration in respect of a period is subject to three problems. First, what is it that is to be measured? Take a share option as an example. Are we trying to measure the value of the share option, i.e. how much it would cost, when the option was granted, to have bought such an option in the market. Let's call this the "day- 1 replacement value". Or are we trying to measure the value achieved at a later point in time when some or all conditions are met? E.g., the value of the share option at the point at which exercise becomes unconditional or the value crystallised by exercising the option (share value less exercise price). Let's call this the "end point achieved value".

The second problem is whether the measurement should be the cost to the company or the benefit to the director. Sometimes these are the same e.g. the "day 1 replacement value" of a share option. Sometimes they are not: e.g., employment taxes levied on the company in relation to the director's salary; e.g., certain technical details about an IAS 19 measurement of defined benefit pension costs make it different from the benefit to the director, which is the transfer value – the amount that he would have to have paid to an insurance company to acquire pension rights equivalent to the increase in his benefit entitlement that year.

The third problem is the allocation of the remuneration measure to the periods. There are, for the sake of completeness, five options:

i) all on day-1 of the arrangement;

ii) over the period when the arrangement remains contingent on performance conditions – meaning conditions measuring some aspect of the quality of the director's discharge of his role either directly (director behaviours) or indirectly (company performance);

iii) the day on which all performance conditions are met;

iv) over the period when the arrangement remains contingent on any conditions. This is known as the vesting period and will be longer than the performance conditions period when there is also a required period of service, without performance conditions, after any performance conditions have been met; and

v) the day on which all conditions are met.

The second problem is independent of the first and third, and we agree that the benefit-to-director basis is appropriate for the Directors' Remuneration Report.

The first and third problems are connected. E.g. if the "end point achieved value" basis is used then any of (i) to (iv) will inevitably involve not only a basic charge for the period but also a true-up for changes in estimate of the uncertain future "end point achieved value". Method (v) is a practical approach with the "end point achieved value" measure but has the disadvantage of reporting a (potentially) large figure in a single year when in fact it is in respect of several past years also. That seems distorting.

The accounting solution

Accounting needs a single figure too, i.e. a discrete figure to charge against profits. Its solution to the first and third problems is to use "day-1 replacement value" and charge this over period (iv) (the vesting period). Thus the amount charged is the cash that the director or employee would have to have spent on day-1 to buy his way into such an arrangement at an estimated market value. The charging period is that over which his entitlement to keep the arrangement accrues. This may not be perfect, but it is a workable compromise as a result of professional debate.

The proposed Directors' Remuneration Report solution

It is, of course, difficult to communicate a complex arrangement in a single figure. We note that the draft regulations do not do so: i.e. although columns (d) and (e) of the table give a single figure, disclosure under paragraphs 8, 9 and 12 try to give a broader picture. Whilst we agree in principle with such a combined approach, we have concerns that the single figure is an "end point achieved value" booked, subject to what follows, in period (v). This has the disadvantages noted above and, in addition, makes comparisons with accounting measures (paragraphs 24, 30) meaningless or necessitates that the remuneration measure is switched, for comparison purposes, to the accounting basis.

Implementation in the draft regulations

We do not believe that the HMRC method for pensions bears sufficient relation to the benefit to the director. For example, suppose that a director's pension entitlement per annum has increased by £1,000 over the year. On the HMRC method, this contributes £20,000 to the single figure total. However, there is a significant difference in the benefit to the director depending on, for example, whether that £1,000 p.a. is flat or index-linked; whether it is single or joint life; whether retirement is far into the future or only a few years away. We believe that, instead, transfer value is the appropriate measure of benefit to the director.

We also foresee many difficulties in the application of the draft Regulations and in particular paragraphs 5(d), 6(d) (column (d)):

- Since this covers money "or other assets", it is not clear how arrangements are split between this column (d) and column (e).
- "Award" is undefined. Whilst this naturally suggests the original grant, on conditions, of an interest in money or other assets, 5(d)(i), (ii) refer to "payments which are awards/ awarded" suggesting that the actual, eventual payment (so in money, not other assets?) is what is meant.

- 5(d) refers to "final vesting" as a result of achieving "performance conditions". This suggests that "performance conditions" mean all conditions. Yet paragraph 7(3) talks of service conditions and performance conditions as if each were only some of the complete set of vesting conditions.

- After excluding the items specified in 5(e)(i), (ii) it appears that 5(e) covers awards in the current year vesting this year and prior year awards that remain unvested. Suppose, then, that £100,000 is awarded in year 1 but is subject to conditions in years 2-5. It will not be included in the single figure in year 1 or year 5, but it will be included in each of years 2, 3, and 4 (i.e., triple-counted). That seems inappropriate.

- Since this figure includes "other assets" at their "cash equivalent" it is necessary to specify as at what date the assets are valued and hence the "cash equivalent" amount is determined. This has not been done.

We also foresee difficulties with paragraphs 5(e), 6(e) (i.e., column (e)):

- This, too, is unclear in relation to vesting and performance and other conditions.

- Paragraph 5(e)(iii) seems redundant as these fall into the paragraph 5(d) and so are excluded from 5(e) by virtue of paragraph 7(3)(a) (although 7(3)(a) seems inconsistent with the chapeau of 7(3)).

- Where dividends accumulate it appears that paragraph 6(e)(ii)(XY), (XYZ) requires these monetary amounts to be multiplied by the share price. The product seems to be a meaningless number.

- When the award has not fully vested, paragraph 6(e)(ii), (iii) makes provision for determining its value. Yet unvested awards do not appear to be captured by paragraph 5(e) at all. We also note that if unvested awards *were* captured, then this rule in paragraph 6(e)(ii), (iii) would depart from the Government's stated intention of disclosing such awards only in the year of vesting; and would instead disclose them in every year from grant to vesting (with no deduction for any amounts disclosed in prior years, thus counting some amounts multiple times).

Recommendations

We recommend that the government should:

- adopt transfer values for defined benefit pensions rather than the HMRC method, which is not representative of the benefit to the directors;

- re-appraise the proposal for "end point achieved value" measures included in the year of meeting all (or just performance) conditions and whether there is a solid consensus for it among shareholders and companies; and

- take a fresh look at how the eventual policy is implemented in the regulations.

Appendix 2

Questions raised in the Consultation Paper

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

We believe that the Regulation, as currently drafted, will not lead to consistent and clear disclosure; and therefore fails to achieve the objective of consistent and transparent disclosure set out in the Consultation Paper. The draft uses a number of undefined terms (for example 'performance conditions' and 'cash equivalents') and sets out the disclosure and measurement requirements in a manner that allows or requires a significant level of interpretation.

Furthermore, the draft Regulations are sometimes difficult and at times impossible to understand without reference to the explanatory material in the Consultation Paper or the commentary provided in the Financial Reporting Lab ("Lab") project report. We believe that it is sound policy and one, moreover, that was promoted by the Company Law Review's drive for accessible legislation, that the text of the Regulations should stand alone without the need for additional commentary.

Some examples to illustrate our concerns are set out below and in Appendix 1. Further detailed drafting points are set out in Appendix 4 – Inconsistencies in terminology and clarity issues.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

Corporates are better placed to respond to this question; however, we do not expect the costs of adjusting to the revised reporting regulations to be significant if the Regulations can be made clear.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

Subject to our comments as to its basis, we support the expansion of the current 'tabular approach' to include, now, all elements of remuneration, adding up to a 'single total figure'. Of itself, a single total remuneration figure for each director would not provide meaningful information for shareholders since the total is composed of components of differing nature. This needs to be disaggregated and supplemented with additional information. It is the detailed information presented in the table (and other disclosures), including the balance between different elements of pay, which enables shareholders to understand how and how much directors are paid.

We query the suggestion (in Question 3) that Government does not propose to prescribe the specific disclosures that are required for each element of pay. Not only is some degree of specification necessary for consistency but the draft regulations provide considerable specification, albeit, as explained above, we are concerned that the complexity will make the legislation inaccessible and reduce the likelihood of consistency.

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

We have answered this question in three distinct parts as follows.

Service contracts

While we support transparency with regard to directors' service contracts in general and those matters relating to directors' remuneration in particular, we believe that the proposals set out in paragraph 21 of the draft Regulations – that the policy report must set out "all the provisions that relate to remuneration contained in the directors' service contracts" – is unduly onerous and likely to lead to lengthy and complex statements. We believe that a *summary* of the service contract provisions relating to remuneration would be more appropriate and of greater benefit to readers.

We also note the lack of clarity as to whether this section applies to each director's service contract or more generically to all directors' service contracts.

Scenarios

We welcome the proposals to disclose possible remuneration in differing performance scenarios. This has the benefit of encouraging remuneration committees to consider a wider range of potential outcomes – to the extent they don't already – as well as providing a degree of transparency around the link between pay and performance.

Notwithstanding our support for the general principle, we believe that the proposals set out in paragraphs 22 and 23 of the draft Regulations – graphical representation of expected remuneration for below target, on target and above target performance – are unclear. It would be straightforward to apply if all components of remuneration had only three potential values: pays X if target failed, Y if on target, Z if target exceeded. However, it is difficult to interpret the requirements in the context of schemes with multiple thresholds or "sliding scales". What would "threshold met" mean here (thresholds corresponding to corporate plans' coming to fruition)? What do "falls below the threshold" and "exceeds the threshold" mean? Perhaps a better approach would be to graphically represent the maximum and minimum remuneration that could be achieved. It could be left at that or one might add, as some kind of mid-point, the remuneration if corporate plans come to fruition.

Relative importance of the spend on pay

We recognise that shareholders need to understand the overall spend on pay in the wider corporate context, but we do not believe that paragraph 24 of the draft Regulations is sufficiently clear to meet this objective. In particular, it is not clear as to whether "overall expenditure on pay (as a whole)":

- relates to directors' pay or total employees' pay;
- includes non-financial pay such as LTIPs and pensions and how they are measured for this purpose; and
- includes employment taxes.

Some of these difficulties spring from the apparent assumption that the term "expenditure on pay" will be clear. However, since "pay" isn't a term used in the accounting literature ("staff costs" in SI 2008/410, "employee benefits" in IFRS), the hoped for clarity is not achieved. Assuming that the full accounting basis is intended (and this is the only one that would make a comparison with profit meaningful), we also note that this is a measure of the cost to the company and not, as the other measures in the [DRR], the benefit to the recipient, furthermore, the accounting basis takes a charge on a different measurement basis and over different periods than appears intended by the proposed single figure regime.

The terms "profit", "of the company" and "reporting period" also require further consideration. Is, for example, "profit in the financial year" (SI 2008/410)/ "profit and loss" (IAS1 paragraph 81A) intended, or some sub-total of profit higher up the profit and loss account? Is "group" intended rather than "company"? Should "reporting period" read "financial year" (the usual term in Part 15 of the Act and supporting regulations)?

Lastly, we do not see the immediate relevance of benchmarking "pay" against dividends as dividends are not necessarily indicative of performance. We accept the appeal of placing returns to directors in the context of returns to shareholders. However, dividends are only one component of the return to shareholders. We also note that a comparison of CEO (or equivalent) pay to "total" shareholder return is already proposed in section 13 of the draft Regulation.

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We support both the principle that the company's approach to exit payments should be disclosed in the policy report and the specific disclosures as set out in sections 25 and 26 of the draft Regulations.

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

We strongly believe that Remuneration Committees should *inter alia* take into account the pay and employment conditions of employees when determining executive pay policy. However, the decision as to whether or not to consult employees as part of this process is clearly one for the Remuneration Committee and we would not wish to create an expectation that Remuneration Committees "should" consult with employees. In our view the proposed disclosure does create such an expectation and therefore we believe paragraph 28 should be removed.

With respect to paragraph 30(1) – the percentage increase in chief executive officer pay and that of employees generally – factors such as employee demographics and local pay inflation and broader economic considerations can affect the comparison. On the other hand, the option to identify an appropriate comparator group is easy to manipulate. This disclosure requires further consideration if the information is to be meaningful and not subject to abuse.

We also note some drafting points about paragraph 30. The term "pay" is used again. Is this the "single figure for remuneration" or the accounting basis? (See also above.) We note that the former would require significant additional effort to calculate for the employees generally. We also note that the period over which the "percentage increase" is to be computed is not specified. Finally we question whether it is necessary, to achieve the purpose of this paragraph, to introduce non-statutory terms such as, "any director fulfilling the role of chief executive officer". The real target, we assume, is simply the percentage by which: the current financial year's largest figure in column (f) at paragraph 4 (largest "single total figure for remuneration"); exceeds the largest such figure for the preceding financial year (making suitable adjustments when any figures in the tables do not represent a full year).

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

The Consultation Paper suggests that the single figure is comprehensive, reflects actual pay earned rather than potential pay awarded and is consistent with the conclusions drawn by the Lab, which included that understanding the benefit to the individual is more relevant than disclosing the cost to the company.

We agree that the measurement methodology proposed for salary, fees and benefits express the benefit to the individual.

Regarding bonuses and long-term awards, as we explain in Appendix 1, we recommend that the Government re-appraise the proposal to use this "end point achieved value" basis and timing of disclosure.

Questions 8 and 11: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach? Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We do not believe that the HMRC method for pensions achieves the intention set out in the consultation as the resultant figure does not bear sufficient relation to the benefit to the director. For example, suppose that a director's pension entitlement per annum has increased by £1,000 over the year. On the HMRC method, this contributes £20,000 to the single figure total. However, there is a significant difference in the benefit to the director depending on, for example, whether that £1,000 p.a. is flat or index-linked; whether it is single or joint life; whether retirement is far into the future or only a few years away.

We also observe that the recent Lab report notes that companies could not agree on either the IAS 19 methodology or transfer values but did not favour the HMRC methodology, albeit the majority of investors did. So it is unclear to us as to why the Government has chosen the HMRC value when there is no all-parties consensus for any method and this one seems least representative of the benefit to the director. We believe that the transfer value is the appropriate measure of the benefit to the director.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

We agree that any claw-back should be recorded as part of the single figure. Furthermore, where claw-back has a significant effect on either the overall figure or the amounts recorded under any separate category, we should expect companies voluntarily to set out the amounts, circumstances and factors affecting the decision.

We note, however, that the draft regulations themselves do not refer to the presentation of claw back arrangements and therefore the Government's intentions, as reflected in the Consultation Paper, are unlikely to be implemented in practice – or even, arguably, no deduction is permitted in arriving at the "single total figure". Once claw back is reflected it the Regulations, we believe that it will be necessary to refer also to claw back in relation to *former* directors (many cases of claw back occur after a person has ceased to be a director).

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

If the objective of providing meaningful disclosure about the link between pay and performance is to be met, then some commentary on the extent to which previously agreed performance targets have been achieved is required. With this in mind, we support the proposed disclosures with the proviso that companies should not be expected to disclose commercially sensitive metrics. A requirement to explain why such metrics are not disclosed should be introduced to prevent any "commercial sensitivity" exemption being abused.

We believe that companies are, for the most part, able to provide meaningful information of the type proposed without straying into the commercially confidential arena. We also believe there is an opportunity for the Lab to promote good practice in this area and dispel the myth that meaningful information can't be given without disclosing prospective financial information and other price sensitive material.

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We note that "face value" is not defined in the Regulations and therefore we are unclear as to what figure is required. Is it intended that in the case of (say) the number of share options granted is x times base salary, the face value is simply x times base salary? What might "face value" mean in other situations? As we have discussed elsewhere, it is essential that the regulations are clear and unambiguous.

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details?

We consider the proposed disclosures relating to directors' interests to be useful and welcome the proposed simplification of the current requirements.

We note, however, that the Listing Rules require additional disclosures for premium listed companies. While these are not inconsistent with the current proposals, we believe that the Companies Act's regulations should be the primary source that sets out disclosure requirements so that companies need not look elsewhere, including to the Listing Rules. Accordingly, the Listing Rules need to be consistent with the Companies Act on this matter (or be removed altogether).

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

We believe the graph would be useful and that total shareholder return is an appropriate and easily calculable proxy for company performance. Likewise, CEO pay is a useful proxy for directors' pay and not subject to the deflationary impact of large numbers of relatively low paid non-executive directors. However, we question whether the Government's intention could be achieved without introducing non-statutory terms like "CEO". Perhaps the highest paid director – namely the individual with the largest figure in column (f) at paragraph 4 (largest "single total figure for remuneration") would be more appropriate.

We note that section 13(1)(b) refers to the term "total pay". We assume the intention is that this would be the amount included in column (f) of the table, but this is not stated.

In practice, there may be more appropriate proxies for company performance and in such circumstances we should expect companies voluntarily to plot these on the graph *in addition* to total shareholder return and accompany with explanatory narrative.

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We agree that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay should all subject to audit.

The degree of assurance required on the other sections of the report is principally a question for shareholders, but we generally believe that if a company reports information then it is on the basis that it believes that it is of value to shareholders; and that there is an expectation that such information is accurately reported and that it is not otherwise misleading (which might be what "fair, balanced and understandable" means). Independent assurance on such information therefore has the potential to provide value to stakeholders by increasing confidence in its accuracy. In this context, we note that some FTSE 100 companies already publish an independent review report on remuneration matters including whether the Remuneration Committee has discharged its duties in line with the stated policy on executive remuneration.

Appendix 3

Other matters

The summary statement (Part 2 of the draft regulation)

It is unclear what information should be present in the summary statement. While the consultation notes that many companies already produce a statement from the chairman of the remuneration committee, these statements often do not cover the full scope of the remuneration report. It would be helpful if Part 2 of the draft Regulations were redrafted to give some clarity (albeit short of detailed specification of particulars) the nature of information sought in the summary statement. This part of the Regulations should be dropped if the proposed content cannot be clearly articulated and differentiated from the revised disclosures intend to provide concise information in the main body of the disclosure.

Alignment with the Listing Rules

In paragraph 36 the Government states that it will work with UKLA to consider whether the Listing Rules need to be changed. We support this initiative as we believe that there is duplication of requirements. Duplication, with subtle differences, in the Listing Rules is a problem that is best addressed by their removal from the Listing Rules. For example, at the moment compensation for loss of office has to be included in the table under the Listing Rules but is excluded from the definition of remuneration in legislation. Also, pension disclosures (the current conflict with LR 9.8.8 is a long-standing problem, with BIS (then the DTI) wanting the UKLA to move into line many years ago) and long-term incentive schemes disclosures need to be harmonised.

Schedule 5 of the Companies Act 2006

The Regulations are intended to revoke and replace Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410) and replace the existing disclosure requirements. Our understanding is, however, that Schedule 5 will continue to require aggregate disclosure of information about the benefits of directors of quoted companies.

We strongly suggest that either Schedule 5 should apply only to companies not within the scope of Schedule 8 (our preference) or that the requirements should be aligned. Differences between the aggregate requirements for unquoted companies and for companies within the scope of Schedule 8 should be eliminated as far as practicable to improve the overall quality of the regulations. The differences in definitions and disclosure requirements between the two schedules will continue to cause complexity and confusion for both preparers and users of information.

Certain existing schedule 8 matters

We recommend that some disclosures included in existing Schedule 8 should remain as they would be useful in the proposed Schedule 8. For example, in the proposed Schedule 8, disclosure of payments for loss of office applies only to persons who have served as directors of the company at any time during the year. The existing Schedule 8 requires disclosure of awards made to any person who has or previously had been a director of the company, thus including payments made in, e.g., the year following the retirement of a director.

Finally, we note that the proposed revised Schedule 8 does not include "sums paid to third parties in respect of a director's services" whereas the existing schedule captures such payments (eg, payments to an investment house whose employee serves as a director of the company in which the investment house is an investor). We note that such payments do not directly represent a benefit to the director in question and that the existing disclosure is presumably required because it is not necessarily possible to identify what element of the person's benefits (eg, from the investment house) actually relate to his services as director (of the investee).

Requirement to present comparative information

Is it intentional that no comparative information is required?

Remuneration consultants

We support the suggestion that companies should be required to disclose the fees paid to remuneration consultants and include disclosure of the services they provided to both the remuneration committee and to management as well as confirmation that no conflicts of interest exist.

Greater scrutiny of the activities of remuneration consultants and how they interact with the remuneration committee could have a significant effect on practices. This could be achieved by building on the work already done in this area by the Remuneration Consultants Group – a group representing the overwhelming majority of executive remuneration consultancy firms advising UK listed companies.

Appendix 4

Other drafting and clarity issues

The table below sets out drafting issues identified so far, in addition to those set out earlier in this response.

Para reference in draft Regulations	Comment
1(4)	The effect of this is that all information in the report must be linked to specific persons. On the face of it, this means the policy part too. Is that the intention?
2	Since there is no statutory "remuneration committee", it would be better to refer to this possible committee of directors in some other way. In fact, paragraph 15 takes exactly that approach and ought to be replicated here.
5(b)(ii)	This refers to "cash dividend[s] *received*". Does this only include actual cash paid in the period or should it also refer to "amounts receivable"?
	The table on page 24 of consultation refers to "dividends received in cash over the vesting period of long term incentives *and deferred awards*" [emphasis added]. However, the draft regulation refers only to long term incentives.
	The reference to "long term incentives" is not defined. How does this differ from awards granted under "Schemes" that are disclosed in column (e)?
7(1)(b) and 33	Benefits include emoluments and emoluments are defined to include "bonuses". So is an annual bonus intended to fall into column (b) or (d)?
5(c)(i)	Presumably what is meant here is, "cash in lieu of pension *contributions*."
6(c)(i) and 6(d)	6(c)(i) refers to "cash value" whereas (d) refers to "cash equivalent", Is a different meaning intended? A definition might be helpful.
6(c)(ii)	The wording here results in double counting in consecutive years. Suppose that in respect of the last month of year 1a contributions of £1,000 arises but that it is paid in the first month of year 2. It would be disclosed in year 1 as "payable by the company for the relevant financial year". It would also be disclosed in year 2 as "paid by the company in that year for another financial year."

6(c)(iii)	We do not understand the logic for requiring a disclosure when there has not been a pension contribution. In such a case this paragraph requires a disclosure that measures (albeit unsatisfactorily) the investment performance. As the director is taking the investment risk (as he is any year in which there is also a contribution), we don't understand why such disclosure could be appropriate.
6(d)	The table on page 24 of consultation includes reference to measurement of the deferred element at face value on date of award. It is not clear what that means and no such guidance/ definition is given in the draft Regulation.
6(e)	Some "short hand" or vernacular seems to have been included here, eg "signed off" (cf approved under section 422) and "remuneration report" (cf, directors' remuneration report).
	We also assume that the phrase, "value of the benefit", refer to 6(e)(ii)'s "value of the shares or share options". Such introduction of new terms makes the drafting confusing. It also raises a question as to whether there could, in fact, be other items falling within column (e) that are not shares or share options and hence there is no provision for their valuation.
7	Is on-going service a "performance condition"? Would a deferred annual bonus arrangement in which an amount determined by reference to a profit target achieved in the current financial year, but paid out at the end of a further two year service period, fall to be disclosed in column (d) or (e)? Intuitively, such deferred annual bonus arrangements would fall in column (d) – the performance conditions relate to the year being reported upon. However, section 7(3)(a) might lead to a different conclusion – namely that a deferred annual bonus should be included in column (e). Section 7(3)(a) excludes from the definition of arrangements to be included in column (e), any payment under section 5(d) the amount of which falls to be determined by reference to service **or** performance within a single financial year. If the arrangement fell to be disclosed in column (d) the equivalent amount would be disclosed in full in year 1, whereas if it fell in category (e) disclosure would be provided in year 3.
	(5) this refers to 7(4)(a), which does not exist.
8(1)	"Variable pay" is not defined. Looking at the disclosures sought, it appears intended to capture remuneration that is based on performance condition or on the exercise of discretion (and therefore picks up everything in columns (d) and (e) as these are defined as dependent on achieving either performance or service condition). To avoid inventing a new, undefined term, or defining it, it would be simpler to require the disclosures in 8(2), (3) for everything ion

	columns (d) and (e)?
8(1), (2)	Requires disclosure as set out in sub-paragraph (2) relating to **any award.** Sub-paragraph (2) then only refers to "in relation to **any shares".** Is it intended that disclosures are only given for shares rather than any other awards granted under Schemes?
6(e)(iii) and 8(2)	6(e) requires disclosure of an estimate of the value of the benefit where full vesting has not yet achieved. Section 8 requires disclosure of the relevant details of "award/ shares that have become receivable", which would suggest that it refers only to those fully vested (if so, simplicity would be aided by using the word "vested"). .
9	What is the denominator in the calculation of the percentage? Is it a percentage of some amount in the paragraph 4 table? The paragraph also seems to assume that deferral could only be in "cash or shares" and not some other specie.
10(2)	This requires details of the person's accrued benefits under the scheme without giving a definition of what is meant by "accrued benefits". Is it just the monetary amount (£x per annum) or also whether it is index-linked etc?
10(4)	We assume that this refers to the split of the column (c) amount between money purchase contribution and defined benefit amounts (eg, x% money purchase contribution and 100-x% defined benefit). However, it is not clear given that it occurs in a paragraph that also deals with accumulated accrued benefits. Furthermore, we are not sure what need such a split would satisfy – it feels like, "just one more disclosure".
11	(a) refers to "what element of pay made up that compensation". We assume that this is asking for the total to be broken down into component amounts that were calculated independently. It would be simpler to say this, especially as the paragraph then leads on to (b) which asks for an explanation of the calculation.
	(d) refers to policy on "exit payments" (undefined) whereas this paragraph otherwise uses the terminology of "compensation for loss of office". Multiple terminology is making the draft Regulations complex. It would be simpler to refer to the policies disclosed under paragraphs 25 and 26.
12	Requires disclosure around "Scheme interests". We assume this refers to those items that require disclosure in column (e). How do these disclosures interact with those required by section 8? Are they intended to refer to all types of scheme interests whereas section 8(2) only refers to shares? Would it be helpful to split the additional disclosure into that relating to (d) only and that relating to (e) only? All awards that fall under (e) will meet the

	definition in the header above section 12 "*performance conditions in future periods*".
13	In addition, to our earlier comments, we assume that this does not refer to the individual, who may not have been a director throughout all ten years, but to a graph of the highest total "single figure" remuneration for each of the ten years. We also note that this requires these new calculations of total "single figure" remuneration to be cast back ten years.
8, 12 and 14	It would be helpful to disclose together with the "Schemes" in section 8 and/or 12 the number of shares/option involved as required by section 14.
14	(a) requires disclosure only for shares/ share options of which the director is legal owner. Does this mean that where the shares are owned through a trust or a company that these are not disclosed?
	Are the conditions in (b)(i)-(ii) cumulative or independent?
18	We suggest that the undefined, "short hand" word "package", which is actually unnecessary anyway, be deleted.
	The definition of emoluments refers to the exclusion of amounts due from "long term incentive schemes". The draft Regulation does not include this term. We presume this is now to be replaced by "Schemes" in section 7(3)?
34 and 7(2)	Both paragraphs appear to deal with amounts payable on taking up a directors' post. Are they intended to deal with two different scenarios?
34	This appears to be based on the current Schedule 8. Eg, the definition of emoluments excludes, as it does in the current schedule, amounts under long-term incentive schemes, but these are no longer defined in these draft Regulations. We wonder whether it would be better to start from a clean sheet of paper not only for Part 6 of the schedule but for the whole regulations adopting new terminology and freshly thought through definitions. After all, the regulations seek to effect a fresh approach to capturing and disclosing remuneration and it seem better to do this by reconsidering all terminology and definitions from the ground upwards.
36	This too appears to be copied from the current Schedule. The requirements regard disclosure of amounts "sums receivable in respect of that year (whenever paid), or in the case of sums not receivable in respect of a period, the sums paid during that year are inconsistent with the requirements in sections 5 and 6.
	(1) is inconsistent with the basis on which at least some of the disclosures

	under columns (d) and (e).

Lane Clark & Peacock

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27 September 2012

Dear Mr Walker

Directors' pay: revised remuneration reporting regulations

I am writing on behalf of Lane Clark & Peacock LLP (LCP) in response to the consultation paper issued in June 2012 containing proposed changes to the remuneration reporting regulations.

LCP is a firm of financial, actuarial and business consultants, specialising in the areas of pensions, investment, insurance and business analytics.

We have limited our responses to question 8 relating to the disclosure of directors' pension arrangements ("***Question 8****: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach").*

Our strong view is that a move to using the HMRC methodology to summarise the value of defined benefit pension schemes would be neither practical nor informative – indeed it could substantially mislead shareholders. In particular the methodology does not appropriately distinguish between different "qualities" of benefit offerings and this would undermine comparisons between different organisations' disclosures; but other elements are inappropriate too.

We believe that a cash-equivalent based system is the best approach – best reflecting the underlying pension rights in the scheme; and valuing the true increase in those rights using a measure which is the same as used for the director's right to transfer, that measure reflecting "cost to the scheme". However, the current cash-equivalent based approach in place should be modified, for a fairer and more appropriate disclosure, by making it consistent with the cash-equivalent based approach that has been used for many years under the Listing Rules.

Yours sincerely

Prepared as an attachment to an email at 17:03 on 27 September 2012

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Law Society of England and Wales, The

Director's Pay - Consultation on revised remuneration reporting regulations

Response of the Law Society of England and Wales

September 2012

Introduction

The Law Society is the representative body for over 145,000 solicitors in England and Wales. It negotiates on behalf of the profession, and lobbies regulators, Government and others. This response has been prepared on behalf of the Society by members of its Company Law Committee, which is made up of senior and specialist lawyers practising in this field.

The Law Society welcomes this opportunity to comment on the consultation paper.

Questions

Question 1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

The draft regulations give effect to the proposals in the consultation document for the provisions required in the directors' remuneration report. Whether the new system of binding votes for policy, and advisory votes for implementation of the policy in the reporting year, will lead to shareholders playing a more active role will not be known for some time and may depend on the extent to which the statements regarding policy become anodyne repetition of boilerplate.

Question 2: What costs will companies face in adjusting to these revised reporting regulations?

In the narrow sense, for the first year that the regulations come into force, companies will have to spend more on professional fees in order to ensure that their directors' remuneration report complies with the new regime.

In a wider sense, the costs of the new approach could be that it may make recruitment more difficult for listed companies incorporated in the UK. Listed companies compete against companies incorporated in other states, non-listed companies in the UK and other forms of employer (including the professions, private equity and hedge funds) for the best talent. If there is insufficient flexibility in the remuneration package that can be offered, UK listed companies could lose out.

Question 3: The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

Yes. Different companies in different sectors will need flexibility to reflect their approach to remuneration.

It is not clear how the statement in paragraph 44 of the consultation document, that the government does not expect companies to be forced to disclose performance metrics where doing so would harm shareholder interests, is followed through in the draft regulations; for example, regulation 19 (d) requires the policy to set out what performance metrics, if any, are used. There does not appear to be any exception where this will harm shareholder interests (save for the broad wording of regulation 38).

Question 4: The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

No comment

Question 5: The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

No comment

Question 6: The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so how a company sought employee views on the remuneration policy.

Companies might just respond that it was considered impractical/too costly to consult employees, as that may be the case for many companies, particularly those with international workforces.

Question 7: The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table on page 24 correctly give effect to this intention?

Yes

Question 8: The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

No comment.

Question 9: The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

No comment

Question 10: The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We believe it would be commercially sensitive to require companies to publish full details of performance against metrics.

Question 11: Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

No comment

Question 12: The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

No comment

Question 13: The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

No comment

Question 14: The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measures would be more appropriate?

No comment

Question 15: The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

No.

We have the following comments on the draft regulations:

(i) There is a typo in regulation 4(e)(ii) – the closed bracket at the end should be deleted.

(ii) The cross references in 7(5) appear to be incorrect (should 7(4)(a) be 7(4); and 6(c)(iii) be 5(c)(iii)?)

(iii) The wording at the end of 10(2) is unclear. The reference to the provision at paragraph 80 of the consultation document suggests that the date the benefit becomes receivable is not an assumption (there is a semi-colon before the wording in the paragraph) but that is not clear from the regulation.

(iv) the word "pay" in regulation 20(b) should be deleted.

Legal & General Investment Management

Our Ref
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Date Date: 26 September 2012

Legal & General
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Dear Mr Walker

Response to Consultation on revised remuneration reporting regulations

Please find attached Legal & General Investment Management (LGIM)'s response to the consultation. LGIM being mainly a passive manager in equities and having £381bn of assets under management as at 30 June 2012 means that we hold significant shareholding in all companies listed in the FTSE All Share. As a mainly passive investor in these companies we have a genuine interest in the long term performance of these companies. LGIM's corporate governance department has been communicating with companies on executive remuneration for over a decade. In doing so, we have been trying to improve transparency and alignment with long term shareholder interests. We consider the proposed improvements to reporting on executive pay will help us in this process.

Since Vince Cable announced that there would be a consultation into the whole area of executive remuneration we have seen a marked improvement to the way in which companies view executive remuneration. We have seen a positive shift by companies to engage more with their shareholders and more importantly to listen to our views. This positive momentum is a direct result of increased interest both by Government and the public.

LGIM responded to the initial consultation and we have had many constructive meetings with BIS over the past year. We believe that it is vital that the resultant regulations not only meet with shareholders needs but at the same time does not hamper a company's ability to recruit and retain talented individuals. The regulations should be aimed at steering all companies to follow best practice, simplify their pay structures, and harmonise returns to executives with those of their shareholder base.

LGIM welcomed this opportunity to assist BIS by providing the attached response. I would be happy to assist BIS further if required at a future date.

Yours sincerely

Angeli Benham
UK Corporate Governance Manager

<u>BIS Consultation June 2012</u>

Q1: The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document.

Part 2

LGIM believes that the Remuneration Committee Chairman should demonstrate a full grasp of the aim of the policy that has been set, how it will be implemented and whether the existing arrangements are meeting their stated objectives.

Although BIS has set out that the Chairman of the Remuneration Committee should produce a statement summarising the key messages on remuneration and the context in which decisions have been taken, this is not reflected in the draft regulations. The schedule sets out the requirement to "summarise the contents of the report". We believe para. 2 should be expanded to give clarity to what is expected, i.e. why the chosen policy is appropriate for their business and give account of any discretionary judgements that were made during the year and why.

Part 3

Para 5 e (i)
This refers to awards that are due to vest in the financial year being reported on. There is a danger here of a mismatch where TSR is used. This is because TSR is usually calculated from the date of grant and not taken from the beginning of a financial year. This can mean that the vesting of the TSR element can fall into the following financial year. This needs to be addressed in the wording to ensure that all elements of the award that are due to vest are captured in the same figure. This mis-match was highlighted to us by a firm of remuneration consultants.

Para 6e(ii) the use of "accrued dividend", - as dividends cannot be accrued another phrase ought to be considered.

Para 7. Benefits

There is a reference to recruitment awards here. We do not believe that these payments should be captured in the benefits column as it will distort comparability. In the same way that exit payments are set out in para 25, we believe there should be a separate para that is headed recruitment policy. Shareholders would expect information on their policy on: buy-out awards – how awards foregone will be treated; international hires, their benefits package, whether this is on-going or for a finite period. What additional payments they received in the first year to aid recruitment, The benefits column should only be used for on-going benefits that extend beyond the first 3 years of employment.

Para 14 – Statement of Director's shareholdings

(a) It should be clarified here, that the current market value should be used when calculating whether directors have met their shareholding requirements.

PART 4

Para 24, Relative importance of Spend on pay.

Part (a) profit and (2) “profit” – this needs further clarity and should refer to operating profit.

Para 30 (1) – this refers to the % increase in pay of the CEO. We believe this should be amended to executive directors.

Q2: What costs will companies face in adjusting to these revised reporting regulations?

The costs associated with the additional disclosure will vary from company to company partly depending on the level of disclosure they currently provide. From Legal & General’s point of view, we estimate the cost will be around. £50,000 in the first year, thereafter the costs will fall.

Q3. The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

The purpose of the new regulation is to ensure consistent and transparent reporting that is easier to read and allow investors to compare companies. If companies are not given a clear steer of what is expected other than the headings in bold, there is a real risk that this will lead to confusion and/or you will end up with the same reports but in a different format. Shareholders want remuneration reports to be shorter but include all the necessary detail for analysis. In order to achieve this there has to be an element of prescriptive regulation or guidance notes.

For example, either in the regulation or guidance notes, there should be an explanation of what is meant by:

- Purpose: It would be sufficient to suggest that it is an explanation of how their remuneration policy supports the company’s short term and long term strategic objectives.
- Operation: summary of how each element of pay operates, whether claw back or malus applies, and what the level of dilution may result from any share based plans.
- Opportunity: Explanation of what the maximum award is and what awards they expect to make and what the monetary value of the award might be if all awards vested. What their policy is on the retrospective disclosure of bonus targets.
- Performance Metrics: A summary of the performance metrics selected, the relative weighting of each, the time period over which they will be measured, whether there will be re-testing, whether there will be any holding period after vesting.
- Changes to policy: what changes or decisions the Committee has made for the future period and why.

In addition, under the current proposals, companies are only required to put the future policy to vote once in three years. It would be very helpful for shareholders if the current policy were to be included in all Annual Reports even if it is not subject to a vote. Perhaps in subsequent years, readers can be made aware that the policy was approved by shareholders on X (being the AGM date). We do not believe this will add significant costs to the company.

Q4. The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

As a shareholder we would welcome better disclosure of what an executive is entitled to under different departure scenarios.. Due the present system of good or bad leaver this has left boards with little room for discretion when they want to remove a director who has not necessarily under performed but due to other factors, i.e. succession. It would be more helpful to shareholders if the Board were to set out in their policy what they consider is a good leaver, what they consider is a bad leaver and what their policy is for those departures which are by mutual agreement. This will hopefully lead to fewer instances of everyone being considered good leavers.

Over the past year, we have seen a number of CEO's stepping down due to poor performance and very little has been paid to them as compensation. This is rare. Introducing another category of leaver may help to alleviate the pressure for boards. However, shareholders expect the Chairman and the board to be rigorous in ensuring there are no rewards for failure.

A chart such as the one in page 18 would be in the implementation section.

Requiring companies to provide details about the total cost of employment and how that compares with the dividends paid to shares holders and the level of free cash flow rather than profit generated would be useful. If BIS chose to use profit, the regulations need to be clear that profit relates to operating profit. However, if these numbers are given in isolation there is a real danger that it may lead to the wrong impression being created. It would be useful if this information was contained within the Chairman's statement where he can elaborate on the numbers so that readers can get a fair idea of the challenges that management have faced during the period. Why this may have led to the outcomes. This would allow shareholders to gain a more holistic view of the results.

Q5. The Government proposes that a company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If any additional information would be useful, please give details.

Companies need a certain amount of flexibility to ensure that they do what is right for the business; however, the suggested information requirements will ensure that all boards spend some time considering their position instead of opting for the easiest solution, i.e. to mark the individual as a good leaver. Please also refer to our response to Q4.

Q6. The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and if so, how a company sought employee views on the remuneration policy.

The guidance set out in the box on page 20 seems sensible. Companies should try to engage with their employees about executive remuneration. But due to the global nature of some companies and the different levels of understanding this may prove rather difficult. We do not believe that this should be a regulatory requirement. In addition, many companies offer share schemes to their employees and as a shareholder they can always register their concerns via a vote at the AGM.

At Legal & General, employees are given the opportunity to participate in an employee satisfaction questionnaire every year. The questionnaire asks you to score on questions such as how satisfied are you with your overall level of remuneration etc. It would not be too difficult to introduce other questions such as do you believe the executive directors pay is appropriate for the performance of the company. The outcome to these questions would provide a level of feedback to the Remuneration Committee on how executive remuneration is viewed by their own employees.

At LGIM we consider it more important to address the disconnection that exists between the pay increases awarded to executives and the general workforce. Over the past year, we have noticed some FTSE companies setting pay levels for executives in line with what has been awarded to staff. This is a good start, but we would like all companies to demonstrate this alignment. Regulation can be useful to steer companies by requiring them to disclose the average pay and increases for staff compared with the average pay and increases for executive directors.

Q7. The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

LGIM participated in the financial reporting lab that considered what should be included in the single figure and therefore supports the disclosures in the table on page 24.

However, we believe further explanation is required in terms of recruitment benefits, in the benefits row of the table. For example, will this include joining on compensatory awards for awards left behind at their previous employer? We believe that both the share and cash and deferred shares should be included within this element. Any shares that are subject to future performance should be deferred but should be noted underneath the table.

These can be substantial costs to the company and clear guidelines are required as to how this is to be treated when no performance conditions govern the awards that are to vest. Retention awards that are only subject to time is another example, although it is rare to find them without performance conditions, they do exist from time to time. A recent example is Darty AGM 2012.

All types of payments should be accounted for.

Q8. The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

This was also a matter considered by the Financial Reporting Lab in which participated and therefore support the use of the HMRC methodology as suggested.

Q9. The Government proposes that claw-back is recorded as part of the single figure. Is this practical and informative approach?

We do not believe that claw back should be applied to the single figure. This will distort the actual remuneration for the year and therefore analysis over a number of years. We believe that any claw-back should be detailed elsewhere perhaps below the single figure, with a note to explain the circumstances under which it was applied.

Q10. The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

LGIM expects companies to disclose the relevant performance conditions that gave rise to a bonus award or long term incentive awards that have vested. If there is some commercial sensitivity in announcing the targets prior to the award being made we expect companies to disclose the target and the performance on a retrospective basis.

However, from experience, there are some companies that believe regardless of the time that has elapsed, this information remains commercially sensitive. We would seriously question this argument. However, if for these companies a slightly different approach could be selected in that they provide an explanation of where the performance lied within their target range. Was the performance at threshold, between threshold and target or exceeded exceptional performance? This would still give shareholders some idea of the level of stretch that had been applied to the targets.

Q11. Will the Government's proposed disclosure requirements on pensions lead to reporting sufficient information on benefits received by directors?

The additional disclosure requirement for defined benefit schemes is sufficient.

Q12. The Government proposes that scheme interests awarded to directors during the reporting year are disclosed as face value. Is this a practical and informative approach?

Using face value is the best methodology as it is easily understood by all participants and enables comparisons to be made between companies. The ability to do this would be hampered if expected value is used as the assumptions relied upon would not be universal.

Q13. The Government propose to simplify the reporting requirements regarding director's interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

It would be extremely helpful to shareholders to simplify the disclosure as set out on page 30. Any additional costs of doing this would be minimal as all of the data is already available.

It is very important that a distinction is made between those shares that are owned outright and those shares that are subject to a holding period or performance conditions. We have come across a couple of companies that have combined the two types of shareholdings and suggested that a director has met his shareholding guidelines. In addition, it is vital to require that shares held should be calculated using the market value on a specific date, i.e. when the annual report for the year is published or the close of business when the full year results are announced. A company we have had dealings with were found to have used the share price at the date of purchase to justify the director's shareholdings and did not take into account that the shares had fallen in value since the date of purchase.

Another point to consider is whether family or connected party shareholdings should also be disclosed as this can in some cases be a sizeable shareholding in the company.

Q14. The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for company performance, against CEO pay. Do you agree that this graph would be useful? If so, do you agree that total shareholder return and CEO pay are the best proxies for company performance and pay? If not, what measure would be more appropriate?

We agree that the current disclosure graph is of limited use. The suggested graph that compares the CEO's remuneration against TSR would be valuable. What would make the output from the graph even better is if a ten year graph can be annotated to highlight changes in CEO during the period.

Another point to consider is the considerable time and resource that will be required to ask companies to obtain this level of information for the past ten years. It will be further complicated if during that period there have been a number of changes to the position of CEO. The record keeping at smaller companies may not be adequate to provide this level of historic information. We would recommend BIS to consider starting the historic reporting at 5 years ago and to build up the data over time to become a ten year graph.

Companies may argue that total shareholder return does not give a true and fair view of the performance of the company but we believe it is a good proxy for gauging the value delivered to shareholders vs the value delivered to the CEO, by way of remuneration. Regulation should make it clear that the CEO pay is total remuneration.

Q15. The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

The above list covers the most important areas where shareholders would require assurance.

Legal & General PLC

Mr Barry Walker
Executive Pay Consultation
Department of Business, Innovation and Skills
1 Victoria Street
SW1H 0ET

26th September 2012

Dear Mr Walker

<u>Legal & General Group Plc Response to BIS Consultation on Revised Remuneration Reporting Regulations</u>

I am writing on behalf of Legal & General Group Plc and attach our response to the BIS consultation on the Revised Remuneration Reporting Regulations. Overall, we welcome the proposals to simplify the format of reporting and provide a consistent approach across companies as well as the aims to make the disclosures as simple and transparent as possible. We feel we already support this approach within our own Directors' Remuneration Report.

Our key concerns are as follows :

- We feel that in many instances it would be commercially sensitive to publish full details of performance against metrics. Often objectives form part of a longer term goal and reward may be against key milestones. Publishing these would give away commercial sensitive or strategic information – see question 10;
- We are concerned that the comparison of CEO pay and company performance may be misleading – see question 14;
- We do feel that the Policy part of the document should be published each year, even if no changes are made. This will ease referencing the Implementation section.

We have responded to the specific questions below. However, there are also some areas we feel we should highlight in respect to implementation and that require further clarification and these are set out below. We have received informal responses to these questions but feel that they need formal clarification. They are in no particular order.

- If companies get to the first year of the binding vote on policy and their policy is the same as in previous years we understand they still have to restate this and receive a vote. Please can you confirm this is correct?

- During the first year, a Company may be implementing pay decisions on a current policy and also providing a new / amended policy on which to vote for the future. In these circumstances, we understand that two policies would have to be provided in the Remuneration Report or, at least, a clear indication of where changes are being made. This could cause confusion unless clearly explained.

- We think it is important that existing executive awards made before the requirement comes out for shareholder vote are preserved, notwithstanding that these may become out of line with the policy proposed for approval. It should be clear that the policy that goes to vote is forward looking and only applies from the nominated date.

- Given that implementation is for financial years ending after October 2013, we wonder if this is sufficient time for companies to develop their policy thinking and engage with stakeholders.

- If all companies take their policies to the 2014 AGMs this will mean a large volume of work for shareholders to review. If every company's timing is the same, this volume of work will repeat itself every three years. While this may rectify itself over time if companies make changes to policy more frequently, we draw attention to this in case shareholders have a view.

- On page 10 of the consultation document, it is proposed that Companies need to response to shareholders if a "substantial minority" vote against the policy. We would welcome clarification on what constitutes "substantial". In addition, we would welcome clarification in terms of timing to respond to shareholders – the earlier consultation referred to a company being forced to issue an RNS within 30days which we feel is impractical.

- Consideration may need to be given in relation to what constitutes a "material" change to policy that needs to have new shareholder approval. For example, would a change in weighting of executive directors' objectives between financial, strategic and personal constitute a material change?

Please find our full responses below. Thank you for the opportunity to comment on this consultation. If you have any questions regarding our response or wish to clarify any of the points, please do not hesitate to get in touch with me.

Yours sincerely

Rosemary Lemon
Group Head of Executive Remuneration & Reward
Legal & General Group Plc

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Section 1 : Policy

Question 1 : The Government seeks comments on how well the draft regulations attached at Annex B give effect to the policy set out in this consultation document?

Part 1 Introductory, (3) – page 42
The regulations specify that the Policy part of the report need not be published in the report & Accounts if it has not changed from the previous year but can be referred to on the Company's website. We believe this will make it hard for shareholders to relate remuneration decisions outlined in the Implementation report to the policy when they have two different locations and think that it would be better to republish the policy each year but with a comment that says No Change.

Part 3, 6 (e) (ii) (XY) – page 43
This suggests that the value of accrued dividend needs to be added to LTIP shares that have vested. We would suggest that dividends cannot be awarded retrospectively on performance shares as they would not have been earned or vested at the time the dividend was paid.

Part 3, 13 (2) – page 45
As per Question 14 below, we do not feel it is practical to go back 10 years and report CEO total remuneration against TSR. There may have been several CEOs over this period and to calculate a single figure under the new basis retrospectively over ten years is not practical.

Question 2 : What costs will companies face in adjusting to these revised reporting requirements?

The majority of the information required for the new format is already available and reported on. However, this information will need re-formatting and organising to meet the new reporting layout. It is envisaged therefore that the cost of producing the report for the first time will be higher in relation to :

- re-organising the layout of existing information;
- writing the new policy section in a way that is easy for shareholders to understand what they are approving and that ensures agreement is given to all elements of a policy that is sustainable for three years;
- adding additional requirements and tables;
- in the year of introduction, clearly setting out existing policy for current awards as well as policy going forward for approval;
- if companies choose to introduce the new format early, then there will be a cost of providing both new information and providing current information eg regarding shares that is still required under current reporting legislation;
- audit costs;
- potentially higher costs for remuneration advisers and consultants.

Costs will be associated with additional time for writing, review and collating data, possible external advice on the new requirements and layout redesign before print. There will also be additional audit costs. These costs will vary depending on a company's existing level of reporting. At Legal & General, we have re-designed our Remuneration report to see what it would look like in the new format and to help see any issues raised under this consultation. This initial high level review and layout has cost approximately £12,000 excluding internal time.

Question 3 : The Government intends to introduce a table which sets out the key elements of remuneration and supporting information on the pay policy. The Government does not propose to prescribe the specific disclosures that are required for each element of pay. Is this a practical and informative approach?

We believe it will be helpful for investors to have the policy for each company set out in a consistent way. It is important that investors and shareholders are comfortable with the broad headings and principles of the policy. We foresee that some companies may struggle with the level of detail they need to give and what may constitute a material change that requires re-approval from shareholders.

Question 4 : The Government intends to introduce reporting requirements on service contracts, what remuneration directors can receive in different scenarios and the percentage change in profit, dividends and overall expenditure on pay in the reporting period. Is this a practical and informative approach? If an alternative disclosure would be useful, please give details.

Information is already provided regarding service contracts and we support the disclosure of any contractual entitlements.

We also support the provision of charts to show the proportion of remuneration relating to below, on target and maximum remuneration opportunity. However, in relation to the example shown in the consultation paper, we would not expect to see payment of LTIP in a below target situation. It would also be helpful to clarify how the components of the chart should be calculated eg should LTIP be at face value, how should pension be valued, in order to ensure the comparisons across companies are consistent in approach.

While we are supportive of highlighting the link of pay to individual and Company performance, we are concerned about reporting the overall expenditure on pay and relating it to overall performance. It is not clear whether expenditure on pay relates to just directors' remuneration or total company expenditure. If total company expenditure, then this information could be misleading as the level of pay cost may depend on the structure of the Company and be affected by issues such as outsourcing. It may also vary according to a Company's industry. If it is limited to the executive directors' remuneration costs, then these may also be difficult to relate directly to profit – for example, in a time of severe economic crisis it may be a significant achievement to maintain profit at previous levels and reward directors for maintaining this level in difficult circumstances. The ratio of remuneration to profit or other financial metrics may therefore not reflect the circumstances upon which the reward is based. We feel that the background to pay and bonus decisions should be clearly explained and should have strong ties to performance but are wary of investors drawing the wrong conclusions from using a ratio in the way described.

In addition, for more international companies, this may not work for international contracts when some allowances may be given overseas.

We note too that this information is requested under the Policy section. We feel that any changes in profit, dividends etc should be reported in the Implementation report as these will change from year to year and, if contained in the Policy section, may only be published every three years if the policy does not change.

Question 5 : The Government proposes that a Company's statement on its approach to exit payments sets out the principles on which the determination of the payment will be made. If additional information would be useful, please give details.

We agree that it is important and helpful to set out the principles on which exit payments are determined. However, depending on the circumstances of departure, it should be recognised that a degree of flexibility may be required to facilitate an exit in the best way for shareholders and investors.

Question 6 : The Government would welcome views on the proposal for the policy part of the remuneration report to include a statement on whether and, if so, how a Company sought employee views on the remuneration policy.

We are supportive of explaining the pay policy for below Board insofar as it provides context and a view of how the organisation regards its remuneration philosophy across the Company and provides a link between executive pay and other employee pay.

However we feel that information about how the pay policy for the wider organisation has impacted upon the *decisions* taken by the Remuneration Committee should appear in the Implementation policy as decisions on pay will change from year to year, even though in line with overall policy.

We are pleased that the Government has taken into consideration the previous consultation views on the ratio between CEO pay and the median earnings of the organisation's workforce and has decided not to make this a requirement.

With respect to seeking employee views on the remuneration policy for the executive directors, we do not feel this would be appropriate.

There would potentially be issues with confidentiality of strategy.
The Remuneration Committee members are supposed to be independent and suitably qualified to make decisions and their integrity and views should, therefore, be trusted.

We also believe that employees who hold shares are already shareholders and have the ability to vote on resolutions at the AGM. This would mean they could express their views on the policy for executive directors.

In addition, internal employee surveys can indicate engagement with and understanding of remuneration philosophy.

Executive remuneration is a Board matter and members of the Board are best placed to make decisions in this respect. We do not feel that there is an appropriate role for employees in setting executive remuneration policy.

With regard to taking into account shareholder views and disclosing information in this respect, we are very supportive of engaging with shareholders and are happy to demonstrate how views were taken into account in setting policy.

Section 2 : Implementation

Question 7 : The Government's intention is that the single total figure includes remuneration that becomes receivable as a result of the achievement of conditions relating to performance in the reporting year where the reporting year is the last year of the performance cycle. Do the specific disclosures set out in the table below correctly give effect to this intention?

Legal & General participated in the Financial Reporting Lab's project on the single figure and feel the overall approach is appropriate.

Question 8 : The Government proposes the application of the HMRC methodology to work out the value of defined benefit pension schemes. Is this a practical and informative approach?

We feel this is an appropriate method of valuing DB pensions in the UK. We appreciate that this may not work as well for overseas schemes.

Question 9 : The Government proposes that claw-back is recorded as part of the single figure. Is this a practical and informative approach?

Yes, we are supportive of reporting any claw-back in the Single Figure as this will have affected the total remuneration received for the year. However, we feel this should be set out separately within the single figure and clearly explained so it is transparent as to which year / circumstances the claw back relates and does not "cloud" the reporting of remuneration in relation to performance in the current year.

In addition, we feel it is important to distinguish between indirect clawback ie where an LTIP award entitlement is reduced due to circumstances and actual clawback where money already paid or vested is asked to be returned or a deferred award is reduced or taken away.

Question 10 : The Government would welcome views on whether it would be commercially sensitive to require companies to publish full details of performance against metrics. If so, how can an appropriate degree of flexibility be achieved?

We feel that in many instances it would be commercially sensitive to publish full details of performance against metrics. Often objectives form part of a longer term goal and reward may be against key milestones. Publishing these would give away commercial sensitive or strategic information. However, where possible we would encourage transparency in terms of performance and it should be clear from the overall results of the Company together with any associated narrative given in the Report & Accounts whether awards are merited. We feel that shareholders will hold companies to account in both informal engagement and on the advisory vote if companies do not achieve a sufficient balance between protecting commercially sensitive information and providing transparency on how performance was measured for remuneration.

We support publishing the level of deferrals and the vehicle of deferral.

Question 11 : Will the Government's proposed disclosure requirements on pensions lead to reporting of sufficient information on the benefits received by directors?

We feel that the disclosure required on pensions should give sufficient information to investors and shareholders.

Question 12 : The Government proposes that scheme interests awarded to directors during the reporting year are disclosed at face value. Is this a practical and informative approach?

We feel this is the most appropriate approach providing that there are clear notes about performance criteria and levels of vesting to ensure that the maximum value is not misleading and considered a guaranteed level of payment. Notwithstanding the additional disclosures in relation to the single figure, there remains a risk that audiences less familiar with, or educated about, remuneration structures, such as the media, might draw inappropriate conclusions by looking at the single figure alone.

While the questions do not specifically address this issue, the consultation document also suggests that exit payments should be broken down into key elements, how these were calculated and how decisions made relate to policy. While we are supportive of transparency, some exit arrangements are in relation to complex issues and subject to legal agreement and it may not always be appropriate to fully disclose all calculations. However, we agree that sufficient information should be given to assure that exit payments have been in accordance with policy principles.

Question 13 : The Government proposes to simplify the reporting requirements regarding directors' interests. What are the costs and benefits of this approach? If an alternative disclosure would be more useful, please give details.

We support this approach – we believe that the report should provide clarity and transparency and a simplified approach supports this.

We would recommend that the current share market value is used for calculating this and not the historic market cost as this can be misleading.

We would, however, welcome clarity over whether, under the new requirements, we are obliged to include family holdings?

Question 14 : The Government proposes that the remuneration report includes a graph that plots total shareholder return, as a proxy for Company performance, against CEO pay. Do you think this graph would be useful? If so do you agree that total shareholder return and CEO pay are the best proxies for Company performance and pay? If not, what measures would be more appropriate?

We do not feel that such a graph would provide a meaningful comparison of company performance and pay. As stated, over a period of time there may be several Chief Executives whose pay may vary according to experience and whose influence on Company performance may not be seen immediately. In addition, in times of volatile economic climate, reward may be given for maintaining the Company in a status quo and such a chart may therefore be misleading.

We believe that the other details of performance given in the report combined with the Company’s results both in financial and narrative form, should provide the backdrop for investors and shareholders to obtain a view on pay for performance.

In addition, we note that the graph provided covers a ten year period. If such a graph was produced, we would not propose to give an historic picture. Recalculating a single figure going back ten years for what, as you say, could be several chief executives, may be difficult for many companies.

Question 15 ; The Government proposes that the single figure, detail of performance against metrics, total pension entitlements, exit payments made and detail on variable pay are all subject to audit. Are there any other sections of the report that should be subject to audit?

We consider that shareholding information should be audited to ensure full transparency.