Regulatory Policy Committee	**Opinion**	
Impact Assessment (IA)	Improved transparency of executive remuneration reporting	
Lead Department/Agency	Department for Business, Innovation and Skills	
Stage	Final	
IA number	BIS0355	
Origin	Domestic	
Expected date of implementation (and SNR number)	1 October 2013 (SNR6)	
Date submitted to RPC	30/5/2013	
RPC Opinion date and reference	13/6/2013	RPC12-BIS-1372(3)
Overall Assessment	**GREEN**	

RPC comments

The IA is fit for purpose, but should be improved in a number of areas prior to publication.

Background (extracts from IA)

What is the problem under consideration? Why is government intervention necessary?

Over the last decade, director remuneration in the UK's largest listed companies has increased rapidly with little evidence that this is a result of improved performance. Pay policies which fail to align the incentives of directors with shareholders due to information asymmetries are economically costly through diminished shareholder returns, weakened corporate governance and constitute a market failure. The problem being considered is how to improve the informative content of company reporting on directors' remuneration in order to enable shareholders, as the owners of companies, to engage effectively in the pay-setting process, save time and engage more effectively on other aspects of the business. The current regulatory regime has failed to secure adequate reporting standards and not kept pace with developments in remuneration policy, justifying a refresh of the regulations.

What are the policy objectives and the intended effects?

The policy objective is to address failures in the governance of directors' pay through targeted reforms of remuneration reporting requirements which will provide shareholders with the clear, high quality and consistent information they need to make effective investment decisions. Shareholder empowerment lies at the heart of the UK's corporate governance framework and the proposed reforms are consistent with that approach. Access to clearer remuneration reports places shareholders in a stronger position to challenge unjustified pay policies, which should encourage greater engagement with companies and ultimately steer corporate pay setting behaviour towards an approach that links rewards more closely to performance.

Comments on the robustness of the One-in, Two-out (OITO) assessment

The IA records that this is a regulatory proposal (an IN) with an equivalent annual net cost to business of £5.2 million. This is consistent with paragraph 2.9.10 of the Better Regulation Framework Manual (March 2013) and provides a reasonable assessment of the likely impacts.

Comments on the robustness of the small & micro business assessment (SMBA)

The proposal does not regulate small and micro business and therefore the SMBA is not applicable. The IA should make this clear in accordance with the Better Regulation Framework Manual (paragraph 2.6.6).

Quality of the analysis and evidence presented in the IA

Recurring costs. The Committee's red-rated opinion (15 March 2013) questioned why the IA provided no estimate of recurring costs when it acknowledged that these *"…are not likely to be strictly zero in practice..."* The revised IA continues to hold that the best estimate of these costs is zero on the basis that *"…much of the additional detailed information will be readily available at no or limited additional cost...and already forms part of the decision-making process within remuneration committees…"* (paragraph 74). The IA states that this position is supported by consultation respondents, but the IA would be improved by explaining more clearly why the requirement for businesses to describe and explain to shareholders the links between the pay of their executives and the performance of the business, in terms of both future policy and past outcomes, would involve no recurring costs.

Transitional costs. The Committee previously questioned why these costs were estimated excluding any costs to investment companies. This reduced the estimate from potentially £90 million to £59.5 million. The Committee's opinion (15 March 2013) asked for evidence from investment companies themselves to justify their exclusion. The revised IA (paragraph 66) provides evidence from investment companies' representative body to explain why such companies would not incur any costs from the proposal.

Benefits. The revised IA provides some estimates of benefits in the form of time savings for remuneration committees with respect to *"…explaining pay."* (paragraph 52). The IA states that the benefits from improved company performance *"…are indirect,* [and] *extremely difficult to quantify…"* (paragraph 89). It also states that the actual outcome could depend on a range of factors, not least *"…on the behaviour of individual shareholders and companies…"* (paragraph 41). The treatment of such benefits as being indirect is in line with paragraph 2.9.33 of the Better Regulation Framework Manual (March 2013) and appears a reasonable assessment. However the IA would benefit from a more detailed explanation of why these benefits are classed as indirect.

The IA also provides (paragraph 44) estimates of the increase in market capitalisation and operating profits of businesses that would be greater than the costs of the proposal. While this is useful information it does not explain how the proposal would bring about benefits of at least this scale.

Impact of proposal and alternative options. The IA says that the costs of the proposal would be *"...significantly outweighed by ... improvements in company performance…"* (page 5). However, on the basis that the costs are considered to be relatively low and one-off (because gathering information necessary to comply with the proposed new framework is no more burdensome that that required by the current reporting framework - page 3), it is not clear that there will be significant benefits from this proposal.

Further, the IA records that, for OITO purposes, the proposals would have a net direct cost to business. The IA would therefore be improved by explaining more clearly how this conclusion has been reached and also, given the inherent uncertainties surrounding future benefits, why the optional "*de minimis*" approach was not adopted, at least initially. Within this context, the IA would also be improved by explaining more clearly how any future evaluation would estimate the actual impact of the proposal.

Signed	**Michael Gibbons,** Chairman