

Executive Remuneration: Discussion Paper. Response form

Please send your response by: 25 Nov 2011

About You	
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I am responding on behalf of (please tick)	
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Questions

Role of shareholders

1. Would a binding vote on remuneration improve shareholders' ability to hold companies to account on pay and performance? If so, how could this work in practice?

Yes	No
	No

Comments

We do not support a binding vote on remuneration. We believe that shareholders already have the ability to hold directors' accountable on remuneration through the re-election of directors. We are unsure what a binding vote on remuneration would achieve and are sceptical of its aim to improve shareholders' ability to hold companies to account on pay and performance. Shareholders already have access to all directors and so there is no need to change the way they interact. We believe that shareholders will only re-elect executive directors if they are happy with their performance and remuneration planning plays a significant part in this.

We feel that the Remuneration Committee Chairman is seen as a more important role than the Audit Committee Chairman. This shows that executive remuneration is a hot topic for both shareholders and boards and that there is a need more than ever for shareholders and boards to interact on this subject.

However, we believe that a binding vote is a blunt tool that can present a number of practical difficulties – for example, what occurs when a binding vote is not passed? How does the committee react? What effect would it have on service contracts of directors or bonuses paid out ahead of the AGM? How do companies address the different concerns that shareholders may have and unpick pay packages?

Remuneration committees need to become more attentive to concerns of shareholders and shareholders in turn must be more engaged with the committees over pay matters. However, we are not sure that a binding vote on remuneration will help to achieve and encourage effective engagement. Engagement on remuneration should be year round and not just after the notice of an AGM and/or at the AGM.

2. Are there any further measures that could be taken to prevent payments for failure?

Comments

Companies and investors should be encouraged to continue developing practices such as phased termination payments and proper performance conditions, which will reduce the scope for discretionary additional payments other than for work done. Directors are also already prevented from receiving ex gratia payments.

We would caution against the creation of legislative measures in this area, as we believe that developing a body of best practice will have a more positive effect on influencing behaviours than regulation.

3. What would be the advantages and disadvantages of requiring companies to include shareholder representatives on nominations committees?

Comments

To have shareholder representatives on nomination committees is very difficult in practice. The main issue is whether the larger shareholders are representative of all shareholders. Larger shareholders will have different interests to other minor shareholders. This is why trust on the nomination committee is so vital. The representatives involved with the nomination committee are responsible to represent all shareholders and, if only certain shareholders are

involved with these committees, it is highly likely that a conflict of interest may arise.

Another major issue is insider information. As mentioned in the consultation paper, shareholders wish to avoid becoming a company 'insider'. Shareholders in small and mid-cap quoted companies already have difficulty trading their shares at times due to liquidity issues; if they are also 'insiders' to the company, this would become ever more difficult.

Role of remuneration committees

4. Would there be benefits of having independent remuneration committee members with a more diverse range of professional backgrounds and what would be the risks and practical implications of any such measures?

Comments

We believe the costs and legal difficulties of having independent remuneration committee members would outweigh any benefit. This proposal would be particularly difficult for small and mid-cap quoted companies, who already have difficulties recruiting skilled and independent non-executive directors.

As outlined in paragraph 85 of the consultation paper, the legal implications of this proposal are significant and definitely undermine directors' responsibilities to shareholders, the UK's director liability regime and the current basis of UK company law. Unless these independent committee members are elected directors they would not be directly accountable to the owners of the company – this highlights the issue of accountability.

We note that remuneration committee members should already be independent, and it is the responsibility of shareholders to challenge any company's remuneration committee membership where they believe independence is lacking. We view it as more practical and cost-effective to encourage boards to appoint those that have remuneration experience, and to more generally promote diversity on boards, which is an underlying principle of the UK Corporate Governance Code.

Ultimately, what matters is that the remuneration committee does its job well. The Quoted Companies Alliance understands that this is not always the case and is in the process of developing a Remuneration Committee Guide, which will help develop best practice for small and mid-cap quoted companies.

5. Is there a need for stronger guidance on membership of remuneration committees, to prevent conflict of interest issues from arising?

Yes	No
	No
Comments	
We do not believe that this issue is as prominent as suggested in paragraph 86 of the consultation paper in the context of small and mid-cap quoted companies.	

6. Would there be benefits of requiring companies to include employee representatives on remunerations committees and what would be the risks and practical implications of any such measures?

Yes	No
	No
Comments	
<p>We believe this would result in a severe conflict of interest and we do not support employee representatives on the remuneration committee. The employee representative on the remuneration committee would have a completely different agenda to that of the other members of the committee. It is nearly impossible to have one employee represent all the different employees in the group.</p> <p>There would also be difficulties for directors in terms of their fiduciary duties to shareholders and questions surrounding the accountability of non-directors to shareholders. Moreover employee representatives would not be privy to the board's discussions on strategy, risk and other matters that are key to developing a pay policy and structure.</p> <p>We also believe that the costs of implementing this would be an additional burden for small and mid-cap quoted companies.</p>	

7. What would be the costs and benefits of an employee vote on remuneration proposals?

Comments
<p>We do not believe that having an employee vote on the remuneration proposals would provide significant benefits to the company or employees or result in effective engagement on the issue.</p> <p>We believe that companies should be encouraged through best practice to engage with employees as much as possible about how remuneration is linked to company performance and strategy. However, we do not believe that this should be mandated, nor should it be expressed solely through a vote. Voting does not replace the need for constructive and on-going engagement.</p>

8. Will an increase in transparency over the use of remuneration consultants help to prevent conflict of interest or is there a role for stronger guidance or regulation?

Yes	No
Yes	
Comments	
<p>We believe that an increase in transparency over the use of remuneration consultants is the preferable option.</p>	

In Question 26 of our response to BIS's consultation paper on narrative reporting, we agree that the level of fees paid to remuneration consultants may, in some cases, result in a conflict of interest. However, we do not believe that disclosing the fees paid will help to prevent this conflict of interest or increase transparency by itself.

It is key that remuneration committees satisfy themselves and investors that remuneration committees are independent. As such, we would recommend that companies disclose any services provided by the remuneration consultant's firm together with how the committee has determined its independence. We believe that this should be encouraged through promoting best practice, rather than strict regulation.

Structure of remuneration

9. Could the link between pay and performance be strengthened by companies choosing more appropriate measures of performance?

Yes	No
Yes	
Comments	
<p>The link between pay and performance can almost always be strengthened by moving away from TSR and EPS as the key measures of performance. However we do not necessarily believe that one metric is appropriate for use by all companies and each has its positives and negatives.</p> <p>In Question 20 of BIS's Narrative Reporting consultation paper, we noted that there are a number of performance measures that could be disclosed by companies over a 5 year period, including:</p> <ul style="list-style-type: none"> i. TSR (in absolute terms) ii. TSR relative to an index (eg FTSE Small Cap, or mid 250) iii. TSR relative to a sector or specified group of companies. (sophisticated fund managers judge management on a relative basis and make investment decisions on whether they expect companies to do better than their peers.) iv. Earnings Per Share v. Profits before tax and exceptionals vi. Turnover 	

10. Should more companies be encouraged to defer a larger proportion of pay over more than three years?

Yes	No

Yes, but not through regulation	
Comments	
<p>We agree that this is best practice, but we do not believe that a three year period should be mandated through regulation. This is an area where companies need to have discretion. There must be flexibility to allow companies to grow their businesses and choose options that are most appropriate for them.</p> <p>Companies' explanation and engagement with shareholders is key to ensure that they have support for the vesting periods they adopt. We believe that this engagement will increase the alignment of shareholders and directors interests and encourage the directors to hold onto their shares for the long-term.</p> <p>We would caution against a one-size-fits-all approach to this.</p>	

11. 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?

Yes	No
Yes, but the frequency for review should not be regulated	
Comments	
<p>We agree with the consultation paper that companies should be focusing on identifying the appropriate long-term performance measures from the outset of setting out plans. We believe that practically this is a difficult area to regulate, as practice varies from company to company. Sometimes regular review of performance conditions and plans are appropriate and other times they are not.</p> <p>Additionally, it is not just companies that initiate creating new plans - sometimes investors request new plans are constructed for the company to ensure that executives are incentivised appropriately.</p> <p>We would prefer encouraging best practice in this area and stress the need for shareholders to engage with companies to encourage regular, and less frequent review, of long-term incentive plans.</p>	

12. Would radically simpler models of remuneration which rely on a directors' level of share ownership to incentivise them to boost shareholder value, more effectively align directors with the interests of shareholders?

Yes	No
Yes, but we do not believe that this can be regulated	

Comments
<p>Yes. We believe that simpler models of remuneration that rely on directors' level of share ownership to incentivise them to boost shareholder value will effectively align directors' interests with shareholders.</p> <p>However, there is a debate as to whether it will achieve the right motivation. Shareholders may not want to sacrifice some of their ownership within the company, so to surrender shares would not be an ideal outcome. Conversely, there may be other shareholders who feel that giving directors' cash bonuses can leave the company financially less secure and so favour issuing shares as an alternative.</p> <p>While simplifying incentive plans is an important aspect to consider, we would not support legislative action that designs directors' pay packages, as each company is different and there would be no one-size-fits-all model that works for all companies.</p>

13. Are there other ways in which remuneration - including bonuses, LTIPs, share options and pensions – could be simplified?

Yes	No
Yes	
Comments	
<p>We do not have any specific suggestions at this time as to how remuneration could be simplified, but fully support the Office of Tax Simplification's current review on share schemes as a first step in this process.</p> <p>We do think it is important that companies have flexibility to adopt remuneration structures that are most appropriate to their businesses and this will inevitably mean that there is no one model that will work for all. While remuneration should be simplified throughout companies, shareholders should more generally be encouraged to engage with companies to encourage explanations as to why their specific remuneration structures are most appropriate for their company and strategy.</p>	

14. Should all UK quoted companies be required to put in place claw-back mechanisms?

Yes	No
	No
Comments	
<p>We believe that it is already best practice for companies to have in place some form of claw-back mechanism. Again, this an area where flexibility should be maintained for companies to decide what is most appropriate for their company and this should not be mandated.</p> <p>We believe there may be other action that the Government could explore rather than mandating claw-back mechanisms. We would note that encouraging greater deferral of payments to directors and appropriate vesting periods would achieve the same aim as</p>	

requiring claw-back mechanisms. Additionally, companies can be reluctant to use claw-back mechanisms currently, while the tax and employment law implications are unclear. If the Government were looking to encourage companies to put in place in claw-back mechanisms, it would be useful for the Government to clarify these implications.

Promoting good practice

15. What is the best way of coordinating research on executive pay, highlighting emerging practice and maintaining a focus on the provision of accurate information on these issues?

Comments

We do not believe there is a need for an independent body to collate information on executive pay. There are already a number of bodies that monitor this and report on it, including the Association of British Insurers, Risk Metrics, Pirc and Manifest.

Executive pay is also an issue that is monitored and regulated to a certain extent by a number of different regulators, for example the FSA and the Listing Rules and the FRC and the UK Corporate Governance Code. So any monitoring by an additional body may cut into work already done by other regulatory bodies.