

## Directors' remuneration report

### Guidance on the implementation of the new regulations



**Best practice guidelines to assist companies and their investors to successfully implement the new disclosure regulations have been published by the GC100 Investor Working Group.**

The guidance was developed by representatives of the Corporate Governance Forum (an informal network of leading UK Institutional Investors) and the association for the general counsels and company secretaries of companies in the FTSE 100 (GC100). A range of representative bodies and other relevant parties were consulted during its development. It is intended that this guidance will evolve over time and will be updated to ensure it remains relevant.

Key points emerging from the guidance include:

#### **Part 1 - Introductory**

- A recognition that the policy report will need to incorporate a degree of flexibility and that it should allow for the use of judgment and discretion which is considered an important way for the remuneration committee to ensure that the application of arithmetic targets or metrics produces 'fair' results. The guidance does not recommend including a general statement that all elements of remuneration are subject to the discretion of the committee. Remuneration Committees are expected to consider the flexibility, judgment and discretion that they will or may require under each component of remuneration.
- The guidance makes a clear distinction between judgment that is routinely used by the remuneration committee, for example when assessing achievement of targets, versus discretion. The use of judgment, e.g. to determine whether a relevant objective has been satisfied, does not need to be disclosed under the regulations as part of the requirements relating to discretion.
- Companies may want to consider including the policy report in the remuneration report each year irrespective of whether shareholders are being asked to approve it. However,

investors do not favour companies seeking approval for the Policy Report every year.

- Commercial sensitivity – investors do not want commercially sensitive performance targets to be disclosed but will expect disclosure when they cease to be commercially sensitive, justification of the decision not to disclose and an indication of the degree of stretch of the targets.

## **Part 2 – annual statement**

This is considered an important element of the report which sets the tone and should be a personal reflection on the committee's decisions. The guidance includes some of the things that could be included in this section:

- Remuneration philosophy and relationship with business strategy
- How company performance during the year is reflected in remuneration outcome
- A summary of any discretion applied during the year
- Challenges and issues addressed by the committee in the year
- Intended remuneration arrangements for the coming year
- Comment on stakeholder engagement
- Any changes to policy

## **Part 3 – annual remuneration report**

### **Single figure of remuneration –**

Format: the guidance suggests that companies show data for executive and non-executive directors in separate tables.

Other remuneration: Any remuneration that does not fall within the five headings (salary, taxable benefits, short term incentives, long-term incentives and pensions) should be added in separate columns (e.g. promise to pay, not caught in pension disclosure, SAYE and SIP schemes, retention bonus, benefit on which no tax is payable due to an exemption). The guidance adds that if the tax liability on benefits is paid by the company this should be included as part of the benefits value.

Negative value: the guidance states that the loss of vested but unexercised option on termination should be reported as a recovery.

**Payments to past directors** – the regulations specifically exclude payments in respect of employment with, or any other contractual service performed for, the company other than as a director from the payments to former directors' disclosures. However, the guidance suggests that companies should consider disclosing when a former director is appointed to the pension trust, charitable foundation or other connected organisation. The guidance also appears to suggest that some companies may also consider whether it would be appropriate to disclose where a director then acts as a consultant.

**Payments for loss of office** – the guidance suggests that companies should consider

including a clear explanation of the circumstances surrounding the departure especially where discretion has been applied in favour of the director. Disclosure of the termination arrangements as part of the RIS announcement at the point of leaving is considered best practice although it is accepted that this may not always be practical.

**Statement of directors' shareholdings and share interests** – the guidance provides details of what might be included in the section on shareholdings and this includes the timeframe over which any requirement is expected to be met, whether there is any requirement for shares vesting from plans to be retained until the shareholding is met and the definition of which shares can be included to meet the guidelines. In terms of what details should be disclosed in relation to share interests, on which the regulations are silent, the guidance suggests this could include how many shares/options awarded, when the award will vest, the share price on grant and any exercise price. The guidance also suggests disclosing details of any hedging arrangements in place.

**Relative importance of spend on pay** – the regulations do not specify what categories of expenditure should be included in this section in addition to total employee pay which the guidance stated should be taken from the notes to the accounts relating to employee cost, dividends and share buy backs, which the guidance suggests are shown separately. The guidance provides some examples of what might be included: profits retained, investment for future growth (capital expenditure or R&D costs), debt repayments, tax payments. The guidance suggests that companies should aim to maintain consistency over time in terms of the information provided and the way in which the information is presented, and that companies might consider disclosure over a longer period if this was felt useful.

**Implementation of policy in the next financial year** – the regulations do not include all the details of what should be included in this section but the guidance suggests that companies should consider including changes in salary, any change in maximum bonus or long term awards, changes to share awards compared with awards made in previous period and any other change in the way policy is to be implemented even where this is within the parameters of the approved policy.

**Statement of voting** – the guidance suggest that companies should include the number of votes for and against as well as the percentages. In terms of recognising a low level of support for the report, the guidance suggests that this could be considered to be a combined level of votes against and withheld of 20% or more of the total number of votes submitted but recognises this will depend on company's specific circumstances.

#### **Part 4 – Directors' remuneration policy**

The guidance includes some key principles:

- Companies should embrace the spirit of transparency
- The policy should be broad and flexible enough for companies to respond to changing circumstances for a period of three years without needing to be amended
- It should provide sufficient detail for investors to be able to evaluate the policy and assess

whether payments fall within the policy

The guidance states that investors are generally in favour of the policy taking effect from the AGM, other than for the first year.

### **Policy table**

**Salary** – the factors taken into account when determining salaries and salary increases should be disclosed. Where directors are paid in different currencies any discrepancies caused if converted to a common currency should be explained. The guidance states that current level of salary should be disclosed, as well as a maximum which may be expressed in monetary terms or otherwise (e.g. as a percentage of salary).

**Benefits** – companies may want to consider separating out regular benefits from those that may be paid as a result of specific circumstances such as relocation. The guidance suggests a maximum should be disclosed.

**Pension** – any anticipated changes to the arrangements should be disclosed.

**Annual bonus** – where performance measures are described in broad terms, details should be given in the annual remuneration report.

**Long term plans** – more details on performance measures are expected and if a company wants to significantly change these measures or groups of measures, shareholder approval will need to be sought.

### **Approach to recruitment remuneration**

Companies should disclose the principles and parameters which the remuneration committee will apply in a recruitment situation. The guidance notes that too much detail may raise expectations on the part of a director and may weaken the company's negotiating position. The guidance suggests that companies should disclose the remuneration arrangements agreed as part of the announcement of the appointment. It also suggests that companies may want to disclose the principles on relocation. In relation to sign-on payments the guidance suggests that companies disclose:

- The policy on compensation for forfeited awards and golden hellos.
- The type of awards that could be made, the use of performance measures and holding periods and any application of clawback/malus.
- A commitment to disclose a full explanation of the sign on payment at the time of recruitment and a breakdown of that payment and approach taken to determine a fair level of compensation.

The guidance also notes that in case of internal promotion, making it clear that any commitments made before promotion can continue to be honoured.

### **Statement of consideration of shareholder views**

The guidance notes that this disclosure will vary from company to company but lists some of the disclosures a company may want to consider including the broad topics included in the engagement, an indication of investor reaction and any changes to the remuneration policy made as a result of the engagement.

### **Deloitte view**

Deloitte welcomes the guidance provided by the GC100 Investor working group, particularly where these provide an indication of what investors are expecting from the new disclosures in areas where the regulations are deliberately silent. As we have seen over the decade since the introduction of the current regulations, best practice will start to emerge and guidelines such as these will help and support this process.

The full guidance can be found at:

<http://uk.practicallaw.com/groups/uk-gc100-investor-group>

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