



Remuneration Committee Alert

Highlights from the 2017 Danish Remuneration Reporting Year

The 2017 'season' for shareholder voting on Danish companies' Guidelines for Incentive-Based Compensation saw a number of companies making changes to their remuneration plans. We summarise these changes here, as well as make some observations on future remuneration disclosure requirements under the Shareholder Rights Directive.

We looked at the top 20 listed Danish companies' remuneration proposals (both in relation to Guidelines for Incentive-Based Compensation and Remuneration of Directors resolutions), voting recommendations from ISS and any individual shareholder feedback.

The changes to remuneration practice varied between companies, and included:

- Increases (and decreases) to shareholding requirements;
- Enhancements to share matching plans;
- Changes to performance conditions, including reweighting the TSR component under long-term incentive plans;
- Changes to bonus deferral arrangements, including the level of deferral and removing the compulsory deferral element;
- Introduction of Committee discretion for incentives, including sign-on awards;
- Introduction, or removal, of share option plans;
- Increases to Board fees.

The proxy adviser and shareholder responses to individual company proposals are summarised under three key themes, as shown below.

Key themes from Proxy Advisers and Shareholders

Disclosure of performance targets under incentive schemes	<ul style="list-style-type: none"> • A recurring theme was the absence of robust disclosure of performance targets under bonus and long-term incentive plans. • A call for ex ante disclosure of the detailed performance measures and targets was a consistent theme. • Companies with ex ante disclosure of long-term incentive targets were more likely to receive positive support when increasing the incentive opportunity under these plans.
Disclosure of individual management remuneration	<ul style="list-style-type: none"> • A wide range of practice was noted, ranging from full tabular disclosure of remuneration to the minimum requirement under the Danish Financial Statements Act. • Companies continue to review their disclosure practices, with a view to requirements under the Shareholder Rights Directive.
Discretion	<ul style="list-style-type: none"> • Any proposals to allow for discretion in determining incentive award levels was met with strong pushback. • This was not the case, however, where proposals were supported by detailed disclosure of performance targets or the circumstances in which discretion may be applied.

Looking ahead

There is currently a wide range of executive remuneration approaches in Denmark. This is evident in the variety of different incentive vehicles in use (performance shares, options/warrants, restricted shares and share matching plans). Performance measures are also similarly varied, reflecting the strategy and requirements of individual companies.

This company by company approach is underpinned by the best practice recommendations of the Committee on Corporate Governance, which are principle-based and mostly non-prescriptive. The Danish model therefore contrasts to other countries where governance codes are more prescriptive and a conformity in incentive plan design prevails.

In terms of remuneration-related disclosure, however, there are large gaps between current Danish practice and the requirements of the European Shareholders Rights Directive. We have outlined the provisions of the Directive in prior publications. In brief, the European Commission proposed amendments to the Shareholder Rights Directive in April 2014. The Directive has been agreed by the Parliament, Council and Commission negotiators in December 2016 and was adopted in May 2017. Member States have until June 2019 to implement the Directive.

A key focus of the Directive is the separation of a Remuneration Policy and an Annual Remuneration Report. The former is subject to a binding vote at least every four years, while the latter is subject to an annual advisory vote. However, member States will determine how this will apply and whether either or both are subject to a binding or advisory vote. The key intention of the Directive is that the Policy effectively provides a 'licence' to pay management and the Board, while the Remuneration Report provides shareholders with guidance on how the Policy was applied in the last financial year. Again, how this will apply against the current requirements, i.e. Guidelines for the Remuneration Policy for Executive Management and the Board and, the Guidelines for Incentive-based Compensation for Executive Management and the Board, remains to be determined.

Despite these pending details, the direction of travel in terms of future Danish company disclosure is reasonably clear based on the overall substance of the Directive. We also note that the November 2017 changes to the Danish Recommendations on Corporate Governance published in November 2017, reflect for the first time, a best practice principle of including an annual remuneration report. We summarise below the differences in typical Danish remuneration disclosures versus the Directive.

	Typical Danish Practice 	Gaps to Comply with the Directive 
Remuneration Guidelines	<ul style="list-style-type: none"> • Relatively high level narrative • Description of only main elements of pay • Bonus and long-term incentives limits but measures, targets and vesting schedules not always disclosed • Basic pension and benefits summary • Severance limits are typically disclosed • Withholding provisions not always clear • Limited disclosure on conditions allowing for deviation from Guidelines 	<ul style="list-style-type: none"> • Process taken in determining Policy • Link to strategy • Relative proportions of each element of pay • Performance metrics rationale (short and long-term) • Rationale for (lack of) deferral/holding periods • Broader employee pay commentary • Explanation around potential to deviate from the Policy
Annual Report	<ul style="list-style-type: none"> • Bonus metrics/weightings not always disclosed • Incentive payouts are disclosed but often no detail on targets and vesting schedule is included • Tabular disclosure (CEO, management and/or aggregate senior management) fixed salary, variable pay, benefits, total remuneration, varies considerably • Inconsistent disclosure of equity awards 	<ul style="list-style-type: none"> • More detail on performance measures and achievement against incentive metrics • Clear disclosure of proportion of fixed and variable remuneration • Annual change in remuneration vs employee and company performance • Individual tabular disclosure • More details on payments to former directors

There is clearly a large gap between typical Danish practice and the requirements of the Directive. We advise companies to get ahead of the game, and start to evolve remuneration disclosures on a progressive model rather than wait until the Directive takes effect.

European disclosure trends

It is helpful to look at the emerging picture of Danish remuneration disclosure against broader European developments in shareholder and proxy adviser reactions to executive remuneration proposals.

Taking the Eurostoxx 100 companies as a reference point, 30% of the 72 Eurostoxx 100 companies for which ISS has published voting recommendation so far received a vote against recommendation.

The key reasons for vote against recommendations are:

- Increase in fixed pay or in long-term incentives
- One off awards
- Award of shares without performance conditions
- Lack of disclosure on treatment of long-term incentives on termination
- Poor pay for performance alignment
- Change of targets for outstanding awards or use of positive discretion
- Lack of disclosure of targets

	Quantum increase – generally met with suspicion
	Pay for performance: discretion to ensure that incentives reflect the performance of the business and align with shareholders
	Termination: Concern around lack of pro-rating of awards for outgoing executives
	Bonus target disclosure: At least retrospective disclosure expected
	Balance of financial and non-financial metrics on variable incentives

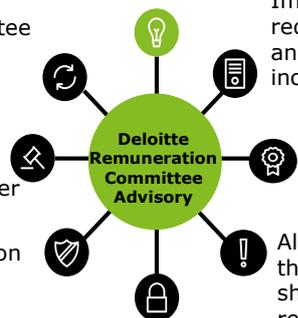
These findings are similar to those outlined above for Denmark. However, with increased disclosure soon applying in Denmark under the Shareholders Rights Directive, companies will be subject to more detailed shareholder and proxy adviser scrutiny. It is therefore important to ensure that current executive remuneration policies and practices are examined to identify any aspects that may need review ahead of this enhanced disclosure regime.

Deloitte Remuneration Committee Advisory

Discussions of how the Remuneration Committee creates value and operates effectively

An annual documented remuneration report taking into account legislation, regulatory requirements, market practice, and shareholder perspectives

A formal process to determine the remuneration structure and pay levels for the most senior executives and for the entire organisation



Implementation of new hard and soft law requirements into charter with a clear link to annual work plan, including qualifications, including the need for training

A strong alignment between levels of pay and business, personal responsibility and performance

Alignment of incentive structures, especially for the most senior individuals, with the interests of shareholders, strategy and business requirements

A documented remuneration policy taking into account legislation, regulatory requirements, market practice, and shareholder perspectives

Establishment

- ✓ Development and drafting of charter and annual work plan
- ✓ Development and drafting of process for how to work in the Remuneration Committee
- ✓ Development of process for the Remuneration Committee's oversight of the remuneration and performance management processes
- ✓ Drafting of remuneration policies
- ✓ Drafting of annual remuneration reports

Evaluations & Assessments

- ✓ Facilitate and discuss needs for achievement and improvements
- ✓ Participate in meetings to discuss evaluation, priorities, expectations and action plan
- ✓ Perform assessments of "Remuneration Committee Effectiveness", and report the results

Compliance

- ✓ Update of charter and annual work plan, both to ensure compliance and effective processes
- ✓ Updating the process for the Remuneration Committee's oversight of the remuneration and performance management processes, and ensuring compliance with it
- ✓ Ensure independence between Remuneration Committee and Management, including consideration of the recommendation not to use of the same external advisors
- ✓ Ensure transparent reporting under EU Shareholders' Rights Directive and in the annual reports
- ✓ Ensure appropriate consideration of sector benchmarking, tax and valuations as well as clear communication

Training & Labs

- ✓ Training on various topics like remuneration and human capital strategies, EU Shareholders' Rights Directive, accounting, valuation, tax and benchmarking – generally and/or in detail
- ✓ "Remuneration Committee Lab"



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