Financial Reporting Council

Directors' Remuneration consultation document

NAPF response

Introduction

The National Association of Pension Funds (NAPF) is the UK's leading voice for workplace pensions. Our members have combined assets of around £900 billion, and operate some 1,300 pension schemes. NAPF membership also includes over 400 providers of essential advice and services to the pensions sector; these include accounting firms, solicitors, fund managers, consultants and actuaries.

We welcome the opportunity to respond to the FRC's consultation document on potential changes to the UK Corporate Governance Code (the "Code") in relation to Directors' Remuneration.

The consultation document rightly recognises that there have been very significant regulatory changes in the area of executive remuneration in recent months and a fair amount of related guidance has been issued by various organisations. In this context we do not consider that there is merit in making any significant or prescriptive changes to the Code at this stage. Instead the new regulations should be allowed to bed in allowing companies and investors to adapt and good practice to evolve. We have commented upon the three mooted areas for revision below and have suggested some areas where minor revisions would prove helpful.

Extended clawback provisions

We believe that it is right that companies should ensure their executive remuneration policies include provisions that allow the company, in specified circumstances, to adjust or recover awards.

The "Code" currently states that *"consideration should be given to the use of provisions that permit the company to reclaim variable components [of remuneration] in exceptional circumstances of misstatement or misconduct".*

The terminology used in the Code at present relates largely to clawback provisions which are in practice difficult to utilise and would likely only be used in very narrow circumstances. In general, performance adjustment (malus) will apply to a broader range of circumstances than for clawback and we would welcome the Code reflecting this in its wording.

Additionally, the Code at present simply encourages "consideration" of the use of such provisions. It is now standard practice for companies to have at least limited clawback and/or malus provisions within the executive remuneration policies; as such we would welcome revised wording which moved this towards a "comply of explain" presumption that such measures are in place.

Finally, we wish to see remuneration committees taking greater ownership of, and being accountable for, both the remuneration policy and its outcomes. As such we would like to see companies looking at broadening out the circumstances where they are willing to use malus beyond circumstances of material misstatement. However, we do not consider it appropriate for the Code to go so far as to specify the circumstances under

which payments could be recovered and/or withheld. Instead we believe that this should be a matter for the remuneration committee to consider and disclose to their shareholders.

Remuneration Committee membership

We do not believe that there are any significant issues of concern with regards to the presence of current executive directors sitting on remuneration committees of other large companies.

Shareholders look to the Remuneration Committee to protect and promote their interests in setting executive remuneration. As per the current Code wording, the Committee should be constituted of independent directors and executive directors of other companies would currently be classified as independent unless other links hinder this.

We note and acknowledge the analysis presented in the consultation paper which suggests that there is no significant difference between the levels of shareholder dissent expressed against a remuneration report emanating from a committee with an Executive Non-Executive Director (ENED) as compared to one without an ENED. We are not aware of any evidence that a serving executive director is any more generous in his or her view of remuneration awards than other directors. Indeed, anecdotal evidence is often suggestive of the reverse.

We believe that it should remain the responsibility of the shareholders to judge the deliberations and judgements of the remuneration committee. If they have concerns with these deliberations, including any concerns that an executive director or any other director, is unsuitable to their committee position then they should raise this with the Chairman or SID. Furthermore they have the ultimate power, through the annual re-election of directors, to express their dissatisfaction publicly. Therefore we believe it would be unnecessary to introduce any new requirement in this area.

Votes against remuneration resolutions

The NAPF considers it essential that there is effective dialogue between companies and their shareholders; this requires both on-going and responsive dialogue.

We welcomed the inclusion in the new Regulations that companies must include in their annual remuneration report details of the vote on any remuneration resolutions at the previous meeting and, where there was a significant percentage of votes against, give a summary of the reasons for those votes and any actions taken in response.

The GC100 Investor and Investor Working Group's guidance suggested that "votes against in excess of 20% as being significant, although there may be reasons why, for some companies, a higher or lower level might be more appropriate." It also suggests that "where the board considered the outcome to be a 'significant' vote against, or otherwise showing a significant lack of support for the resolution that they plan to address, the company may also wish to consider including a statement to that effect in the RIS announcement relating to the results of the AGM."

We would concur with the recommendations in this guidance. Furthermore we would emphasise that while 20% may be a marker in the sand, a level significantly lower (or indeed higher) may be more reflective of 'significant dissent' for some companies' dependent upon the nature of their share register. We would

encourage companies to consider what they deem is a significant level of dissent for them and tailor their response accordingly.

We would welcome encouragement within the Code for companies to consider the voting results of each resolution at their AGM – not just those relating to remuneration - and to communicate to shareholders those, if any, they deem received a 'significant' level of dissent. This should be sufficient to initiate a dialogue between the company and its shareholders about the issue at hand and will enable the company to then report in its subsequent annual report how it responded.

We would caution against including within the Code any specific figure or a criterion for determining what constitutes a 'significant' percentage of dissent. Instead this should be for each company to consider for themselves giving thought to the makeup of their share register and the particular resolution in question. The percentage of dissent deemed 'significant' in relation to a remuneration related resolution may well differ to that for a resolution for the re-election of a director.

In the spirit of fostering a more positive and engaged dialogue we would like to see this left as open and flexible as possible. It is important that voting results should not be interpreted against the Code as being "significant" or "insignificant" but instead left to the judgement of the board and the company's shareholders.

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To discuss further please contact:

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