FRC Consultation on Directors' Remuneration
dated October 2013

Response from the Share Plan Lawyers Group

This response is sent on behalf of the Share Plan Lawyers group ("**SPL**"). SPL was originally formed approximately 25 years ago by lawyers in law firms in London whose main practice is employee share arrangements. It has nearly 300 members representing more than 60 law firms and a number of specialist practitioners. Those members include senior lawyers from all the major London law firms and most major regional firms in the UK.

The main purpose of SPL is to meet, consult with and make representations to the Government and other institutions involved in taxation, corporate and other regulatory issues in relation to employee share plans. Members of the SPL advise on the drafting and operation of all types of employee share plans, including those operated by a large proportion of UK listed companies.

Taking the questions in the Consultation Paper in turn:

Extended Clawback Provisions

1. Is the current Code requirement sufficient, or should the Code include a "comply or explain" presumption that companies have provisions to recover and/or withhold variable pay?

In our experience remuneration committees of listed companies which do not already have provisions to recover/withhold pay are now almost invariably considering, when remuneration structures are discussed, whether to adopt malus and/or clawback provisions, to apply at the least in exceptional circumstances of mis-statement or misconduct (i.e. complying with the current Code requirement). Often the provisions that are adopted are expressed more widely. It seems to us that the current requirement is therefore sufficient. Introduction of a "comply or explain" provision would push companies, who may have considered the introduction of clawback but who have, after proper consideration, decided that, in their particular circumstances, it was not appropriate, to provide for clawback purely to avoid having to "explain". In our view it would be better to leave the issue one for remuneration committees to decide.

2. Should the Code adopt the terminology used in the Regulations and refer to "recovery of sums paid" and "withholding of sums to be paid"?

We agree that it may be preferable for a change in the wording to differentiate between withholding of sums to be paid (often called "malus" provisions, but also often just an incident of appropriate performance conditions) and recovery (usually called clawback). We accept that "clawback" is often loosely used for both and "malus" is not always understood.

3. Should the Code specify the circumstances under which payments could be recovered and/or withheld? If so, what should these be?

We do not think that the Code should specify the circumstances under which payments could be recovered and/or withheld. The current wording in the Code referring to "exceptional circumstances of mis-statement or misconduct" is it seems to us sufficiently broad. In practice companies have used many different formulations and what is appropriate for one company in one sector may be less appropriate for a company than another. We think therefore the companies should be free to design their own circumstances.

4. Are there practical and/or legal considerations that would restrict the ability of companies to apply clawback arrangements in some circumstances.

There are a number of legal arguments (untested in the courts) which have been suggested could be used to try to resist application of clawback (i.e. recovery of amounts paid). These include that:

(a) provisions under which benefits already provided can be required to be returned in the event of breach of contract by the individual amount to an unenforceable penalty, if the amounts that may be clawed back are excessive by reference to the nature of the breach;

(b) in exercising its discretion to apply clawback the relevant committee has acted improperly in not taking account of all relevant issues;

(c) where the clawback may be triggered by breach of post-termination restrictive covenants, that may be an unlawful restraint of trade; and

(d) potentially, there is a breach of individual's human rights if benefits already paid can be clawed back.

From a practical point of view a company may well decide that it is likely to be impossible or very difficult to recover amounts from an employee. The employee may, once the misconduct is discovered, have become a former employee and, even if he has not, there may well not be any future bonuses from which to recover payments. Where an individual has become a former employee the monies received may have been spent or passed on to spouse or other family members. The former employee may have moved abroad or become bankrupt. In those circumstances the company may well determine that the cost of seeking to recover is greater than the value that will be obtained.

Companies will also appreciate that recovery of monies paid may involve a public legal process which may reveal information about the company which is sensitive or at the very least embarrassing.

Remuneration Committee Membership

5. Are changes to the Code required to deter the appointment of executive directors to the remuneration committees of other listed companies?

We do not think the changes in the Code are necessary to deter the appointment of executive directors to the remuneration committees of other listed companies. We think that the most that should be suggested is that companies should be required to consider, in determining the make-up of the remuneration committee, whether somebody who is an executive director of another listed company should be a member of that committee. Smaller listed companies may only have a limited number of non-executive directors and it may therefore be difficult for them to assemble a remuneration committee without using individuals who also have an executive role.

Votes against the Remuneration Resolutions

6. Is an explicit requirement in the Code to report to the market in circumstances where a company fails to obtain at least a substantial majority in support of a resolution on remuneration needed in addition to what is already set out in the Regulations, the guidance and the Code?

We do not believe that an additional requirement over and above what is contained in the Regulations, the guidance and the Code is necessary.

7. If yes, should the Code:

- **set criteria for determining what constitutes a "significant percentage";**
- **specify a time period within which companies should report on discussions with shareholders; and/or**
- **specify the means by which companies should report to the market and, if so, by what method?**

It follows that we have no comment on this question.

8. Are there any practical difficulties for companies in identifying and/or engaging with shareholders that voted against the remuneration resolution/s?

We are not best placed to consider the practical difficulties of identifying shareholders who voted against remuneration resolutions. There are, however, clear practical difficulties, once a company knows which shareholders voted against a resolution for a company to determine from those shareholders why they did so. A company may realistically be able to devote time to discussing reasons for a vote against with a small number of large shareholders but not with potentially a very large number of other institutions.

Other Possible Changes

9. Is the Code compatible with the Regulations? Are there any overlapping provisions in the Code that are now redundant and could be removed?

We certainly believe that any provisions that overlap with the Code should be eliminated. However it should be noted that more companies are subject to the Code than are subject to the Regulations. The Regulations only apply to companies incorporated in the UK whereas the Code applies to all companies with a premium listing, wherever incorporated. On that basis strictly no provisions in the Code are entirely redundant.

10. Should the Code continue to address these three broad areas? If so, do any of them need to be revised in the light of developments in market practice?

We believe that the broad areas set by the Code remain appropriate. We do not believe that any changes are needed as a result of developments in market practice.

If you have any queries on the responses above please contact Jonathan Fenn at Slaughter and May (jonathan.fenn@slaughterandmay.com).

3 December 2013