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Dear Catherine

GC100 response to FRC's consultation on directors' remuneration

I am writing on behalf of the GC100 in response to the above consultation paper. As you will be aware, the GC100 is the association for the general counsel and company secretaries of companies in the FTSE 100. There are currently 128 members of the group, representing more than 82 companies. Please note, as a matter of formality, that the views expressed in this response do not necessarily reflect those of all individual members or their employing companies.

Set out below is our response to the questions raised in your consultation paper.

1. Extended clawback provisions

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?

Under the new remuneration regulations[1], companies are required to disclose what, if any, provisions exist in the company's incentive plan rules in relation to recovering and/or withholding variable pay, and whether those provisions were used during the year.

These are new disclosure requirements. While we believe the new requirements, complemented by the recent GC100 and Investor Group guidance[2] on their implementation, are appropriate, we also believe they are, at this stage, sufficient. Their application by companies should be monitored over several reporting periods before developing any proposals about whether there is a case for requiring companies to report on a comply or explain presumption. It is premature at this stage to introduce a presumption into the UK Corporate Governance Code (Code).

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 support the alignment of the Code's terminology with that used in the new regulations. The Code should therefore state (in Schedule A) that "consideration should be given to the use of provisions that permit the company to recover sums paid and/or withhold the payment of any sum". It is important that the Code continues to make it clear that this relates to variable pay.

[1] Schedule 8 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended).
[2] GC100 and Investor Group's Directors' remuneration reporting guidance published on 12 September 2013.

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

We do not believe it would be helpful for the Code to do this. There will be a wide range of different circumstances in which particular companies might wish to consider withholding and/or recovering variable pay, some of which may be industry or sector specific. It is not possible to foresee all these circumstances. Some companies may wish to disclose examples of the circumstances which they might wish to consider, although even here there is a danger that this could be misinterpreted as a definitive list. Further, companies may apply the recovery or withholding differently to the executive directors depending on their level of culpability. Specifying the circumstances may therefore prove unhelpful or even risk the company breaching employment law.

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

It is almost certainly the case that practical and legal considerations would restrict the ability of companies to apply clawback arrangements in some circumstances. One example is the treatment of tax that has been withheld at the date of vesting. Looked at from a "cost to the company" perspective the total number of shares awarded might be seen as the appropriate recoverable amount, but from an "actual remuneration received" perspective the number of shares awarded net of those sold to cover tax could be seen as the appropriate amount to pursue. Whilst it should be possible for companies to articulate in a form consistent with the regulations the provisions that a remuneration committee would seek to apply in particular circumstances, this should be in the form of an overarching framework, in other words, giving sufficient flexibility for companies to look at individual circumstances.

2. Remuneration committee membership

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

There are a number of reasons why the GC100 does not believe that there should be any deterrent to the appointment of executive directors to the remuneration committee of other listed companies and, to the contrary, it believes that such appointments are beneficial.

A director has a duty to act in the best interests of the company at all times. This duty applies whether as an executive or non-executive director. To suggest that a serving executive director could not fulfil that duty in relation to a role on another company's remuneration committee would be a damaging distinction to draw and would set an unfortunate precedent. It would certainly be a fundamental change for the worse in the role of trust that is placed on those appointed to the board of a company. If the logic were followed then there may equally be times that a serving director should not be on an audit or a risk committee.

The Code already clarifies the proper constitution of a remuneration committee being "at least three....independent non-executive directors". There already exists a clear definition of independence in the Code along with the requirement that the board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect or could appear to affect the director's judgement. These provisions along with a director's fiduciary and statutory responsibilities provide a perfectly adequate framework to determine who is suitable to be on a remuneration committee and how its members should act.

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This form of governance has worked well for the vast majority of companies as is evidenced by the re-election of directors to boards and the approval by advisory vote of remuneration reports. Of the 282 FTSE 350 premium equity commercial companies that published their 2013 AGM results by 8 November 2013, 80% (226 companies) received 90% or more of the votes cast in favour of their directors' remuneration report[3]. Shareholders as the owners of the company have more than adequate means to express their views on the activities of the board and the remuneration committee through contact with the chairman, the senior independent director and the chairman of the remuneration committee. If this should fail, views can also be expressed through shareholder bodies or ultimately through a proper exercise of votes at a general meeting.

We do not believe that there is any evidence that the presence of a serving executive has had an adverse effect on the executive remuneration policies reviewed and adopted by remuneration committees or has contributed to excessive remuneration or reward for failure. In fact, this pool of serving executive directors is already relatively small due to the time commitment involved, but, equally, is viewed as being of particular value and relevance to committee considerations. The experience of our members is that they do not see these individuals exercising an undue and adverse influence within the remuneration committee on remuneration policy for UK PLC as a whole. Indeed, in our members' experience, serving executives are often better able to test and challenge remuneration principles with first hand and current knowledge, and make a key contribution to the debate whilst taking into account shareholders' interests. In that way, the additional perspective they bring improves the quality of the committee's decision-making. This is particularly the case in being able to apply the experience of weighing up and challenging the evidence and benchmarks prepared by remuneration consultants, and in testing proposals put forward by management.

It is hard to see where the perceived conflict arises when a director accepts such an onerous role with the responsibility to act in the best interests of the company. The opposite is therefore more likely to be true.

If companies are unable to have serving executives on their remuneration committees the likely consequences are; an increase in the size of boards and the consequent non-executive fees in order to ensure there are enough suitable directors to be members of committees; it will be harder to attract individuals with recent and relevant experience as they cannot play a full part in the board committees; and it will be harder for boards to continue progress on diversification.

This last point is of particular significance given the encouragement in the Davies Report for companies to increase the number of women in non-executive positions. If women who are executives in other companies are going to be disbarred from serving on the remuneration committee of a company which is considering appointing them as a non-executive, they will be perceived as being less "valuable" as an independent non-executive director, given that they will not be eligible to serve on an important board committee. We believe that this proposal will have the unintended consequence of making it more difficult for women executives to secure non-executive positions in other FTSE 350 companies.

An important additional protection is being given to shareholders this year through the remuneration regulations, when the shareholders can clearly express their views on policy and implementation of the work carried out at the remuneration committee through a binding vote and an advisory vote. Details are required on the other roles carried out by the remuneration committee members which will confirm the board's view on an individual's independence. Each

[3] This information has been taken from Practical Law's What's Market Annual reporting and AGMs 2013 report.

GC100 Group
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director is individually proposed for re-election including the chairman of the committee, so once more there is an adequate opportunity for the owners of the company rather than distant observers to make any changes they feel are necessary.

In conclusion, we would strongly advise against encouraging such discrimination in the memberships of remuneration committees.

3. Votes against the remuneration resolutions

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?

As already set out in the GC100 and Investor Group's guidance, we fully support the need for continuing engagement between companies and their investors and recognise that acknowledging when things have gone wrong is one of the first steps a company might take in rebuilding the trust of its shareholders when there has been a significant vote against the remuneration resolution. We also recognise that although a resolution may have been passed legally, there are cases when a high number of votes either cast against or withheld indicate a level of dissatisfaction with the company's proposals. We would agree that in such cases, it is often in the company's best interests to acknowledge that there is an issue and to begin to take steps to understand the cause of shareholder concerns and either alter its practices or explain them more effectively to their shareholders. If a company ignores shareholder dissatisfaction expressed as a high level of votes withheld or a substantial majority of votes cast against, then there is a real danger that levels of dissatisfaction will increase and lead to a negative vote in future years.

However, we believe that the circumstances of each company are very different and we would not support the introduction of a Code provision specifying what constitutes a "significant percentage", a time period in which to report on discussions with shareholders, or the means by which a company should report to the market. Examples where over-prescription in this area would not be appropriate include:

- A single large shareholder could well distort voting numbers, meaning that a percentage higher or lower than 20% might be more appropriate for the company concerned.

- At the time of the AGM voting announcement, a company will often not know exactly which investors have voted against a particular resolution or their reasons why. Whilst enlightened investors engage with companies ahead of the AGM and explain their reasons for voting against or withholding, this is not always the case. It is particularly difficult to ascertain how underlying shareholders within an omnibus account have voted if the total shares may have been voted in different ways. If companies do not know which investors have opposed, they will not know the reasons for the opposition. Companies will therefore need time to interrogate the voting registers and follow up with individual shareholders where necessary before making any announcement, and setting a "one size fits all" deadline would not be appropriate.

- It is rarely a single issue that leads to shareholder opposition. If there are a number of different issues influencing a significant percentage against or withheld, or if the issues

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concerned are in fact mutually exclusive, companies will need to spend time understanding and reconciling these issues before publicly committing to a given course of action.

The GC100 and Investor Group's guidance is specifically "guidance" or helpful advice for companies and investors. It is not law or regulation, as it recognizes that all companies are different. The guidance makes a clear distinction between disclosures which are mandatory and disclosures that "companies may like to consider". The suggestions that 20% could be considered as a significant percentage and that a statement be included in the RIS announcing the AGM results were not intended to be construed that in all cases this would be the correct approach, and we do not believe that these suggestions should be carried over into the Code. We support effective engagement between companies and their investors, but this can take many different forms and over prescription is more likely to hinder than advance an effective engagement process.

If you would like to discuss any of these points further, we would be happy to do so.

Yours sincerely

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