



# Director Remuneration Policy/Report Workshop – Learning from last year

Hosted by Baker & McKenzie LLP  
and MM&K

Tuesday 28th October 2014

# Director Remuneration Report/Policy Workshop

## Agenda

- Part 1: The Annual Statement and the Annual Report on Remuneration – Cliff Weight, MM&K
- Part 2: The Remuneration Policy – Jeremy Edwards & Kathy Hood, Baker & McKenzie



## **Remuneration Report**

# **Annual Statement and Annual Report on Remuneration**

**Cliff Weight  
Remuneration Consultant and Director, MM&K**

## About MM&K

- MM&K is a leading independent executive remuneration consultancy:
  - based in the City
  - owned by directors, employees and EBT
- Established 1973
- Six Principals, each with over 25 years experience in the field
- Remuneration Committee adviser in over 50 companies over last three years, including FTSE 350, Small Cap, AIM and private companies
- Strong focus on alternative investment firms, particularly Private Equity Fund Managers and Hedge Fund Managers
- Member of the Remuneration Consultants Group and committed to its code of practice.

## We will cover

- Key issues
- 2014 voting results
  - FTSE 350 voting patterns
  - Companies with high protest votes and reasons
- Examples of good practice
- A shareholder's viewpoint (recap)
- Questions for discussion

# Contents of Annual Report on Remuneration (implementation report)

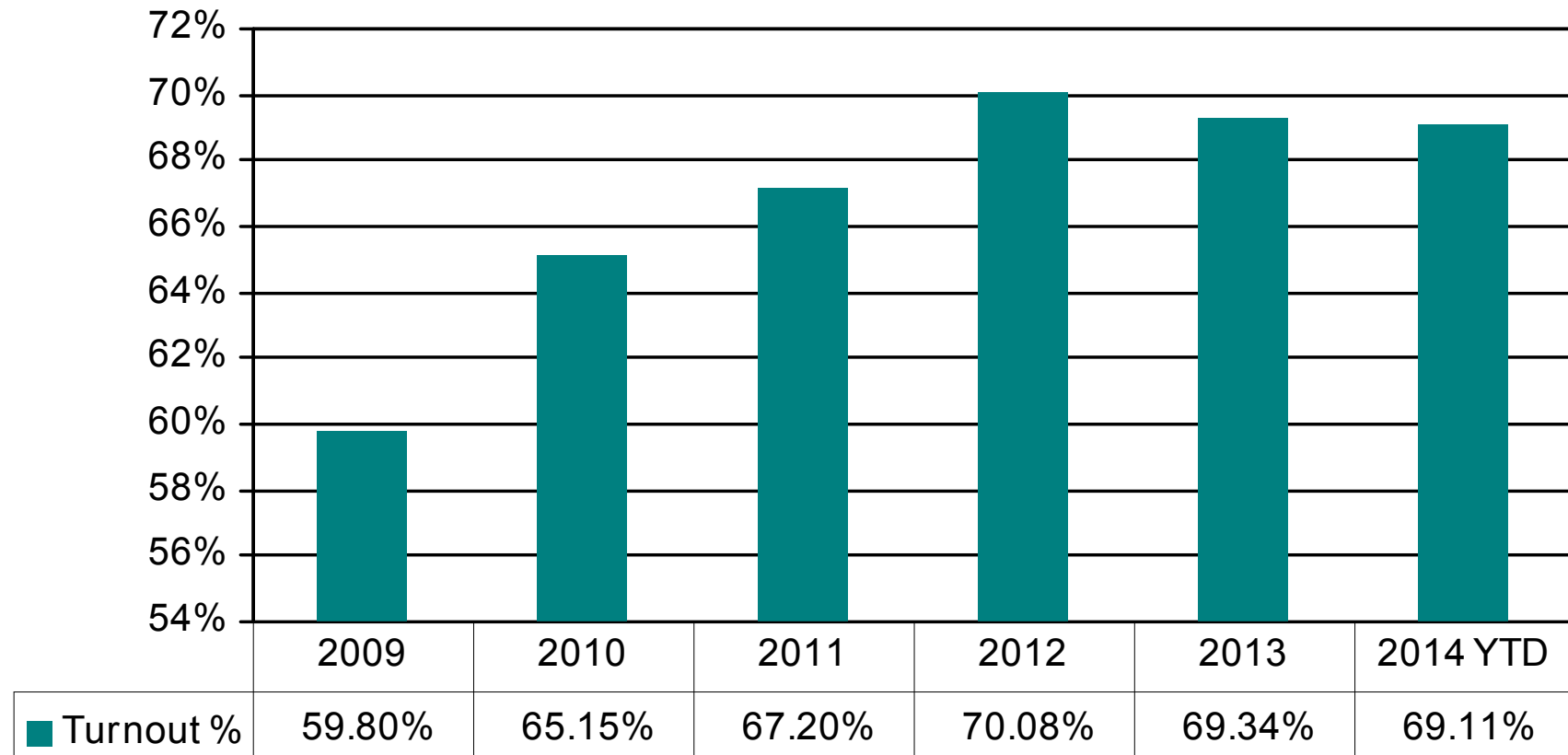
- Single total figure table
- Additional requirements in respect of the single figure table
- Total pension entitlements
- Scheme interests awarded in the year
- Payments to past directors
- Compensation for loss of office
- Directors' shareholdings
- Line graph comparison of TSR performance and Index over 5 years ( 6 years from 1 October rising to 10 years)
- 6 year (rising to 10 year) record of CEO Single Figure of Total Remuneration and Bonus as % maximum and LTIP vested %
- Percentage change in remuneration of director undertaking the role of CEO
- Relative importance of spend on pay
- Statement of implementation of remuneration policy in the following financial year
- Consideration by the directors of matters relating to directors' remuneration, including remuneration committee advisers and their fees
- Shareholder voting

# UK Voting Trends 2014

# AGM Turnout - Top 350

## % of shareholders who registered a vote or abstention is reducing

Top 350 UK Listed Companies- AGM Turnout

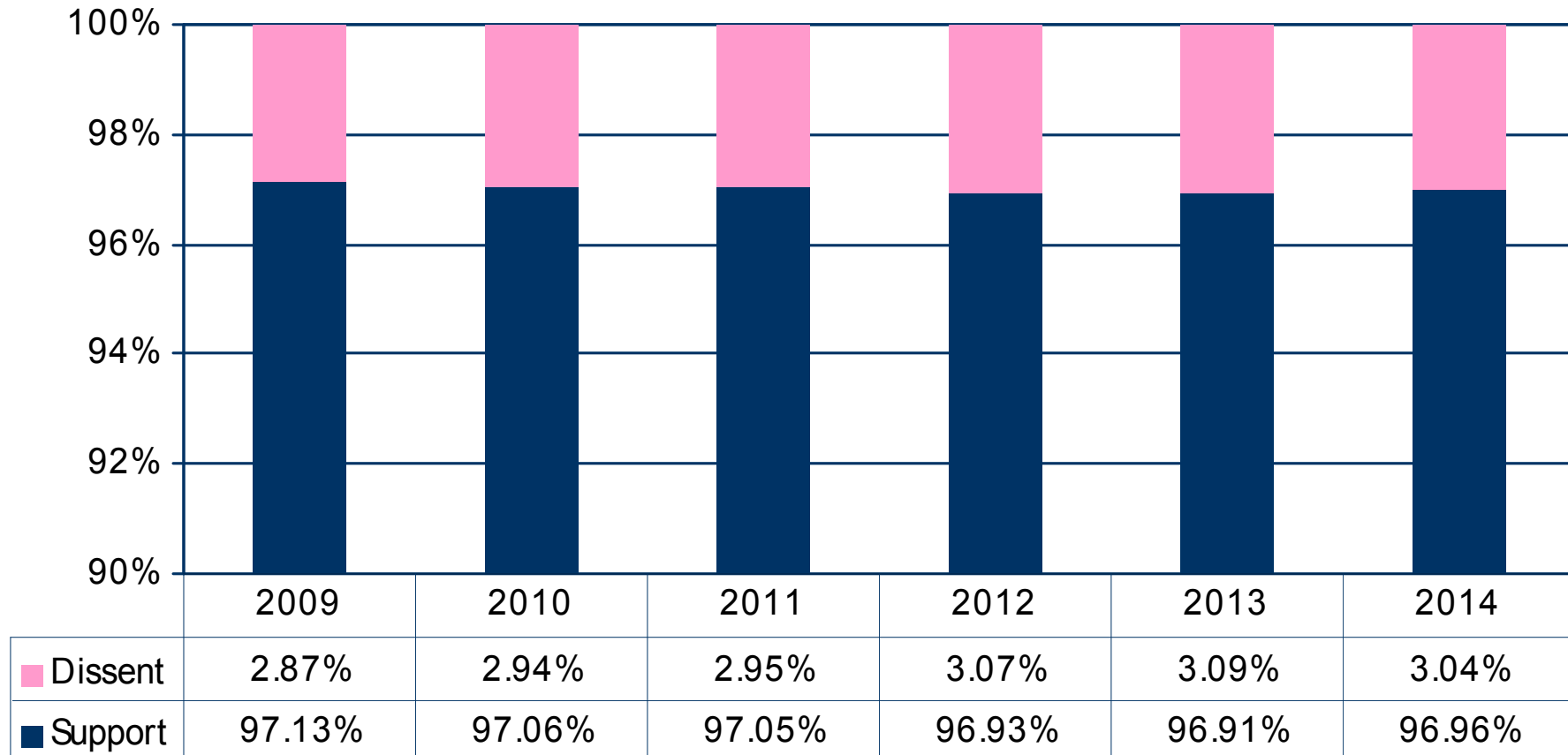


Source of data: Manifest, The Proxy Voting Agency



# Voting against has not got worse

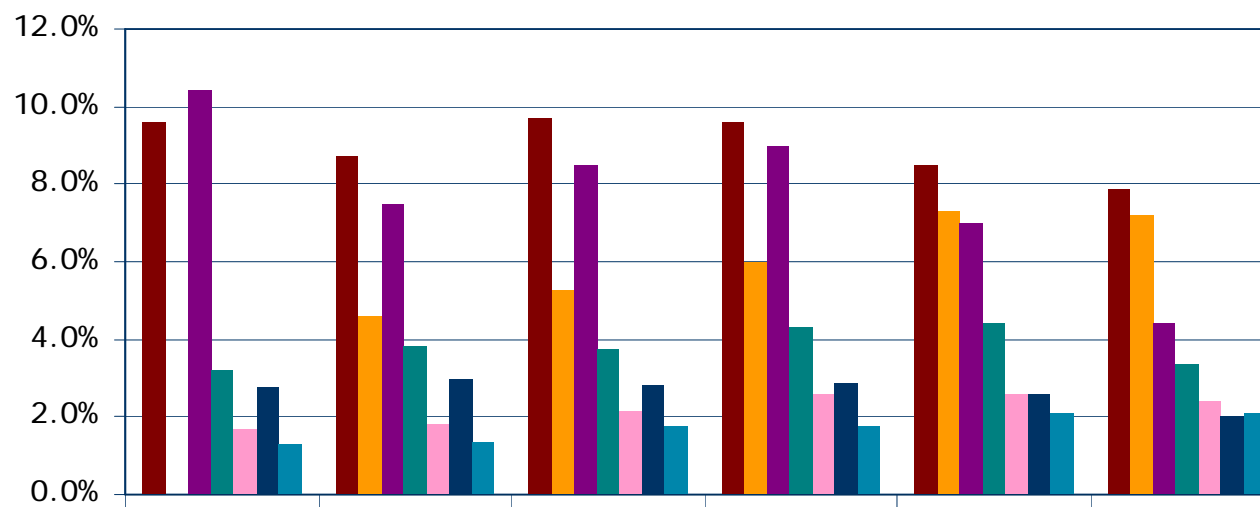
## Top 350 Shareholder Support (Avg)



Source of data: Manifest, The Proxy Voting Agency

# Remuneration is the main source of shareholder dissent

## Dissent by Resolution Sub-Categories



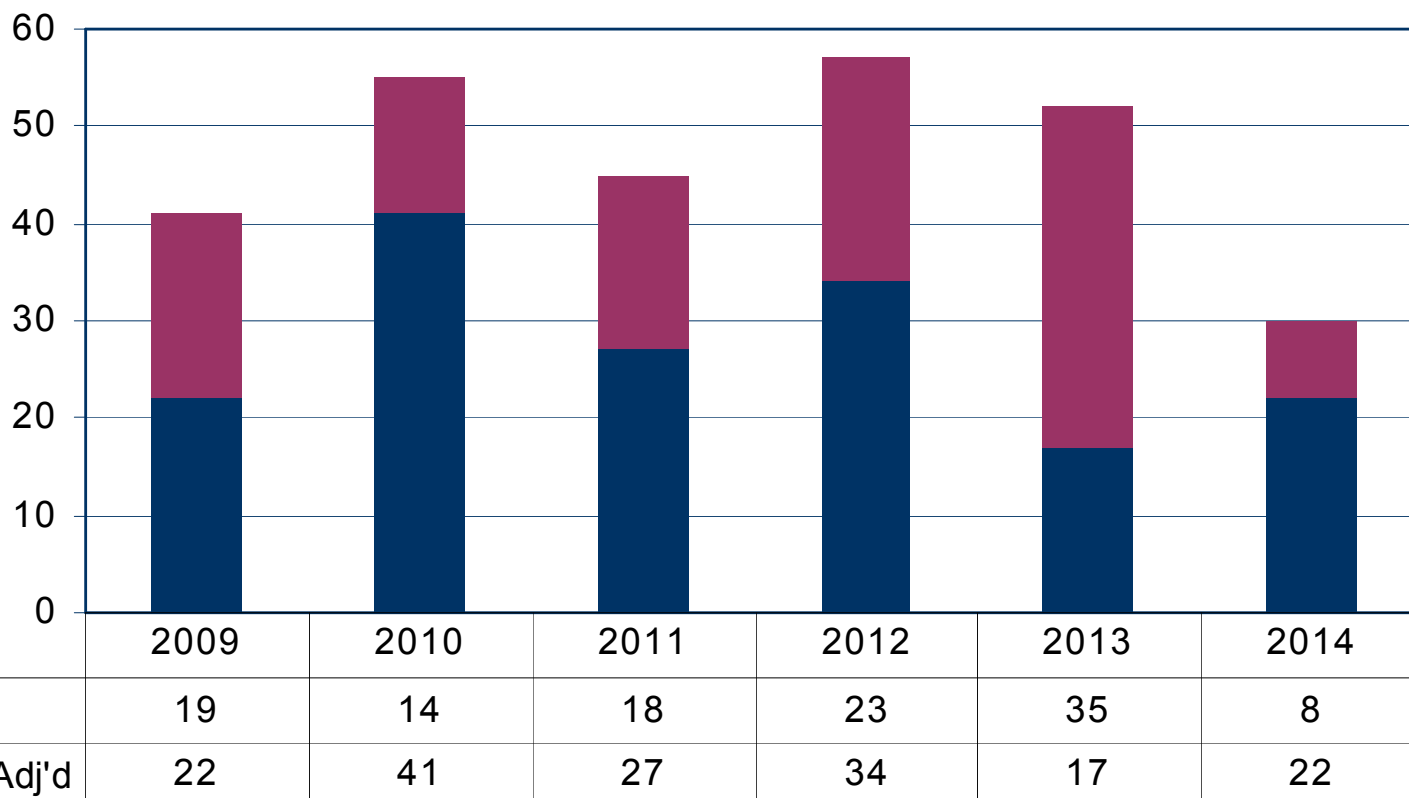
	2009	2010	2011	2012	2013	2014
■ Remuneration Report	9.6%	8.7%	9.7%	9.6%	8.5%	7.9%
■ EGM Notice Periods	0.0%	4.6%	5.3%	6.0%	7.3%	7.2%
■ Incentives - Long Term	10.4%	7.5%	8.5%	9.0%	7.0%	4.4%
■ Issue of Shares & Pre-emption Rights	3.2%	3.9%	3.8%	4.3%	4.4%	3.4%
■ Auditor - Election	1.7%	1.8%	2.1%	2.6%	2.6%	2.4%
■ Directors - Elect	2.8%	3.0%	2.8%	2.9%	2.6%	2.0%
■ Auditor - Remuneration	1.3%	1.4%	1.8%	1.8%	2.1%	2.1%

Source of data: Manifest, The Proxy Voting Agency



# Reduction in defeated resolutions

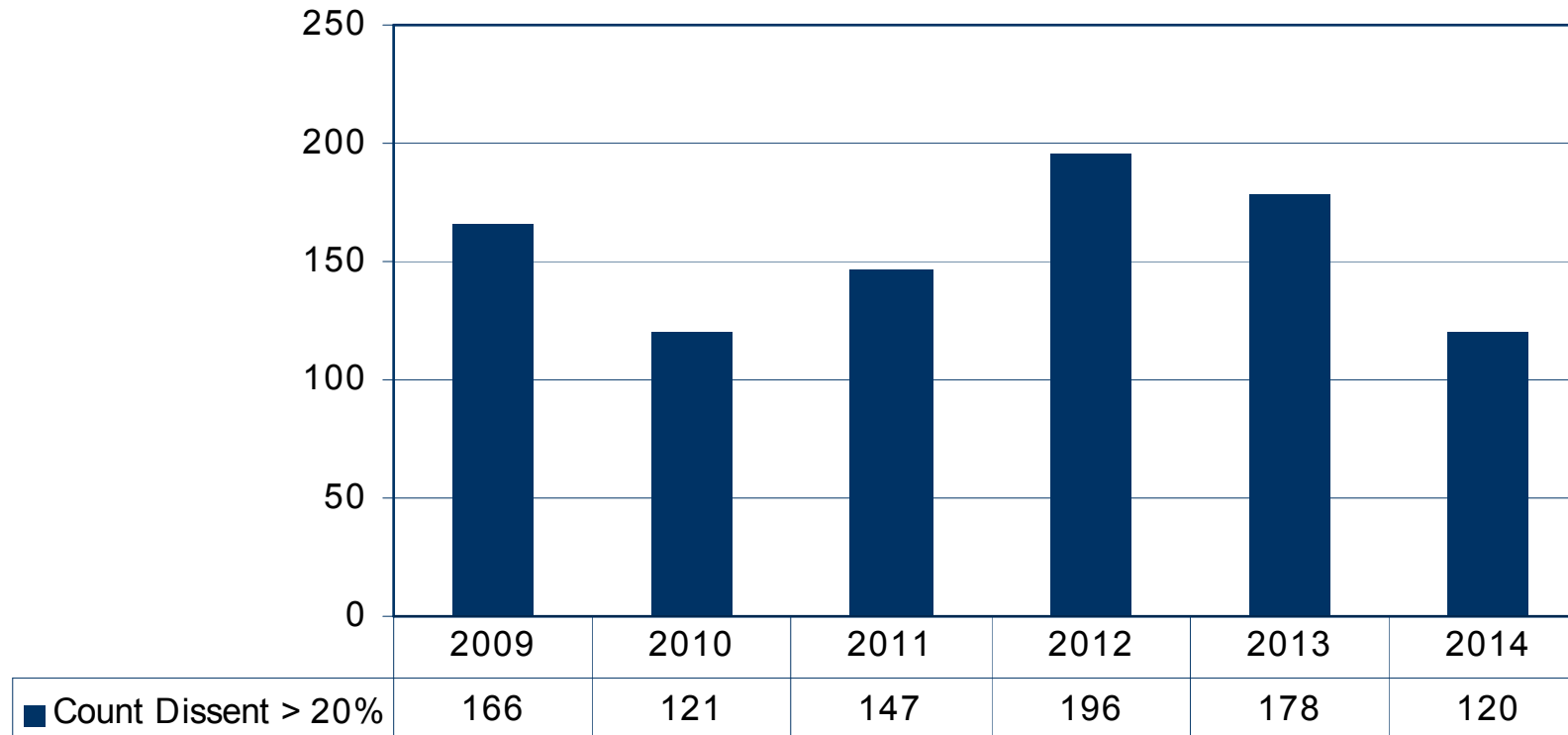
Adjourned/Withdrawn & Defeated Resolutions



Source of data: Manifest, The Proxy Voting Agency

# Cases of High Dissent Reducing

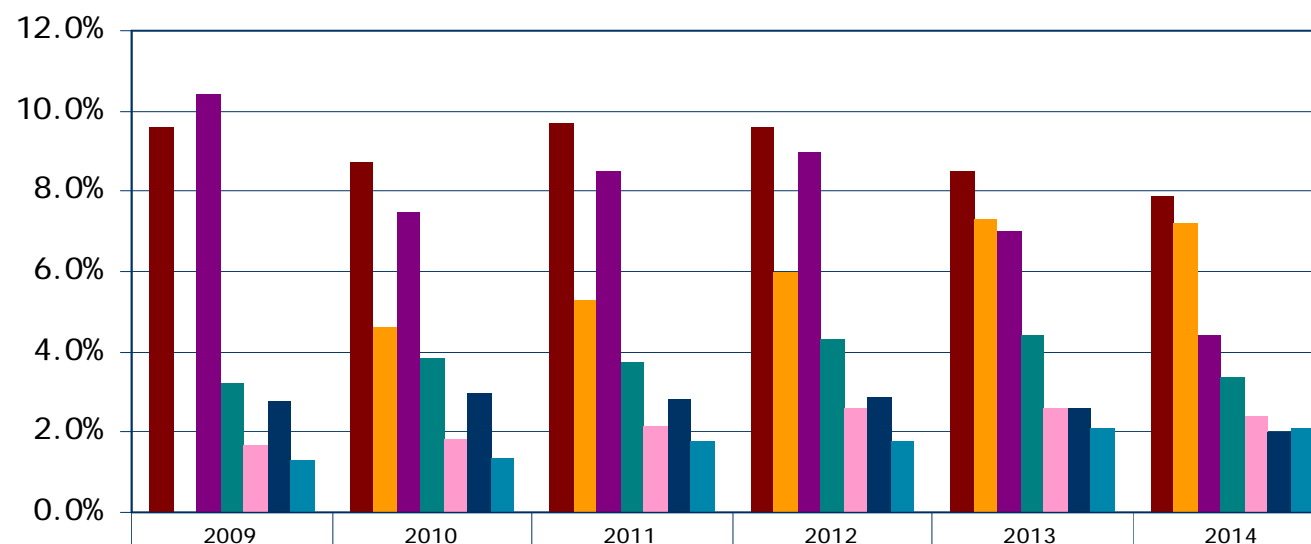
High Dissenting Resolutions



Source of data: Manifest, The Proxy Voting Agency

# Remuneration is the main source of shareholder dissent

## Dissent by Resolution Sub-Categories

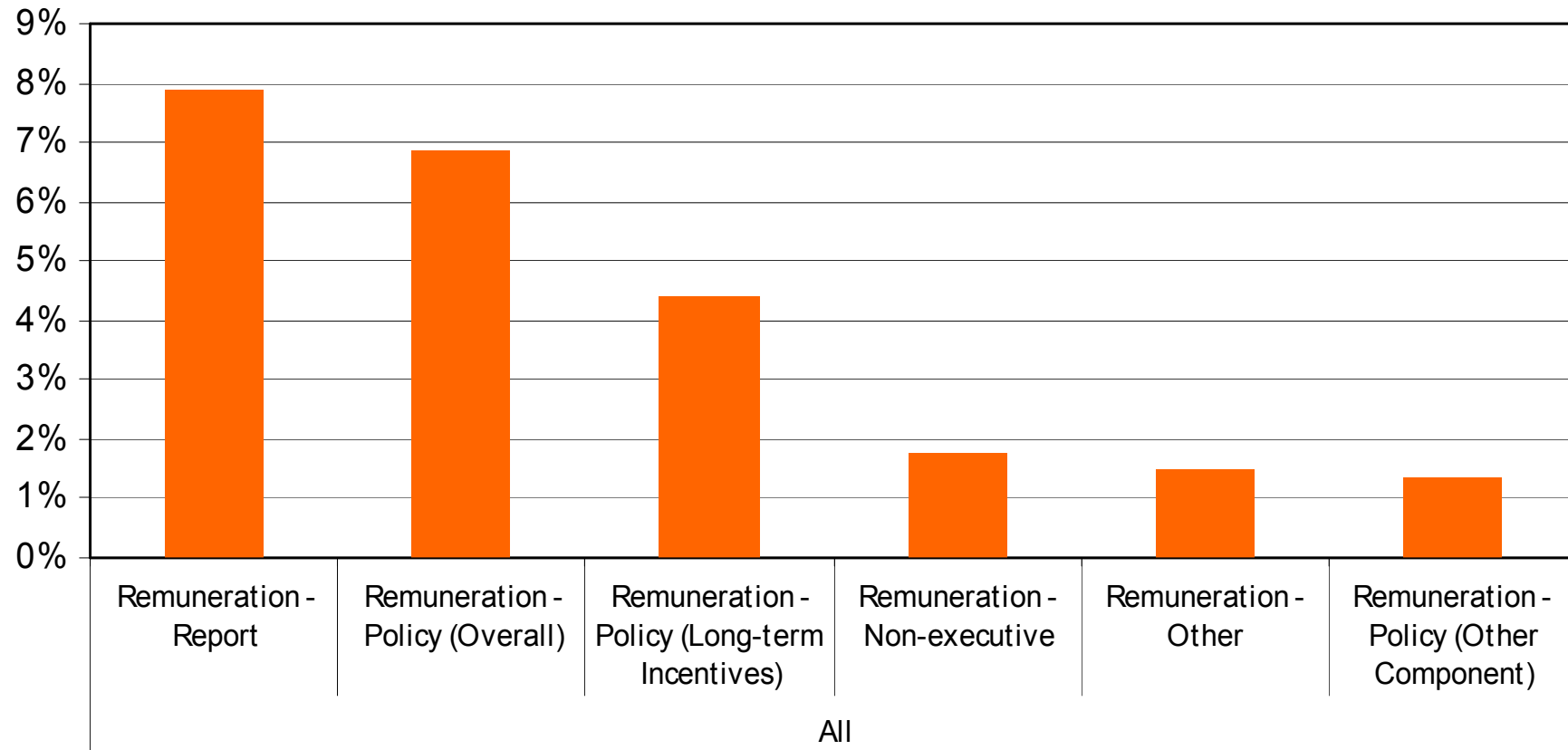


■ Remuneration Report	9.6%	8.7%	9.7%	9.6%	8.5%	7.9%
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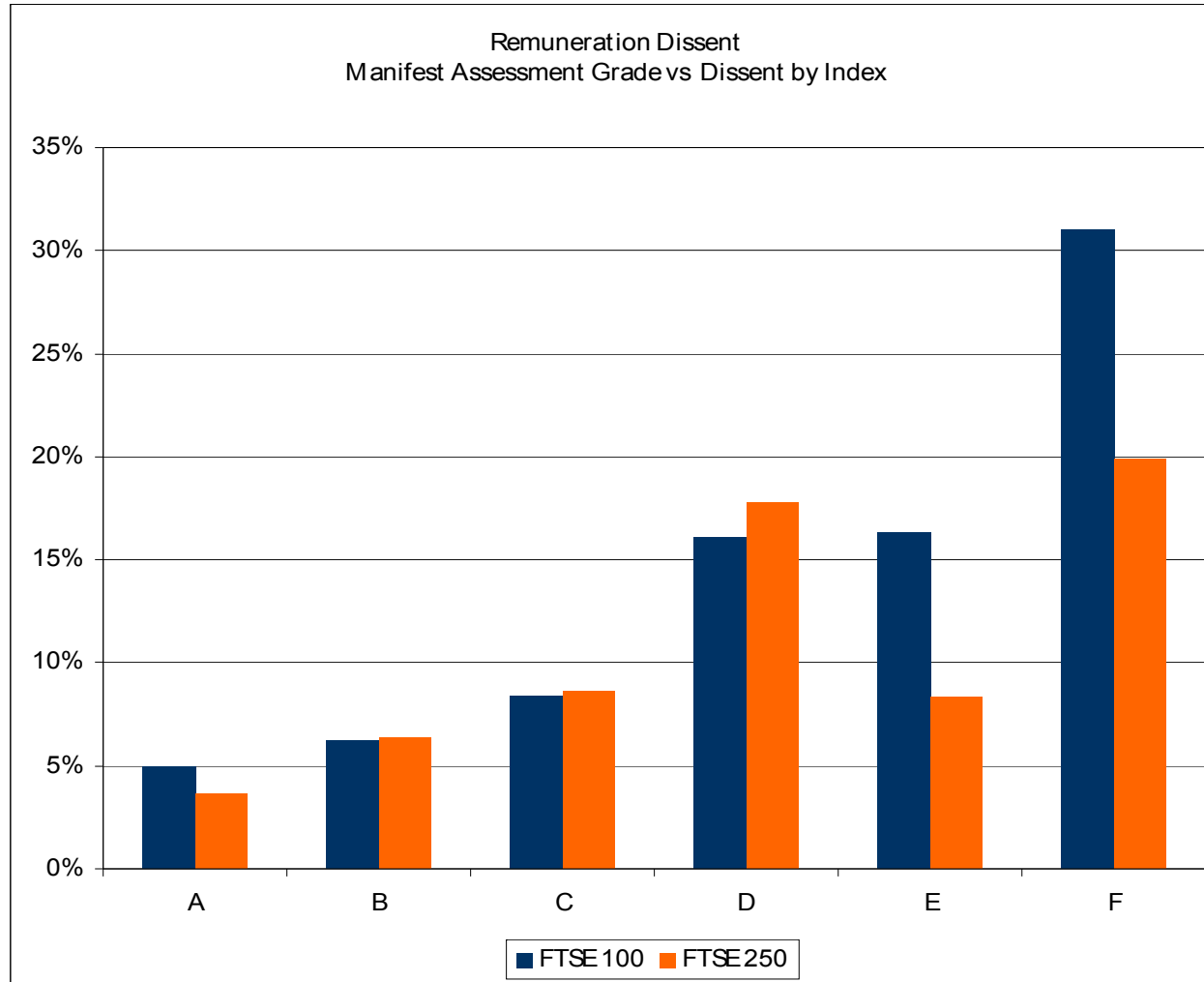
# Shareholders create more of a fuss about last year's remuneration than future policy

Remuneration-related Average Dissent



Source of data: Manifest, The Proxy Voting Agency

# Manifest Scoring System is a good predictor of dissent



Source of data: Manifest, The Proxy Voting Agency




## D Grade Worked Example

REWARD ELEMENT	% SCOREWEIGHT	MAXIMUM PENALTY POINTS	ACTUAL
<b>Alignment</b>	<b>40</b>	<b>100</b>	<b>10</b>
- Link to Strategy	12	30	0
- Short Term Incentive - Performance Measures	8	20	7
- Long Term Incentive - Performance Measures	16	40	3
- Director Shareholdings	4	10	0
<b>Quantum</b>	<b>48</b>	<b>120</b>	<b>67</b>
- Total Remuneration	12	30	28
- Salary	12	30	4
- Pensions & Other Benefits	4	10	9
- Short Term Incentive	10	25	8
- Long Term Incentive	10	25	18
<b>Contracts</b>	<b>8</b>	<b>20</b>	<b>0</b>
<b>Dilution &amp; Cost</b>	<b>4</b>	<b>10</b>	<b>0</b>
<b>Overall Assessment Score</b>	<b>100</b>	<b>250</b>	<b>77/D</b>

Source of data: Manifest, The Proxy Voting Agency



# Companies with major dissent

Company	2014 Resolution	2014 dissent	Issues of Concern
Kentz Corporation	Remuneration policy	58%	Remuneration Committee retained discretion to make emergency payments outside the remuneration policy  Additionally, the annual bonus was to be paid in cash only and there are no shareholding guidelines
	Remuneration report	58%	CEO received a one-off bonus following the announcement of the completion of the Class 1 transaction in acquiring Valerus Field Solutions
			CEO also received a substantial increase (38%) of his basic salary
Burberry	Remuneration report	53%	A generous pay package awarded to the new CEO Christopher Bailey despite a lack of previous ED experience and including a one-off award worth nearly £15m
Reckitt Benckiser	Remuneration report	43%	Targets deemed insufficiently stretching to justify the level of awards granted.
Hiscox	Remuneration policy	42%	Significant flexibility allowed within the recruitment policy and lack of ability to implement malus and clawback.
Carnival	Remuneration report	42%	Annual bonus paid out despite poor corporate performance over the last three years. In additional generous recruitment arrangements provided for the new CEO including a guaranteed bonus.
Standard Chartered	Remuneration policy	41%	Generous remuneration package with a weighting towards short-term performance and the use of EBA discounting adding an undesired level of complexity.
AstraZeneca	Remuneration report	39%	A lack of (even retrospective) transparency around the targets for the metrics that would determine the vesting of the LTIP. Additionally, generous awards given to the departing CFO and overly generous recruitment awards given to incoming CFO.
Crest Nicholson Holdings	Remuneration report	39%	"Exceptional" LTIP awards granted during the year for retention purposes despite crystallisation of pre-IPO awards. Additionally, the awards granted against apparently unchallenging ROCE targets.
International Personal Finance	Remuneration report	39%	Significant salary increase for the CEO alongside share award at 'exceptional' level without sufficient rationale.
 Dissent is calculated as composing votes against + abstentions			

Source of data: NAPF

## Companies with major dissent - summary

Company	Discretion	One off bonus/ award	Big Salary Increase	Targets not stretching	Too much flexibility	High Pay
<b>Kentz Corporation</b>	✓	✓	✓			
<b>Burberry</b>		✓	✓			✓
<b>Reckitt Benckiser</b>				✓		
<b>Hiscox</b>					✓	
<b>Carnival</b>				✓		
<b>Standard Chartered</b>						✓
<b>AstraZeneca</b>				✓		
<b>Crest Nicholson Holdings</b>				✓		
<b>International Personal Finance</b>			✓	✓		

Source of data: NAPF

# Update of ABI (now IMA) Principles

## Re-emphasise:

- **Amounts and Gearing of variable pay**
  - In normal circumstances, basic salary increases should not exceed inflation or the increase for the general workforce
  - The reasons for any increase to maximum variable pay should be clearly explained Threshold performance –concerned about the absolute amounts payable for the achievement of threshold performance.
- **Length of performance/holding period**
  - Should be linked to the implementation of the strategy of the business
  - Consider additional holding periods.
- **Retrospective changes to performance conditions**
  - Retrospective changes to performance conditions to take account of recent movements in exchange rates, - not supported
  - Shareholders are not immune to these exchange rate fluctuations and consider the management of exchange rate risk to be part of an Executive's role.

# Update of ABI (now IMA) Principles

## The last AGM season

- **Engagement process** – could be improved by:
  - **Consulting or informing shareholders.** Companies should be clear with shareholders if they are only notifying shareholders of a change;
  - **Consult shareholders as early as possible.** Problems when too late to consider proposals properly and give feedback;
  - **Full information.** Problems often arise if the full details of a proposal are not given during the consultation.
  - **Provide a wrap up of the consultation process.** Helpful if companies send a wrap-up letter confirming that the consultation process has closed and setting out what has been decided.
- **Retrospective disclosure of annual bonus targets** – The level of retrospective disclosure companies have provided on performance targets has been disappointing.
- Shareholders are concerned that disclosures deteriorated under the new regulations, with a large number of companies using the “**commercially sensitive**” opt-out. Remuneration Committees should retrospectively disclose the performance range for annual bonus targets as well as the performance actually achieved. This is important in demonstrating the link between pay and performance.

## Update of ABI (now IMA) Principles

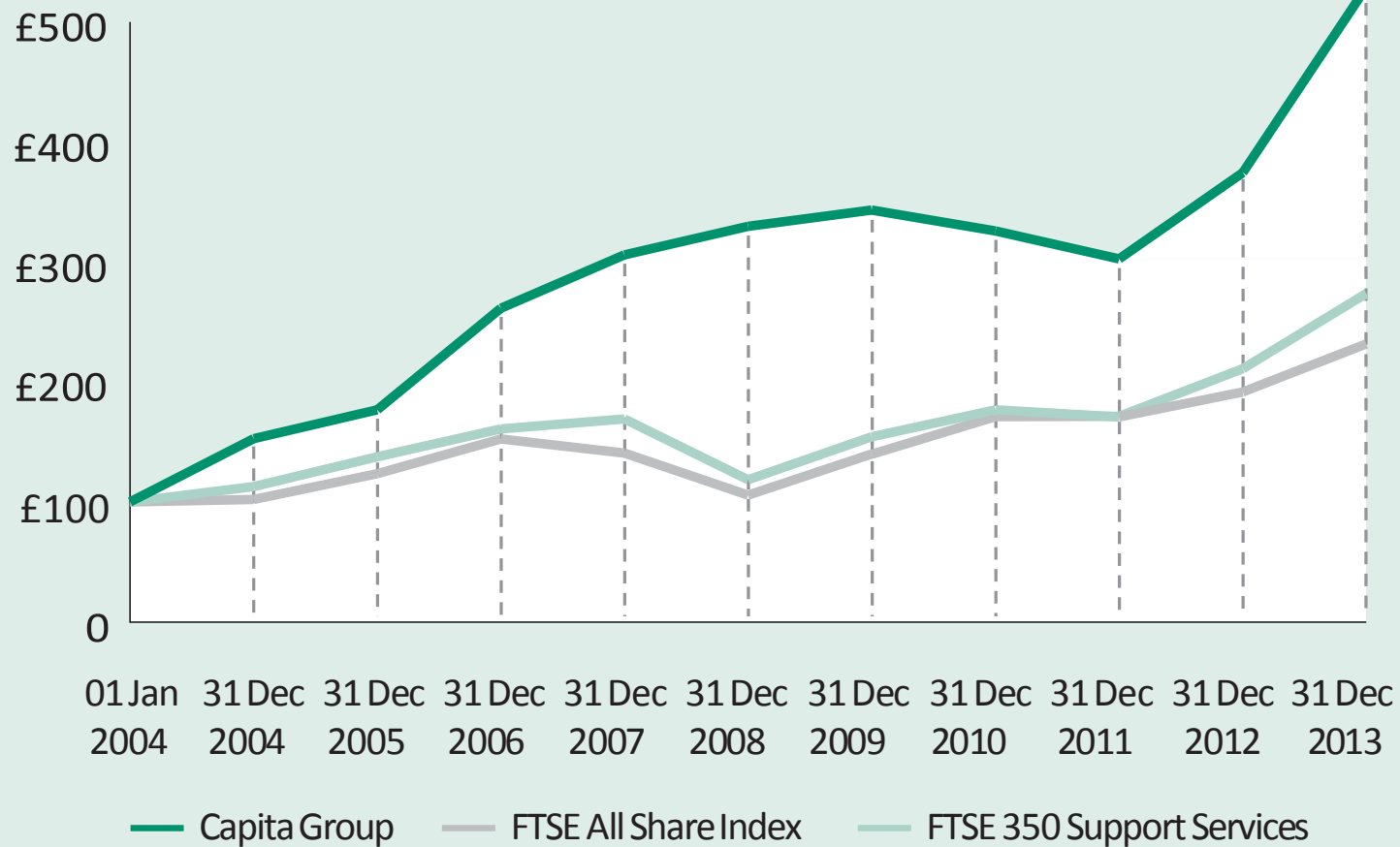
- **Public Assurances** – A number of companies provided public assurances or further information on the operation of their Remuneration Policies ahead of the AGM. These were helpful and welcomed. Members do not expect companies to seek a re-approval of their policy at the next AGM to incorporate these assurances, but would expect details of them to be included in the next Remuneration Report.
- **Disclosure of the Policy Report** – Although not required by the Reporting Regulations, it will be helpful to shareholders if the Policy Table is disclosed in the Remuneration Report on an annual basis.

# Chairman's letter

- **Two distinct styles:**
  - 'Intrinsic' – focused on report format, remuneration membership and activities
  - 'Extrinsic' – focused on remuneration philosophy, KPIs, company performance and remuneration outcomes
- **Some companies included an extra section after the letter to show remuneration at a glance**
  - Most companies provided more information than required by the new regulations (e.g. committee terms of reference, activities and attendance)
- **Include a summary remuneration table in the chairman's letter**
- **References to shareholder consultation are more useful (and powerful) if they describe the issues and responses (also part of para 40)**

# Telling the story and logic of pay over 10 years is better than 5 or 6

Capita vs. FTSE All Share Index and FTSE 350 Support Services Index  
Value of investment of £100 on 1 January 2004



## Annual bonus: the 'relevant details'

- **Disclosure rules require measures, weighting, target, maximum opportunity, actual performance, actual payout**
- **There is of course a blanket 'cop out' for commercial sensitivity, but requiring an explanation and when, if ever, members can expect to get full disclosure**



# Bonus targets and measures - example easyJet

**easy-read**  
**easy-understand**  
**easy-full disclosure**  
**easy-links to KPIs**

## How was pay linked to performance in 2013?

Measure	As a percentage of maximum bonus opportunity		Performance required			Actual	Payout
	CEO	CFO	Threshold	On-Target	Maximum		
Profit before tax (£m)	70%	60%	283	315	362	478	100%
On-time performance	10%	10%	80%	83%	88%	87%	94%
Customer satisfaction targets <sup>1</sup>	10%	10%	77%	82%	85%	83%	62%
Cost per seat (ex. fuel) <sup>2</sup>	10%	10%	£36.82	£36.59	£36.24	£36.81	11.7%
Departmental objectives	–	10%	Successful	Exceeding	Outstanding	Outstanding	100%

<sup>1</sup> easyJet changed survey provider during the year and future targets will be set on the basis of a different survey provided by Milward Brown. For future reference, the correlated customer satisfaction scores for achievement and targets above, on the basis of the new provider, would be: 80.4% achieved versus targets of 74.8% threshold, 79.7% on target and 82.6% stretch.

<sup>2</sup> Cost per seat (excluding fuel) targets are at constant (plan) currency.

## Long-term incentives – the ‘relevant details’

- **Most companies do not appear to have a problem with disclosing the vesting targets for performance periods ending in the relevant year**
- **Mostly these were EPS growth and relative TSR**

# Consideration of employees pay

## **Percentage change in remuneration**

- Generally this was presented as a table

## **Relative importance of spend on pay**

- All complied
- Some used charts – but most used a table
- A few gave a comprehensive breakdown of the allocation of funds

## **Ratio of CEO pay to employee pay**

- Not required by legislation
- Very few have voluntarily disclosed this
- Dodd Frank requirement in US
- High Pay Centre and others are pressing for this

## A shareholder view

*Threadneedle questions for reviewing remuneration reports  
(from Iain Richards, Head of Governance and Responsible  
Investment)*

- **Are they clear, simple and understandable?**
- **Are the package and its elements balanced and proportionate?**
- **Is remuneration aligned with strategy?**
- **Are payments subject to stretching performance conditions?**
- **Do the policies mitigate the risk of rewards for failure?**
- **Most importantly of all, does the policy produce a payout which matches the returns to our own clients**

## Questions for discussion

*Please first describe to your table if you are involved in preparing for/drafting/consulting on your company's remuneration policy and remuneration report and the timing of your shareholder circular/AGM*

- **What did you find or are finding is the toughest issue in preparing the Annual Report on Remuneration and how did you/ are you addressing it?**
- **Are you planning to put any additional information in the 5 (to 10) -year graph to 'tell the story'? What, and how are you presenting it?**
- **What is your thinking on reporting last year's targets and outcomes, with an eye on commercial sensitivity?**