Review of the Effectiveness of the Combined Code

Submission by

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Summary of our responses

1. MM & K are remuneration consultants. We have wide experience of working with listed and unlisted companies and have a particular niche with private equity companies. As experts in remuneration, we have limited our comments to those parts of the code concerned with remuneration.
2. The last decade has seen no gains for shareholders (the FT-SE 100 index is at the same level as it was 10 years ago). However, the total remuneration of the average chief executive of a FTSE 100 company has gone up fourfold. This suggests there may be a serious problem.
3. It is widely agreed that remuneration practices were a contributing factor to the disasters in the financial services industry. It is our view that in the financial services industry:
    a. the disclosures of remuneration failed to give shareholders adequate information for them to be able to recognise and evaluate the risks that managers were being incentivised to take
    b. the performance measures chosen and the timeframes in which they were measured created asymmetric rewards;
    c. Schedule A of the Combined Code encourages:
        i. the choice of performance measures and performance scales which incentivise and reward volatility[1]; and
        ii. timeframes which are significantly shorter than many business cycles ;
    d. Generous defined benefit pension schemes mean that the executives of some banks have been able to leave and still receive very high levels of rewards. This problem is further exacerbated by the high levels of salaries paid to some chief executives. The Combined Code warns of the dangers of ratcheting up salaries.
    e. There was a strong financial incentive to make acquisitions. As a consequence of what has become custom and practice, executives know that their pay would be significantly enhanced if they make an acquisition. In addition, the companies who increased salaries of the chief executives following an acquisition or merger also increased the value of his/her pension scheme.
    f. Generous pension schemes undermine the link between pay and performance by increasing the proportion of fixed remuneration.
4. It is also widely agreed that there have been fundamental and very grave failures of corporate governance and regulatory supervision of the financial services industry on a number of levels. What is less clear is whether such failures apply to the rest of British industry which makes up the vast majority of listed companies.
5. Nevertheless, in respect of remuneration, it is our view that there are several areas of concern, where practice can be improved. Revisions to the Combined Code should be aimed at achieving these improvements.

[1] We use the term volatility in its statistical and technical sense as the standard deviation of share price movements.

6. Our proposals can be summarised under ten headings:

a. The total value of the various components of the package should be added together to form a total remuneration value. This should be expressed in two ways: companies should firstly disclose the net present value (economic value) of total remuneration at the time it is awarded, and secondly the value of total remuneration actually realised (i.e. including options exercised and performance shares that vest in the year). Providing a total value is a requirement in the US and we think it should be the same in the UK. At present its constituents are spread over several pages and not added up.

b. There should be disclosure of chief executive pay over the previous five years so that the pay linkage to performance is clear to shareholders. Currently, the disclosure requires a five-year graph of TSR. We think chief executive pay should be shown alongside this. (Companies could then explain the linkage of pay to performance and pay awarded and realised versus the stated policy – this supports the goal of accountability.)

c. Chief executive total remuneration should be disclosed alongside the average remuneration of employees and the ratio of the two should be shown. There has been widespread concern about the growing differentials between chief executives' and average employees' remuneration, but this is not the reason for our proposal. We believe that chief executive pay should be linked to performance and any increase above the average for employees should be justified to shareholders. The combination of this disclosure together with a comparison of chief executive pay over the previous five years with TSR (and any other relevant performance measures) will force companies to explain why they have paid the chief executive the way they have.

d. Improved disclosure of the proportion of pay that is linked to performance. Pay should include all elements of remuneration including pension. The proportion that is performance related, for both awarded remuneration and realised remuneration, should be stated as a percentage of the total remuneration.

e. Improved disclosure of potential termination payments. We propose a table showing the maximum that might be paid as well as a target figure using reasonable assumptions regarding mitigation, etc.

f. Disclosure of the top five executives' remuneration. This would match the requirement in the US.

g. The Schedule A guidance on performance related pay should encourage:

   i. steady growth over volatility
   ii. long-term performance rather than short-term
   iii. absolute returns to shareholders

h. There should be improved support for the non-executives serving on the remuneration committee. Remuneration is the area in which there is the most potential for conflicts between the executive and non-executive directors. The current Combined Code allows for the provision of external support for non-executives. However, we think the wording needs to be strengthened and made more explicit.

i. The fees paid to advisers for remuneration committee advice and, separately, fees for their other services to the company and its pension fund should be shown in the annual remuneration report.

j. There should be a code of ethics for remuneration consultants.

THE PROBLEMS

There are several problems relating to executive remuneration and we are listing these problems so that our recommendations can be put into context.

1. Pay has not been linked to performance in practice

   a. Performance pay has increased substantially over the past 10 years but not performance, as ultimately reflected in share price. (See Appendix 1, which contains an extract from the MM & K/Manifest 2009 Executive Directors Total Remuneration Survey. Appendix 2 shows comparative data since 1983.)

   b. There continue to be large payoffs for executives who leave underperforming companies. These payments attract large amounts of publicity and undermine the general public's faith in the proposition that pay is linked to performance. Part of the problem is that the payments are unexpected because the disclosure in annual reports is not "clear, transparent and readily understandable to shareholders" as required in early versions of the Combined Code. For example:

      > The cases of Michael Green at Carlton in 2002 and Sir Fred Goodwin at RBS in 2007/08 are examples of why we feel there is a need for further legislation/disclosure rules. It is not at all "clear", "transparent" or "readily understandable by shareholders" (these are the 2003 Combined Code words – preamble Para 11) from reading the 2002 Carlton annual report that such large amounts on termination would be due. It is "transparent" to an expert, but only on reading the 2002 report together with the shareholders circular of 2001. The 2007 RBS annual report is not at all clear that the early retirement provision for Sir Fred Goodwin was "custom and practice" and therefore was a contractual entitlement.

   c. Pension top ups at or close to exit. When senior executives retire early, it is usually a polite way of saying that they are no longer fully effective. For most employees, an actuarial reduction is expected. For example, it appears that RBS custom and practice for senior executives was to make no reduction. The Combined Code warns of increases in salary close to retirement. However, the lack of clear disclosure of pay in a single figure means that the pension implications are not readily discernible by shareholders.

   d. There has been a switch to short-term pay. There is higher emphasis on bonus and less on long-term incentives. Previously, the proportions of salary, annual bonus and long-term incentives that many remuneration consultants targeted were 40/20/40 although in some cases the ratio was 5/5/90 (e.g. Vodafone, Orange). If we look at the banks it appears that in some cases the ratio has now moved towards 40/40/20. The data in appendix 1 confirms this general trend.

   e. The long-term emphasis has switched from 10 years to 3 years. Previously, share options were the main type of long-term incentive and they have a ten-year life (although there is evidence that executives exercise sub-optimally, i.e. prior to the ten years). This meant that the executives had an interest in the long-term share price performance. This is particularly the case when the share price had increased and the options were significantly in the money. Following the Greenbury Report there has been a shift away from share options towards performance shares, which has gained momentum with the introduction of the accounting charge for options. The use of performance shares has been encouraged by the Combined Code which talks of relative performance. The ABI and NABF and other institutional investors have also encouraged this. The result has been the introduction of the three-year relative TSR plans, with no payout for below median performance and maximum payout usually for 75th percentile performance.

   f. Any student of gaming theory will realise that, to maximise one's income from such relative TSR plans, you need, in some cases, to increase the volatility of the share price rather than aim for steady growth. The effects of volatility may be felt in a number of ways:

i. In some cases, it is the volatility of the share price that has caused many performance share plans to fail to vest even though underlying performance was good. To illustrate this suppose the underlying business performance was very good and justified a 20% p.a. increase in the share price. With a volatility of say 40%, there is still a fair probability the relative TSR plan will not vest or only partially vest. With a volatility of 20% there is a much higher expected payout.

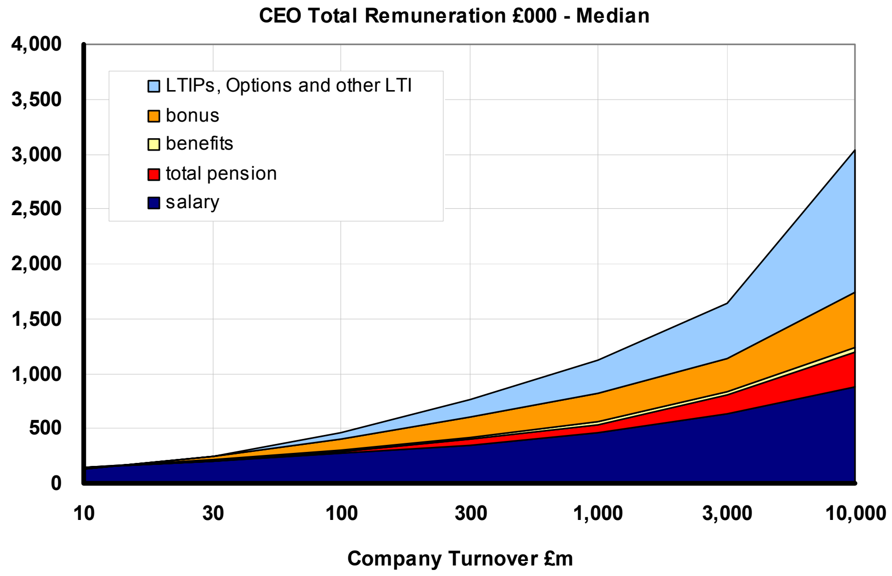
ii. Suppose the underlying business performance resulted in an 8% p.a. increase in the share price. With a volatility of say 40%, there is a 50% probability the relative TSR plan will partially vest and about 30% probability of maximum vesting. With a volatility of 20% there is a much lower probability of maximum vesting.

iii. Suppose the underlying business performance was poor and resulted in justified a 20% p.a. decrease in the share price. With a volatility of say 40%, there is still a chance the relative TSR plan will partially vest and about 3% probably of maximum vesting. With a volatility of 20% there are much lower probabilities of payouts.

g. One way to increase the volatility of the share price is by making an acquisition. Another is to increase the debt to equity ratio by taking on more debt and paying back cash to shareholders. Advisers to companies (e.g. banks, lawyers, accountants) have strongly encouraged such behaviour. Remuneration committees have also strongly encouraged an acquisition culture by linking salary to company size. (The ABI and NABF have recognised the dangers of transactions and have argued strongly against transaction bonuses. However, they have not recognised the inherent incentives in the remuneration systems, which encourage growth by acquisition and merger.) It is also worth noting that the advisers to companies (who so strongly encourage acquisitions, mergers and higher debt) all received their fees for their advice at the time of the deal. What has arisen is a whole edifice which encourages behaviour of short termism, and what President Obama in his Inaugural Speech called “greed and irresponsibility”.

h. In the UK most remuneration is driven off base salary – pension is a % of salary, contractual compensation is a number of years and months of salary (plus other pay and benefits), annual bonuses are calculated as a % of salary and long term incentive awards are made as multiples of salary. So unless salary is set at an appropriate level, there is no chance of controlling pay! Most guidelines and consultative documents miss this key point! Few consultants advocate a more conservative approach to salaries – i.e. hold fixed salaries back and detach the other elements of pay from salary – e.g. pool based bonuses, absolute DC contributions, LTI grants defined in numbers of shares. (There is an argument that the Chief Executive’s salary should be fixed on appointment and should not be subsequently increased; or not by more than CPI or the average employee increase. However, this is beyond the scope of this paper.)

i. Pay has increased most rapidly in the largest companies. Ned Hay (the founder of the Hay Job Evaluation System in the 1930s) found that there was a relationship between pay and job size and that discernable increases were subject to a geometric scale. This is reflected in the pay of Chief Executives which is linked to the logarithm of the turnover of their company. This relationship worked well since the 1930s, but this is no longer the case as is shown in the following chart from the MM & K/Manifest 2009 Executive Director Total Remuneration Survey. It is therefore important that any review of the Combined Code considers its impact on the total level of pay, in particular for the largest companies where pay appears to be above the historic norms. There is an argument that for most of the small cap and AIM companies the average level of chief executive remuneration is appropriate.



2. Disclosure of remuneration has led to fewer executive directors and therefore to less disclosure

   a. There is increasingly a disincentive to becoming an executive director. A number of people have declined board appointments, as they do not wish to be in the public eye.

   b. There are now fewer executive directors than in 2002. The Directors Remuneration Report Regulations may have influenced some companies to keep high paid executives off the main board. This is also partly a by-product of Higgs, who wanted reasonably sized boards and a majority of independent non-executives.

   c. There are many cases of people who are not on the board who are paid large amounts of remuneration. We believe the disclosure of remuneration should extend to executives other than just directors.

   d. To avoid this disincentive, we recommend that disclosure should apply to the 5 highest paid executives and all directors.

   e. The US SEC requires the disclosure of the remuneration of the top five executives. We think it is sensible for the UK to have the same disclosure in this respect.

3. Disclosure has been inadequate – total remuneration not clearly shown

   a. The Directors Remuneration Report Regulations have produced very long and confusing reports, e.g. the 16 pages of GlaxoSmithKline. However, it is not clear how much the chief executive or other executive directors actually received or were awarded. There is lots of explanation, but this seems only to obscure the facts.

   b. The actual remuneration received/earned in a year is reported in 4 separate tables (Schedule 7A Part 3 Paras 6, 7-9, 10-11 and 12.) Nowhere is there a requirement for these separate elements of remuneration to be totalled. We doubt this aids transparency, which is a stated key objective.

   c. It will be difficult to get agreement from all the experts on which figure to use for options and performance shares. When options disclosure was proposed in the US the chief executives of corporate America set up a fighting fund with $70 million to lobby against disclosure. We do not under-estimate the difficulty of getting agreement here.

d. Total emoluments make up only one third of total remuneration (see IRS survey of chief executives of the ten largest UK plcs). Pensions, share plans and options make up the other two thirds.

e. The press coverage of "fat cat" pay is ugly, unfriendly, uncompromising, unhelpful and totally negative. There is no competitive advantage in providing more and/or better information to shareholders as this only provides more ammunition to the press which they will use to criticise the company.

f. Therefore the Government/FSA/FRC has a legitimate role to intervene to require better disclosure and help the market work more effectively.

g. However, we note that the FRC has removed its demand in the Combined Code for remuneration disclosure, relying instead on the Directors' Remuneration Reporting Regulations. The 2003 Combined Code (in the preamble) says that Remuneration Reports should be "clear, transparent and understandable by shareholders". The pre-amble to the current Combined Code no longer contains these words. We think these words should be reintroduced as a clear goal of what is expected as best practice.

   i. In the current environment companies have been unwilling to provide such clarity. Therefore the Government/FSA/FRC should legislate or introduce rules to force companies to do so.
   ii. 16 pages for an annual report on remuneration rarely results in a report which is clear transparent and readily understandable by shareholders. We have attached, as appendix 3, a one-page illustration which clearly shows how much the chief executive has been paid over five years. It does this in a transparent way. We think it is readily understandable by shareholders. We do not advocate that the FRC stipulate that this is a requirement, as it may not be the most appropriate means of communicating to shareholders by all companies. What is important is that any company which writes its report in a way which is not "clear, transparent and readily understandable by shareholders" should be non-compliant with the Combined Code and should be required to explain why it has chosen not to comply.
   iii. In this respect, the FRC may wish to consider the 2007 Royal Bank of Scotland report and the disclosure in that report of pension entitlements of the executive directors.

h. The FT leader column on 15th April 2003 also recommended providing a total remuneration figure.

i. As we have noted above, it is possible to explain chief executive pay simply on 1 page of A4 (see Appendix 3 for our example). No-one has done this voluntarily.

j. Figures on dilution only refer to new issue shares. Some companies use shares bought in the market place and held in trust. Others use treasury shares, which is a recent development in the UK. From a remuneration point of view, it is more useful to know the total number of shares under option/ granted under shares schemes and what proportion have been granted to the chief executive, top 5 executives and other employees. The ABI/NAPF guidelines are "behind the curve" (i.e. out of date) in this respect. [The IAIM guidelines in Ireland require all shares used to be taken into account when considering dilution.

k. The US disclosure requirements regarding long term incentives seem to represent best practice and could be replicated in the UK. The value should be stated as well as the potential gain if the share price were to increase by 5% or 10%. The following table illustrates the disclosure for options:-

	Individual Grants				Potential Realisable Value at assumed annual rate of share price appreciation for option term (1)	
Name	Number of shares over which options granted	% of total options granted to employees in 2000	Exercise Price £/share	Expiration date	5% ($)	10% ($)
Chief executive	200,000	2.8%	20.00	01/05/2010	2,515,579	6,374,970
Dir 2	-	-	-	-	-	-
Dir 3	60,000	0.8%	20.00	01/05/2010	754,674	1,912,491
Dir 4	50,000	0.7%	20.00	01/05/2010	628,895	1,593,742
Dir 5	100,000	1.4%	20.00	01/05/2010	1,257,789	3,187,485
Total of all shareholders (2)					17,890,835,187	45,338,889,012

(1) The amounts are the result of calculations at the 5% and 10% growth rates set by the SEC; the rates are not intended to be a forecast of future share price appreciation. A zero percent share price growth rate will result in zero gain for all optionees.

(2) The amounts are included for comparative purposes to show the gain that would be achieved by the holders of the outstanding shares of the Company at the assumed share price appreciation rates at the end of the 10-year term of the Company options granted on 1st May, 2000 at an exercise price of £20.00.

4. Remuneration committees need but have not usually received independent advice:

a. Remuneration is increasingly complex. Performance measures are more complex. Committee members need to consider risk and in some cases complex statistical modelling. The taxation of remuneration is more complex and will become increasingly so, from 2010 onwards. There is a need for greater understanding of the use of pensions, trusts and complex subsidiaries structures and the use of management companies/partnerships. The legal issues are more complex. It is unrealistic to expect members of remuneration committees to have all this technical knowledge themselves and so they will need independent expert advice. There is a conflict here if this advice is provided by internal resources. If external advice is sourced by executives there is also a potential conflict. It is critical that non-executives on the remuneration committee assess the advice they are receiving and, where necessary, seek independent advice.

b. There should be improved support for the non-executives serving on the remuneration committee. Remuneration is the area where there is the most potential for conflicts between the executive and non-executive directors. The executives have huge internal resources available to them in order to make their case for higher pay. They can and do supplement these internal resources with external consultants, many of whom find it difficult to give objective, independent advice on pay as they know that other consultancy projects will be at risk if they upset the chief executive and other executive directors. Many of these external consultants become culturally attuned to pleasing the executives, so that even when appointed by the non-executives their advice is will still favour the executives, rather than the shareholders' long-term needs. The current Combined Code allows for the provision of external support for non-executives. However, we think the wording needs to be strengthened.

c. We think that Schedule A to the Combined Code has been misinterpreted by most remuneration consultants so that they have promoted remuneration arrangements that favour executive management and in particular:

    i. short-term rewards and
    ii. rewards for higher volatility rather than steady growth.

d. Some remuneration consultants have used private equity comparisons to justify higher pay for executives in listed companies In practice, these comparisons are not as relevant as some people would lead one to believe. The private equity industry model for companies in which they invest is of low salary, high risk, high leverage and tax effective rewards via capital gains which are taxed at 18% (entrepreneurs' relief is still only taxed at 10%). In listed companies, salaries are higher, often with generous pensions and a much lower risk of being exited by shareholders. In summary:

Private Equity backed company	**Listed company**
Pay structure is simple	Pay structure is complex – many plans
Equity is key component	Incentives through annual bonus and long term plans
Equity gains taxed at 10%/18%	LTIP/ share option gains taxed as income at 40% +1% NI and 12.8% Employers NI – soon 50%, 1.5% and 13.3%!
Salaries set at basic level	Salaries ratcheted up each year
Lower bonuses	Bonus opportunity typically 100% of salary – more in bigger companies - and trend is rising. Very few chief executives get nil bonus
Risk of failure/downside	Often generous severance terms and good pensions
Dilution of 10 to 20% and mainly front end loaded	ABI/NAPF guideline of 5% over 10 years = 0.5% p.a.
Highly leveraged	Modest debt /equity leverage
Managers closely monitored by investors	Most shareholders have small (<5%) stakes and need to build consensus over time before they can convey their view to boards about management performance
Clear strategy and performance drivers	Very bland performance criteria, resulting in blunt instrument

e. Many consultants are not independent and this issue needs to be addressed. How can the auditors or actuaries give independent advice to remuneration committee, concerning the pay of the Chief Executive and his/her directors, if they are also receiving hundreds of thousands (or even millions) of pounds in fees for other services provided to the chief executive and his/her directors?

f. Some remuneration consultants have a potential conflict of interest, for example:-

i. auditors, such as E&Y, PWC, KPMG or Deloitte & Touche;
ii. actuaries such as Mercer, Towers, Watson Wyatt or Hewitt;
iii. part of a larger group selling advisory services, e.g. Mercer which is part of Marsh, Aon Consulting which is part of Aon.

g. Such organisations predicate their business strategy on cross-selling other services. Such behaviour is culturally embedded. Progress up the career ladder requires consultants to act in the best interest of the group by introducing their colleagues, by cross selling other services and by not doing anything that might threaten existing relationships. Even if they have externally announced changes, it will take years to change an embedded culture – even assuming they really want to change!

h. The Conference Board in the US in its 2002 report on Public Trust and Private Enterprise concluded that management had got too close to their remuneration consultants. This is also true in the UK. It is a big problem. Companies and directors are still in denial mode. The problem needs some light shedding on it. The Government can help by legislating as described below. This will give investors and the press the necessary information to force directors to recognise the problem exists and must be managed better.

i. There is no code of ethics for remuneration consultants. We note the ABI and Financial Times (15 May 2009) have called for a code of ethics.

5. Some of the Code is out of date

a. Schedule A to the Combined Code is no longer appropriate. It was written by Greenbury in the middle of a bull market. Our suggested re-drafting of the Code is in Recommendation 1 on page 11.

6. Shareholders are absentee landlords

a. The average time that shares are held is nine months. We believe it is essential that executive directors' remuneration is aligned with shareholders interests. However we cannot conclude that this should be aligned over a nine-month time-frame!

b. There is a Companies Act requirement to manage in the best interests in the long term.

   i. This duty is set out in section 172 of the Act. This is a new duty developed from one of the heads of the overriding principles of the fiduciary duties, i.e., duty of good faith to act in the company's best interest.

   ii. The Act imposes a duty to act in the way a director considers, in good faith, would be most likely to promote the success of the company. Although this duty is still owned to the members as a whole, when exercising this duty the director is required to have regards to various non-exhaustive list of factors listed in s.172 (1) including the long term consequence of the decisions as well as the interests of the employees; the relationships with suppliers, customers; and the impact of the decision on community and environment; the desirability of maintaining a reputation for high standards of business conduct; and the need to act fairly as between members of the company.

   iii. It can be seen that among other things, this duty introduces wider corporate social responsibility into a director's decision making process.

   iv. 'Success' is not defined in the Act. The DTI's guidance to the Bill suggests that a success in relation to a commercial company is considered to be its "long-term increases in value".

c. The Combined Code in its second sentence in the preamble states "Good governance should facilitate efficient, effective and entrepreneurial management that can deliver shareholder value over the longer term."

d. Most listed company shareholders have small (<5%) stakes and need to build consensus (with other shareholders, but without forming a concert party) over time before they can convey their view to boards about management performance.

e. The alignment of interest should be over the long term which in many cases should be well in excess of three years.

f. Many hedge funds want increased volatility, as they gain by trading in and out of shares. Remuneration schemes should not be aligned with the desires of such shareholders.

g. The ABI and NAPF claim to be representative of shareholders. It is no longer the case that their members own the majority of shares in many companies. They are trade associations often seeking publicity to justify themselves and to help attract new members.

h. The ABI and NABF guidelines also suffer from the same problems of short-term-ism and encouraging dysfunctional higher volatility. They also very long and detailed. It is possible that some remuneration consultants may have colluded with these representatives of institutional investors to create a cottage industry which is not in the best interest of long-term shareholders. IVIS is the “for profit” subsidiary of the ABI. Risk Metrics is a “for profit” organisation who assess whether the NAPF guidelines are being followed. It is in their interests of both to generate more complexity through more detailed and complex rules/guidelines. Public rows on pay help them establish their profile.

i. There is a strong argument that the ABI and NAPF guidelines have had their day – that they were useful but are now too complex. If it is felt that more detailed guidelines than Schedule A of the Combined Code are required, then they should be written by a neutral body such as the FRC or a committee constituted by it.

j. Views of shareholders, who own shares for the long-term, should be given a higher weight than the views of short term shareholders in any consultation or shareholder engagement around the issues of directors’ remuneration.

7. The City is driven by transactions and a mergers and acquisitions culture and the fees this generates for advisers. In too many cases, remuneration of listed plc executives is aligned with the short term interests of the City rather than with the interests of long-term shareholders.

8. Scope of the Combined Code

a. The Code currently applies to some 600 companies plus investment trusts listed on the UK main market.
b. The problem with the current process is that the very big companies ignore the Code, ABI and NAPF guidelines, which become a burden for the smaller companies. Many smaller companies feel obliged to tick the boxes, rather than the remuneration committee spending their limited time and energy in thinking carefully about what is best for their company in their particular circumstances.
c. We believe that the vast majority of public concern is with the FT350 companies and that the Code should cover these directly, whilst recommending those outside the 350 to follow best practice.
d. Perhaps the remuneration parts of the code should apply only to the top 30 companies? These are the Bellwethers?

Detailed recommendations follow.

Only Recommendations 1, 2 and 3 are proposed changes to the Combined Code.

The rest are recommendations on best practice arising from B2 Supporting Principle ‘the Remuneration Report should be clear, transparent and readily understandable by shareholders’. They could form a new Schedule D to the Code, or alternatively be proposed changes to the DRRR. The DRRR are part of the Listing Rules and as such fall under the responsibility of the FSA. It is therefore imperative that the FRC and FSA liaise on this issue.

RECOMMEDATION 1

Revised Schedule A - changes shown in red

Schedule A: Provisions on the design of performance-related remuneration

1. The remuneration committee should consider whether the directors should be eligible for annual bonuses. If so, performance conditions should be relevant, stretching and designed to enhance shareholder value. Upper limits should be set and disclosed. There may be a case for part payment in shares to be held for a significant period.

2. The remuneration committee should consider whether the directors should be eligible for benefits under long-term incentive schemes. Traditional share option schemes should be weighed against other kinds of long-term incentive scheme. In normal circumstances, shares granted or other forms of deferred remuneration should not vest, and options should not be exercisable, ~~in less than~~ for at least three years. Directors should be encouraged to hold their shares for a further period after vesting or exercise, subject to the need to finance any costs of acquisition and associated tax liabilities. Directors should normally not sell their shares until at least two years after vesting. Directors should normally not sell their shares until at least two years after they leave the company.

3. Any new long-term incentive schemes which are proposed should be approved by shareholders and should ~~preferably replace any existing schemes or at least~~ form part of a well considered cohesive, integrated overall plan, incorporating existing schemes. The total rewards potentially available should not be excessive.

4. Payouts or grants under all incentive schemes, including new grants under existing share option schemes, should be subject to challenging performance criteria reflecting the company's objectives. [2] [3] ~~Consideration should be given to criteria which reflect the company's performance relative to a group of comparator companies in some key variables such as total shareholder return.~~

5. Grants under executive share option and other long-term incentive schemes should reflect the business strategy and the need to incentivise and retain key executives - in normal circumstances they would ~~normally~~ be phased rather than awarded in one large block.

6. In general, only basic salary should be pensionable.

7. The remuneration committee should very carefully consider the pension consequences and associated costs to the company of basic salary increases and any other changes in pensionable remuneration, **especially**[4] for directors close to retirement.

8. Remuneration strategy should aim to reward the long term performance of the company and its executive directors. The remuneration committee should be aware of the risks inherent in the business of the company and the chosen risk strategy/appetite and should ensure that the remuneration strategy is not rewarding excessive risk-taking.

9. The remuneration design should consider if the company's culture, code of conduct, human resource policies, and performance reward systems support the business objectives and risk management and internal control systems.

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[2] We recommend the next sentence is deleted. An alternative wording could be considered "Consideration should be given to criteria which reflect the company's performance relative to a group of comparator companies in some key variables such as total shareholder return as well as absolute returns over the long term."

[3] Note in the period 1991-95 there was a bull market and options got a bad name. The phrase "all boats go up on a rising tide" highlighted the then concerns and so relative performance was promoted. In addition in the late nineties all the fund managers, who were themselves compensated on relative performance, said that if they were paid this way then so should company directors. Their logic was flawed. The relative TSR approach did not work and created the wrong culture. We believe companies should consider both absolute and relative measures.

[4] The recommended change is to underline and bold the word especially

RECOMMENDATION 2

Revisions to Combined Code Section B: Remuneration

B.1 The level and make-up of remuneration

Main Principles

Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose.

A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.

The remuneration design should consider the risks that are being incentivised.

Supporting Principle

The remuneration committee should judge where to position their company relative to other companies. But they should use such comparisons with caution, in view of the risk of an upward ratchet of remuneration levels with no corresponding improvement in performance.

They should also be sensitive to pay and employment conditions elsewhere in the group, especially when determining annual salary increases.

The remuneration committee should consider if the company's culture, code of conduct, human resource policies, and performance reward systems support the business objectives and risk management and internal control systems.

Code Provisions

Remuneration policy

B.1.1 The performance-related elements of remuneration should form a significant proportion of the total remuneration package of executive directors and should be designed to align their interests with those of shareholders and to give these directors ~~keen~~[5] incentives to perform at the highest levels. In designing schemes of performance-related remuneration, the remuneration committee should follow the provisions in Schedule A to this Code.

~~B.1.2 Executive share options should not be offered at a discount save as permitted by the relevant provisions of the Listing Rules.~~ **[Comment: some performance shares are offered as nil price options so this drafting is out of date.** Sometimes a partly discounted option provides a good hybrid between the two types of plan. The relevant thing is the total value, not the issue of discounting.**]**

B.1.3 Levels of remuneration for non-executive directors should reflect the time commitment and responsibilities of the role. ~~Remuneration for non-executive directors should not include share options.~~ If~~, exceptionally~~, options are granted, shareholder approval should be sought ~~in advance~~ and any shares acquired by exercise of the options should be held until at least one year after the non-executive director leaves the board. Holding of share options could be relevant to the determination of a non-executive director's independence (as set out in provision A.3.1).

B.1.4 Where a company releases an executive director to serve as a non-executive director elsewhere, the remuneration report should include a statement as to whether or not the director will retain such earnings and, if so, what the remuneration is.

[5] In some banks some incentives were too "keen".

Service Contracts and Compensation

B.1.5 The remuneration committee should carefully consider what compensation commitments (including pension ~~contributions~~[6] and all other elements) their directors' terms of appointment would entail in the event of early termination. The aim should be to avoid rewarding poor performance. They should take a robust line on reducing compensation to reflect departing directors' obligations to mitigate loss.

B.1.6 Notice or contract periods should be set at one year or less. If it is necessary to offer longer notice or contract periods to new directors recruited from outside, such periods should reduce to one year or less after the initial period.

B.2 Procedure

Main Principle

There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.

Supporting Principles

The remuneration committee should consult the chairman and/or chief executive about their proposals relating to the remuneration of other executive directors.

The remuneration committee should also be responsible for appointing any consultants in respect of executive director remuneration. Where executive directors or senior management are involved in advising or supporting the remuneration committee, care should be taken to recognise and avoid conflicts of interest.

The chairman of the board should ensure that the company maintains contact as required with its principal shareholders about remuneration in the same way as for other matters. The Remuneration Report should be clear, transparent and readily understandable by shareholders. Schedule D contains additional good practice provisions for remuneration disclosure.

Code Provisions

B.2.1 The board should establish a remuneration committee of at least three, or in the case of smaller companies, two, members, who should all be independent non-executive directors. The remuneration committee shall have access to adequate resources to fulfil its remit. In addition, the company chairman may also be a member of, but not chair, the committee if he or she was considered independent on appointment as chairman. The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board. Where remuneration consultants are appointed, a statement should be made available of whether they have any other connection with the company.

B.2.2 The remuneration committee should have delegated responsibility for setting remuneration for all executive directors, company secretary and the chairman, including pension rights and any compensation payments. The committee should also recommend and monitor the level and structure of remuneration for senior management. The definition of 'senior management' for this purpose should be determined by the board but should normally include the first layer of management below board level.

[6] This drafting fails to consider defined benefit pension. We do not think this was the intent and recommend the drafting is tidied up in this respect.

B.2.3 The board itself or, where required by the Articles of Association, the shareholders should determine the remuneration of the non-executive directors within the limits set in the Articles of Association. Where permitted by the Articles, the board may, however, delegate this responsibility to a committee, which might include the chief executive.

B.2.4 Shareholders should be invited specifically to approve all new long-term incentive schemes (as defined in the Listing Rules) and significant changes to existing schemes, save in the circumstances permitted by the Listing Rules.

B.2.5 The remuneration committee should ensure that it has access to independent expert advice, when and where necessary.

B.2.6 Remuneration Consultants who are appointed by the remuneration committee should agree to follow the Code of Ethics for Remuneration Consultants in Schedule E.

RECOMMENDATION 3

SCHEDULE E Code of Ethics for Remuneration Consultants

CODE OF ETHICS

FOR UK REMUNERATION CONSULTANTS

Application Any remuneration consultant who is appointed by or on behalf of the remuneration committee of a UK listed company (Remuneration Consultant).

Scope The Code applies at all times to Members' conduct in their work as Remuneration Consultants, but will also be taken into consideration where conduct in other contexts could legitimately be considered to reflect on the profession of remuneration consulting.

Status The Code will be taken into account where a Member's conduct is called into question.

Purpose The Code contains principles which Remuneration Consultants are expected to observe in the public interest in order to build and promote confidence in the work of Remuneration Consultants.

Definition: Member means any Remuneration Consultant, either an individual or a firm, who agrees to follow the Code.

THE PRINCIPLES OF THE CODE

1. Integrity: Members will act honestly and with the highest standards of integrity.

1.1 Members will show respect for others in the way they conduct themselves in their professional lives.
1.2 Members will respect confidentiality except in the exceptional circumstances that disclosure is required to comply with the law or the enforceable requirement of a regulatory body.
1.3 Members will be honest, open and truthful in promoting their business services

2. Competence and Care: Members will perform their professional duties competently and with due care and attention.

2.1 Members will not act unless they have an appropriate level of relevant knowledge and skill.
2.2 Members will take care that the advice and services they deliver are appropriate to the instructions and needs of the client, having due regard to those parties (such as shareholders, bond and loan holders or analogous persons) whose interests may be affected by the work of the Member.
2.3 Members will agree with the client in writing the scope and nature of any appointment or instruction.
2.4 Members will agree with the client in writing the basis of their remuneration before commencing an appointment or instruction and before any material change in the scope of an existing appointment or instruction is acted upon.
2.5 In giving advice to a client, due regard shall be had to the client's risk appetite and risk map, the expressed views of the client's shareholders and general levels of remuneration and increases in salary across the client's workforce.
2.6 Members will keep their competence up to date.

3. Impartiality: Members will not allow bias, conflict of interest, or the undue influence of others to override their professional judgment.

Definition: A conflict of interest arises if a Member's duty to act in the best interests of any client conflicts with:
a) the Member's own interests, or
b) the interests of the Member's firm, or
c) the interests of other clients.

3.1 Members will ensure that their ability to provide objective advice to their clients is not, and cannot reasonably be seen to be, compromised.

3.2 Members will disqualify themselves from acting where there is a conflict of interest that cannot be reconciled. In particular, the Member will decline to act where the Member's firm acts also as the client's auditor or as search consultant on behalf of its nomination committee.
3.3 Members will fully document the steps they have taken to reconcile a conflict and agree them with all clients who are affected by the conflict whenever such agreement is necessary for them to be effective.
3.4 Before accepting any assignment, Members will consider carefully whether they should consult with any Member who previously advised the client, with a view to ascertaining whether there might be any professional reason ['professional reason' is too vague; 'reason of conflicting interests' might be better]why the assignment should be declined.
3.5 Members will ensure, before commencing work on a contingency fee basis, that:
a) they can comply with paragraphs 3.1 and 3.4 and
b) the client understands and agrees a contingency fee arrangement and either this basis of charging is not unusual for the work in question or the client has particularly requested a contingent basis of remuneration.
3.6 Members will disclose promptly to their clients any relevant interest, including income, which they or their firm have. Members will take reasonable steps to ensure that they themselves are aware of any such interests.

4. Compliance: Members will comply with all relevant legal, regulatory and professional requirements, take reasonable steps to ensure they are not placed in a position where they are unable to comply and challenge noncompliance by others.

4.1 Members will notify their clients, or their employers, or both, if they believe, or reasonably ought to believe, that a proposal or course of action is or may be unlawful, unethical or improper.
4.2 Members will fulfill any obligations to report information to relevant regulatory authorities.
4.3 Members will promptly report any matter which appears to constitute misconduct or a breach of any relevant legal, regulatory or professional requirements. To the extent that the consent of a third party is required for this purpose in order to disclose information, Members must take all reasonable steps to obtain such consent.

5. Openness: Members will communicate clearly and completely and meet all applicable reporting standards.

5.1 Members will ensure that their communication, whether written or oral, is clear and comprehensive, indicating how any further explanation can be obtained, and that their method of communication is appropriate, having regard to:
a) the intended audience;
b) the purpose of the communication;
c) the significance of the communication to its intended audience; and
d) the capacity in which the Member is acting.
5.2 Members will take such steps as are sufficient and available to them to ensure that any communication with which they are associated is accurate and not misleading and contains sufficient information to enable its subject matter to be put in a proper context.

6. Complaints: Any complaint by a client shall be referred to the managing partner or chairman, or similar person, of the firm who shall use his best endeavours on behalf of the Member's firm to resolve the complaint with all reasonable dispatch to the reasonable satisfaction of the client.

Annexe to the code of ethics – this illustrates the operation of the principles in practice.

Qualifiying the nature of advice
Advice can be provided at a number of levels. The consultant should make it clear at the outset at what level the service is being provided
(a) Raw (uninterpreted) market data and practice information- it is unlikely that any consultants appointed by the remuneration committee would be providing this, but the survey departments of the bigger firms do
(b) Interpreted market data and practice information - data which the consultant has selected to be relevant to particular roles and to the client company
(c) Advice about the context and options for future remuneration policy
(d) Recommendations for future policy

Market data (Levels (b) to (d) above)
Rational basis for selection of comparison data
Relevance of comparison data to the remuneration of a particular executive explained
Openness with the client about the sources and limitations of data provided - sample sizes, data aging; degree of approximation
Making the client aware of the other factors that should be considered before applying market data
Avoiding the ratchet - stressing the difference between comparing pay levels and comparing pay rises
Advising clients that total cash and total remuneration comparisons should be viewed in the context of company performance comparisons

Evaluation of remuneration plans (Levels (c) and (d))
Providing the client with a full understanding of the financial implications of remuneration plans
Openness about the limitations of the valuation methodology used
Clarity about the assumptions used, eg discount rates, volatility, growth

Relating advice to strategy (Levels (c) and (d)
Insisting on a proper understanding of the business, business strategy and intended management culture/reward philosophy before providing advice or recommendations.
Taking a long-term company success perspective

Dealing with conflicts of interest within the board
Clarity about the personal client - ie who to take instructions from (normally the chairman of the remuneration committee)
Nevertheless, providing advice from the perspective of the interest of the company as a whole
Without compromising the requirement to provide this objective advice, act in a way that generally promotes harmony in the board
Having the courage to say explicity when their objectivity is being compromise
Not providing advice to any executive (or their subordinate) about the competitiveness or design of their own remuneration package, without the explicit involvement and agreement of that executive's superior manager, and/or the remuneration committee (where relevant)

Draft 22 May 2009 prepared by MM & K Limited

RECOMMENDATION 4

SCHEDULE D to the Combined Code – Examples of Best Practice and Explanatory Notes

D.1 Recommended Total Remuneration disclosure

This would be best done by the disclosure of both the total remuneration awarded in the year and the total actually realised in the year.

Total remuneration **awarded** is the sum of salary, bonus, benefits, the increase in the transfer value of accrued pension and the expected value of share plans and share options and any other long term incentive arrangement.

Total remuneration '**realised**' is the same as that awarded except for all long term incentives and share options, the amount of money made, or lost, in the latest year is included, i.e. the amount in £s of LTIP that vests in the year and for options amount of any gain on options exercised in the year. (An alternative that is more complex but could be considered is the increase in the appreciation in potential realisable performance shares and option gains over the year, including both vested and unvested options).

The figure for realised gains would be added to the other remuneration received to get the total remuneration realised:

Example of Best Practice:

	Total Awarded £000	Total Realised £000
Salary	1,100	1,100
Benefits	81	81
Pension: Defined Benefits -Transfer Value of increase; plus Defined Contribution Employer Contribution plus pension cash allowances	990	990
sub total fixed	2,171	2,171
Cash Bonus Paid	516	516
Deferred bonus Expected Value	223	
Options awarded Expected Value	7,800	
Performance shares awarded Expected Value	880	
Value of Deferred Bonus shares that vested in year		100
Value of other shares vested in year		500
Gain on options exercised in the year		5,000
Sub total variable	9,419	6,116
Total Remuneration This Year	**11,590**	**8,287**
Total Remuneration Last Year	**9,590**	**6,287**

The simplest way to do this would be to change the total emoluments disclosure in the DRRR so that it also had to show the pension TV and the long term incentives awarded and realised and the total remuneration awarded and realised. i.e.

Current	Proposed
Salary	Salary
Benefits	Benefits
Bonus	Bonus
	Pension: Defined Benefits =Transfer Value of increase; plus Defined Contribution Employer Contribution; plus pension cash allowances
	Long term incentives awarded
Total Emoluments this year	Total Remuneration awarded this year
Total Emoluments previous year	Total Remuneration awarded last year
	Long term incentives realised
	Total Remuneration realised this year
	Total Remuneration realised last year

For options, this requires an estimate of the future value of the performance related elements of remuneration. This should be calculated on a recognised basis such as the Black-Scholes method for options: The assumptions used should be stated, e.g. for Black-Scholes the volatility, dividends, risk free rate, term of the option and risk of forfeiture.

For performance shares[7] we recommend the disclosure should include the estimated value of the award, i.e. at the date of grant. Where complex performance conditions apply to awards the Company should provide an estimate of the probability of payment and the estimated value of the payment. Where performance shares are based on relative performance, guideline of performance assumptions should be:

median TSR of 8% p.a. (e.g. risk free rate of 3% plus equity risk premium of 5% and Beta of 1);

upper quartile 18% (i.e. 10 percentage points p.a. above median); and

upper decile 28% (i.e. 20 percentage point p.a. above median).

Companies should be free to choose other assumptions, but be required to justify them.

[7] Performance shares in this context means a restricted share plan where awards of shares are made contingent on continuous service and performance conditions. Typically performance conditions are TSR versus a comparator group of companies or index eg FTSE100.

RECOMMENDATION D.2

Chief Executive 5 YEAR DISCLOSURE

The 5 year TSR graph is a great step forward. But companies seem to have missed the point that it is meant to demonstrate the linkage between pay and performance.

Therefore we recommend the following disclosure for the chief executive:

	2004	2005	2006	2007	2008
TSR of company	100	80	70	75	85
TSR of relevant index	100	75	67	75	89
Companies would be free to include other measures such as turnover, profits, profit margin, EPS, dividends, ROCE, Cash Flow, assets, market cap, debt, debt/EBITDA, etc					
Chief executive Total Remuneration Awarded £ million	*2.5*	*1.0*	*5.4*	*3.2*	*3.0*
" indexed to 100 in 2004	100	40	216	128	120
Chief executive Total Remuneration Realised £ million	*2.1*	*5.5*	*10.8*	*4.6*	*4.2*
" indexed to 100 in 2004	100	262	514	219	200

Companies could be given the option to put this information in a graph, with the total remuneration £s amounts underneath the graph or as data labels.

Best practice will soon emerge to show the total remuneration awarded and realised, for at least the chief executive, for the past 5 years, together with an explanation of changes in total remuneration and the linkage to performance in terms of TSR and possibly other performance measures and key performance indicators.

It is unnecessary to require the disclosure of others than the chief executive(and/or the highest paid director) as this will add volume without clarity. If the pay of the chief executive is right, then the pay of the other directors is usually right too. If there is a problem, then the other disclosures will give the necessary information to identify this.

RECOMMENDATION D.3

Disclosure of chief executive Total Remuneration and Average Employee Pay

This should also be done a 5 year period so the trend can be easily seen. We suggest the following rows are added to the table in Recommendation 3

	2004	2005	2006	2007	2008
Total Number of Employees	4,570	4,703	4,419	5,293	5,041
Total Employee Emoluments £m	£119m	£128m	£136m	£136m	£156m
Average Employee Emoluments £	£25,955	£27,254	£30,842	£25,677	£30,994
Ratio of Chief Executive to average employee	119	121	107	151	128
CEO total remuneration £	£3,087,028	£3,304,533	£3,308,814	£3,876,921	£3,957,612

RECOMMENDATION D.4

We would recommend that the relative importance of those elements which are and are not related to performance should be shown as the % of pay that is performance related, e.g.

Name	% of awarded total remuneration that is performance related	% of realised total remuneration that is performance related
Chief Executive	60%	60%
Dir 2	50%	50%
Dir 3	60%	60%
Dir 4	55%	55%
Dir 5	30%	30%

We note that this requires an estimate of the future value of the performance related elements of remuneration. This should be calculated on a recognised basis such as the Black-Scholes method for options: for bonus plans the payment for achieving budget may be appropriate. The assumptions used should be stated, e.g. for Black-Scholes the volatility, dividends, risk free rate, term of the option and risk of forfeiture.

For performance shares[8] we recommend the disclosure should include the estimated value of the award, i.e. at the date of grant. Where complex performance conditions apply to awards the Company should provide an estimate of the probability of payment and the estimated value of the payment. Where performance shares are based on relative performance there should be a guideline of performance assumptions should be:

median 8% (i.e. risk free rate of 5% plus equity risk premium of 3% and Beta of 1);

upper quartile 18% (i.e. 10% p.a. above median); and

upper decile 28% (i.e. 20% p.a. above median).

Companies should be free to choose other assumptions, but be required to justify them. Total Remuneration should include all elements of pay **including pensions.**

[8] Performance shares in this context means a restricted share plan where awards of shares are made contingent on continuous service and performance conditions. Typically performance conditions are TSR versus a comparator group of companies or index eg FTSE100.

RECOMMENDATION D.5

CONTRACTUAL TERMINATION PAYMENT DISCLOSURE

Note: Shareholders need to know the total remuneration of each director in order to evaluate if termination arrangements are appropriate.

We recommend that companies should have to state in the remuneration committee Report the potential termination payment payable to each executive director if he were to leave. The amount should be in £.

This data should be in addition to the current explanation required regarding contracts, which should explain the way the termination payment would be calculated.

Where payments are contingent (e.g. linked to the individual's performance), then a target level should be estimated.

For the avoidance of doubt, any payments from long term incentive and bonus plans that may be accelerated, or where performance conditions may be waived, would be included in the potential maximum termination payment.

Improvements in pension provision (not already reflected in the estimated transfer value of the accrued pension) would also be included in the maximum termination payment figure. If "custom and practice" had established a contractual commitment this would be reflected in the target figure.

Where payments are linked to share prices the payment should be estimated based on the year end share price.

Notes:

1. This approach would ensure there will be no surprises.
2. All remuneration committees should be aware of this information, so it should not be a burden.

Example of Recommended disclosure

Director	Salary	Contract notice length	Maximum termination payment	"Target" termination payment
Smith	£500,000	12 months	£1,250,000	£750,000
Jones etc				

RECOMMENDATION D.6

DISCLOSURE SHOULD BE FOR THE 5 HIGHEST PAID EXECUTIVES

We recommend the UK adopts this approach.

Note: In the US the 5 highest paid executives have to be disclosed.

RECOMMENDATION D.7

THE FEES PAID TO CONSULTANTS FOR ADVICE TO THE REMUNERATION COMMITTEE, AND THEIR FEES FOR OTHER SERVICES TO THE COMPANY SHOULD BE STATED FOR EACH CONSULTANT.

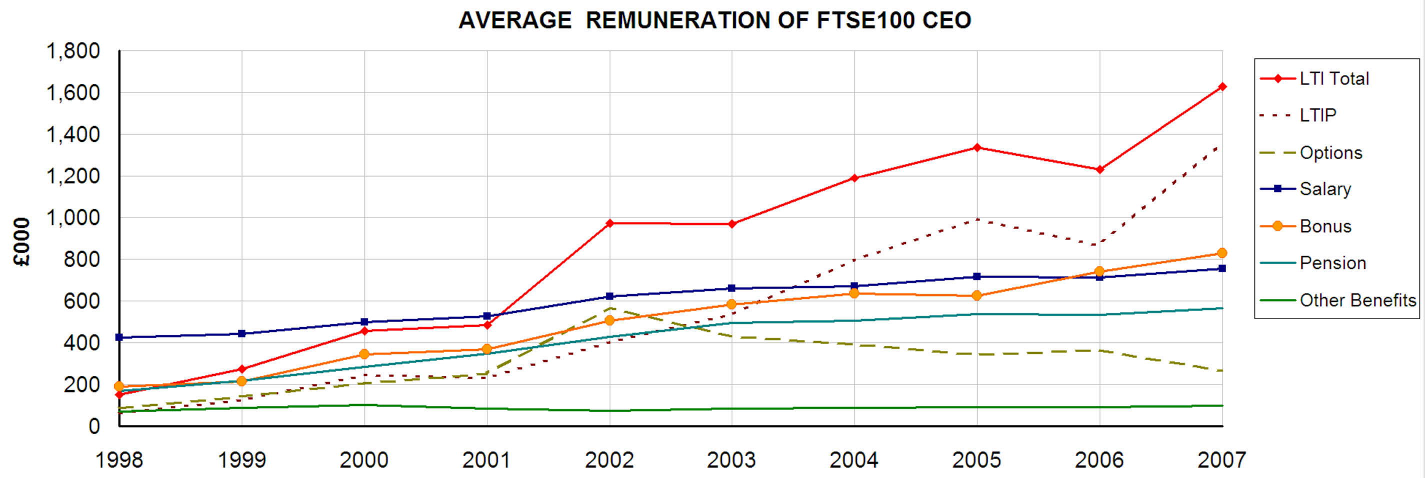
Example disclosure to meet this new requirement would be:

Fees for advice on executive remuneration

Consultant	Fees for advice on remuneration committee issues	Fees for other services to the Company and Company Pension Funds	Appointed by remuneration committee?
(1) Independent Remuneration Consultants Ltd	£25,000	N/a	Yes
(2) AAA Accountants	£100,000	£2,500,000	Yes
(3) BBB Actuaries & Pension Consultants	£150,000	£1,250,000	Yes
(4) CCC Lawyers	£20,000	£5,000,000	No
(5) DDD Generalist Firm	£2,000	£150,000	No

Trends in Salary and Total Remuneration

Long term incentives may now be more important than salaries. However, most companies still set their award policy as a % of salary. Page 28 shows the proportion of pay at risk varies widely between companies.
In the past 10 years, salaries have raced ahead of inflation and total remuneration has grown even faster. This has been driven by the economic necessity of paying competitive rewards to attract and retain executives. Many of our largest companies operate in a global economy, with a global market for talent.



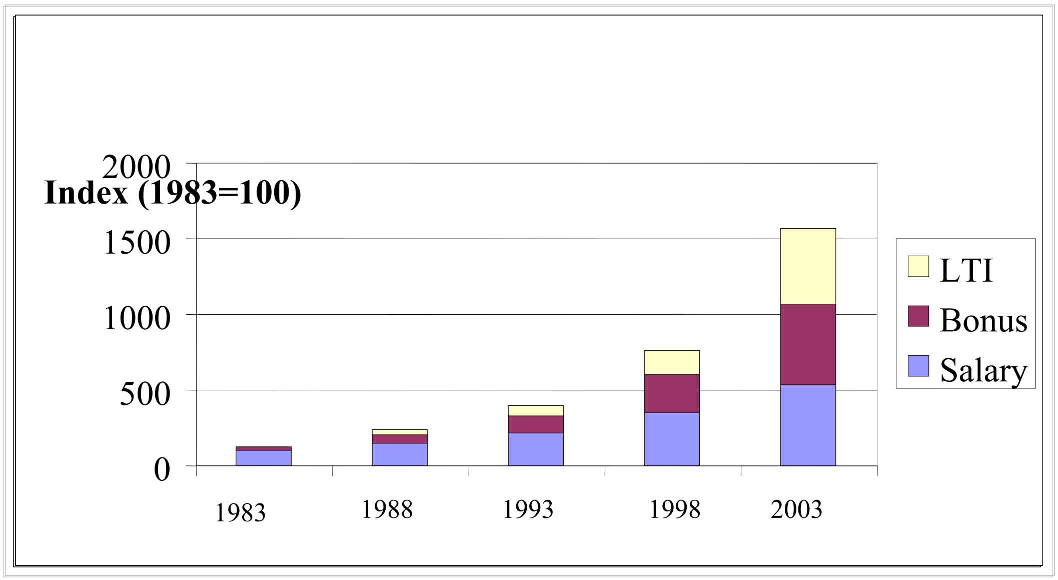
	Year	Salary	Bonus	Other Benefits	Options	LTIP	LTI Total	Total Remuneration exc. pension	Pension	Total Remuneration	Market Cap £bn	Turnover £bn	FTSE100
Amounts in £000	**1998**	425	188	70	88	62	150	832	170	1,002	10.3	5.8	6,200
	1999	444	214	87	145	128	273	1,018	217	1,235	10.3	5.7	6,600
	2000	499	345	103	209	246	455	1,402	285	1,687	14.1	6.8	5,700
	2001	525	369	83	252	231	483	1,459	347	1,806	12.7	8.1	5,200
	2002	620	504	75	568	405	973	2,172	427	2,600	9.3	8.1	3,700
	2003	659	581	84	433	535	968	2,292	494	2,786	10.4	8.7	4,400
	2004	672	635	87	393	796	1,190	2,583	504	3,087	11.7	8.8	4,740
	2005	716	623	91	343	994	1,337	2,767	537	3,305	12.2	9.5	5,950
	2006	711	740	91	366	867	1,233	2,775	534	3,309	15.1	11.2	6,221
	2007	755	828	99	267	1,360	1,627	3,310	566	3,877	14.1	8.8	6,457
	2008												4434.2
% Increases	**1999**	4%	14%	25%	66%	105%	82%	22%	28%	23%	-1%	-2%	6%
	2000	13%	61%	19%	44%	93%	67%	38%	31%	37%	38%	20%	-14%
	2001	5%	7%	-20%	21%	-6%	6%	4%	22%	7%	-10%	19%	-9%
	2002	18%	37%	-9%	125%	76%	102%	49%	23%	44%	-26%	0%	-29%
	2003	6%	15%	12%	-24%	32%	0%	6%	16%	7%	11%	8%	19%
	2004	2%	9%	3%	-9%	49%	23%	13%	2%	11%	13%	1%	8%
	2005	7%	-2%	5%	-13%	25%	12%	7%	7%	7%	4%	8%	26%
	2006	-1%	19%	0%	7%	-13%	-8%	0%	-1%	0%	24%	18%	5%
	2007	6%	12%	10%	-27%	57%	32%	19%	6%	17%	-7%	-22%	4%
	cumulative 98- 07	78%	341%	43%	204%	2087%	985%	298%	233%	287%	36%	52%	15%
	average p.a. 98-07	7%	18%	4%	13%	41%	30%	17%	14%	16%	4%	5%	1.6%

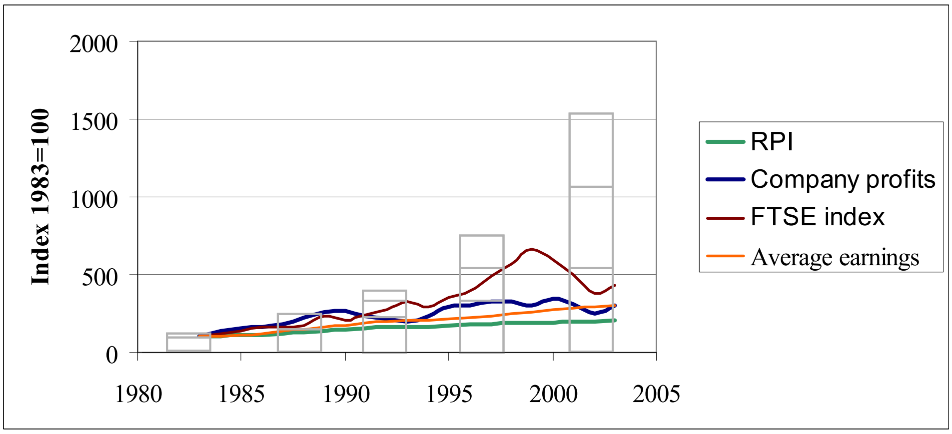
Pre 2002 data includes new hires and internal promotions. 2002 and later excludes these, so may not be directly comparable.

The Executive Director Total Remuneration Survey
Sep 2008

MM&K, in association with Manifest
Page 26

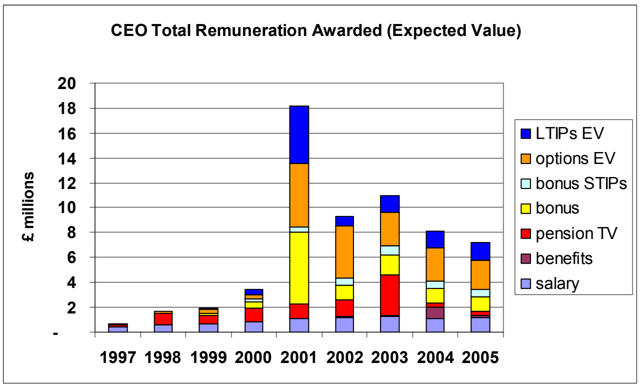
Appendix 2 - Chief Executive Earnings, 20 year history versus FTSE 100 and average earnings





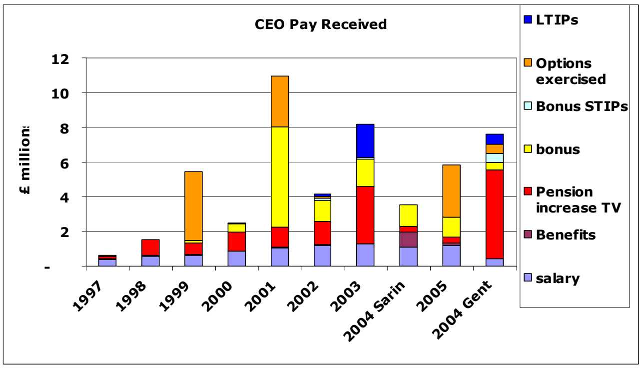
Appendix 3 - Chief Executive Pay Simplified ("clear, transparent and readily understandable") - An example using Vodafone data up to 31st March 2005.

The estimated value of awards made by the remuneration committee in each year since 1997:



Notes: Arun Sarun appointed as chief executive in 2004, Sir Christopher Gent was chief executive prior to 2004 Mannesmann acquisition in 2001.

The actual amount of hard cash received, plus gains on options exercised and performance shares and STIPs vesting in the year, plus the increase in the transfer value of accrued pension/DC contributions.

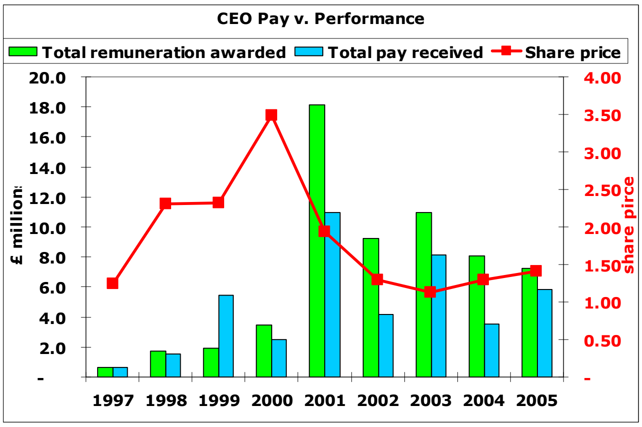


Wealth Accumulated to date (£ million)

Pension TV of accrued benefit	0.7
Shares owned	8.2
Options - unexercised gains	3.1
Subtotal	**12.0**
performance shares unvested (max)	5.4
STIPs unvested (max)	1.4
"Total" (max)	**18.8**

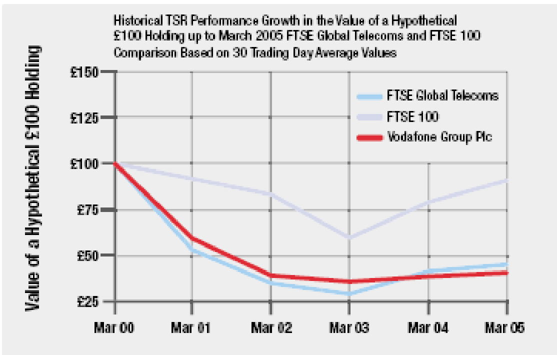
Performance shares and STIPs are unlikely to pay out at the maximum. However, the remuneration report [may] give a projection of the estimated payout on the basis of performance to date.

The link of pay awarded and realised to performance is shown in the next two graphs.

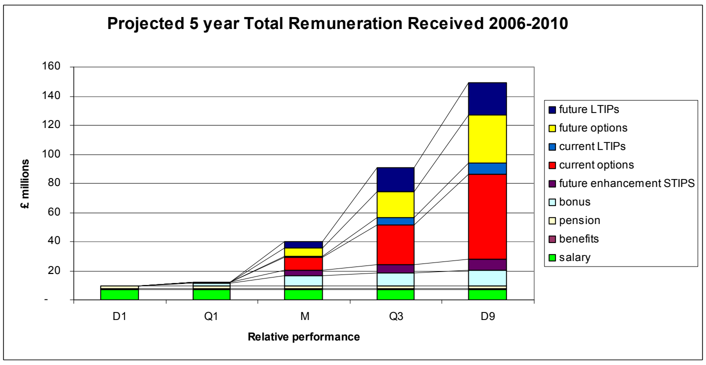


[Companies may wish to include a history of other relevant measures here]

Performance Perspective



Future Potential earnings in next 5 years:



Assumes salary increases at 5% p.a., bonus payout at max for D9, 50% of target at median and nil at D1, standard assumptions re share price growth, TSR and vesting of performance conditions.

Appendix 4 - About MM&K

MM & K is a leading independent consultancy specialising in the planning, design and implementation of pay and reward strategies.

Founded in 1973, MM & K focuses on directors and senior executive remuneration, but we have added other services to support our clients' needs through the acquisitions of Independent Remuneration Solutions and The Share Option Centre and the launch of higher talent, our specialist recruiter of HR professionals. MM & K is owned by its employees and directors.

Our consultants' expertise areas include HR, share schemes, law, accountancy, tax, corporate governance, business management and statistics. Our multi-disciplinary approach to remuneration is always tailored to individual client requirements.

Who We Are

Paul Norris, Chief Executive

Masters graduate in Law and Barrister. Paul started his career with MWP Incentives Limited, and then spent a period in merchant banking before joining the buy-in team that created MM & K in 1985. He advises a number of remuneration committees on business-linked remuneration strategies and is experienced in the design and implementation of cash and share based incentive plans.

Nigel Mills, Director

PPE graduate and chartered accountant. Nigel joined MM & K in 1985 having spent 6 years at Price Waterhouse after graduating from Oxford. He is an authority on executive and all employee cash and equity based incentive schemes for public and private companies. He also leads the Private Equity business of MM & K and is an expert on carried interest and co-investment plans for Private Equity houses.

Cliff Weight, Director

Graduate in Mathematics and Statistics from Cambridge. Cliff has over 20 years' experience as a remuneration consultant. He was a Director of Independent Remuneration Solutions, who merged with MM & K in November 2006. He specialises in advising companies on executive directors' remuneration, annual and long term incentives and non-executive directors' fees. He is a regular speaker at conferences and is co-author of Tottel's Corporate Governance Handbook.

David Henderson, Non Executive Director

David has been Chairman of Kleinwort Benson Private Banking since November 2004. David began his career specialising in personal tax and UK trusts. He subsequently spent ten years (1974-1984) as a banker at Morgan Grenfell and, following that, eleven years in financial services executive recruitment with Russell Reynolds Associates before joining the Board of Kleinwort Benson Group plc as Personnel Director in 1995. He was appointed Chief Executive of its private banking business in June 1997. David is also a non-executive director of Novae Group Plc, Price Forbes & Partners Ltd and Camp Hopson & Co.

Allan Johnston, Non Executive Director

MA and Chartered Fellow of CIPD. Allan was an Executive Director of Corus Group plc with responsibility for HR and some of the devolved businesses of the company until he retired from them in 2005. He is Chairman of UK Steel Enterprise Limited and Chairman of the Trustees of the £9.8Bn British Steel Pension Scheme. He is a Councillor of the City and Guilds of London Institute. Specialist in all areas of HR with particular expertise in change management.

Damien Knight, Principal

Physics graduate. After a period in construction management, Damien has followed a career in human resources and remuneration consulting, spanning 30 years. Damien was a director of the Hay group where he worked for over 20 years and most recently Damien was Senior Consultant with Watson Wyatt. For the past 15 years he has specialised in executive remuneration and has advised the remuneration committees and management of a wide range of companies in the UK and elsewhere in Europe, including several FTSE 100 and other major corporations.