18 December 2013

Our ref: ICAEW Rep 177/13

Catherine Woods
Financial Reporting Council
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By email: remcon@frc.org.uk

Dear Ms Woods

Directors' Remuneration

ICAEW is pleased to respond to your request for comments on *Directors' Remuneration*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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ICAEW REPRESENTATION

DIRECTORS' REMUNERATION

Memorandum of comment submitted in December 2013 by ICAEW, in response to the Financial Reporting Council consultation document Directors' Remuneration published in October 2013

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation document *Directors' Remuneration* published by the Financial Reporting Council on 2 October 2013, a copy of which is available from this link.

WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

4. This response reflects consultation with the ICAEW Corporate Governance Committee which includes representatives from the business and investment communities. The Committee is responsible for ICAEW policy on corporate governance issues and related submissions to regulators and other external bodies.

MAJOR POINTS

5. In our view the UK Corporate Governance Code is not the right place to deal with specific requirements on directors' remuneration. The Code sets out a principles-based corporate governance framework. It has never been intended to repeat or mirror law and regulation. Changes to the Code therefore should take place only when this is to change the scope or substance of the corporate governance framework. An increasing number of specific requirements could irrevocably damage the balance and overall integrity of the Code.

6. Furthermore, the Code is primarily implemented on the comply-or-explain basis while legislation requires full compliance. We do not believe that the Code is the right tool to supplement legislative requirements. In fact, we consider that provisions within the Code may be removed once they are incorporated into legislation. The Government may issue helpful guidance material but that should be supplementary to regulations.

7. Remuneration-related debate has been attracting public attention over recent years. The Government has already introduced new requirements related to voting on remuneration policies and disclosure. We also recognise continued political pressures for the Secretary of State to propose changes to the Code.

8. However, new legislation and the practice it intends to encourage need time to become embedded. For example, the new requirement on shareholder voting on forward-looking remuneration policies could affect remuneration policies significantly when used in conjunction with other shareholder rights such as annual votes on directors. Introducing new requirements without seeing the effect that legislation has in practice undermines the value of legislation as well as leading to duplication.

RESPONSES TO SPECIFIC QUESTIONS/POINTS

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?

9. We are aware that many in the investor community are generally supportive of greater use of clawback provisions. We think that companies should take account of these views when considering such provisions in accordance with Schedule A of the Code. Therefore, we do not support inclusion in the Code of specific or detailed provisions on clawback. Good practice should develop by way of increased engagement between investors and companies. Specific clawback policies are for the board to develop and set out for shareholders to vote on.

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

10. No. The wording does not need to be mirrored in the Code which should remain as principles-based as possible. However, for the purpose of implementation, we found the Regulations useful in that it differentiates between the recovery of sums paid and the withholding of the payment of any sum.

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

11. No. Please see paragraph 9.

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

12. Yes. We anticipate that there would be both legal and practical difficulties in recovering sums that have already been paid.

Remuneration Committee Membership

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

13. No. We are unconvinced by the logic that remuneration committee members who are executives in other large companies are invariably conflicted as they 'have a personal interest in maintaining the status quo in pay setting culture and pay levels.'

14. The Manifest analysis of shareholder votes against FTSE 350 remuneration reports based on which remuneration committees include FTSE All Share Index executive directors ('ENEDs') does not indicate any apparent link between shareholder dissent and the presence of ENEDs. In any case, the same analysis indicates that the number of companies with ENEDs is in decline. As shareholders can vote on NED appointments as well as remuneration reports, we do not support any changes to the Code.

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?

15. No. In general we do not believe that explicit requirements to deal with a company's failure to obtain a substantial majority in support of a resolution need to go into the Code. Therefore, while we support companies commenting publicly on such resolutions in respect of remuneration, we do not think that this should be covered by a Code provision.

16. Determination of what constitutes a substantial majority is a matter of judgement and the 80 per cent threshold suggested in the consultation appears arbitrary. If any reference point at all were needed, we think that this should be 75% because it is used as a threshold for a special resolution. However, disclosure of remuneration resolutions and related disputes can be complex and so one time limit is unlikely to be applicable in all cases. Therefore we do not believe that a threshold should be included in the Code.

If yes, should the Code:

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

17. Please see our response to the previous question.

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

18. Yes. However, the difficulties will depend on individual company circumstances and therefore is inappropriate for the Code to specify how these should be addressed.

Other Possible Changes

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

19. Yes, the Code is compatible with the Regulations. We generally support the idea of removing any overlapping provisions in the Code. However, with regards to these particular Regulations, we have not identified any specific provisions that should be removed.

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

20. Yes, the Code may address these three broad areas though only at a principles-based level. The FRC should rightly keep the Code under a regular review to consider any need for its revision in the light of developments in market place.

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