Executive Reward Briefing, 11 June 2018

FIT Remuneration Consultants

Pay ratios rules published

As was reported across media outlets on Sunday 10 June, on Monday 11 June 2018 the Business Secretary, Greg Clark, has brought forward secondary legislation to make a number of amendments on company reporting, including amendments to the reporting regulations for Directors' Remuneration Reports ("DRR Regs"). The new rules for DRRs will be in effect for financial years beginning on or after 1 January 2019, and so will impact the majority of DRRs published in 2020.

There are 3 changes on DRR reporting, the main items of which have previously been "flagged" in consultations.

CEO to employee pay ratio

UK listed companies subject to the DRR Regs (main list companies) with more than 250 UK employees will be required to prepare and publish in their DRRs ratios of CEO pay to three employee pay data points:

- Lower quartile UK employee
- Median UK employee
- Upper quartile UK employee

The comparison is to be made between the CEO's Single Figure Table total and employees' pay and benefits: there are detailed provisions as to how a company may calculate the employee pay and benefits, including applying the same rules as for the Single Figure to all employees, or identifying the upper quartile, median and lower quartile positions from the gender pay gap data set, and calculating the employee pay and benefits for these three cases. The actual £ sterling figures for the employee data points must be disclosed as a total figure, and also separately for the base salary element within the totals.

The ratio comparison must be carried out each year until a full 10-year picture is presented in a table. Each year a level of commentary to the table is required including:

- Explaining increases in the ratios year-to-year, and
- How the ratio at median relates to pay, reward and progression practices for employees

Impact of Share Price on Executive Directors' pay

Two new disclosures are proposed:

- Within the notes to the Single Figure Table, where any disclosed amounts in the table for either annual incentives or LTIs relates to share price appreciation, the proportion of the total that was related to share price appreciation must be disclosed
- Within the scenario charts that show minimum, "on-target" and max pay potentials for EDs' packages, a new column must be added showing the max scenario plus a 50% share price increase over (in effect) 3 years

Discretions

Whilst there is an existing obligation in the DRR Regs to disclose any exercises of discretion on remuneration outcomes by the Remuneration Committee (as part of the <u>auditable</u> Single Figure Table notes), the exercise of such discretion will additionally need to be disclosed as an item in the introductory Annual Statement to the DRR by the Remuneration Committee Chairman.

What happens next?

The FRC's final version of the revised UK Corporate Governance Code is expected later this month. This will include the following additional items which were part of the Government's review of Ggovernance in 2017 and which are relevant for remuneration:

- Board engagement with the workforce and gathering their views. (Note: the 11 June legislation extends existing obligations in the main Annual Report to report on employee involvement to also say how the directors engaged with employees in the year)
- Diversity within the succession pipeline
- Remit of Remuneration Committee to include setting senior management pay and oversight of workforce policies
- Alignment of pensions with the workforce

For completeness, the 11 June 2018 legislation also contains new obligations for the largest unquoted companies to provide information regarding their corporate governance on their websites.

We will provide more updates as we receive further information this month, including with regards to the revised UK Corporate Governance Code.

If you wish to discuss anything arising from this briefing, please ask your usual contact at FIT or call us on 020 7034 1111 or email us at Info@fit-rem.com.

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