SLAUGHTER AND MAY/

NEWSLETTER

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INCENTIVES BULLETIN

Financial Reporting Council Review of Corporate Governance Reporting

Federated Hermes letter to FTSE 100 companies

Glass Lewis 2021 UK Proxy Paper Guidelines

QCA Remuneration Committee Guide

What key dates and developments in incentives should be on your radar?

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Welcome to the December edition of our Incentives Bulletin, updating you on the latest developments in executive remuneration and share plans. In this Bulletin, we look at the Financial Reporting Council's review of corporate governance reporting, Federated Hermes' recent letter to FTSE 100 companies, the Glass Lewis 2021 UK Proxy Paper Guidelines and the QCA Remuneration Committee Guide for smaller and mid-sized quoted companies.

FINANCIAL REPORTING COUNCIL REVIEW OF CORPORATE GOVERNANCE REPORTING

The Financial Reporting Council ("FRC") has published its review on how UK premium-listed companies have reported on the application of the 2018 UK Corporate Governance Code (the "Code") and its expectations for the future application of the Code.

Overall, the FRC found a mixed picture on remuneration, with improvements in reporting on workforce pay, the use of Remuneration Committee discretion and the determination of executive directors' remuneration policy and practices, but disappointing conclusions regarding the disclosure of performance conditions, the alignment of executive and workforce pension contributions and workforce engagement. The FRC also noted that shareholder engagement on remuneration issues among companies which experience shareholder opposition in this area is often unsatisfactory.

As a result of its review, the FRC expects improved reporting on both (i) the impact of companies' engagement with their shareholders on the development of new directors' remuneration policies and (ii) how the views on executive pay of, and the remuneration of, a company's wider workforce have affected the terms of that company's directors' remuneration policy.

We anticipate that, particularly given the impact of the coronavirus pandemic, there will be in the 2021 AGM season increased focus on (i) executive pension contributions in excess of the level offered to the wider workforce; (ii) the operation of any discretion in respect of any directors treated as "good leavers"; (iii) meaningful engagement on executive to wider workforce pay ratios; and (iv) the non-disclosure of bonus targets.

FEDERATED HERMES LETTER TO FTSE 100 COMPANIES

In a letter to FTSE 100 companies, fund manager and corporate governance adviser Federated Hermes voiced its increasing concern about performance-based executive remuneration arrangements which do not serve long-term investors' interests and which do not align with companies' core long-term objectives, particularly in the context of the coronavirus pandemic.

The letter observes that 2020 has highlighted the limitations of performance-based incentive schemes, in particular that share price volatility and the ongoing uncertainty generated by the pandemic renders it difficult for companies to set meaningful performance targets and creates the possibility of windfall gains for executives participating in share-based incentive schemes.

Federated Hermes expects boards to use their judgment to ensure that executive pay can be justified in the context of the experience of other stakeholders, particularly where companies have made use of Government support (including the Coronavirus Job Retention Scheme), have made redundancies or are otherwise in distress. It continues to make the case for switching to simpler pay schemes aligned to long term success and the desired culture in the organisation, based on fixed pay and long-term time-restricted stock, with an emphasis on long-term share ownership for executives.

The letter also sets out Federated Hermes' 2021 voting policy guidelines, which include increased minimum shareholding requirements for executives, restrictions on variable pay as a multiple of fixed pay and the alignment of performance metrics to the company's corporate strategy.

Federated Homes' letter reinforces the expectations of institutional shareholders already expressed by the Investment Association and other bodies that any "discretionary payments" made in respect of the 2020 pay round to management (either through annual bonuses or through the performance underpins applicable to any long-term incentive awards) should take into account company performance.

GLASS LEWIS 2021 UK PROXY PAPER GUIDELINES

Glass Lewis has published its UK 2021 Proxy Paper Guidelines the "Guidelines"). The remuneration aspects of the Guidelines focus on the relationship between executive remuneration and pay levels among the wider workforce. In particular, Glass Lewis expects forward-looking decisions on executive remuneration to take into account the experience of shareholders and employees, and it may recommend that shareholders vote against remuneration policies where increases in executive remuneration substantially outpace employee salary increases. The Guidelines are further evidence of the heightened level of scrutiny on executive remuneration that we expect to see in the 2021 AGM season.

QCA REMUNERATION COMMITTEE GUIDE

The Quoted Company Alliance (the "QCA") has this month published an updated version of its Remuneration Committee Guide (the "Guide") for smaller and mid-sized quoted companies. The Guide contains five main sections covering:

(1) the effectiveness of the Remuneration Committee, including consideration of the objectives and responsibilities of a Remuneration Committee and how to evaluate the Remuneration Committee's effectiveness;

(2) the practical aspects of running a Remuneration Committee, including its composition, terms of reference, appointment of new members and use of third party advice;

(3) the factors to consider in setting a remuneration policy, including the different types of remuneration and examples of key performance indicators;

(4) relevant remuneration reporting obligations, including both the relevant legal framework and recommendations for any voluntary disclosures; and

(5) communicating with shareholders.

The Guide highlights in particular that there is no "one size fits all" approach for a company's remuneration policy. It reinforces the principle of a "say on pay" from the QCA's Corporate Governance Code and, for the first time, includes a recommendation that new share schemes and long-term incentive plans are put to a shareholder vote. The revised Guide represents a useful resource regarding best practice for the Remuneration Committees for smaller listed companies, in particular those on the London Stock Exchange's junior markets, such as AIM, for which full compliance with the UK Corporate Governance Code is not (commercially or administratively) practical.

WHAT KEY DATES AND DEVELOPMENTS IN INCENTIVES SHOULD BE ON YOUR RADAR?

31 December 2020	Transitional arrangements under UK-EU withdrawal agreement expected to end unless extended
29 January 2021	End of consultation period for European Banking Authority consultation on revisions to its 2015 guidelines on sound remuneration policies (including amendments introduced by CRD V)
6 April 2021	Off-payroll working rules (IR35) come into force for the private sector

Best wishes from the Slaughter and May Employment and Incentives Team for a Merry Christmas and a Happy New Year.

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