SLAUGHTER AND MAY/

BOARDROOM ESSENTIAL

Need to know for non-executive directors and senior management

November 2024

CONTENTS

THE POST OFFICE SCANDAL – A FAILURE OF GOVERNANCE 3

TAKEOVERS IN 2024 – A SHARP REBOUND OF ACTIVITY 7

THE EMPLOYMENT RIGHTS BILL – A NEW ERA FOR EMPLOYMENT 10

PREVENTING SEXUAL HARASSMENT – THE NEW DUTY 12

INVESTMENT ASSOCIATION REVISED PRINCIPLES OF REMUNERATION: OCTOBER 2024 14

Welcome to the winter issue of Boardroom Essential, our regular publication for non-executive directors and senior management.

In this edition we look at the Employment Rights Bill, the most significant piece of employment legislation for decades, which will implement a number of the key pledges from the Labour government's plans for employment. We also look at a new duty on employers to prevent sexual harassment of their employees in the course of their employment; failure to comply with the new duty may expose employers to increased financial, regulatory and reputational risk.

We have seen a sharp rebound of UK takeover activity in 2024; we examine the key trends and examine what boards of target companies should be thinking about.

We also consider a recent report by the Institute of Directors that looks at the failures of governance exposed by the Post Office Horizon Inquiry; what lessons can all directors learn from this?

Finally, of particular relevance to Remuneration Committees, the Investment Association has significantly revised its Principles of Remuneration. We summarise the key areas of focus.

If you would like more information on any of the matters covered, please speak to your usual Slaughter and May contact. We hope you enjoy the issue.

Paul Dickson
Partner

THE POST OFFICE SCANDAL – A FAILURE OF GOVERNANCE

Last month, the Institute of Directors ("IoD") published a Report, "The Post Office Scandal – A failure of governance". The Report sets out the conclusions of an IoD working group which examined the evidence from Phase 6 of the Post Office Horizon IT Inquiry, focussed on issues of governance.

What is revealed is "*a fascinating picture of a dysfunctional board*". As the Report notes, "*on the surface, the POL* [Post Office Limited] *board appeared to be operating normally. Board and committee meetings were conducted in an orderly and well-documented manner. Many of those involved appeared to be well-meaning people who had convinced themselves that they were doing the right thing for the organisation. There was little evidence of tell-tale signs that have characterised other governance scandals, such as hubris, personal greed or large-scale fraud.*" How then did things go so badly wrong?

KEY LESSONS FOR DIRECTORS

The Report highlights certain key lessons, summarised below, that could be relevant to the directors of other organisations.

1. **Face up to uncomfortable truths:**
   A leitmotif of the evidence is that directors joining the Post Office board were quickly absorbed into an accepted view that the Horizon system was fit for purpose and that sub-postmasters were generally untrustworthy. This thinking led to a lack of challenge. The lesson for directors is to be ready to discuss and test prevailing assumptions, however uncomfortable for the organisation.

2. **Break out of the boardroom bubble:**
   The views of the board were almost entirely guided by management. Directors failed to test those views by engaging with other stakeholders (such as external experts, Fujitsu or even the sub-postmasters themselves). To truly understand what is going on, it may be necessary to listen to other voices inside and outside the organisation.

3. **Don't ignore red flags:**
   The Post Office directors missed or ignored numerous red flags that should have prompted them to challenge management. The normal critical scrutiny expected from a board of independent directors was lacking, and at times seems to have been actively stifled. The board did not show the necessary curiosity or persistence to understand and pursue these warning signs.

4. **Ensure proper governance of outsourcing:**
   The Report observes that there appears to have been remarkable confusion at senior level about who was responsible for what. A key factor was the mismanagement of the IT outsourcing relationship with Fujitsu and overreliance on Fujitsu's assurances about the Horizon system. As a board, control of outsourcing arrangements and proper reporting are critical. Assess your organisation's vulnerability to "supplier capture", where an outsourcing partner becomes too difficult to challenge or replace.

5. **Directorship is about more than one thing:** The Post Office directors were very focussed on turning around the business's financial prospects, but too often took a 'hands off' approach when dealing with other issues, such as the legacy IT issues and the legal prosecutions of sub-postmasters. A striking example from the Inquiry of this came when it questioned Ken McCall, a former Senior Independent Director. He was asked why, when there was evidence that Horizon was not robust, he had not challenged the Chair, Paula Vennells, over her unbending policy of denial to press inquiries. He repeatedly insisted that he was "*not responsible for media strategy*". Directors have collective responsibility for decision-making and must sufficiently address all the key risks of the business. They cannot pick and choose.

6. **Demand full access to all relevant information:** Important reports and information were withheld from the Post Office board, including on the basis of what the Report calls "*questionable advice*" over legal privilege (see further below on *Legal Privilege*). Boards are urged actively to determine what information they need from management and to be alert to filtered information that may inhibit them from making informed decisions.

7. **Advisers advise, directors decide:** The Report concludes that Post Office board members deferred too much to the views of internal and external legal advisers. While proper advice is a crucial input for decision-making, the Report advises directors not to accept advice without question and directors should apply their own independent strategic judgement and "*moral compass*".

8. **Get properly trained as a director:** Several of the Post Office directors joined the board without previous experience or training as a director. Others who had served as directors in the past nonetheless showed a weak understanding of a director's responsibilities. The Report recommends that all directors should receive specific training.

9. **Due diligence and induction is more than a 'nice to have':** Many Post Office directors started out with an incomplete understanding of the issues facing the organisation. The Report recommends that directors do robust due diligence before accepting a board seat and undergo a systematic induction process after appointment.

10. **Use board evaluation as a key governance tool:** Strangely, almost no evidence from board effectiveness reviews was presented to the Inquiry. The only board review documented in the Inquiry was a 2013 internal review, which the Report concludes was ineffectual and lacking in rigour. Robust board evaluation processes might have provided an opportunity for the Post Office board to reflect on how it was functioning, with the benefit of an external perspective. The UK Corporate Governance Code recommends that boards conduct an internal review every year, bolstered with an external review by an independent body every three years.

11. **Insist on IT literacy:** Many board members lacked IT literacy or experience. The Report advises that although every director does not need to be an IT expert, a high level of tech literacy should be seen as a prerequisite for directorship, particularly in relation to overseeing IT projects, and in light of the AI and cybersecurity challenges facing businesses.

12. **Maintain a moral compass:** The Report surmises that executives and board members lost sight of basic ethical business behaviour and became absorbed into a distorted corporate culture. It urges directors to behave in way that is anchored in strong ethical principles.

It goes on to urge all boards and directors to align themselves with an explicit code of conduct, such as the IoD Code of Conduct of Directors. However, as discussed in the last edition of Boardroom Essential, we are not advising directors to sign up to the IoD Code of Conduct.

LEGAL PRIVILEGE: USED OR ABUSED?

The Report observes that "*questionable advice*" over legal privilege fuelled Post Office management's "*instinct to suppress key information*" and withhold crucial information from board oversight.

In particular, in 2019 the then-Chair of the Post Office, Tim Parker, chose not to share with the rest of the board a report from external legal counsel (Jonathan Swift QC) raising concerns about the safety of past prosecutions of sub-postmasters. He said he made this decision on the basis of advice from the Post Office General Counsel that sharing the report would lead to a loss of privilege and could result in it becoming public.

The Report concludes that it "*is rarely acceptable to withhold information from board members on the basis of considerations such as legal privilege.*"

In reality, though, questions about losing legal privilege can be complex and should be carefully addressed with the benefit of relevant legal advice and taking into account particular circumstances. By way of some general comments:

- *What is legal privilege?*
  Legal professional privilege, where it applies, acts as a heightened form of protection over confidential information, shielding from disclosure certain types of communications between a lawyer and their client and, where made in relation to litigation, between the lawyer or client and third parties.

- *Who is the client?*
  Privilege is subject to important limits. One such limit relates to the identity of the 'client'. Outside of litigation, only communications between a lawyer (in-house or external) and a 'client' made for the dominant purpose of seeking or giving legal advice in a relevant legal context are protected by privilege. 'Client' for these purposes means only those persons within a corporate entity who are authorised to seek and receive legal advice on the company's behalf, not everyone who works at the company. On this definition, in many cases, particularly in large corporations, the board may not be the 'client' and is instead a 'third party' falling outside the protections conferred on privileged communications between lawyer and client.

- *Can privileged advice ever be shared?*
  In reality it may nonetheless be necessary to share legal advice outside the narrow 'client' group within a company. For example, actions related to that advice may need to be agreed at board-level, and actions contained in the advice may need to be carried out. English law recognises that privileged legal advice can be shared with third parties, including internally within a company, on a limited and confidential basis without waiving privilege as against the rest of the world.

There are inevitably risks in sharing privileged information with third parties. Where privileged information is shared too widely, even internally within a company, there is a danger that confidentiality – a fundamental component of privilege – is lost. Where privilege is lost in a document, that document (and potentially related documents) may become disclosable in litigation or to a regulator.

On the other hand, it is also important that the right people within an organisation – especially the board – have access to the information they need to ensure effective governance and decision-making. Where that information is legal advice, the risks of losing privilege by sharing that advice need to be balanced with the risks and consequences of not sharing the advice.

Where on balance legal advice needs to be shared, mitigations can be put in place to limit the risks of losing privilege in that advice. Care should be taken to ensure that legal advice is shared internally on a 'need to know' basis on express terms that the information is confidential and privileged, privilege is not being waived and the information should not be shared more widely. Express agreement should be obtained from the 'third parties' receiving the legal advice that they will maintain confidentiality (and therefore privilege) in the information being shared. Marking documents 'confidential and privileged,' whilst not determinative, is a helpful marker about the sensitive nature of the material being shared.

TAKEOVERS IN 2024 – A SHARP REBOUND OF ACTIVITY

Takeover activity has returned sharply in the UK in 2024, particularly with the return of higher-value bids. This is in part due to a backlog as interest rates and inflation stabilise, coupled with the oft-quoted undervaluation of UK listed companies, as well as an abundance of PE "dry powder" (albeit less so than in 2021-2022) and – perhaps the key trend of 2024 – corporates seeking strategic acquisition opportunities.

In this article we look at key takeover trends and developments, and what they may mean for the year ahead, and we share insights from our recent experiences on the leading deals in the market. You can read about these topics and deals in more detail here.

WHAT BID-SIDE TRENDS ARE WE SEEING?

1. **2024 has seen a huge uptick in corporate-to-corporate activity,** as corporates continue to search for growth amid a more confident environment. Bidders with strong cash balances and/or the ability to offer their own shares as consideration have been well placed to meet target boards' value expectations.

2. **Europe-UK and UK-UK offers have been the prominent trend this year,** although there have been some examples of US bidders. This trend is despite predictions that the undervaluation of UK businesses compared to their US peers would result in an influx of US bidders for UK targets.

3. **Private Equity also remains active behind the scenes.** We are seeing PE bidders talking to targets in private, often downing tools when there is a valuation gap between their offer and target management expectation. With some exceptions, it has tended to be more challenging for PE to offer the large premiums we saw when interest rates were at their lowest. We expect to see an uptick of high-value PE bids as debt conditions improve and PE needs to deploy its "dry powder".

4. **Bidders are increasingly using bear hugs,** i.e. where a bidder publishes an indicative offer and price for the target, without the target board's consent. Bidders are also increasingly "wall-crossing" shareholders privately before formally approaching target boards. For target boards, advance preparation for a possible bear hug approach is therefore key (see below).

5. **Increased number of deals where shares are offered** as part (or all) of the consideration. While debt availability has improved, it remains a restraint. Including shares as part of the consideration reduces the cost of financing for the bidder. It can also play a part in "selling" the deal to reluctant target shareholders, since offering shareholders a means of staying in the business under new ownership can be presented as an attractive, synergic equity story.

WHAT ARE TARGET BOARDS THINKING ABOUT?

1. **Valuation:**
   Price/valuation remains the key focus. The undervaluation of UK companies compared to their listed US peers is well publicised, and PE sponsors are tending to offer lower premiums to market value than they historically have. As the market improves, we are seeing target boards be more resistant to bear hugs, especially where an approach appears opportunistic and fails to meet their valuation expectations. This has led to more possible offers being announced that have not subsequently translated into a firm offer.

2. **Deliverability:**
   Given the ever more difficult regulatory environment, targets are increasingly ready to reject proposals where deliverability is uncertain. We are seeing more up-front negotiation not just of price, but of other key commercial points, such as regulatory undertakings and the length of long-stop dates. We are also seeing targets ask for up-front break fees prior to granting any access to due diligence materials as well as break fees for regulatory conditions.

3. **Shareholder reaction:**
   Target boards are often engaging earlier with shareholders after receiving an approach from a bidder (although the Takeover Code places some restrictions on the number they can engage with before the fact of an approach must be made public). We are seeing target boards making "minded to recommend" announcements before making a formal recommendation, as an opportunity to test shareholder reaction. Target boards should be aware of some recent examples of investor discontent towards deals which were recommended by the board and then subsequently rejected by shareholders. Furthermore, shareholders appear more willing to oppose proposed deals publicly and vociferously.

IS THE IDENTITY OF THE BIDDER RELEVANT?

The question is sometimes asked: should target boards, when considering whether to recommend an offer, take into account the suitability of a bidder as a guardian for the business, and consider how the business may fare under its new ownership? Or is price the overriding factor, so that they must recommend if the "price is right", even if they think that the new owner may be bad for the business in the long-term?

By way of example, in 2021, the board of Vectura, a UK inhaler manufacturer and respiratory specialist company, recommended an offer by Philip Morris International (the manufacturer of Marlboro), after an auction process between PMI and the private equity group Carlyle. Critics pointed out the absurdity of a tobacco company buying a pharmaceutical business, criticisms which arguably may have been justified when, this year, PMI sold Vectura for a third of what it paid. This deal, and others, have even led to calls from some quarters for reforms to statutory directors' duties.

However, there are two important points we would make in this context:

1. Where a takeover is governed by the UK Takeover Code, the Code requires the directors to give their views on the offer, including the effects of the offer on all the company's interests, and to give a recommendation from the board as to the action that shareholders should take in respect of the offer. The board's advice can be nuanced – as it was in the case of the Glazers' bid for Manchester United in 2005, for instance: the board expressed their reservations about the new ownership but the price being offered was too high not to be put to shareholders. Target boards also have to remember that in reality it is always open to an unwelcome bidder to bypass

the target board entirely and make a bid directly to shareholders – target directors may face a backlash if they are seen to have tried to deprive shareholders of a good offer (as well as potentially being in breach of the Code's General Principle 3).

2. The key statutory duty – that a director must act in the way he or she considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole – is qualified by six statutory factors that the directors must have regard to, including the likely consequences of any decision in the long-term, the interests of the company's employees, and the impact of the company's operations on the community and the environment. These factors provide the directors some autonomy to voice their concerns about the possible impacts of a takeover by a particular bidder when framing their advice to shareholders.

HOW CAN POTENTIAL TARGETS PREPARE?

Advance preparation is key as, once an approach is received, things move very rapidly. Boards should ensure the following steps have been taken:

1. Have a bid defence manual
2. Choose inner circle (and ensure all are well-briefed)
3. Monitor share price and know your valuation
4. Keep record of profit forecasts
5. Cultivate shareholder relationships
6. Monitor the shareholder register
7. Consider potential strategies for an approach scenario
8. Undertake regulatory / competition analysis
9. Maintain board and management consensus on strategy

If you would like help with any of the topics discussed, please get in touch with your usual Slaughter and May contact.

THE EMPLOYMENT RIGHTS BILL – A NEW ERA FOR EMPLOYMENT

The Employment Rights Bill is the most significant piece of employment legislation in decades, implementing around a third of the key pledges from Labour's Plan to Make Work Pay. In some cases, the Bill contains detailed provisions but, in many others, it simply provides ministers with the power to make regulations. This will allow the detail of certain proposals to be fleshed out following consultation.

The key provisions of which employers should be aware are:

1. Day one unfair dismissal rights

The Bill repeals the current two-year qualifying period for unfair dismissal. It also introduces a power for ministers to make regulations governing dismissal during "an initial period of employment". This will be subject to consultation during 2025, but will effectively create a statutory probation period, likely to be a maximum of nine months, during which the employer will be able to assess the employee's suitability for the role and will only need to follow a 'lighter touch' dismissal procedure. These changes are not expected to come into force until autumn 2026.

2. Industrial Relations

The Bill repeals the restrictions introduced by the previous government on the procedure for trade unions both to secure recognition for collective bargaining and to call industrial action. In addition, it will introduce electronic balloting, a new right of access for trade unions to workplaces and a new requirement on employers to notify their workers of their right to join a trade union. It also introduces protection for workers against suffering detrimental treatment for taking strike action. These are anticipated to be among the first changes to take effect once the Bill passes into law, likely in the first half of 2025.

3. Fire and rehire

The Bill severely restricts the ability for employers to effect changes to terms and conditions though a fire and rehire process. It makes it automatically unfair to dismiss an employee because they do not agree to a proposed variation of their contract, or to enable the employer to employ another person (or re-engage the same employee) under a varied employment contract to carry out substantially the same duties. There will be a limited defence if the employer can show that the changes are necessary to significantly reduce or mitigate the effect of any financial difficulties which were affecting or likely to affect the viability of its business.

4. Collective redundancies

The Bill expands the scope of the obligation to consult collectively on proposed redundancies of 20 or more employees within a period of 90 days or less, by removing the criterion that these redundancies should be "at one establishment". The government is also considering increasing the protective award for failure to comply with this obligation (currently capped at 90 days' pay per affected employee) by doubling the minimum consultation period where an employer is proposing to dismiss 100 or more employees from 45 to 90 days and also allowing employees to claim interim relief for failure to comply.

5. Protection from harassment

The Bill expands the new duty on employers to take reasonable steps to prevent sexual harassment by requiring that "all" reasonable steps must be taken. This is the subject of a separate piece in this edition of Boardroom Essential. It also reintroduces employer liability for harassment of its employees by third parties and allows regulations to prescribe what will constitute "reasonable steps" for both of these purposes. Finally, a complaint that sexual harassment has occurred or is likely to occur is explicitly included as one of the disclosures which may qualify for protection under whistleblowing legislation.

6. Family friendly and equality

The Bill will expand protection for new mothers and parents by allowing regulations to prescribe when dismissals will be permitted during an 18 month 'protected period' following the birth or adoption of the child. It will also require large employers (with 250 or more employees) to create action plans to address gender pay gaps and to support employees through the menopause. Gender pay gap reporting will be extended to contract workers (there are also plans to introduce race and disability pay gap reporting via separate legislation). The right to request flexible working will be strengthened with additional reasonableness requirements. Finally, the Bill also extends the existing right to parental bereavement leave to a more general right to bereavement leave.

7. Guaranteed hours offers and shift protections

The Bill includes complex provisions entitling qualifying workers on zero hours or low hours contracts to a 'guaranteed hours offer' from their employer. This will essentially require an employer to make an offer of guaranteed hours to the worker based on his or her average hours worked over a defined reference period. The detail will be prescribed by regulations.

There are also provisions for workers to receive reasonable notice of a shift, or of any cancellation or changes to a shift. Workers will then be entitled to receive compensation for any shifts cancelled, moved or curtailed, with the amount of that compensation to be set out in regulations.

NEXT STEPS

The Bill is now in committee stage and a number of consultations have already been launched on its provisions, with more expected in Q1 2025. This is an opportunity for employers and other stakeholders to share their views and suggest potential amendments to the Bill's provisions, and to the detail which will be prescribed in regulations.

If you would like to discuss the implications of the Bill for your business, or take part in any engagement on consultation on the Bill, please contact Phil Linnard or Philippa O'Malley, or your usual Slaughter and May contact.

PREVENTING SEXUAL HARASSMENT – THE NEW DUTY

WHAT HAS CHANGED?

On 26 October 2024, employers came under a new duty to take reasonable steps to prevent sexual harassment of their employees in the course of their employment. This new ‘preventative duty’ was implemented via the Worker Protection (Amendment of Equality Act 2010) Act 2023, which inserted a new section 40A into the Equality Act 2010.

The preventative duty applies not just to sexual harassment of one employee by another, but also to sexual harassment by third parties – including customers, clients and contractors and anyone else interacting with the employer’s employees in the course of their employment. This is despite the fact that employers are not currently liable for sexual harassment of their employees by third parties.

WHY DOES THIS MATTER?

Failure to comply with the preventative duty could lead to enforcement action by the Equality and Human Rights Commission (EHRC) against the employer (for example, issuing an “unlawful act” notice requiring the employer to prepare an action plan for how it will prevent future failure), even if there has been no incident of sexual harassment. In addition, where an employee succeeds in a tribunal claim for sexual harassment and is awarded compensation, the Employment Tribunal can uplift that compensation by up to 25% if it considers that the employer has not complied with the preventative duty. There is therefore a risk of increased financial, regulatory and reputational exposure for employers.

WHAT IS “REASONABLE” HERE?

The EHRC has published an updated version of its Sexual harassment and harassment at work: technical guidance, to reflect the introduction of the preventative duty. The guidance makes it clear that what steps are “reasonable” to prevent sexual harassment will depend on a number of factors, including:

- the employer’s size and resources;
- the working environment and risks present;
- the nature of contact with third parties;
- compliance with any applicable regulatory standards;
- concerns about sexual harassment that have been raised previously;
- whether steps taken have been effective; and
- the cost/benefit analysis of taking a particular step.

WHAT DO EMPLOYERS NEED TO DO?

In terms of what the duty translates to in practice, employers should take the following steps:

- Carry out a risk assessment, to anticipate scenarios when its employees may be subject to sexual harassment in the course of their employment, and what action may be needed to prevent it.
- Produce an action plan, setting out what preventative steps the employer has determined are reasonable for it to take. As the guidance suggests, these will likely include:
    - reviewing the effectiveness of policies and procedures;
    - setting up specific training for managers, and running regular refresher training for all staff;
    - setting up clear and effective reporting channels; and
    - making a record of all reported incidents of sexual harassment and keeping that under regular review.
- Continually monitor the action plan and conduct fresh risk assessments as required, in light of any workplace changes or concerns raised.

The EHRC has also updated its 8-step guide for employers on preventing sexual harassment at work.

WHAT ABOUT FUTURE DEVELOPMENTS?

The Employment Rights Bill will make three important further changes in this area (the Bill is summarised in a separate article in this edition):

- Clause 15 strengthens the preventative duty by requiring employers to take all reasonable steps to prevent sexual harassment.
- Clause 16 reintroduces employer liability for harassment (not just sexual harassment) by third parties, unless the employer has taken all reasonable steps to prevent it.
- Finally, Clause 17 provides for regulations to outline what may constitute "reasonable steps" to prevent sexual harassment, for the purposes of both the proactive duty and third party harassment.

The commencement date for these changes is not yet known. Employers should therefore act now to ensure they are complying with the preventative duty and be prepared to take further steps once the Bill comes into force.

If you would like to discuss the implications of the preventative duty for your business, please contact Phil Linnard or Philippa O'Malley, or your usual Slaughter and May contact.

INVESTMENT ASSOCIATION REVISED PRINCIPLES OF REMUNERATION: OCTOBER 2024

In October 2024, the Investment Association ('IA') revised its Principles of Remuneration for PLC directors (the 'Principles'). This update constitutes a significant re-write of the Principles and a step back from some of the more granular recommendations in previous versions. It re-iterates that the Principles are not prescriptive rules, but rather guidelines seeking to foster good practice and alignment with investor expectations. The Principles should guide companies in developing remuneration frameworks that satisfy their particular business needs and companies should be prepared to explain to shareholders any divergence from the Principles. We summarise the key areas of focus below.

CONSULTATION WITH SHAREHOLDERS

The guiding light of the new Principles is full and appropriate consultation with shareholders. The Principles encourage companies to adopt a remuneration framework that is appropriate to their business and then to explain to shareholders how it aligns with their long-term interests. They stress that the purpose of these discussions is to provide the company and shareholders with a forum for transparent two-way dialogue on remuneration issues, rather than seeking approval for a particular company proposal. At the end of the process the remuneration committee should send a letter to consulted shareholders outlining its final proposals and the rationale behind them. Remuneration committees are encouraged to describe this consultation process in their remuneration report, to allow all shareholders to understand how the company's proposals have evolved in light of shareholder feedback.

HYBRID PLANS

Building on the IA's letter to FTSE companies published in February 2024, the Principles recognise that 'hybrid' LTIPs may be suitable for certain companies, in particular those which have a significant US footprint and/or compete for global executive talent. Hybrid plans consist of grants in the same year of:

I. a performance share component (i.e. share awards subject to challenging performance targets); and

II. a restricted share component (awards subject to ongoing service and a performance underpin but not stretching performance conditions).

While the restricted share component should be discounted to reflect the certainty that it will normally vest, the 'typical' 50% discount may not be appropriate in all circumstances, depending on company circumstances and the performance measures being replaced.

DILUTION LIMITS

The IA has relaxed its guideline on dilution limits by removing the “5% in 10 years” dilution limit for discretionary incentive arrangements/“executive” share plans – although in most cases we expect companies will need shareholder approval to amend their existing plan rules to remove this cap. In practice we expect this will be of most interest to smaller listed companies. The overall “10% in ten years” dilution limit (applicable to shareholder dilution as a result of all of a company’s share plans) remains in place.

ANNUAL BONUSES AND SHARE OWNERSHIP

The Principles now state that mandatory deferral into a company’s shares for annual bonuses can be reduced if the remuneration committee determines that the executive has met their share ownership guidelines and malus and clawback provisions apply. The benchmark for setting executive share ownership guidelines should be the same as the long-term incentive grant size.

MALUS AND CLAWBACK

The guidance around malus and clawback, a continuing area of focus, reminds remuneration committees that executives need to agree to these provisions to ensure enforceability.