SLAUGHTER AND MAY/

CLIENT BRIEFING

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# 2024 INVESTMENT ASSOCIATION GUIDANCE - EXECUTIVE REMUNERATION BRIEFING

On 23 February, the Investment Association (IA) issued its long-awaited guidance on executive remuneration for UK-listed companies. This took the form of a relatively short letter to Remuneration Committee chairs, rather than the usual annual update to the IA's existing Principles of Remuneration. In the letter, the IA covers i) changes to long-term incentive awards to reflect pressure from the US market and ii) the introduction of "hybrid" incentive plans, as well as acknowledging the role of executive remuneration in maintaining the UK's attractiveness as a listing venue.

## BACKGROUND

The IA is the standard-bearer of the UK's institutional investor representative bodies, with the publication of its Principles of Remuneration in late November a milestone in the year for executive remuneration professionals. The fact that the IA did not in Q4 2023 issue a further iteration of its guidance is perhaps in itself evidence that, in its discussions with its members, the IA has not found a universal consensus as to the preferred approach on executive remuneration.

As a result, one of the central themes to come out of the IA letter is that there is no "one size fits all" approach to a framework for directors' pay expected by the IA and companies should develop remuneration arrangements which fit their particular circumstances (including, where relevant, the specific challenges that they are experiencing in terms of employee incentivisation and retention).

## INCREASED FLEXIBILITY

There has been for some time a debate in boardrooms about the relative attractiveness of a listing in the UK compared to the United States, where senior executives can command a significant premium for their services compared to current FTSE practice. This debate has been recently accentuated by the relative paucity of companies seeking an IPO in London (or on other European markets) in 2023, in comparison with the more buoyant market on the New York and NASDAQ exchanges. The IA states in its letter that it wishes to advance London's reputation as a "good place to do business" and therefore to encourage as broad a selection of companies as possible to consider listing on the London Stock Exchange.

To facilitate this, the IA highlights two particular issues for Remuneration Committees' consideration:

1. **US exposure:** In its discussions with companies, the IA has noted a particular concern with UK-listed companies being able to recruit and retain US executives. The IA acknowledges that, where a company is particularly focussed on or exposed to the US market, there may be a rationale for higher LTIP awards (as is common in the US) to incentivise and retain these particular individuals; and

2. **"Hybrid plans":** These arrangements combine the grant of performance-related awards (what might traditionally be thought of as "PSP awards") with the grant of non-performance related awards (so-called "RSP awards") under a single plan. The key advantage of these arrangements is that participants have the comfort that there will definitely be a (relatively small) vesting if they remain in employment, under the "RSP element" of the plan, whilst still delivering the upside of more substantial gains if the company achieves significant levels of performance under the "PSP awards" granted.

UK institutional investors have historically been more sceptical of these hybrid plans, recommending to companies that they take a binary choice between the RSP and PSP model. It is therefore heartening to see that IA members are more open to have the conversation about companies moving to a hybrid structure, which may go some way to addressing the retention issues that some FTSE companies have been experiencing. In formulating proposals for shareholders, Remuneration Committees will wish to consider what, for their particular circumstances, the appropriate balance is between RSP and PSP awards and how the RSP award can be structured to avoid delivering payments for failure, whether by granting RSP awards subject to a performance “underpin” condition or by making RSP awards subject to a discretionary holistic performance assessment by the Remuneration Committee on vesting. These safeguards should be balanced with giving participants a certainty of outcome in respect of the RSP element of the plan, which is one of the key attractions of the “hybrid structure”.

## A LIGHTER TOUCH APPROACH?

The IA acknowledges that the guidance provided to companies over the last couple of years, both through the UK Corporate Governance Code and investor guidance, has markedly increased the granularity of oversight of remuneration practices and that this has limited the scope of companies to produce tailored arrangements for their most senior executives. In response to this, the IA has decided to review its Principles of Remuneration over the course of 2024, with a view to ensuring that they are a framework of principles to guide companies, rather than anything more restrictive, and that they do not overlap with or duplicate the requirements of the UK Corporate Governance Code.

Overall, this is a welcome contribution to the debate on executive pay, in which the IA has recognised that Remuneration Committees are commonly subject to countervailing demands and may need slightly more flexibility than they have been accorded previously to deliver optimal outcomes for shareholders.

If you would like to discuss this further, please contact your usual Slaughter and May contact or one of the individuals listed below:

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