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By e-mail to executive.pay@bis.gsi.gov.uk
Cc: Richard Carter and Gemma Peck, BIS

Dear Mr Walker

Consultation on Shareholder Voting Rights in relation to Executive Remuneration

The GC100 welcomes the opportunity to respond to the recent consultation paper issued by the Department of Business Innovation and Skills on Shareholder Voting Rights in relation to Executive Remuneration. The GC100 is the association for the general counsel and company secretaries of companies in the UK FTSE 100. There are currently over 120 members of the group, representing some 80 companies. Please note, as a matter of formality, that the views expressed in this letter do not necessarily reflect those of each and every individual member of the GC100 or their employing companies.

As you are aware, over the past few weeks, we have been in discussion with Richard Carter and colleagues reviewing the practicalities of implementing some of the proposals set out in the consultation paper. We do not propose to reiterate all the points we have discussed, as we believe that they have been well understood. Nor do we intend to answer each of the questions posed in the consultation paper, but rather to make general comments in each of the key areas. We would be very willing to work constructively with BIS over the summer months to assist in determining what information might be required to be provided in the material for each of the binding and the advisory votes.

As principles, we support the aim for a better link between performance and pay and the goal that there should be no reward for failure. We do believe that some of these issues are better resolved through engagement and discussion with shareholders rather than through a vote, which can easily be hijacked by activist or short term shareholders with different agendas. We believe that shareholders are similarly motivated but recognise the resource constraints currently faced by some institutions.

We are strongly of the view that the Remuneration Committee remains the best body to determine these issues with appropriate oversight and engagement from the shareholders. The Remuneration Committee should comprise only independent directors who, as part of their broader board responsibilities are charged with setting strategy and monitoring operational performance, both of which create the context in which pay must be determined. There must be encouragement for and acceptance of the use of discretion by Committees. The legislation should not be used to take back the very clear delegation already given to Boards.

We also note that a company could potentially be required to put five remuneration resolutions to an AGM in any given year (retrospective advisory vote, policy binding vote, exit payment vote, approval of executive share plans and approval of all-employee share plan). Whilst remuneration is important, this focus does seem excessive given all the other matters a company will be managing.

Binding Vote on Remuneration Policy

As previously stated in our response to your discussion paper on executive remuneration, it is our opinion that the current advisory vote works well and provides shareholders with an appropriate framework to express their views. However, although we do not believe that a binding vote is warranted, we do understand the societal concerns surrounding executive remuneration. Therefore, should the government decide that a binding vote on future remuneration policy is necessary, we would suggest that the following points are reflected in the final proposal:

- We question whether such a vote need be on an annual basis, particularly if, as is the case for most companies, the policy may not change from year to year. We would prefer a system which would require an initial vote on policy with subsequent binding votes only if certain triggers occurred, such as a proposed material change to the policy. If there has to be a backstop vote we would suggest that such a vote every five years may be more appropriate. This period would be consistent with the powers available to the Board under section 551 of the Companies Act 2006 (which involves a material relaxation of shareholders' rights in permitting the issuance of new equity). An annual vote for every company will mean a great deal more work for investors. A five yearly vote will mean that over time, the vote will become staggered and investors would have more time to analyse each remuneration policy. We believe that this will improve the quality of engagement between companies and their investors. An annual vote would be more costly for both companies and investors.

- If this proposal is accepted, in the event that a company wishes to adopt a new remuneration policy, then it may choose to put the remuneration policy to the vote earlier.

- Similarly, we suggest that should the level of support for the advisory vote fall below a certain level, then a company should be required to put the remuneration policy to a binding vote the following year. We would re-iterate that in UK company law, a vote withheld is not a vote. We note however that this is not entirely straightforward as shareholder opposition to how the policy has been implemented in one year does not necessarily mean dis-satisfaction with the policy itself, but merely how it has been applied. In addition, our members have regularly experienced votes being cast against this resolution for a variety of different reasons, such that while there may be clear "dissent", this may have no single root cause.

- We would also suggest that in the event that approval is not secured for the remuneration policy, companies should be required to continue with the policy approved in previous years until the next AGM. We would not expect that many companies will wish to go to the expense of holding another general meeting purely to approve the remuneration policy.

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- If companies do wish to hold a further general meeting, the 90 day period may not provide sufficient time for companies to make the necessary arrangements and carry out effective shareholder engagement.

- We see no reason for the binding remuneration vote to require approval from a higher percentage of shareholders than is required to appoint the directors concerned in the first place or indeed to accept a takeover offer to sell the company and therefore suggest that this resolution should be an ordinary resolution requiring a simple majority. A higher threshold would increase the risk that the remuneration policy could be voted down by one large, but nevertheless minority, shareholder.

- We also suggest that further work needs to be done in clarifying when the remuneration policy approved at an AGM will take effect. Given that the AGM usually takes place four or five months into the financial year, it would be impractical, given the need for internal communications post-approval, for the remuneration policy to take effect in respect of a financial year, four months into the year. Equally so, approving a policy to take effect in eight months' time seems somewhat distant.

- We also suggest that further work needs to be done in agreeing a common approach for calculating a single figure for total remuneration. Whilst some companies already report a total figure, there is some discrepancy over how the amounts in respect of long term share plans, for example, are calculated. A number of our members are working with the Financial Reporting Lab to help them develop a standard approach and we would suggest that the results of this work be used in formulating an appropriate definition for total remuneration.

Advisory Vote on Implementation of Remuneration Policy in Previous Year

We welcome the proposal that the vote on the implementation of the remuneration policy in the previous year should be subject to an advisory vote, given the impracticality of implementing a binding vote which did not support payments and awards already made.

As with the binding vote, we would suggest that this should also be an ordinary resolution. Shareholders also have the option of voting against specific directors should they be dissatisfied with how the remuneration policy has been applied.

Whilst we see the logic in a failed advisory vote leading to a compulsory binding vote on the policy itself in future years, we recognise that the policy and its implementation are two separate things and shareholders may still support the policy but not its implementation in the year under review.

We do not believe that it is appropriate for companies to have to publish a consequence statement upon failure to secure a specified threshold of shareholder votes. To require publication in a set timeframe would escalate the matter inappropriately and require decisions to be taken in an unnecessarily short timeframe without allowing for proper identification and consideration of shareholder concerns. This matter should ultimately be for companies and shareholders to determine as they see fit, recognising the wide range of

actions already available to shareholders should they wish to register their disquiet more forcefully.

Exit Payments

We do not believe that it would be practical or in the best interests of the company and its shareholders to hold a shareholder meeting at the same time as trying to negotiate termination arrangements with a departing director.

Our general view is that limiting exit payments in every situation to one year's base salary could have detrimental consequences for UK business. UK companies already find it very difficult to attract and retain top talent willing to serve on the Board. This is already resulting in fewer executive directors on UK Boards and a smaller pool of suitably experienced talent for such roles within UK companies. Some companies may decide to delist and relocate their head company outside the UK. Other companies may place less emphasis on long term plans and increase base pay significantly. None of these consequences will be in the interests of UK business as a whole at a time when UK businesses should be focusing on building an economy that will be sustainable for the future.

Changing contractual rights under service contracts will be subject to legal challenge and could be a costly exercise for companies and ultimately shareholders. Executive directors may seek higher pay to compensate for the additional uncertainty in termination provisions.

We suggest that the experience in Australia should be examined. Australian law requires companies there to seek shareholder approval *before* paying an executive in excess of "one year's base pay" upon termination. Some Australian companies, including BHP Billiton, have sought prospective shareholder approval of potential payments under executive contracts (generally, being the senior executives, for example. the executive committee of the company in question) that would exceed this termination payments cap. Such approval requires detailed disclosure of those potential payment arrangements and would of course only be valid so long as those arrangements remain unchanged. In these circumstances, shareholders would approve the details of the potential termination payments in advance and not by reference to a specific leaving situation. Executives are therefore very clear about the parameters that would apply to various termination scenarios.

We suggest that a similar practice could apply in the UK. This would mean further disclosure, would be required regarding the operation and calculation of exit payments. This could form part of the remuneration policy subject to a binding vote on a five year basis, as described above and need not necessarily be a separate resolution.

We believe that more work needs to be done in understanding how exit payments work and it is generally more complex that merely considering the service contract. We would be happy to work with BIS on this. In particular, we would make the following points:

- An executive's package comprises many elements governed by different contractual rights. The service contract will typically cover base salary, benefits in kind and notice period. Share plan entitlements however will be set out in share plan rules, approved by shareholders, bonus entitlements will be set out in bonus scheme rules and pension entitlements are subject to the rules of the pension

scheme. Typically, share plan rules will contain provisions for "good leavers" which mean that share awards will typically vest, subject to performance conditions and pro-rating for time, over a period of time post termination.

- Whilst we would agree wholeheartedly that an executive who had failed or had been found guilty of defrauding the company, should not walk away with an egregious exit payment, most departures are not as clear cut as this. While there are clear "good leaver" (ill-health, redundancy, retirement) and "bad leaver" (dismissal following fraud or other impropriety) scenarios, in our experience the termination of employment for the vast majority of directors falls into a grey area between the two. We would identify the following three groups:

    - Group 1 - Those for whom there is no longer a role and have stepped aside voluntarily (for example, to enable a merger to be consummated).

    - Group 2 - Those "whose face no longer fits" although the executive concerned has not actually "failed". This would be the scenario where the board feels that new ideas and vigour are needed in place of a long-serving executive, or there is no chemistry between the executive and an incoming chairman.

    - Group 3 - Those who must share part of the blame for their exit, through inadequate performance and/or poor relationships with the board.

  We believe that only the Board can determine which of these groups applies in a given circumstance and then determine the extent to which it might be appropriate for share awards to vest or bonus payments be made in accordance with the rules of the applicable plans.

- Finally and with application to both issues, the timing for approval for share plans needs to be woven into this system as they have major implications for both the policy and the approach to termination payments.

We would welcome the opportunity to discuss these points with BIS in greater detail. We have not focused our response on each of the questions in the consultation paper, but rather stood back and considered what changes could be made to existing practices regarding engagement between companies and investors on remuneration which will curb excessive remuneration and prevent payments for failure.

Yours sincerely,

Grant Dawson
Group General Counsel and Company Secretary, Centrica plc
Chairman of the GC100
For and on behalf of the GC100