ICAEW fully participated in the Committee’s Third Report of 2016-2017. We submitted written evidence, and we actively supported the Committee by analysing the written evidence made to that inquiry. We are grateful for this opportunity to provide our refreshed thoughts on the subject of executive pay. We have provided an Action Plan for boards as our answer to the Committee’s fourth question, and we trust it will be of significant interest to the Committee. In summary, this calls for boards to:

1. Treat everything as though it is public
2. Recognise all the reasons why pay is important
3. Look at the entire pay structure
4. Talk about fairness
5. Use simple language
6. Lift the lid on what executives do
7. Have real conversations
8. Admit mistakes
9. Set out pay principles
10. Persist and be patient

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 150,000 chartered accountant members in over 160 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

This ICAEW response of 9 May 2018 reflects consultation with the Corporate Governance Committee whose members are drawn from business, investment and wider stakeholders. The Committee informs our thought leadership and policy work on corporate governance issues and related submissions to regulators and other external bodies.

Q1. What progress has been made on implementing the recommendations on executive pay by the previous Committee in its 2017 report on Corporate Governance?

It is a mixed picture as the Government’s response to the BEIS Green Paper on Corporate Reform picked up on some of the Committee’s recommendations but not others. We hope that our update is of assistance, but the Committee should also seek updates directly from BEIS and the Financial Reporting Council.

- As far as we are aware the FRC are not pursuing a traffic light rating system for the remuneration aspects of the Corporate Governance Code (‘the Code’) or for any other aspects of the Code. Measuring culture and the effectiveness of corporate governance processes is challenging. ICAEW will be looking at this issue in detail in due course, as part of our Connect and Reflect series of thought leadership papers, eg, we will be considering the IOD’s Good Governance Index and the ASEAN Corporate Governance Index created by the ASEAN Capital Markets Forum.

- Long-term incentive plans are not being phased out and shareholders are not being given more binding votes. However, the revised Code is likely to lengthen the minimum
vesting and post-vesting periods for shares from 3 years to 5 years, and new legislation will require quoted companies to provide a clearer explanation of the range of potential outcomes from complex, share-based incentive schemes.

- The matter of stretching targets and clear objectives is covered in the existing Code, and this is very likely to be repeated in the revised Code. The FRC’s revised Board Effectiveness Guidance will also develop this area. Of course targets may be financial or non-financial.

- We do not expect compliance with the revised Code to allow employee directors (or workforce directors) to sit on remuneration committees as they will not be independent NEDs. However, the revised Code will place greater emphasis on stakeholder engagement, and a new provision concerning workforce engagement suggests three options: director appointed from the workforce; a formal workforce advisory panel; or a designated non-executive director. Both new types of director will have the same role and responsibilities as all other directors, plus the additional responsibility of presenting the workforces’ perspective, but not of representing employees or the wider workforce. Code provisions operate on a ‘comply or explain’ basis.

- The new Code will say that any Chair of a remuneration committee should normally have previously sat on a remuneration committee (not necessary the remuneration committee they will chair) for at least one year. Chairs of remuneration committees will not be expected to resign if their proposals do not receive the backing of 75% of voting shareholders, but greater prominence has been given to opposition votes of 20% or more through the Investment Association’s register and through changes to the Code. The current Code says that when, in the opinion of the board, there has been a significant vote against a resolution, the board should explain what action it intends to take to understand the reason behind the vote result when it is announced. The revised Code will be stronger as it will include a new provision will explicitly refers to 20% or more votes being cast against a resolution. Companies will still have to explain, when announcing voting results, what actions they intend to take to consult shareholders in order to understand the reasons behind the result, but in addition, updates should be published no later than six months after the vote. The board should then provide a final summary in the annual report, or in the explanatory notes to resolutions at the next meeting, on what impact the feedback has had on the decisions the board has taken and any actions or resolutions now proposed.

- The pay ratios being introduced will compare CEO pay to the median pay of UK employees across the group, and this will be a legal requirement rather than a Code matter. CEO pay will not be compared with the pay of senior executives. We are not aware of similar ratio requirements being developed for public or third sector bodies.

- There is likely to be a provision in the revised Code which says that annual reports should include an explanation of the company’s approach to investing in, developing and rewarding the workforce and what engagement with the workforce has taken place to explain to how executive remuneration aligns with wider pay policy.

- The Government has appointed PwC’s economics team, supported by Professor Alex Edmans of London Business School, to undertake research into share repurchases. This is making progress by way of a survey and interviews, and we understand that findings will be shared with BEIS in mid-June.
The Committee’s recommendation for a code for large private companies is being progressed. Some private companies will be legally required to report on their compliance.

We are surprised by the public announcement that these new principles will not deal with executive pay.

We believe that clawback and malus deserve closer attention, and we would like to encourage the Committee to consider this area as part of the current inquiry.

**Q2. What improvements have been made to reporting on executive pay in the last 12 months?**

ICAEW does not monitor reporting on executive pay.

**Q3. What steps have been taken by Remuneration Committees and institutional investors to combat excessive executive pay in the last 12 months.**

ICAEW does not monitor reporting on executive pay.

**Q4. What further measures should be considered?**

The Committee’s Third Report said that it is now up to businesses to respond positively, in their own interests, to adjust to raised expectations in relation to executive pay. We wholeheartedly agree. Our response to this question reflects the contents of a ICAEW publication ‘How to end excessive pay’ which forms part of our Connect and Reflect thought leadership programme.

9 May 2018