Willis Towers Watson

FTSE 100

The story so far... an update

This update is based on over 70% of FTSE 100 companies that have published their annual report and accounts to date, primarily based on December year ends.

In this report we explore some of the current market responses to COVID-19 as well as providing our usual updates on market practice in the FTSE 100 to date. As expected, we have seen more changes to remuneration levels this year as the majority of companies are tabling a new Policy for approval. Whilst AGMs are on-going, we have also provided a summary of proxy agency recommendations and AGM voting out-turns.

Fixed pay

2%
Median CEO salary increase

1 in 4
CEOs received no salary increase
(1 in 8 CFOs)

Aligning pension for existing Executive Directors with the wider workforce has been a key area of investor scrutiny this year, with the IA stating that this should be achieved by the end of 2022.

Pension contributions for existing EDs were already aligned with the wider workforce in 30% of companies, with an additional 12% achieving alignment following reductions in 2020. A further 23% of companies are committing to aligning levels by the end of 2022. Based on current disclosures, around 1 in 3 companies are not compliant with the IA's guidance.

Of those companies making reductions, the most common approach is a phased reduction over a number of years.

Annual bonus

Nine companies have increased the annual bonus opportunity and two companies have decreased.

9 ↑ 2 ↓

Of these, three companies have implemented an increase on recruitment of a new ED/for future ED appointments. Three companies increased the bonus opportunity while decreasing LTIP levels resulting in a re-balancing of incentives.

The link between ESG measures and incentives has been a consistent theme in recent conversations with investors and will be a 'hot topic' this decade. The use of such measures is significantly more prevalent in the annual bonus than the LTIP, with the most typical measures used being linked to "Social" (e.g. an employee / HR / stakeholder measure). Where used, the typical weighting of ESG measures in the annual bonus is 10% - 20% of the total.

Long-term incentive plans (LTI)

Changes to LTI opportunity have been more frequent than last year, this is unsurprising given we are in a policy year. So far, we have seen fourteen companies increasing and eight companies decreasing.

14 ↑ 8 ↓

Of these, two companies implemented an increase on the appointment of a new ED and five companies have made changes for one ED only.

Three companies in the FTSE 100 have proposed Restricted Share Plans so far this AGM season.

Around 20% of companies in the FTSE 100 now operate an incentive structure other than a 'typical' annual bonus and Performance Share Plan.

Pay out-turns

2019 median CEO single figure
£3.77 million

▶

2020 median CEO single figure
£3.32 million

The median annual bonus payout as a % of maximum has decreased slightly from **70%** last year to **65%** this year. **Discretion** was applied by Remuneration Committees to reduce bonus payments in fourteen companies and increase payments in two companies.

Median LTI vesting has remained the same this year vs. last year, paying out at 65% of maximum. Discretion was applied by Remuneration Committees to reduce LTI vesting in four companies and increase vesting in two companies.

CEO pay ratio
c.90% of companies have published their CEO to worker pay ratio with the median ratio at 73:1. The highest median CEO pay ratio is 2605:1 and the lowest median CEO pay ratio is 15:1.

Post-employment shareholding guidelines

- The UK Corporate Governance Code applies to companies with financial years starting on or after 1 January 2019. Of these, c. 84% now have a post-employment shareholding guideline in place.
- Just over half of these are compliant with the IA's guidance to hold the lower of the shareholding requirement immediately prior to departure or the actual shareholding on departure for two years post-cessation. Where companies are not IA compliant, typically a smaller shareholding is required on cessation (e.g. 50% of the in-employment guideline) or a phased approach is taken to the time for which shares must be held.

Proxy agencies, AGM voting and governance

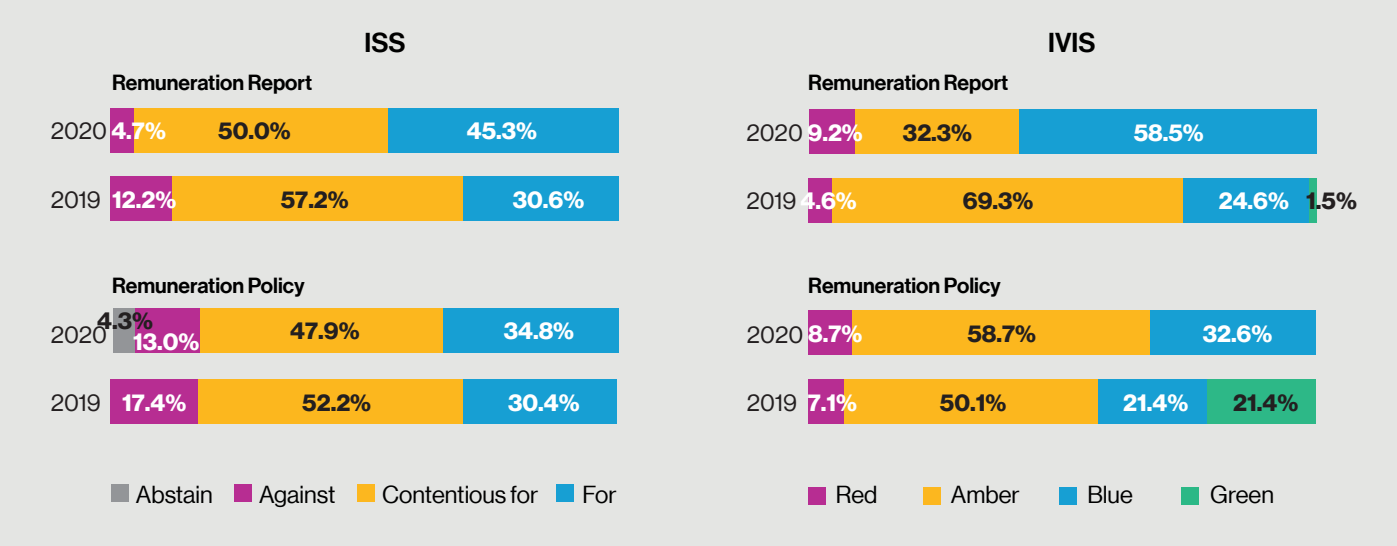
Proxy agency recommendations

With over half the recommendations now issued, current results indicate that the proxy advisors are taking a mixed approach. ISS are issuing slightly less negative voting recommendations for both Remuneration Reports and Policy. The IVIS picture is more varied, with more 'red' and 'blue' tops for Reports and more 'amber' tops on Policy. There have also been two instances of "Abstain" recommendations on Policy from ISS.

Following the clear guidance from the IA on pensions, recommendations to date show ISS is also taking a firm stance on alignment for existing EDs. Three companies received an "Against" recommendation from ISS on their Remuneration Policies in part due to pension contributions for existing incumbents above market levels with no commitment to align them with the wider workforce. One company received an "Abstain" due to no disclosed plan towards alignment for the US based ED. A plan for UK based EDs was disclosed and triggered the abstention rather than "Against", (alongside other Policy improvements).

Aside from pension, the pay for performance link and large salary increases continue to be key areas of focus:

- Incentive opportunity increase when not accompanied by a compelling rationale.
- We have seen an increase in scrutiny around incentive targets over recent years with concerns around the stretch of targets and increased disclosure expectations, particularly where adjustments have been applied.
- Base pay levels and increases. Companies that award above inflationary/broader employee base salary increases without clear communication and compelling rationale continue to receive push-back.

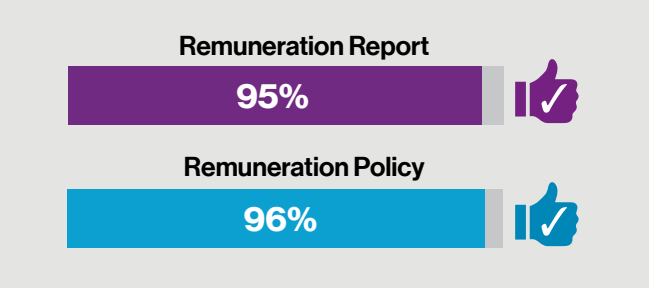


AGM voting out-turns

Shareholder support at AGMs remains high with **median support of 95% for the Remuneration Report** (96% last year). The median support for Remuneration Policies this year is 96% vs. 93% last year.

One of the three companies introducing a Restricted Share Plan has received a low vote (<70%) for Policy, with the proxy agencies stating that the reduction in quantum does not sufficiently offset the certainty of payout introduced by the new plan. The AGM for the other two companies have not yet been held.

We have seen five companies receive votes of less than 80% for the Remuneration Report or Policy at AGMs this year. All five companies also received a vote 'Against' for the respective resolutions from ISS. Cited issues include incentive increases, excessive quantum and lack of pension alignment.



Response to COVID-19 and other governance developments

How companies and investors have responded to COVID-19

- Since our last update, proxy agencies have issued guidance on COVID-19 and executive pay. While some guidance is more prescriptive, it is clear that there is an expectation of transparent disclosure if any changes are made to pay in response to the current environment. Any adjustments to in-flight awards will generally not be supported. The overarching principle that executive pay shouldn't be isolated where wider company action has been taken is also consistent. There does seem to be some acceptance that there may need to be a delay to target setting given the current uncertainty and that judgment and discretion may need to be used in future years, particularly to ensure pay is reflective of performance and there are no windfall gains.
- It is clear that, while market practice is of note, there are other considerations for companies to take into account when making decisions around how COVID-19 impacts the approach to pay. The key reference points Remuneration Committees are considering are (i) the impact on the wider employee population (ii) financial implications on the business including the need to preserve cash and take-up of Government aid and (iii) the shareholder experience through share price performance and impact on dividends.
- To date, c.67% of FTSE 100 companies have announced changes to pay due to COVID-19 via a regulatory announcement. For executives, these have mostly been pay cuts (most typically 20%), forfeit of bonus and donating pay to charity. For the all-employee group changes have been concentrated around pay and hiring freezes.
- Given the timing of the pandemic, we saw little disclosure in Remuneration Reports for companies with a December year-end. There has been a delay in reporting for companies with year-ends after this date (e.g. February / March), with only 65% of companies that had reported this time last year reporting to date in 2020. The business impact on Feb/March year end companies has varied significantly which has driven a wide range of practice, although most do make reference to COVID-19. To date, the most common changes are applying salary freezes, delaying incentive target setting and increasing the proportion of incentives deferred into shares. There are also examples of companies changing performance measures in incentive plans to take into account the change in business focus required over the coming months.
- The Government has announced changes to its COVID-19 Corporate Financing Facility (CCFF), to ensure businesses that draw for a term extending beyond 19th May 2021, will provide a letter addressed to HM Treasury that commits to showing restraint on payment of dividends and senior pay during the period the loan is outstanding. It has also been announced that businesses who draw from the Coronavirus Large Business Interruption Loan Scheme (CLBILS) will be subject to more prescriptive restrictions including not making any dividend payments or share buybacks, and not having the ability to pay cash bonuses or award pay rises to senior management (including the board). Exceptions to this are where companies declared payments before taking out the CLBILS loan, and there is no material negative impact on the ability to repay the loan.

ESG developments

- The Task Force on Climate-related Financial Disclosures (TCFD) has provided a framework for companies to develop more effective climate-related financial disclosures through their existing reporting process. They emphasise the criticality on companies to consider the impact of climate change and associated mitigation and adaption efforts on their strategies and operations and disclose related material information. In March 2020, the FCA announced a consultation on proposals which would require companies with a premium listing to make enhanced climate-related disclosures consistent with the TCFD approach, or explain why they are not.
- The IA has released a report which outlines IA member expectations for stewardship with climate change and the employee voice featuring prominently. Executives should be fully versed on the impacts of climate change on their business. Companies are expected to have governance processes in place to oversee their response to climate change with clearly defined responsibilities for oversight, proactively identifying and taking action to manage climate related risks to their business, and making necessary disclosures.
- IVIS have introduced a new section to its ESG report, which highlights to investors whether the company has made climate change-related disclosures and if these are aligned with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations.

Response to COVID-19

Willis Towers Watson Point of view:

- **Take a long-term perspective** – the UK is only a few months into disruption and it is not yet clear how long the economic impact will last – immediate and drastic action should be checked.
- **Maintain good governance and alignment with your reward philosophy** – RemCo and HR governance policies and precedents should continue to apply to decision making.
- **Be consistent and fair from bottom to top** – if wider business actions have had a negative impact on employees, investors may scrutinise decisions to treat executives more favourably.
- **Adapt your reward interventions to your industry** – reward changes very much reflect the nature of operations, sector, and geography – keep up to date with peers as employees may check.
- **Consider shareholder experience and expectations** – some proxies and investors have already confirmed their expectations in light of COVID-19 and pay (particularly executive) should be cognisant of the investor perspective.
- **Support your RemCo in its decision-making** – Continue to provide all necessary information to enable the RemCo to take immediate action.
- **Consider the difference between judgement and discretion** – in taking decisions on executive pay, distinguish between judgement (understood as interpreting performance) and discretion (changing actual performance outcomes in light of the current facts). Any use of discretion must be clearly disclosed and explained to investors.

Further information

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