FairPensions™
The campaign for **responsible** investment

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To whom it may concern,

FairPensions welcomes this opportunity to respond to the consultation '*Bank Executive Remuneration Disclosure*'. FairPensions (Fairshare Educational Foundation) is a registered charity established to promote responsible ownership practices by pension providers and fund managers. FairPensions champions greater transparency and accountability to the millions of people whose long-term savings are managed by institutional investors and other professional agents. We believe that responsible investment helps to safeguard investments as well as securing environmental and social benefits.

We engage closely with BIS on corporate governance issues and responded to the recent consultation '*Executive Remuneration: a discussion paper*'. We hope that the approach taken to disclosure of non-board executive remuneration in financial institutions will be consistent with the government's wider approach to executive pay.

Question 1: Do you agree with the Government's approach to remuneration disclosure, as set out in this chapter, and does the draft legislation, set out in Annex A, achieve this aim?

General principles

We strongly support the extension of disclosure requirements to significant risk-taking decision makers beyond board level. Indeed, we think that this is a sound general principle in relation to remuneration disclosure generally and not only in relation to financial services. We have made this point in discussions with BIS regarding their work on executive remuneration.

There appears to be a slight disconnect in the government's approach to remuneration disclosure. The scope of the provisions (i.e. restricting disclosure to the largest UK banks and UK operations of overseas banks) suggests that the key objective is to facilitate oversight of systemically important actors. However, the primary audience for these disclosures appears to be shareholders (p5) who at present have little or no interest in exercising oversight of systemic risks posed by activities within their firms.

We agree that there is a public interest in the remuneration of systemically important actors. We also agree that, in theory, there is also a shareholder interest in overseeing these actors' incentive structures and the risks they might pose. However, in practice shareholders tend to focus solely on the appropriateness of remuneration at the individual firm level when evaluating executive pay.

If the rationale of these proposals is indeed primarily to reduce systemic risk, then there is a broader need to ensure that shareholders use the disclosures in this spirit. In the case of institutional investors such as pension funds, this means encouraging them to take a broader approach to the interests of their beneficiaries, recognising that they are 'universal owners' (i.e. they have holdings across the economy), and therefore have an interest in the long-term stability and sustainability of the economy as a whole which may not coincide with their interest in maximising short-term profits at individual firms. HM Treasury should work with the FRC in developing the UK Stewardship Code to ensure that it meets this challenge head-on. It should also engage with the results of the Kay Review, particularly as regards the question of whether current interpretations of fiduciary duty are holding institutional investors back from taking this broader approach.

Conversely, if the rationale of these proposals is primarily to give shareholders information they need to judge strategy and risk at an individual company level, then arguably the same approach to disclosure should extend beyond large and systemically important firms, encompassing significant non-board executives in other companies both within and outside the financial sector.

Sunset and review
Regarding the extent to which the draft legislation achieves the government's objectives, we would like to comment on the inclusion of a sunset clause and review requirement (regulations 1(3) and 14). We understand that these clauses originate from the BIS guidance on 'Sunsetting Regulations'. However, we were surprised that the exemption from 'one-in, one-out' for regulations designed to tackle systemic financial risk was not replicated in the government's policy on sunsetting and review.

In this particular case the sunsetting and review provisions seem particularly inappropriate. Given the government's estimated compliance costs of just £2,250 per firm, set against the enormous costs of the financial crisis of which this intervention aims to help prevent a repeat, it would be extremely difficult to argue that the regulations are disproportionate or heavy-handed. The suggestion that government must review whether its objectives "could be achieved with a system that imposes less regulation" therefore seems dangerous, presenting unacceptable scope for a return to the inadequate regulation which all parties acknowledge contributed to the financial crisis. It also sends a counter-productive message, suggesting that this measure is being introduced to meet popular sentiments about 'bankers' bonuses' but that, in the longer term, the government remains fundamentally committed to deregulation even in a financial services context. For these reasons, we believe that the inclusion of sunset and review provisions materially undermines the government's policy intent.

Content of disclosures

We also have some concerns about whether the required content of disclosures entirely meets the government's objectives; please see our response to Question 4.

2. Do you have any comments on the Government approach to defining relevant banking institutions?

The wording of the consultation document and draft regulations in relation to groups with several qualifying institutions is somewhat ambiguous. The consultation document states that group disclosures must cover "the most highly paid senior executives with management responsibility for relevant banking institutions within their group" (p10). The draft regulations likewise state that group disclosures must cover "the eight most highly remunerated relevant executives working for relevant banking institutions in the group" (regulation 7(1)(a)). It is unclear to us whether this is intended to mean

(a) that group disclosures must contain all the information that would be required of each individual firm, i.e. details of the eight highest-paid executives in each qualifying institution; or
(b) that group disclosures must only contain the details of the eight highest-paid executives across the group as a whole.

If the intention is the former, then we support the aim of simplifying disclosures by allowing the parent company to bring together all the required information in one place to avoid confusion and duplication. If the intention is the latter, we are puzzled as to the rationale for this anomaly. We are concerned that the regulations could effectively require a lower level of disclosure in situations which potentially pose a larger systemic risk, i.e. the aggregation of several systemically important institutions within a single group. We would suggest that the wording of this provision requires clarification to the effect that group disclosures must cover "the eight most highly remunerated relevant executives working for *each* relevant banking institution in the group".

Given that regulation 7 is titled 'duty to prepare group executives' remuneration report', we are also puzzled that the regulation states that parent firms 'may' prepare such a report, whereas regulation 5 states that individual qualifying firms 'must' prepare a report.

3. Do you have any comments on the approach the Government has taken in defining relevant executives?

No comment.

4. Do you have any comments on the approach the Government has taken in determining the content of executive remuneration reports?

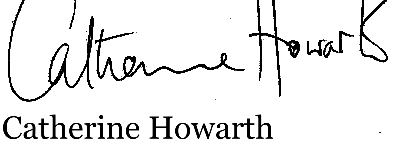
We welcome the comprehensive approach taken to disclosure of the various components of remuneration, to ensure transparency over the balance between fixed and variable remuneration, current and deferred remuneration, etc. We also welcome the inclusion of pension awards to ensure the disclosure requirements are comprehensive and do not inadvertently create loopholes. We assume that the government will work to ensure consistency with any changes to reporting requirements on the remuneration of directors of quoted companies which may be introduced as a result of the current BIS review.

However, we are concerned about one important omission, namely the performance criteria against which variable remuneration is awarded. The current proposals appear only to require disclosure of the quantum of remuneration and not the basis on which it was awarded. It is difficult to see how this meets the government's objective of addressing the problem of "poorly designed remuneration structures [which incentivise] excessive risk taking" (p5), since it does not provide information about the behaviours which remuneration is incentivising or disincentivising. For example, it would do nothing to inform concerns that the continuing use of 'return on equity' (ROE) targets may encourage banks to chase higher returns without taking adequate account of the risks involved. Without the inclusion of this critical information we do not believe that the proposals will meet the government's objectives.

Related to this, we understand the government's concerns about protecting individual privacy, and assume that this underpins the decision to offer no information about the individual's job or division. However, again this decision makes the disclosures materially less useful, since it is not possible to draw a direct line between remuneration structures and particular systemically important decisions or activities. We would encourage the government to reconsider whether the right balance has been struck between privacy concerns and the promotion of useful disclosures which protect the public interest. If the government chooses to continue with the current approach, it becomes even more important to ensure that the definition of 'relevant executives' is appropriate, so that users of disclosures are able to judge the sort of position a given individual holds. Government should liaise with engaged investors to ensure that the current proposals give them the information they need to judge where potential risks may lie and to engage with companies in a substantive manner.

We remain at your disposal and would be pleased to meet with you to discuss any of the issues raised in this response.

Yours sincerely,



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