

Dr Robert Clay
Companies Division
DEPARTMENT OF TRADE & INDUSTRY
5th Floor
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25th March 1996

Dear Dr Clay,

THE COMPANY ACCOUNTS (DISCLOSURE OF DIRECTORS' EMOLUMENTS)
REGULATIONS 1996 - DRAFT STATUTORY INSTRUMENT UNDER THE
COMPANIES ACT 1985 - A CONSULTATIVE DOCUMENT.

This Association has now concluded careful and extensive consideration of the above-titled consultative Document and I now submit, as follows, our various observations and comments upon the content thereof.

At the outset, we record concern regarding the attitude which seems to be implicit in the first sentence of 3.8 (Page 14).

"The proposals are designed to be a useful deregulatory measure but not to remove from the public domain information in which there is a legitimate public interest."

The Consultative Document is wholly concerned with S 232 disclosures required to be made in notes to annual accounts. Arguably + the primary purpose of the requirements that directors prepare and issue annual accounts is to ensure that - in conjunction with the Report of the Directors and the Report of the Auditor - the members of the company (S 238) are properly informed of the affairs of the company during (and at the end of) the year reviewed, and (so far as S 232 disclosures are concerned) are so informed of the costs specifically relating to the governance of the company - and of reasonable 'detail of' such costs.

It is our view that the first sentence of 3.8 (Page 14) would be more 'acceptable', and much more correct, had it concluded with "in which there is a legitimate shareholder or public interest." Apart from other considerations, this wording (and attitude similarly) would be more 'in accord with' the relevant part of the S.E. Listing Rules (see top of Page 24) viz "a report to the shareholders on behalf of the board."

We feel we must emphasise our concern as indicated above; indeed we find it hard to understand how any of the information enumerated within Part 1 of Schedule 6 of the Act is (or, more importantly, ever was) of other than very marginal interest to 'the public' (other, of course, than potential future shareholders). Accordingly, the desirability of any lessening of disclosure requirements should be considered by the Department with maximum regard to the interests of the members

of the company (both present and future).

As you would of course expect, our considerations of the content of the consultative document have been undertaken from the viewpoint of the (non-board member) shareholder. Accordingly, the comments which we make in this submission may well differ - maybe significantly - from those submitted by other consultees who, we suspect, will be more concerned with the governance of unlisted companies rather than with the provision thereto of equity finance.

We do urge the Department to fully bear in mind that if limited company members (shareholders) are to properly and responsibly exercise their 'corporate ownership role' they must not be frustrated - especially by statute - in access to information of pertinent and legitimate interest. It is our strong view that boardroom costs (and a meaningful degree of 'breakdown' of such costs) are of very pertinent and very legitimate interest to committed company members seeking to act responsibly both in their own interests and in the interests of the company.

In regard to the foregoing paragraph we are particularly mindful of recent-time statements repeatedly made by senior members of H.M. Government (and concerning perceived boardroom emolument abuse and excesses) to the effect that "these are not matters for H.M. Government; they are matters to be addressed by a company's shareholders."

Limited company directors are (in the main) subject to election and, as appropriate, re-election by shareholders. On this count alone it can properly be argued that shareholders should - by board disclosure - be made fully aware of 'the cost implications' to their company of their approval (or, indeed, non-approval) of any individual director's election or re-election.

We are especially mindful that the recent-time relevant changes to the S. E. Listing Rules stemmed almost directly from extensive shareholder and public perceptions of abuse and excesses in regard to boardroom emoluments in general and also in regard to the 'believed' inadequate disclosure of such emoluments - and the levels thereof. It seems to us that it is far from logical or prudent - in the present climate - for regulation to rigorously tighten-up and extend the disclosure rules for listed companies and then almost immediately for the Department to seek to lessen or relax already existing statutory rules for disclosures by unlisted limited companies.

In general terms we do not view the deregulatory aspects of the Department's proposals as a useful measure (indeed, rather, the reverse) and we urge that the Department reconsider these aspects of the proposals.

In the event that the proposed Regulations continue to allow almost solely the aggregate cost of directors' emoluments to be disclosed (albeit that such aggregate cost is to be shown/disclosed in three 'categories'), then we are strongly opposed to the dropping of the 'banding disclosure' requirement for unlisted companies. This present disclosure requirement has been - and continues to be - useful to company members in so far as it facilitates the members' awareness of what may be termed 'anomalies' and enables these to be appropriately addressed.

Clearly, in light of the new S.E. Listing Rules, it is senseless to continue the (statutory) 'banding requirement' for listed companies but to remove this requirement from unlisted companies can, in our view, only be justified in the event that the actual emoluments of each individual director are required to be, separately, disclosed. Indeed, the Greenbury recommendation (Your 1.4, Page 3) was to "remove (solely) from companies which make full disclosurethe obligation to show in £5,000 bands".

We are, further opposed to removal of the requirement for the emoluments of the chairman to be disclosed (when he is not the highest paid director). We consider it to be wholly desirable and proper for company members to be notified of the emoluments of the chairman (which could be at a level of some 95% of the emoluments of the highest-paid director, yet in respect of an extremely limited time devoted to the affairs of the company). Under the Department's proposals the emoluments of the chairman will, effectively, be 'hidden from' the members of the company; this is hardly a 'useful deregulatory measure'.

After the most searching considerations, we recommend that the new Regulations require - in the case of a public limited company - disclosure of the emoluments of each individual director separately (in which event all mention of 'banding', 'highest-paid director', 'director operating outside the UK', etc; become pointless). We do accept that the Department has a problem in this regard; the manner (and the extent) of the disclosures we recommend has, admittedly, only very marginal legitimate interest to the public at large but does have very high legitimate (and very pertinent) interest to the members of (the true owners of) the company. On balance - and taking the view that 'Schedule 6 disclosures' are primarily 'aimed at' the members of the company - we feel that consideration of the Draft Statutory Instrument should give emphasis to 'members of the company interests' rather than 'public interests'. See also comments, following, concerning your 2.4, Page 7.

Under your 1.4 (page 4) it is stated that for unlisted companies the objectives are:

to reduce the present disclosure requirements, where this is reasonable;

to ensure that any new disclosure requirements are easy to comply with.

From the viewpoint of the (non-board member) shareholder, it is considered that the proposed reduction of disclosure requirements is unreasonable. To fully disclose each individual director's emoluments is considered to be just as easy to comply with as is 'disclosure in aggregate'.

We now deal with various miscellaneous matters:

item 2.4, Page 7: We agree with the Department that there is no Continuing need for Para. 1(3) of Schedule 6 in its present Format. Indeed, we must question why it was originally drafted (and enacted) in its present form. To disclose 'the amounts' applicable to (2)(a) and (2)(b) separately to members is both logical and desirable and we take the view that this manner of segregated disclosure should now be required in any new Regulations. The amalgamation (aggregation) of part of the amounts applicable to (2)(b) into (2)(a) 'corrupts' otherwise

useful (to shareholders) data.

Under UK law, directors have no statutory or common law - or even any implied - right to receive any remuneration for their services as directors of the company. Accordingly such a right (and the monetary amount thereof) must be resolved/sanctioned (directly or indirectly) by the company members. It has now long been established practice for (authority for) such remuneration to be dealt with in a clause in a company's Articles which is, prudently, separate and distinct from the clause (or clauses) dealing with remuneration payable to directors for 'other services to the company'. We are of the firm view that separate disclosure of remuneration 'for services as a director (of the company)' and 'for other services to the Company (and, if appropriate, subsidiary undertakings)' should be mandatory on the grounds that this segregation is of very legitimate shareholder interest.

Items 2.6 and 2.7, Page 8: Whilst we are in general agreement with the Department's proposals, we do have some unease upon two matters:

1. It seems the Draft Statutory Instrument requires disclosure of share options solely upon the exercise thereof. Whilst it is accepted that the valuation (the 'worth' to a director) can really only be realistically quantified at that stage, we question whether it is the Department's intention that statutory regulation will only require company members to be informed of the numbers of directors' share options when exercised. If this is indeed the Department's intent, then we question the 'reasonableness' (from the shareholders point of view) of such intent.

In the last sentence of 2.7. are the words "is excluded from the definition because at the time when a right to subscribe is granted.....". We are not sure how this 'accords with' the following wording within Article 43 of the Fourth Directive, -viz "the amount of the emoluments granted in respect of the financial year....."

2. Under 2.7 there is a reference to S 259 (2) being "excluded from applying to the definition". (See also Pages 30 and 36). We can see the logic of 'excluding' S 259 (2)(a) but have considerable doubt about the prudence of excluding the whole of S 259 (2).

Item 2.9, Page 8: Is there a need for the Statutory Instrument to define 'market price' somewhat more precisely? Should this be 'closing market price' on the day on which, etc."? Where there is a recognised market, is it the intention that the 'buying price' or the 'mid-price' be used in the relevant Calculation? Should this be clarified/specified?

The last sentence of 2.9 is strongly supported.

Item 2.11, Page 9: Content strongly supported.

Item 2.12, Page 9: In line four, should not the reference be "Rules 12.43 (x)(iii),(iv), and (v)"? In response to the final sentence of 2.12, we are of the view that the proposed new provision is entirely appropriate for unlisted public limited companies. Indeed, were it not included then one would question

the validity of including gains upon share options (and the like) in the Statutory Instrument at all - other than, of course, in regard to the stated object of a 'statutory underpinning' for the S.E. Listing Rules.

It cannot be denied that there will be some additional cost to companies stemming from the proposed new provisions, but such costs can be at least minimised by the issue of realistic (Accounting Standards) 'Valuation Guidelines'. It seems to us that a company's auditor (with such guidelines) should be well able to calculate meaningful valuations - at least of sufficient accuracy for the purpose intended. Indeed, without the auditor being adequately knowledgeable upon 'such valuation' one must question his ability to properly comply with S 235(2) - viz "have been properly prepared in accordance with this Act".

We do not regard the valuation of gains upon share options (and the like) as potentially presenting any greater degree of difficulty than 'the valuation of pension entitlements accrued'.

Item 2.17, Pages 10 and 11: Referring to sub-section (a), a company pension scheme having fewer than 100 members is unsuited to a defined benefit (DB) scheme. However, there are many large unlisted companies which we assume will largely have DB schemes.

Sub-section (b) poses three questions. Transfer values are most probably calculated every week and the law requires an offer of a transfer value to all leavers. Regarding the new minimum funding requirement, this concerns schemes, not individuals. It would not be at all costly or time consuming to calculate the required information because all DB schemes are required to have an actuary.

Regarding sub-section (c), the Method Three calculation would not be burdensome because transfer values need to be routinely calculated in any case. The other methods would not be preferable because they are misleading.

Item 3.1, Page 12: The raising (and the amount of the raising) of the emoluments threshold is supported, as also is the 'part of a group' change. The other stated main changes are opposed (see various earlier comments).

Item 3.9, Page 14: In the event that the final form of the proposed new Regulations do not require the, separate, disclosure of each individual director's emoluments, then we must recommend the following - minimum - separated disclosures:

- (a) The chairman
- (b) The highest remunerated UK based director (where not the chairman).
- (c) Each director whose remuneration exceeds that of the highest remunerated UK based director.

Items 4.2 and 4.3, Page 15: We are of the strong view that the present requirement to disclose 'emoluments waived' should be Retained. This is no less necessary or desirable in present time than when the requirement was originally introduced. To fail to retain this (considered to be essential) requirement would result in company members potentially being misled - maybe very significantly - especially in circumstances where there are appreciable waivers for a number of consecutive years. In such circumstances, potential future boardroom costs would be "hidden from" both present members of the company and intending

members of the company; this surely a retrograde step and most certainly not a useful deregulatory measure.

Item 4.4 to 4.11, Pages 15 to 17: The Department's proposals are supported and are considered to be adequate.

Item 4.15, Page 18: We are in agreement that it would be pointless to continue with the disclosure requirement as presently contained in the last three lines of Para 8(2)(b) and question how this disclosure was ever logical! We do, however, take the view that separate disclosure should be required in respect of Para 8 (2)(a) and Para 8 (2)(b). See, earlier, comments relating to Item 2.4, Page 7.

Item 4.16 and 4.17, Page 18: It is our view that the retention of this provision is essential.

Item 4.18, Pages 18 and 19: We cannot agree with the Department's view with regard to the deletion of Para 10(3). Having particular regard to the inclusion (and wording of) Para 10(2)(c) - and its potential relevance to Para 8 'amounts' - we consider the retention of Para 10(3) should have further consideration.

We are in agreement with the deletion of Para 13 (3)(c).

Item 5.1 to 5.12, Pages 20 to 22; We are of the opinion that our earlier comments herein adequately respond to the content of Pages 20 to 22.

Para 1 (2)(b)(ii), Page 29: We question whether the perpetuation of the three words "management of the" (both here and later in the Draft Regulations) is desirable. It has now long been established practice for company Articles to give directors power to sanction and determine the amount of remuneration payable to any of their number for 'any services' outside 'the scope of the ordinary duties of a director'. Such 'any services' may well include services which are arguably outside the scope of definition of "management of".

Para 1 (3)(d), Page 29: Having regard to the drafting of Para 1(3) as a whole, we have difficulty in understanding the need for, or the prudence of, perpetuating the inclusion of the last four words of Para 1 (3)(d). Same comment applies to later, similar, inclusions of these four words.

Para 1(4), Page 29: See earlier comments relating to Items 2.7 and 2.8, Page 8.

We urge the Department to give serious reconsideration to the present proposals within the Draft Statutory Instrument - especially the deregulatory aspects thereof - this to take into account the observations made in this submission; which observations we will be pleased to amplify verbally at your behest.

Yours sincerely,

Donald B Butcher
Chairman