ICGN Executive Remuneration
Principles and Policy Disclosure Guidance
The ICGN is a global membership organisation of around 550 leaders in corporate governance based in 50 countries with investors collectively representing funds under management of around US$18 trillion. The breadth and expertise of ICGN members from investment, business, the professions and policymaking extends across global capital markets and our mission is to raise standards of corporate governance worldwide. For more information about the ICGN contact the Secretariat by telephone: +44 (0) 207 612 7098, email: secretariat@icgn.org or visit www.icgn.org.
Preamble

There are few subjects in finance and corporate governance that receive more consistent attention than executive remuneration. Certainly, few subjects have generated as much criticism over recent years. So important is the topic that regulators, legislators and the general public have taken a keen interest in this area. These have forced some dramatic changes in how companies and investors view the importance of executive remuneration. There are many different constituencies with a legitimate interest in executive remuneration, each of whom may view the same issue in very different contexts, which, ultimately, leads to some of the tension surrounding this topic. From an ICGN perspective, the primary objective of companies is to generate sustainable shareholder value over the long-term. We believe that remuneration policy should reflect this objective throughout its design and implementation.

The ICGN is a worldwide organisation focused on the role of investors in promoting good corporate governance, globally. Its members span the globe in terms of geography, as well as perspective, and represent assets under management of approximately US$18 trillion. Long-term investors are united in their overarching views regarding remuneration practices and the need for significant improvement in the areas of long-term alignment of their interests with the interests of a companies’ management. This includes clear and transparent disclosure, coupled with basic fairness in the use of shareholders’ capital to retain and incentivise management.

Investors have a distinct role in relation to executive remuneration. Investors have a fiduciary responsibility as well as a strong economic interest in remuneration. No aspect of corporate governance touches as many drivers in terms of performance, risk and incentive, or is ultimately more critical to long-term alignment of interests. However, investors are not, typically, insiders and in almost all cases are not in a position to dictate executive remuneration practices.

The ICGN offers these Principles and Policy Disclosure Guidance in an attempt to accomplish several goals. First and foremost, we wish to provide a consistent perspective focused on major aspects of remuneration policy and practice that will assist companies in better understanding long-term shareholders’ views. From a macro standpoint, investors are focused on efficient capital allocation and effective risk management; remuneration is critical in this regard.

We recognise that remuneration practices, as well as regulation, may differ between markets and even from company to company. We believe this is completely appropriate. Overly complex structures or complicated incentive schemes are not necessary and are undesirable. In some markets, financial remuneration is viewed as only one, and perhaps not the primary, component of a more holistic view of factors that motivate and align employees. The key is to help identify the method(s) companies are using to motivate and align employees and to communicate this clearly to shareholders and other constituencies.

This document is organised by topic. Each section provides the ICGN’s Principles related to the particular topic and, separately, Policy Disclosure Guidance. The Principles and Policy Disclosure Guidance are distinct but complimentary and should be evaluated as a whole. The Principles provide minimum standards the ICGN believes are critical in the practical steps to setting, evaluating and overseeing remuneration programmes. As such, they are oriented towards structure. The Policy Disclosure Guidance is intended to assist companies in a process to develop and disclose a well thought-out policy related to remuneration.
Certain fundamental policy objectives and basic levels of appropriate alignment must be achieved regardless of the circumstances. These Principles and Policy Disclosure Guidance are intended to provide just this type of guidance. Balancing the obvious needs of companies related to flexibility in remuneration structure and the just as obvious need and desire of long-term investors for appropriate alignment and efficient use of capital. Recognising that companies may achieve these goals through some combination of financial incentives and other forms of alignment, the Principles and Policy Disclosure Guidance focus on the desired result as much as the methods used to obtain that result. This is intended to provide flexibility such that the guidance is useful across many markets yet addresses the detail needed in some markets for evaluating remuneration programmes.

A second goal of these Principles and Policy Disclosure Guidance is to provide companies with a comprehensive discussion of major policy topics that investors seek to understand when evaluating a company. This information is critical for long-term shareholders in making decisions regarding a company, including those related to investment, exercising voting rights and effectiveness of board directors. In recognition that companies’ approach to accomplishing major policy objectives may differ between regions and other circumstances, the Policy Disclosure Guidance is intended to be as universal as possible. It also aims to set a minimum standard for what companies should explain to their shareholders. The Principles and Policy Disclosure Guidance are oriented more towards helping companies articulate a rationale that supports a particular remuneration practice or structure, as opposed to strict rules. Transparent and clear disclosure must provide a solid foundation for the relationship between companies and their long-term shareholders.

Due to the complex nature of executive remuneration, as well as its paramount importance to companies and shareholders, this document provides extensive detail. While each section or policy topic may be read stand-alone, it is critical that companies understand the inter-related nature of the various elements of their remuneration programmes. This understanding needs to extend across their approach in design, implementation and disclosure of remuneration arrangements. It is not uncommon for investors to identify one or more strong points regarding a plan that are then undermined by poor design in other aspects of the remuneration programme. Thus, the detail in this document is necessary in an attempt to address the remuneration programme in its whole.

A number of important topics regarding executive remuneration are likely to remain under intense scrutiny. As we have witnessed, remuneration is fair game for additional legislation and regulation; this may be a mixed bag in terms of its effectiveness and unintended consequences. It is imperative for companies and long-term shareholders to collaborate more effectively in the area of executive remuneration. This will help to demonstrate our collective ability to manage efficiently this tool with minimal negative side effects, while maximising the benefits. This collaboration should take into account the delicate and often difficult balance between the primary goals of remuneration programmes and the other, not insignificant, contexts in which it is perceived.

It is the sincere desire of the ICGN and its membership that these Principles and Policy Disclosure Guidance provide clear disclosure from investors to companies regarding the ICGN's perspective on executive remuneration, together with sparking an increasingly collaborative and healthy relationship and dialogue on this subject.
1.0 The Remuneration Committee

1.1 Role

Principle

The remuneration committee is responsible for all aspects of the remuneration arrangements. The committee should take ownership of devising, drafting and implementing these remuneration arrangements.

The committee has the responsibility to integrate all components of remuneration into a cohesive structure. This structure needs to be aligned with, and support, the strategic objectives of the company, which may be both short-term and long-term in nature.

Guidance

Policy disclosure guidance to include:

- The role and responsibilities of the remuneration committee, including its authority and interaction with the full board, consultants and management in regard to designing, implementing, monitoring and evaluating the executive remuneration arrangements.

- How the committee will monitor and evaluate the effectiveness of the arrangements over time, integrate the concept of risk in to the remuneration programme and disclose to shareholders the results of this analysis on a periodic basis.

1.2 Composition and structure

Principle

Ideally, the committee should comprise entirely independent non-executive directors or supervisory board members. However, depending on best practice in the relevant market, a clear majority of its members should be independent. In particular, the chairman of the committee should be independent.

Special care should be taken to ensure that the committee, as a whole, has adequate qualifications, experience and expertise, together with diverse perspectives.

The committee should consist of at least three members.

Current CEOs of other companies may have a potential conflict or bias in setting their peers’ remuneration, yet they can also have valuable insights into remuneration issues. Committees should consider carefully the role of present or former CEOs in the process of formulating remuneration arrangements and should recognise that many investors prefer a strict limit on the number of CEOs on the committee (such as one), or an outright ban.

Guidance

Policy disclosure guidance to include:

- How the committee make-up is established, which should extend to the process for appointing members and how the committee evaluates its effectiveness. This should include how both director evaluation and committee evaluation is used in the nomination and re-nomination process, whether the committee will rotate, periodically, its membership
and how the committee maintains the appropriate skill sets, perspectives and independence.

- Whether the remuneration committee is chaired by an independent and objective board member. The policy should endorse this concept, include its definition of independence and provide a summary of the board’s selection process for the Committee’s chairman. It should also include the policy and procedure for ensuring that appropriate succession planning is in place.

- The committee’s policy on meetings, including the minimum number of times/frequency the committee may meet and the circumstances in which the committee may act by written consent. In cases where the committee may act by consent, which should be limited, the policy should specify how the committee will ensure full discussion and review of pertinent information.

1.3 Support

**Principle**

In order to fulfil its duties and obligations, the committee should be permitted to employ any necessary resources, such as remuneration consultants. The committee should control all aspects of the engagement of any resources that are employed, including their selection, terms of engagement and eventual release.

The committee should meet regularly with the company’s senior risk officer(s), or others as may be appropriate, to help fully integrate the concept of risk into the remuneration programme.

**Guidance**

Policy disclosure guidance to include:

- How the committee will ensure that it receives all complete and relevant information needed to support its role and responsibilities. This should extend to the committee’s policy regarding the use of external advisors and specialist training providers and how it ensures that they are independent.

- Any potential role that management may play in executive remuneration, such as the CEO’s role in recommending design characteristics, should be explained. For example, the degree to which the committee relies on management recommendations in identifying specific performance metrics that may be included in the remuneration plans.

- How the committee will provide for continuing education of its members relating to remuneration matters.

1.4 Conflicts of Interest

**Principle**

It is important that special care be taken to avoid conflicts of interest among committee members and between the committee and its advisors, which could impair their independence. For example, an advisor to the committee would not be considered independent if it is also engaged by the company’s management.

Disclosure should include any consulting or other fees paid to remuneration consultants for work unrelated to remuneration plan work.
Guidance

Policy disclosure guidance to include:

- The committee’s approach to identifying and avoiding conflicts of interest that may be present amongst its members and also between its advisors and the company.

- How the committee will ensure the effectiveness, objectivity and independence of its contract negotiations, including who will be responsible for this role, and if the committee will use any outside resources to facilitate negotiations.

1.5 Communication

Principle

It is the committee’s responsibility to maintain appropriate communication with shareholders, either directly or via the board. This includes a responsibility to provide full disclosure regarding the remuneration arrangements, as well as maintaining a dialogue and seeking input from shareholders as appropriate.

Guidance

Policy disclosure guidance to include:

- The company’s policy on communication with shareholders and how the committee ensures that it captures shareholders’ views. This may include the role of an advisory vote on executive remuneration policies as one means of facilitating communication with shareholders.

2.0 Remuneration Structure

2.1 Fundamental Design

Principle

Well-structured remuneration arrangements should be aligned with shareholders’ interests of creating and sustaining long-term shareholder value. They should help foster a culture that is also aligned with the company’s strategic objectives. Accordingly, the ICGN is generally opposed to “guaranteed” elements of remuneration, while recognising that this does not apply to retirement benefits (which is discussed elsewhere).

An effective remuneration structure is only part, albeit an important part, of the employment relationship that will be entered into with an executive. That relationship should encourage the right behavior, while also helping to recruit and retain successful employees and to provide the right level of reward for good performance. It will also ensure that only the necessary level of remuneration is paid and that poor performance is not rewarded.

When designing and implementing remuneration arrangements, the remuneration committee should be mindful of the role of remuneration within the larger context of employment. Does it, for example, encourage the individual and the organisation to behave with fiduciary loyalty to its shareholders? Does it ensure that the structure will not encourage excessive risk taking, either by an individual or by a group?

When reviewing a company’s remuneration arrangements, shareholders should be able to understand, clearly, how their management is being incentivised to perform and how much this may cost.
Remuneration arrangements should be structured with an appropriate balance of short-term and long-term incentives. This ratio may vary based on market conditions and the specific circumstances of the company. It is incumbent upon the committee to evaluate, carefully, all relevant information in establishing the desired mix of short-term and long-term remuneration elements, together with updating this evaluation over time to ensure that the plan evolves to meet the company’s changing situation.

The remuneration committee should establish goals for total remuneration, as well as each major sub-component of the plan. This should be done in the context of a total compensation analysis. Committees may use tools, such as tally sheets, to gain a complete perspective of the remuneration programme. This will help the committee to evaluate the overall mix of remuneration and determine how to integrate the various elements. Remuneration levels may take into account relevant benchmarks and market conditions but these criteria should not be used exclusively to justify levels of remuneration or plan design. Too much reliance on relative peer analysis leads to unjustified escalation in executive pay. Each plan should be tailored to the unique circumstances of the company as well as the responsibilities of the position(s) in question and the experience and expertise of the individual.

**Guidance**

Policy disclosure guidance to include:

- The company’s philosophy regarding total remuneration and the relative mix of base salary, short-term incentive, long-term incentive and retirement arrangements. This section should include the following specific points:

  - How the committee conducts total remuneration analysis (such as the use of tally sheets) and any other tools that may be employed in plan design and evaluation. This will ensure that the structure is fair and effective (such as the concept of internal pay equality versus a highly competitive “star performer” internal pay structure).

  - The company’s policy regarding overall remuneration targets and how the committee will determine these levels and monitor them against the plan. This should include targets related to total remuneration as well as key elements of the plan.

  - Specific attention should be applied to identifying and discussing relative strengths and weaknesses of the various forms of remuneration in relation to the company’s strategic objectives and situation.

  - The role of risk in the context of the executive remuneration arrangements, which should include both a defensive perspective: how the committee ensures potential remuneration does not incentivise excessive risk, and an offensive perspective: how the arrangements are designed to incentivise appropriate risk and aligns the interests of management with those of long-term shareholders. Discussion of risk should include how the company’s risk appetite relates to compensation potential. Disclosures should describe the roles of those with responsibility for monitoring risk, incorporating how the company addresses any potential conflict of interest, if any, in the event that their compensation is at risk.
In relation to risk management, for all forms of incentive remuneration, the policy should address how the committee will mitigate or eliminate the potential for unintended drivers or consequences. This should include a discussion of how incentive plans can be initially structured and continually monitored to mitigate unintended drivers. The policy should also discuss the company’s provisions for recapturing unearned incentive remuneration (claw back or disgorgement policies, for example). As a related topic, the policy should discuss how the company will minimise the potential for manipulation of performance related metrics, and monitor performance for potential fraud (internal risk controls, for example).

The ICGN suggests a three-prong approach to addressing the issue of unintended drivers or consequences related to incentive remuneration.

(Phase one) The policy should address these issues in plan design and implementation; considering such factors as the relationship between short-term and long-term performance measures and the differing accounting measures (and the potential links to drive behaviour) that are key in each of the performance metrics utilised.

(Phase 2) The policy should address the role of the committee and internal control with regard to plan oversight and, specifically, to monitor the integrity and effectiveness of the performance metrics. This should have a qualitative aspect (monitoring for effectiveness and link to ultimate performance) as well as a quantitative (monitoring for abuse).

(Phase 3) The policy should provide significant flexibility for the company to recoup (claw back) incentive remuneration in circumstances where it is later determined to have been unearned. These policies should extend beyond the basic protections in law, as may be applicable, and should include circumstances beyond intentional misconduct.

The company’s rationale for the desired approach (remuneration mix) including differences in the relative mix of remuneration between various levels of executive management.

The degree to which the company may utilise peer comparison analysis or benchmarking, and how the committee will ensure these factors do not dominate the justification for plan design or remuneration levels. This should also include the company’s procedure for selecting relevant survey data, the rationale for the methodology utilised and its process for disclosing the constituents of any survey data used.

The extent of, and circumstances that may surround, any discretion, if at all, that is afforded to the remuneration committee.

2.2 Base salaries

Principle

Owing to the many variables that need to be considered when deciding on appropriate salaries and any increases, peer comparison information should be used with caution. When setting and reviewing base salaries for executives, the remuneration committee should be mindful of salary levels and any merit increases that have been awarded across all employees.
Guidance

Policy disclosure guidance to include:

• The remuneration committee should disclose the extent to which comparative peer information has been used when determining base salary levels. Any increases in base salary should be justified by a supporting statement. In addition, the salary level provided to a newly appointed executive should be explained. Overall, the policy should discuss any changes to base salaries of executives in the context of any changes to salary levels across all employees.

2.3 Short-term incentives

Principle

Generally, it is appropriate for short-term incentives to be reliant upon annual performance measures. Objectives should be set and recorded at the beginning of the performance period. Companies should consider the circumstances in which short-term performance measures may be adjusted, including the process and timing of disclosure of these actions. Short-term performance measures should not be adjusted, except in very limited circumstances, and never after the performance period has past. Companies should avoid performance periods shorter than one year. For further discussion on performance, see the section entitled ‘Performance-based methodologies’.

Guidance

Policy disclosure guidance to include:

• Insight into the company’s intended forms of incentive remuneration, including the types of measures that will be used to drive incentive remuneration. The role that an appreciation of risk plays in these remuneration arrangements should also be disclosed. This section should include the following specific points:

  - The company’s philosophy for the major components of incentive remuneration (e.g. annual vs. long-term, etc.), including the strengths and weaknesses of each in general and in relation to the company’s strategy and situation.

  - For all forms of incentives, the policy should address how the company will amend incentive plans during their terms, if at all, including the need for shareholder approval of plan amendments. This should provide justification for the policy position, the basic process the company would use to consider such amendments and how the company will disclose such amendments, including justification for the individual amendment(s) at the time they are made. The policy should also address time periods within incentive plans in which amendments may be allowed (permitting amendments only in the first quarter of a one-year plan for example), and if there are caps on the overall portion of the incentive plan that may be affected or the elements of the plan that may be amended (permitting amendments only to the threshold but not the types of metrics, for example).

  - The company’s policy on providing incentive pay related to transactions or other corporate events. This should include a definition of what constitutes long-term and short-term incentive-related activities and what is a routine part of the job. For example, would the policy permit debt reduction targets to form part of an incentive award, or would this be considered a routine part of an executive’s duties?
2.4 Long-term incentives

Principle

The long-term incentive component of an individual’s total remuneration may consist of an appropriate mix of cash and/or equity and equity like tools. The equity tools may include share options, restricted shares, and/or stock appreciation rights, for example.

A remuneration committee will need to consider the target dilution levels, cumulative dilution to date and projected run rates over a multi-year period, together with actual run rates over previous years. This consideration should extend to the methodology that will determine the appropriate dilution, the run rate and the effectiveness of the plan over time, including its impact on long-term value creation. For the ICGN’s Principles on performance, see the section entitled ‘Performance-based methodologies’.

Any share-based remuneration plan and subsequent potential dilution of shareholders should require prior shareholder approval. Companies should also seek shareholder approval regarding key amendments to long-term incentive arrangements, including changes to performance targets.

Long-term incentives should have vesting terms that are consistent with the company’s capital allocation and investment horizon. As a general rule, vesting of long-term incentives should be a minimum of three years.

The ICGN is opposed to share repurchase plans that are designed, strictly, to offset equity plan dilution. Share repurchase plans should be an integral component of the company’s capital allocation decision and not to simply satisfy its remuneration arrangements.

Equity grants should be scheduled at regular (annual) intervals. Companies should adopt and disclose a formal pricing methodology for establishing the exercise price of grants. For example, this may entail a policy of establishing the exercise price at the average closing price of the company’s common shares over the previous four-week period. In no circumstances should boards or management be allowed to backdate grants to achieve a more favourable exercise price.

Equity exposure can be achieved in a variety of ways and may include direct personal ownership, forced ownership by way of shareholding guidelines or through certain remuneration arrangements. Each individual member of a company’s management team or board should be prohibited from hedging, or otherwise manipulating, any financial exposure that they may have to any of the company’s equity.
Guidance

Policy disclosure guidance to include:

- The company’s philosophy regarding equity-based remuneration, including the company’s objectives in utilising these tools, the relative strengths and weaknesses of each type of equity tool in relation to the company’s business objectives and situation. This section should include the following specific points:
  
  - For each form of equity and equity-like remuneration, the policy should address the company’s overall objectives in utilising these tools. Following this, the policy should address the efficiency with which these tools can accomplish these objectives and provide consideration of alternative approaches. For example, the policy should examine the relative advantages of equity ownership obtained through outright purchases versus share options, restricted shares, and equity-like grants under the remuneration arrangement.
  
  - The equity plan should also include a maximum annual limit on individual participation and the planned distribution ratio of awards between senior executives and other employees.
  
  - In cases where a company may utilise various forms of equity, the policy should address the relative values of each in the context of the remuneration arrangement, including how the company would determine a ratio of “value” between various equity tools. For example, if a company intends to shift emphasis in the equity component of its remuneration arrangement from share options to restricted stock, would it utilise a ratio (1-to-4 or 1-to-3 for example) in determining the grants and, if so, how would the ratio be determined?
  
  - The committee’s philosophy regarding award structure, including the size, timing, valuation and terms of grants. This should include whether the company would use any forms of “mega-grants” and, if so, how they fit into the long-term objectives of the arrangements.
  
  - In regards to valuation, the policy should discuss the company’s approach to establishing the intended value of awards, including the expectation for performance vesting, the performance levels that should be achieved to obtain specific levels of “value” in awards and, also, the approach to establishing grant size (specified value target or specified share amount for example). For the ICGN’s Policy Disclosure Guidance on performance, see the section entitled ‘Performance-based methodologies’.
  
  - The policy should also include the company’s methodology for grant-date pricing. If the company intends to time equity grants to take advantage of pending news or other information, the policy should fully explain the rationale for this approach and provide the company’s process for disclosure of actions related to grant timing.
  
  - The policy should explain the treatment of dividends, dividend equivalent rights or other cash flow and corporate actions in relation to the equity component of the arrangement.
  
  - The means by which participants will be permitted to monetise equity and equity related grants, which should extend to the potential impact on the goals of the remuneration arrangements.
Performance-based methodologies

Principle

The ICGN supports, strongly, the use of performance measures that govern the vesting of short-term and long-term incentives. This may include indexing or premium pricing methodologies and other performance criteria such as key operational metrics. Indexing and premium pricing methodologies are forms of performance-based vesting. Indexed stock options have an exercise price that is relative to an appropriate index of comparable companies such that the exercise price is adjusted to reflect the performance of the index. Premium priced options have an exercise price set at a premium to the current market price at the time they are granted.

The ICGN does not support time accelerated vesting as a legitimate or desirable performance vesting methodology (time accelerate vesting is a methodology that accelerates the vesting of an equity award based upon meeting some pre-determined criteria or performance hurdle. Under time accelerated vesting, the equity awards will vest even if the performance criteria for acceleration are not met, the performance criteria is tied only to the acceleration of vesting).

Performance metrics should be consistent with the creation of sustainable long-term value and achieving superior performance. They should also support the strategic objectives of the company.

For long-term incentives, it is expected that performance hurdles be established that measure sustained performance over long periods that span multiple accounting periods. Care should be taken to mitigate potential unintended negative incentives that may be associated with performance measures. For example, poorly constructed performance measures could provide an opportunity to manipulate short-term accounting measures in order to meet performance goals.

Performance hurdles should be designed to minimise or eliminate potential adverse incentives. This may be achieved in a variety of ways and could include the following:

- utilising multiple performance metrics with some offsetting drivers that would mitigate the ability to manipulate accounting measures or drive poor business decisions to reach goals (for example, if revenue growth is a desired performance target, it should be accompanied by a profitability or margin measure to ensure that the “incentive” is not to increase revenue at any cost);
- adopting performance methodologies that encompass multiple periods, such that no opportunity to manipulate one accounting period over another exists (channel stuffing or expense shifting for example);
- utilising varied performance metrics over time in an effort to evolve with the company’s situation;
- adopting a “claw back” policy that provides for the re-capture of performance-related pay in cases of re-statement or fraudulent reporting if either resulted in the vesting of an award;
- providing the remuneration committee with downward discretion should it be felt that the achievement of the set performance hurdles does not reflect an improvement in the underlying performance of the company; and
• limiting the level of payout at threshold or avoiding cliff-edge vesting given that this can encourage unnecessary risk taking.

Re-testing or re-pricing represents a potential fundamental shift in the relationship between long-term performance and remuneration. In its basic form, such actions undermine, materially, this relationship by altering the impact of poor performance on plan participants, thus altering the risk reward profile of the plan and the alignment with long-term shareholders. The ICGN does not favour ‘re-testing’, ‘re-pricing’ or the granting of additional time to meet performance hurdles should they not be achieved within the pre-determined time frame. In cases where companies wish to re-test or re-price unvested awards, this should be done only with explicit shareholder approval.

Guidance

Policy disclosure guidance to include:

• The committee’s philosophy on performance. A company should disclose the performance metrics and target ranges that are used to govern the size of awards granted and those that govern the levels at which these awards vest, including the calculation methodology for each performance metric. The length of performance periods should also be disclosed. In addition, rationale should be provided that justifies the selection of these performance metrics as drivers of long-term sustainable value for shareholders.

• The performance metrics and target ranges that will be used to determine the vesting of short-term, intermediate-term and long-term components of the arrangements; including the rationale for these metrics and targets. This should also include the company’s policy on using peer comparisons versus company specific measures and how the arrangements will balance between these two. The policy should consider the role that these play in the achievement of long-term total shareholder return.

• How the committee will scale incentive awards to be consistent with the remuneration philosophy and the company’s performance objectives. For example, will the committee use sliding scales to set performance awards versus cliff hurdles, and what level of award would be set for median performance?

• If the company intends to utilise any adjusted performance measures (non-GAAP/IFRS or not conforming to accepted accounting principles), the policy should contain the following, as a minimum:

  - A detailed rationale for the use of adjusted performance measures. This should be directed at each level and discuss the positive and negative effects of this practice. It should also include the role of the committee in approving the proposed adjustments and how it monitors the impacts of this approach.

  - A line item reconciliation for each metric to GAAP or IFRS, clearly demonstrating the magnitude of the adjustment for each measure. In cases where benchmark comparisons may be made to similarly adjusted measures, this should be disclosed. However, reconciliation should still be provided to compare against a recognised accounting standard.

• How the company will achieve a consistent approach to incentive plan measurement. The policy should disclose the formulae and methodologies associated with performance metrics and targets; together with providing adequate
information for investors to assess the quality of the performance plan.

- The company’s policy on any non-financial performance metrics that may be utilised in an incentive arrangement. This should include the rationale for utilising non-financial metrics, their target weight in the overall plan and how the committee will ensure accuracy in measurement of non-financial metrics. For example, this may include the committee’s commitment to use quantifiable measurement methodologies to the greatest degree possible, or using a proxy to capture the desired goal if possible. To illustrate, if a company wishes to incentivise customer satisfaction, it may commit to use quantifiable and consistent survey methodologies to capture the desired goal, and it may utilise easily identifiable metrics, such as retention and complaints, to help determine levels of customer satisfaction. The degree to which any non-financial metrics may be measured by subjective evaluation should be clearly explained. The policy should include how any non-financial metrics relate to company performance and how any unintended consequences may be mitigated.

- The policy should contain the company’s philosophy regarding the dilution of existing shareholders. This section should include:
  - A comprehensive plan covering dilution associated with all equity remuneration arrangements, addressing the intended life of individual arrangements, including optimal yearly and long-term run rates. The dilution plan should provide the rationale for projected run rates, and how the company will evaluate the effectiveness of the dilution plan over time. This may extend to providing and justifying a cost of management ratio (COMR) that captures all elements of remuneration arrangements.
  - The plan should contain a detailed description of how the company will treat equity grants that expire or are not earned through vesting requirements, including if these awards would be returned to the pool of “eligible” equity under the plan.
  - If the company’s plan(s) permits re-pricing of any kind (assuming shareholder approval), the company’s policy regarding dilution should take re-pricing into account.
  - If the company plans to repurchase equity through share buyback programmes to reduce dilution from equity remuneration plans, the policy should articulate how the repurchase decision is made in relation to other capital allocation decisions. The ICGN is opposed to share repurchase plans that are designed solely to offset equity plan dilution.

- In relation to re-testing, re-pricing or the granting of additional time to meet performance hurdles, it is incumbent upon companies to provide clear policies and to consider the serious concerns of shareholders in regards to this topic. The ICGN’s strong preference is that plans prohibit re-pricing in any form and that this fact be clearly communicated to participants in an effort to manage expectations. In cases where companies wish to re-test or re-price unvested awards, the ICGN believes this should be done only with explicit shareholder approval.
2.6 Change in control

Principle

In the event of a change in control, or other corporate event where a loss of employment is realised, only pro-rata performance criteria that reflect a real measure of underlying achievement should be awarded. The ICGN is opposed to a blanket acceleration of the vesting of equity instruments based on corporate events. The remaining long-term incentive awards should be subject to the long-term success of the new entity, not the execution of the transaction.

Guidance

Policy disclosure guidance to include:

- If the company’s plan(s) permits re-pricing of any kind (assuming shareholder approval), the company’s policy regarding dilution should take re-pricing into account.

- If the company plans to repurchase equity through share buyback programmes to reduce dilution from equity remuneration plans, the policy should articulate how the repurchase decision is made in relation to other capital allocation decisions. The ICGN is opposed to share repurchase plans that are designed solely to offset equity plan dilution.

2.7 Post employment and other benefits

Principle

Post employment and other benefits include pensions, healthcare and other benefits that may be provided during and after employment. Should companies utilise any of these forms of remuneration, care should be taken to integrate these structures within the overall philosophy and structure of the total plan.

Post employment and other benefits can give rise to significant liability for the company and may represent significant portions of the total value of the remuneration arrangements. As such, the alignment and incentive characteristics of these elements of the remuneration arrangements can have a material impact on its overall effectiveness. As a general rule, benefits may detract, significantly, from the performance and alignment qualities of remuneration plans, while, arguably, having some value to attract and retain key employees. These competing interests must be balanced in the best long-term interests of shareholders.

- The company’s philosophy regarding the dilution of existing shareholders. This section should include:
  - A comprehensive plan covering dilution associated with all equity remuneration arrangements, addressing the intended life of individual arrangements, including optimal yearly and long-term run rates. The dilution plan should provide the rationale for projected run rates, and how the company will evaluate the effectiveness of the dilution plan over time. This may extend to providing and justifying a cost of management ratio (COMR) that captures all elements of remuneration arrangements.
  - The plan should contain a detailed description of how the company will treat equity grants that expire or are not earned through vesting requirements, including if these awards would be returned to the pool of “eligible” equity under the plan.
Guidance

Policy disclosure guidance to include:

- The parameters by which the company will utilise post-employment and other benefits as forms of remuneration, including all forms of healthcare cover and any deferred remuneration arrangements or retirement benefits.

Companies should disclose all material aspects of the remuneration plan, which includes post employment and other benefits. Companies should disclose the existence of all retirement programmes for executives, noting clearly any supplemental benefits or sweeteners provided beyond those offered to other company employees (such as above market earnings on account balances or additional years of service credit, for example). Disclosures related to defined benefit pension programmes should include an estimate of the actuarial present value accrued during the applicable year and an estimate of the expected benefit at normal retirement age. These disclosures should be specific to each individual executive covered in the disclosures.

If any portion of post employment benefits (retirement, healthcare, other benefits) are unfunded, the company should provide adequate detail as to the potential liability to the company under these programmes. This section should include:

- Any limitations placed on retirement or other benefits, including amounts and time period for executives.
- Eligibility of family or other beneficiaries to receive benefits.
- The company’s policy on benefit calculations and how the executive plans are consistent with all other plans. Any differences, such as the basis for calculating eligible income and additional multipliers available to executives, should be explained.
- A general list of appropriate types of benefits that may be included in future remuneration plans.
- The company’s policy and procedure for valuing benefits, including the rationale for the method and why it is considered accurate.

2.8 Shareholding guidelines

Principle

Shareholding guidelines and requirements should be an integral component of a company’s equity plan and overall remuneration philosophy. Ownership guidelines, often expressed as a multiple of salary, serve to align the interests of the management team with the interests of long-term shareholders.
The guidelines should require significant ownership levels over an appropriate period of time. Generally, holding requirements require executives to hold significant portions of equity grants for extended periods, which should include requirements to hold some portion of grants for a fixed period of time after separation (such as retirement or other event in which employment is ceased).

Individuals subject to shareholding guidelines should be prohibited from entering into derivative contracts in order to hedge against their exposure to the company’s shares.

Guidance

Policy disclosure guidance to include:

- For each level of management, the company’s approach to ownership and retention guidelines, including the objectives, ownership levels targeted over specific time frames, periods in which retention would apply (including post retirement), and how it will be monitored and enforced. Long-term investors are interested, particularly, in the role of equity ownership in the overall context of the remuneration plan.

The expected value of the alignment from equity ownership, most specifically in relation to long-term investors, and how the role of equity may evolve over time. For example, are there levels at which the value of equity in the remuneration plan reaches a saturation point and the incremental alignment and motivation is mitigated?

The ICGN supports management buying shares in the market rather than waiting for share-based remuneration awards to vest. Assurances should also be disclosed that prohibits hedging, together with how such a policy is monitored.

3.0 Contractual Provisions

3.1 Employment contracts, severance, change in control

Principle

Contracts, employment agreements, severance and change in control arrangements should be strictly limited. As a rule, these arrangements should not affect, adversely, the executive’s alignment of interest with shareholders or their incentive to pursue superior long-term value.

Employment contracts should not extend longer than one year and should not be open-ended or renewed on an “automatic” basis. Where it is deemed essential that contracts run for a multi-year period for the purpose of recruitment, these should revert to a one-year contract after the initial contract period. Within this context, boards should seek to minimise the cost of post-employment generally.

It is preferred that employment arrangements do not provide guaranteed raises, bonuses, or other incentives such as equity grants. Guaranteed provisions can have a negative impact on the alignment and incentive characteristics of the remuneration arrangement.

Severance payments should be limited to situations where the company terminates employment without cause, death, or disability.

Companies should not compensate executives for any excise or additional taxes payable as a result of any employment, severance or other agreement.
Guidance

Policy disclosure guidance to include:

- Disclosure of the existence of all employment agreements, severance arrangements, change in control agreements and any other contractual agreements with key executives. Disclosure should include a description of the agreements, which contain sufficient detail of all material factors such that shareholders have a complete understanding of their terms. Companies should provide estimated payments under specific scenarios such that shareholders can determine the potential payouts under each agreement. This section should include:

  - A definitive statement of the company’s philosophy on employment agreements, severance arrangements, change in control contracts and any other contractual employment or benefit-related arrangements.

  - Justification for the use of these arrangements and be specific to the company’s circumstances, while also being consistent with the overall purpose of the remuneration arrangement. Special care should be taken to explain the rationale for these arrangements within the overall context of a performance-based plan, including how the arrangements impact its alignment and incentive characteristics.

  - Disclosure of the overall parameters of how benefits, severance and change in control provisions will be used. These should include specific detail regarding the positions within the company that may receive these provisions. As a minimum, disclosure should extend to the maximum periods covered by the arrangements; the circumstances by which the arrangements will be reviewed, renewed or eliminated, and;

- a clear description of the company’s philosophy related to key terms of the arrangements, such as triggering events, and how the company intends to define terms such as termination for cause. Companies should also disclose where investors can view the entire text of the applicable agreements or contracts.

4.0 Annexes

4.1 Acknowledgements

The ICGN is grateful for the work of the members of the Remuneration Committee in developing the principles and policy disclosure guidance. As with all ICGN projects, the members of the Committee are acting in a personal capacity. Affiliations below are noted solely for reference and interest. This includes:

Ian Burger, Newton Investment Management Ltd, UK (Co-Chair)
Ted White, Knight Vinke, USA (Co-Chair)
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The ICGN and the Remuneration Committee are also grateful for the comments provided by ICGN members throughout the consultation process.
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ICGN Guidelines

ICGN Guidance on Political Lobbying and Donations (2012)
ICGN Model Contract Terms Between Asset Owners and Managers (2012)
ICGN Corporate Risk Oversight Guidelines (2010)
ICGN Non-executive Director Remuneration Guidelines (2010)
ICGN Global Corporate Governance Principles (2009)
ICGN Securities Lending Code of Best Practice (2007)