Mercer

FTSE350

UK board remuneration handbook 2023

Executive and non-executive director remuneration at a glance

welcome to brighter

Introduction

Welcome to Mercer's 2023 UK Board Remuneration Handbook, covering the latest FTSE350 board remuneration practices and trends.

As the major effects of the pandemic begin to abate, 2022 was a return to a more 'steady-state'. However, after a long period of low inflation and pay moderation, higher inflation led to higher UK executive salary increases. These were between 3% and 5%, although generally these remained below the level of the workforce.

Bonus outcomes in respect of 2022 performance reverted to the long-run average bonus payout level, following the peak seen in 2021 when performance rebounded following the pandemic-hit year of 2020.

LTI outturns recovered somewhat but remain depressed, with FTSE100 and FTSE250 LTI payouts still below the pre-pandemic level.

2023 is a year in which a majority of the FTSE350 are required to hold a Policy vote. Shareholders have been mostly favourable as companies' proposals have been fairly conservative, with only a handful of companies submitting more 'radical' proposals.

Some FTSE100 companies chose to accept some reduction in voting support in order to secure increases in fixed pay and/or incentive opportunities to address perceived competitive issues (e.g. Unilever, Pearson). Otherwise, most low voting outcomes were a result of common issues seen in previous AGM seasons such as the application of discretion to adjust incentive outcomes and the misalignment of executive-workforce pensions.

ESG has continued to grow in prevalence as a metric and as it does so investors are focussing more on the robustness and relevance of the chosen measures.

Mercer is a leading executive remuneration consultancy supporting many FTSE remuneration committees and/or management teams on all aspects of remuneration design and implementation.

We trust this handbook is helpful. Please contact any of the team with comments or questions – refer to the back of this handbook for details.

Mercer UK Executive Reward team
October 2023

Note: this handbook comprises data for FTSE financial year-ends up to and including 31 March 2023. Where relevant, data has been converted to GBP using the Q1 2023 average FX rate (£1 : €1.13 : $1.22)

2023 AGM season

Summary of key trends during the 2023 AGM season

Aspect of reward	Details
Salary	• Typical executive salary increases in 2022/23 were higher than we have seen since 2008's financial crisis, as higher inflation led companies to award executives increases in the range of 3%-5% • However, these executive salary increases were typically below increases offered to the wider workforce as moderation and pay equity continues to be a principle expected by shareholders
Annual bonus outcomes	• Median bonus payments in respect of 2022 performance were lower than in respect of 2021, but have reverted to the pre-pandemic average level and were higher than companies' stated target level of around 50% of maximum • Given UK economic growth for the coming 12 months is forecast to be weak, investors might begin to focus more on the level of payouts if bonuses in respect of 2023 remain significantly above the target level
LTI outcomes	• LTI payout levels varied significantly between different companies and sectors • While median LTI vesting levels were slightly higher than in 2021, they remain below the pre-pandemic average level of payout
Pension	• Almost all FTSE250 companies have now aligned executive director pension contributions to the wider workforce • The remaining handful of companies that have not yet aligned pensions for incumbent executive directors may find that over time they come under greater scrutiny on this issue
Total earnings	• In broad terms, the median actual total single figure levels are slightly lower than last year by c.10% for CEOs and c.5% for CFOs at FTSE350 companies
Compensation design	• Performance share plans remain the predominant LTI vehicle in the UK market with only a handful granting restricted shares to Executive Directors, typically with a 5-year time horizon and performance underpin(s). Restricted share plans are very common below Board creating a potential disconnect in the design of remuneration for Executive Directors compared to other employees • ESG measures continue to increase in prevalence, most notably in annual bonus plans. Companies with more clearly defined ESG strategies have also included ESG metrics in their long-term incentive (mostly extractive industries)

Average shareholder support for remuneration Policies has increased slightly, although support for implementation reports has been broadly unchanged

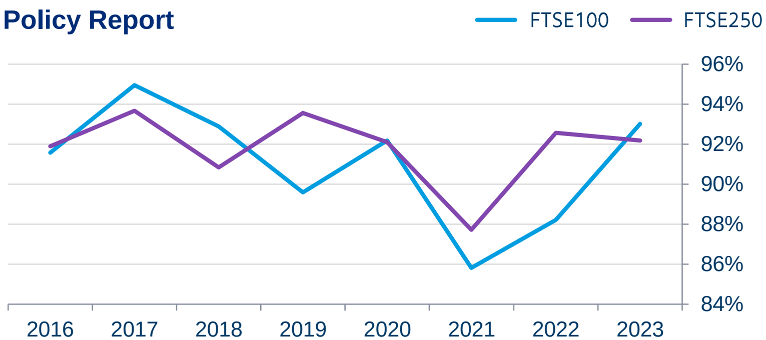
Around half of FTSE350 companies sought a shareholder vote on a new remuneration Policy at 2023 AGMs compared to around one quarter last year. The higher number of Policy votes reflects the fact that most of the FTSE remains on the same three-year Policy cycle.

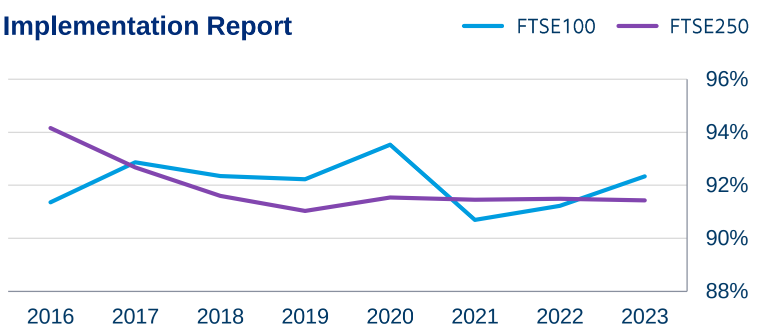
For the FTSE350, the average level of support has increased from 90% to 93% year-on-year. This increase in support is similar to that seen in other years when a majority of companies were required to hold a Policy vote and reflects the greater proportion of Policies being rolled-over with only minor changes – whereas in other years we would expect more companies seeking significant changes. No companies have failed their Policy votes so far in 2023.

Implementation report votes have remained broadly flat compared to 2022. Around 22 companies obtained votes in favour of 80% or lower (vs. 25 last year). Two companies failed to receive a majority vote for their remuneration reports: Unilever (42%) and Plus500 (25%).

Trend in AGM voting outcomes

Average % votes in favour





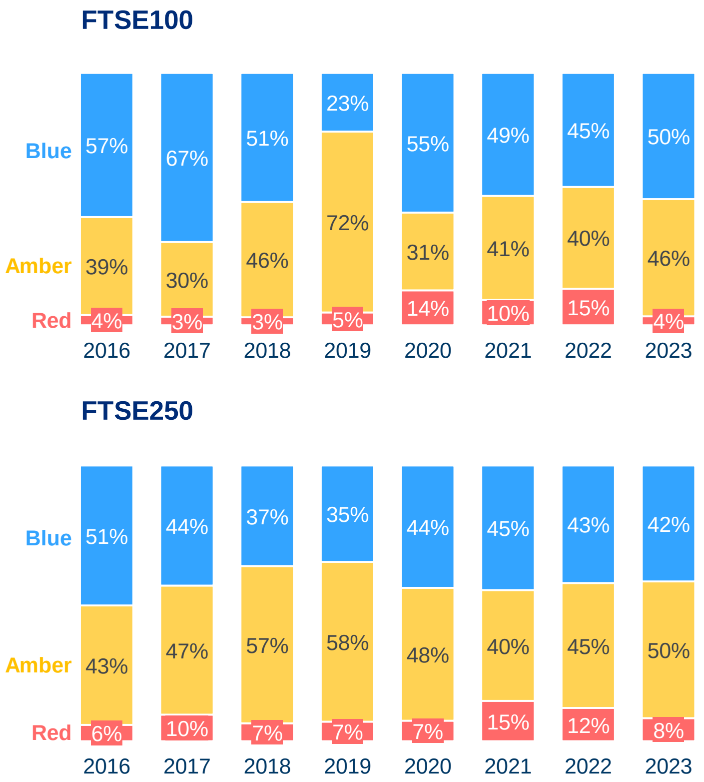
The 2023 AGM season saw a decrease in the number of red tops and an increase in amber tops

There was a smaller proportion of ‘Red Tops’ in 2023 compared to the previous year, with the distribution of tops more in-line with pre-2019 outcomes. Many of the shareholder voting issues were familiar ones from prior years.

Shareholder ‘hot spots’ for the 2023 AGM season

- One of the most common reasons for Red Tops has been the lack of alignment between executive director pension levels and wider workforce levels.
- Another common reason was not ‘scaling-back’ LTI award sizes where the share price had dropped significantly year-on-year.
- Some of the Red Tops were also triggered in relation to significant salary increases to executives compared to the wider workforce.
- Other reasons for Red Tops included generous treatment of leavers, poor disclosure of targets or insufficiently stretching goals or bonuses based on individual performance only.

IVIS colour tops
% of implementation reports



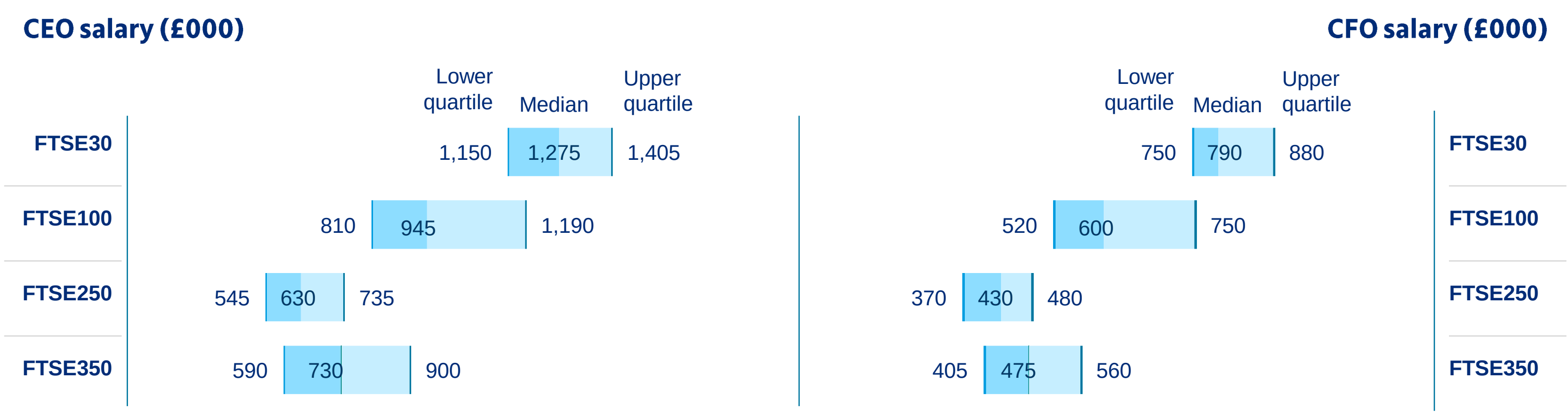
Salaries

High inflation resulted in increased salary increases for 2023?

Salaries for executive directors (ED) increased on average by around 3%-5% in 2023, higher than in recent years; increases of 2% to 3% have been typical since 2008's financial crisis and salaries were frozen during the pandemic; driven by higher UK inflation.

Salaries continue to be well correlated with company size. Median FTSE100 salaries are now £945k and £600k for the CEO and CFO, respectively (vs £900k and £575k last year), and £630k and £430k in the FTSE250 (vs £610k and £410k last year).

Whereas investors have been content for ED salaries to move in-line with the general workforce increase while inflation was around 2%, their expectation has been that, given higher UK inflation, salary increases for EDs should be lower and certainly no higher than the average of the workforce. Further details on levels of increase are included on the next page.



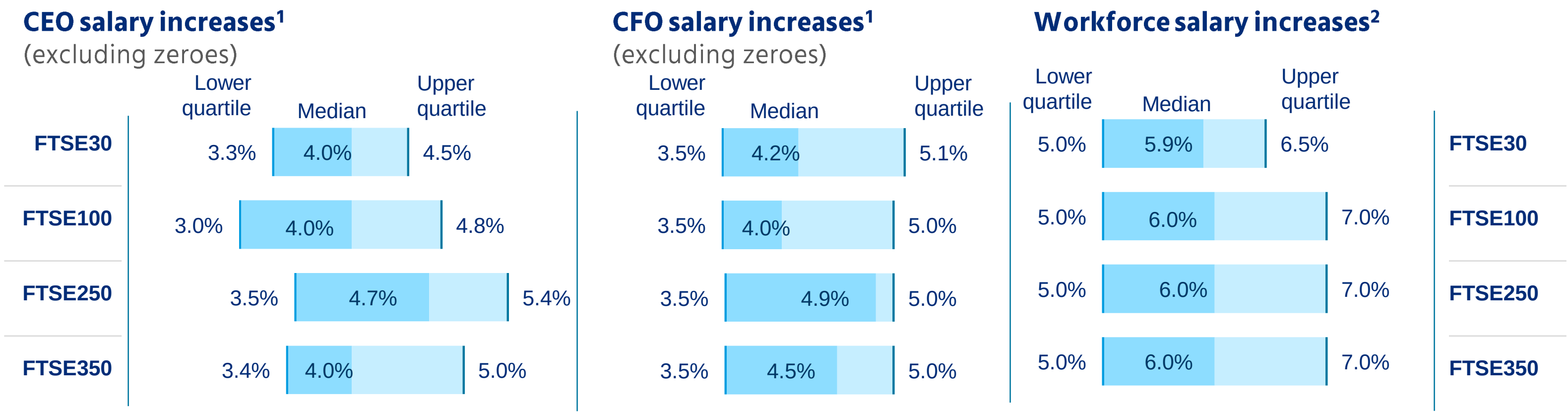
Executive salary increases have generally been below that of the wider workforce

Pressure to moderate executive salary increases for 2023 was clearly signalled and this expectation has generally been met. 79% of FTSE350 constituents awarded lower increases to EDs than the workforce.

Of the remaining companies, 12% aligned ED and workforce increases and 9% awarded higher increases quoting market benchmarks, past pay freezes and increases to the scope of the role as their rationale.

Many firms disclosed other initiatives brought in to aid the workforce during times of inflation. Examples include one off payments to their lower earners and raising wages that had fallen below the national living wage.

Where ED salaries were increased, the median rise was around 4.0% to 5.0%, with the median workforce increase higher at around 6.0%. This compares to 3.0% to 3.5% for EDs last year.



1. *% increase figures relate to contractual salaries and do not take into account any temporary reductions that were applied in 2021*
2. Not all companies disclose a figure for wider workforce increases, and instead stated a relative position to the executive salary increases

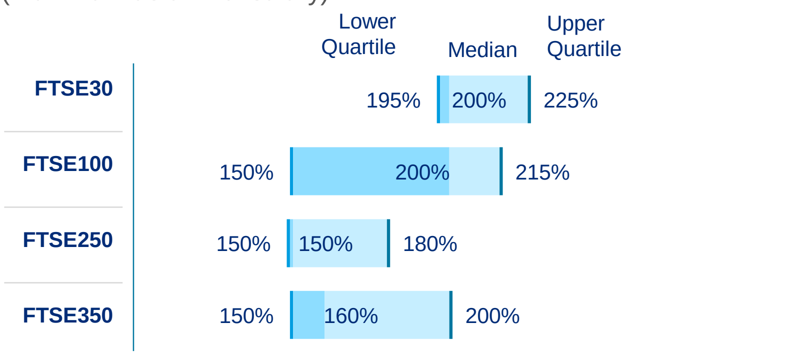
Annual Bonus

Maximum bonus opportunities remain stable

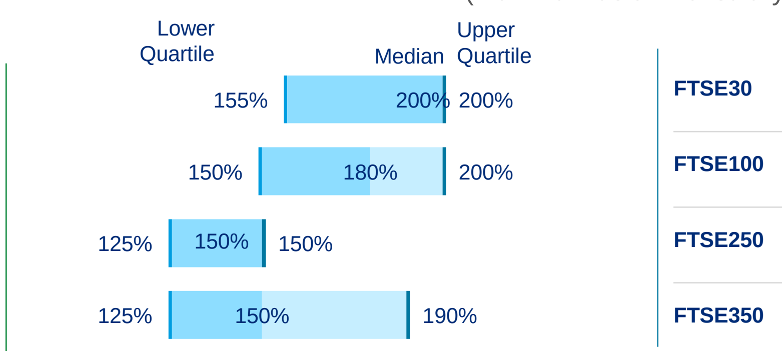
2023 median maximum annual bonus opportunities have remained almost unchanged. Only the median maximum bonus opportunity for FTSE100 CFOs increased (from 170% to 180% of salary).

Investors expect the target bonus opportunity to be no more than 50% of the maximum. Around 80% of the FTSE350 have a target bonus of 50% of maximum, with only c.12% of companies with a target bonus above 50% (vs 15% of companies last year).

CEO annual bonus opportunity
(maximum as a % of salary)



CFO annual bonus opportunity
(maximum as a % of salary)



Companies continue to include more measures in bonus scorecards, in-particular ESG metrics

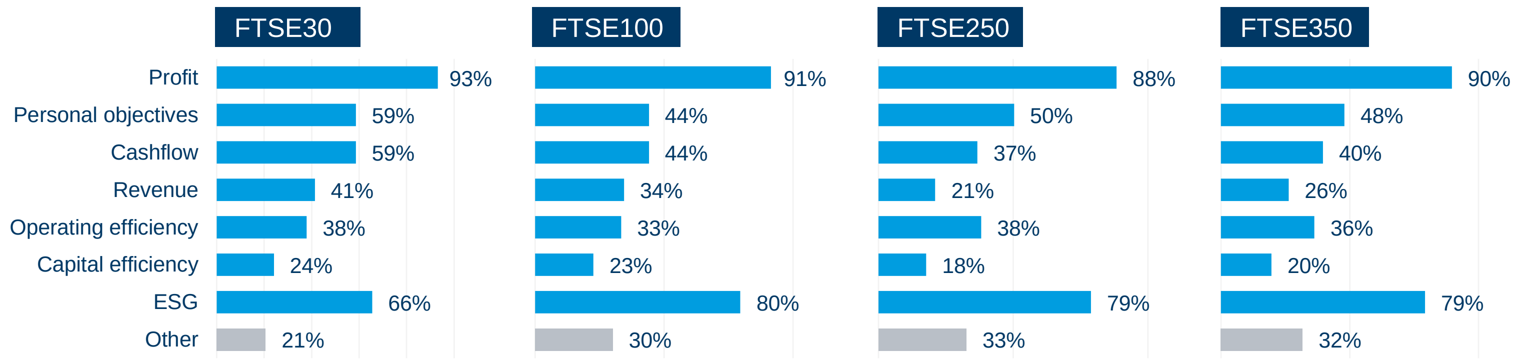
Around 93% of FTSE350 companies that operate a bonus plan use three or more measures (up from c.85% last year). ESG metrics continue to rise in prevalence and are now used by c.80% of the FTSE350. Further details on the use of ESG is included on the next page.

Profit metrics remain the most common financial measures – used by c.90% of the FTSE350. This is followed by cashflow, revenue and operating efficiency measures.

Annual bonuses are commonly complemented by non-financial measures. Personal and strategic measures are common but are now less common than ESG measures.

While non-financial measures are common, financial metrics generally have the most significant weighting, with an average ratio of financial to non-financial measures of 70:30.

Annual bonus performance measures
(prevalence as a % of companies)



Companies are increasingly including ESG metrics in incentives

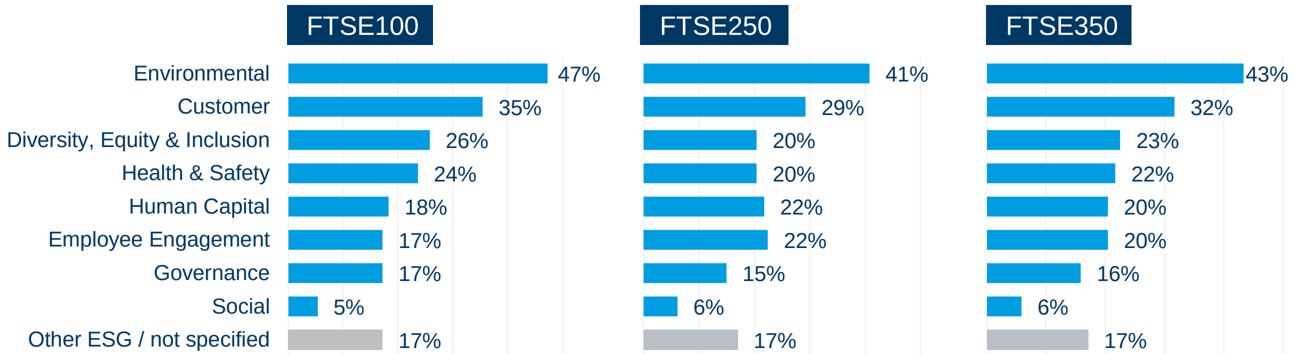
Environmental, social and governance (ESG) measures are now the second most common type of metric used in annual bonuses.

The type and scope of ESG measures adopted by FTSE companies depends on factors such as sector as well as the maturity of each company's ESG strategy. Across all FTSE companies, the most common ESG measures include environment, customer, DE&I and health and safety.

Health and safety and governance measures are often used as underpins to the bonus, while environment or employee engagement performance measures typically have a discrete weighting and a sliding scale of targets.

The level of disclosure varies considerably and many companies have opted for broad, qualitative targets. We expect measures to remain relatively diverse, reflecting each company's business model and circumstances.

Annual bonus performance measures
(prevalence as a % of companies)



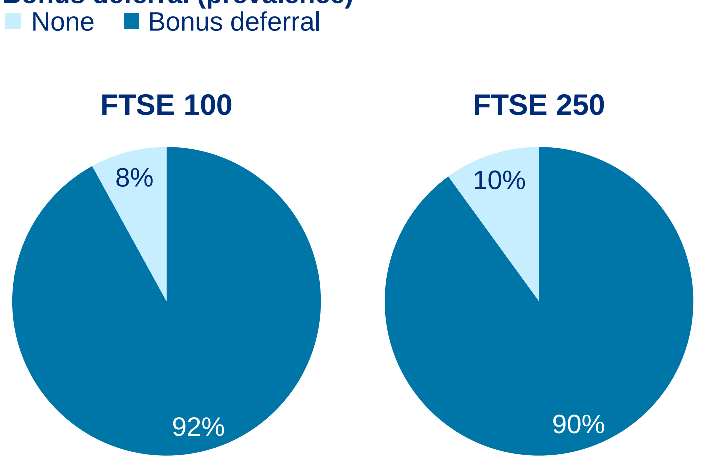
Bonus deferral remains commonplace in FTSE350

The vast majority of the FTSE350 now operate mandatory bonus deferral into shares.

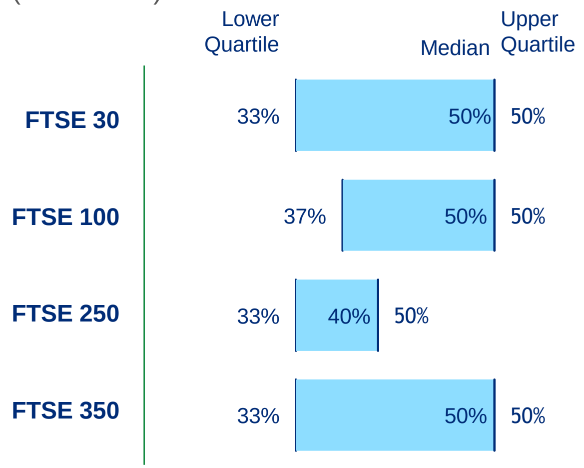
Over 80% of FTSE350 bonus deferral policies are based on a fixed percentage of bonus earned (most often 50% of any payout), with the remaining companies deferring any bonus earned above a threshold (e.g. 100% of salary).

Shareholder pressure for simplified remuneration policies has resulted in the demise of voluntary deferral and share matching plans, with only a small minority of companies now offering such arrangements.

Bonus deferral (prevalence)



Mandatory deferral amount
(% of bonus)



Median bonus outcomes for the 2022 financial year have reverted to pre-pandemic levels

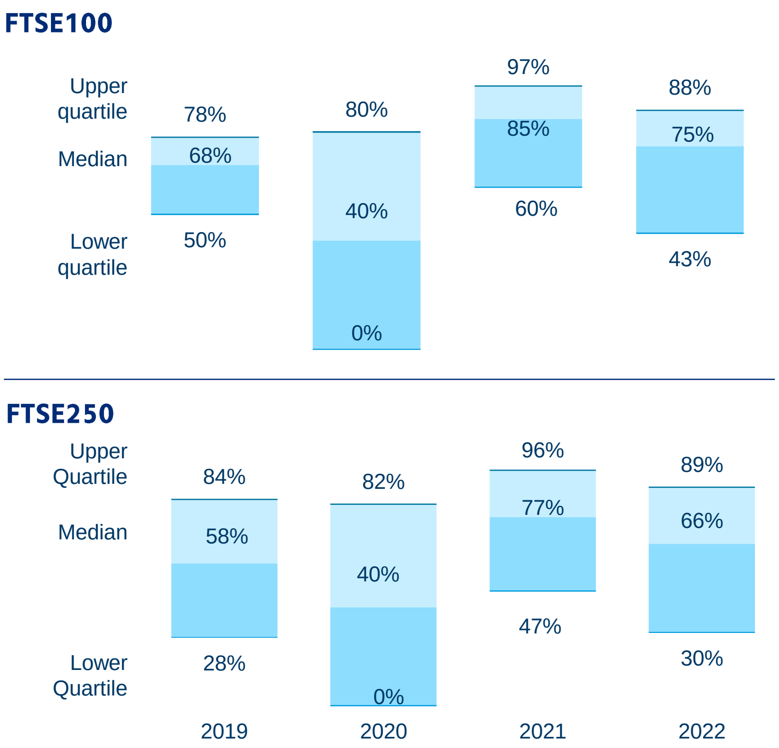
Following the sharp rebound in median bonus payouts from 2020 to 2021, bonus payouts in respect of 2022 fell slightly.

The 2022 median bonus payouts have reverted to pre-pandemic levels but remain above the c.50% of maximum level that most companies state is their on-target levels. This level of payout implies that on average FTSE350 companies have outperformed their forecasts by a significant margin.

As forecasts for UK economic growth remain weak, investors who experience disappointing returns may begin to focus more on bonus target setting if payouts continue to be significantly above target in coming years.

Trend in CEO bonus outcomes

% of maximum opportunity



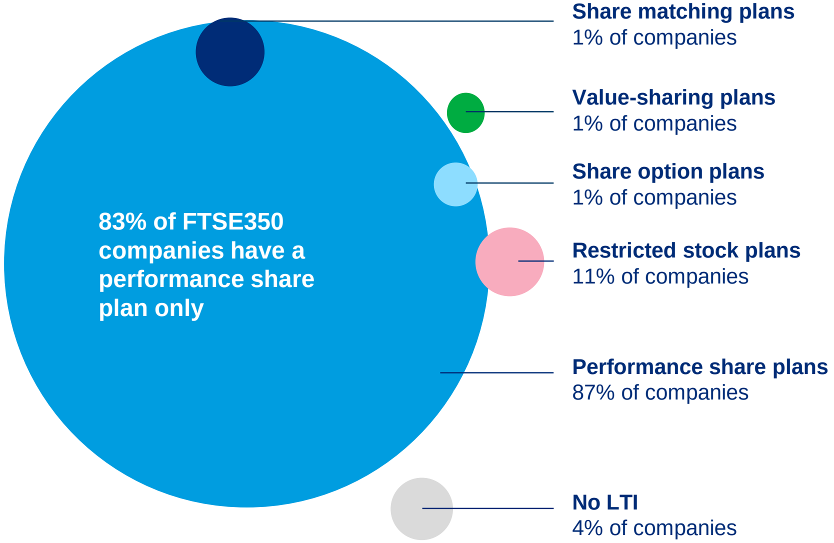
Long-Term Incentives

Performance shares remain the predominant long-term incentive structure in the FTSE350, with no change in the prevalence of restricted shares year-on-year

The majority of companies (80%+) continue to operate a performance share plan as the sole form of LTI.

A minority of companies have other arrangements in place. Around 11% of the FTSE350 use restricted shares (unchanged from last year) as companies seek to increase the likelihood of vesting in the long-term incentive and mitigate the concerns around 3-year target setting. Investors expect the face value of restricted shares to be reduced by 50% compared to the face value of performance shares, to compensate for the more guaranteed nature of the awards.

Prevalence of long-term incentive vehicle
(% of FTSE350 companies)



A handful of companies increased LTI maxima however overall LTI award values remain broadly unchanged

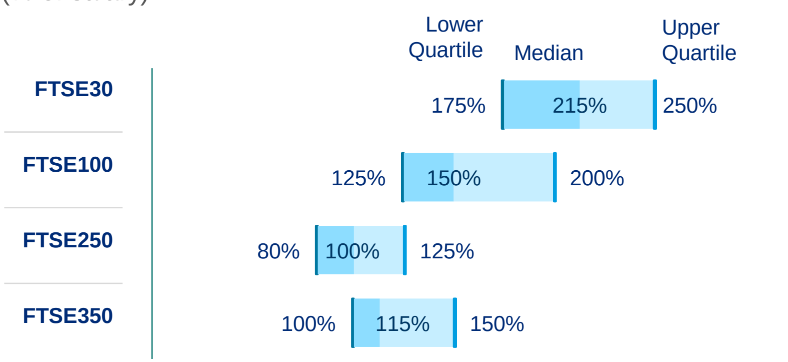
Companies looking to address competitive issues with Executive Director packages mostly focused on increasing LTI opportunities over annual bonus opportunities. In the FTSE100, median PSP median maximum awards increased to 290% of salary (275% last year), whilst some FTSE250 companies also increased awards, with the upper quartile PSP maximum increasing from 200% of salary last year to 250% of salary this year.

Shareholders continue to expect remuneration committees at companies where share price has fallen (by 25% or more) to scale-back LTI awards at grant or commit to apply discretion on vesting to mitigate the potential for windfall gains.

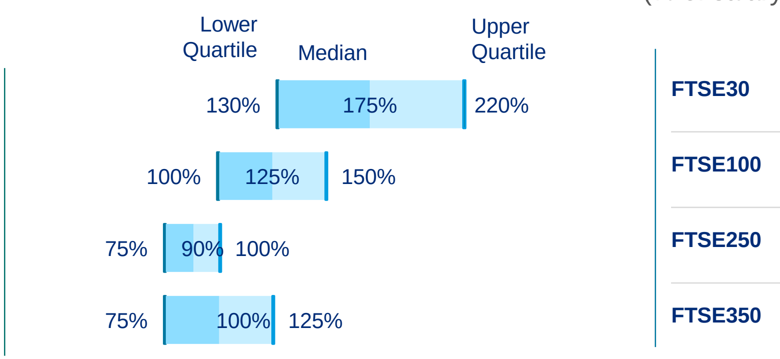
Face value of CEO LTI by plan type (% salary)

		Lower quartile	Median	Upper quartile
FTSE100	PSP (max)	235%	290%	385%
	RSP	100%	125%	150%
FTSE250	PSP (max)	150%	200%	250%
	RSP	100%	100%	125%

Fair value[1] of LTI opportunities (all plans) for CEOs
(% of salary)



Fair value[1] of LTI opportunities (all plans) for CFOs
(% of salary)



1. *Estimated at 50% of face value for Performance Share Plans, 20% for Option Plans, 100% for Restricted Share Plans and Monte-Carlo valuation for Value Creation Plans*

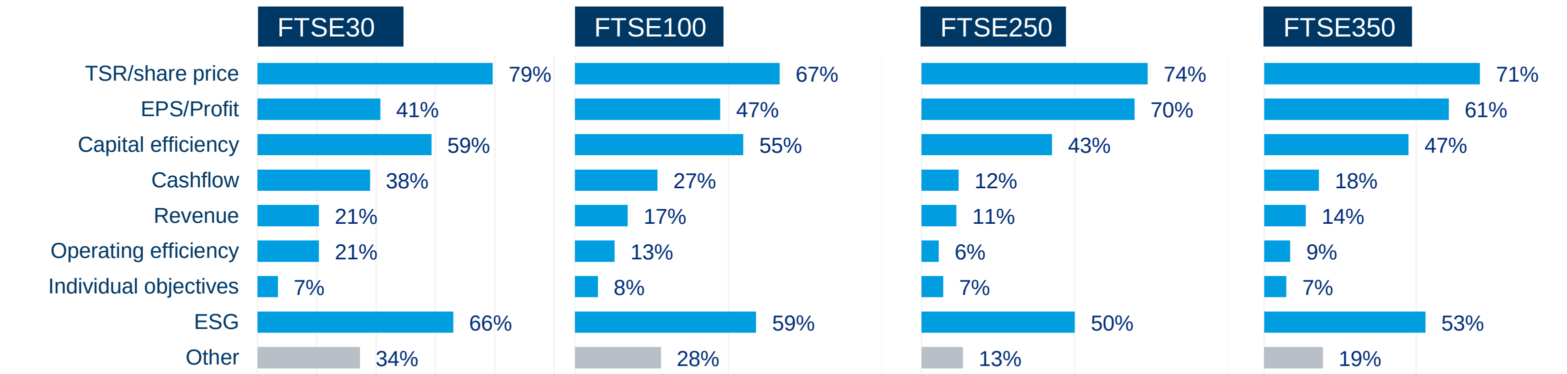
LTI scorecards remain consistent year-on-year

Over 75% of FTSE350 companies (vs. c.67% last year) now use three or more measures in determining vesting.

TSR and EPS remain the most common measures. Other measures such as returns, revenue, cashflow, and in more recent years, ESG, continue to gain traction. These typically supplement rather than replace TSR and EPS.

The prevalence of ESG measures remains unchanged, with 53% of the FTSE350 including such metrics in their most recent LTI grants. Where ESG measures are used in the LTI, the most prevalent measures by far relate to environmental objectives.

Long-term incentive performance measures
(prevalence as a % of companies)



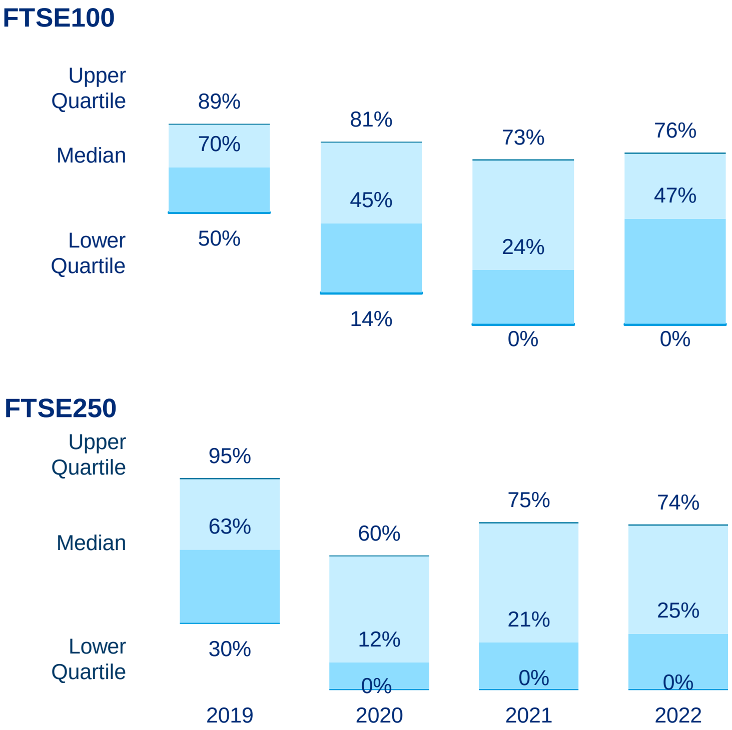
LTI vesting outcomes remain below pre-pandemic levels

Companies continue to recover from the business impacts of COVID-19 and the Brexit transition (although the severity of the impact varies by sector and business model) and this is reflected in LTI vesting levels. The median FTSE100 LTI vesting for 2022 was almost double that of 2021, but still below the long-run pre-pandemic average of c.60%-70% vesting.

FTSE250 median LTI vesting levels also remained considerably below pre-pandemic levels when the average was c.50%-60%.

Shareholders continue to expect Remuneration Committees to exercise care when adjudicating incentive outcomes. While LTI payouts remain generally depressed, this is not a uniform picture and some LTIs delivered significant payouts. Where significant payouts occurred in circumstances where investors believed there was a windfall element, this was reflected in lower support for DRR votes at 2023 AGMs.

Trend in CEO LTI outcomes
% of maximum opportunity

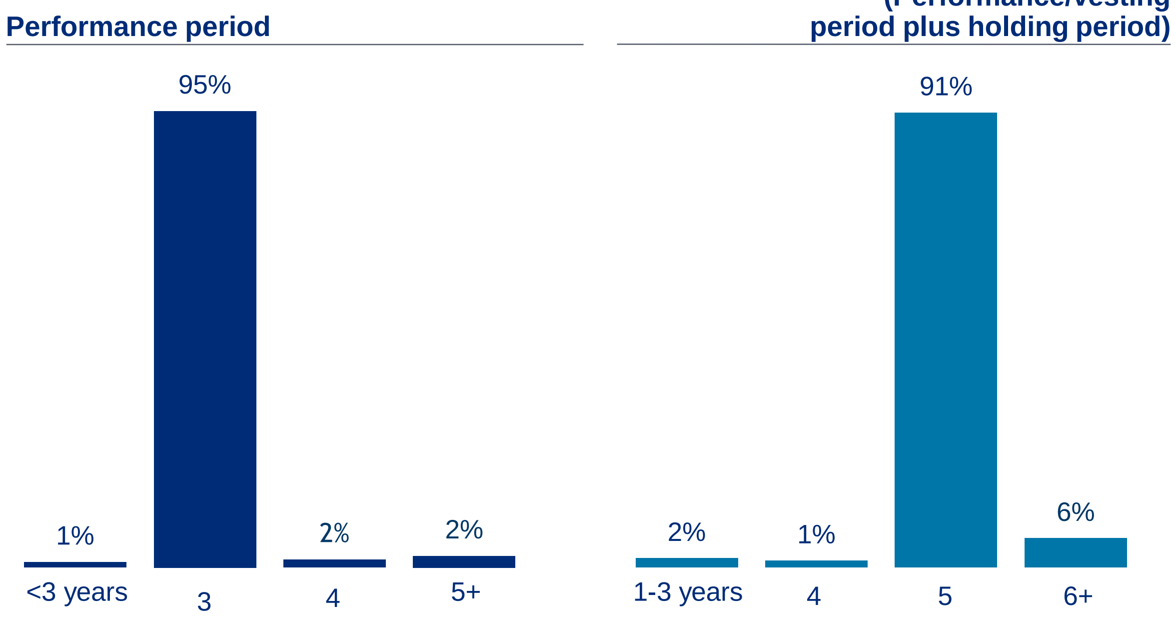


3-year performance periods and a 5-year total time horizon are commonplace

3-year performance and vesting periods are the norm in FTSE long-term incentives, with over 90% of companies also imposing a 2-year post-vest holding period consistent with the requirement in the UK Corporate Governance Code.

Where companies have introduced restricted shares, investors expect that the plan includes a total time horizon of at least 5 years too.

FTSE350 LTI time horizons
(% of plans)



Pensions

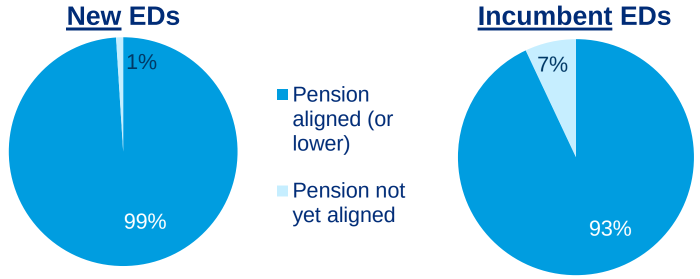
Practically all companies have now aligned ED pensions with the workforce

The 2018 UK Corporate Governance Code (the Code) sets out an expectation for companies to align their pension contribution rates for executive directors (EDs) with those available to the wider workforce.

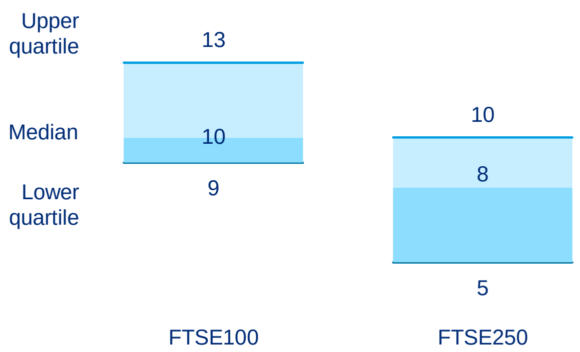
The Investment Association has stated its expectation that companies should match new and incumbent ED pensions to the workforce rate, with alignment for incumbent EDs by 31 December 2022.

Virtually all FTSE350 companies already comply with the Code in respect of new EDs and around 93% of the FTSE350 have reduced pension rates for incumbent EDs (vs c. 70% last year). The median workforce pension rate in the FTSE100 is 10% of salary, whilst in the FTSE250 the median pension rate is 8% of salary.

FTSE350 ED pensions alignment with workforce



Workforce pension rates (% of salary)



Executive pension contributions are beginning to converge at around 8% to 10% of salary, in-line with the UK workforce average

Almost all incumbent executive pensions have aligned with pensions provided to the wider workforce.

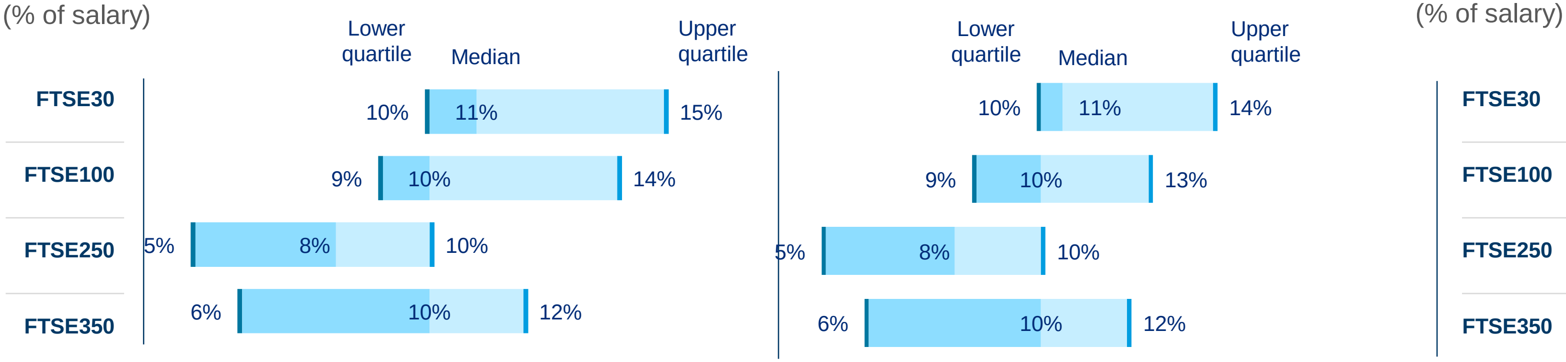
The FTSE100 median incumbent CEO pension reduced to 10% of salary vs. 12% last year. In the FTSE250, the CEO median has fallen from 10% to 8% of salary.

Some companies with workforce pension rates of <10% of salary have used this opportunity to review pension rates across the wider workforce to bring them more in-line with the UK market, an outcome that was encouraged by the UK Government and investors when this policy was communicated in 2019.

Employer contributions to DC schemes (or cash in lieu allowances) – incumbent executives

CEO pension
(% of salary)

CFO pension
(% of salary)



Executive share ownership guidelines

Companies that increased LTI opportunities often complemented that with increased shareholding requirements

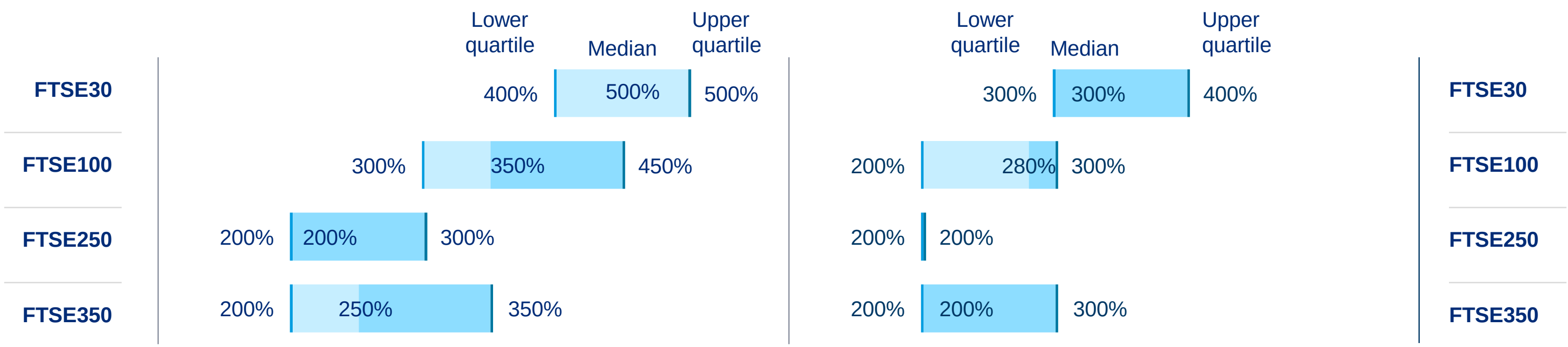
Almost all FTSE companies operate shareholding requirements for their executives. The minimum expected by most investors is 200% of salary, a level met or exceeded by the majority of the FTSE350. The median FTSE100 CEO share ownership requirement is now 350% of salary (c.f.300% of salary last year), whilst FTSE250 companies have mostly kept their shareholding requirement unchanged.

The majority of companies require executives to hold a proportion of vested shares from deferred bonuses or vested LTIP shares until the guidelines are met. Most also now specify a time horizon over which the guidelines must be achieved (generally five years).

Shareholding requirements are broadly linked to the size of the LTI opportunity, with companies with higher award levels also operating higher shareholding requirements.

CEO share ownership requirement
(as a % of salary)

CFO share ownership requirement
(as a % of salary)



Post-exit shareholding requirements are commonplace in the FTSE350

Around 97% of FTSE350 companies operate post-exit shareholding requirements.

The minimum expectation by the Investment Association (IA) is that the post-exit shareholding requirement should apply for at least two years at a level equal to the lower of the in-post guideline and the individual's actual shareholding on departure.

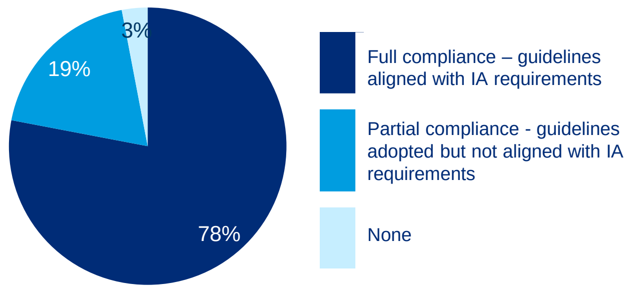
Out of the FTSE100, over three-quarters of companies have adopted a policy in line with the IA's expectation, with around 20% of businesses in partial compliance (e.g. reducing the shareholding requirement for the second year post departure).

In the FTSE250, practice is more split, with around half of companies in full compliance and c.45% in partial compliance.

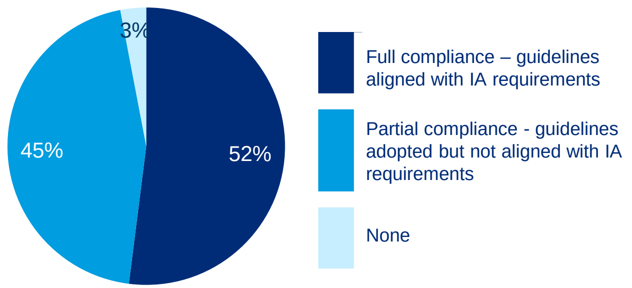
Given the majority of FTSE350 companies held Policy votes in 2023, a greater increase in the percentage of companies in full compliance with the IA guidelines might have been expected; however, the percentages of companies in the FTSE100 and FTSE250 that fully comply show only minor increases from last year.

Prevalence of post-employment shareholding requirement

FTSE100



FTSE250



Chair and NED fees

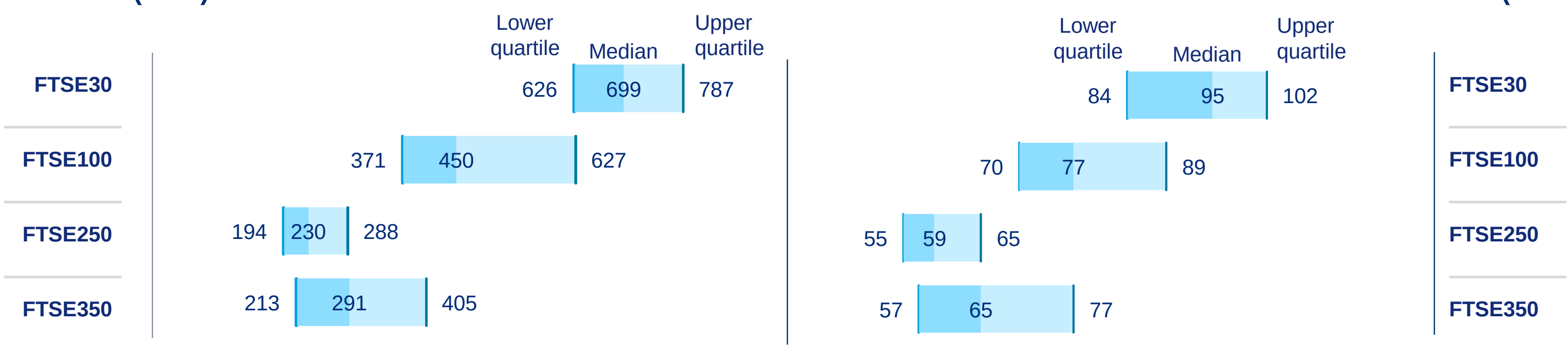
Company chair and non-executive director base fees increased by c.3%-5% since last year

Following some years of freezes, most companies increased their Board fees in-line (or slightly below) the salary increase offered to executives and the wider workforce.

Historically companies have increased NED fees once every two to three years, however, as Board members and shareholders have become more concerned that NED time commitments and responsibilities are increasing without a commensurate increase in fee levels, we have seen a greater number of companies moving to annual fee reviews as a means of keeping pace with the growing demands on NEDs.

Board fees

Chair fees (£000) **NED base fees (£000)**

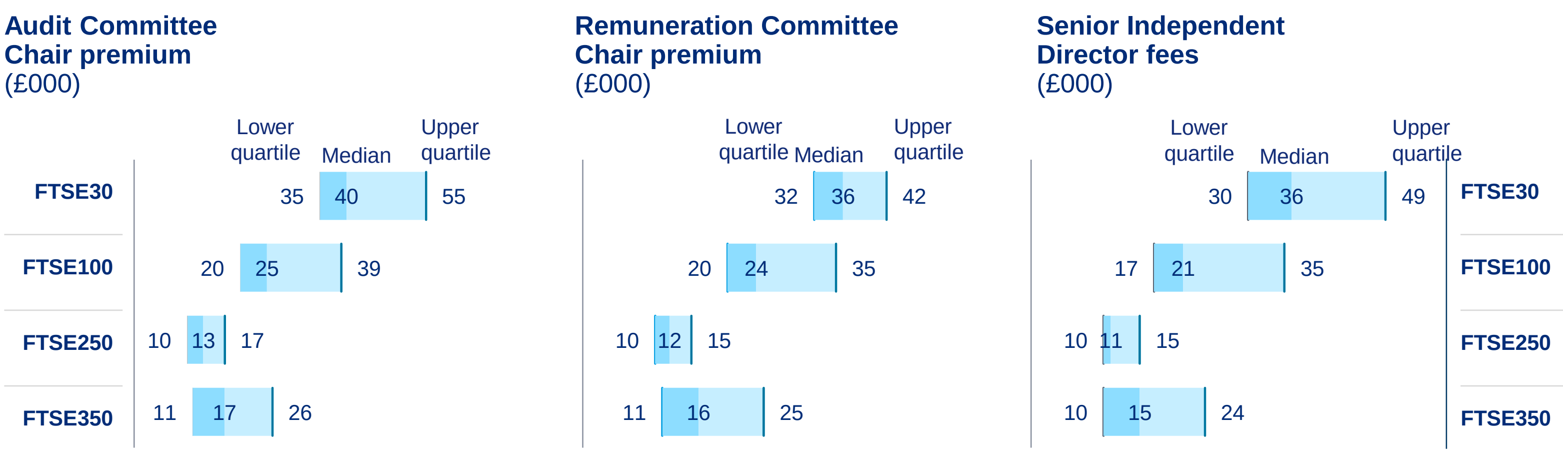


Similar to base fees, there have been some increases in additional SID and committee chair fees

The fee premium paid to FTSE350 SIDs and committee chairs for their additional board and committee responsibilities also increased by c.3%-5% from last year. The median audit chair premium continues to be the higher than the median for, say, chairing the remuneration committee although in practice over 75% of the FTSE350 pay identical fees for chairing the audit and remuneration committees and the difference in median is the result of the minority of companies that differentiate fees between the two roles.

Board meeting attendance fees are a minority practice within the FTSE as the base fee is generally considered to be all-inclusive, although some directors at the largest companies receive additional international travel allowances.

A significant minority of FTSE350 companies pay an additional fee to their designated NED for representing the views of the workforce to the board. Where a fee is paid, the median fee is c.£13,000 for the FTSE100, and c.£10,000 for the FTSE250 (vs. £10,000 and £9,000 respectively last year).



Committee membership fees are paid by around 25% of the FTSE350

Committee membership fees are more common at the largest FTSE constituents, which generally have larger boards with more dispersed responsibilities. As a result, only just under half of the FTSE100 pay an annual fee for being a member of a Board committee. Such fees are more common in some other markets, e.g. North America.

Only a small minority of FTSE250 companies pay additional committee membership fees.

Audit Committee member premium (£000)

	Lower quartile	Median	Upper quartile
FTSE30	20	25	30
FTSE100	10	18	24
FTSE250	5	6	10
FTSE350	6	10	20

Remuneration Committee member premium (£000)

	Lower quartile	Median	Upper quartile
FTSE30	18	20	30
FTSE100	10	17	20
FTSE250	5	6	10
FTSE350	5	10	18

Other[1] Committee member premium (£000)

	Lower quartile	Median	Upper quartile
FTSE30	17	20	27
FTSE100	10	16	20
FTSE250	5	7	10
FTSE350	7	11	18

1. Includes Risk, Sustainability and other Committees

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About us

We are a leading team of executive remuneration consultants

Our service offering

Remuneration design

- Reward strategy development
- Short and long-term incentive design
- Performance measure selection
- Balanced scorecard design
- Peer group selection
- Calibrating targets, modelling potential pay outcomes
- Modelling of pay and performance
- Financial modelling
- Tax and accounting implications

HR support

- Pay benchmarking
- Recruitment packages for new hires
- Pay and grading structure design
- Employee communication / handbooks
- Total reward statements
- Salary administration and support
- Performance management and reporting
- Pensions and benefits
- Employee engagement

Remuneration Committee support

- Independent advice on all aspects of executive remuneration and governance
- Updates on market trends
- Executive remuneration reviews
- Pay and performance benchmarking
- Pay for performance analysis
- Target setting
- Shareholder consultation
- Drafting the remuneration report