



# HM TREASURY

## Financial Reporting Advisory Board Paper REMUNERATION REPORT – INCLUSION AS PART OF THE FINANCIAL STATEMENTS

<b>Issue:</b>	The preparation of a Remuneration Report for inclusion in financial statements prepared by bodies falling within the scope of the FReM.
<b>Impact on guidance:</b>	The proposals will have an impact on the FReM.
<b>UK GAAP adaptation?</b>	Only marginally – see paragraph 4 below.
<b>IAS/IFRS compliant?</b>	N/A
<b>IPSAS compliant?</b>	N/A
<b>Impact on budgetary regime?</b>	No
<b>Recommendation:</b>	The FRAB is invited to approve the proposal for the preparation of a Remuneration Report and the proposed wording for the FReM.
<b>Timing:</b>	2005-06

## DETAIL

### Background

1. Section 234B and Schedule 7A to the Companies Act 1985 (see Statutory Instrument SI 2002 No 1986 *The Directors' Remuneration Report Regulations 2002*) require quoted companies to disclose information about the remuneration payable to their directors in a separate Directors' Remuneration Report rather than in the notes to the accounts. Although the requirements apply to quoted companies, the general policy is for public sector bodies to apply the best private sector practices, and this paper proposes that the bodies falling within the scope of the FReM should prepare a Remuneration Report.

2. One of the requirements of Schedule 7A – the disclosure of Cash Equivalent Transfer Values (CETVs) – has already been implemented; see FRAB (64) Minor H (7 November 2003) and FRAB (66) 6 (8 March 2004).

3. The requirements of Schedule 7A include the disclosure of information on share options, long-term incentive schemes and other aspects of remuneration which are either not applicable in a public

sector context or, if applicable, are unlikely to arise in practice. Annex A to this paper summarises the requirements and indicates the extent to which they appear to be applicable to the public sector. It seems likely that, in most cases, the Remuneration Report will give information about (a) the policy on determining the remuneration arrangements (b) information on service contracts and (c) salary and pension entitlements. Item (c) is currently given in the notes to the accounts.

### **UK GAAP compliance**

4. The proposals are compliant with UK GAAP, with the exception that the separate disclosure of the various elements of the remuneration package (in particular, bonuses and compensation payments) as required by paragraph 6(1) of Schedule 7A of the Companies Act is not required. The current level of disclosure (in which the various elements are aggregated) was agreed after consultation with departments and others and any increase in that level will require further consultation. The intention is to retain the current level of disclosure for the time being and to initiate a consultation exercise in due course.

### **IAS/IFRS compliance**

5. There is no equivalent disclosure requirement in IAS/IFRS.

### **IPSAS compliance**

6. There is no IPSAS on this subject.

### **Impact on the budgetary regime**

7. There is no impact on the budgetary regime.

### **Proposed amendment to the Government Financial Reporting Manual**

8. See Annex B for the proposed amendments to the FrEM.

### **Summary and recommendation**

9. The FRAB is invited to approve the proposal to require the preparation of a Remuneration Report for 2005-06 onwards (which will replace some of the information currently given in notes to the accounts) and to approve the wording for the FrEM.

**HM Treasury**

**25 January 2005**

## ANNEX A

### SUMMARY OF REQUIREMENTS OF SCHEDULE 7a OF THE COMPANIES ACT 1985 AND POSSIBLE APPLICATION TO THE PUBLIC SECTOR

*NB: The summary of requirements is not reproduced verbatim and reference should be made to the Schedule itself in cases of doubt*

No	CA REF: SCHEDULE E 7a	SUMMARY OF REQUIREMENTS	APPLICATION TO PUBLIC SECTOR
01	Para 2(1)	Name of directors in committee reviewing remuneration report; Name of any person offering advice to committee; If this person is not a director, details of services provided and whether that person was appointed by the directors.	Applies if there is a Remuneration Committee
02	Para 3(1)	Statement of the policy on directors' remuneration for current and future financial years.	Applies, but information likely to be restricted to information of work of Senior Salaries Review Board.
03	Para 3(2)	Summary of any performance conditions subject to share options; Summary of any performance conditions subject to long-term incentive scheme [NB annual performance arrangements are not included]; Explanation of why these conditions were chosen; Explanation of methods used to assess whether performance conditions were met and of why those methods were chosen; If the methods involved comparison with outside organisations – why; Description of, and explanation for, any significant variation in terms and conditions of entitlement to share options or long term investment scheme.	Provisions re share options do not apply.  Provisions re long- term incentive schemes will apply, but considered very unlikely to arise in practice (see also point 14 below).
04	Para 3(3)	Explanation of relative importance of the relevant proportions of remuneration which are, and which are not, subject to performance conditions	Applies.
05	Para 3(4)	Summary and explanation of <b>policy</b> on duration of contracts, and notice periods and termination payments	Applies.
06	Para 4	This paragraph refers to the need for a graph showing performance of the company's shares against the average movement in the equity market	Not relevant.
07	Para 5(1)	Details of service contract – date, unexpired term, details of notice period, provision for compensation for early termination, other details sufficient to determine the potential liability in the event of early termination	Applies.
08	Para 5(2) and 14	Explanation of any significant awards made to former directors (see also point 18 below)	Applies.
09	Para 6(1) and 6(2)	For each director who served during the year show separately: Salary and fees paid or receivable; Bonuses paid or receivable; Taxable expense allowances; Compensation for loss of office paid or receivable and any other payments connected to termination of service; Estimated value of non-cash benefits; Total of the above for both this and previous year.	Applies., although the information may be aggregated and not shown separately.
10	Para 6(3)	Details of any element of the remuneration package which is not cash	Applies.
11	Para 6(4)	All this information to be given in tabular form	Applies.
12	Paras 7 – 9	These paragraphs refer to share options	Not relevant.
13	Paras 10 –11	Requirement to show information about long term incentive	Applies

		schemes in tabular form - includes definition of long term investment scheme	
14	Para 11	Details of long-term incentive scheme interests at beginning of year or appointment Details of scheme interests awarded during the year Details of scheme interests at the end of the year or on cessation as a director	See points 03 and 13 above – considered to be very unlikely in a public sector context.
15	Paras 12(1) and (2)	Details of the changes in the accrued pension benefits during the year Details of the accrued pension benefits at the end of the year The transfer value of the accrued benefits at the end of the year The transfer value of the accrued benefits at the beginning of the year The difference between the two transfer values, less any contributions from the director	Applies
16	Para 12(3)	Details of any contributions to a money purchase scheme	Applies
17	Para 13	Details of any amount of retirement benefit which is in excess of amounts payable to that individual either when he/she first become entitled thereto, or 31 March 1997 (whichever is later)	Applies, but unlikely to apply as exemption granted for any increases which are generally available to all pensioners
18	Para 14	Details of compensation payable to former directors (see also point 08 above)	Applies
19	Para 15	Details of amounts payable to third parties for services of director	Applies

## **PROPOSED AMENDMENT TO THE GOVERNMENT FINANCIAL REPORTING MANUAL (FreM)**

*NB: the following text will appear in Chapter 7 of the FReM; paragraph numbers may need to be amended.*

### *Remuneration Report*

#### *Applicability*

7.2.8 Section 234B and Schedule 7A of the Companies Act (see also Statutory Instrument SI 2002 No 1986) apply as interpreted for the public sector context, to all entities covered by the requirements of this Manual.

#### *Objective of section 234B and Schedule 7A of the Companies Act*

7.2.9 Section 234B requires the preparation of a Remuneration Report containing certain information about the directors' remuneration in accordance with the requirements of Schedule 7A. Certain of the information is subject to audit and will be referred to in the audit opinion; the audit opinion will also note that the remainder of the Report has been reviewed by the auditors.

7.2.10 The Remuneration Report shall be signed by the Accounting Officer or Chief Executive.

#### *Interpretation of the Companies Act's requirements for the public sector context*

7.2.11 References in the Act to "Directors" shall be interpreted to mean persons in senior positions having authority or responsibility for directing or controlling the major activities of the entity. This means those who influence the decisions of the entity as a whole rather than the decisions of individual directorates or sections within the entity. Such persons will include advisory and non-executive Board members and, in the case of departments, Ministers. In the following paragraphs, such persons are described as "senior managers".

7.2.12 Details of salary and allowances shall be analysed between (a) salary and allowances (see 7.2.14); and (b) benefits in kind, notwithstanding the requirements of paragraph 6(1) to Schedule 7A for the separate disclosure of the various elements of the remuneration package.

7.2.13 The Remuneration Report shall include information under the following headings to the extent that they are relevant. In addition to the headings listed below, Schedule 7A requires information to be given about long-term incentive schemes (as defined in paragraph 10(5) of Schedule 7A). It seems unlikely that entities to which this Manual applies will have such schemes and they are not considered further. The aspects of the Remuneration Report which are subject to audit are indicated as such.

- a. Details of the membership of the Remuneration Committee;
- b. Statement of the policy on the remuneration of senior managers for current and future financial years. In most cases, it will be sufficient to refer to the work and recommendations of the Senior Salaries Review Body;
- c. Explanation of methods used to assess whether performance conditions were met and why those methods were chosen. If relevant, why the methods involved comparison with outside organisations;

- d. Explanation of relative importance of the relevant proportions of remuneration which are, and which are not, subject to performance conditions;
- e. Summary and explanation of **policy** on duration of contracts, and notice periods and termination payments;
- f. Details of the service contract for each senior manager who has served during the year:
- Date of the contract, the unexpired term, and details of notice period;
  - Provision for compensation for early termination; and
  - Other details sufficient to determine the entity's liability in the event of early termination.
- g. Explanation of any significant awards made to past senior managers;
- h. For each senior manager who served during the year show, in tabular form [this information is subject to audit]:
- Salary and allowances (see 7.2.14 below) (for officials, in bands of £5,000, and actual amounts for ministers);
  - If a payment for compensation for loss of office paid or receivable has been made under the terms of an approved Compensation Scheme, the fact that such a payment has been made (but no details of the amounts paid);
  - Estimated value of non-cash benefits (benefits in kind) (to the nearest £100),
- together with the total of the above for both this and the previous year.
- i. Details of any element of the remuneration package which is not cash [this information is subject to audit];
- j. For each senior manager who has served during the year: [this information subject to audit]
- The real increase during the reporting year in the pension and (if applicable) related lump sum at age 60 (ministers age 65) in bands of £2,500;
  - The value at the end of the reporting year of the accrued pension and (if applicable) related lump sum at age 60 (ministers, age 65) in bands of £2,500;
  - The value of the cash equivalent transfer value at the beginning of the reporting year to the nearest £1,000;
  - The real increase in the cash equivalent transfer value during the reporting year, to the nearest £1,000;
  - Where the senior manager has a partnership pension account, the employer's contribution to the partnership pension account. [in these circumstances, the disclosures in the first four bullets will not apply].
- k. Details of compensation payable to former senior managers [this information is subject to audit];
- l. Details of amounts payable to third parties for services of a senior manager [this information is subject to audit].

7.2.14 Salary and allowances covers both pensionable and non-pensionable amounts and includes, but may not necessarily be confined to: gross salaries; performance pay or bonuses payable; overtime; reserved rights to London Weighting or London allowances, recruitment and retention allowances; private-office allowances or other allowances to the extent that they are subject to UK taxation and any ex-gratia payments. It does not include amounts which are a reimbursement of expenses directly incurred in the performance of an individual's duties. For **ministers**, only the salary payable in respect of their role as minister of the department should be shown.

7.2.15 Subject to the need to obtain their prior consent, there is a presumption that information about named individuals will be given in all circumstances, except on grounds of national security or where it conflicts with existing legislation. In the latter case, the fact that certain disclosures have been omitted should be disclosed.

7.2.16 Further guidance on salary and pension disclosures is given in Employer Pension Notices (EPNs) and formerly Pension Circulars issued by the Cabinet Office [link to be provided]