

# ICSA Guidance on Terms of Reference – Remuneration Committee

---

## Contents

---

If using online, click on the headings below to go to the related sections.

- A Introduction
- B The Combined Code
- C Notes on the terms of reference
- D Model terms of reference

## A Introduction

---

This guidance note proposes model terms of reference for the remuneration committee of a quoted company in the UK seeking to comply fully with the requirements of the Combined Code on Corporate Governance (the Combined Code). It draws on the experience of senior company secretaries and is based on best practice as carried out in some of the UK's top listed companies.

## B The Combined Code

---

The Combined Code states that:

‘There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors.’<sup>1</sup>

It goes on to state that:

‘The board should establish a remuneration committee ... [which] should make available its terms of reference, explaining its role and the authority delegated to it by the board.’<sup>2</sup>

It is clear therefore that the Combined Code not only requires companies to go through a formal process of considering executive remuneration, but to be seen to be doing so, and that establishing clear terms of reference for the remuneration committee, and making them available,<sup>3</sup> is an essential part of this process.

The Combined Code also states that the chairman of the committee should attend the AGM prepared to respond to any questions that may be raised by shareholders on matters within the committee's area of responsibility.<sup>4</sup>

## C Notes on the terms of reference

---

The list of duties we have proposed are based on those contained within the *Summary of Principal Duties of the Remuneration Committee* which ICSA helped compile for the Higgs Review.<sup>5</sup> Some companies may wish to add to this list and some smaller companies may need to modify it in other ways.

The Combined Code recommends that the committee should comprise of at least three independent non-executive directors (although two is permissible for smaller companies).<sup>6</sup> In addition to the independent non-executives, the company chairman may also be a member of the committee if he or she was considered independent on appointment as chairman, but may not chair it.<sup>7</sup>

---

1 The Combined Code, June 2006, B.2

2 The Combined Code, June 2006, B.2.1

3 Footnote 4 to the Combined Code clarifies that the requirement to make the terms of reference available would be met by including the information on a website maintained by or on behalf of the company.

4 The Combined Code, June 2006 D.2.3

5 The Higgs Report list of duties was originally appended to 2003 version of the Combined Code but is now incorporated in a document entitled *Suggestions for Good Practice from the Higgs Report*, available from the FRC website [www.frc.org.uk](http://www.frc.org.uk) as associated guidance.

6 A smaller company is defined in footnote 3 to the Combined Code as one which is below the FTSE 350 throughout the year immediately prior to the reporting year.

7 The Combined Code, June 2006, B.2.1. This code provision was amended in 2006 to allow the company chairman to serve on the committee.

Although not a provision in the Combined Code, the Higgs Review states as a matter of good practice in its non-code recommendations, that the company secretary (or their designee) should act as secretary to the committee.<sup>8</sup> In this regard, the company secretary has a responsibility to ensure that the board and its committees are properly constituted and advised and would normally act as an intermediary between the main board and the various committees to ensure clear co-ordination.

The frequency with which the committee needs to meet will vary from company to company and may change from time to time. It is clear, however, that it must meet close to the year end to review the directors' remuneration report which quoted companies must now submit to shareholders for approval at the AGM. We would recommend that the committee should meet at least twice a year in order to discharge its responsibilities properly.

*References to 'the committee' are to 'the remuneration committee'.*

*References to 'the board' are to 'the board of directors'.*

*Square brackets contain recommendations which are in line with best practice but which may need to be changed to suit the circumstances of the particular organisation.*

## D Model terms of reference

---

### 1. Membership

---

- 1.1. Members of the committee shall be appointed by the board, on the recommendation of the nomination committee and in consultation with the chairman of the remuneration committee. The committee shall be made up of at least [3] members, all of whom shall be independent non-executive directors. The chairman of the board may also serve on the committee as an additional member if he or she was considered independent on appointment as chairman.
- 1.2. Only members of the committee have the right to attend committee meetings. However, other individuals such as the chief executive, the head of human resources and external advisers may be invited to attend for all or part of any meeting as and when appropriate.
- 1.3. Appointments to the committee shall be for a period of up to three years, which may be extended for two further three-year periods, provided the director still meets the criteria for membership of the committee.
- 1.4. The board shall appoint the committee chairman who shall be an independent non-executive director. In the absence of the committee chairman and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting. The chairman of the board shall not be chairman of the committee.

### 2. Secretary

---

- 2.1. The company secretary or their nominee shall act as the secretary of the committee.

### 3. Quorum

---

- 3.1. The quorum necessary for the transaction of business shall be [2]. A duly convened meeting of the committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the committee.

---

<sup>8</sup> Higgs Review of the Role and Effectiveness of Non-executive Directors, January 2003 para 11.30

#### 4. Meetings

---

- 4.1. The committee shall meet [at least twice a year][quarterly on the first Wednesday in each of January, April, July and October] and at such other times as the chairman of the committee shall require.<sup>9</sup>

#### 5. Notice of meetings

---

- 5.1. Meetings of the committee shall be summoned by the secretary of the committee at the request of any of its members.
- 5.2. Unless otherwise agreed, notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed, shall be forwarded to each member of the committee, any other person required to attend and all other non-executive directors, no later than [5] working days before the date of the meeting. Supporting papers shall be sent to committee members and to other attendees as appropriate, at the same time.

#### 6. Minutes of meetings

---

- 6.1. The secretary shall minute the proceedings and resolutions of all committee meetings, including the names of those present and in attendance.
- 6.2. Minutes of committee meetings shall be circulated promptly to all members of the committee and, once agreed, to all members of the board, unless a conflict of interest exists.

#### 7. Annual general meeting

---

- 7.1. The chairman of the committee shall attend the annual general meeting prepared to respond to any shareholder questions on the committee's activities.

#### 8. Duties

---

The committee shall

- 8.1. determine and agree with the board the framework or broad policy for the remuneration of the company's chief executive, chairman, the executive directors, the company secretary and such other members of the executive management as it is designated to consider.<sup>10</sup> The remuneration of non-executive directors shall be a matter for the chairman and the executive members of the board. No director or manager shall be involved in any decisions as to their own remuneration
- 8.2. in determining such policy, take into account all factors which it deems necessary. The objective of such policy shall be to ensure that members of the executive management of the company are provided with appropriate incentives to encourage enhanced performance and are, in a fair and responsible manner, rewarded for their individual contributions to the success of the company
- 8.3. review the ongoing appropriateness and relevance of the remuneration policy

---

<sup>9</sup> The frequency and timing of meetings will differ according to the needs of the company. Meetings should be organised so that attendance is maximised (for example by timetabling them to coincide with board meetings).

<sup>10</sup> Some companies require the remuneration committee to consider the packages of all executives at or above a specified level, such as those reporting to a main board director, while others require the committee to deal with all packages above a certain figure.

- 8.4. approve the design of, and determine targets for, any performance related pay schemes operated by the company and approve the total annual payments made under such schemes
- 8.5. review the design of all share incentive plans for approval by the board and shareholders. For any such plans, determine each year whether awards will be made, and if so, the overall amount of such awards, the individual awards to executive directors and other senior executives and the performance targets to be used
- 8.6. determine the policy for, and scope of, pension arrangements for each executive director and other senior executives
- 8.7. ensure that contractual terms on termination, and any payments made, are fair to the individual, and the company, that failure is not rewarded and that the duty to mitigate loss is fully recognised
- 8.8. within the terms of the agreed policy and in consultation with the chairman and/or chief executive as appropriate, determine the total individual remuneration package of each executive director and other senior executives including bonuses, incentive payments and share options or other share awards
- 8.9. in determining such packages and arrangements, give due regard to any relevant legal requirements, the provisions and recommendations in the Combined Code and the UK Listing Authority's Listing Rules and associated guidance
- 8.10. review and note annually the remuneration trends across the company or group
- 8.11. oversee any major changes in employee benefits structures throughout the company or group
- 8.12. agree the policy for authorising claims for expenses from the chief executive and chairman<sup>11</sup>
- 8.13. ensure that all provisions regarding disclosure of remuneration, including pensions, are fulfilled
- 8.14. be exclusively responsible for establishing the selection criteria, selecting, appointing and setting the terms of reference for any remuneration consultants who advise the committee
- 8.15. obtain reliable, up-to-date information about remuneration in other companies. The committee shall have full authority to commission any reports or surveys which it deems necessary to help it fulfil its obligations

## 9. Reporting responsibilities

---

- 9.1. The committee chairman shall report formally to the board on its proceedings after each meeting on all matters within its duties and responsibilities
- 9.2. The committee shall make whatever recommendations to the board it deems appropriate on any area within its remit where action or improvement is needed
- 9.3. The committee shall produce an annual report of the company's remuneration policy and practices which will form part of the company's annual report and ensure each year that it is put to shareholders for approval at the AGM

## 10. Other

---

- 10.1. The committee shall, at least once a year, review its own performance, constitution and terms of reference to ensure it is operating at maximum effectiveness and recommend any changes it considers necessary to the board for approval.

---

<sup>11</sup> It is suggested that the more common arrangement is for the chairman of the board to authorise the chief executive's expenses and for the chairman of the remuneration committee to authorise the chairman's claims. An alternative would be for the committee to authorise the expenses of both.

## 11. Authority

---

- 11.1. The committee is authorised by the board to seek any information it requires from any employee of the company in order to perform its duties.
- 11.2. In connection with its duties the committee is authorised by the board, at the company's expense
  - 11.2.1 to obtain any outside legal or other professional advice
  - 11.2.2 within any budgetary restraints imposed by the board, to appoint remuneration consultants, and to commission or purchase any relevant reports, surveys or information which it deems necessary to help fulfil its duties

*October 2007*

[BACK TO THE TOP](#)

The information given in this Guidance Note is provided in good faith with the intention of furthering the understanding of the subject matter. Whilst we believe the information to be accurate at the time of publication, ICSA and its staff cannot, however, accept any liability for any loss or damage occasioned by any person or organisation acting or refraining from action as a result of any views expressed therein. If the reader has any specific doubts or concerns about the subject matter they are advised to seek legal advice based on the circumstances of their own situation.