**THE RELEVANCE OF SHARE SCHEME GUIDANCE**  
1993  
  
  
1. Although share options are just one element of employee remuneration, shareholders are required to approve the proposals for the establishment of a scheme. Guidance issued by shareholder bodies aims to provide parameters within which companies can devise schemes with reasonable certainty of approval by major shareholders. Similarly, those shareholders generally regard schemes with increased confidence if they understand that they comply with general principles regarded as reasonable and appropriate by shareholder bodies.  
  
  
  
**SHARE SCHEMES AS REMUNERATION**  
  
  
  
2. It is recognised that share schemes can be an important part of an executive's remuneration. However, executive share schemes can deliver reward to company managements even when it is judged that the company's performance has been poor. This is not in the interests of shareholders nor is it readily understandable by the public or by employees.  
  
**It is a fundamental requirement that exercise of executive share options should be subject to some realistic measure of management performance**. The difficulties of prescribing one single measurement of long term sustained performance - which will be regarded as appropriate for all situations - is recognised. It is generally acknowledged, however, that linking the exercise of options to sustained underlying financial performance is in the best interest of the company and long term investors. Such linkage requires sustained results before any benefit can be taken by an option holder and creates a community of interest between corporate management and the shareholder.  
  
It is expected that the rules of any executive scheme should include prudent limits concerning the level of share option grant to any individual and concerning the timing or phasing of such grants.  
  
Although, by law, companies are permitted to issue executive options at a discount to the share's market price in certain circumstances, companies should note that this is viewed as undesirable.  
  
  
  
**THE MANAGEMENT OF SHARE SCHEMES**  
  
  
  
3. It is felt that a Remuneration Committee - constituted in accordance with the "Cadbury" Code of Best Practice (see Note 1) - is best placed to determine how management should be motivated to produce results which further the aim of sustained financial performance. **Any company proposing a share scheme should note, therefore, that support for the proposals is unlikely to be forthcoming unless the company has in existence a properly constituted Remuneration Committee which has formal responsibility for the scheme.** Such a Committee will be fully aware of the circumstances of the company in question and it follows that it should, therefore, be in the best position to determine the most relevant and effective performance criteria.  
  
It is important that shareholders understand the basis on which the chosen criteria have been set. Full details of the criteria which are felt appropriate should, therefore, be disclosed both when the scheme is put forward for approval by shareholders and annually thereafter.  
  
4. In concluding that the criteria should be set by the Remuneration Committee, it is recognised that some indication of what is looked for in such a formula would be helpful. The ABI and the NAPF are agreed that the aim of any formula should be to produce significant and sustained improvement in the underlying financial performance of the concern in question. Both will expect the formula to be based, therefore, on criteria which genuinely reflect the effort and achievement of the management in question.  
  
Safeguards must be incorporated by the Remuneration Committee to ensure that measures chosen are appropriate to the circumstances of the company and are used consistently. Furthermore, they must not be capable of manipulation nor must they be influenced by the particular accounting treatment of various items.  
  
5. The institutions represented by the ABI and the NAPF will be looking, therefore, at the details disclosed by Remuneration Committees to satisfy themselves that, in the circumstances of an individual company, the criteria chosen are consistent with the foregoing. The manner in which the Remuneration Committee undertakes these responsibilities will be viewed by shareholders as one of the measures of the effectiveness of a company's non-executive directors.

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| **Notes:**  **1.** *Cadbury recommends "...that boards should appoint Remuneration Committees, consisting wholly or mainly of non-executive directors and chaired by a non-executive director...". The non-executive directors must clearly be independent.*  *In its document "The Role and Duties of Directors", the Institutional Shareholders' Committee makes an assessment of the term independent. Its comments may be summarised as follows:*  *\* not to have been employed by the company in executive capacity in last 4 years;*  *\* no involvement as a professional "adviser" to company;*  *\* not a significant supplier/customer;*  *\* no participation in share options, performance related remuneration or pension scheme;*  *\* no compensation for loss of office;*  *\* no other directorships in same industry (without Board approval).*  ***2*** *The NAPF recognises that, for many years, the ABI has monitored the details of share schemes in accordance with more specific guidelines and intends to continue with this role. This considerable effort is greatly appreciated by the NAPF.* |

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15 July 1993

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