



Attracting executive talent to the listed sector

Attracting the right executives to manage the businesses in which we invest is proving increasingly difficult, due to competing demand from private companies. It is therefore critical that investors support companies in attracting the right talent. A survey conducted in the summer by the Financial Times and the Finance Directors' Forum found that almost one in three executives had received at least one job approach from private equity in the past year, and 57% of respondents believed that, in future, listed groups will find it harder to retain key executives. The article contrasted the potential for high personal earnings and an entrepreneurial culture within the private equity market with the onerous requirements of regulation and disclosure within the quoted arena.

Insight is acutely aware of the need to ensure that remuneration packages are as attractive as possible while at the same time aligning executives' rewards with shareholders' interests. We therefore continue to carefully evaluate all remuneration schemes put forward by companies in which we invest. (For previous articles on this subject, see Investor Responsibility bulletins for January – March 2005 and April – June 2005.)

Insight believes that investors should avoid being too dogmatic when reviewing remuneration proposals. For example, in certain cases, it may be appropriate for investors to support generous 'golden hellos' and share-based incentive schemes that pay out without demanding performance tests. Investors should also recognise that there may be particular reasons why companies have targeted specific financial metrics rather than TSR (total shareholder returns – a measure favoured by some investors) as the basis for determining short and long-term bonuses. Performance metrics chosen by companies to measure targets will vary, depending on an individual company's situation.

The case studies below highlight examples of companies that have recently put forward remuneration proposals with some of these features:

J Sainsbury

The J Sainsbury 2005 Share Plan applies to over a thousand employees, executives, senior management and store managers and uses two metrics to measure performance: sales targets and EPS (earnings per share). Although the

plan has relatively short-term targets, we believe that these metrics are appropriate given the current recovery strategy. The board did not choose share price or TSR as metrics because it does not believe these measures will appropriately reflect whether the strategy has been successfully implemented by management, as take-over situations and other events outside management's control could influence the outcome.

WH Smith

WH Smith recently introduced a co-investment plan that applies to board and senior management. The scheme's key feature is that executives must invest considerable amounts of their own money in the company at the outset. The rationale is that this will allow management to share in the success of the business and strongly aligns incentives with shareholders' interests. However, the scheme is unusual in that participants' initial investments will be affected if the business does not do as well as expected. Insight recommended voting in favour of the scheme.

Marks & Spencer

Marks & Spencer has introduced a Performance Share Plan that applies to approximately one hundred employees including board directors but not to store managers. The scheme uses a single performance metric – EPS (earnings per share.) We believe the performance target of growing EPS by 15% per year from an adjusted base 23.9p is a suitable target against which the company should judge its success. We were therefore comfortable recommending voting in favour of this scheme.

Barclays

When Barclays announced Matt Barratt's appointment as chairman in spring 2004, one of the issues we raised with the outgoing chairman, Sir Peter Middleton, was the absence of Barclays Capital from the board. Barclays Capital is a significant and fast growing part of Barclay's business. We were assured that the reason that Barclay's Capital head Bob Diamond had not been appointed to the board was not to keep his reward package away from shareholder and public scrutiny.

Earlier this year, this decision was reconsidered, and, ahead of the public announcement of Bob Diamond's appointment

to the Barclays board, Insight and other investors were briefed about his pay package. Although large, reassuringly, it was certainly not out of line with others in the investment banking sector. As with those of other board members, his remuneration package details will be published in the company's Annual Report and Accounts next summer.

Conclusion

Competition for talent extends from the board level to senior management and other management levels. Companies should ensure that all management levels are appropriately incentivised. Executive remuneration continues, rightly, to be a central focus of both investors and the media. Such scrutiny is essential.

We believe that Insight has responded appropriately to remuneration schemes proposed recently and has shown flexibility where appropriate. And we have done more than simply vote; we continue to have active dialogue with companies in which we invest to address governance issues as they arise, in a constructive and timely manner.

We also continue to discuss remuneration issues with key opinion formers – maintaining all necessary confidentiality with respect to specific schemes – in the hope that the City and its observers will develop a more balanced view of highly complex schemes and avoid misunderstanding and misrepresenting them.

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