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5 December 2013

Dear Catherine,

**AFM response on consultation on Directors' Remuneration**

1. I am writing in response to this discussion paper, on behalf of the Association of Financial Mutuals. The objectives we seek from our response are to:
  - Comment on the proposals in the consultation; and
  - Highlight the need for the Code to avoid transposing regulations beyond their intended audience.
2. The Association of Financial Mutuals (AFM) represents 53 member companies, most of whom are owned by their customers. Between them, AFM members manage the savings, protection and healthcare needs of over 20 million people, and have total funds under management of £120 billion. The nature of their ownership and the consequently lower prices, higher returns or better service that typically result, make mutuals accessible and attractive to consumers, and have been recognised by Parliament as worthy of continued support and promotion.
3. The AFM maintains a version of the UK Corporate Governance Code annotated for mutual insurers. We recognise that the listed companies for whom the Code is primarily aimed are many times bigger than most of our members, and also that the focus on shareholder-owned businesses does not entirely adapt to other business models. In 2012 we undertook a review of our Annotated Corporate Governance Code, and as a result the AFM Board renewed its commitment to keep our Code in step with FRC's, and that the FRC code expresses generally acknowledged good practice.
4. AFM maintains an extensive compliance exercise for our annotated Code, and reports on results to Treasury, the regulators and FRC each autumn. These reports demonstrate how effectively our members embrace good governance standards. However the one area where we have traditionally seen lower levels of compliance with the Code have been in relation to remuneration, for our very small members. This is essentially because for many of these organisations, their mutual ethos means that executive directors are paid no or minimal bonuses, and non-executives receive only a small attendance allowance or expenses. As a result, many of our members do not strive to comply with aspects of the Code focused on bonuses.

5. We have a specific concern, for 'voluntary' adopters of the Code, that FRC is amending the Code to reinforce changes to primary legislation, or is being expected to do so. This duplicates the requirements, making version control a risk in future. Of greater concern to us though is that FRC is exporting requirements beyond their intended audience, by implying that voluntary subscribers should be expected to comply in full. To illustrate, most members of AFM are not subject to Companies Act legislation, and are very clearly outside the scope of changes to the legislation provided by BIS. Hence by adopting the same requirements in the Code, FRC is presenting a new and unwarranted hurdle, the result of which will be higher costs to firms that comply, higher levels of exception reporting to firms that cannot comply, less relevance in the Code to the owners of mutuals, and greater risk that AFM and its members will be unable to support future Code developments which gold-plate or contradict our primary legislation. This is clearly an unwelcome distraction for our members, and risks undermining the principles of democratic primacy.
6. With this in mind, and looking at the specific issues raised in the consultation, we see very little value in the FRC simply transposing existing legislation, or the content of other standards, into the Code. We would prefer, with regard to mutuals, for AFM to provide a guidance note to its members, covering the impact of the legislation and exploring how that might best apply to our sector. In relation to the specific issues raised in the consultation, our response is:
- a. *Extended clawback provisions*: we welcome the government's work in this area, and firmly believe the potential for clawback of bonuses is an explicit expectation for all organisations or individuals where variable pay is high; however there does not appear to be any clear justification for amending the Code, given the extensive legislation already in place;
  - b. *Remuneration Committee membership*: we share the broader concern that there is potential conflict/ vested interest where executives of one company sitting on the remuneration committee of another. The analysis presented shows no clear evidence that this leads to greater shareholder dissent, though it is not clear from the analysis whether this reflects proper probity of directors, or lack of interest from shareholders. It would not seem appropriate to amend the Code on the basis of this evidence;
  - c. *Votes against the remuneration resolutions*: the existing Regulations appear to appropriately address this issue, and we do not see any obvious reason to amend the Code;
  - d. *Other possible changes*: we are content that the current provisions produce clear expectations and do not see any obvious areas for change.
7. We would be pleased to discuss further any of the issues raised by our response.

Yours sincerely,



Chief Executive  
Association of Financial Mutuals