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The Choice, Design and Strategic Implications of Executive Incentive Pay Schemes at the Time of an Initial Public Offering

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Abstract

This paper presents a descriptive survey of the choice and design of executive pay incentive scheme arrangements implemented at the time of a company's initial public offering. Using a unique sample of 311 entrepreneurial companies over a five year period (1998-2002) it illustrates the strategic choices made with regards to incentive pay schemes by the board of directors at this crucial time in a company's development. Furthermore, it discusses the importance of the configuration of incentive schemes in respect of three critical elements: the performance target, comparator, and target level requirement for the shares to vest. It finds that company's choices are split between schemes that do have performance targets linked and others that are contrary to the guidelines of the Combined Code and best practice. In light of this it proposes strategic reasons why this might be the case for initial public offerings and develops this discussion in line with the uniqueness of this event.

Key words: executive pay, share options, initial public offering, corporate governance

Introduction

Executive compensation packages have been increasingly used as a strategic tool to attract, retain and motivate key employees in an increasingly global labour market (Conyon, 2000). In the UK the typical executive package seen within the range of mature publicly quoted companies, will comprise a base salary (and benefits such as company car,) an annual bonus and a long-term incentive component, typically in the form of executive share options (ESOs) or long-term incentive plans (LTIPs) (Conyon & Murphy, 2000a). An overview of the components of modern executive pay can be clearly demonstrated in the following diagram:

Figure 1

Increasingly share options and LTIPs are incorporated in the executive director's remuneration package (Pass, Robinson, & Ward, 2000), indeed they are now seen as the norm rather than the exception (Conyon, Peck, Read, & Sadler, 2000b). Globally the impact of share options within the compensation package for Chief Executives within large, mature UK companies has now begun to be addressed, particular with reference to increased levels of company performance (Conyon et al., 2000a; Main, Bruce, & Buck, 1996). However, little research has been transferred to the initial stages of the development of a listed company, i.e. the transferral of entrepreneurial ownership to public ownership via the initial public offering (IPO) company.

Executive remuneration, long term incentive schemes and the IPO company

The rationale behind the use of equity based schemes can be seen to have its roots within agency theory (Fama, 1980; Fama & Jensen, 1983). The modern company, with its large dispersed ownership faces a principal - agent problem where the managers (agents) are able to make company decisions but the owners (principals) are often remote from the company (Jensen & Meckling, 1976). Within the business there are a wide variety of decisions and actions that face the board of

directors (as agents) that might lead to them being accountable to the shareholders as owners. Prior to the IPO, much accountability for such actions would remain in-house, however following the IPO, shareholders will want to ensure that the actions and decisions taken by the board of directors are enhancing the value of the company (Rappaport, 1981). Thus the first agency problem is highlighted as shareholders will typically, being outside the company, not know what direct actions will enhance the company value (Jinghui & Dennis, 2008). Even if they did, imparting this on the board of directors whilst being outside the organisation would be almost impossible.

As a result of this, and in order to provide a solution to the principal agent problem, outcome based contracts such as the incorporation of executive incentive pay schemes have often been adopted (Fama, 1980; Fama et al., 1983). This not only enables the executive (at a future date) to become a part owner of the company, it also provides a positive attempt to tie a proportion of the executives pay directly to shareholder values and wealth (Association of British Insurers, 2005).

Much of the current literature on executive pay focuses on the pay performance links established from option holdings (see Hallock & Murphy, 1999 for an overview). One of the most widely cited estimates of the pay performance link in the mature company is that of Jensen and Murphy (1990), who reported that total CEO wealth changed by \$3.25 for every \$1000 change in shareholder value. Similarly this was re-enforced by Hall and Leibman's (1998) study which showed that there was a doubling of the pay performance sensitivity between the period 1980 – 1994. This seems to provide a positive picture with regards to the pay-performance link, but links are only deemed to be weak (Canyon & Leech, 1994; Gregg, Machin, & Symanski, 1993; Jensen et al., 1990). This seems to infer a rosy picture with regards to CEO wealth; however the important point here for an IPO company is not necessarily the changes in the pay-performance size but a more complex issue of how such schemes are used and might motivate the person. In order to fully discuss such issues in

line with the IPO company an understanding of the different types of schemes available must first be sought.

Long term incentive pay strategies

Long-term incentives have now been accepted as the norm within the global executive pay package (Deloitte & Touche, 2005). Indeed, within the USA they have emerged as the single largest component of executive compensation (Conyon, Peck, & Sadler, 2000c; Hall & Murphy, 2002).

The development of such strategies proves to be a direct attempt to motivate executives to improve company performance and align their interests with those of the company's shareholders as per agency theory (Bender & Moir, 2006). In theory, the rewards received through such schemes should reflect added shareholder value (Aggarwal & Samwick, 2006). Long term incentive strategies with regards to pay tend to take one of two main forms, namely the Executive Share Option (ESO) or the Long Term Incentive Plan (LTIP). Developments in disclosure following the recommendations for greater transparency in various government initiated reports (Cadbury, 1992; Greenbury, 1995; Hampel, 1998a, b; Higgs, 2003) and the adoption of The Directors' Remuneration Report Regulations (2002) means that the grants and holdings of such compensation elements can now be incorporated into any empirical study on executive compensation (Johnston, 2005).

Typically in the UK all long-term incentives should now have some form of performance criteria attached (Association of British Insurers, 2005; Financial Reporting Council, 2006). Indeed Greenbury (1995) recommended that all Remuneration Committees should design such schemes that are subject to 'challenging performance criteria' (section 6.38) and subsequently this has been incorporated in The Combined Code on Corporate Governance (2006). Such schemes can now be seen as a standard instrument to link pay to performance throughout many UK companies although,

post Greenbury, a wide and often complex variety of company ESO and LTIP schemes have been developed (Thompson, 2005).

The standard UK executive share option provides the executive with the right (but not the obligation) to purchase shares at a fixed, predetermined price (exercise or strike price) following some specified period of time (Conyon, 2000). Within the UK, as previously mentioned these often have performance criteria attached, thus preventing the executive from exercising their right to purchase until such criteria have been met (Association of British Insurers, 2002). Performance criteria are seen to be inline with measurements of growth required by shareholders reflecting profitability, such as earnings per share. These will be discussed in more detail later.

As opposed to ESOs where executives have the right to purchase shares, the long term incentive plan awards a grant of shares (at zero cost) that vest (i.e. transfer ownership to the executive) upon the attainment of pre-determined performance criteria. Typically such schemes are run over a ten year period, with the shares vesting to executives after a period of three years.

Performance evaluation

Inspection of incentive pay schemes and their performance criteria shows that conditional schemes have three interrelated elements: a performance target measure, a comparator and a performance target; and operate over a specified time period, typically three years (Pass et al., 2000). All three components must be considered by anyone attempting to describe or evaluate any incentive pay scheme.

Performance target measures

Ideally any performance measure set by a company will be simple for both executives and investors to understand, provide a balance between the results for shareholders and factors that are within the

control of the executives and should be correlated to the creation of shareholders value if the scheme is seen to be an attempt to re-align the executives motivation with those of the shareholders. There are two main issues to consider when deciding upon a performance measure, namely whether it should be accounts based or stock market based. It is generally considered that EPS is more accounts based, reflecting profitability, whilst TSR is stock market based.

An accounting based measure, such as EPS, may be preferable, as they are not subjected to general trade shocks, which can influence the share price. It is aligned to shareholders' interests in that it reflects the profitability of a company and thus dividends paid to shareholders, it does not reflect market value. It is however easy to show a short-term gain in this figure by acquiring a company with a lower P/E ratio. Thus it could be deemed to encourage takeover activity and a focus on company size rather than performance.

TSR, the market based measure, again could be considered to reflect the aspirations of shareholders in that share price is seen as part of the reflection of the overall present value of the company.

Furthermore, executives' immediate actions are seen by the city and thus this is reflected in share price too. However, it too has a number of drawbacks. TSR is composed of dividends paid and the capital appreciation as measured by the change in share price. So it can give a distorted picture of performance in that it may reflect expected value (fuelled by city rumours). In this way it could reward an executive before value has been delivered or alternatively, not at all if the value is not realised until after the executive has left. Thus TSR is affected by many factors that are well beyond the control of the company executives, so may be considered to be inadequate as a measure of management performance.

Thus performance measures have to be considered very carefully by the Remuneration Committee.

An overwhelming number of UK companies use 'earnings per share' as the performance criteria

attached to stock options, with the next favourable measure being the stock market based measure 'total shareholder return' and a few companies still use share price as the benchmark. However, if one looks towards LTIPs then this trend is reversed with TSR being the more popular measurement (Pass et al., 2000).

Performance comparators

A measurement alone is of little significance, it needs to be brought into perspective and this is the role of the comparator. Comparators, namely the FTSE, peer groups or the Retail Price Index, all look towards external elements. The Retail Price Index, detailing the level of inflation, seems to be a popular comparator for many UK option schemes (Pass, 2003). This measure however is influenced predominantly by factors beyond company performance and can be seen to be relatively low since 1995.

By contrast, LTIPs focus predominantly on inter-company measures. As these have predominantly developed post Greenbury, this can be seen to be in line with its recommendations that company performance should be set against a group of comparator companies. This measure may be seen as more realistic than that of RPI and takes steps to negate any industry effects that may become apparent over time.

Performance target figures

The level of performance standard required to trigger a payment is the performance target. This can be one figure or a combination of figures often given on a sliding scale. Typically for options that use RPI as their comparator this would be some percentage above the RPI for the year.

'Success or 'failure' can then be categorised in terms of achieving the predetermined company set target. However, with different values across many different companies, comparison between the

effectiveness of executives is more problematic than simply seeing rewards given for a target achieved. For example achieving 1% above RPI is significantly easier than achieving 4% above. This also brings into question how ambitious the target figure really is, large payouts may simply be indicative of the requirements for higher targets rather than demonstrating effective executives. By contrast, some companies will see more rigorous targets against those higher in the FTSE or more prestigious within their peer group comparisons.

Thus the payout thresholds simply being translated into 'successful' or 'non successful' companies may hold little truth for effective company performance. Similarly can be the case with both EPS and TSR figures. These also provide particular difficulties for the IPO company as the benchmark for such comparators is relatively unknown when they are set prior to the flotation of the company.

Methods

The Data Sample

The data sample has been collected from those companies floated on the London Stock Exchange (Main market and the TechMark) and the Alternative Investment Market (AIM) over a five year period from 1 January 1998 and 31st December 2002. The data sample used in this analysis comprises of a unique data set of initial public offering companies that have founders on the boards of directors at the time of flotation. The listings for the study have both been sourced from the London Stock Exchange's market statistics for New Issue and IPOs. For the given period, the London Stock Exchange lists shows that 872 companies were floated as initial public offerings. An initial exclusion of any companies with non UK incorporation took place, as this might be seen as leading to different governance structures. The IPO prospectuses for all remaining 766 UK companies were obtained. These were predominately obtained from Thomson Research, which provides a comprehensive coverage of company filings for publicly quoted UK companies. Missing prospectuses were obtained either via company web sites, or by telephone/written request

to the companies or their advisors whichever was deemed more appropriate. The data sample used in this analysis comprises of a unique data set of initial public offering companies that have founders on the boards of directors at the time of flotation. Unit and investment trusts were excluded from the sample (these have particular governance characteristics) along with any company involving a de-merger, merger or acquisition, corporate spin off, equity carve outs, reorganisations, or those that could be considered as solely acquisition vehicles (Filatotchev & Bishop, 2002). This resulted in 311 companies who clearly demonstrated that they had been developed via the entrepreneurial process with entrepreneurial founders and those founders were serving as directors at the time of the company's flotation.

Results and Discussion

From the initial investigation of the 311 companies, 126 had incentive pay schemes operational for the board of directors prior to their IPO. Indeed these companies were able to disclose valuable information about their schemes in their prospectus document. More importantly, 172 companies introduced executive pay schemes at the time of (or immediately prior to) going public. Of those implementing their initial incentive pay scheme 77 companies chose to introduce conditional performance based Executive Share Option Schemes only, whilst 2 companies implemented conditional ESOs and LTIP schemes. Of the remaining companies, 76 chose to implement unconditional scheme and 17 did not declare whether their scheme was conditional or unconditional. Only 13 companies chose not to introduce an incentive pay scheme. As can be seen from Table 1, there is almost an even division between those implementing unconditional schemes and those who tie their schemes to performance criteria at their initial public offering.

Table 1

Whilst it is encouraging to see that companies without incentive pay at the point of their flotation implement schemes, only 79 companies that have disclosed the use of conditional schemes that can be seen to help promote the alignment of executive and shareholder interests by the imposition of performance targets linked to increasing shareholder value. The others are yet to employ what is considered to be the ‘best practice’ recommendation of the Greenbury Report (1995) and ABI guidelines (Association of British Insurers, 2005).

Performance evaluation

As discussed earlier, performance criteria for conditional schemes have three interrelated elements, i) a performance target measure, ii) a comparator and iii) a performance target ; and operate over a specified time period, typically three years. Ideally, any performance measure set by a company will be simple for both executives and investors to understand, provide a balance between the results for shareholders and factors that are within the control of the executives and should be correlated to the creation of shareholders value if the scheme is seen to be an attempt to align the executives motivation with those of the shareholders.

For the 79 companies with performance criteria attached to their implemented scheme, the most popular by far was the measure of earnings per share (EPS).

Table 2

Table 2 details the performance measures required for schemes in this sample in order for them to vest to the executive. As can be seen from Table 2, the accounting based EPS is the most popular measure for this sample specified growth in share price and profitability being the second most popular. For the IPO company, these two measures provide particular relevance. Firstly, for earning per share, having never been previously traded, there is no real reference for the

benchmarking of this measure to prior performance. Secondly, with regards to share price growth, this would be most advantageous for the executive, as gains from options are the difference between the exercise price and the share price. This too might provide an ideal measure for shareholders who would also be looking at increased prices for their portfolio. Similarly with the measure of increased profitability, this could be considered to be beneficial to the external investor who would presumably benefit by increase profits being passes on to investors via dividends.

Selecting an appropriate target level can be controversial particularly more so for the IPO company. Performance may be judged against the company's own self-selected target (for example, a requirement that the company's own EPS growth over the next 3 years must be at least equal to that of the previous 3 years growth), or an external comparator/target may be used, for example a requirement that the company's EPS growth must exceed the increase in the RPI by at least 6% over a 3 year period. Either way companies often find themselves criticised for setting targets, which are too easily achieved. This can be even harder to assess for the IPO company, which may not have years of trading data to realistically base future targets on. Also disappointingly, there is a lack of transparency and disclosure with the companies in this sample, with 18 companies failing to reveal details of their chosen performance target measure.

A caveat has to be mentioned here, with regards to the missing measures, comparators and targets.

Whilst attempts have been made to verify the schemes where there is a statement that there is a performance target, some still remain unknown. Although the disclosure of such schemes has improved over the latter years, this only took place after the sample years of this research.

Although subsequent Annual Report and Accounts have been examined, especially in light of The Directors' Remuneration Report Regulations (2002), this has still resulted in missing information as only schemes in existence need be reported. The missing data has resulted due to two instances, the main being that the company no longer exists, often due to failure or sometimes due to mergers and

acquisitions, and grants have ceased. The second reason being that the initial scheme has subsequently ceased, thus there are no requirements for reporting in accounts.

Table 3 presents details of the incentive scheme comparators selected by the IPO companies. It must be noted that internal comparators predominate, i.e. own EPS, own share price growth, individual targets (35 companies) over peer group reference although overall RPI is the main external comparator, with 18 companies choosing this comparator.

Table 3

As noted above, the achievement of a specific performance ‘target’ is required in order to enable executives to exercise their options and LTIP awards. The actual target levels set are thus crucial in this regard. Target levels may be relatively undemanding or they may be stretching. Whilst this may be difficult for the IPO company to assess, many mature companies have been criticised by investors for setting an ‘easy’ threshold target for their incentive schemes and have subsequently set tougher target levels (Pass, 2003). Comparing the degree of difficulty in achieving performance targets for schemes which have the ‘same’ performance measures and comparator but which have different target levels is straightforward. Furthermore, this might have a particular impact on the IPO company as previous levels are not available to benchmark against. Furthermore, their might be another particular challenge for the IPO company and their remuneration committee, who might not have such experienced members as the mature company. Similarly, inter-scheme comparisons also become problematic. For example, how does one compare the degree of difficulty of two schemes one of which requires EPS growth to exceed the increase in RPI by 5% over 3 years with that of a scheme which requires the company’s share price growth to exceed that of the average share price growth of a ‘peer group’ of companies?

Table 4, combines together all known performance measures, comparators and target levels for the 79 companies implementing schemes at the time of the IPO. As can be see the IPO companies operate a diverse range of schemes which makes it nigh impossible to make any definitive comparisons at this micro level.

Table 4

Whilst making direct comparisons on Table 4 would have no value, some generalised observations can be made. The presumption underlying incentive pay is that with the dilution of ownership and control there will be a principal-agent problem. Interestingly, even prior to IPO, 126 companies in the sample had incentive pay schemes in place. This may seem surprising given the fact that the founding owner was also a key executive director of the company. In such circumstances the potential principal-agent conflict should not materialise since the interests of the owner (as ‘principal’) and executive (as ‘agent’) are one and the same. However, even in these cases the use of incentive pay schemes for other executive directors could be seen as important as an inducement in attracting high calibre executives to the board, as a means of encouraging loyalty and commitment to the company and to reward their efforts over and above basic salary by giving them a stake in the growing prosperity of the business.

An important consideration at IPO, however, is that companies should be concerned to have incentive pay schemes in place. The IPO nature of the data does mean that many of these companies do not have to fully comply with the Combined Code. This is only applicable to companies listing on the main market (the official list). Many of the new listings reflect the growing trend to float on the Alternative Investment Market (AIM) and thus do not have the need to comply with the Combined Code. However, they are still subject to agency theory and the guidelines for AIM flotation perhaps do not emphasis strongly enough the importance of ‘best

practice' for public companies and the influence that incentive pay schemes can have as a governance tool. This may explain the more relaxed nature of implementing unconditional rather than conditional schemes as 72 percent of the companies in this sample were AIM IPOs.

Notwithstanding this, companies with performance targets are able to send a much stronger 'strategic signal' to prospective investors (i.e. shareholders) that they will be particularly mindful of their responsibilities to protect and enhance the interests of shareholders and thus provide better future returns for shareholders than those companies without such schemes. This might have an influence over the offer price and short term performance. With the flotation marketplace, it may be much more important to gain the 'right' investors at this uncertain time and period of potential growth and good corporate governance strategies will aid this.

Creating better pay strategies

Creating better pay strategies bring human resource management into the competitive business strategy of the firm. Boxall and Purcell (2003) argue that strategic HRM is concerned with explaining how HRM influences organisational performance and this is particularly relevant to incentive based pay strategies. The descriptive results show the popularity of incentive based equity packages however, the actual value the executive ties to share options is questionable. Hall (1998) proposes that executives have no real idea as to the value and wealth held within their unexercised options.

One of the main significances of options is that they allow for large swings in their payouts, which can be either positive or negative. However just imagine, for a moment, a corporate world without options. Any changes in pay would have to come from basic pay and short term payment of bonuses. It is unlikely that these two components could parallel the high powered impact that options can have; it is also unlikely that the IPO company could afford to pay high salaries and

bonuses to attract executive directors to the board. Also, as a newly floated company, large basic salaries and bonus are likely to attract the attention of future shareholders and may have a dramatic impact on the issue price and the capital raised at the IPO. A new company would not want to risk adverse the media and the public criticism about large salary payments.

On the downside, decreases in salary are naturally resisted by executives. Members of the remuneration committee generally serve on more than one board of directors and executives can also be non-execs on other boards so they would be reluctant to decrease pay. Whilst it may not be the case that directors are paired on the same boards, when setting pay as part of the remuneration committee they also have their own interests at heart. In trying to consider the top rate for executive directors they are in turn playing a part in factoring their own levels of remuneration via other board of directors' decisions. It is therefore unlikely that base salary and bonus alone would ever be able to provide the same motivation and 'high powered' incentive that options could give.

This study has two types of options, namely 'unconditional' and 'conditional'. In the UK options are issued "at the money" that is to say the exercise price is equal to the prevailing market share price. This has particular implications for options issued at the time of the IPO with regards to the pricing of the shares at the IPO.

Consider the scenario of the executive that had been issued an unconditional option. These confer the right (but not the obligation) to purchase shares in the company at the given price some time in the future (but with the limits of the maturity date imposed). Options generally 'vest' to the executive after a period of three years; they then have a further seven years to exercise their rights over the options. With unconditional options the executive simply have to hold their shares following vesting until they are 'in the money' i.e. their exercise price is lower than the share price in order to make a gain against the prevailing share price. So the risk to the executive is spread

over the ten year period, thus enabling decisions to be made with, rather than against, market fluctuations.

Conditional options have greater risk for the executive. They have much the same principles as unconditional options when considering value and gains against share price. However, if the performance conditional associated with the grants are not met, the options do not vest to the executive and thus the rights to then exercise conditional options are lost and the option becomes worthless. Thus reaching the performance target is paramount for the executive to make any option gain. By comparison to unconditional options, conditional ones carry far greater risk of no return.

The fact that the use of options has grown over the sample period for FTSE firms (IRS Employment Review, 2000) and that options make up approximately 40% of overall earnings of FTSE 100 companies in 2003 (PWC, 2005) shows the importance of their presence in top management contracts even past the sample date they are still seen to boost directors' earnings substantially (IDS, 2005) so they can not be ignored.

The strategic advantage to the company is that options minimise their costs. For accounting purposes options are able to be valued using the Black-Scholes model. This means that a typical value of an 'at the money', ten year option is roughly a third of the value of the underlying share. Thus the 'profit' gained by the executive is from the external sale in the marketplace and not a cost borne by the company.

Concluding remarks

Even in the case of those companies which adopted a conditional option scheme, there remain a number of questions. Firstly, many of the performance 'targets' appear to be undemanding and will

need to be made ‘tougher’ in order to satisfy investor bodies such as the National Association of Pension Funds and the Association of British Insurers, which look to, for example, an EPS/RPI +9% over three years as a minimum yardstick.

Secondly, the ‘preference’ of companies to use their ‘own’ rather than external comparators maybe, in the eyes of some critics, too introverted and myopic. A more objective ‘test’ of performance is to compare your performance against some other external comparator rather than ones own previous performance, since the former gives some indication of relative performance. Ideally it is argued, the comparator should be a ‘peer’ group of other companies in the same line of business activity. This would enable investors to judge whether the company’s performance was mediocre or truly excellent.

Thirdly, in a substantial number of cases a big problem is the lack of transparency and disclosure. At IPO 18 of those implementing conditional schemes had failed to fully reveal their performance criteria and this has often remained the case. Clearly this is an unsatisfactory situation and undoubtedly shareholders will bring pressure to bear on this matter. Similarly, an element of shareholder dissent may be directed at those schemes that are ‘unconditional’ or where selected performance targets appear to be undemanding.

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Figure 1: An overview of executive compensation structures (page 2 in text)

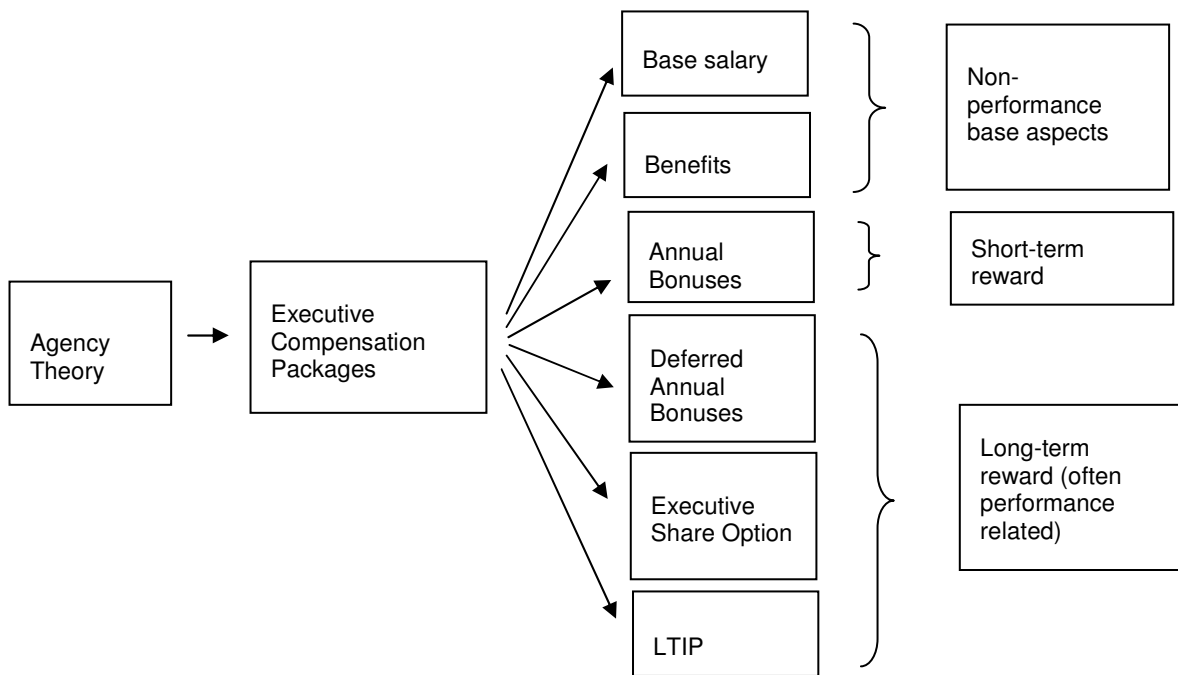


Table 1: Companies implementing incentive pay schemes for the first time at IPO (approximate placing on page 10)

Description	1998	1999	2000	2001	2002	Total
Executive Share Option Scheme (unconditional)	6	8	32	20	10	76
Executive Share Option Scheme (conditional)	12	8	35	17	5	77
Executive Share Option Scheme (conditional) & Long Term Incentive Plan (conditional)	0	0	0	1	1	2
Executive Share Option Scheme (un-stated as to conditional/unconditional)	2	3	12	0	0	17
Total	20	19	79	38	16	172

Table 2: Performance measures for ESO schemes and LTIP (approximate placing on page 11)

Performance Measures	1998	1999	2000	2001	2002	Total
Budget targets	0	0	1	0	0	1
Distributable reserves	0	0	1	0	0	1
Earnings Per Share (EPS)	11	4	4	5	2	26
Earnings Per Share and Share Price	0	0	1	0	0	1
Individual Executive Basis	0	0	4	4	0	8
Market Capital	0	0	2	0	0	2
Profit Before Interest and Taxation (PBIT)	1	0	3	4	1	9
Share Price	0	3	3	2	1	9
Share Price & Net Asses Value	0	0	1	0	0	1
Total Shareholder Returns (TSR)	0	0	0	0	1	1
Turnover	0	0	2	0	0	2
Not stated	0	1	13	3	1	18
TOTAL	12	8	35	18	6	79
LTIP						
Earnings Per Share (EPS)	0	0	0	1	0	1
TSR	0	0	0	0	1	1

Table 3: Performance comparators for ESO schemes and LTIPs (approximate placing on page 13)

Performance Comparators	1998	1999	2000	2001	2002	Total
Own Earnings Per Share (EPS)	5	1	1	1	2	10
Individual Executive Basis	0	0	4	4	0	8
Own EPS and share price	0	0	1	0	0	1
Own Market Capital	0	0	2	0	0	2
Own PBIT	1	0	1	3	1	6
Own Share Price	0	2	1	2	1	6
Own TSR	0	0	0	0	1	1
Own Turnover	0	0	1	0	0	1
Retail Price Index (RPI)	6	3	5	4	0	18
FTSE all share	0	1	1	0	0	2
FTSE 250	0	0	1	0	0	1
Not stated	0	1	17	4	1	23
TOTAL	12	8	35	18	6	79
LTIP						
Retail Price Index	0	0	0	1	0	1
Peer Group of Companies	0	0	0	0	1	1
TOTAL	0	0	0	1	1	2

Table 4: Performance measures, comparators and targets for ESO schemes and the LTIP
(approximate placing on page 14)

No co's	Measure	Comparator	Target: all over 3 years unless otherwise stated
1	Budget targets	Not stated	Not stated
1	Distributable reserves	Not stated	Not stated
3	Earnings Per Share (EPS)	Own earnings per share	Not stated
1	Earnings Per Share (EPS)	Own earnings per share	+3%
1	Earnings Per Share (EPS)	Own earnings per share	+8%
1	Earnings Per Share (EPS)	Own earnings per share	+15%
4	Earnings Per Share (EPS)	Own earnings per share	Specified EPS value
1	Earnings Per Share (EPS)	RPI	+0%
3	Earnings Per Share (EPS)	RPI	+2%
1	Earnings Per Share (EPS)	RPI	+ 3%
5	Earnings Per Share (EPS)	RPI	+ 5%
1	Earnings Per Share (EPS)	RPI	+ 6%
1	Earnings Per Share (EPS)	RPI	+ 8%
2	Earnings Per Share (EPS)	RPI	+ 9%
1	Earnings Per Share (EPS)	RPI	+ 10%
1	Earnings Per Share (EPS)	RPI	+15%
1	Earnings Per Share and Share Price	Earnings Per Share and Share Price	Specified values for both earnings per share and share price
8	Individual Executive Basis	Individual Executive Basis	Not stated
2	Market Capital	Market Capital	Exceed value specified at grant of option
6	Profit Before Interest and Taxation (PBIT)	Own Profit Before Interest and Taxation (PBIT)	Exceed value specified at grant of option
3	Profit Before Interest and Taxation (PBIT)	Not stated	Not stated
5	Share Price	Own Share Price	Exceed value specified at grant of option
1	Share Price	Own Share Price	Increase by 9 times value of flotation price
1	Share Price	Own Share Price	+37.5 + 150% sliding scale of grants to vest
1	Share Price	Own Share Price	+250%
1	Share Price	RPI	+5%
1	Share Price & Net Asses Value	FTSE Allshare	> FTSE allshare & net asset value per share doubles over 3 yr period
1	Total Shareholder Returns (TSR)	Own TSR	+100%
1	Turnover	Own Turnover	Turnover to exceed £20 million
1	Turnover	RPI	+5%
18	Not stated	Not stated	Not stated
LTIP			
1	EPS	RPI	+ 8%
1	TSR	Own TSR	+ 100%