SHARESOC REMUNERATION GUIDELINES – SMALLER COMPANIES

Setting Pay in Public Companies

This document gives ShareSoc's guidelines for the remuneration of Directors in smaller public companies.

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Summary

ShareSoc has developed its Remuneration Guidelines specifically for companies with less than £200 million market cap. Small companies are less complex than large companies and their remuneration should reflect this. The ShareSoc guidelines are consistent with the principles of the QCA Remuneration Committee Guide (which is designed for Small and Mid-Size Quoted Companies), but ShareSoc provides specific guidance on levels of salary, incentives and the percentage of equity dilution.

Salaries

Salaries should not be more than median of comparable sized companies. For a CEO, the following show what is reasonable.

Turnover £m	1	2	3	5	10	25	50	100	250
Salary £	125,000	136,000	139,000	148,000	158,000	196,000	245,000	300,000	366,000

Market cap £m	0-3	5	10	25	50	100	250
Salary £	100,000	127,000	154,000	175,000	205,000	244,000	333,000

Bonus

Fast growth companies should conserve cash. ShareSoc prefers such companies to reward management through equity incentives. Once a company is profitable, a bonus may be appropriate. For a profitable company, the maximum bonus for a CEO should not be more than 100% of salary: a lower limit is often sufficient.

Share Incentives

Share Options are a simple and clear incentive for managers of small companies. The exercise price of share options should be set at not less than the market price at the date of grant. **LTIPs and nil cost options, with complex performance conditions are unnecessary for small companies and should not be used.** Value Creation Schemes should also not be used.

Dilution should be less than 10% of equity over a 10-year period. This can be front ended, but some should be reserved for top ups and new recruits.

A typical structure might be 2% for the CEO with another 3% for top team, so the CEO and top team have 5%, but how this is shared out will depend on the roles and skills of the top team.

Disclosure

There should be clear disclosure of remuneration in the annual report and shareholders should asked to vote on remuneration and share schemes.

ShareSoc's 5 Pillars of Good Remuneration

These Remuneration Guidelines are based upon and supported by 5 underlying Pillars:

1. **Performance Linkage:** There should be a demonstrable linkage between historic pay and performance (shown by 6 year TSR graph, Single Figure Remuneration and % of maximum pay-outs from bonus and options/long term variable pay).
2. **Pay Level:** Remuneration (salary, equity incentives, bonus and benefits) should be demonstrably reasonable. This is measured in terms of:

    i) £ amount.

    ii) % share of revenue, profits, cash flow, market cap, increase in market cap, dilution, etc.

3. **Share Ownership:** Management should own and retain significant amounts of shares in their company.
4. **Clarity and Transparency.** Remuneration policies should be clear and easily understandable by investors.
5. **Good Remuneration Governance** – independence, consultation, disclosure, voting and sound business practices.

The ShareSoc methodology looks at each of the 5 Pillars of Good Remuneration, but does not give weightings to each of them. We believe that in some cases that a particularly bad approach for any one of the pillars could result in a bad overall assessment for a company. We do not want companies to be able to trade off a good assessment under one pillar with a poor performance under another.

Our focus is on the CEO’s remuneration (or Executive Chairman or highest paid director as the case may be). In nearly all cases with smaller companies, if the CEO’s remuneration package and awards are reasonable, then this will be reflected acrss the board and management structure.

PILLAR 1 - Pay for Performance Linkage

1.1 Principles

ShareSoc expects that pay should be linked to performance and shareholders should have a say on pay (see Pillar 5). Poor performance should not be rewarded with high pay, nor should mediocre performance be rewarded with high pay. High pay may be acceptable when performance is very good.

Pay should be linked to performance over a period of years. Companies should show the relationship of performance and pay, together with a commentary to explaining both the linkage and the reasons for lack of a relationship. Doing this will help build trust between investors and the company.

PILLAR 2 - The Level of Remuneration

2.1 Remuneration Principles

Salary (and benefits) should be reasonable. Most incentives should be equity based. Companies that pay less than average in cash may provide more generous equity incentives. Bonuses should not normally be paid unless the company is profitable.

The remuneration of the CEO sets the tone for the rest of the organisation. It should not be excessive. It should be demonstrably reasonable against peer benchmarks, measured in terms of:

i) £ amount.

ii) % share of revenue, profits, cash flow, market cap, increase in market cap, dilution, etc.

The CEO remuneration should not be overly large in comparison to the rest of the organisation. Excessive pay differentials are likely to be demotivational, unless there are special reasons which can be clearly explained to employees and shareholders.

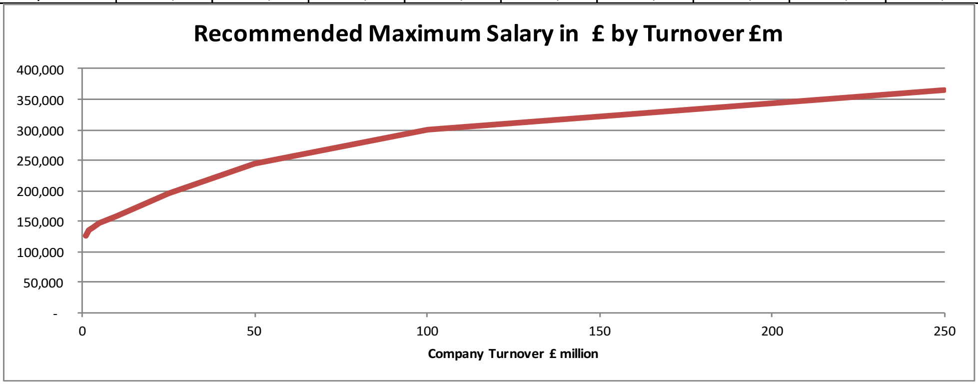
2.2 Salaries

The CEO’s salary should be set on appointment and thereafter should normally only be increased in line with the average increase awarded to employees. A CEO is paid to perform and when he/she does, an increase in salary is not necessary, as he/she will be rewarded through incentives.

Salaries should ideally not be more than the median (of other companies) and certainly not excessively more. ShareSoc’s Recommended Maximum Salaries are shown in the graphs below. Salaries increase with the size and complexity of the company. The turnover or market cap is a good proxy for complexity. For a CEO, the following graphs show what is acceptable to ShareSoc. For example, ShareSoc believe that a £50m turnover company should pay their CEO a salary of not more than £245k pa.

Recommended Maximum CEO Salary in £ by Turnover £m

Turnover £m	1	2	3	5	10	25	50	100	250
Salary £	125,000	136,000	139,000	148,000	158,000	196,000	245,000	300,000	366,000

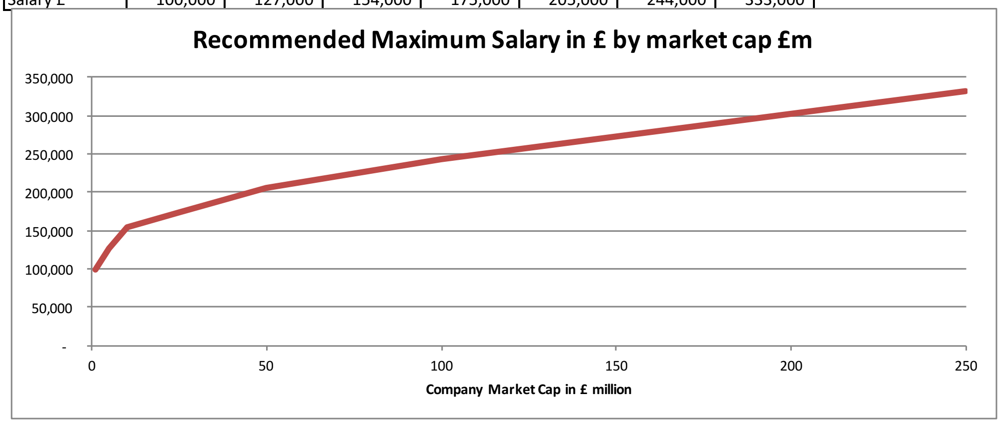


ShareSoc recognises that some sectors have significant revenues but minimal profits; this should reduce the level of what is a reasonable salary. Conversely, high margin businesses may warrant higher salaries. The ShareSoc guidance permits flexibility to allow for the type of company.

Recommended Maximum CEO Salary in £ by Market Cap £m

An alternative way to benchmark salary is to look at the market cap of the company. This is notoriously unreliable as share prices and market caps go up and down by considerable amounts and very rarely do salaries go in tandem with such movements. Some (weak) remuneration committees ratchet up salaries when market cap increases, but do not even consider adjustments the other way. With this proviso, the following table and graph show the ShareSoc Maximum Recommended Salary for companies with market caps at the following levels:

Market cap £m	0-3	5	10	25	50	100	250
Salary £	100,000	127,000	154,000	175,000	205,000	244,000	333,000



2.3 Equity/Share Incentives

Share Options are a simple and clear incentive for managers of small companies. The exercise price of share options should not be set at less than the market price at the date of grant. LTIPs (see Glossary) and nil cost options, with complex performance conditions are unnecessary for small companies and should not be used. Value Creation Schemes (see Glossary) should not be used.

Dilution should be less than 10% of equity over a 10 year period. This can be front ended, but some should be reserved for top ups and new recruits.

A typical structure might be 2% for the CEO with another 3% for the top team, so the CEO and top team have 5%, but how this is shared out will depend on the roles and skills of the top team.

Typically, there should be another 3% for other managers and all employees; with another 2% in reserve for new recruits. (Note leavers' awards will usually fall back into the pool, so there will be more than 2% available in practice.)

Potential gains from this approach are sufficient to incentivise management, see table below:

Share price increase multiple x	**Management share option gains from 10% dilution**		
5x	£4m	£12m	£40m
3x	£2m	£6m	£20m
2x	£1m	£3m	£10m
	£10m	**£30m**	**£100m**
	Market cap at start		

For example, if the share price increases fivefold (5x), and the company was £30 million market cap when the options were granted, then the market cap will grow to £150 million and if the management (including directors) had been awarded options over 10% of the shares, their collective option gains would be £12 million.

We believe that a fast growth company should be targeting at least doubling its returns to shareholders (i.e. share price plus dividends) over the planning period. The smaller the company, the larger will be the expectation of growth. Modelling the potential gains, using illustrative changes in share prices, identifies the potential rewards from equity incentives: the company and its shareholders can then decide if the potential rewards are appropriate.

Equity incentives encourage management to build up and retain significant stakes in their company. Shareholders should view with concern companies whose management sell down their stakes.

Share Options should not be exercisable for at least three years after grant. (ShareSoc prefers 50% of options to vest after 3 years and 50% after 5 years. This creates a longer term focus and reduces the possibility that the CEO will request a large top up incentive after 3 years have elapsed.)

EMI (Enterprise Management Incentives - see Glossary) are highly tax effective for management and for companies and should be implemented whenever the company meets the qualifying conditions.

Sharing Success with employees

EMI options can provide a share in success when awarded in small amounts to all/most employees.

Awards of shares to all employees under a SIP (Share Incentive Plan - see Glossary) can be very tax effective. Reserving 5% of profits for all employee profit sharing distributed via a SIP can be one way to help avoid divisiveness and encourage a culture of all sharing in success together.

2.4 Bonuses

Start up companies should conserve cash, as should fast growth companies. ShareSoc prefers such companies to reward management through equity incentives. Once a company is profitable, a bonus may be appropriate.

For a profitable company, the CEO's maximum bonus should be 100% of salary: a lower limit is often sufficient. Payment of half of the bonus in cash and half in shares (e.g. as nil cost options) that must be held for at least three years is encouraged. In general, the higher the bonus, the more that should be paid in shares.

The performance measures that determine bonus should link to the key strategic milestones and KPIs shown in the strategic report in the annual report.

In exceptional circumstances, a bonus may be paid to a CEO of a loss making company. In such cases, the maximum bonus should be 50% of salary and it may be better to pay this in shares in order to conserve cash. A bonus may be appropriate in some pre-revenue/pre-profit companies, where it is linked to measurable and stretching milestones along the path to commerciality.

Companies should have a clear policy on how profits are split between the bonus pool, dividends and reinvestment in the business and explain this to its shareholders.

2.5 Adjustments to incentive targets

Where the incentive scheme rules permit, any adjustments to incentive targets (e.g. as a result of issuing new shares, raising or paying off debt, acquisitions or disposals, decisions re whether items are exceptional or trading) must be fair to both shareholders and management. Softening of targets so as to increase incentive scheme payments is an unacceptable practice.

2.6 Reloading/Repricing

Reloading or re-pricing can potentially occur when a company's share price has reduced. If the share price reduction is a result of management's performance, then ShareSoc will (normally) expect some of the management to have left. Under such circumstances, ShareSoc would agree with the need to re-incentivise the rest of the team. However, it may not be necessary to award as much equity as before, as there should be scope to grow the market capitalisation substantially and increases in shareholder value of 5 times or even 10 times may be possible in such circumstances. Careful modelling of potential outcomes is required and will justify what the appropriate rate of dilution should be in such circumstances.

2.7 Fair rewards through the cycle

Some business sectors are notoriously cyclical. A company that invests at the top of the cycle may find its share price subsequently declines by 50% or even 90%. Issuing management with new incentives at the bottom of the cycle, which pay out for failing to get back to the original situation is highly dubious. Shareholders should look for fair rewards through the business cycle.

PILLAR 3 - Management Share Ownership

3.1 Share Ownership Principles

Management should build up and retain significant stakes in their businesses. Stakes should be both personally material and represent a reasonable percentage of outstanding shares.

ShareSoc would like the major part of management's rewards to be linked to increases in the share price over the long term.

Management should not normally sell shares in their companies. If they do, they should explain clearly the reasons why they are doing so.

3.2 Example Analysis

Shareholders should review the share ownership of the CEO over the past several years, e.g.:

Year	2010	2011	2012	2013	2014	2015
Number of shares owned	100,000	100,000	150,000	150,000	200,000	200,000
Share price at year end	£0.05	£0.03	£0.04	£0.07	£0.08	£0.10
Value of shares owned	£5,000	£3,000	£6,000	£10,500	£16,000	£20,000
Vested options - number	0	200,000	300,000	500,000	750,000	1,000,000
Gains on vested options		£2,000	£4,500	£20,000	£37,500	£60,000
Unvested options number	200,000	200,000	200,000	200,000	200,000	200,000
Gains to date on unvested options	£6,000	£2,000	£0	£4,000	£6,000	£10,000
Total of shares owned plus gains to date on options	£11,000	£7,000	£10,500	£34,500	£59,500	£90,000
Shares sold in the year-number	0	0	0	0	0	0
Shares sold in the year -value £	0	0	0	0	0	0

PILLAR 4 - Clarity and Transparency

4.1 Principles

The annual report should show clearly how much the CEO and other directors have been paid and how much they may be paid, potentially.

The explanation should be in plain English.

Complexity should be avoided. If remuneration cannot be simply explained, shareholders should view this negatively.

The full requirements of the Remuneration Disclosures required for main market companies are unnecessary for smaller companies. (Our view is that while those disclosures add additional data, they also add to the complexity of understanding the key remuneration issues)

The recommended minimum remuneration disclosures for companies wanting to build trust with their investors are provided in the Appendix.

Cross-referring to other year's remuneration reports and to circulars to shareholders may be "transparent" but is not helpful to shareholders. All relevant information necessary to explain remuneration to shareholders should be in one place in the remuneration report. It should not be necessary to follow a complex trail to find out what is really happening and companies that try to hide remuneration details in this way will be exposed and criticised.

PILLAR 5 - Good Governance and Business Practices

Principles

A remuneration committee should make remuneration decisions, with Independent Non-Executive Directors in the majority.

Companies should consult with key shareholders (to include a representative number of individual shareholders) about potentially contentious remuneration issues.

Where concerns are raised by shareholders about a company's remuneration arrangements, the company should engage with its key shareholders about the issues raised and explain how it intends to address the concerns.

Companies should table an advisory vote on their remuneration report at the AGM and invite shareholders to approve any new long-term incentive schemes (including their performance targets, unless clearly commercially sensitive).

Companies must be concerned about their culture, values and ethics. It matters how business results are achieved, as well as what is achieved.

APPENDIX - Remuneration Disclosures

Suggested minimum remuneration disclosure for AIM/ISDX companies wishing to build trust with their investors

Statement from the Rem Com Chair. Example:

The Remuneration Committee aims to set remuneration packages that motivate and reward executives to deliver long term sustained performance. We think our packages are reasonable. The graph and table below shows the historic relationship of pay of the CEO and performance in terms of share price [or TSR] and other KPIs and demonstrate a satisfactory linkage. The scenario chart shows the potential rewards which we feel are both reasonable and motivational for the executive team. The policy summary table shows the key elements of our remuneration approach. Shareholders are asked to approve our remuneration and I very much hope to receive your support via the vote[s] on Resolution[s] xxx at the AGM.

1. History of pay and performance

A chart should be displayed showing the share price performance over the last five years together with relevant comparator indices (e.g. Sector Index and Small Cap Index) so as to give a general impression of performance. Some companies may prefer to include a comparison against a specific group of companies or an index excluding specific companies (e.g. overseas miners) which are felt not to be relevant comparators. Some companies may prefer to use TSR (see Glossary) rather than share price as the basis of comparison.)

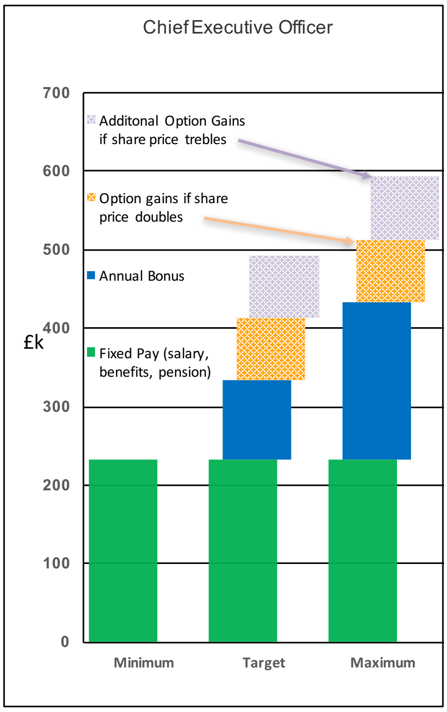
Historic data on turnover, profits, ROCE, debt and market cap should be displayed together with CEO remuneration data as in the following example.

Five Year Trading Record + Forecasts								
year ended 31-Dec		**2011**	**2012**	**2013**	**2014**	**2015**	**2016(E)**	**2017(E)**
Turnover	£m	43.12	50.31	57.20	59.88	61.93	54.50	58.62
Reported Pretax Profit	£m	-21.65	-3.62	2.23	3.09	5.37		
Norm. Pretax	£m	-14.54	-1.44	1.93	2.93	6.93	4.18	6.16
Dividend Per Share	p	1.25	1.25	1.25	1.25	1.25	1.60	1.70
Operating Margin	%	-33.03	-2.90	3.32	4.88	11.42		
ROCE	%	-46.99	-8.17	9.66	14.85	26.52		
Net Borrowings	£m		-10.15	-8.13	-3.70	-0.38		
Market Cap at B/S date	£m	34.3	23.64	28.76	51.26	50.27	= £31m @ 17 Mar16	
Remuneration Data for CEO								
Bonus payout as % maximum	**%**	**50%**	**25%**	**25%**	**80%**	**100%**		
LTIPs % vesting in the year	**%**	**50%**	**0%**	**0%**	**52%**	**90%**		
Salary	**£**	**200,000**	**200,000**	**200,000**	**200,000**	**200,000**	**200,000**	
Single Figure of Remuneration	**£**	**300,000**	**250000**	**250,000**	**350,000**	**550,000**		
Shares owned - number		2,000,000	2,000,000	2,000,000	2,000,000	2,000,000		
Shares owned value - at year end	£	368,450	253,941	308,940	550,635	540,000		

note: estimates (E) are average of broker estimates and are not company forecasts (except for salary which is the policy for 2016).

2. Illustration of Payouts from Remuneration Policy

2. Illustration of payouts from remuneration policy



	Illustrative scenarios		
Values in £k p.a.	**Minimum**	**Target**	**Maximum**
Salary	**200**	**200**	**200**
Fixed Pay (salary, benefits, pension)	233	233	233
Annual Bonus	0	100	200
Option gains, if **no change in share price**	0	0	0
Option gains if **share price doubles**	0	80	80
Option gains if **share price trebles**	0	160	160
Total if no share price change	**233**	**333**	**433**
Total if share price doubles	**233**	**413**	**513**
Total if share price trebles	**233**	**573**	**673**
Loss in value of shares owned if share price halves	-270	-270	-270
Gain in value of shares owned if no share price change	0	0	0
Gain in value of shares owned if share price doubles	540	540	540
Gain in value of shares owned if share price trebles	1,080	1,080	1,080

LTI/Option gains estimated using all awards and assumes gains are made over the next 5 years and annualised by dividing by 5.

Notes should explain the assumptions, for example:

Minimum assumes nil bonus and nil vesting of LTI performance conditions. Target assumes bonus at 50% of maximum and LTI vesting at median performance for market related performance conditions and target performance for financial/other performance conditions. Maximum assumes maximum bonus payout and maximum vesting of bonus matching and LTI performance conditions.

3. Remuneration Policy

A summary of the key elements of the remuneration policy table should also be included as best practice. The focus should be on the CEO, but, if there are likely to be contentious issues, details of all directors' remuneration should be clearly disclosed. An example of the recommended format is given on below.

Item	Policy
Salary	**£xxx,000 w/e dd/mm/yy.** **Set at median level of comparable sized companies.** **Reviewed annually. Any increases normally in line with those of the general workforce.**
Benefits	**Health insurance – family cover** **Pension (x% of salary) and Life insurance at, both at same level as other employees**
Bonus	**Target 25% salary. Maximum 50% salary.** **Targets and measures set each year to reflect KPIs.**
Share options	**CEO has options over 2% of the company awarded on ddmmyy, with an exercise price of £y.yyp** **(The above is a simple award structure. In other cases, the company should explain its policy and list all option awards, number of shares in award, dates of award and when exercisable, exercise price and any performance conditions that apply, see example below.)**
Share Ownership	**CEO owns xx shares, currently worth £yy. He/She is expected to build a stake over time of at least 3 x salary and not to sell shares, other than to pay taxes on exercised options, until this threshold level is achieved. Any share sales must be discussed and pre-agreed with the Chairman.**

Directors' Share Options

	Options @31.12.14	Awarded in year	Options exercised	Options lapsed	Options @31.12.15	Option Price	Date of grant
Name1	x				x	21p	1 Aug 08
Name1	x				x	26p	1 Aug 11
Name1	X				X	35p	1 Aug 14
Name1	X	X			X	45p	1 Aug 15
Name2	X				X	35p	1 Aug 14
Name2	X	X			X	45p	1 Aug 15

Add details of performance conditions that apply to the above. If none say so.

Add details of vesting, e.g. options are normally exercisable 50% 3 years after date of grant and 50% after 5 years.

4. *Remuneration Outcomes – Single Total figure of Remuneration*

	Salary		Benefits		Pension		Bonus		Long Term Incentives		Total	
	2015	2014	**2015**	2014	**2015**	2014	**2015**	2014	**2015**	2014	**2015**	2014
CEO name	**200**	200	**10**	10	**23**	23	**90**	100	**227**	17	**550**	350
Exec dir. 2 name	**135**	130	**10**	9	**14**	13	**90**	50	**52**	0	**300**	202
Chair name	**50**	50									**50**	50
NED1 name	**35**	35									**35**	35
NED2 name	**35**	35									**35**	35

For definition of terms see Schedule 8 of "The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013."

5. *Companies Act Required Disclosures for Directors' Remuneration*

- Aggregate remuneration paid to directors, excluding option/LTI gains and pensions.
- Remuneration of the highest paid director.
- Aggregate gains by directors on exercised share options.
- Aggregate gains made by Directors from other long term incentive schemes.
- Aggregate pension contributions.
- See Schedule 5 to "The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008" for full details of requirements.

Notes about suggested data

The graph, valuation metrics and 5 year trading record data are a standard set of data, such as provided by Morningstar, London Stock Exchange or Stockopedia.

Bonus payout as % max, LTIPs % vesting and Single Total Figure are as defined in the remuneration reporting regulations.

Illustration of payouts from policy is partly as defined in the remuneration reporting regulations, but enhanced to show the impact of share price changes. Share price changes and their impact are a very important part of reward for fast growth companies.

Value of shares held is also very important for smaller AIM companies, as many CEOs are founders and have large stakes in their companies.

Glossary

EMI: Enterprise Management Incentives. These are tax advantaged share options. For EMI details see:
http://www.mm-k.com/content/documents/2015emisummary.pdf

LTIPs: Long Term Incentive Plans. LTIPs are operated by the majority of FTSE 100 companies and are sometimes called performance share plans, or performance restricted stock plans.

SIP:Share Incentive Plan. Schemes that allow employees to acquire shares in various ways. For SIP details see:
http://www.mm-k.com/content/documents/201506SIP-summary.pdf

TSR: Total Shareholder Return. The percentage change in the share price plus dividends received by shareholders expressed as an annual return figure.

Value Creation Schemes. These give a share of the gain in the value of a company above a threshold to executives via a subsidiary company created for this purpose.

ShareSoc

UK Individual Shareholders Society

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These Director Remuneration Guidelines were prepared by a subcommittee of ShareSoc Directors, led by Cliff Weight, ably supported by Roger Lawson, Chris Spencer-Phillips, who instigated the project, and Mark Lauber.

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