CEO REMUNERATION
POSITION PAPER

NORGES BANK INVESTMENT MANAGEMENT POSITION

1. The board should ensure that remuneration is driven by long-term value creation and aligns CEO and shareholder interests. A substantial proportion of total annual remuneration should be provided as shares that are locked in for at least five and preferably ten years, regardless of resignation or retirement.

2. The board should develop pay practices that are simple and do not put undue strain on corporate governance. Allotted shares should not have performance conditions and the complex criteria that may or may not align with the company's aims.

3. The board should provide transparency on total remuneration to avoid unacceptable outcomes. CEO remuneration should be determined and settled in cash and locked-in shares each year. The board should also disclose a ceiling for total remuneration for the coming year.

4. The board should ensure that all benefits have a clear business rationale. Pensionable income should constitute a minor part of total remuneration. The board should commit to not offering any end-of-employment arrangements that effectively shorten or dilute the lock-in of shares.

ARGUMENTS FOR THE POSITION

Long-term shareholding better aligns CEO and shareholder interests
Requiring the CEO to invest a meaningful part of his or her remuneration in company shares is a simple and transparent way of aligning the interests of the CEO with those of shareholders and the wider society.

The accuracy of finely calibrated performance targets is illusory
The performance conditions of so-called long-term incentive plans are often ineffective and may result in unbalanced outcomes. Long-term incentive plans tend to have complex and opaque metrics that are open to discretion, and boards often adjust, supplement or rebalance metrics during the measurement period.

Transparent remuneration provides legitimacy
The board will provide transparency by settling remuneration up front without performance conditions and disclosing a total amount of cash and shares that is not subject to later adjustments. Transparency will also limit the prospect of unanticipated and outsized awards that challenge legitimacy.

Simplicity ensures that board and CEO can focus on business
Share allotment without performance conditions is less vulnerable to any information asymmetry between board and CEO. Performance conditions can encourage short-term behaviour. A simplified structure also ensures that CEO, board and shareholders can focus on the company's strategic aims.

ARGUMENTS AGAINST THE POSITION

Locked-in shares may drive up total pay levels
Settling a significant part of pay in shares locked in for several years will increase perceived remuneration risk, for which CEOs could demand compensation.

Remuneration must be tailored to the management challenge
Boards must be able to tailor remuneration plans to the challenges of the company and encourage the CEO to take appropriate risk. Boards should be able to reward strategic moves by the CEO, even if the market does not immediately appreciate their significance.

Restrictions on compensation will drive away leadership talent
There is a market for leadership talent, and every company should be free to offer the compensation structure necessary to attract the leadership it wants. Long-term incentive plans with performance conditions enable companies to set pay at levels that would otherwise be hard to defend.

Reliance on share price will reward factors outside management control
The business cycle or other external factors may drive the share price more than value creation by management. Well-calibrated performance conditions can better capture the achievements of management.

NORGES BANK INVESTMENT MANAGEMENT'S CONSIDERATION

As a global investor, our main concern is that CEO remuneration should be value-creating for the company. We believe that most leaders have an intrinsic motivation to succeed and contribute. Substantial long-term equity exposure reinforces this motivation and removes the distractions embedded in the design of long-term incentive plans.

We understand that share returns may not be a perfect gauge of the performance of a CEO, as non-controllable factors may drive share prices. However, we believe that the total return on shares in the long run reflects the value of the company for shareholders and society at large. Long-term shareholding exposes the CEO to both upside and downside risk from company performance.

Diversified investors should be able to compare companies' remuneration plans and vote appropriately. We believe that settling total remuneration each year and setting a ceiling for the next year will provide such transparency up front and prevent unanticipated outcomes.

The board is responsible for attracting the right CEO and establishing appropriate remuneration, but should be conscious of the cost of pay. Outcomes should be reasonable for the company and its shareholders. We believe that the pay transparency that comes with this structure will contribute to moderating pay levels in the longer term. Increased equity exposure and deferral is a cost to the CEO, but removing performance conditions will at the same time reduce uncertainty for the CEO.

We will invite peer investors to consider shared principles for effective remuneration, and we look forward to discussing with boards how this general position could be applied, taking into consideration the company's specific circumstances.