

 <p><b>INTERNATIONAL OIL POLLUTION COMPENSATION FUNDS</b></p>	<b>Agenda item: 6</b>	<b>IOPC/OCT09/6/2</b>	
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	1992 Fund Assembly	<b>92A14</b>	•
	1992 Fund Executive Committee	<b>92EC46</b>	
	Supplementary Fund Assembly	<b>SA5</b>	•
1971 Fund Administrative Council	<b>71AC24</b>	•	

## REMUNERATION PAYABLE TO THE JOINT AUDIT BODY AND THE JOINT INVESTMENT ADVISORY BODY MEMBERS

### Note by the Director

<b>Summary:</b>	<p>At its 13th session, the 1992 Fund Assembly decided to instruct the Director to analyse the roles and responsibilities of the members of the Joint Investment Advisory Body (IAB) and those of the Joint Audit Body and to present to its next session in October 2009 a document setting out a systematic approach to the honoraria/fees paid to the IAB members and all members of the Audit Body, including a comparison with market conditions and an exploration of the possibility of index-linking the fees, thereby making an automatic annual adjustment.</p> <p>In this document the Director sets out how he has acted upon that instruction and presents his findings and recommendations.</p>
<b>Action to be taken:</b>	<p><u>1992 Fund Assembly:</u></p> <ul style="list-style-type: none"> <li>a) to decide the level of honoraria/fees for the various roles as set out in paragraph 4.10;</li> <li>b) to decide whether the honoraria/fees should be indexed as proposed in paragraphs 4.11; and</li> <li>c) to decide whether the respective tasks and responsibilities of the various roles as set out above should be reviewed every five years, as proposed in paragraph 4.12.</li> </ul> <p><u>Supplementary Fund Assembly and 1971 Fund Administrative Council:</u></p> <p>To take note of the decisions taken by the 1992 Fund Assembly.</p>

### **1 Introduction and background**

- 1.1 At its 13th session, during the consideration of the draft 2009 Budget for the administrative expenses of the IOPC Funds' joint Secretariat and the assessment of contributions to the 1992 Fund General Fund, the 1992 Fund Assembly discussed the rationale for a proposed increase in the fees paid to the members of the joint Investment Advisory Body (IAB) and to the 'external expert' (formerly called the 'outsider') in the joint Audit Body. In particular, the apparent disparity between the fee paid to the 'external expert' in the Audit Body and the honorarium paid to the other members of the Audit Body was queried by some delegations.

1.2 Following a discussion, the 1992 Fund Assembly decided to instruct the Director to analyse the roles and responsibilities of the members of the IAB and those of the Audit Body and to present to its next session in October 2009 a document setting out a systematic approach to the fees paid to the IAB members and all members of the Audit Body, including a comparison with market conditions and an exploration of the possibility of index-linking the fees, thereby making an automatic annual adjustment.

1.3 At present, the annual honoraria/fees for the various positions are as follows:

Audit Body

- Members: £3 000 (since October 2005)
- Chairman: £3 000 (since October 2005)
- External expert: £30 000 (since October 2008)

Investment Advisory Body

- Members: £15 000 (since October 2008)

**2 Methodology chosen for the analysis requested by the 1992 Fund Assembly**

2.1 In order to make sure that the analysis would adequately take into account market conditions, the Director instructed Mr Gerald Russell FCA, Deputy President (and President-Elect) of the Institute of Chartered Accountants in England and Wales and a former senior partner in Ernst & Young, to interview a representative cross-section of the members of both the Audit Body and the IAB and any other persons he would see fit, with a view to providing a report to the Director containing an objective analysis of the roles of the members of both bodies, taking into account the differences in positions and linking them to normal market conditions. To that end Mr Russell was provided with all relevant Fund documents relating to the role of both bodies and given access to all information he thought he might need in the execution of his task. Mr Russell's curriculum vitae is set out at Annex I.

2.2 In the execution of his task, Mr Russell interviewed Mr David Jude, Mr Simon Whitney-Long and Mr Brian Turner (the three members of the IAB), Mr Wayne Stuart (the present Chairman of the Audit Body, who also has experience as an 'ordinary' Audit Body member from his previous term), Mr Nigel Macdonald (the 'external expert' in the Audit Body), Mr Charles Coppolani (the Chairman of the Audit Body during the first six years of its existence), and Mr Graham Miller (the representative of the IOPC Funds' External Auditor, the Comptroller and Auditor General of the United Kingdom). Mr Russell's report is set out at Annex II.

**3 Report by Mr Russell**

3.1 In his report, Mr Russell clearly distinguishes between the role of the Audit Body and that of the IAB in various respects. Whereas the Audit Body concentrates on issues of oversight and risk, the IAB provides expert financial advice to the Director regarding the secure management of the assets which the Funds are holding for the purpose of paying claims. This difference, together with his analysis of the various roles as set out in his report, leads him to a recommendation for the IAB which is further from the present situation than his recommendation for the Audit Body is. He is also mostly indicating a range rather than a fixed amount to reflect the fact that even in normal market conditions a single appropriate figure cannot be identified.

- 3.2 Mr Russell's conclusions are set out at the end of his report. For the various positions he recommends an annual honorarium/fee as follows:

Audit Body

- Members: £5 000-£7 500
- Chairman: £7 500-£10 000
- External expert: £30 000 (no change)

Investment Advisory Body

- Members: £22 500-£27 500

- 3.3 He also recommends that these amounts should be indexed annually. He suggests that using the Consumer Retail Prices Index or another general index of inflation for this purpose would be most practical.

#### **4 Director's analysis and recommendations**

- 4.1 Based on the report by Mr Russell, as well as other information collected and made available to him, the Director has come to the following conclusions.

*The role and nature of the IOPC Funds*

- 4.2 The IOPC Funds are intergovernmental organisations, which are independent but closely linked to the UN system, in particular the International Maritime Organization. They have a mission to fulfil in the public interest and as such they are in principle not subject to commercial principles and practices, nor should they necessarily adapt to them. On the other hand the IOPC Funds have a long-standing tradition of operating in a pragmatic, business-like manner, based on the idea that the Funds have to co-operate closely with the maritime and insurance industry in order to fully and properly fulfil their mandate. This mixed nature of the IOPC Funds puts them in some respects at the crossroads of the public and the private sector. This presents the Funds with a choice between two basic approaches in connection with the issue of remuneration of members of bodies set up by the Organisations.
- 4.3 The first approach would be to choose to pay only subsistence and travel costs, but no honorarium to members of such bodies. This would emphasise the nature and public responsibility of the IOPC Funds as intergovernmental organisations. Based on the information available, this is at present the case in a number of intergovernmental organisations, such as the World Meteorological Organisation, the International Criminal Court, the World Food Programme, the Commonwealth Secretariat and the Council of Europe. It should be noted, however, that a trend appears to be emerging also for intergovernmental organisations to move towards paying a reasonable fee for work of this nature.
- 4.4 The second approach would be to choose to pay a remuneration fully in line with market conditions for the important tasks carried out in the interest of the Organisations by bodies set up by them. This would emphasise the business-like way of operating of the IOPC Funds and would put the Funds effectively on par with normal business practice in this respect.
- 4.5 The present situation can therefore be characterised as an 'in-between' solution in this respect. An honorarium/fee is paid, but it is limited to a relatively modest amount which is not necessarily a reflection of the 'value' of the work put into it at that level in market conditions. The Director considers that this can be seen as an example of how the IOPC Funds have over the years positioned themselves in a pragmatic manner in their interaction with the maritime and insurance industry, whilst preserving their independence and specific character as intergovernmental organisations.

*The difference between the Audit Body and the Investment Advisory Body*

- 4.6 The Director has taken note of Mr Russell's finding that, in relative terms, the present fee for the members of the IAB is considerably below what would be reasonable under normal market conditions. He acknowledges that the nature of the work of the IAB is quite different from that of the work of the Audit Body in that it is more like the provision of a concrete service (expert financial and investment advice) to the Organisations, similar to what a host of companies/persons provide to the Organisations in order to enable them to fulfil their mandate. It is also worth noting that, in the present market conditions, the work of the IAB for the IOPC Funds is significantly more difficult and in particular time-consuming than under the market conditions that existed before the developments on the international financial markets toward the end of 2008. It would be sensible, however, to base the decisions in this matter on a rather more stable situation towards which the financial world will be moving again.

*Director's recommendations*

- 4.7 For the reasons given above, the Director takes the view that the present approach is broadly justified, as it takes into account the specific nature of the IOPC Funds as intergovernmental organisations with a mission which is clearly in the public domain and general interest, but which also involves close co-operation and constant interaction with the maritime and insurance industry. He also considers, however, that Mr Russell's report highlights some room for a possible improvement of the extent to which the differences between, and the relative weight of, the various roles are reflected in the respective honoraria/fees.
- 4.8 In respect of the Audit Body, the Director shares Mr Russell's opinion that the role of the Chairman of the Audit Body is generally more time-consuming and entails a greater responsibility than that of the other members (other than the 'external expert'). He considers, therefore, that it would be appropriate to reflect that by way of an increase in the honorarium for the Chairman compared to other members (other than the 'external expert'). The Director agrees with Mr Russell's recommendation that the recently-agreed fee of £30 000 pa payable to the 'external expert' of the Audit Body, Mr Nigel Macdonald, is reasonable. However, he considers that, since the role and input of the 'external expert' are in practice closely linked to the person of Mr Nigel Macdonald, who has held this position since the creation of the Audit Body and has put a great deal of effort and work into it, it would seem sensible to link this amount specifically to Mr Macdonald and explicitly leave room for another level of fee for any person succeeding him in future.
- 4.9 The Director also shares Mr Russell's opinion that, taking into account the nature of their work and market conditions, an upward correction of the fee of the members of the IAB would seem justified. He is not convinced, however, that the increase should be of the magnitude suggested by Mr Russell. It is important to note that the existing fee for the members of the IAB has so far not given rise to major problems in finding suitable and willing candidates. On the contrary, the present members have the highest qualifications and have fulfilled their role in an outstanding professional manner and the level of their fee has not, as far as the Director is aware, been a decisive element for a member in considering whether or not he/she would be willing to extend his/her mandate.
- 4.10 On the basis of the considerations set out above, the Director would consider the following package reasonable, both in terms of the absolute level of the honoraria/fees and in terms of the appropriate relative level for the various roles involved:

Audit Body

- Members: £4 000
- Chairman: £6 000
- External expert: £30 000

Investment Advisory Body

- Members: £20 000

- 4.11 The Director also proposes that all honoraria/fees will be indexed annually, using the UK Retail Price Index at the time of the preparation of the relevant budget.
- 4.12 The Director further proposes that the respective tasks and responsibilities of the various roles be reviewed every five years to make sure the rationale for setting the honoraria/fees still applies.

**5 Action to be taken**

1992 Fund Assembly:

The 1992 Fund Assembly is invited:

- a) to decide the level of honoraria/fees for the various roles as set out in paragraph 4.10;
- b) to decide whether the honoraria/fees should be indexed as proposed in paragraphs 4.11; and
- c) to decide whether the respective tasks and responsibilities of the various roles as set out above should be reviewed every five years, as proposed in paragraph 4.12.

Supplementary Fund Assembly and 1971 Fund Administrative Council:

The Supplementary Fund Assembly and 1971 Fund Administrative Council are invited to take note of the decisions taken by the 1992 Fund Assembly.

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## ANNEX I

### **GERALD RUSSELL CV**



**Gerald Russell (age 59) retired recently from Ernst & Young and is Deputy President – and President elect – of The Institute of Chartered Accountants in England and Wales. He is also a member of the Institute's Corporate Governance Committee.**

**His business experience demonstrates an unusual combination of skills. He has held senior management positions at Ernst & Young as well as being the Audit and Client Service Partner for major clients. This blend of commercial management experience with senior client handling skills, together with recent involvement in professional matters at the ICAEW and corporate governance matters for Ernst & Young, provides an excellent perspective on the role of the Non-Executive Director and particularly the Audit Committee member.**

#### **Recent roles**

- Senior partner – London with special responsibility for independent assessment of client service
- Chairman – Ernst & Young's Non Executive Director programme comprising workshops, seminars and thought leadership for that community
- London member of the UK firm's Governing Council
- Chairman – Audit & Assurance Faculty of the ICAEW which oversees the promulgation of professional guidance
- Chairman – The ICAEW's Audit Quality Forum which brings together investors, companies, regulators and auditors to support improvements in the quality of audit and reporting
- Vice Chairman of the Audit Committee Chair Forum, a joint venture between the CBI and Ernst & Young

#### **Other relevant experience**

- Managing partner of the Industrial & Commercial Office of Ernst & Young in London, at that time the firm's largest practice (1998 – 2004)
- Member of the firm's Strategy & Implementation Group (1996 – 2004)
- Client partner for Scottish & Newcastle plc and NEXT plc, both FTSE 100
- Other clients have included: Lloyd's of London, Bass Taverns (now Mitchells & Butler), Greene King, Xansa, Young's Brewery, Celltech (was FTSE 100), Black & Decker Europe, Blackwells
- Managing partner for Thames Valley/South Region (1988 – 1998)
- Executive partner for the firm's 'change' programme (1992 – 1995)
- National marketing partner (1985 – 1988)
- London Group leader (1983 – 1985)

#### **Other interests/roles**

- Trustee of Action for Children, the children's charity, and Chairman of its Finance Committee
- Council member of the Institute of Directors
- Governor of Notre Dame School for Girls, Cobham
- Visiting speaker on Audit Committees for Cranfield Business School's non executive programme

Gerald lives in Weybridge. He and Tessa have 5 children. He relaxes by sailing, driving his classic cars, playing some bad golf and undertaking extensive DIY.

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## ANNEX II

### Report to the International Oil Pollution Compensation Funds

#### Background

At its 13th session held in October 2008, the 1992 Fund Assembly of the IOPC Funds instructed the Director to analyse the roles and responsibilities of members of the Investment Advisory Body (IAB) and the Audit Body and to present proposals to the next session in October 2009 for a systematic approach to the fees payable to the members of those bodies.

At the request of the Director, Willem Oosterveen, I met with him and Ranjit Pillai, Head of Finance and Administration, who asked me to assist them with formulating such proposals. I was requested to apply my independent judgement and experience to analyse the roles being performed and skills required and to advise what would be reasonable remuneration for such services in normal market conditions.

I trust that my CV which is attached as Annex I to the covering document demonstrates that my experience is relevant to the task that I was invited to undertake.

#### Research

At the meeting, I received an oral briefing on the work of the IOPC Funds and was given papers with further background of the Funds and each of the above Bodies. Furthermore, I had very full and open conversations, subsequently, with:

##### *Audit Body*

- Charles Coppolani (Chairman 2002-2008)
- Wayne Stuart (Chairman 2008-2011)
- Nigel Macdonald ('External expert')

##### *Investment Advisory Body*

- David Jude
- Simon Whitney-Long
- Brian Turner

##### *External Auditor (United Kingdom National Audit Office which is led by the Comptroller and Auditor General)*

- Graham Miller

I would like to thank all these people for the very helpful information that they gave me.

In conducting my review work I applied experience drawn from advising large national and international businesses and organisations. I also obtained up to date information relating to current levels of payment to members of audit committees being made by the wider business community and I also reviewed fees payable to non-executives generally (ie independent directors who are members of boards to provide oversight). There is a significant range of fees payable for such services depending on the size and complexity of the respective organisations.

I also sought information in relation to other inter-governmental bodies but found it difficult to find anything to compare to the unique nature of the IOPC Funds. Furthermore, not all such organisations have remunerated Audit Bodies (or Audit Committees to use a parallel term). It may be that the role and benefits of Audit Committees have not been widely recognised in this sector, perhaps because there have not been the same regulatory pressures within it that have affected the international business community.

## Findings and Proposals

### *Audit Body*

The Audit Body is required to meet twice a year but more commonly meets three times. The Chairman of Audit Body, and others, attend the annual October sessions of the Funds' governing bodies. There are also meetings with the IAB and the External Auditor, which are normally held on the same day as meetings of the Audit Body.

However, this formal meeting time commitment does not fully measure the work undertaken by members of this Body. Leaving aside the specialist and technical role of Nigel Macdonald, the 'external expert', much of this work falls to the Chairman of the Audit Body but others also get involved in special projects from time to time. For example, the proposal to review the appointment of the External Auditor, whilst the normal business of an audit committee, can be a very time consuming task. From discussion, and the information I have gathered, it appears to me that the Audit Body operates in a fairly 'hands on' way and often gets involved with a high level of detail. For example, the work it has undertaken in reviewing control over the funding and payment of outstanding contributions from contributors, and an earlier review of the legal and other options available to the Organisation to stimulate the submission of oil reports, are examples of direct assistance to the Secretariat (and the wider membership) on business related issues. In the same way, previous detailed work in reviewing claims assessments, and the overall control procedures for this work which are of central importance to the Funds, provide further examples of the 'hands on' way in which the Audit Body works.

The current chairman has kept diaries of his time which amounts to between a half and a full day of elapsed time per week for most of the year. This excludes travelling time. It should be noted that members receive a travelling allowance based on the UN daily subsistence allowance which is not regarded as part of any honorarium or remuneration.

The Audit Body members are not full non-executives in the normal sense of the term. Therefore to benchmark payment to them against the level paid to non-executives in commercial organisations would not be helpful. It has, though, become common practice for many UK companies to pay non-executives who serve on a particular committee an additional fee for doing so. In fact the majority of listed companies now do this as well as paying a supplement to the chairman of each committee (source: Price Waterhouse Coopers).

It would be logical to use the level of such additional payments as a benchmark for the pure audit work undertaken for the IOPC Funds. My limited research indicates that a fee of between £5 000 and £7 500 is a reasonable range for such additional amount paid for such membership. For the avoidance of doubt, such additional remuneration comes on top of non executive director fees which are typically in the range of £30 000 to £75 000 and quite often more.

I recommend this range of between £5 000 and £7 500 be used as the basis for agreeing payments to members of the Audit Body going forward. Furthermore, Chairmen of audit committees most often receive a premium as their workload is higher and I therefore suggest that a range of £7 500 to £10 000 would be appropriate for that role.

At the request of the Director I have also considered payment to the member of the Audit Body, Nigel Macdonald, who has the 'external expert' role. Audit committees are generally required to have as a member at least one person with 'recent and relevant financial experience'. This is the current UK Corporate Governance Code requirement and there are similar rules in Europe, USA and other jurisdictions. This role brings not only relevant financial input and overview in terms of the Audit Body's reports but the expert is also called upon from time to time to undertake specific tasks and projects for that body. For example, the claims handling and risk control work done by the Audit Body drew largely on the expert's experience and on extensive detailed work carried out by him. This is a specific role for the Audit Body and does not carry with it other non-executive type duties.

From my discussions, I am informed that the typical time commitment varies from around twenty to over thirty days pa depending on the extent of such project work. In my view, the upcoming review of the arrangements for the external audit is likely to require involvement at the top end of this range. I therefore consider that the recently agreed annual fee of £30 000 for the next three years for the 'external expert' is reasonable.

#### *Investment Advisory Body (IAB)*

This is a very different type of body to the Audit Body. It is not so much concerned with independent oversight but – as its title indicates – its role is to advise the Director and his team on investment matters and developments. This is a crucial role from the point of view of the security of the significant amounts of money the Funds are normally holding.

The IAB has four regular meetings each year which are attended by members of the Funds' Secretariat. In addition, these are each preceded by a full-day meeting for discussion and preparation. In future this will be a half-day (morning). Other formal meetings comprise one with the External Auditor and at least one with the Audit Body, and attendance at the October sessions of the governing bodies. This represents approximately ten full days in all for such purposes. Additionally, I have learned that there are regular phone calls/e-mail exchanges and occasional *ad hoc* meetings between some members and the Secretariat. This degree of regular involvement is consistent with what I would expect from a group of individuals charged with providing regular advice in this highly important area of ongoing change and hence potential risk.

In current market conditions I am in no doubt that this work has been particularly important, both as regards counter-party risk and exchange rate volatility. General experience of financial business and markets is essential but additionally each member of the IAB brings specific skills directly relevant to the range of advice that it provides. Together, its members form a well-knit, experienced and balanced team to advise appropriately.

In addition to the ten appearances at formal meetings, therefore, much of its advisory work is undertaken behind the scenes. From my discussions with the members it seems that anything between an extra ten to fifteen man days is spent on such activity. Occasionally a special, more time consuming exercise will arise, eg the current review of hedging arrangements.

It is difficult to be precise on time spent from an IOPC Funds point of view as some of the members undertake similar work for other organisations and there is therefore some synergy across the whole. My view is that it would not be unreasonable to regard twenty man days as being reasonably representative of the workload for the IOPC Funds.

The current fee for such service is £15 000 pa, increased from £12 500 pa recently. Although direct responsibility clearly lies with the Director and his Secretariat, the expertise that the IAB provides is sought precisely because the Director and his own staff cannot be expected to replicate that range of skills and experience. Hence I consider that this work is more in the nature of the provision of specific executive advice rather than mere oversight, and I consider that the existing levels of remuneration are significantly lower than I would expect for this role.

As a relevant benchmark, consultancy fees for such advice are commonly £1 500 per day (indeed one committee member charges this to his other clients) and can often range to £2 000 per day. Taking the lower figure, this would lead to an annual fee of £30 000 based on my estimate of the actual work involved. Of itself, this equates to the level of non executive fees paid in some 'simpler' financial institutions, such as a smaller building society. However, given that the risk profile that goes with general non executive functions is not present with the IOPC Funds - as responsibility remains with the Director and his Secretariat, overseen periodically by the governing bodies - such an amount would seem high for the specific IAB role.

I consider that it is also relevant that I was asked to review payments in the light of 'normal market conditions' and it is apparent that the past year has not been one of those. On a normal basis, one would not expect so much continuous review of rates, security and volatility. Such matters could revert to being reviewed over a longer time frame, say six monthly or even annually, rather than every three months (and sometimes much more frequently) as now.

Considering all of the above, my view is that an appropriate level of remuneration for a member of the IAB would be in the range £22 500 to £27 500 pa. Certainly I consider that it would be difficult, but not impossible if the appointment was made through contacts, to fill the role and recruit from the market at a figure below £25 000. I realise that this is a significant increase on the current amount, but I do feel that it is a more realistic figure. Maybe, if it is decided to go for an increase of this nature, it might be done in two bites, eg £20 000 in the first year, and £25 000 in the second.

As indicated above, I understand that the IAB works as a close-knit team, and hence although I have learned that David Jude customarily takes the role of principal interlocutor for the findings of the group, I have not considered it necessary to recommend any additional remuneration for his position, whereas it will be seen that I have considered additional remuneration to be appropriate for the position of Chairman of the Audit Body.

For the avoidance of doubt, I believe the outsourced, individual consultancy arrangement created by the existence of the IAB is considerably more cost effective than if it were to be resourced fully in-house as part of the Secretariat.

### Conclusion

My recommendations are that:

- a) Members of the Audit Body should receive remuneration for their services in the range £5 000 to £7 500 per annum and that there should be consideration of paying the Chairman of that Body a further £2 500 in recognition of the extra duties.
- b) The 'external expert' on the Audit Body should continue to be remunerated at £30 000 per annum.
- c) Members of the Investment Advisory Body should receive remuneration for their services in the range £22 500 to £27 500 per annum
- d) Such amounts should be indexed annually so as to provide a formula and some certainty for both parties. A suitable pay index might be chosen but for ease the Consumer Retail Prices Index or another general index of inflation might prove easier.
- e) The work and respective responsibilities of both Bodies should be similarly reviewed at regular intervals, say every four or five years.



Gerald Russell FCA  
9 September 2009