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it's our business

newspad of the Employee Share Ownership Centre

Gordon Gekko alive and well in Europe

Gordon Gekko* ("greed is good") has arrived in Europe from the US, delegates were told during the European Centre's 19th annual conference in Cannes.

The failure of UK, European and US listed companies to align executive reward fully with performance and shareholder value came under sustained attack by speakers The widespread practice of giving large bonus rises to mediocre executives who had failed to meet their share incentive scheme targets came in for sharp criticism from **Doreen Lilienfeld** and **Paula Holland** of lawyers Shearman & Sterling and from **Leslie Moss** of Hewitt Associates.

The scale of executive reward in the US had been rightly condemned by *Fortune* magazine as 'highway robbery' said Mr Moss: "Transparency is a double-edged sword as anyone can now see the value of everyone else's executive reward package. So there is a further spiral upwards of reward levels, as people think it important for the prestige of the company to have its executives in the top reward bands. We are seeing an increasingly rapid turnover in ceos and as the churn rate gets faster, the reward level for their posts always goes higher. Executive stock option awards equivalent to four times salary were once unusual, but now they are normal."

Mr Moss added: "Gordon Gekko has arrived in Europe – we are getting used to the culture of super-rich executives in Europe." L'Oreal's ceo now enjoyed an annual reward package worth £18m and the Deutsche Bank ceo had faced shareholder protests over his recent 19 percent pay rise.

Doreen and Paula explained trends and best/worst practices in UK and US executive equity pay. In the UK, rewards were not sufficiently aligned with shareholder value. There was a perception that if the incentive scheme didn't pay out, the bonus would compensate for mediocre performance. Bad practice included: performance share plan annual awards worth more than 100 percent of salary; up to 30 percent vesting of incentive awards for median performance and deferred annual bonus awards creeping up towards two shares for every one held in executive share matching schemes.

In the US, they condemned the options back-dating scandal and the frequent re-pricing of options when performance stood still. Bad practices included *spring loading* – awarding equity incentives knowing that something good is about to happen to the company – and *bullet dodging* – granting options after publishing bad news which they knew would send the share price down. Excessive severance payments (*golden parachutes*) and boardroom cronyism were also condemned.

John Pymm of Watson Wyatt however begged to differ. Executive reward opportunity in the US had "performance dynamic" – pay levels were strongly linked to both financial performance and total shareholder return. "The media has got it wrong – performance pay does work " he said. Regulators like the ABI were issuing more amber and red top warnings to investors about remuneration committee proposals on executive pay, but despite this, shareholders had gone on to approve the recommendations. However, remuneration committees were under pressure to obtain more thoughtful analysis and creativity in executive long-term incentive programmes than ever before, John added.

Doreen and Paula said that all shareholders should exercise a vote over equity policy, which had to protect their rights and create value for all of them. Remuneration committees should be independent of management, have access to their own advisers and hold an objective approach to fixing executive pay. Corporates should not try to emulate private equity practices, as 'super profits' made by top performers were exposed to media and public scrutiny in the listed company sector which would damage

From the Chairman

It is difficult to divorce the politics of envy from righteous indignation. But there is something rotten about the remuneration of top people which it is difficult to pinpoint. Nobody opposes the rewards of luck - lottery and pools winners are fine, and many of the most successful acknowledge the role of luck in their affairs—nor reward for success. Perhaps what stick in the throat are the rewards for manipulation, working the reward systems and the tax breaks to achieve the opposite of what taxpayers and shareholders intended. The debate at Cannes, reported on this page, was excellent...let us hope John Pymm was right and the correction is taking hold.

Malcolm Hurlston

**Mr Gekko, played by Michael Douglas, was the fictional 'hero' of the seminal film Wall Street and became a symbol of 1980's greed. corporate*

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the company if they could not be clearly justified. In the US, company de-listing was still in progress, even though the Sarbanes Oxley legislation had been overhauled. US media interest in executive pay was enormous and there were many other pressure points, including the NYSE and NASDAQ listing rules, shareholder activists, mutual and pension funds and the tax code. In the UK, the Association of British Insurers' guidelines had shown that benchmarks for executive pay had to be used with caution as they tended to create an upward ratchet of remuneration levels with no linked improvement in performance. The ABI guidance was that no more than ten percent of the equity should end up in the hands of employees and not more than five percent in executive hands. This protected shareholders from dilution. All new share-based incentives should be prior approved by shareholders by means of a separate and binding resolution, as per the 2006 ABI guidelines.

More than 50 delegates from nine countries attended the conference and were blessed with glorious sunshine throughout. Newcomers commented on the high technical quality of the agenda topics and the pre-conference dinner, held at a quayside restaurant in old Cannes, was enjoyed by all. Two incidents marred the occasion: – the French immigration authorities inexplicably delayed issuing entry visas in good time to our first ever delegates from Dubai, prompting the two lady bankers concerned to vow they would never visit France in future. Worse still, one of our speakers Grant Barbour of Channel Islands based Bedell Group Trustees slipped on a wet towel in the hotel and ended up in Cannes hospital, having 16 stitches inserted into a nasty head gash. His colleague Paul Anderson supervised Grant's speechless departure from Nice Airport the following day. All at the Centre wish him a speedy recovery.

Conference chairman **Malcolm Hurlston** told delegates that the UK was booming because its government had proved itself more in favour of enterprise than the over-regulated US. The flight by companies from the NYSE had shown that in some cases the need for being 'double quoted' in both NY and London was dubious. Almost 20 years ago the industry had been challenged by the then Government to prove that Eso worked and we had tried to do so, said Mr Hurlston. When Gordon Brown first became Chancellor he had committed himself to advancing Eso in order to raise productivity in UK plc. Recent research papers, especially from the US, seemed to have proved Eso's beneficial long-term effect on the bottom line but now it looked as though the UK Treasury under Alastair Darling might again be asking us to prove that Eso's current £1.5bn annual tax advantages were giving good value for money. The issue was whether these tax reliefs were being applied correctly. The first sign of this was the probe into EMI launched by the HMRC wing of the Treasury (see previous issue)

Henk Potts of Barclays Wealth said that the pensions time-bomb facing western Europe was steadily worsening owing to several factors, most obviously ageing populations with a threatened shrinking tax base as the percentage of working populations faced future decline. In the UK this was exacerbated by the gradual disappearance of final salary pension schemes, coupled with the general failure of people to save. Financial education was the key but not enough was being done to educate populations. Huge private equity deals had been blamed for disenfranchising employees who were not always able to participate in the new equity arrangements. But the pace of such deals would slow as "low hanging fruit" would be harder to come by.

Maoiliosa O'Culachain of Global Shares UK presented the new service provider's first share scheme admin practices survey, carried out jointly with Buck Consultants. It showed that HR had provided the most common career path – 51 percent - among share scheme administrators. Almost 20 percent of those share scheme administrators surveyed had started their careers specifically as share scheme pros and almost one half of respondents had some kind of share scheme certificate or other pro qualification. Furthermore, almost 70 percent of administrators report to HR, the survey indicated. Overwhelmingly, respondents said that networking provided them with continuing education, but only 40 percent felt that internal training was of any use. Regarding types of plans being administered, stock options were still the most popular, although more than half the respondents still administer stock purchase plans such as ESPP, SAYE and SIP. Only 57 percent of the companies surveyed said they outsourced some or all of their share schemes and that tallied with research by Deloitte, which had shown that 60 percent of its surveyed companies outsourced scheme admin, said Mao. But new legislation and changes in financial reporting obligations combined with zero tolerance surrounding breaches of corporate governance were inciting a dramatic increase in the demand for professional expertise in the stock plan services market**.**

Mike Kemsley and **James Murray** of Cyril Sweett plc explained how their award-winning international construction consultancy had embraced all-employee share ownership to the extent that 86 percent of its employees own shares, or rights to shares, in the company. Cyril Sweett was now a public company and was seeking an AIM listing, but in no way would this involve a U-turn on Eso, Mike assured his audience. "We need to get access to more capital for corporate growth, but Eso will still be the cornerstone of our business." The company had launched a group Self-Invested Pension Plan in January and though it was still early days, two percent of its shares were held already via SIPPs. Cyril Sweett operated various share option schemes and a Share Incentive Plan, but it still required effort to get employees to buy shares in the company, added Mr Kemsley.

Jeffrey Mamorsky and **Joseph Saburn** of US lawyers Greenberg Traurig described the plethora of fiduciary responsibilities and rules facing sponsors of US employee equity and retirement plans. Severe penalties could be imposed on US companies by the IRS (Revenue) for unintentional footling errors in audit documentation, even when there was no adverse impact on plan participants, said Jeff. Huge amounts of staff time were being used up dealing with mob-handed IRS audit teams, which had been sent in to examine employee equity retirement plans. Whereas previously the focus of such IRS audit work had been compliance, it was now revenue driven, he added. The penalties for failing to satisfy IRS disclosure requirements – eg 'informed consent' by employee widows etc – were mind-boggling – up to $26m in some cases. Failure to comply with some of the dreaded Sarbanes-Oxley Act certification provisions could result in prison terms of up to 20 years for executives and senior managers of any company (whether US or European based), which was listed in the US. Executives could be imprisoned too for failing to monitor the "reasonableness" of employee equity plan administration fees. The new pay disclosure rules published by the Securities & Exchange Commission a year ago had certainly tightened up the rules surrounding fixing reward levels for senior executives, said Joe. Companies now had to provide a comprehensive overview of their objectives in setting compensation levels, including a breakdown of how each element fitted in.

Nicholas Greenacre of White & Case said that the damage inflicted on international employee equity programmes by the Prospectus Directive was less than had been expected. Some EU member states paid more attention to the PD than others. In France there was a "fairly low level of compliance," he said. Guidance issued by the Committee of European Securities Regulators on the impact of the PD on the issue of restricted shares, share options and stock purchase plans had been helpful. So far, 41 PD 'passports' to the EU had involved employee equity offerings by UK companies, but at least 30 had been filed by one law firm, said Nicholas. "However a lot of companies don't go to the regulators because they don't want to appear on their radar screens. One client gave up for this reason and didn't go ahead with his plan to issue new employee equity," he added.

Justin Cooper of Capita Share Plan Services presented his company's sixth survey of customer trends in the Share Incentive Plan. He said that there had been a drift away from the issue of free shares to participating employees, so the partnership and matching shares combination was the most popular SIP design. The practice of giving employees lump sum payments to facilitate the purchase of company shares was now very popular. Most companies purchased their SIP shares in the market to avoid shareholder dilution. Very few employees had withdrawn their shares voluntarily, even though companies had been reluctant to impose holding periods of more than three years for free and matching shares, said Justin. Companies new to Eso were now far more likely to look at SIP, rather than SAYE, the Capita survey revealed.

Stephen Walmsley, of Australia-based lawyers Freehills, talked about face-offs between board and shareholders in certain prominent Oz companies. At Bendigo Bank, major shareholders forced the board to include performance hurdles in its management reward plan. He characterised the Oz Eso regulatory regime as "strange" – participants had to elect to be taxed straight away in qualifying plans – and the recent Remuneration Report (Corporations Act) was "too complicated to work," he said. Average Oz employee plan participation rates in the first year were between 25-30 percent, but higher in the second and third years of new plans, said Stephen.

Recent lobbying work by the Eso Centre was described by Mr Hurlston: Pinsent Masons had prepared a paper for the Centre on how to improve the Enterprise Management Incentives scheme and Clifford Chance had prepared a paper for the Centre on how Eso plans might be incorporated more easily into companies which had been acquired by private equity groups. He said he had intervened, at the request of Foster & Partners employees, in the question of its employee benefit trust and the Jersey Financial Services Commission was now looking at the EBT transaction last January. The Society of Trust and Estate Practitioners had been vociferous on the subject of trust regulation and the Centre would be pleased to receive comments and papers on this issue, added Mr Hurlston.

Alan Judes of Strategic Remuneration and Charles Cooper of BWCI Trust Co described how they had helped Oz based Lend Lease Corporation to extend its Eso to its overseas employees, who were invited to buy amounts of company shares related to salary levels. A Guernsey trustee company was set up to help administer a restricted share plan in addition to an approved UK trust for a profit-sharing plan. Alan managed to win HMRC approval to continue the tax free status for existing awards which would be stapled to a unit in a unit trust, which is part of the Lend Lease empire. He explained how visits to the client's Oz sites suddenly unlocked the project roadblocks and how the UK SIP can be an ideal model for certain kinds of international employee equity plans.

Peter Mitchell of HBOS Employee Equity Solutions described the benefits of having trust services and share plan administration under one roof. The rash of international company takeovers and mergers had produced situations in which is was not uncommon to have three separate plan administrators, two savings providers and three trusts all now forced to work together in employee equity plan work. Peter said that share schemes did not sit well in HR departments, where they looked out on a limb. Perhaps they were better off under the wing of the company secretary or finance director. The integrity of the data regarding the plan participants was the key underpin. "This is where the mistakes occur, where the extra zeros get added," he said.

European Centre 2007 Award winners

UBS, the Swiss based worldwide banking group, won the European Centre's 2007 award for the *'Best International Eso Plan'* (major companies section). The plan's administrators were Corporate Employee Financial Services, which is part of the overall UBS group, and the legal advisers were Linklaters. The two runners-up, both highly commended, were plans submitted by BT plc and HSBC. Both were advised by HBOS Employee Equity Solutions, while BT was also advised by Allen & Overy. The SME company *Best International Eso Plan* award was won by Cyril Sweett plc, the international construction consultancy. Mike Kemsley, group finance director, received the certificate in Cannes from Centre chairman Malcolm Hurlston during the European Centre's 19th annual conference. Cyril Sweett's plan administrators were Capita, its financial advisers PwC and its legal advisers Pinsent Masons.

Listing Rule changes affecting share plans

The UKLA has announced changes to the Listing Rules, which came into effect on August 6. These are most likely to affect companies in three ways, writes ***Linklaters***. They may need to put more information on director share interests in their annual reports than previously thought; it will be easier to use treasury shares with share plans and the model code will apply to fewer people than before.

The listing rules still say that it is necessary to show in the **annual report** details of the share and option holdings of directors and connected persons during the year and any changes from the year-end to a date no more than one month before the AGM. Linklaters had been told by the UKLA that this requirement would fall away as a result of the repeal of the Companies Act requirement to keep a register of interests, but the new Listing Rules bring it back. The new rules appear to go much further than what was previously required as all changes in holdings during the year must also be reported. But Linklaters has been speaking to the UKLA who will change the rules again so that directors' interests only need to be noted at the end of the year. Also, it is unclear how the date of August 6 works with financial years.

Until now, it has not been possible to use treasury shares to satisfy options or awards under employee share schemes during a prohibited period. There are circumstances when vestings are not caught by the model code but it was still not possible to use treasury shares. The changes to the listing rules permit the use of treasury shares during a prohibited period for the purposes of a HMRC approved Share Incentive Plan or SAYE Plan or plans extended to all employees on terms similar to those of a SIP or SAYE. This aligns treasury more with the model code. It is still not possible to use treasury shares for other types of plans during close periods. From August 6, the model code will only apply to people discharging managerial responsibility (PDMRs) who, in most companies, are the board and senior managers who report to the board, said Linklaters' employee incentives team. Anybody who is not a PDMR will be able to deal in the company's shares without obtaining clearance. They will still be subject to the rules about market abuse and insider dealing and so companies may wish to instruct them to apply for clearance anyway. This does not change the requirement to put the names of all those who have access to insider information (not just PDMRs) on the company's insider list.

CONFERENCES

Centre – IoD October 9

Speakers at the 12th joint Centre – Institute of Directors annual share schemes conference for SMEs at One Whitehall Place, SW1, will be: Justin Cooper of Capita Registrars; David Craddock of David Craddock Consultancy Services, Juliet Halfhead of Deloitte, Alan Page of Killik Employee Share Services, Michael Sterchi of KPMG, Sara Cohen of Lewis Silkin, Aidan Langley of PWC, Robert Postlethwaite of Postlethwaite Solicitors and Colin Gibson plus Jim Taylor of HMRC share schemes valuation division. The conference regularly attracts 100 delegates, mainly from unlisted companies interested in setting up Esos. Admission costs £360 + VAT each for Centre and IoD members and £460 + VAT for non-members.

Centre – STEP Guernsey November 9

A speaker from the Guerney Financial Services Authority will join Charles Cooper of BWCI Trust Co, Amanda Flint of Chiltern Reward, William Franklin of Pinsent Masons, Alison MacKrill of Turcan Connell and David Craddock (see above) at the joint Society of Trusts & Estates Practitioners/Centre share schemes conference to be held at Old Government House Hotel in St Peter Port, Friday November 9. The focus will be on trustee issues, which have attracted mainstream media attention as the winding up of Foster and Partners' former EBT has come under scrutiny. Admission prices will be £295 +VAT for STEP or Centre members (discount for 2nd and subsequent delegates) and £425 + VAT for non-members. If you would like to speak at this event please contact jlewis@hurlstons.com with your preferred topic. Speakers from the mainland can reclaim their economy airfares and will be accommodated overnight in the OGH Hotel, if needs must.

Davos Jan 30 – Feb 1 2008

Scheduled speakers at the European Centre's ninth Global Employee Equity forum in Davos include: Grant Barbour of Bedell Trustees Group, Peter Mossop of Capita Fiduciary Group, Michael Sterchi of KPMG; David Pett of Pinsent Masons, Paul Stoddart of HBOS Employee Equity Solutions, Nadine Weber of Richemont and Mahesh Varia of Travers Smith. The Centre seeks more speakers and presentation subjects for this prestigious event, which takes place in the five-star Steigenberger Belvedere Hotel, Davos Platz, from Wednesday (Jan 30) to Friday (Feb 1). Speakers obtain a £200 attendance price discount. Please contact Fred Hackworth at fhackworth@hurlstons.com if you and/ or a colleague would like to speak at this event. Delegates' pre-paid (by the Centre) bed nights in the Belvedere will be Jan 30 and Jan 31. Member practitioner delegates will pay £775 for the all-in (except travel) package deal, while non-member practitioners will each pay £995. Exceptionally, Centre member plan issuer delegates will pay only £275 for their accommodation + conference package deal. Return tickets from London to Zurich can be booked for less than £100, including taxes and surcharges,

using Centre member BA's website www.ba.com
The discounted room rates are available to delegates who arrive earlier and/or depart later.

European Centre 20th anniversary conference
The European Centre intends to assemble a star-studded speaker and guest list for its 20th anniversary conference which will take place at the Majestic Hotel in Cannes, between **Wednesday June 4 and Friday June 6** next year.
Re all of the above: please visit the Centre website at www.hurlstons.com/esop for agendas, logistics and registration details.

COMPANIES
Bord Gáis's 900 employees are set for an average €36,000 stake in state-owned gas supplier under an Esop, which is close to completion. The plan will see staff take a 3.27 percent stake in Bord Gáis as part of an agreement with unions that will enable the company to achieve €32.7m of cost savings over five years, sources said. The 31-year-old commercial state body has been independently valued at €1bn, which is €400m below the company's net tangible fixed assets as of the end of 2006, according to its annual report. The 3.7pc stake allocation is the smallest Esop set up to date in the semi-state sector. In the Esots at the ACC Bank, ICC Bank, Eircom and Aer Lingus staff received five percent with an option of purchasing a further ten percent.

Eiffage chief executive Benoit Heitz said that the French construction group 'is not hostile to investors,' provided they respect two principles: the central role of employee share ownership, and the group's current business model. Speaking in an interview with French financial daily *Les Echos*, Heitz did not rule out the idea of an investor other than Sacyr Vallehermoso taking a capital stake in the group. But he stressed that "employee share ownership is and must remain the pivotal force within Eiffage." Some 90 percent of staff hold a combined capital stake of 22 percent, he explained, while the executive managers own five percent (via Eiffaime), a shareholder structure, which 'is an essential key to the operation of the group'. Eiffage must also retain its integrated construction-concession business model, which allowed it to win the Millau viaduct contract, Heitz said

Global Shares completed a second round of investment and raised £1.8m by way of an issue of preference shares convertible into ords on sale or flotation. The company was advised by KPMG corporate finance in Dublin, working closely with Ciara Reardon, Global Shares VP Finance and the funding provided by an investment group led by Richard Hayes, founder and former CEO of IFG Group, a second group assembled by KPMG corporate finance and by Enterprise Ireland. Richard Hayes joins Global Shares' board as a third non-executive director along with Ron Bolger (Chairman) and Roy Bukstein. The proceeds will enable the company to build on the success it has achieved since it commenced operations in October last year. The promoters Carine Schneider, CEO, based in California and Maoiliosa O'Culachain, COO, based in Ireland, aim to build Global Shares into a leading global player in stock plan administration and the company has already attracted 35 clients, including Yahoo! eBay, Philips, Unilever, GSK, Reed Elsevier and CEVA Logistics.

Italian banking group **Intesa Sanpaolo** concluded its purchase programme of its own shares and assigned them, free of charge, to employees on June 27, in line with shareholders' wishes. The Italian subsidiaries also concluded their purchase programme of the parent company's shares to finance the free assignment plan for employees. In all, the Intesa Sanpaolo Group purchased 23m of its ords for almost €131m- through Banca IMI, in order to fund the staff Eso programme.

On the move

From September 1, Raulin Amy and Dan Richards will become partners of **Ogier Group** and the Ogier legal partnership in Jersey. Raulin and Dan are part of Ogier's business and trust law group in Jersey and were each promoted to managing associate in 2006. Raulin joined Ogier as an English solicitor and qualified as an advocate of the Royal Court of Jersey in 2003. He advises on a wide range of local and international corporate transactions, restructurings and related banking matters as well as investment funds. Dan joined Ogier in 2005 from Mourant du Feu & Jeune. He qualified as an advocate of the Royal Court of Jersey in 2005. Dan's practice includes investment funds, as well as corporate and banking finance.

Nathan Powell has been promoted to managing associate in Ogier's Jersey legal practice. Nathan joined Ogier from Freshfields Bruckhaus Deringer. He specialises in corporate advisory work (including private equity structures, mergers and acquisitions and IPOs) and investment funds. Jane Pearce has been promoted to associate director in Ogier Fiduciary Services. She is part of the investment funds administration team and joined Ogier in 2006 from Kleinwort Benson in Jersey.

EMI: Both the *Financial Times* and the *Daily Telegraph* newspapers followed up last month's *newspad* exclusive story about the Government's new research probe into the Enterprise Management Incentives scheme in order to establish whether it gives taxpayers value for money. The *Telegraph* headline read: 'Treasury reviews tax break for small firms.' The *FT* headline was 'Revenue to probe value of scheme.'

EMI scheme is a rip-roaring success, though one which the Treasury has been curiously reluctant to crow about." The commissioned research is being collated by HMRC project manager Jane Taylor, KAI Tax Products and Policy Analysis Room 2C20, 100 Parliament Street London SW1A 2BQ Tel: 020 7147 2987.

Centre chairman Malcolm Hurlston told the *FT:* “The EMI scheme is a rip-roaring success, though one which the Treasury has been curiously reluctant to crow about." He noted that a 2003-04 study, commissioned by the then Revenue, found that some companies had switched from the Company Share Option Plan to EMI because the latter offered better tax advantages and easier admin. The Revenue's findings will be published on its website: www.hmrc.gov.uk The research is being collated by HMRC project manager Jane Taylor, KAI Tax Products and Policy Analysis Room 2C20, 100 Parliament Street London SW1A 2BQ Tel: 020 7147 2987.

Esop Institute diploma awards

Two students were awarded Diplomas in Employee Share Ownership Studies by the Esop Institute this term after successfully completing the four modules of the Esop Institute's distance learning (internet) course. They were:

Kirsty McNicol, client relationship supervisor, Corporate Employee & Executive Services, Royal Bank of Canada, who passed with merit and

Samantha Clark, HRRS, Global Employee Share Purchase Plan, Shell International Ltd

To learn more about this course, please visit the Institute website at: www.esopinstitute.com or send an email to: registrar@esopinstitute.com. You can download an application form from the website. Registrations for the autumn term should be lodged by the end of September.

Jobs Creation Act changes

The US Jobs Creation Act 2004, which added Section 409A to the US Internal Revenue Code, introduced a punitive tax regime for non-qualified deferred compensation, including certain employee share plans. The concept of deferred compensation is very broad and can generally include any right to any future payment of cash, shares or other property, writes ***Clifford Chance*** in the latest edition of *Employee Benefit News.* In general, deferred compensation caught by Section 409A is subject to early taxation (e.g. taxation is on vesting of a non-qualified share option instead of on exercise) and is also subject to an additional 20 percent tax penalty, as well as interest. Following the enactment of Section 409A, the Treasury Department and the Internal Revenue Service issued: Notice 2005-1, which set out initial and transitional guidance on the application of Section 409A, lengthy proposed regulations under Section 409A and additional notices providing interim and transitional guidance. On 10 April, final regulations were issued under Section 409A. These, although retaining many of the provisions of the interim regulations/guidance relating to employee plans, also contain some helpful changes. The overall position for various types of employee share plans is: The final regulations confirm that Section 409A does not apply to US tax-favoured incentive stock options and Section 423 employee stock purchase plan options. As previously, share options (other than US tax-favoured options referred to above) are not subject to Section 409A if certain conditions are met. Options over “service recipient stock” which have an exercise price that cannot be less than the fair market value of the shares at the date of grant are not generally subject to Section 409A (provided the share option has no other deferral features). Stock appreciation rights, whether share or cash-settled and including phantom options, are generally now treated in the same manner as share options and are referred to collectively as stock rights in this article. Options that are granted at less than market value (e.g. discounted Sharesave options and nil cost options under Long Term Incentive Plans (LTIPs) continue to be caught by Section 409A. Although the longstanding exclusion for certain market value stock rights provided welcome relief, it also raised a number of questions, e.g. which classes of shares would qualify as service recipient stock and how fair market value should be determined.

In summary, Section 409A should only apply to discounted e.g. Sharesave or LTIP options, but even then, only where the exercise period can extend beyond two and a half months after the end of the year of vesting. So, for UK companies operating employee share plans in the US, the impact of Section 409A on those plans now appears to be much less than was originally feared. The final regulations are applicable for taxable years beginning on or after 1 January 2008 (subject to various grand-fathering and transitional rules). Companies operating employee share plans in the US should review their plans now in light of the final regulations. It should also be noted that Section 409A has extra territorial effects and in principle applies to all US citizens and resident aliens (human), wherever they work, although certain limited exemptions may apply. Companies generally have until the end of this year to bring their non-qualified compensation into compliance in order to avoid the adverse tax consequence and penalties. The final regulations do not deal with all of the issues surrounding the application of Section 409A and it is expected that additional guidance will be provided by Treasury in due course. *This is an extract from a summary of certain complex provisions of the Final Regulations and should not be relied upon without first contacting **Clifford Chance**.*

Your newspad

Please email us your Eso news regularly, whether about a share scheme maturity, new clients, or personnel changes/reorganization. We will acknowledge the source, unless told otherwise. Send to fhackworth@hurlstons.com

The Employee Share Ownership Centre is a members' organisation which lobbies, informs and researches on behalf of employee share ownership. It is operated by staff of Malcolm Hurlston Corporate Consultancy Ltd.