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it's our business

newspad of the Employee Share Ownership Centre

Clawback in, golden parachutes out, in big remuneration shake-up

The sweeping US Congressional election Democrat gains, coupled with Barack Obama's emphatic presidential victory, heightened fears of a co-ordinated legislative and regulatory push against 'excessive' executive remuneration on both sides of the Atlantic in the New Year.

Universal clawback of executive bonuses, which later prove to be unjustified, is one probable repercussion of the Democrats' clean sweep of the US urns. Clawbacks are common in the US where a recent study found that 60 percent of top companies had such clauses in contracts. The US Treasury is demanding clawback clauses be inserted in the contracts of directors at banks participating in the Fed backed bail-out.

Senior European Commission officials are drafting executive remuneration guidelines, which are expected to include clawback proposals. Now the Association of British Insurers too is calling for bonus clawback clauses to be inserted into executives' contracts in a move to prevent reward for failure. The industry body, which represents insurers accounting for about a fifth of investments in the LSE, has held discussions with the European Commission about implementing the change. It is beginning to look as though companies throughout the western world will be compelled to insert clawback clauses into all senior executive contracts. In practice clawback of all or most of their bonuses would occur when directors signed off incorrect accounts, or backed overseas deals, which turned out to be loss-making. Companies might be allowed up to five years in which to recoup the bonus from the executive if the so-called 'performance' was later found to be misleading, or even fraudulent. Peter Montagnon, director of investment affairs at the ABI, told Reuters in an interview: "There is support in the market for this. It would be desirable to have something in contracts with such a clause in them as part of best practice."

The UK Government pledged to crack down on the bonus culture in banks. It unleashed its attack dogs at the Financial Service Authority, which launched an overhaul of the "unacceptable" bonus culture in the City. In a clear threat to banks and traders, the FSA promised "immediate action" if their bonus policies were not reformed. In a five-page letter to City bank bosses, the FSA ceo Hector Sants said there was "widespread concern" that excessive bonuses had "contributed to the present market crisis." Bonus-laden bank salesmen didn't ask questions about the poisoned debt bond parcels they so willingly sold on to other financial institutions worldwide.

City bonuses are expected to be well down on recent years, but around £3.5bn is still likely to be paid out at the year's end. FSA officials will carry out a programme of visits to banks to make sure 'bad practices' have been eliminated. The watchdog also plans to publish its findings about the City's bonus culture next year. Sant's letter outlined unacceptable bad practices that it wants to stamp out, including: *Linking bonuses to just one year's performance rather than average performance over a number of years *Calculating bonuses only on the basis of financial performance (The FSA wants the bonus to be linked to other skills such as risk management) *Bonuses paid wholly in cash. (The FSA wants a higher proportion of bonus to be made up of shares or share options). *Traders being able to assess the value of their own positions, giving them too much influence over the value of bonuses (The FSA says there should be more independent assessment) This overhaul applies to the tens of thousands of employees in the City who are rewarded with a year-end payments, totalling £50bn during the past decade.

The Treasury demanded that banks taking £37bn of British taxpayers' funds consider executive bonuses closely. Executives at RBS and HBOS are not receiving cash bonuses for 2007, while those at Lloyds TSB will take any payment they are entitled to in shares rather than cash.

In 1990, equity-based pay for chief executives of American companies was about five percent of their total

From the Chairman

With so many of the undeserving being bailed out it is shocking that the government has failed to take account of Sharesave victims. Employees who entered Sharesave schemes in good faith have every right to expect that their savings are protected in full and it is unspeakable meanness that puts at risk the savings of those who by chance save with the same bank as the scheme. Think again, Alastair Darling.

Malcolm Hurlston

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remuneration. By 1999, the proportion had risen to 60 percent.

The French government said it wants all listed companies to abide by guidelines on executive bonuses and golden parachutes set out by business lobby Medef by the end of this year. If this were not achieved, it would draft the guidelines into a new law. The guidelines include limiting so-called golden parachutes when a company is failing, or the departure of an executive is voluntary. They stipulate that an executive's performance should determine whether they receive share awards and that executives should acquire shares at market prices. The French government said it will propose an amendment preventing executives from receiving stock options if other employees don't benefit from a stock-option programme, share awards or bonus schemes.

CENTRE PROTESTS OVER ESO DISCRIMINATION

Esop Centre chairman Malcolm Hurlston has written to the Chancellor of the Exchequer decrying apparent state-backed discrimination against employee Sharesave participants who keep their plan savings in the same bank as their personal savings. The chairman asked Mr Darling to remove the anomaly whereby any amount deposited with a bank or building society via a SAYE scheme counts towards an individual's compensation limit with that bank or building society. He told the Chancellor: “As the leading employee ownership organisation in the UK, we are dismayed that the Financial Services Compensation Scheme will not cover employees whose Sharesave savings are with the same bank as their personal savings. It is unjust that there should be a difference between those employee owners whose savings happen to be with the same bank as their personal savings should be worse off. Sharesave is a key element in the structure of employee participation and I would urge you to remove this anomaly forthwith which will deter enterprise and send the wrong signals about the government's commitment.” Two million participants in SAYE-Sharesave share option plans are to have their savings protected by the FSCS, regardless of whether employee savings are held in individual or common savings accounts. This ends any lingering doubt about whether the level of employee participant protection varies if the savings plan is operated through a third party, such as an external plan administrator.

The FSCS statement said: "Money deposited via a SAYE scheme that is run in the standard way will be protected in the same circumstances as any other deposit will be. This is the case regardless of whether the scheme holds the deposit in individual accounts for each employee, or in one common scheme account, provided that the scheme holds full details of the individual depositors and the proportion of the money to which they are entitled. In particular, it should be noted that any amount deposited with a bank or building society via a SAYE scheme counts towards an individual's compensation limit with that bank or building society". This sting in the tail means that the amount of employee share plan savings will be offset against the minimum £50,000 of personal bank or building society savings guaranteed by the government if the accounts are in the same bank. Hence if an Eso participant has £10,000 invested in an approved plan, only £40,000 worth of other personal savings in the same bank will be guaranteed if that savings institution collapses.

AWARDS DINNER

The inaugural esop award winners’ black tie dinner at the Oriental Club in central London was an outstanding success as more than 70 members thronged the tables to hear about – and see- the leading entrants collect their certificates. Tables were booked by Equiniti, HBOS EES and Linklaters. Half tables were taken by Deloitte & Touche and by RBC Cees. Guest of honour Shadow Treasury minister David Gauke MP praised the ESOP Centre’s efforts to bolster SAYE-Sharesave schemes during the crisis (Access the Centre website at: www.hurlstons.com/esop news section to read his speech in full). The chairman said he was gratified by the large turn-out for the event, which would be repeated next year. He thanked Linklaters – in the person of Janet Cooper and her husband, David, (who is a member of the Oriental) – for arranging the excellent venue. Mr Hurlston said that the Treasury had informed him that the government had taken Centre concerns on board re SAYE-Sharesave. All the guests had their silhouettes prepared by Megumi Biddle, most rather lifelike.

Megan Cook of Capita collected the ‘Best International Eso Plan 2008 Award for Smaller Companies’ certificate on behalf of winners Telecity Group. Marsha Francis and Jan Henry of RSA (formerly Royal & Sun Alliance) collected the 2008 Award certificate for Larger Companies. Its plan advisers were Equiniti. The two runners-up, within half a point of the winners, were Diageo, represented by Lucy Blackie, Vikki Scott and Sue Mellors – and Pearson Group, represented by Gabbi Stopp and by Robert Head. Diageo’s plan advisers were Linklaters and Pearson’s advisers were Equiniti (John Daughtrey), Ernst & Young and Freshfields. The Esop Insitute’s student of the year was Kristopher Poulton of Deloittes; he received a mont blanc pen from Mike Kemsley of Cyril Sweett who is a member of the Institute’s academic committee.

SECTION 409A DEADLINE LOOMS

PWC is concerned that many companies are not aware that 409A of the US Internal Revenue Code is an issue for their share plans, reports Graham Rowlands-Hempel of PWC: "409A affects all forms of deferred pay for US taxpayers. Oddly, Sharesave is treated as deferred compensation for these purposes. In order not to incur penalties, companies should be amending their Sharesave plans by the end of the year. The changes will need HMRC approval. They should also be reviewing their LTIPs. In many cases a simple amendment to the plan will make the plan exempt," said Graham.

Section 409A was introduced as part of the US Jobs Creation Act to regulate certain deferred compensation plans. It is wide ranging and affects many plans, including: options granted at a discount to market value, as under HMRC approved Sharesave plans; restricted stock units, nil cost options, discounted stock appreciation rights and other phantom share plans; market value options granted with certain dividend equivalents; and many employment, severance and change of control agreements. LTIPs are caught within its net too. Section 409A restricts the use of offshore employee benefit trusts. For example, a Jersey trust should not be used to provide shares to US taxpayers under a share plan. Failure to act, could result in the imposition of severe tax penalties: an employee tax liability will arise immediately on vesting (again this is widely drawn and could include an option becoming exercisable); an additional 20 percent tax penalty will be payable with the risk of interest; and the employer could be subject to penalties for failure to withhold taxes or report the income at the right time. PWC advises clients to: amend all Sharesave plans that include US taxpayers. It has agreed the appropriate wording with HMRC; other plans should be reviewed to see if they are exempt from 409A or whether they should comply with the new rules; if necessary, amend plans or introduce a section 409A compliant sub-plan for US taxpayers and communicate any changes to employees. Changes should not require shareholders' approval.

ON THE MOVE

Anne Croft, counsel in the employee incentives division of Linklaters, plans to climb Mount Everest - "Well, not to the very top - that would be a ridiculous idea, for an unfit middle-aged woman with a sedentary lifestyle," she joked. "But I am going to climb as far as Everest Base Camp, which is 5,545 metres above sea level." She will endure 11 days of trekking up a lot of steep hills, for up to nine hours a day, followed by three days walking back down again. But the stunning mountain views should make up for the hardship and exhaustion. "For the last six months I have been trying to get fit enough to do this - which has involved buying a pair of walking boots, poles and a rucksack, and doing a lot of walking. I hope it will turn out to be enough." She is asking for donations for the charity Child Welfare Scheme (registered charity number 1106156). Its aim is to support disadvantaged and vulnerable children and young people in Nepal. The link to its website is http://www.cwsuk.org/ She is paying all the costs of the trip herself, so donations will not be paying for a holiday - it will all go to CWS. "Please do give what you can, either by visiting my JustGiving site or by going direct to the CWS site and downloading a form, or just sending them a cheque - to 32-36 Loman Street, Southwark, London SE1 0EH. Don't forget GiftAid - that will increase the value of your donation by adding the tax."

Linklaters has agreed to match the first £500 of donations. The link: http://www.justgiving.com/annecroft She has already raised almost £3000 in pledges, mostly online. Anne's co-ordinates are **+44 20 7456 3706** and **anne.croft@linklaters.com**

Catherine Ramsay joined the **Bird & Bird** UK employee incentives team on October 27. Catherine is newly qualified with extensive private equity and tax experience during her traineeship with SJ Berwin. "We need the extra fire power as I am delighted to say we are due to launch the incentives and cash sections of 'HR Knowledge Zone' on November 17," said partner Colin Kendon. "This is a website, free to clients and prospects, which will enable companies to cut the cost of dealing with cross-border HR issues relating to employee share plans, cash, employment and business immigration with an easy to use cross-jurisdiction comparative functionality."

NEW MEMBER

The Centre welcomes into membership Credit Suisse, which has long been associated with pioneering ideas and entrepreneurial thinking. It has a history of bringing new perspectives to meet clients' needs; the Esop team is no different. Based in Canary Wharf, the Corporate Trading Desk (CTD) is a specialised area within Credit Suisse that focuses on providing tailored brokerage solutions to listed companies and their employees - covering share dealing and option exercises. The CTD works either directly with the corporate client, their employee benefit trust or in many cases with their third party plan administrator. Popular CTD facilities include: multi currency dealing, reporting and settlement - cashless option exercise facility - immediate execution for participants (including first time sales)- ability to transact cross-border, supporting internationally based employees - warehouse & extended settlement facility where required CS and the CTD are-consistently ranked as a top tier broker on most global exchanges and in particular the FTSE100 and 250. - One of the best capitalised and secure banks globally. In today's market conditions, these credentials provide clients with the confidence that CS will remain a stable a bank to work with and furthermore that it has the ability to carry out their trading requirements with minimal market impact during large vestings. The CTD is proud to serve numerous clients including FTSE100 & 250, Small Cap and S&P 500 names, along with many of the leading share plan administrators and employee benefit trust companies. The CTD appreciates that every client's needs and circumstances are different. With its flexible approach to handling Esop activities, CS offers clients a solution that best suits them and their employees. For enquiries, please contact: Michael A W Smith, Head of the Corporate Trading Desk, Credit Suisse, One Cabot Square, Canary Wharf, London E14 4QJ **Michael.smith@credit-suisse.com +44 207 883 379**

CONFERENCES

Dubai: The revised programme for the Centre's Pathfinder conference in Dubai on November 17 & 18 has been finalised and delegate handbooks prepared. Any logistical enquiries – flights, hotel and/or timings- should be referred to Anna Burgess at the Centre: **+44 20 7436 9936** or **aburgess@hurlstons.com**

Davos February 5 & 6: Speakers lined up for the tenth Global Equity Forum at the Steigenberger Belevedere Hotel in Davos on Thursday February 5 and Friday February 6 include: Sarah Pickering (Alvarez & Marsal Taxand); Paul Stoddart (HBOS Employee Equity Solutions), Jean-Nicolas Caprasse (Riskmetrics Group); Kevin Lim (RBC Corporate Employee & Executive Services); Euan Fergusson (White & Case LLP); Alan Judes (Strategic Remuneration); Peter Mossop (Sanne Group); Sara Cohen (Lewis Silkin); John Pymm & Julie Withnall (Watson Wyatt); Dale Giedd and Ulrich Semmler (UBS); Rosemary Marr (Investec) & Grant Barbour (Bedell Group) and Caroline Labregere (Schneider Electric). There is room in the programme for three more speaker proposals from Centre members – especially plan case studies, or reports on technical issues. Davos speakers will pay only £695 (and no VAT) for the conference and two-day hotel package deal, instead of the normal Centre member practitioner fee of £875. Please email Fred Hackworth at: **fhackworth@hurlstons.com** to summarise your proposed presentation now.

Cannes 2009: The 21st annual conference of the European Centre in Cannes will take place on Thursday July 9 and Friday July 10 at the Majestic Hotel. The usual conference plus accommodation package deal Majestic Hotel bednights will be Wednesday July 8 and Thursday July 9.

COMPANIES

Employees of Cazenove Capital Management own more than 30 percent of the business. Andrew Ross, ceo of CCM, said: "Remuneration is key, but it is also about being an owner of the business." CCM is privately owned, having demerged from Cazenove Group in 2005, but there are still strong links between them.

The UK capital markets arm of collapsed Icelandic bank Kaupthing has risen from the ashes thanks to a management-led buy-out. Singer's employees will reap the benefits of the buy-out because the broker intends to pass part of the equity on to them. About 95 percent of employees already own stock, but Kaupthing's ownership stake had placed strict limits on how much the company could give them. "Hopefully this is an incentive to staff," said ceo Tim Cockcroft: "What we aim to do is return this firm to being a totally employee-owned business." The renamed Singer Capital Markets will be an independent corporate broker focusing on the UK small and mid-cap market. It has 70 employees and makes markets in 500 stocks and issues research in a dozen sectors. The management, led by Cockcroft, already owned one-third of the business. It bought the remaining 67 percent from the administrators of Kaupthing's UK banking business. Its name comes from Singer & Friedlander, the City merchant bank bought by Kaupthing.

Bosses at struggling furniture firm Land of Leather have agreed to take a pay cut to help steer the company through the economic crisis. The firm's four directors and some senior managers will not take part of their salary during the current slump. The move, which will save around £200,000, was revealed as the group reported an 88 percent slump in profits. The group, who have shed around 100 jobs, made £2.3m in the year to August 3, which was down from £18.5m the previous year.

CREDIT CRUNCH

Employee shareholders are counting the cost of the credit crunch in terms of the reduced value (temporarily, one hopes) of their holdings. Those who joined employee equity plans in the past two years are almost certainly facing paper losses, though this is not necessarily the case for those who joined five year plans in the early stages. The heavy stock market falls have allowed SAYE-Sharesave to come into its own – for participants lose nothing if the discounted options price they were originally awarded is still higher than the actual share price at maturity. In those plans maturing shortly, employees will get their savings back + interest, unless markets stage a huge recovery. By contrast, worries are focussed on participants in the Share Incentive Plan, especially those who have bought heavily into Partnership Shares. Assuming at least half bought their Partnership shares - around 2m employees could be sitting on paper losses. However SIP participants have to keep their shares in the scheme for five years to get full tax advantages - so they are unlikely to crystallise losses by selling up in the near future. However, even 'virtual' losses are mitigated by fact that most SIP schemes drip feed employee money month by month into share purchases, smoothing out the impact of big falls in share prices.

The Employee Share Ownership Centre Ltd is a members' organisation which lobbies, informs and researches on behalf of employee share ownership.