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it's our business

newspad of the Employee Share Ownership Centre

Government unveils massive Eso plan for postal workers

At least ten percent of the soon-to-be issued share capital in the Royal Mail will be offered for sale – probably at a discount - to more than 150,000 postal employees, the coalition government announced.

This will be the largest employee shares scheme of any privatisation for 25 years – second only to the privatisation of British Telecom in 1984. The percentage of equity being allocated to employees is also potentially the largest – larger than BT, British Gas or British Airways.

The new commitment – with further details - will be written in to the Postal Services Bill, which the Government plans to introduce in the autumn. This was revealed by the Business Secretary Vince Cable, at the Liberal Democrat annual conference in Liverpool.

The Communication Workers Union (CWU), which represents Royal Mail staff, is strongly opposed to privatisation.

The Centre welcomed Cable's announcement but believe employees should receive more than ten percent of shares. Malcolm Hurlston, Centre chairman, said: "Change is coming to Royal Mail. It is of huge importance that employees have a significant stake to ensure the ethos of the service is preserved.

"Previous employees share models in privatisations have followed the BT model too slavishly but this must be avoided with Royal Mail. However, other models have been deployed where the employees received more meaningful stakes. Under the de-municipalisation model used for bus companies, employees received as much as half of the business."

Mr Cable said: "I want to take action to secure the future of two cornerstones of British life – Royal Mail and the Post Office. The much-valued Post Office is not for sale and there will be no repeat of the previous closure programmes. Royal Mail is a different business, with different challenges. It is struggling under the weight of some huge pressures: pressure from email and falling mail volumes; pressure from a dire pension position; pressure from a lack of money to invest."

Mr Cable said that 'mutual ownership' would be promoted, spreading worker ownership alongside private capital. "The Liberal Democrats were the first and only party to call for an employee stake and we are now implementing it in government," he said. "The only way to save it for the future is to bring in new private capital to support the ongoing modernisation and growth opportunities. This will bring new commercial disciplines and the enormous public sector deficit means that the taxpayer does not have an endless supply of money to meet the company's investment needs.

"We also have to tackle the multi-billion pound pension deficit and put in place lighter touch regulation that gives the company a good chance in the market and protects the universal postal service that so many of us depend on.

From the Chairman

The Centre is putting the finishing touches to a policy document recommending government action to support employee share ownership.

The Centre's position was requested by consumer affairs minister, Edward Davey, at a meeting for co-ops, mutuals and employee ownership organisations held at the HQ of the Department for Business on September 16 .

The centrepiece of the Centre's suggestions will be a radical tidying of anomalous material in existing plan legislation which both deters entrepreneurs and involves HMRC in unnecessary cost. Otherwise a raft of proposals will aim at refreshing existing plans without serious implications for the public purse.

Together these proposals are designed to allow the government to relaunch employee share schemes and increase their potential to aid economic recovery.

The meeting with Ed Davey was also attended by Big Society minister Lord (Nat) Wei. However many decisions will lie not with Business but with Treasury. Even so strong support from Business may help Treasury to see merit in our plans.

One case in point is a revision of EMI to take better account of private equity. This may become a necessity for the government in the light of its plans to sell off Royal Mail.

Edward Davey is also postal minister: he has received a summary from the Centre of the role of employee ownership in past privatisations. Next week the Centre's RM thinktank will meet for a second time to hone more detailed suggestions in the light of the announcement that at least ten percent of RM is destined for employees

Malcolm Hurlston

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Just as important is the engagement and participation of staff in turning this company around. That is why our legislation will include a specific provision to make available at least ten percent of the shares in Royal Mail to employees, as part of the privatisation process. This is a once in a generation chance to transform the culture at Royal Mail – energising everyone and allowing employers and employees to share in the company's future success."

The government plans to look at the example of department store group John Lewis, which has an employee ownership structure. It has not yet decided whether employees will be given shares or offered the chance to buy them at a discount – or a combination of the two - as government sources said all options were open.

"We do not believe there is a need for Government to keep a stake in Royal Mail in the long term -- but we will retain some flexibility so that we can negotiate the best possible outcome," Cable said.

Some postal workers already own 'Colleagueshares' (a surrogate Eso scheme) which have to be cashed in at the end of four or five years and/or whenever an RM employee leaves, but they are not real shares and RM, not the markets, decides their value.

Mr Hurlston has met Postal Affairs and Employment relations minister Ed Davey MP to discuss the shape and nature of employee share ownership within a transformed Royal Mail. The last mega Eso privatisation was in 1984 when more than 100,000 employees were offered shares in BT at very favourable terms.

ABI writes to remcos

The Association of British Insurers wrote to FTSE 350 company remuneration committee chairmen, noting that the Financial Reporting Council's revised UK Corporate Governance Code and Stewardship Code represents: "A significant development to the process of engagement between companies and shareholders and is particularly relevant to executive share schemes and remuneration". It confirmed that the ABI's own executive remuneration guidelines and position paper, published last December, remains "appropriate and useful" and it will not be amended this year. However, rem com chairmen themselves should lead the discussions and the committee should ensure that there is an adequate explanation of the link between remuneration and strategy and that shareholders are given adequate time to consider the issues and to respond, added Hugh Savill, the ABI's acting director of investments affairs.

Social enterprise co-ownership

Centre member **Field Fisher Waterhouse LLP** advised on the transfer of front-line healthcare services provision from Hull Teaching Primary Care Trust (NHS Hull) to the City Health Care Partnership (CHCP), a community interest company. Hull will be amongst the first places in the UK to have services such as health visiting and district nursing delivered by a not-for-profit community interest company in which all employees are shareholders. In 2006, Hull was identified as a Pathfinder for social enterprise by the Department of Health and since then has been working towards the separation of its commissioning and healthcare provider roles. Around 1200 staff transferred to CHCP, which will reinvest any financial surpluses it makes into staff and service development. The restructuring project is significant given the new Government's emphasis on growing social enterprise and the co-ownership of public services. FFW advised CHCP on the novel employee-owned business structure, the constitution of the new business, the transfer of NHS Hull's provider services business, ten separate service contracts and on property law issues.

How Eso can stop takeovers

BA ceo Willie Walsh scattered the pigeons when he hinted that up to a dozen airlines are in his sights for possible future takeovers. "I think the industry is overly fragmented and would benefit from some consolidation. There are some restrictions in place still around ownership and control and there's political influence that makes it difficult, but I think ultimately we will see a reshaping of the industry," said Mr Walsh. However, his former employer Aer Lingus is not among his top targets: "You have got to look at the shareholding in the airline. With Ryanair a significant shareholder at 30 percent, the Government with 25 percent and the ESOT with 15 percent, I struggle to see how anyone would invest or would want to invest with that sort of structure," he said. Walsh has been awarded 469000 shares worth £1.13m under the airline's performance plan. The shares will vest after three years, but only if BA's total shareholder return is better than a group of other airline companies. This award is transferable to the enlarged International Airlines Group , if BA's proposed merger with Iberia goes through.

Postlethwaite's Eso guide

Solicitors Postlethwaite have published an easy to use share schemes fact card, which many in the industry will find useful on a day-to-day basis. It gives comparisons of all the main employee share schemes (including non-approved schemes), together with a star rating for each - according to their tax efficiency, their ease of setting up, plus their overall incentive and reward value. Using these criteria, Postlethwaite has the Share Incentive Plan (SIP) consistently outscoring SAYE-Sharesave. One side of the card compares schemes for key people, while the other focuses on all-employee schemes. To obtain the fact card, contact Robert Postlethwaite (**rmp@postlethwaiteco.com**) Tel 020 7470 8805 or David Reuben (**dgr@postlethwaiteco.com**)

The top Eso lawyers 2010 named

Linklaters and Clifford Chance are both highly recommended among law firms specialising in employee share schemes, according to *The Legal 500.*

The annual guide to the UK legal profession is now in its 23rd year. Linklaters' blue-chip clients include Aviva, BAE Systems, Centrica, Diageo, National Grid, Serco and Vodafone, while standalone share scheme clients include Citi, Morgan Stanley and UBS. Clifford Chance was found to provide 'excellent support' and 'easy-to-understand advice on complex issues'. Its stand-alone work has included advising Barclays on the design and implementation of a new all-employee global share purchase plan. Clients rate the share schemes team at Allen and Overy as 'excellent'. The firm acts for Interwoven and Thomson Reuters. Meanwhile, Freshfields Bruckhaus Deringer is said to have a 'really commercial' employee share schemes practice and is noted for its 'practical advice and commercial approach' In addition. Other leading law firms mentioned in the employee share scheme arena include: Hogan Lovells International, Slaughter and May, Ashurst, CMS Cameron McKenna and Norton Rose.

Eso pays off

Employee owned companies outperformed the FTSE All-Share in the first six months of this year, according to the UK Employee Ownership Index (EOI) published by law firm and Centre member **Field Fisher Waterhouse**. Employee owned companies' share prices were down 4.5 percent, performing better than the FTSE All Share companies' share prices, which went down by almost eight percent over the same six-month period. Analysis of Q2 showed employee owned companies' share prices were down 7.5 percent, still performing better than the FTSE All Share index, which was down 12.6 percent over the quarter. The EOI, compiled by the firm's Equity Incentives team, monitors the share price performance of listed companies, comparing the performance of FTSE All-Share companies with 'employee-owned companies' i.e. *companies that are more than ten percent owned by employees*. The EOI started in 1992 and shows that over 18 years, employee owned companies have outperformed FTSE All-Share companies each year by on average 11 percent. Over successive three-year periods they have outperformed by 38 percent and over successive five-year periods by 74 percent. An investment of £100 in the EOI in 1992 would at the end of June 2010 have been worth £647 whilst the same investment in the FTSE All-Share Index would be worth £212. Graeme Nuttall, head of equity incentives at Field Fisher Waterhouse said: "The EOI demonstrates that this trend is also seen over the long term - employee owned companies generally do better over time than FTSE All-Share companies."

Accounting charges

The Interpretations Committee (IFRIC) of the IASB (International Accounting Standards Board) debated at its September meeting whether the accounting charge for a share option should be split into equity settled and cash settled parts. The suggestion was that, on exercise of an option, if a company withholds some of the shares to fund the tax arising on exercise, a financial liability was being discharged and a proportion of the award relating to this liability might need to be accounted for as a cash settled share based payment. In the UK, the amount of tax payable on exercise varies with the size of the gain. The practical complexities of applying such an approach would be horrendous, said William Franklin of Centre members Pett, Franklin & Co. LLP. Fortunately, the consensus is that if the company was only acting as an agent (which would be the usual situation in the UK) in settling the employee's tax liability, then the entire award should be accounted for as an equity-settled share based payment. Other matters considered by the committee, including redrafting the definitions of the various conditions determining whether an award can vest and their associated accounting treatment, may have a more significant impact on UK share schemes. In particular, the reclassification of some performance targets as non-vesting conditions may lead to some targets unexpectedly losing the right to 'true up.' There was some nervousness amongst committee members about making the changes, as the proposals were referred back to the IASB itself for a final decision.

On the Move

Global Shares plc, a leading provider of global share plan administration and consulting services, announced the appointment of Dario Sanchez as new Asian client relations manager. Dario will work with partners, clients and prospects in Asia. He will be based in the Global Shares Shanghai office and will be the new editor of *GlobalTimes,* the quarterly Global Shares newsletter. Dario has a degree in both Economics and Chinese. He has a very strong interest in East Asian culture and affairs, and is able to communicate in Japanese and Korean, as well as Spanish. "Asia continues to be an important focus for Global Shares," said Carine Schneider, ceo of Global Shares. "Our clients throughout China and Asia appreciate our local support. I'm pleased to have someone with the language and customer service skills Dario possesses work directly with our clients, partners and prospects. We expect continued growth in the region." Dario can be contacted at dsanchez@globalshares.com or by calling the Shanghai office at +86 21 6279 7208.

Internet house-hunting agency Rightmove plc has joined **Killik Employee Services'** expanding portfolio of clients. KES will be licensing its share plan administration software, Centive, to the company, making it possible for Rightmove to manage its executive share plans in-house.

Law graduate Lisa O'Connell joined leading independent remuneration consultancy **MM & K** in August as senior client manager in share plan administration. She has 15 years experience of employee share plans and their administration. After intially working in-house as company secretary, Lisa worked exclusively within the share plan administration arena, first at myShares, part of the Capita Group and then at Transcentive Inc and Computershare. Most recently she was md at Halliwell Integra, the share plan management arm of Halliwell Consulting which was acquired by PwC. Lisa has extensive knowledge of the practical, legal and regulatory aspects of share plan management and administration both in the UK and overseas, as well as the software requirements.

RBC Wealth Management, part of Royal Bank of Canada, announced that Michael Lagopoulos has been appointed deputy chairman, RBC Wealth Management, Ultra High Net Worth (UHNW) - International. He will focus on developing RBC Wealth Management's UHNW business by deepening existing relationships and acquiring new UHNW clients outside Canada.

Warning for UK 'non-resident' employees

Employers who automatically treat employees seconded to work abroad for at least a complete tax year as UK non-resident could be making an expensive mistake, Centre member **Deloitte** warned in a client bulletin. "It is often overlooked that, as well as spending less than 91 days on average in the UK over the assignment period, the employee must also be employed full-time abroad," Deloitte said. If that condition is not met, the employee may not break residence unless he goes abroad permanently or indefinitely. HMRC's guidance says that an individual working regular hours is employed full-time abroad if they work a full working week of 35-40 hours abroad. Nothing is said about the common situation where a small part of the employee's job remains in the UK and he or she has to make regular return visits to the UK, but is still averaging at least 35 hours a week abroad. Further, in many regulated industries, residual UK duties are commonly required by the regulator – in the financial services sector, for example, Financial Services Authority approval may be dependent on continuing UK duties. Tax legislation prescribes that employees may not break UK residence on account of working abroad if they continue to perform employment duties in the UK which are more than 'merely incidental'. If HMRC applies the law strictly, an employee who returns to the UK for a key sales or strategy meeting would be treated as remaining UK resident for the whole tax year and perhaps for the whole assignment period, because the business visit was 'non-incidental.' Recently, HMRC has been taking a strict line on non-incidental duties with employees who they consider are going abroad primarily to avoid UK tax. The fear is that this attack may broaden into a wider campaign against UK employees abroad who have continuing duties in the UK. The risk is twofold: additional cost and compliance failure, added Deloitte. Employers who tax equalise assignees abroad may be liable to pay substantial additional tax and NI if their employees are found to be UK resident – even with a foreign tax credit for the non-UK tax, given the current 50 percent top UK tax rate, there will very likely be a residual UK liability. Where employees pay their own tax, employers may be held accountable for PAYE and late payment penalties where they should reasonably have known that assignees had actually remained UK resident.

With zero fanfare, Britain has gained a multinational. The accountancy firm Deloitte Touche Tomatshu has quietly shifted its legal registration from Switzerland to London. The firm, which has 169,000 staff around the world and is vying with PricewaterhouseCoopers for the title of the world's biggest professional services group, is thought to have moved because of legal controversy surrounding its previous status as an obscure Swiss entity known as a *verein*_– a membership structure originally intended for sports clubs, voluntary organisations and unions. The change – which was not announced publicly by Deloitte – has little tax implication for the Treasury because Deloitte's decentralised structure means taxes are paid by its member firms on a country-by-country basis. But it amounts to a vote of confidence in English corporate law over Switzerland's regime.

COMPANIES

Aberdeen based transport giant, **FirstGroup**, won the award for the 'most effective all-employee share scheme strategy,' at the Employee Benefits annual awards ceremony. The judges recognised the work First did to better engage with its younger employees. A subtle change of approach in communications addressed low participation rates of First's employee share option schemes in the under 30 age group, with outstanding results. The judges praised First's 'easy to use and stylish' online interactive system. One judge said: "This is a scheme to be proud of." Lisa Proctor, FirstGroup's Reward Manager, said: "Encouraging our younger employees, particularly those under 30 to take advantage of our industry leading employee share packages has been one of our leading objectives in the last 12 months. I am delighted that with the help of our partners, Yorkshire Building Society (YBS), more than 20 percent of our staff participate in our share schemes – a very high figure in the transport industry." Jill Evans, Head of YBS Share Plans said: "We are delighted that one of our clients has once again achieved success at these annual awards. We are committed to the share plan market and we encourage our clients to shout about the innovative ideas and communication strategies that have been developed. It is extremely rewarding when all the hard work that goes into helping make our companies' plans stand out from the crowd is recognised by the industry."

Victoria Oil & Gas completed a share placing of 368,000,000 new ords at 2.5p per share, raising £9.2m before expenses and conditional on admission. This will enable the company to complete all necessary gas plant facilities and the pipeline to deliver first gas production. In addition to the placing, almost two million shares have been allotted to directors and employees in lieu of cash salary for the six-month period ended 31 July 2010 in accordance with their standard employment contracts at a weighted average month-end market price of 3.5p per share. More than 10m new ords have been allotted to advisers in lieu of cash payments and 48m ords to the trustee of the company's Esop.

CONFERENCES & EVENTS

Esop 2010 Awards Dinner: Oct 5

Lord Newby, LibDem spokesman for HM Treasury will be presenting awards at the 2010 dinner. More than 60 people have already booked their places for the black tie occasion to be held on Tuesday October 5, *but there is still time, just, for other members to book.* The event takes place at the Oriental Club, Stratford Place, London W1C 1ES (*nearest tube is Bond Street*), starting with drinks at 6:30pm followed by dinner in the main drawing room. The cost per table of ten is £1,300 & VAT. Individual places cost £140 & VAT. Contact Dave Poole at the Centre in order to book your places: Tel + 44 20 7239 4906 or email: **dpoole@hurlstons.com**

Guernsey: November 19

More than 20 delegates have already booked to attend the Centre's next joint *Share schemes for Trustees* conference with STEP (Society of Trust & Estate Practitioners) Worldwide on Friday November 19. This half-day event, centred on latest employee equity developments affecting trustees, will be held at the Saint Pierre Park Hotel, Guernsey. The speakers include: **Malcolm Hurlston**, Esop Centre Chairman, **Alison MacKrill,** STEP Guernsey/Carey Olsen, giving a Channel Islands & trusts update; **Justin Oliver**, Collins Stewart Wealth Management, on investment trends for trustees; **William Franklin**, Pett Franklin & Co. LLP, speaking on JSOPs,which he co-invented, and flowering shares; **David Craddock**, David Craddock Consultancy Services, who received excellent reviews from his speech in Jersey earlier this year, will address the use of LTIPs with case studies and **Helen Hatton** former Deputy Director General of the Jersey Financial Services Commission (JFSC), now of Sator on whether the standard financial services concept of risks fits Esops Admission costs £295 for Centre members and STEP Practitioners or £425 for non-members. Would-be delegates should register soon as seating capacity is limited. All this will be followed by luncheon. The attendance fee is £295 for Centre and STEP members and £425 non-members. The half-day course will earn all attendees 3.5 hours CPD credits. Contact dpoole@hurlstons.com as soon as possible to reserve your place.

Davos: Feb 3 & 4

The World Centre's 12th annual Global Employee Equity Forum, which takes place in the Steigenberger Belvedere Hotel, Davos Platz, Switzerland, on **Thursday February 3 and Friday February 4,** has already attracted eleven speakers. They are: **Louise Jenkins** of Ernst & Young; **Alan Judes** of Strategic Remuneration; **Mike Landon** of MM & K; **Kevin Lim** of RBC CEES; **Martin Osborne-Shaw** of Killik Employee Services; **Adrian O'Shannessy** of Greenwoods & Freehills Ltd (Australia); **David Pett** of Pett, Franklin & Co. LLP; **John Pymm** of Towers Watson; **Michael Sterchi** of KPMG AG (Zurich); **Julie Withnall** of Britvic plc and Centre chairman **Malcolm Hurlston** have booked their slots, but more agenda ideas are needed. Other would-be speakers should contact organiser Fred Hackworth (fhackworth@hurlstons.com) asap with their topic suggestions. Please see the latest speaker interest and logistical info about Davos 2011 in the 'events' section of the Centre website: www.hurlstons.com/esop. The speaker price for the two hotel nights (on a half-board basis) + conference package seal is an unbeatable **£725** and no VAT charged. This compares with a minimum £899 fee for non-speaking Centre member practitioner (service provider) delegates and £1250 for non-member practitioners. Speakers from plan issuer companies (either appearing under their own steam or as guests of Centre practitioner members) will pay only £415 for the package deal. Contact Fred Hackworth at: fhackworth@hurlstons.com for delegate places, or register online at: www.hurlstons.com/esop and click onto 'events.' Davos 2011 qualifies for 11 hours of CPD credits.

Bank bonuses tax bonanza

Banks paid 40 percent more than predicted in a one-off bonus tax to the British government, suggesting the levy on payrolls failed to limit executive pay. Lenders paid £3.5bn pounds by Aug. 31, according to government figures. Chancellor of the Exchequer George Osborne said in June he expected to raise £2.5 bn from the tax. His predecessor Alistair Darling introduced the one-time 50 percent levy on discretionary bonus payments exceeding £25,000 pounds almost a year ago when the Labour Party was in power. The then government originally forecast the levy, which covered bonuses awarded between December 2009 and April 2010, would raise £550m.

UK Corporates have axed guaranteed bonuses

Only five percent of top UK corporates continued to pay out guaranteed bonuses to senior executives last year, Centre member **Pinsent Masons** revealed in its latest client bulletin. Its survey of corporate bonus strategy showed that the percentage of companies paying guaranteed bonuses to executives, regardless of personal performance and/or the company's profitability, had halved from ten percent in 2008 to five percent in 2009. An analysis of pay and remuneration for *The Daily Telegraph* found FTSE 100 ceos were paid a basic salary of £751,459 on average in 2009-10, an increase of five percent on the previous 12 months. In 2008-09, pay was frozen, and in 2007-08, salaries were cut by one percent on average to £718,199, the analysis showed. The research by RTF Navigator shows bonus payments also rose by 12 percent in 2009-10 compared to the previous year. In 2008-09, bonuses fell by 24 percent. In a sign that companies are increasingly using share options to encourage long-term performance, share incentives grew significantly by 61 percent year-on-year, compared to a 43 percent rise in 2008-09, the analysis found.

The Pay Report includes an analysis of businesses that reported in April, as well as for the whole of last year. Of the FTSE 100 companies that reported for the year-end to March 2010, Michael Spencer, ceo of ICAP, was the highest paid, with total remuneration of £24.3m. The bulk of the package came from Spencer cashing in share options, ahead of the introduction of the 50 percent tax rate on annual earnings of more than £150,000 from April this year. Graham Mackay, head of brewer SAB Miller, was the second highest-paid ceo when taking looking at those companies that reported in April, with total reward of £17m, ahead of Sir Terry Leahy, the outgoing ceo of Tesco, with £15.6m. Angela Ahrendts, ceo of luxury fashion chain Burberry, was the highest paid woman joining the list of top 20 earners in the year-end to March, with £6.1m total pay. However, Bart Becht, the head of Cillit Bang owner Reckitt Benckiser, retained his position as the highest-paid ceo in the FTSE 100 with a total pay package of ***£92.6m*** in 2009, Mr Becht outstripped the remuneration paid to any other of the FTSE 350's top earners by £56.2m. The huge payout came after Mr Becht cashed in share incentives accumulated over the previous decade. FTSE 250 executive director Tony Pidgley, of Berkeley Group Holdings, was the second highest paid, with £36.4m, ahead of Mick Davis, chief executive of miner Xstrata, with £25.5m. Making up the top five, Mr Spencer came fourth, ahead of Frank Chapman, head of gas company BG Group, with £23.1m.

Pay experts said the research reflected the wider trend that ceo pay had recovered from the gloom of the recession, with companies reluctant to freeze or cut the pay of senior management for more than two consecutive years. Tom Gosling, remuneration partner at PricewaterhouseCoopers, said: "There is generally an unwillingness of companies to freeze pay more than two years in a row. During the recession there was a desire to set the tone for cost control and senior management had to undergo pay freezes. Now pay increases have started again." However, Mr Gosling said the pay figures might not reflect a turning point for chief executive pay. "The 2009-10 pay increase doesn't reflect the performance in individual companies. I would expect to see modest increases in the coming years, of between two and four percent," he said.

A director, who helps set the pay and bonus policies of the nationalised **Royal Bank of Scotland,** has blamed the public disclosure of boardroom pay in annual reports for ratcheting up executive pay. Penny Hughes, a part-time non-exec director of RBS, said: "Disclosure has been part of the acceleration of pay" as executives demanded deals to match those of their peers. She warned that countries such as Sweden, which were "less tolerant" of high pay, were losing out in the competition for talent. Hughes, who is also chair of the bank's remuneration committee, was speaking at a conference organized by the Association of British Insurers in London at which a former top banker urged directors to resist shareholder calls for pay restraint.

No surprise that five out of the top ten directors' salaries listed by the Labour Party research department's *Fact Service* are employed by electricity distributor National Grid, which has been forced by the US authorities to retract more than $4m worth of "outrageous" expense claims, including for face cream, school fees of employees' children, picture hanging fees and the cost of wine shipments – all of which would have helped inflate power prices for New York consumers, had they not been spotted and vetoed. Steve Holliday, ceo of National Grid, tops Labour's RD table with £2.27m and fifth is National Grid colleague Tom King on £1.58m. But three other NG directors - Steve Lucas, Nick Winser and Mark Fairburn won't be feeling too hard done by as they all got salaries of more than £1m

Bankers' bonuses: Boris speaks out

Mayor of London, Boris Johnson, warned *Daily Telegraph* readers to expect a 'train crash' if the UK's top bankers award themselves massive bonuses this Christmas. "What else do we expect to happen around about Christmas, just as large numbers of public sector workers realise that they have to look for a new job and just as businesses of all kinds start to feel the chilling effects of cuts in public spending? The bankers will be getting their bonuses – that's what. The banks have to understand that this year public feeling may be even more inflamed than last and politicians will be facing colossal pressure to appease public indignation – and the risk is that this year they may take steps of a fiscal or regulatory kind that would do long-term damage to London as a financial centre and as a tax generator for the rest of the economy," said top Tory Boris. "We need the bankers to break the habit of a lifetime and anticipate this problem. We still have time. There are months to go before we see this combustible contrast, between public sector lay-offs and vast bankers' bonuses."

A corporate mea culpa came from **Network Rail** chairman Rick Haythornthwaite, who admitted the company had been "under-reporting" minor accidents – ones where a worker is forced to take off at least three days from normal duties. He said the matter was "deeply regrettable". His admission that a fifth of such injuries failed to make the logbook – contrary to Health and Safety Executive rules – partly explains Network Rail's suspiciously low ratio of minor accidents (100 last year) to the 85 major ones, such as broken legs. NR, which takes £4bn a year from taxpayers, docked points from managers for reporting minor incidents. That gave them an incentive to keep quiet – or risk being passed over for promotion and the consequent rise in pay and bonuses. Haythornthwaite has put an end to that scheme – as well as reviewing what's been going on for more than five years. But he refuses to demand that seven present and past directors give back at least part of their bonuses. These NR directors who shared £2.36m in bonuses last year pocketed bigger awards than they should have done. The trade union Unite's claims were supported by findings from the Office of Rail Regulation, which described Network Rail's reporting of the incidents as "obscure and wrong". Such under-reporting, Unite alleges, had the effect of boosting directors' bonuses, including the £641,000 paid last year to outgoing chief executive Iain Coucher. That was on top of his £613,000 salary for running the state-backed company. Network Rail's remuneration committee, chaired by former Boots boss Steve Russell, has to take the company's safety record into consideration before awarding any bonuses.

City bonuses this year are expected to rise from £6bn to £6.8bn, according to the Centre for Economics and Business Research. **HSBC r**evealed that it had set aside £1.6bn for its investment bankers in the first half, a £200m increase on last year despite a one percent drop in net operating income. "Performance-related costs were lower, as performance declined from the exceptional levels reported in the first half of 2009," the bank said. Higher salaries, though, more than offset the decline in bonuses. Remuneration reform is beset with difficulties: the marketplace is global and competition fierce. UBS banned all bonuses in 2008 and lost so much talent that profits in its investment bank collapsed. Politicians dare not take that risk on a national scale. Changes in the structure of bonuses have been implemented, with as much as 60 percent paid in shares and deferred for three years, but size has been left unregulated. As a result, a lot of mediocre bankers are still vastly overpaid, as one top investment banker readily admits. Another problem is how to measure pay. Investment banks use a compensation-to-income ratio that tended to settle at about 50 percent. Barclays' annual report defines the ratio as 'staff compensation compared to total income net of insurance claims.' But the measure excludes provisions on bad debts, so strips out the worst mistakes made by staff in previous years. Barclays' ratio in 2009 was 38 percent, which was applauded. But, including the £2.6bn of provisions, the ratio was 49 percent. The bank executive reckons a simple improvement would be to measure the ratio *net of insurance claims and provisions*. Policymakers want to go further still. Andy Haldane, the Bank of England's executive director of financial stability, described much of banks' profits in the past decade as a "mirage" and believes an entirely new measure of shareholder return needs to be developed to better capture the cost of risk. "Banks' profits may have been flattered by the mismeasurement of risk. Risk illusion, rather than a productivity miracle, appears to have driven high returns to finance. Think of a £100,000 house bought with a £10,000 deposit. If prices rise ten percent, the house is worth £110,000. As the mortgage remains £90,000, the homeowner's return on equity is 100 percent. However, the return on assets is just ten percent – the growth in value of the home." As Mr Haldane puts it: "Virtually all of the increase in the return on equity of the major UK banks during this century appears to have been the result of higher leverage. Banks' return on ***assets*** – a more precise measure of their productivity – was flat or even falling over this period." In other words, bankers were not being smart, just borrowing more. And reward structures encouraged them to do so. Little surprise, then, that "those banks with highest leverage are also the ones which subsequently reported the largest writedowns," Haldane noted. Knight Vinke, the activist investor, has been more explicit – arguing that return on assets is the only measure by which bankers should be measured. In a submission to the Future of Banking Commission, it said*: "Management compensation schemes should reward real returns on assets, not leverage. Incentive schemes need to be overhauled."* The idea is that real performance, stripped of the multiplying force of debt and the risk that carries, should be recognised. So far, though, there is no momentum to change compensation structures. Global regulators prefer to align staff incentives with those of shareholders, which misses the point that both have been incentivised in the wrong way. Lehman Brothers was a paragon of share-based remuneration, yet the risks it took nearly destroyed free-market capitalism. George Osborne and Vince Cable are threatening to crack down on bonuses if the banks fail to support the recovery by lending to business. Behind their words lurks the threat of another tax, on top of the £2.5bn balance sheet levy already in place. Lenders are far from impotent. According to th**e Bank of England** they could set aside £10bn this year to support lending by restraining bonuses and dividends. It is unlikely they will, but the pressure for bonus reform is mounting.

Credit Suisse hinted that its decision to distribute a multi-million pound bonus-round was necessary to avoid losing key people to its rivals over the next few months. Around 400 bankers are thought to have benefited from windfall payments, in addition to the payments traditionally made at the end of the year. The bank consulted with the Financial Services Authority over the September bonuses, although it is not clear if the Government was warned in advance. Credit Suisse emphasised that the payments are compliant with the FSA's latest rules and include tough conditions including deferred payment and claw-back provisions.

Politicians are lining up to give shareholders greater control over executive pay, said Bill George, professor of management practice at Harvard Business School. On the surface these changes sound like shareholder democracy, which would be a good thing. But rather than solving problems with executive compensation, they may result in myriad unintended consequences. Case in point: The Dodd-Frank Wall Street Reform and Consumer Protection Act grants shareholders advisory votes on compensation, allows activist shareholders with only three percent ownership to nominate board members, and prohibits voting by retail brokers representing small shareholders. These changes are likely to empower short-term money movers such as hedge funds at the expense of long-term owners—and pressure management to focus on the short term, which is the exact opposite of what's needed.

"We could have sworn that last year wasn't much fun for UK plc, what with that nasty recession," said *Management Today*. "However, according to a new report by **Deloitte**, the average bonus for FTSE 100 executives nonetheless actually jumped from 95 percent to 98 percent last year. The theory seems to be that although things were bad last year, they weren't quite as bad as everyone expected - so for many top bosses, their bonus hurdle was set too low. Now we remain firm believers in the value of bonuses, and recognise the difficulties in trying to predict what represents a decent performance twelve months down the line. But this is no way to convince a sceptical public that UK plc has learned its lessons about 'rewards for failure'.

INTERNATIONAL

The **Brisbane** based RiverCity Motorway company, has not let a Au $1.67bn (£988m) full-year loss stop it paying bonuses to its senior staff. The company, which runs Brisbane's CLEM7 tunnel, warned it could breach the covenants on its $1.34bn of debt unless traffic volumes picked up. It is now seeking a reprieve from its lenders. Fortunately for the road's chief ceo Flan Cleary, some of the bonuses were only calculated not on traffic volumes - which are less than half their original forecast - but simply on the toll-road being open! Cleary was paid a Au $370,960 incentive (£219,500) for the year, which included a bonus of 65 percent of his base wage in May which was linked to 'completion' of the construction of the toll-road. Cleary saw his base salary rise 23 percent for the year to $410,670. His total remuneration almost doubled to $830,797 (£491,600). RiverCity's cfo Christine Hayward bagged a $229,312 (£135,687) bonus, largely due to the opening of the road. ''The directors know that a significant improvement in traffic volumes, revenue growth and close management of expenditure will be necessary for the group to stop drawing on cash reserves, meet its first debt covenant test in June 2012, and prevent default under project and loan documents which would crystallise immediate repayment of the loans,'' warned RiverCity in its accounts.

Commerzbank, Germany's second-biggest bank, was the winner after dismissal of appeals cases filed by 14 former Dresdner Kleinwort investment bank employees over bonus cutbacks. The Frankfurt labour appeals court backed a lower tribunal, which dismissed the cases last year. The employees seek bonuses for 2008 ranging from about €29,000 to €450,000. Commerzbank acquired Dresdner Bank AG last year and faces similar suits in London. Commerzbank, which was forced to tap Germany for €18.2 bn of capital during the credit crisis, cut prospective 2008 bonuses for Dresdner employees by as much as 90 percent after the unit posted an operating loss of €6.3 bn that year. "Like the lower court, we think that the Dec. 19 letter didn't say that the lender wanted to promise a specific amount as bonus," Presiding Judge Georg Schaefer said. "Quite the contrary, in a very clear manner it expressed that the prospect to get a bonus was a preliminary one which was subject to a later review of the results." The ruling is the first by a German appeals court over the dispute and Manuel Rhotert, a lawyer for some the plaintiffs, said he will appeal against the decision. The long-term significance of this case grows by the hour as regulators force the West's top banks to defer pay-out of up to 80 percent of large bonuses for at least three years, thus creating potential uncertainty should the employer bank be taken over in the interim period.

Germany's troubled **Hypo Real Estate bank,** which last year narrowly avoided bankruptcy before being nationalised, has paid out €25m in executive bonuses, *Der Spiegel* reported. Hypo, the property and municipal funding specialist, paid out the bonuses for 2009 after executives threatened legal action, the German weekly said. HRE board chairman Manuela Better gave the green light to fulfil a promise made by her predecessor, Axel Wieandt, who left suddenly in March after disagreeing with Germany's banking sector stabilisation fund SoFFin over the question of remuneration. Directors' salaries at HRE were set at a maximum €500,000 per year, in line with the rule at all banks in Germany which have benefited from state aid. During the 2008 financial crisis HRE collapsed, partly due to major business errors made by its German-Irish subsidiary Depfa, and has only been saved by 100 percent nationalisation and an infusion of €142 bn in state guarantees. HRE was the only German bank to fail Europe-wide stress tests in July, and it has become heavily dependent on state guarantees to be able to refinance its debt on the financial markets at affordable interest rates. In July it began creating a 'bad bank' to which it plans to transfer €210 bn in risk positions and non-strategic assets.

Philippines President Benigno Aquino III has issued an Executive Order suspending all allowances and incentives—including Christmas bonuses—to the board members of government-owned corporations amid a public outcry over these officials' excessive perks.

These officials will receive only their basic salaries and "reasonable per diem" until Dec. 31, and there will be a moratorium on the increases in salaries, allowances, incentives and other benefits—except those covered by the Salary Standardization Law—until the increases are approved by the Palace. The President has created a task force on corporate compensation that will review all remuneration granted, including the discretionary funds to the board members, officers and rank-and-file employees of government corporations.

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