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it's our business

newspad of the Employee Share Ownership Centre

Let them eat CoCos, says Bank of England

Banks are too focused on executive pay and shareholder dividends and need to focus more on the rights of employees, their creditors and wider society, according to the **Bank of England**'s chief economist. **Andy Haldane** argued that companies in the UK and the US, and particularly in the financial sector, are structured in a way that encourages them to take big risks and pay out large sums to bosses and investors, rather than taking a long-term view. As a result, businesses underinvest in the future and can be prone to the kinds of collapse that led to the financial crisis, he said in a speech to the University of Edinburgh's corporate finance conference. Although governance and ownership structures do not necessarily fall under the Bank of England's remit, Mr Haldane said the impact on the wider economy can be severe. Some action has already been taken on this, e.g. making sure executives' bonuses can be clawed back if something goes wrong even several years after they leave a bank, to encourage them to work for the long-term good of the institution. However, Haldane said that more needed to be done. Steps to try to align bosses' interests to those of shareholders by paying bonuses in shares appear to have failed, he said. Instead, Haldane suggested executives should be paid in debt instruments like *contingent convertible bonds* (CoCos), which are wiped out when the bank takes a major financial hit. *Under the terms of a CoCo, an investor is sold a bond by a bank with the condition that should the lender's core capital fall below a certain level the debt will transform into shares to provide the institution with an increased buffer to take new losses.*

Meanwhile, shareholder rights could be changed for the better, for instance by giving more voting rights to investors who have held shares for a longer period of time, in line with a new French law. Haldane suggested using different classes of shares, as is sometimes done in US companies when the founder of a company wants to sell equity in their firm without losing overall control. "These laws and emerging practices are in their early throes and are controversial, especially among institutional shareholders. Nonetheless, they are symptomatic of a common desire to strengthen long-term investors' hand in the oversight of companies," added Mr Haldane in his speech. "If these initiatives grew in prominence, they would begin to address some of the short-term and risk-shifting problems embedded in the current corporate governance model." Employees could be given a greater say in running firms, he said, pointing to Japan, Germany and France, where staff can influence the board. *"A majority of Japanese, German and French company executives put employee job security above shareholder dividends. For UK and US companies, a strong majority place the balance the other way around,"* he said. *"This suggests a very different set of managerial objectives and incentives across countries."*

From the Chairman

The world roller-coaster has been making investors large and small queasy over the past weeks. The brave have bought or been sitting tight. But occasional sharp market corrections like this present a long-term opportunity for share scheme sponsors to issue invitations to employees to participate in new schemes, especially SAYE-Sharesave which benefits from a fixed option price. Curiously, however, many do not do so, but wait instead until share markets appear firmly on the up. This reduces the potential upside which employee participants can look forward to either at scheme maturity three or five years down the line.

Recent market events underline that employee share ownership is not always a one-way bet. Participants get their money back if their SAYE share option award price is higher than the maturity market value. SIP participants however are at risk of making real losses, though these can be tempered by employee share buying at regular intervals. That's why employers should always consider making free or partnership share awards to reduce the prospect of future losses. In any event, the employee share ownership industry should hold its nerve. (I called the bottom last Thursday - famous last words?)

Malcolm Hurlston CBE

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*Chief executive officers in Britain's biggest companies are getting paid on average almost £5m in total annual reward **- 183** times as much as the typical UK shop-floor employee, according to a report from the left-leaning **High Pay Centre**.

It revealed that ceos in FTSE 100 companies earned on average £4.96m in 2014, compared to £27,195 median pay for a full-time UK employee last year. The ceo:worker pay ratio - now at 183 times the earnings of the average full-time UK employee - has risen sharply from 160 times just five years ago.

Furthermore, the top ten FTSE ceos last year earned £156m between them in total reward, led by **WPP** boss **Sir Martin Sorrell**, whose package was £43m.

However, most media reports ignored the fact that, for the most part, the base salary of the ceos constituted less than half – and less than a quarter in some cases - of their total reward. Maturing long-term incentive plans (LTIPs) and other executive performance-based incentive schemes were the reason why the headline numbers were so large.

As some of these maturing LTIPS were launched in 2009, when business worldwide was still on its knees, post the financial crisis, it is hardly surprising that they have paid out big time – as the partial recovery has taken hold. By comparison, the top FTSE100 share price index has risen by 52 percent during the last five years and average dividends have risen sharply over the same period too, despite a poor year in 2013.

Predictably, the High Pay Centre report triggered a wave of protest from unions and others, though defenders of the executive reward status quo were more reluctant to come forward than in previous years. Even the so-called 'bosses' union,' the **Confederation of British Industry (CBI),** warned that very high executive reward was only ever justified by exceptional performance in the workplace and that the two should always be linked. This was a dig in the ribs of those misaligned FTSE100 companies who continue to raise ceo and executive salaries when pre-tax profits are going ***down.***

The question of whether stratospheric total executive reward packages will be more tightly regulated in future years will feature strongly in the agenda of the Centre's **17th Global Employee Equity Forum** in **Davos** on **January 28 & 29** *(see inside for more detail),* as will the structure of LTIPs, which have been criticised recently by remuneration experts. Research published last May by the same High Pay Centre 'think-tank' said that LTIPs allegedly created 'perverse incentives' by encouraging executives to focus on gaming the system to maximise the amount they can earn. "LTIPs still encourage behaviour that disregards long-term sustainability in favour of medium-term performance," the HPC claimed. "They could encourage cutting costs or buying back shares just for the sake of improving the share price, or discourage investment in long-term improvements to protect short-term profit margins," it claimed.

Last year's ceo total reward packages rose slightly from the previous year's £4.92m, but were well ahead of the £4.13m average in 2010. The HPC said that its latest report would create pressure for further action "to reduce gap between the super rich and low and middle-income earners."

Since 2013 UK-listed companies have had to publish a single figure detailing their top executive's salary, as well as being required to give shareholders a binding vote on directors' pay. Shareholders had the ability to vote against ceo pay packets, but rarely did so - only an average 6.4 percent of voters objected to their ceo's proposed salaries at recent agms, added the HPC.

"Pay packages of this size go far beyond what is sensible or necessary to reward and inspire top executives," said HPC director Deborah Hargreaves. "It's more likely that corporate governance structures in the UK are riddled with glaring weaknesses and conflicts of interest." Hargreaves told the **BBC**'s *Today* programme: "We've seen executive salaries pulling right away from the rest of society, creating a small elite of people who are just paid astronomically. The Coalition Government introduced some welcome reforms in 2013 that have at least enabled us to get a better understanding of the executive pay racket. However it's clear that these reforms didn't do nearly enough to start building a pay culture where everybody is rewarded fairly and proportionally for the work that they do."

In response to the study, the **TUC** said that pay inequality had now reached "stratospheric levels" while the **Unite** union called for institutional investors to "use their clout to draw a line in the sand over ceo pay".

The CBI said that high pay was only ever justified by 'exceptional performance' and there must always be a clear link between the two. In FTSE 100 firms and beyond, it's important that boards and shareholders hold the highest earners to account. Shareholders now have a vote on companies' pay policies and it is important that this is used effectively," added the CBI.

The free-market think tank, the **Adam Smith Institute**, was more combative, saying that the quality of a ceo could make or break a company: "Ceo pay rewards extraordinary talent and skills in a highly competitive, globalised market," said its deputy director Sam Bowman.

The HPC report claimed that changes to regulations so that UK-listed companies have to publish pay details of their leading executive appear to have had virtually no effect in curbing 'excessive' executive pay. "It seems highly unlikely that the gap between ceos and other workers will close in the foreseeable future," said the report.

According to the **Office for National Statistics**, the UK's average total pay was around **£488** a week in June this year. Comparing April to June 2015 with a year earlier, UK wages increased by 2.4 percent including bonuses, and by 2.8 percent excluding bonuses. That's over a period in which there was zero consumer price inflation — so wages are rising while the prices of ordinary goods people buy aren't. Average total pay for UK employees in nominal terms (that is, not adjusted for consumer price inflation) increased from £311 a week in January 2000 to £488 a week in June 2015; an increase of more than 56 percent.

*Almost 4,000 US public companies will have to disclose the pay ratios of their ceos against the median pay of their workforce, thanks to a split vote by the US **Securities and Exchange Commission (SEC)**. Its chairwoman Mary Jo White said the regulator had no option other than to pass the rule, which passed in a 3-2 vote, with the two Republican commissioners voting against. The disclosure, set to come into force in 2017, will fuel a growing debate over income inequality and the minimum wage.

The SEC then published the text of its final rule that U.S. public companies disclose: the median of the annual total compensation of all employees of the issuer, except the issuer's ceo; the annual total compensation of the issuer's ceo and the ratio of those two amounts, said lawyers *Sullivan & Cromwell*. Disclosure will be required from the first fiscal year beginning on or after January 1 2017; accordingly, the rule will not be effective until the 2018 proxy season. The requirement will not apply to emerging growth companies, smaller reporting companies, foreign private issuers and registered investment companies. Highlights of the final rule include:

*Median employees are now required to be identified only once every three years unless there has been a change in the issuer's employee population or employee compensation that it reasonably believes would result in a significant change to the pay ratio.

*Full-time, part-time, temporary, seasonal, U.S. and non-U.S. employees continue to be included, but issuers may now exclude up to five percent of non-U.S. employees (or more to the extent necessary to comply with foreign data privacy laws).

Cost-of-living adjustments are now permitted in determining the compensation of employees but the issuer must simultaneously disclose the pay ratio without any cost-of-living adjustments applied.

*An issuer may continue to select a methodology for identifying the median employee that is appropriate to its size, structure and compensation practices, including statistical sampling or consistently applied compensation measures (such as payroll or tax measures).

Democrat presidential hopeful **Hillary Clinton** said recently that the typical US ceo earns about *300 times what the average worker is paid.* The SEC was tasked with enforcing provisions contained within the Dodd-Frank Wall Street reform act, which marked its five-year anniversary in July, including the pay-ratio rule. "It is the law and we are required to carry it out," White said. Opponents called the rule "pure apple sauce, unconstitutional and a page from big labour playbook". It will provide a counterweight to current practice, which is simply to compare an executive's pay with that of other ceos in the same industry, a method which has contributed to ever upward spiralling executive pay: ceo compensation is currently about 300 times that of average line workers, compared with 30 times in 1980. Company-specific ratios will help shareholders evaluate the effect of skewed pay policies on company performance. The Dodd-Frank Act forces US corporations to reveal what their ceos earn compared to the average worker, but some companies, (*usually those with comparatively low ceo: line worker pay ratios)* are already embracing pay transparency to build their corporate reputations. Under the final rule, companies will determine the methodology to find the median employee. This can be determined using statistical sampling, calculated once every three years instead of each year, which should lower compliance costs. Nevertheless, compliance won't come cheap. What corporations fear most, according to the *Washington Post*, is that the widespread use of social online networks will encourage consumers from 2017 onwards to mount boycott campaigns against the products of companies they perceive as having exceptionally high ceo v line worker pay ratios.

Timing issue over posties' ten million new free shares

Although the government confirmed it would make a free allocation of a further **10m shares** (around one percent of **Royal Mail'**s issued equity) to eligible postal employees, it was still unclear, as *newspad* went to press, how much longer they would have to wait to get them.

For the promised new allocation of up to 70 more free shares each is tied to the timing of the sell-off of the government's remaining 15 percent stake in Royal Mail (RM) and therein lies a problem for Chancellor George Osborne.

He is keen to unload the taxpayers' final stake in RM in order to meet the state's huge benefits and services spending obligations, but the price of RM shares has been on the slide for weeks, in tune with the performance of the main LSE index, the FTSE100. By August 26 RM ords were trading at *ca* **454p** each, after market falls, compared to an average price of 520-525p back in mid-June.

Happier days last June, when the **Department for Business, Innovation and Skills (BIS)** placed 15 percent of RM's shares – half its remaining taxpayers' holding - with City institutions, selling them at **500p** a share, seem already far away.

The sale, at a three percent discount to the prevailing market price, was conducted by the investment banks **Bank of America, Merrill Lynch and JP Morgan,** as well as by **Goldman Sachs**, which retained the role it held during RM's controversial flotation.

If BIS tried the same tactic next week, the government would get nowhere near the 500p per share price it obtained in June, though the new selling price, in all probability, would be still considerably higher than the flotation price of 330p in October 2013.

Nevertheless, the government has pledged to push the sale through before the end of the current fiscal year on April 5. BIS secretary of state **Sajid Javid** announced in a corporate report: "The Government believes that there is merit in rewarding the employees of Royal Mail for their hard work, which has contributed to the recent performance of the company and the maintenance of the universal postal service in the UK. The Government has decided, therefore, to make a free allocation of 10m shares (around one percent of the value of the company) to employees.

"The new allocation will follow the same rules that applied to the original scheme to promote its longevity, enable employees to benefit from those tax advantages and to strengthen employee engagement:

*shares must be held for at least three years. Full tax benefits are only available if the shares are held for at least five years or for 'good leavers'

*shares will be forfeited if an employee leaves Royal Mail within three years of their award. This will not apply to 'good leavers' whose shares will vest and benefit from tax advantages upon departure

*shares will be allocated to employees equally, regardless of grade or pay levels. The allocation will be pro-rated based on an employee's paid hours to differentiate between full and part time workers

*to be eligible for shares, employees will be subject to a qualifying period of employment."

Mr Javid, who had an explosive clash with his sceptical departmental permanent secretary about the merits of the further free shares allocation to postal employees, is determined to see the postal employees' free shares award through as soon as possible. However, he cannot go it alone – Mr Javid has to liaise at every step with Mr Osborne. When the final sale happens, all eligible full-time Royal Mail employees will get about 70 more free shares each to add to the 729 they received, in two batches, from October 2013. *Posties* who stay the course until the new free shares distribution will have free RM shareholdings worth ca **£3,750** each in their Share Incentive Plans (SIPs), provided the share price does not fall further.

Meanwhile, **Communications Workers Union** general secretary **Dave Ward** continues to lobby hard for the voting rights of postal employee shareholders. In the union's in-house journal '*The People's Post*', he said: "When it announced the sale of half of its remaining stake in June, the government said it would give 'up to one percent' of its final 15 percent to employees. When the government awarded employees free shares in the initial sale, it designed the trust to deny them the ability to exercise a collective voice. If it wants employees to have a long-term stake and a proper voice in Royal Mail it must reverse this and set up a meaningful workers' trust."

Almost 150,000 postal employees each received their allocation of free shares as part of the then Coalition government's pledge to award ten percent of Royal Mail's total equity to its employees as part of the privatisation process. The SIP which was set up in RM is the biggest all-employee share scheme in the UK.

As with the original allocation, the shares will be held in their SIPs, so that employees can benefit from tax advantages. RM's huge all-employee SIP and Sharesave plans are administered by Centre member **Equiniti.**

RM is paying a final dividend of 14.3 pence per share, so eligible full-time employees with 729 Free Shares received £104 pre-tax as a final dividend payment on **July 31**. Eligible full-time employees with 729 Free Shares have received around £248 in dividends since privatisation. Eligible part-time employees received a dividend based on their pro-rata allocation of free shares. CWU-grade employees will receive a payment because the profit gateway as part of the 2014-15 incentive plan was achieved. The amount will be confirmed shortly.

Equiniti explains on the Royal Mail website that the *Dividend Reinvestment Plan* (DRIP) is an easy and cost effective way for postal employees to build up their shareholding by using cash dividends to buy additional shares in their company. Rather than receiving a dividend cheque through the post or having their bank account credited with the dividend payment, shareholders in companies that operate a DRIP can choose to use their cash dividend to buy additional shares. Whole shares are purchased with any residual money being carried forward and added to the next dividend. However, if the amount of the dividend, less any dealing costs, is insufficient to buy a single share no charge is made and the dividend is carried forward.

Treasury to consider Centre views

The Treasury has assured Centre chairman **Malcolm Hurlston CBE**, that its ministers will take into account the Centre's views when employee share scheme issues are next studied in detail.

This encouraging promise came after Mr Hurlston had written to **Work & Pensions secretary of state, Iain Duncan-Smith**, asking him to boost employee share ownership in general and, in particular, to help raise the profile of the Company Share Option Plan as a good example of the 'One Nation' society which the government espoused.

Mr Duncan-Smith passed on his letter to the Treasury, where Edward Johnson, of the Business and International Tax desk, replied to Mr Hurlston on behalf of the chancellor, **George Osborne**:

"Your letter discussed raising the profile of share schemes and increasing the tax advantages they provide. This Govt firmly believes in the importance of share schemes to support and encourage staff productivity and staff retention. Any increase in the tax advantage would have a cost to the Exchequer and this would need to be carefully balanced against other priorities.

"This government has demonstrated its support for these schemes by increasing the limits for Share Incentive and SAYE schemes and enabling digital filing of share scheme returns to make their administration simpler. In addition, the government has been very happy to see number of companies with schemes increase to more than 10,000 in 2012/13.

"I would like to reassure you that the government keeps all elements of the tax system under constant review and very much appreciates your comments, which will be taken into account when considering these issues."

Use of ESS not as intended

Newspad has for some time voiced concerns, as have others, that the controversial **ESS (Employee Shareholder Status)** scheme, nicknamed 'Shares for Rights', could end up offering far greater tax benefits than originally intended, and that the scheme should be capped or possibly withdrawn and the tax relief better targeted. The scheme has also been criticised for having a detrimental impact on employee rights and the image of employee share schemes generally.

Writing in **CMS's** client employment newsletter, **Nicholas Stretch** reports how private equity executives are now large users of the scheme and that HMRC are often giving helpful valuation confirmations for participants, which gives some support to this. So far though, there has been little sign of any political change leading to any withdrawal or scaling-back of the scheme or any hardening of HMRC attitudes towards it.

"As predicted, ESS has so far not proved popular in practice, although law firms have implemented this for various clients," said Mr Stretch. "For most employees, the security provided by the rights not to be unfairly dismissed and to receive redundancy pay is probably worth more than the £2,000 in tax-free shares, which is all that has to be offered. For most employers, the mechanics involved are relatively cumbersome and the implementation costs are high. Furthermore, many employers do not want large numbers of small shareholdings.

"However, ESS has proved to be a big hit with private equity and venture capital firms," he said: *"The senior management of a company with private equity backing is less likely to be concerned about giving up statutory employment rights, being protected by more generous contractual rights. In addition, the tax advantages are extremely useful in protecting the gains realised, as special classes of share with a low initial value but which can significantly increase on a sale of the company, can be devised."*

What has been missed, or played down, in some commentaries about ESS is that the CGT exemption, though limited to the first £50,000 worth of shares acquired, could produce huge gains for senior executives when these shares are finally sold later on. For example**,** a senior employee of XYZ Ltd accepts £49,500 worth of ESS Shares and five years later he sells them, making a gain of £300,000. Because the original value of his shares was within the £50,000 maximum, his **entire gain of £300,000** on this transaction would be exempt from CGT.

"*The UK Revenue has been keen to show the success of the policy and has been agreeing relatively favourable share valuations. Indeed, concerns exist that this is becoming a major source of tax loss/ abuse and that ESS may be withdrawn or have its tax benefits capped,"* wrote Mr Stretch.

"Nonetheless, ESS remains an interesting development in UK employment law. With growing concern across Europe in achieving increased employment flexibility, ESS will be of interest to other jurisdictions as an example of how taking away statutory rights can help realise this. This is likely to be an increasing cross-European trend over the next few years. It is a general principle that employees cannot opt out of their statutory employment rights.

"In the UK, this has been eroded by the concept of ESS, introduced into legislation in September 2013. ESS involves an employee giving up rights to receive specified amounts on any future termination of employment. In exchange, employees receive free shares in their employer with special tax advantages."

A minimum £2,000 of free shares must be received for waiving these future rights (although up to

£50,000 of shares can be provided, but Income Tax is due on any value above £2,000). Any gains on these shares will be free from tax when the shares are sold.

Employees of any company and at any level of seniority qualify for ESS (except those who (broadly) already have a 25 percent interest in the company). ESS can be made compulsory for new employees, which is where it has been most used. An existing employee can choose to give up his rights, but cannot be forced to accept this status.

ESS was an attempt by the UK government to address two separate issues - to encourage increased ownership of shares by employees, allowing them to participate in the success and growth of their employer and to address broader concerns that the UK's employment regime is too restrictive, and that reducing the statutory costs of dismissing employees would make employers keener to hire in the first place.

Mr Stretch concluded: "ESS was (and remains) controversial for understandable reasons. The legislation introducing ESS was twice rejected by the House of Lords in the last parliament. It only became law following the 'ping pong' procedure, when legislative amendments are passed between the two Houses at the last minute until a resolution is reached, which is used relatively rarely for issues of this size."

COMPANY SHARE PLANS NEWS

*More than 23,000 **BT** staff have profited from a £265m employee share scheme maturity at the company, with some employees making more than £50,000 each. Participants saved between £5 and £250 a month over a period of either three or five years. They will now be able to buy shares at the fixed option prices set when the schemes started. The 13,000 staff who saved in the five-year scheme will be able to buy shares at £1.04 while 12,730 who saved under the three-year scheme will be able to buy at £1.89. The BT share price stood at £4.68 on July 30. The shares under option can be bought collectively for £77m under the scheme while their market value is £265m, representing a considerable profit for staff. BT said the average gain for staff who saved for five years would be £10,236, while most of those who saved for three years would make £4,400. Those who saved the maximum amount per month – £250 – in the five-year scheme would stand to make £54,064 if they sold the shares at current prices. Those who saved the maximum amount in the three-year scheme would profit by £13,279. A third of BT's UK staff took part in the schemes which matured last month (August), said the company. BT's ceo Gavin Patterson credited the staff with gains in the share price. "I'm delighted that so many BT colleagues are sharing in the company's success through our Saveshare plans," he said.

*Shareholders in the **Esh Group** – many of whom work for the contractor – enjoyed a £6m windfall as the company posted a strong set of results. Around 100 shareholders received an average payout of £60,000 as Esh reported a rise in pre-tax profits to £9.6m for the year to December 31 2014 compared to £3.2m in 2013. The company share scheme is now being modified to "create further scope for management and employees to be rewarded and incentivised towards further growth," said ceo Brian Manning. "This re-organisation has created headroom in order that we can reward more people through the share scheme. The payments made have been directed towards those who have left the company or are nearing retirement so that they may enjoy the fruits of their hard work. None of the founder shareholders or senior team has taken money out." Esh now employs 1,200 people. Manning added: "Our dedicated employees have been our hard-working foundations and, with their continued support, we remain confident of further success."

***LexisNexis** bought the regulatory newswire **MLex** for an undisclosed sum. Employee-owned MLex is a subscription-based wire service providing news and intelligence about regulatory developments. Established in July 2005 by former Bloomberg journalist Robert McLeod, an Australian, and Briton Duncan Lumsden, the service focused first on EU competition law and policy, but has since expanded into areas like telecoms and energy and into jurisdictions such as the US and China. McLeod will stay as ceo and editor-in-chief of MLex, which hopes to take advantage of LexisNexis' global reach to expand further.

***Reward Gateway** will share £6.5m among 269 employees following its purchase by technology investor Great Hill Partners from current owners Inflexion Private Equity. Staff below management level hold a five percent stake in the organisation through Reward Gateway's employee share plan. The more than 100 employees that have joined the organisation since the last share allocation in 2014 will receive a bonus equivalent to one month's salary. The employee engagement software provider distributed more than £1m among 70 staff members in 2010 when Inflexion acquired a majority stake in the organisation. A third programme will be launched shortly. Management and staff have a 40 percent shareholding in the organisation through its shared ownership scheme. This will increase to 45 percent once the deal is complete. Glenn Elliott, ceo of Reward Gateway, said: "Employee engagement has become central for a number of forward-thinking successful organisations. They have realised that engaged employees make better decisions, as they understand more. Engaged employees are more productive, as they enjoy what they are doing, and engaged employees innovate more, as they want their organisation to succeed."

On the move

Iain Hasdell, ceo of the **Employee Ownership Association** steps down in October, when **Deb Oxley**, currently director of membership, will take over.

Newspad*'s* report of the **Centre**'s recent annual conference in **Rome** is featured in the investment bankers **ButcherJoseph & Co.**'s latest bulletin for US clients.

Ramona 'Mona' Hanes will be leaving after two years of service as senior executive for North America with Centre member **Global Shares**, the international software company, to focus on her consulting projects as a principal with her company Red Cape Partners.

Will national living wage rises hurt Eso?

Some in the Eso industry are wondering whether Chancellor George Osborne's summer Budget boost for the low-paid may make Eso schemes a harder sell in future among SME companies. In a surprise announcement, Osborne told MPs that workers aged over 25 would be entitled to a **National Living Wage (NLW)** from next April, to soften the impact of in-work benefit cuts. The Chancellor said employers would be forced to pay such staff a minimum of **£7.20** an hour from next April and raise wages by an average six percent a year to around **£9 an hour** by the scheduled end of this parliament in 2020.

As the current **National Minimum Wage (NMW**) is only £6.50 per hour, Mr Osborne was projecting an increase of almost 30 percent in total to the obligatory minimum wage for millions of base rate adult employees by the year 2020. The extra 70p per hour which employers will be forced to pay to millions of employees from next April would raise the wage bill of a company employing 200 NMW adult workers by £290,000 next year. However, by 2020, assuming a national living wage of £9 per hour is in place, that same company would be paying each employee £5,200 more per annum than today and **£1m** more in total would be added to its annual wage bill. In fact, their extra pay bills will be higher still because supervisors and others will demand additional rises to preserve their pay scale differentials over base level staff on NLW rates.

While multinational companies will shrug this off, as it will affect only their UK payrolls, the implications for UK SME companies, especially in the care homes, hospitality and retail sectors could be dire. Pub groups and cleaning companies, among others, have already spoken out against Osborne's programmed series of large stepped pay hikes for the low paid. These are the kind of businesses which may have considered adopting the HMRC approved **Company Share Option Plan (CSOP),** of which the Centre is the leading advocate.

Companies who already run employee share schemes are unlikely to stop doing so, but the extra national living wage obligations could put off those who were considering whether to install Eso plans for the first time. Either their profits or their reserves will be hit by the need to pay many employees much more than expected and so such companies might feel that an all-employee Eso scheme on top of much higher base pay would be a bridge too far for them.

Hitherto, a powerful argument in CSOP's favour has been that low-paid supermarket check-out staff and the like are most in need of the one-way bet characteristics of CSOP – a scheme in which employees don't have to put in any cash up front. However, from next April, the enforced 10.8 percent increase in base hourly pay for many adult full-time employees under NLW will remove much of the moral force for offering low-paid staff in the private care, food, hospitality and retail industries the chance to improve their lot through participation in a CSOP.

The Centre has always said that employee share schemes should not be used as a bargaining chip in pay negotiations between companies and trade unions, but the issue from now on may be the affordability of Eso schemes in the context of much higher base pay levels in many manufacturing and service industries.

The Centre faces the prospect of grappling with company owners who may be less keen on Eso than before, while at the same time tapping into growing UK employee sentiment that employee share ownership is a good thing, which they want to share in.

Mr Hurlston said: NLW could cast a dark cloud over the endangered CSOP but we must balance the present with the future. We shall watch carefully as the months to 2020 go by."

The **Office for Budget Responsibility** said that up to six million UK earners will see their pay packets boosted as a result of the policy, but it warned that 60,000 people could lose their jobs as a result of the enforced pay rises.

Executive reward monitoring changes gear

The **Investment Association**, which inherited the monitoring of executive reward from the **Association of British Insurers**, is passing on this key consultation service to the **Institutional Voting Information Service (IVIS).**

Andrew Ninian, the IA's director of corporate governance & engagement, has told all leading remuneration consultants: "I am writing to inform you of a number of changes to the process **The Investment Association** will follow for consultations on executive remuneration at UK listed companies. The IA (previously through the ABI) has for many years been consulted along with institutional shareholders on proposed changes to executive remuneration structures at UK companies. This remuneration consultation process will now be taken on by the IVIS team, which is part of the IA.

"IVIS will produce a short summary of the company's proposals which will be sent to our members which the company inform us, they have consulted. As was the case previously, we will then collate member views and feed these back to the company for their consideration in the further development of their proposals."

He promised: *"We will continue to review the need for further engagement or collective engagement with a particular company on an individual proposal.*

"We would ask that if you would like to consult The Investment Association on changes to your client's remuneration structures, you email the proposal to ivis@theinvestmentassociation.org. It would be helpful if you could give us the names of institutional investors the company is consulting.

"In order to provide sufficient time in collating shareholder views on specific proposals, we would ask you to provide any proposals in good time to review and respond to draft proposals. We would appreciate if you could note those communications which are for information purposes only and which do not require further substantial input by your investors. Should you have any questions regarding your future engagement with The Investment Association, please contact Mr Ninian or Nicholas Malasinski (Senior Corporate Governance Analyst, 020 7269 4610)."

Hidden tax implications for eso in the Budget

Centre member employee share ownership law firm **Pett, Franklin** has explored some semi hidden implications for employee shareholders from Chancellor George Osborne's July Budget.

In it, he announced that from April 2016 the current system of dividend tax credits will be removed. Instead, a new tax-free Dividend Allowance of £5,000 per year will be created for all taxpayers, above which dividends will be taxed as income at the rate of 7.5 percent for basic rate taxpayers, 32.5 percent for higher rate taxpayers and 38.1 percent for additional rate taxpayers. While the details of how this change is to be implemented are as yet unpublished, the government stated that it expects ordinary investors to see no change to their tax liability, but that some investors who receive significant dividend income may pay more in tax. Reference to this is made in the Fact Sheet issued on August 17 (Dividend Allowance Factsheet) These changes will have a significant impact on small owner-managed businesses, and the government has stated that reducing the incentive to incorporate is one of its goals in making this change.

*Participants in a statutory Share Incentive Plan (SIP) may choose to reinvest dividends paid on their SIP shares in purchasing 'Dividend Shares'. If they choose to do so, they will not be required to pay any tax on such dividends at the time they are paid. Only if participants leave employment within three years of receiving the dividend will they be charged to tax, which will be on the amount of the dividend originally reinvested to acquire the shares. What impact will the Dividend Allowance have on SIPs? The result may be that some leavers no longer have to pay any tax on their Dividend Shares when they leave. But in other cases, a significant minority of SIP participants may have received more than £5,000 worth of Dividend Shares within the past three years (and some participants may have other dividend income from different sources), *with the result that tax will be payable*.

"The removal of the ten percent dividend tax credit means that some basic rate taxpayers may have to pay tax who would not have in the past," said Pett, Franklin & Co. "We note that this change could require more taxpayers to complete self-assessment returns, potentially in many cases because of a requirement to pay quite small amounts of tax on income over the £5,000 threshold; it remains to be seen how HMRC will deal with this change in practice."

*Companies who are willing and able to encourage their employees to acquire shares may therefore, by paying a dividend on the shares, be able to boost the tax-free income of such employees by up to £5,000 per year. The opportunity for tax free dividends should increase the attractiveness of SIP shares for dividend paying companies, particularly when compared with the costs of rewarding employees through employment. *For an illustration of the potential equivalent costs of a £1,000 dividend, go to Pett, Franklin Share Schemes at a Glance.*

*For independent ***private*** companies in particular, by using a SIP, the company might issue and award to all eligible employees shares of a special class (Employees' Shares) which, for example, carry an obligation to forfeit such shares on leaving employment with the company or group. The unrestricted market value of such shares awarded to each eligible employee in a tax year must not exceed the annual limit of £3,600, but the acquisition of such Employees' Shares, upon and subject to the rules of the SIP, would be free of income tax and NICs. From next April, participants in such a SIP would, in common with all other individual shareholders, then be able to receive dividend income of up to £5,000 per tax year free of income tax (assuming they have no other dividend income save, perhaps, on shares in an ISA). The idea of allowing employees to acquire a special class of restricted shares in a tax-efficient manner would not work in relation to CSOP or SAYE share options as the legislation governing such schemes includes an additional requirement that the shares used must be either 'employee-control' shares or 'open market shares.' The acquisition of shares through the grant and exercise of EMI options, similarly, only affords relief from income tax and NICs on the growth in value of the shares over the option period. It is only by using a SIP that shares may be acquired by employees entirely free of tax.

For listed companies, while offering shares of a separate class may not be feasible, it will still be possible to make tax-free share awards under a SIP which are subject to forfeiture if an employee leaves. Employees may then be paid tax-free dividends on the same basis as all other shareholders.

Taxation of pensions – a new role for employee share ownership?

The total amount an individual can save into a pension plan in a given year without triggering a tax charge is limited to the annual allowance. Originally set at £215,000 when first introduced in 2006, this has since been substantially reduced and is currently set at £40,000 per tax year for 2015/16. This allowance is now set to be reduced even further for high earners. This reduction will apply on a tapered basis, reducing by £1 for every £2 by which the individual's income exceeds £150,000, so that individuals earning £210,000 or more will be limited to an allowance of £10,000 per tax year which they may contribute to their pension each year without incurring tax charges.

Many high earners are likely to find this level of pension contribution insufficient and the challenge for employers is therefore how to respond. "*It may be that the new pension limits should encourage the introduction of different forms of employee share plan - similar to those more often seen in the US and consistently with the pressures from regulators and investors, particularly in financial services, to encourage significantly longer term shareholdings - where share awards are made with an expectation that shares will continue to be held in the long term, with the employee receiving the cash value only on retirement.*" added senior partner David Pett.

CONFERENCES

Centre-IoD Thursday, September 3

There is still time, just, for you to book a seat for the Centre's next joint share schemes conference with the **Institute of Directors,** which takes place on **Thursday September 3** at the Pall Mall HQ of the IoD. This all-day event is co-promoted by Bird & Bird, David Craddock Consultancy Services, Fieldfisher, MM&K, Nabarro, Pett Franklin & Co, Primondell and the RM2 Partnership. The programme will focus on SME companies and will attract owners, ceos, directors, fds, HR specialists and other key decision makers in such companies. Speakers from Centre member firms will help the SME attendees decide whether to introduce an employee share scheme or to deepen existing employee share ownership in their businesses. Confirmed speakers are: **Steve Thomas**, HMRC Share and Assets Valuation unit; **Colin Kendon,** Bird & Bird**; Graham Muir,** Nabarro**; Mike Landon**, MM & K; **Mark Gearing**, FieldFisher; **David Craddock**, David Craddock Consultancy Services; **Nigel Mason**, RM2 Partnership; **David Pett** and **Stephen Woodhouse**, Pett Franklin & Co.; **Jeremy Mindell**, Primondell and **Robert Head**, formerly of Pearson. For further details on the presentations and speaker bios please visit the event page.

Delegate prices: Centre / IoD members: £360 + VAT; non members: £460 + VAT. If you are a Centre member, contact the IoD events team at events@iod.com or +44 (0)207 766 8919 to register at member prices. If you are a non-Centre or non-IoD member you can register to attend this conference through the IoD website. For all enquiries, contact Jacob Boult at Centre HQ – email jboult@esopcentre.com or phone him at +44 (0) 20 7239 4906

Centre – STEP Guernsey, Friday October 9

The Centre's annual Guernsey share schemes seminar, held in partnership with the Society of Trust & Estate Practitioners (STEP), Guernsey branch, will take place on **Friday** morning **October 9 2015** at the St. Pierre Park Hotel, St. Peter Port.

The latest addition to the programme, Mahesh Varia of Travers Smith will review the disguised remuneration rules.

The event will cover employee share schemes from a trustee perspective, providing an update for trustee delegates. Law Society accredited, this half day seminar will run from 9am till 1.15pm, prefaced by refreshments and followed by lunch.

Gavin St Pier, States of Guernsey minister for treasury & resources, is guest of honour, speaking on the issues of the moment. Gavin is a former member of the Centre's steering committee. The following expert speakers will be presenting: Stephen Woodhouse, **Pett Franklin & Co**; Alison MacKrill, **Carey Olsen**; Jeremy Mindell, **Primondell**; David Craddock, **David Craddock Consultancy Services**; Mahesh Varia, **Travers Smith**. For further details, including a breakdown of the presentations and speaker bios visit the event page.

Delegate prices: ESOP Centre/STEP members: £325 Non-members: £450. To register to attend as a delegate, contact the Centre at:

esop@esopcentre.com, tel: +44 (0)207 239 4971.

Centre Awards Dinner & Reception October 28

Ticket sales are going well for the Centre's 14th annual employee share ownership reception and awards dinner, which will be held in the grand Italianate surroundings of the **Reform Club**, Pall Mall, on **Wednesday October 28**. Winners and runners-up for all the categories of the Centre's annual share scheme awards will be announced at this prestigious black-tie event. The candidates for this year's awards are listed below. Applications by members or their clients for places should be made without delay, as there is a ceiling on the number of diners. For details of this year's awards categories and nomination submissions, please visit the Awards 2015 page on our website.

Approved nominations for Centre Awards 2015:

Best international all-employee share plan in a company with more than 1,500 employees in at least three countries

Amadeus IT Holding S.A., self-nominated

Royal Dutch Shell, nominated by Computershare

Imagination Technologies Group plc, self-nominated

Best all-employee share plan in a company with fewer than 1,500 employees

Abzena, nominated by MM&K

Henderson Global Investors, self-nominated

Best all-employee share plan communications

Abzena, nominated by MM&K

Royal Dutch Shell, nominated by Computershare

Amadeus IT Holding S.A., self-nominated

Close Brothers, nominated by Equiniti

Henderson Global Investors, self-nominated

Best in financial education of employees

Auto Trader, nominated by Capita

Henderson Global Investors, self-nominated

Best integration of an all-employee share plan into a wider programme of employee engagement

Talk Talk, nominated by Equiniti

Please note: further nominations for this category are being accepted through the ***Involvement and Participation Association (IPA),*** *and will be announced following its call to members for submissions. To submit your entry please use our secure online application form (applies to the seven main categories).*

Best use of video in share plan communications

Home Retail Group, self-nominated

Amadeus IT Holding S.A., self-nominated

Telefonica, self-nominated

The best employee equity intervention by a major company chairman or ceo

Sacha Romanovitch, Grant Thornton ceo

Cesar Alierta, Telefonica chairman

In all categories the judges' first consideration will be whether to make an award or not.

DAVOS 2016: Jan 28 & 29

Members who want to register more than one representative for the Centre's 17th winter conference in **Davos** on **Thursday January 28** and **Friday January 29** can make a huge saving of almost **£400** on the cost of our two-nights accommodation + conference package. *This exceptional deal is offered solely to Centre members making an early bird reservation.*

Attendance at this seminal event in the Centre's calendar, which opens only days after the closure of the World Economic Forum, gains delegates 11 hours of credits under the Law Society's CPD programme.

Prospective Centre speakers are invited to suggest ideas for slot topics and these will be added to those being studied by the programme committee, which to date comprises: **Mike Landon**, a director of **MM & K**; **David Pett**, partner at **Pett, Franklin, Kevin Lim** of **Solium UK**; **Malcolm Hurlston** Centre chairman and Centre international director, **Fred Hackworth**.

We are looking for more presentations on technical share plan and executive compensation issues and equity plan case histories where, in the latter case, the lectern is normally shared by service provider and client.

The Centre negotiated an unusually favourable deal with the four-star **Hotel Seehof** in Davos Dorf, allowing us to **reduce all early bird attendance fees, most by at least £100** as compared to those in force last February. Our *early bird* charges for the two nights half-board accommodation + conference + cocktail party conference package in the Seehof are: **Speakers**: practitioners **£825**; plan issuers **£399**; **Delegates:** member plan issuers **£495**; non-member plan issuers **£599**; member practitioners **£945**; non-member practitioners **£1450**. *No VAT is charged as the event takes place outside the UK.*

Centre member Davos privileges:

*Member speakers may invite an **issuer** client to attend for the speaker package price of **£399**, irrespective of whether the client is a speaker or not.

*Registered speaker or delegate **service providers,** who are Centre members, may invite a **second** person from their organisation to attend as a delegate (qualifying for the accommodation and conference package – *see above*) for the much reduced price of **£550** (instead of the normal delegate price of £945). Email Fred Hackworth:

fhackworth@esopcentre.com now with copy to the Esop Centre at: esop@esopcentre.com to reserve your speaker or delegate place or to suggest topic themes for this annual share schemes brains trust. As usual, there will be an informal dinner for delegates in the Seehof on **Wednesday January 27**, the night before the conference starts. The Parsenn, next door to Hotel Seehof, is the largest ski area in the Davos region, offering 35 top quality ski runs.

The best city in Europe to live in is... Vienna

That's according to the Economist Intelligence Unit's annual survey of the livability of 140 global cities. The Austrian capital and host city to the Centre, again finished only second to Melbourne in the world ranking, which is based on factors such as stability, healthcare, culture, education and infrastructure. Mid-sized cities in wealthy countries tend to do well in the list, while London and Paris suffer because of their size. Warsaw moves into the top tier of liveable cities this year because of lower crime. Getting worse: Kiev, Athens, Moscow, St Petersburg. Report can be downloaded from: www.eiu.com/home.aspx. No surprise then that the European Centre has chosen Vienna as host city for its 28th annual employee equity conference on Thursday/Friday, June 2 & 3 next year. Contact Fred Hackworth at: fhackworth@esopcentre.com if you wish to speak at, or simply attend, this flagship event.

Public sector pay-off cap

The Government is studying consultation responses to its proposed public sector exit payment cap, reported Centre member **Deloitte.** Ministers plan to introduce a cap of £95,000 on the *total* value of exit payments made to an individual when leaving public sector employment. The consultation sought views on the scope, level and design of the cap. In addition, the Government is considering reforms to the calculation of compensation terms and to employer-funded early retirement as part of redundancy packages and plans to consult on these areas in due course.

Equal pay US boss comes a cropper

The Seattle ceo who reaped a publicity bonanza when he boosted the salaries of his employees to a minimum of $70,000 (£45,500) a year says he has fallen on hard times. **Dan Price**, 31, told the *New York Times* that things were now so bad he'd been forced to rent out his house. Three months ago Price was generating headlines when he announced the new salary minimum for all 120 employees at his **Gravity Payments** credit card processing firm. Price said he was doing it, and slashing his $1m pay package to pay for it, to address the wealth gap: "I'm working as hard as I ever worked to make it work," he told the Times. "I'm renting out my house right now to try and make ends meet myself." The article said Price's decision ended up costing him a few customers and two of his most valued employees, who quit after newer employees ended up with bigger salary hikes than older ones. "He gave raises to people who have the least skills and are the least equipped to do the job, and the ones who were taking on the most didn't get much of a bump," Gravity financial manager Maisey McMaster, 26, told the paper. She said when she talked to Price about it, he treated her as if she was being selfish and only thinking about herself. "That really hurt me," she said. "I was talking about not only me, but about everyone in my position." She quit, as did Grant Moran, 29, saying the new pay-scale was disconcerting: "Now the people who were just clocking in and out were making the same as me," he told the paper. "It shackles high performers to less motivated team members." Price said: "There's no perfect way to do this and no way to handle complex workplace issues that doesn't have any downsides or trade-offs." The Times said customers who left were dismayed at what Price did, viewing it as a political statement. Others left fearful that Gravity would soon hike fees to pay for salary increases. Brian Canlis, co-owner of a family restaurant, already worried about how to deal with Seattle's new minimum wage, said the pay raise at Gravity "makes it harder for the rest of us." The Times said Price has dozens of new clients inspired by his move but those accounts won't start generating profits for at least another year.

Salary sacrifice on probation

Salary sacrifice, which in dynamic young SMEs is being increasingly used in conjunction with share option schemes to incentivise key staff, may be soon on the way out. Chancellor George Osborne's July Budget implied that salary sacrifice arrangements are being monitored, which suggests that the government may legislate in the future to disallow them.

HM Treasury will "actively monitor" the effect of salary sacrifice on tax receipts and has left the door open to cutting back on the benefit, revealed the Budget small print.

There were rumours and fears of action targeting salary sacrifice in the run-up to Osborne's Budget, but for the moment, he had other fish to fry.

For the most part, salary sacrifice schemes are set up to enable both employers and their employees reduce their NIC payments, but that's not all they can be used for….

However, HM Treasury has clearly been alerted to the rising cost to the taxpayer of salary sacrifice schemes. The Budget document noted: "Salary sacrifice arrangements can allow some employees and employers to reduce the income tax and National Insurance that they pay on remuneration. They are becoming increasingly popular and the cost to the taxpayer is rising. The government will actively monitor the growth of these schemes and their effect on tax receipts."

Commentators previously warned against cutting the policy as it is seen as a force for good. Salary sacrifice, where employees give up part of their salary in exchange for other benefits including pension contributions, currently costs the Exchequer about *£15bn* a year. The benefit means that as employees earn a lower salary, both the employees and their employer pay lower National Insurance (NI) contributions. Employers can pay part or all of the NI saving into the worker's pension, but it is not mandatory.

Move to streamline share scheme expensing

The US Financial Accounting Standards Board (FASB) issued a proposed Accounting Standards Update intended to simplify the accounting for share-based payment transactions, which is part of FASB's simplification initiative. The proposal did not suggest an effective date, reported Centre members **KPMG** and **PwC.** The FASB will decide the effective date and whether to permit early adoption after considering stakeholder feedback. The comment period ended mid August.

"The proposal that could have the most significant impact is a new requirement to record all of the incremental current and deferred tax effects related to share-based payments at settlement (or expiration) through the income statement," said PwC. The current standard provides for all windfalls – actual tax benefits to the company greater than the accumulated deferred tax asset – and some shortfalls — actual tax benefits to the company less than the accumulated deferred tax asset — to be recorded in additional paid-in capital. Although this proposal would eliminate the complications of tracking a windfall pool to determine the amounts to be charged to APIC, it would increase the volatility of income tax expense. "As a result, we anticipate that this proposal will be controversial."

In a related change, the Board proposed to remove the requirement to delay recognition of a windfall tax benefit that may arise on settlement until the tax benefit is realised through a reduction in current taxes payable. Previously, if these benefits merely increased a net tax loss, recognition was suspended, creating the need for complex record-keeping outside the primary accounting system. On the statement of cash flows, all tax-related cash flows resulting from share-based payments would be reported as operating activities. The requirement to present windfall tax benefits as an inflow from financing activities and an outflow from operating activities would be eliminated.

The proposed simplification would allow companies to withhold an amount up to the highest marginal tax rate applicable to employees in the relevant jurisdiction, without resulting in liability classification of the award. Additionally, the Board proposed that all cash payments made to taxing authorities on the employees' behalf for withheld shares would be presented as financing activities on the statement of cash flows.

"The proposed amendments are aimed at reducing the cost and complexity of accounting for share-based payments," added PwC. "However, they may result in significant changes to net income and earnings per share, including the effect of the exclusion of windfall tax benefits from the hypothetical proceeds used to repurchase shares under the treasury stock method. Additionally, there may be administrative and other challenges (such as systems, processes, and controls) to implement the proposed standard for companies with significant share-based payment activities. The proposed transition methods are complex, calling for prospective, retrospective, or modified retrospective adoption, depending on the provision. Companies with significant share-based payment activity may want to begin considering the potential implications of the proposals."

Non-exclusive jurisdictions

Are exclusive jurisdiction clauses of any use? wonders Centre member **Clifford Chance** in its latest client UK employment update. The Court of Appeal recently considered the extent to which it was appropriate to grant an anti-suit injunction to prevent proceedings continuing in the courts of the jurisdiction provided for by the exclusive jurisdiction clause in a share option agreement. P was employed by E Europe at a very senior level. E Europe's parent company was a Massachusetts company (EMC). P was a member of EMC's stock option plan which provided for Massachusetts' governing law and exclusive jurisdiction of the Massachusetts courts. The plan provided for the cancellation of any awards if a recipient engaged in detrimental activity; the definition of which included not competing for up to 12 months following resignation from the company. By signing and accepting the restricted stock unit (RSU) agreement under which the options were granted, P formally acknowledged that he was bound by its terms. P left to join a competitor and a dispute arose over whether EMC was entitled to cancel his stock options. "Multinational employers need to be aware that in light of this decision where an employee is based in the UK (or another EU country) the UK courts (or courts of the EU country where the employee works) *will disregard any exclusive jurisdiction clause* in favour of the courts of another jurisdiction, said Clifford Chance. This will be the case regarding such clauses in both the employment contract and any ancillary contractual arrangements related to the employment relationship such as bonus, stock option and other benefits schemes. A UK based employee will therefore be in a position to apply for an anti-suit injunction to ensure that any dispute is heard in the English courts even if the English courts then have to consider the dispute in the context of the relevant governing law clause. [Petter v EMC Europe Ltd & anr]

Employee shareholders cost less in taxes, claim

Employee-owners—people who own stock in the companies where they work—are far less likely to lose their jobs than non-employee-owners. An analysis by the California based **National Center for Employee Ownership (NCEO)** of data from the 2015 General Social Survey (GSS) showed that in 2014, 9.3 percent of all working adults in the private sector not in employee ownership plans report having been laid off in the last year, compared to just 1.3 percent of those respondents who said they own stock in their company through some kind of company-sponsored employee ownership plan. Unemployment is expensive for the federal government, particularly in terms of federal expenses for unemployment benefits and forgone taxes. The study estimates the cost to the federal government per unemployed worker, said NCEO founding father **Corey Rosen**. "We believe that the lower job losses among employee-owners saved the federal government approximately $17bn in 2014. Looking just at employee stock ownership plans (ESOPs), we estimate the federal government's savings at approximately $8 bn. For 2010, a recession year, the numbers were $37 bn for all plans and $15 bn for ESOPs alone. In the non-recessionary period of 2002 and 2006, the average annual savings were $16bn for all plans and $6bn per year for ESOPs alone for the 2002-2010 period. These numbers are necessarily estimates based on numerous assumptions. We do not claim that they are anything other than broad estimates, although we believe they are very reasonable estimates. We have been conservative in our approach and have not counted federal costs for unemployment related programs such as retraining. Even if our numbers were as much as one-third too high, which is unlikely, they still would show that the saved costs and tax revenues to the federal government are a multiple of the annual tax costs of ESOPs," said Mr Rosen.

Trustees' £200,000 'fine' over breach of trust

Two UK pension fund trustees were held *personally liable* for payments totalling almost £200,000, made in breach of trust not protected by the exoneration and indemnity provisions contained in the scheme trust deed and rules, in a ruling by the UK deputy Pensions Ombudsman.

Two trustees of the **Pilkington's Tiles Pension Scheme**, Mr Burrows and Mr Lloyd, authorised the return of £193,000 of excess employer contributions to the sponsoring employer. The scheme had both defined benefit (DB) and defined contribution (DC) sections and the excess employer contributions arose under the DC section as a result of members leaving the scheme and taking a refund of their own contributions before their benefits had vested. The scheme rules provided that excess employer DC contributions should be held in a general reserve and "*applied by the trustees as the principal employer shall from time to time direct to pay the costs and expenses of the scheme and/ or to reduce the amount of contributions which would otherwise be required from the employers*".

It was originally understood that the excess DC contributions amounted to around £30,000. At a meeting between the four scheme trustees (Mr Burrows and Mr Lloyd, both of whom were directors of the company, and the two member-nominated trustees, Mrs Hirst and Mr Gratrix) and the financial director of the company, it was agreed that that the excess DC contribution "*should be pooled with the DB section and considered an additional contribution.*" The administrators subsequently told Burrows and Lloyd that the excess DC contributions were in fact valued at £198,647 and arranged for this sum (less fees) to be transferred to the trustees' bank account. On the same day, Burrows and Lloyd authorised payment of £187,191 to the company's bank account. Within the next three months Burrows and Lloyd authorised the transfer of a further £5,819 to the company relating to excess contributions. While B & L were certain that the return of excess contribution had been informally discussed with the other trustees, Mrs Hirst and Mr Gratrix said they had no knowledge of such discussions. Furthermore, there were no references to the repayments in the minutes of the trustees' meetings.

Lawyers *William Fry* said: "Trustees can take note of many important lessons from this ruling. In particular, it highlights the potential conflicts of interest that can arise for trustees and the personal liability which they can face if such conflicts are not managed effectively. It illustrates how important it is for trustees to act in the best interest of scheme members, to be aware of the provisions of the governing scheme documentation and to take legal and tax advice where necessary."

SEC claw-back proposals

The **US Securities Exchange Commission** announced that it had completed proposals for the Dodd-Frank compensation rules by publishing a new claw-back provision. Though somewhat limited by the requirement that a financial restatement take place, in other ways it makes it easier for companies to go after the bonuses earned by current and former employees. "This rule targets the lack of accountability and the inflated compensation that helped contribute to excessive risk-taking in the run-up to the financial crisis," said Kara M Stein, a Democratic commissioner at the SEC, who has pressed the agency to take tougher stances on several issues.

In response to the new rule, some companies might decide to adjust their compensation packages so that executives receive more fixed pay, and less in bonuses, to reduce the amounts subject to the new rule. But shareholders, who generally favour bonuses tied to performance instead of large fixed salaries, might push back against such a shift. The rule allows companies to opt against pursuing a claw-back if the costs of doing so might exceed the amount it wants to recover. That aspect of the rule could become a loophole. It might not be hard for companies to show that the legal costs of going after a bonus would exceed the size of the bonus.

The authorities are overhauling compensation on other fronts as well. The SEC and banking regulators are working together on compensation rules that focus on pay at financial institutions. In addition, the **Federal Reserve** has instituted compensation guidelines that apply to the big Wall Street banks it regulates. These can require a bank to claw back the pay of an employee even when a financial restatement has not taken place and even when no loss has occurred.

Shareholder Rights Directive (2)

Amendments proposed to the **Shareholders Rights Directive** will require companies throughout the EU to hold either a binding or advisory vote on their remuneration policy for directors, said Centre member **New Bridge Street**, part of the **Aon Hewitt** consultancy group.

*Companies would be required to set out their remuneration policy which would be subject to a shareholder vote; all subsequent payments to directors would have to fall within that policy *Companies would be required to hold an advisory vote (or, for smaller companies, an agm agenda discussion item) on the remuneration paid and reported in the year under report *Required disclosure of remuneration paid or awarded to directors would increase significantly and would need to include each element of pay for each director, performance metrics for variable pay and comparison of directors' pay to that of the average employee over a five year period

Other more radical proposals being considered include a requirement to set and report pay ratios, to compare employee pay to non-executive directors' fees, and to permit employees to monitor their company's proposed remuneration policy. At this stage, however, it is too soon to say which, if any, of these proposals will make it into the final regulations.

Details of the amended Directive remain uncertain, since their final form must also be agreed by both the European Parliament and the Council of Ministers (comprising government representatives from each member state); at this stage in the process, either body may propose amendments that could be challenged by the other.

On September 8 the European Parliament is due to vote on the amendments to the Directive (as recommended by its Legal Affairs Committee). If approved, the amendments must then be approved by the Council of Ministers before adoption. If it fails to do so, the Council may propose its own amendments for the Parliament to consider, a process which can continue until the parties agree a formal conciliation process in order to reach an agreement. Already, the Council has its own proposed amendments and will seek to negotiate a compromise ahead of the Parliament's vote in September.

Every EU member state could be forced to introduce measures to reward long-term shareholders, even as concern rises that such measures undermine corporate governance. Two amendments to the EU's Shareholder Rights Directive, currently working its way through the European Parliament, would compel the bloc's 28 states to reward long-term shareholders with additional voting rights, enhanced dividends, loyalty shares or tax incentives. One of the aims of the directive is to improve corporate governance and ensure a "correct and sustainable" executive remuneration policy.

Yet the push comes as evidence from **France,** where double voting rights for long-term investors are long established, shows entrenched investors using such powers in order to disenfranchise minority shareholders and undermine corporate governance. **Proxinvest,** a Paris-based proxy voting agency, said 32 board resolutions that would have been rejected by investors at agms last year on the basis of 'one share, one vote' were carried because of double-voting rights. Many of the resolutions involved issues of remuneration, such as granting free shares to executives or protecting severance payments, or dilutive capital increases. This practice was described as "cheating" by Pierre-Henri Leroy, chairman of Proxinvest, who described double voting rights as "a gimmick ensuring the main shareholder a disproportionate weight allowing him to control a company and to pass resolutions that would otherwise have been rejected".

The findings come as a swath of large investors have rallied in opposition to France's new *Florange law*, which from 2016 automatically extends double-voting rights to long-term investors (who have held the shares for at least two years) at all listed French companies unless they vote to opt out of the provision.

Opponents say that double voting rights – which are supposed to encourage long term investing – entrench the power of majority shareholders and weaken smaller institutional investors, thereby making management less accountable. More than 90 per cent of investors at **Unibail-Rodamco, Vinci, L'Oréal, Air Liquide** and **Capgemini** have now voted to overturn the law, with similar levels of support expected at the agm of **Crédit Agricole**.

But, while shareholders are increasingly flexing their muscles on pay and fighting back on double voting, they are not always winning the battles. In April, institutional shareholders could only look on helplessly as the French government spent €1.23bn to buy shares in **Renault** on a short-term basis, to give it the votes it needed to defeat plans for keeping the one-share-one-vote system. It worked. In the end, 60 percent of shareholders voted against the ruling, but this was not enough as a two-thirds majority was needed. Renault's management was sharply critical of the government's manoeuvre, fearing that increased state influence will scupper plans for greater integration with Japanese partner **Nissan**. The French government then repeated the ploy: it spent €46m to increase its stake in **Air France** to ensure it would be able to enforce double voting there as well. Government victories on double voting have been secured

at **GDF Suez,** and further wins followed at **EDF** and telecoms group **Orange.** At **Vivendi**, the Florange law change was similarly adopted, but this time through the support of major shareholder Vincent Bollore.

However, two resolutions proposed by members of the European Parliament's economic and monetary affairs committee, Sergio Gaetano Cofferati, an Italian centre-left MEP who is rapporteur for the Shareholder Rights Directive, and Pascal Durand, a French Green MEP, would compel all member states to introduce similar measures.

Peter Montagnon, formerly with the ABI and now associate director at the **Institute of Business Ethics**, criticised the resolutions, saying "extra voting rights for a core of long-term shareholders tend to entrench management and make them less open to challenge. Compelling listed companies to introduce voting distortions neither they nor their shareholders want it is an assault on contractual freedom." Mr Cofferati's amendment would impose a minimum two-year qualifying period for investors to be considered long term, while Mr Durand's has a five-year minimum.

UK 125th of 152 in money laundering league

Finland's financial system is the least likely to be used for money laundering or funding terrorism, claims a report by the non-profit Basel Institute on Governance. Next cleanest are Estonia, Slovenia and Lithuania, based on the Institute's review of 152 countries' financial regulations, corruption, political disclosures and rule of law. Iran and Afghanistan are rated the worst at stopping money laundering; among European economies, Greece ranks 75th, Switzerland 88th, Germany 89th, Italy 98th, Spain 108th, France 124th and the UK 125th. Report can be accessed at: http://bit.ly/1hKtTSi

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

Esop Centre - IoD 2015: Employee share schemes for SMEs

September 3 @ 9:00 am - 5:00pm

The Centre’s next joint share schemes conference with the **Institute of Directors** takes place on **Thursday September 3** at the Pall Mall HQ of the IoD.

The programme will focus on SME companies and will attract owners, ceos, directors, fds, HR specialists and other key decision makers in such companies. Speakers from Centre member firms will help the SME attendees decide whether to introduce an employee share scheme or to deepen existing employee share ownership in their business. Confirmed speakers are: **Colin Kendon,** Bird & Bird**;** **David Craddock**, David Craddock Consultancy Services; **Mike Gearing**, Fieldfisher; **Steve Thomas**, HMRC Shares and Assets Valuation; **Mike Landon**, MM & K; **Graham Muir,** Nabarro; **Nigel Mason**, RM2 Partnership; **David Pett** and **Stephen Woodhouse**, Pett Franklin & Co**.; Robert Head,** formerly of Pearson; **Jeremy Mindell**, Primondell.

For further details on the presentations and speaker biographies please visit the event page at http://tinyurl.com/nfc2zha

Delegate prices:
Centre/IoD members: £360 + VAT
Non members: £460 + VAT
If you are a Centre member, contact the IoD events team at events@iod.com or +44 (0)207 766 8919 to register at member prices.

If you are a non-member or IoD member you can register to attend this conference through the IoD website:
http://tinyurl.com/qx5c9qj

For all enquiries, contact Jacob Boult at Esop Centre HQ – email: jboult@esopcentre.com or phone him at +44 (0) 20 7239 4971.

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