

Insight: Global equity-based compensation

November 2009

NASPP Special

Prospectus update

At the beginning of this year, we published an Insight which set out proposed changes by the European Commission (“**EC**”) to the Prospectus Directive. If adopted, as originally drafted, these changes would have meant that all employers, whether listed or unlisted, and whether incorporated in the European Union (“**EU**”) or elsewhere, would be able to operate their global equity based compensation plans for their employees in the EU with complete certainty that they would not have to file a prospectus. The proposals have now been changed so that the extended exemption would not cover private companies, public companies listed on an EEA market that is not a regulated market (eg AIM), or companies listed on markets outside the EEA that are not considered to have equivalent standards.

The EC published on 24 September 2009 a further proposal for the review of the Prospectus Directive. This proposal is the culmination of an extensive and continuous dialogue and consultation with all major stakeholders concerned with the application of the Prospectus Directive, including securities regulators, market participants and investors. It also takes into account the findings of the consultation conducted from 9 January to 10 March 2009 and, insofar as employee share plans are concerned, there were no changes to the original suggestions which we commented on at the beginning of this year. Under the 21 September proposal, it remained the intention that the existing employee share plan exemption set out in Article 4(1)(e) of the Prospectus Directive will be widened to cover the employee share plans of companies that are not listed on a regulated market in the EU. However, on 21 October 2009, the Council of the European Union published a revised proposal directive to amend the Prospectus Directive. Under these proposed amendments, the exemption will be widened only to cover offers of securities made to employees of companies with securities listed on markets outside the EEA which have standards equivalent to those which apply within the EU.

We are aware that other advisers have suggested that a separate “mini” prospectus, along the lines of the short form prospectus currently available to non-EU listed companies as an interim measure, may still be required. The EU proposals carry no such intention. Rather, the existing obligation on EU listed entities to make available a document containing information on the number and nature of securities and the reason for and details of the offer will continue to apply. In practice, this obligation is very easily addressed by including relevant wording in the standard form employee communications.

We expect that the implementation measures at directive level will be completed shortly after the New Year, although EU member states will then have a period of time (a year is likely) to incorporate the amendment into local law.

This publication is prepared for the general information of our clients and other interested persons. It is not, and does not attempt to be, comprehensive in nature. Due to the general nature of its content, it should not be regarded as legal advice.



Our global equity-based compensation practice is a key part of the Global Executive Compensation Benefits and Employment Law group which numbers more than 100 lawyers worldwide. We offer extensive expertise in dealing with the key issues involved in operating international equity-based compensation plans. Our work includes:

- implementing global employee stock plans
- advising companies on the effects of major M&A transactions on their equity incentive plans
- implementing equity incentive plans for companies preparing for an IPO
- establishing offshore trusts for the benefit of employees
- implementing global profit-sharing plans

In This Issue...

- Prospectus update
- Global executive remuneration developments
- China - favourable tax treatment for equity awards



Global executive remuneration developments

Executive remuneration has been subject to global critique and analysis as a result of the 2008/09 financial crisis, the worldwide cost of which was estimated by the IMF in August 2009 to be around £7.1 trillion.

In an effort to promote a global approach to curbing remuneration excesses, German Chancellor Angela Merkel and French President Nicolas Sarkozy proposed caps and taxes on bonuses at the Pittsburgh G20 meeting in September 2009. While it is evident from various commentaries that not everyone is convinced that bonus caps are the best approach, the G20 members endorsed the Financial Stability Board's recommendations for remuneration policy at large financial institutions. These included:

- an annual report on remuneration, outlining the decision-making process for remuneration policy;
- disclosure of remuneration for senior executives and employees whose actions have a material impact on the risk exposure of the firm;
- disclosure of assessment of performance measures, the link between pay and performance, deferral policy and criteria for vesting of share awards;
- disclosure of the methodology for the ratio of shares to cash remuneration;
- disclosure of any sign-on and severance payments;
- a substantial proportion of any bonus – generally regarded as between 40 to 60 per cent. – to be deferred for not less than three years;
- more than 50 per cent. of any bonus to be awarded in shares or share-linked instruments, and this proportion to increase incrementally for the most senior members of staff;
- a ban on guaranteed bonuses;
- powers of claw-back of bonuses where a firm performs badly;
- ability to restructure remuneration in a manner aligned with sound risk management and long-term growth; and
- remedial action and corrective measures for non-compliance.

Some countries have already been proactive in introducing restrictions on remuneration. Dutch banks agreed on 10 September 2009 to limit executive board members' bonuses to a maximum of 100% of their salaries. While this is currently a voluntary measure introduced by the Dutch banks, it is expected that it will be introduced into Dutch law in due course.

In the US, The Conference Board, a business lobby group, convened a Task Force on Executive Compensation (the "Task Force"), which released its recommendations on 21 September 2009. Robert E. Denham and Rajiv L. Gupta, co-chairs of the Task Force, stated that the recommendations were an "important step in restoring the damaged trust in American companies". Recommendations made included the establishment of clear links between pay, strategy and performance, and the elimination of compensation practices that might be perceived as unfair, including "golden parachutes" and "golden coffins".

In Australia, the Productivity Commission released on 30 September 2009 its Discussion Draft on Executive Remuneration. Included in its recommendations is the barring of executives from sitting on remuneration committees and a strengthening of shareholders' powers in relation to board remuneration, including the potential for boards to face re-election if they ignore shareholders' concerns on consecutive remuneration reports.

Meanwhile, in the UK, Gordon Brown announced on 27 September 2009 his intention to introduce the Business and Financial Services Act into Parliament during the ensuing weeks. This legislation will seek to end automatic annual bonuses, and empower the FSA to intercede if it considers a bank to be undertaking excessively risky practices. In support of these proposals, on 1 October 2009, the UK's "big five" banks (RBS, Lloyds, HSBC, Barclays and Standard Chartered) announced that they have committed to apply the recommendations endorsed at the G20 summit in Pittsburgh to their remuneration policies with effect from 1 January 2010.

In general, the proposals being made to restrict executive compensation are still in the consultation or planning phase. However, changes in regulation appear to be inevitable. We will continue to update you on future developments.

China - favourable tax treatment for equity awards

Cai Shui [2005] No. 35 ("**Circular 35**") is specifically designed to cover stock option plans and provides for the availability of a preferential regime for income tax arising under such plans. Under this regime, the proceeds derived from the exercise of stock options can be taxed separately from monthly salary income and therefore a lower marginal tax may apply to the equity based gains.

In accordance with supplementary tax circulars issued so far this year (the latest being on 24 August 2009 - Circular 461), the provisions of Circular 35 are now understood to apply expressly to stock appreciation rights and restricted stock units.

However, Circular 461 also makes it clear that specific registration requirements with the local tax bureau ("**LTB**") must be complied with if the favourable treatment is to apply. If these registration requirements are not met, any income related to the equity based awards will be taxed together with the participant's salary income for that month. This means that participants will potentially be taxed at a higher marginal tax bracket on the total proceeds.

In order to comply with these registration obligations, it appears that the local subsidiary of an overseas listed company is required to submit a copy of the relevant rules to the LTB at the time the plan is introduced. Other documents may also be required although we do not believe that the obligation should prove to be too onerous. Please note that this registration obligation should not be confused with SAFE filings. If you are considering taking advantage of the preferential tax treatment afforded by Circular 35 then further consideration may also need to be given to possible filings under SAFE.

STOP PRESS!

Australian Tax Bill Introduced into the House of Representatives

On 21 October 2009, the Australian government introduced its Tax (TFN Withholding Tax (ESS)) Bill 2009 (the "**Bill**").

Senator the Hon Nick Sherry outlined in a press release on the same date some of the changes made to the content of the Bill and its explanatory materials (as compared with the proposals previously announced). These include:

- widening provisions to ensure that a refund will not be denied when employee share scheme benefits are forfeited upon leaving employment;
- the provision of additional guidance and examples of the real risk of forfeiture test;
- clearer transitional arrangements for shares and rights acquired prior to 1 July 2009;
- the adjustment of salary sacrifice provisions in order to facilitate the offering of complex schemes which include both shares or rights with a real risk of forfeiture, and salary sacrifice arrangements;
- the exemption of employee share trusts from capital gains tax over shares acquired to satisfy the exercise of rights provided under an employee share scheme; and
- the amendment of some of the tests to facilitate compliance with the rules.

We shall keep you updated on any future developments.

For more information please contact:



Nicholas Greenacre Partner

Tel: + 44 20 7532 2141

E-mail: ngreenacre@whitecase.com



Ken Raskin Partner

Tel: + 1 212 819 8508

E-mail: kraskin@whitecase.com



Euan Fergusson Senior Associate

Tel: + 44 20 7532 2122

E-mail: efergusson@whitecase.com



Mark Hamilton Counsel

Tel: + 1 212 819 8262

E-mail: mhamilton@whitecase.com

Worldwide. For Our Clients.

36 Offices. 25 Countries.

London

White & Case LLP
5 Old Broad Street
London EC2N 1DW
Tel: + 44 20 7532 1000
Fax: + 44 20 7532 1001

New York

White & Case LLP
1155 Avenue of the Americas
New York, New York
10036-2787
Tel: + 1 212 819 8200
Fax: + 1 212 354 8113

www.whitecase.com

In this publication, White & Case means the international legal practice comprising White & Case LLP, a New York State registered limited liability partnership, White & Case LLP, a limited liability partnership incorporated under English law and all other affiliated partnerships, corporations and undertakings.