global peRSpectives

A QUARTERLY LOOK AT INCENTIVE AND COMPENSATION ISSUES AROUND THE WORLD – WINTER 2012, Vol. II, No. 1

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ISS ISSUES FINAL POLICIES FOR 2012

On November 17, 2011, Institutional Shareholder Services Inc. ("ISS") issued its final U.S. Corporate Governance Policy for 2012. The policy includes changes from the ISS 2011 policy, which may affect ISS's recommendations with respect to say-on-pay votes on executive compensation, and the election of directors of public companies. The following analysis summarizes the changes made to the ISS policy for executive compensation as they apply to the upcoming 2012 proxy season.

Equity Plans of Newly Public Companies

In the executive summary to its final 2012 policies, ISS stated that equity plans coming to a shareholder vote for the first time after a company's initial public offering will be evaluated under the same guidelines as a standard equity plan, even if no new shares are being requested. ISS will make its recommendation based on evaluation of all aspects of the particular plan, including consideration of total shareholder value transfer, repricing, burn rate (if applicable), and any liberal change-in-control provisions. Other factors, such as pay-for-performance or problematic pay practices as related to say-on-pay, may be considered if deemed appropriate.

In explaining its rationale for this change, ISS stated that it anticipates continuing to support the majority of the equity plans of newly public companies, but that its ultimate recommendation is intended to ensure that any adverse equity plan provisions would not have a more detrimental potential impact on shareholders than the potential loss of the company's tax deductions related to named executive officer grants. The recently proposed regulations under Internal Revenue Code section 162(m), requiring newly public companies to obtain shareholder approval before awarding certain performance-based restricted stock units to named executive officers, will likely increase the impact of the new ISS rule as more plans are presented for shareholder approval.

To view entire *Client Alert*, click here.

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FRENCH GOVERNMENT PUBLISHES 2012 FINANCE ACTS, AMENDED 2011 ACT

Following their adoption by the French Parliament, the Fourth Amended Finance Act for 2011 and the Finance Act for 2012 were published in France's official journal on December 29. The Social Security Finance Act for 2012 was published on December 22. This article focuses on the notable tax aspects of these three bills.

Individuals

Income Tax – The income tax brackets remain unchanged: that is, between 0 percent and 41 percent.

Surcharge Contribution for High-Income Earners – A 3 percent surcharge contribution applies to the portion of income between €250,000 and €500,000 for a single person, and between €500,000 and €1 million for a couple. For income exceeding €500,000 for a single person or €1 million for a couple, the surtax is 4 percent. The contribution applies to income from 2011 and will continue to apply until the tax year during which the public deficit disappears.

Passive Capital Income

Withholding Taxes on Dividends and Interest – The following changes will apply to the final withholding tax, the prélèvement forfaitaire libératoire (PFL):

- The withholding tax rate applicable to dividends is increased from 19 percent to 21 percent
- The standard withholding tax rate payable on income distributed to nonresidents is increased from 25 percent to 30 percent (when no tax treaty applies)
- The reduced rate for dividends and similar distributions received by individuals who are tax resident in an EU country, Iceland, Norway, or Liechtenstein is increased from 19 percent to 21 percent
- The increased rate for income paid in a noncooperative state or territory is increased from 50 percent to 55 percent
- The rate of withholding tax applicable to interest on fixed income investment is increased from 19 percent to 24 percent, but the rate remains 50 percent for interest paid in a noncooperative state or territory when the debtor is established in France

These changes apply to income received on or after January 1, 2012.

Specific Regime for SIICs and SPPICAVs – Dividends paid to individuals by SIICs (listed real estate investment companies) and SPPICAVs (real estate companies with variable capital) will no longer benefit from a 40 percent deduction and cannot benefit from the PFL. Also, related shares will no longer be eligible for a shares saving-plan (plan d'épargne en actions, or PEA). This measure came into force October 21, 2011, but SIIC titles that were already in a PEA up to that date may remain, and their owners may continue to benefit from the specific exemptions applicable to securities lodged in a PEA.

Capital Gains

Sale of Securities – The measure planned for 2012 that would have exempted some capital gains on securities after an eight-year holding period has been replaced by a general mechanism for tax deferral, subject to the following conditions:

- The owner and some members of his family must have held at least 10 percent of the securities, directly or indirectly, continuously for a period of eight years from January 1 of the acquisition year
- The company must be liable for corporation tax, have an activity other than portfolio management or real estate management, and be located in the European Union
- At least 80 percent of the proceeds from the sale of shares or rights must be invested, within 36 months, in the cash subscription to the initial capital or an

(continued on page 4, middle)

UK: SPOTLIGHT INCREASES ON EXECUTIVE PAY

With renewed difficulties for the world economy and numerous austerity measures imposed in the UK, there is little surprise that executive pay continues to remain in the public spotlight here. The increased scrutiny applies in all industry sectors, albeit the greatest intensity remains in the financial services sector.

Public disquiet has increased in the UK following the revelation that, since 1980, top executive pay has increased by 4,000 percent, compared with the average pay by 300 percent. There has been a backlash against what is seen as unfair rewards. Politicians from all of the major parties have joined in, with even the Prime Minister railing against "crony capitalism". Only recently, the CEO of a large multinational bank which is majority-owned by the Government was put under overwhelming pressure before he agreed to turn down a bonus, even though it was to be paid in accordance with the Financial Services Authority Remuneration Code.

It seems that companies can no longer remain compliant purely by ensuring procedural correctness and regulatory compliance; the substance and quantum of executive pay is now up for discussion and challenge.

In November 2011, the High Pay Commission published its final report on executive pay. This report argued that excessive top pay was deeply damaging to the UK and that action was urgently required. Its main recommendations were as follows:

1. Executives should be paid just basic salary with bonuses payable only if "absolutely necessary."
2. Employees should be represented on the Remuneration/Compensation Committee.
3. Companies should publish a fair pay report, including a ratio of the top paid employee against the company median over a three-year period.
4. Shareholders should have a binding vote on compensation arrangements proposed for the next three years.
5. Companies should offer increased disclosure, including the pay of the top 10 employees outside the boardroom (on an anonymous basis).
6. Remuneration/compensation reports should be standardised to enable easy comparison of executive pay.
7. Companies should publish an annual statement disclosing their income distribution, including the ratio between reinvestment, dividends, executive pay and tax.

The Coalition Government appears to be taking many of these recommendations forward. For now, however, this only applies to the recommendations from numbers 4 to 7 above, but things could change. We do not have details yet of how these recommendations will be implemented, and a number of practical and legal issues will affect relevant businesses operating in the UK.

For instance, the binding vote on executive pay could result in significant renegotiation of executive contracts and possible recruitment deadlock. Further, to be effective, clawback provisions will need to be drafted extremely carefully and be explicitly documented in the relevant clauses.

Any company negotiating provisions on variable compensation in respect of a new hire should, if it can, ensure that the provisions are sufficiently flexible to deal with the implementation of the above. But at the same time, companies will need to avoid being and being seen to be uncompetitive.

Remuneration Committees and compensation and benefits teams will need excellent balancing skills to be able to attract the best teams, meet governance and regulatory expectations and requirements, and be compliant with employment and other laws.

– Jeremy Glover

CHINA – IMPACT OF NEW SOCIAL INSURANCE LAW ON EXPATRIATES

The recently adopted Social Insurance Law includes provisions that, if enforced, would require expatriates, non-PRC nationals working in the PRC, and their PRC employers, to pay social insurance tax on the expatriate's compensation. The social insurance contributions cover several benefits including medical insurance, unemployment insurance, pensions, worker's compensation insurance, and maternity insurance. Expatriates are required to pay at the same contribution rates as PRC nationals. The rates vary by region but are payable on approximately 50 percent of the employee's monthly income capped at RMB11,700 (approximately US$1,850). The employee's portion of the tax is about 12 percent and the employer's portion is about 38 percent.

While the Social Insurance Law went into effect on July 1, 2011, it is still unclear how it will be enforced in the different regions. We understand that many regional social insurance agencies have yet to process social insurance payments for expatriates. It also is unclear how expatriates may participate in the different social insurance programs for which the new taxes are intended to support. For example, it is not yet known how an expatriate will receive benefits under a PRC pension or unemployment insurance. Since most expatriates are assigned to work in China on a short-term basis and may not remain in China if not employed, the process for receiving the social insurance benefits is problematic.

We anticipate that more information about the impact of the New Social Insurance Law will be available later this year. We will provide updates as they become available.

– Craig P. Tanner

IRELAND – SOCIAL INSURANCE TAX WITHHOLDING EFFECTIVE JANUARY 1, 2012

The withholding requirement for employee Pay-Related Social Insurance (PRSI) on stock awards went into effect on January 1, 2012. In August of last year, the Irish Minister for Social Protection announced a change in the Irish Revenue's position on PRSI by imposing the employee PRSI tax on all stock-based compensation received after January 1, 2012. The PRSI rate for an employee is 0.9 percent up to €1,443 per week and 4 percent above €1,443 per week. The date upon which the stock awards were granted to the employee is not a factor in determining if the PRSI must be withheld. In a previous announcement, the Minister of Social Protection had stated that employee PRSI tax would be payable only on stock awards granted after January 1, 2011. The PRSI tax is due on all types of stock awards, including options, RSUs, restricted stock and purchase rights. There is no employer PRSI for stock-based compensation.

– Craig P. Tanner

Tanner to Speak at E*TRADE 2012 Conference

Craig Tanner, along with speakers from Intel Corporation and McAfee, will discuss the objectives and challenges of post-merger integration for Intel Corporation in "Post-Merger Integration in the Modern Age – Maintaining the Acquired Company's Autonomy."

Intel recently acquired Wind River and McAfee. Through the post-merger integration, Intel focused on keeping the equity compensation programs autonomous. In doing so, both entities continued with E*TRADE as its broker while Intel worked with a different broker. Both entities also maintained their award practices that were in place pre-merger. The conference runs May 7–10 in Las Vegas.

French Government Publishes 2012 Finance Acts, Amended 2011 Act—continued from page 2

increase in capital of a company (the securities received in exchange for the cash contribution must represent at least a 5 percent stake in that company)

- Neither the taxpayer nor members of his family may have been a shareholder of the company before the capital contribution, and they could not be members of the top management during the five-year holding period

In addition, to benefit from a definitive capital gains tax exemption, the shares received in exchange must be kept for at least five years.

The tax deferral must be specifically requested and cannot be combined with other tax benefits (income tax or wealth tax reduction).

Sale of Residential Property Other Than Main Home – Capital gains realized on the first sale of a residential property are now exempted if the seller does not own a main home and applies the product of the sale to the acquisition (purchase or construction) of a principal residence within 24 months of the sale. The seller must not have owned a principal residence during the past four years.

This exemption applies to capital gains arising on disposals made on or after February 1, 2012.

Exit Tax – The First Amended Finance Law of 2011, dated July 6, 2011, created an exit tax for taxpayers transferring their tax residence abroad, holding a direct or indirect participation in excess of 1 percent in the profits of a company subject to corporation tax, or holding a value of at least €1.3 million. This threshold was determined for each stake in a company.

The new provision extends the application of this threshold to all the shares held by a taxpayer, rather than to each stake.

Tax Benefits

For 2012 income, the tax benefits available from tax reduction regimes or tax credits are reduced by 15 percent. From January 1, 2012, the global ceiling for tax benefits is reduced to €18,000 plus 4 percent of the taxable income (from €18,000 plus 6 percent).

Real Estate Investment

The tax reduction available under the Scellier regime for fully refurbished and restored homes (performed by the seller before the acquisition) will now be reserved exclusively for BBC standard homes. A new ceiling per square meter (depending on the location of the property) now applies to the cost price taken into account for the tax reduction.

As part of the 15 percent tax niche reduction, the tax reduction is decreased to 13 percent for BBC housing and to 8 percent for non-BBC housing acquired in 2012, but for which planning permission was granted before December 31, 2011.

Capital Subscriptions in SMEs

The tax reduction can now only be applied to cash subscriptions to the capital of small and medium-size enterprises that have fewer than 50 employees, have an annual turnover or balance sheet value below €10 million, and were created within the past five years and are in their start-up phase.

Tax on High Rents of Small Housing

A tax on rental income from housing that is smaller than 13 square meters in size and located where there is an imbalance between the offer and demand, will apply when the monthly rent exceeds an established amount between €30 and €45 per square meter. The tax rate will be between 10 percent and 40 percent.

The tax applies to rental income received on or after January 1, 2012.

Taxation of High Pensions

From January 1, 2012, a new 21 percent rate applies for annuities above €24,000.

– Sophie Borenstein

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