



Global Regulatory Update

Nicholas Greenacre
4 September 2012

Agenda

- **Overview of Global Regulatory Trends**
- **Global Tax Trends**
- **Securities Laws**
- **Regulatory Intervention**
- **Shareholder Intervention**
- **Data Privacy**

- **Management Incentive Plans in Private Equity**

Overview of Global Regulatory Trends

- **Upward movement of tax rates**
- **General tightening of tax laws / removal of exemptions**
- **Simultaneously, a greater focus on equity-based remuneration as a means of limiting risky behaviour**
- **Regulatory intervention, particularly in financial services**
- **Increased mandatory and voluntary use of clawback and malus**
- **Move towards stricter data privacy**

Global Tax Trends – Increased Tax Rates 1

- **UK**

- additional rate of IT ↑ 50%, 2013/14 ↓45%
- 1% NICs increase (social security)

- **France**

- ‘contribution exceptionnelle sur la fortune’
 - assets over €1.3m
- from 2013
 - 75% marginal rate IT > €1m
 - permanent increases in wealth tax

- **China**

- top tax rate now applies to those earning RMB 80,000 (formerly 100k)

Global Tax Trends – Increased Tax Rates 2

- **USA**

- “Bush tax cuts” set to expire at end of 2012
- election crucial but if Congress does not extend into 2013
 - ordinary IT rates to rise
 - e.g. 25% → 28%, 28% → 31%, 35% → 39.6%
 - long term capital gains to rise
 - headline rate 15% → 20%

Global Tax Trends – General Tightening 1

- **France**

- **reduction of qualifying plan benefits**

- 14% → 30% for employers
 - 2.5% → 10% for employees

- **Ireland**

- removal of approved share options relief
 - application of PRSI and new Universal Social Charge to share schemes

Global Tax Trends – General Tightening 2

- **UK**
 - disguised remuneration
 - although note exemptions for benign use, including employee share plans
 - speculation
 - approved options (CSOP)
 - growth shares
 - joint ownership plans (JSOP)
- **US**
 - **“it’s the carried interest, stupid”**

Global Tax Trends – Increased Disclosure Burden

- **US**

- FATCA

- administrators – requirements for “foreign financial institutions”
 - participants – Form 8938 reporting

- **France**

- new sanctions re Form 3916

- **UK**

- UK/Swiss joint declaration against tax evasion
 - tax treaty signed 6 October 2011, expected to take effect in 2013
 - MPs call for UK-style FATCA

Securities Laws 1

- **Don't panic**
- **Although a few countries regulate enthusiastically**
 - Australia
 - Bahamas
- **A few regulate specifically but share plans generally not the focus**
 - US laws very complex
 - 701
 - blue sky
- **Some countries not hostile, but not geared for them either**
 - Russia
 - foreign securities may not be offered in Russia “in any form or by any means”
 - Chinese gap
 - but cf. SAFE

Securities Laws 2

- **Some simple filings required, e.g.:**
 - Quebec
 - Malaysia
- **Europe**
 - Most share plans not public offers
 - options
 - non-transferable
 - care re Germany and Poland
 - free shares
 - no “diguised consideration”
 - offer < €5m

Securities Laws 3

- **Even where public offer, exemption may well apply**
 - no more than 150 persons in any member state OR
 - securities listed and summary information made available
 - applies to EU listed companies
 - now available to foreign listed companies
 - **but** equivalency statement required, which will take time
- **Prospectus may still be required for**
 - stock purchase plans
 - offered by private companies or companies listed on junior markets
 - or foreign listed companies prior to equivalency statement
 - to more than 150 employees in any member state
 - but interpretative position may be possible

Regulatory Intervention

- **Regulation of financial institutions**
 - Financial Stability Board Principles
 - EU CRD III and CEBS Guidelines
 - implemented differently in different jurisdictions – scope for regulatory arbitrage
 - CRD IV, UCITS V, Fund Managers Directive
- **Mandatory deferral with share component**
- **Clawback and malus**
 - spread outside financial services
 - UK Corporate Governance Code
 - Dodd-Frank Act

Shareholder Intervention

- **Say on Pay**
 - shareholders remuneration vote at annual accounts meeting
 - binding votes in Netherlands (partly), Denmark, Norway, Sweden
 - non-binding (advisory) in Australia, Switzerland, US and UK
 - Germany and Canada also introducing advisory votes
 - UK introducing binding vote on future pay policy
 - Switzerland may switch to binding vote
 - European proposal re binding vote
- **Stricter disclosure requirements to keep shareholders informed**
- **Largely pre-emptive**
 - companies want to avoid shareholder backlash
 - more dialogue with shareholders
 - but signs of increased activism
 - Barclays, Citigroup, AstraZeneca

Data Privacy

- **General theme – becoming stricter**
 - Regulators expecting greater consideration of data protection and privacy when setting up plans
- **EU Data Protection Directive**
 - 25 January 2012 – EU Commission released draft European Data Protection Regulation that will supersede the Data Protection Directive
 - Key changes proposed by the EU Commission include:
 - users will have right to demand that data about them be deleted if there are no "legitimate grounds" for it to be kept
 - companies with 250 or more employees will have to appoint a data protection officer.
- **New US bills providing for general EU style data protection and privacy umbrella**

Management Incentive Plans in Private Equity

- **Key Features**
- **Pressure Points**
- **Tax Issues**

MIPs in Private Equity – Key Features (1)

- **Sweet equity**
 - Special class or classes of share
 - in some countries, profit participation rights or similar securities
- **Issued at top Holdco level alongside PE house shares**
- **5-10% of total equity common as “management pool”**
- **Acquisition funded (or part-funded) by managers**
 - “skin in the game”
- **Shares restricted**
 - not transferable until vesting
 - forfeited on termination of employment as “bad leaver”
 - limited or no voting rights

MIPs in Private Equity – Key Features (2)

- **Shares may be held by nominee to enforce restrictions**
 - Employee trust common, especially for UK and Ireland
 - Dutch foundation (Stichtung / STAK) may be used for Dutch holdcos
- **Vesting**
 - full vesting on Exit (IPO or Sale)
 - time vesting for early leavers
- **Liquidity arrangements**
 - Tag-along and drag-along (for Exit)
 - Orderly market provisions may restrict sale following IPO
 - Put and call options (applies to leavers)
 - employee trust / stichtung
 - PE house

MIPs in Private Equity – Key Features (3)

- **Fixed returns on Exit geared to performance measures**
 - principally IRR / ROE
 - management multiple increases with PE House multiple
 - perhaps some element of earnings
- **Ratchet alternatives**
 - downward – start with maximum entitlement and cancel shares to achieve desired balance of returns for managers and PE House
 - upward – “growth shares” – entitlement increases in line with performance

MIPs in Private Equity – Pressure Points (1)

- **Leaver provisions**

- Bad leavers typically bought out at cost
- Good leavers typically bought out at fair value
- But who is good and who is bad?
 - Common PE House position
 - Good = injury, disability, death, sale of business, [retirement, redundancy]
 - Bad = everyone else, unless we decide
 - Common Management position
 - Good = all of the above and termination without Cause
 - Bad = voluntary resignation and termination for Cause

MIPs in Private Equity – Pressure Points (2)

- **Multiples**
 - commercial discussion
- **Dilution**
 - will managers be entitled to further shares / rights on further rounds?
- **Existing incentive plans**
 - managers may have outstanding shares / options / other rights
 - rights may be triggered by PE House acquisition
 - common to require rollover / pay-out to be re-invested in sweet equity

MIPs in Private Equity – Tax issues

- **Overall aim to achieve capital (not income) taxation at Exit**
 - UK CGT 28%, IT up to 50% + social security
 - Irish CGT 25%, IT up to 41% + social security
- **IT may be due on excess of fair value over purchase price (if any)**
 - accurate up-front valuation essential
 - funding may be required for payment of fair value or tax on fair value
 - reinvestment of proceeds from previous incentive plans
 - loan, but consider financial assistance rules and tax issues
- **Shares may need to carry voting and dividend rights**

Worldwide. For Our Clients.

whitecase.com

Nicholas Greenacre

Partner

Telephone: + 44 20 7532 2141

ngreenacre@whitecase.com