

Legal Alert

December 2010

Speedread:

- New legislation comes into effect on 1 January 2011
- The rules will cover a wide range of credit and investment institutions
- New remuneration principles apply to senior management and other employees
- The legislation allows even claw back arrangement, ie the arrangement for repayment of amounts already paid
- New rules should apply on remuneration for 2010 paid in 2011

New rules on bonuses in financial institutions

In July of this year, the European Parliament adopted a Directive amending Directives 2006/48/EC and 2006/49/EC regarding capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies (after this the "Directive"). The Council of the European Union adopted the Directive in October. This leads to an increase in capital requirements for securitisation and resecuritisation exposures and to establishing rules governing the amount and method of rewarding employees of certain credit and investment institutions.

The new remuneration principles will apply to banks, savings and credit cooperatives and securities dealers (after this the "obliged persons"). In these institutions, the new principles will apply to the remuneration of:

- senior management;
- employees whose activities are connected with the risks undertaken by the obliged person;
- all other employees whose way of remuneration is similar to the remuneration of the above mentioned employees;
- members of statutory or supervisory bodies;
- employees in oversight functions.

In accordance with the new rules, at least 40% of the variable remuneration of the respective employees will be deferred over a period of three to five years. In case of a variable remuneration component of a particularly high amount at least 60% of the amount will be deferred.

In addition, a substantial portion, which is at least 50% of the variable remuneration, must consist of shares or equivalent ownership interests subject to the legal structure of the obliged person, of share-linked instruments or other equivalent non-cash instruments. This applies to both the deferred and the non-deferred parts.

In order to establish closer ties between the remuneration and the risks which the obliged person undergoes, the Directive introduces special instruments – the so called malus and the so called claw back. The malus constitutes an additional condition for the admission of the claim for variable remuneration (eg the financial performance of the institution or of the subdivision of the institution or the abidance of the employee in relation to the obliged person). On the basis of this condition, the obliged person is allowed to grant variable remuneration only in part or not at all. The claw back entitles the obliged person to provide a deduction or demand the employee pay back even such variable remuneration already awarded. This should come into question eg when the variable remuneration was calculated on the basis of wrong data. According to explicit specification in the Directive, the claw back should be used within the limits set by



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mandatory provisions of other legal regulations (eg the Labour Code).

Member states have to ensure that obliged persons apply the new rules on remuneration awarded or paid after the effective date of the Directive, as well as on the basis of agreements entered into before this date, and on remuneration awarded, but not paid, before the date of the Directive becoming effective for services provided in the year 2010.

New remuneration principles should be implemented in the legal system of the Czech Republic in order to become effective on 1 January 2011, which requires changing Czech National Bank decree no. 123/2007 Coll., on prudential rules for banks, savings and credit cooperatives and securities dealers. The Czech National Bank is currently also preparing an official information regarding the new remuneration requirements.

Subjects covered by the new principles should therefore consider adjusting how they remunerate their employees and other affected persons in order to reflect the new legislation.

Speedread:

- Three new all-European authorities are going to be established and equipped with extensive powers
- Beside these, a special board will be created to monitor the macroeconomic stability of the financial sector across the EU
- The new authorities will have a supervisory, not a consultative nature and will be empowered to intervene directly in the rights and obligations of respective subjects in exceptional cases
- The new authorities will come into existence on 1 January 2011

European System of Financial Supervisors

The existing European Union consultative institutions, the Committee of European Banking Supervisors (CEBS), the Committee of European Securities Regulators (CESR) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) will be replaced next year by the newly established supervisory authorities. Namely, these authorities will be the European Banking Authority (after this the "EBA") supervising the European banking sector, the European Securities and Markets Authority (after this the "ESMA") supervising the securities market and the European Insurance and Occupational Pensions Authority (after this the "EIOPA") supervising institutions providing occupational retirement and insurance undertakings.

Further, the European Systemic Risk Board (after this the "ESRB") will be established as a board responsible for macro-prudential oversight of the financial system within the European Union. The task of the ESRB will be to monitor and assess systemic risk in normal time for the purpose of mitigating the exposure of the system to the risk of failure of systemic components and enhancing the financial system's resilience to shocks. The ESRB should contribute to financial stability and in case of identifying significant systemic risks issue warnings and recommendations for remedial action.

The EBA, ESMA, EIOPA, ESRB, the Joint Committee of the European Supervisory Authorities and the competent or supervisory authorities in the Member States form together the European System of Financial Supervisors (after this the "ESFS").



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In the context of their defined tasks and activities the EBA, ESMA and EIOPA will be:

- drafting regulatory technical standards, which will be formally adopted by means of European regulations or decisions;
- ensuring the uniform and consistent application of European Union legislation (for this purpose, they will be entitled to issue guidelines and recommendations);
- actively facilitating and where necessary coordinating any actions undertaken by the competent national supervisory authorities in emergency situations;
- settling disagreements between competent authorities in cross-border situations.

The relevant regulations define when it will be possible to adopt an individual decision addressed to a financial institution (or, as the case may be, to a financial market participant) in a particular case. The authorities will be permitted to do so, eg when in an emergency situation a competent national authority does not comply with the decision of the authority within the period laid down therein and where an urgent remedy is necessary to restore the orderly functioning and integrity of financial markets or the stability of the whole or part of the financial system in the European Union.

The new authorities will come into existence on 1 January 2011. Therefore, from next year, it will be possible that under exceptional and strictly defined circumstances, financial institutions or financial market participants might be the recipients of individual decisions adopted by a supervisory authority included in the ESFS.

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