

# Employment Legal Alert

## Bonus schemes in 2009

### Areas of Interest

#### EMPLOYMENT

#### UNITED KINGDOM

In the current economic climate, there is growing pressure on employers to review the bonus schemes they operate and, in many cases, to make changes. Earlier this month, the FSA wrote to the CEOs of some of the country's largest banks and building societies, setting out its concerns and recommendations for good practice with regard to remuneration policies. The FSA has made clear that it is not just targeting the boardroom, but all executives who are incentivised through bonuses.

As a result, serious thought is being given to fundamental changes to existing bonus schemes, not just in the banking sector but across all financial and other industries. The intention, in many cases, is to introduce new rules ahead of the next financial year.

Key recommendations from the FSA's recent letter include:

- Bonuses should be calculated by reference to profits, not revenues.
- A major proportion of the bonus should be deferred so that long-term profits can be measured. The deferred element should be assessed by reference to a moving average of results and adjusted accordingly.
- Bonuses should not be paid wholly in cash but in a mixture of cash and other components such as shares or share options.

- Bonus criteria should not just look at financial production but other performance measures, such as risk management skills and adherence to company values.

Many employers have already been considering a move away from short-term incentive arrangements towards longer-term schemes. No matter how strong the calls from the industry regulators and Government, however, wholesale reworking of bonus schemes is not straightforward. In many cases, the scheme will comprise an express contractual entitlement for the employees participating in it, in which case, the scheme rules regarding the ability to make changes will have to be analysed. In other cases, there may be no express scheme rules, but a consistent policy and formula has been operated over many years which may have acquired the status of a contractual right for the employees concerned.

Whatever the position may be regarding an employer's ability to make changes to its incentive scheme, a process of explanation regarding the new scheme will be required. In those cases where employee consent is ultimately required, that explanation process will have to lead into a consultation process. These processes take time and, where the desire is to implement changes in time for the next financial year, initial steps need to be taken now.

The text of the FSA's letter to CEOs earlier this month can be found at [http://www.fsa.gov.uk/pubs/ceo/ceo\\_letter\\_13oct08.pdf](http://www.fsa.gov.uk/pubs/ceo/ceo_letter_13oct08.pdf). We will be monitoring further communications from the FSA and other bodies, and report on developments. In the meantime, should you have any immediate queries on any of the above, please contact the London Employment Group.

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