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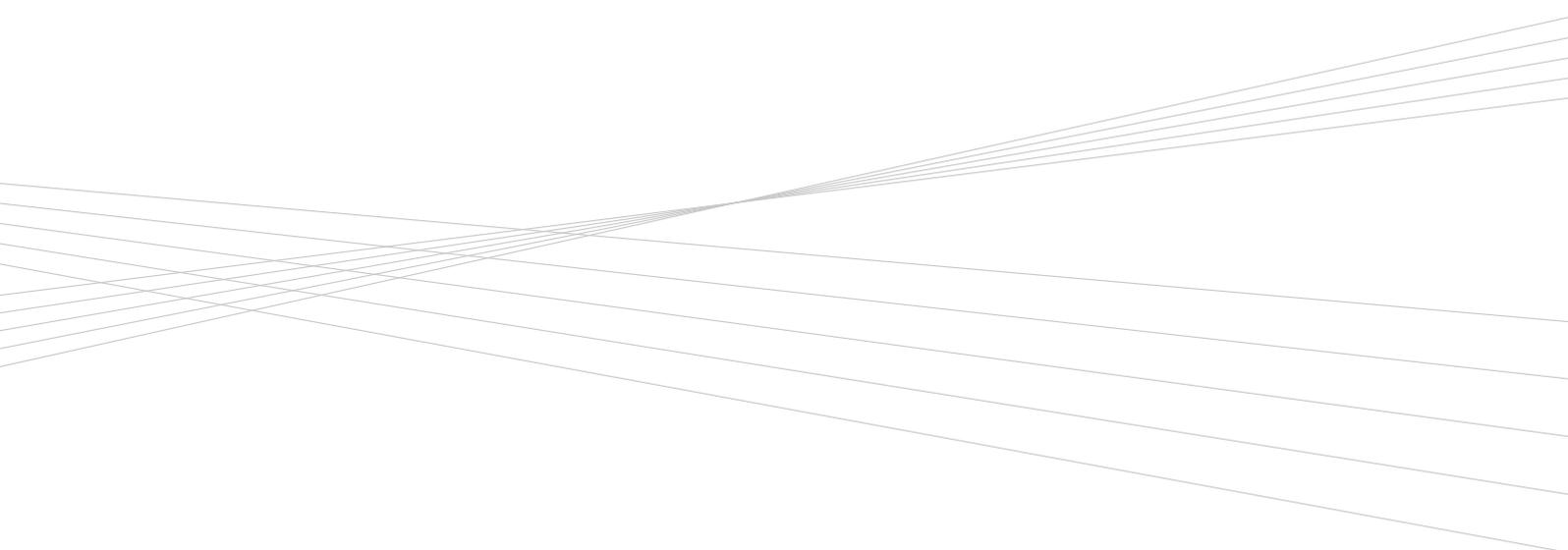
## **Employment Law Newsletter No 6**

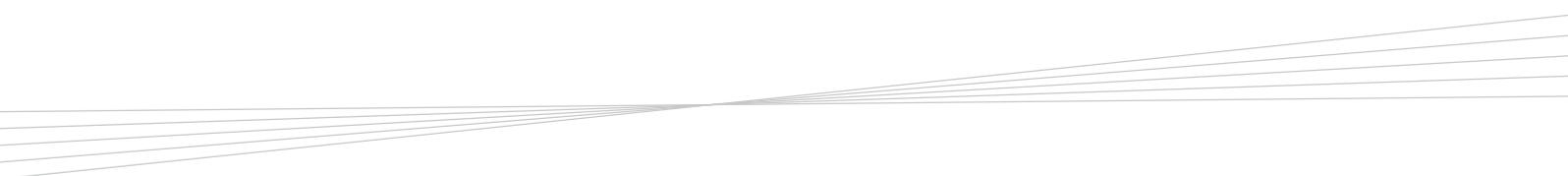
### **EXECUTIVE REMUNERATION IN THE UK AND GERMANY:**

**Similar objectives, different means**

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## Introduction

Executive remuneration has been a hot topic across Europe for a number of years. When the financial crisis hit in 2008, it highlighted the growing gap between executive pay and company performance, as well as the pay of other employees. Another issue was the high proportion of variable compensation payable on fulfilment of short-term objectives which, particularly in the banking sector, worked as an incentive to enter into high-risk business dealings without regard to the company's sustainable economic development.

As a consequence of the 2008 crisis, in 2009, Germany introduced the Appropriate Board Member Remuneration Act (*Gesetz zur Angemessenheit der Vorstandsvergütung – VorstAG*) which is complemented by the German Banking Remuneration Regulation (*Institutsvergütungsverordnung – InstitutsVergV*) providing special rules for the remuneration of board members and other managerial staff of banks and similar institutions, and by the German Insurance Remuneration Regulation (*Versicherungsvergütungsverordnung*) applicable to the insurance sector<sup>1</sup>. These rules are further supplemented by the German Corporate Governance Codex (*Deutscher Corporate Governance Kodex – DCGK*) which sets standards of good practice for German listed companies<sup>2</sup>.

In the UK, the Government has resolved to make significant reforms to the legislation governing executive remuneration. The proposed UK reforms form part of the Enterprise and Regulatory Reform Bill and supporting regulations, and are due to take effect in October this year.

A look at the proposals for reform in the UK and the law in Germany exhibits some interesting contrasts between the two executive remuneration regimes. Although both regimes are designed to curb excessive remuneration and encourage a strong link with corporate performance, the means designed to achieve those objectives differ in a number of respects.

This briefing summarises the key points of contrast between the executive remuneration regimes for listed companies in the UK and Germany, and their practical implications. It also looks ahead to proposed future reforms, including the recent EU-level agreement to cap bankers' annual bonuses.

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<sup>1</sup> Which pursues similar aims as *InstitutsVergV*, but in the interest of brevity, is not discussed further in this briefing.

<sup>2</sup> While the Codex is not a law, it derives its legal force largely through sec. 161 German Stock Corporation Act (*Aktiengesetz*) which requires listed companies to publish an annual declaration stating that they have in all respects adhered to the recommendations contained in the Codex and to state explicitly in which respects they did not.

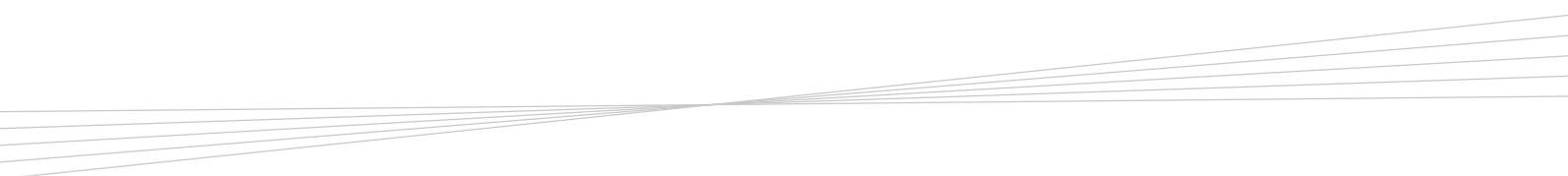
## Shareholder voting

In **the UK**, the current position is that shareholders have no binding power to set the remuneration which is paid to directors of the company. The only exceptions to this principle are (i) the requirement for any new employee share schemes, long-term incentive schemes and discounted option arrangements to be approved by shareholders; and (ii) the need for certain payments for loss of office to be approved by shareholders. In addition, UK companies are required to publish a directors' remuneration report on an annual basis, but the report is subject only to an advisory shareholder vote. This means that there are no legal consequences if the vote is not passed. In practice the company may (and often will) choose to make changes so as to appease the shareholders, but it is under no obligation to do so.

However, reforms to shareholder voting rights are proposed as part of the Enterprise and Regulatory Reform Bill. Firstly, shareholders will be given a binding vote on the policy section of the remuneration report. If a company fails the binding vote, it will have to continue using the last policy that was approved, until a new policy passes the binding vote. The new binding vote will be required at the annual general meeting (AGM) held in the first financial year which begins after the new regime comes into force (expected to be in October 2013). Further votes will then be required at least every three years, and at the next AGM following a failed advisory vote on the implementation section of the remuneration report, or any amendment to the remuneration policy.

The second element of the new regime is that a listed company will be prohibited from making any remuneration payment to a director (current, former or proposed) unless either (i) the payment is consistent with the most recent approved remuneration policy; or (ii) the payment is specifically approved by shareholders. The same applies to any payment for loss of office to a director or former director. "Remuneration payment" and "payment for loss of office" are defined fairly broadly for these purposes, to catch both contractual and non-contractual payments and benefits.

Under **German** law, the situation is quite different. As a matter of background, it is necessary to know that German stock companies (*Aktiengesellschaften*), in contrast to UK companies, have a two-tier board structure consisting of (i) an executive board responsible for the management of the company and (ii) a supervisory board that has the task of overseeing the management. In smaller stock companies, the supervisory board is usually staffed with shareholder representatives only, while for companies having 500 or more employees, employee representatives on the supervisory board are mandatory.



By law (sec. 87 German Stock Corporation Act (*Aktiengesetz – AktG*)), it is the supervisory board that is responsible for deciding on executive board member remuneration. However, pursuant to sec. 120 para. 4 AktG, the AGM (*Hauptversammlung*) of a stock corporation can take a vote of disapproval on the remuneration system for members of its executive board. While the vote has no legal consequences, it is intended that the mere possibility of such a vote will encourage the supervisory board to be particularly diligent in taking decisions on executive remuneration. The introduction of the vote was criticized by workers' unions who wanted to leave the full decision on executive remuneration with the supervisory board, arguing that (i) this would allow employee representatives on the supervisory board to have a say in executive remuneration; and (ii) that by giving the shareholders' meeting a vote, the role of the supervisory board would be weakened, and this would give additional power to institutional investors whose influence, in their eyes, was at the root of the financial crisis.

A proposal to give shareholders a binding vote on executive remuneration was considered in the making of VorstAG in Germany, but rejected for similar reasons as those just described. No special rules apply to banks in this regard. However, in the current political debate, the introduction of a shareholder vote on executive remuneration is a prominent demand – and once again is lobbied against by labour unions fearing the loss of influence of the employee representatives on supervisory boards in favour of institutional investors.

### **Comparison with peers**

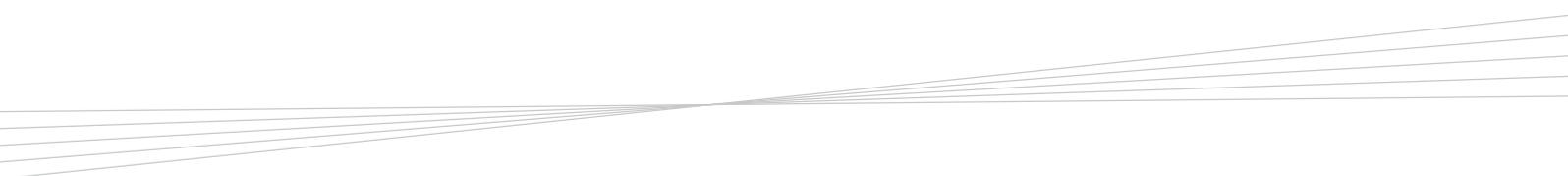
In **the UK**, there is no legal requirement to benchmark executive remuneration against the company's peers, or to disclose whether such comparison has been made. This remains the position under the proposed new reforms. However, institutional investors such as the Association of British Insurers (ABI) recommend that this benchmarking takes place, and is disclosed in the remuneration report. The ABI recommends that if benchmarking is used, the aim should not solely be to match the "median" pay amongst peers, but to provide a point of reference for determining the appropriate salary for the specific job. The National Association of Pension Funds (NAPF) takes a more negative approach to peer group benchmarking, and encourages companies to instead take a more individual approach to setting executive remuneration. In practice, most UK listed companies seek to position their executive remuneration packages in the upper quartile by peer comparison; a practice that has contributed to a ratchet effect to increase executive remuneration year on year.



In **Germany**, the position is quite different. As a rule, executive remuneration may not exceed the remuneration “customarily paid” (*i.e.* by companies in the same trade, of similar size and within Germany) unless there are special reasons for doing so. This is one of the few real novelties incorporated into sec. 87 AktG by the VorstAG-reforms in 2009. The predecessor version of sec. 87 AktG already required that executive remuneration (which included benefits) be adequate in relation to the tasks and performance of the relevant board member and to the economic situation of the company, and allowed the reduction of such remuneration if there was a material deterioration of the company’s economic situation. Under the revised version of sec. 87 AktG, members of the supervisory board must now justify and document the reasons for any decision to award executive remuneration exceeding the remuneration customarily paid, to avoid claims against them by the company. However, the impact of this rule on levels of executive remuneration does not reveal a clear pattern. A recent survey of companies listed in the German stock index DAX has found that between 2001 and 2011, executive remuneration of DAX listed companies rose by 151%. While between 2008 and 2009, executive remuneration fell by an average of 20%, it increased by 22% the following year, and by 7.9% between 2010 and 2011. For 2011/2012, the numbers have not yet been made available.

### **Employee involvement**

In **the UK**, there is no requirement for any employee involvement in setting executive remuneration. There is currently a requirement for companies to disclose in their remuneration report how employee pay and conditions were taken into account when determining executive remuneration. In the new regime, it was initially proposed that companies should have an employee representative on their remuneration committees, and that employees should be given a non-binding vote on executive remuneration. However, both proposals proved very unpopular in consultation with businesses, and they were dropped. The new regime will require companies to make a number of additional disclosures in the remuneration report, namely: (i) whether (and why) the remuneration policy for employees is different from the remuneration policy for executives; (ii) whether employees have been consulted in relation to executive remuneration; and (iii) whether comparison metrics have been used in setting executive remuneration.



In **Germany**, pursuant to the explanatory memorandum (*Ausschussbegründung*) of VorstAG, it was intended that board members' remuneration should not be disconnected from the remuneration customarily paid and the wage and salary structure of a company. Consequently, the memorandum states that the wage and salary structure of a stock company can be used as an argument to establish that the remuneration payable to a member of an executive board is customary. However, it was not made a legal requirement to look at the wage and salary structure of employees of the company in defining executive board members' pay as customary within the sense of the German Stock Corporation Act, despite demands to that effect by workers' unions and some legal writers during the legislative procedure (*Gesetzgebungsverfahren*). Further, suggestions to limit executive remuneration to (for example) 150 times the average employee pay were not implemented. However, it has become common practice in German listed companies, that the system, amounts and development of upper level and overall employee pay and benefits are examined by the supervisory board when determining the remuneration of executive board members.

Under draft amendments to the German Corporate Governance Codex (which are likely to be adopted in May 2013), it would become good practice for the supervisory board to take into account the relationship between the individual board member's remuneration and the remuneration of the upper management on the one hand, and the entire staff of the company on the other, in determining whether the remuneration of an executive board member is adequate.

The supervisory board of the company has sole responsibility for determining the executive remuneration package of a stock company (sec. 107 para. 2 phrase 2 AktG). In larger companies, employees are represented on the supervisory board pursuant to the One-Third Participation Act (*Drittelbeteiligungsgesetz* – more than 500 employees) or the German Co-Determination Act (*Mitbestimmungsgesetz* – more than 2,000 employees). Employees will therefore have a role (albeit a limited one) in setting executive remuneration.

In significant banks within the meaning of InstitutsVergV<sup>3</sup>, a remuneration committee (*Vergütungsausschuss*) has to be installed, with members including employees from HR, business generating and controlling divisions. The remuneration committee reports to the management and to the supervisory board on the adequacy of the bank's remuneration system and can be consulted by the chairman of the supervisory board in this context any time.

<sup>3</sup> I.e. banks (i) whose average balance sheet total (*Bilanzsumme*) at the end of each of the preceding three financial years reached or exceeded EUR 10 billion and (ii) which, based on a risk analysis, consider themselves as significant; banks where the three-year average balance sheet total has reached or exceeded EUR 40 billion will as a rule be considered significant (cf. sec. 1 para. 2 of InstitutsVergV).

## Variable remuneration

In **the UK**, variable remuneration forms a key part of the remuneration package for most executives. Outside the financial sector, there are no strict rules governing the amount or structure of variable remuneration, although listed companies are expected to structure a significant proportion of executive remuneration so as to link rewards to long-term corporate and individual performance.

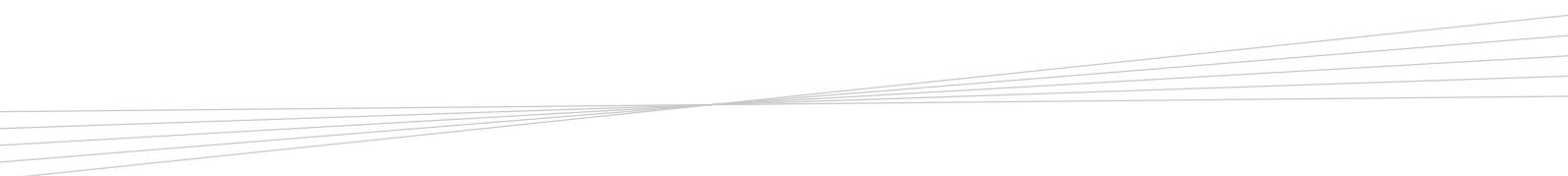
In the financial sector, there is a Remuneration Code which regulates the award of variable remuneration to senior employees<sup>4</sup>. Under the Code:

- Firms must ensure that any variable remuneration is paid only if it is sustainable according to the financial situation of the firm as a whole, and justified according to the performance of the firm, the business unit and the individual concerned.
- Firms cannot pay variable remuneration unless at least 40% of it is deferred over a period of not less than three years to five years.
- When variable compensation is particularly high (typically over £500,000) at least 60% must be deferred.
- At least 50% of any variable remuneration component should be paid in shares, share-linked instruments or equivalent non-cash instruments (in the case of a non-listed firm).
- Firms are required to set appropriate ratios between the fixed and variable components of total remuneration, to ensure that they are appropriately balanced.

In **Germany**, one of the key purposes of the 2009/10 reforms was to align executive remuneration to the objective of sustainable development of the employing entity. The increasing ratio of variable remuneration in relation to fixed compensation, the fact that success factors determining the absolute amount of variable compensation payable were often based on a single financial year, and that clauses negatively impacting an executive's remuneration in case of a negative development of the employing entity were largely unknown in Germany, were found to be at the root of the financial crisis. They were perceived as an invitation to risk-prone dealings, particularly in the banking sector.

While it is sometimes debated whether there is a legal requirement under German law that a portion of the remuneration payable to an executive has to be variable, this is common practice. If variable compensation is paid, the law recommends that it have a

<sup>4</sup> The Remuneration Code was previously enforced by the Financial Services Authority (FSA), which ceased to exist with effect from 1<sup>st</sup> April 2013. The FSA has been replaced by two new regulatory entities who will enforce the Code; the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA).



multi-year assessment basis. The law does not prescribe how this should be attained, although legal writers discuss bonus-malus provisions, clawback clauses, performance reviews encompassing the entire term of a service agreement and payment deferrals. Short-term incentives remain permissible, but the overall focus of incentives must be long-term.

In addition, caps should (*sollen*) be agreed to apply in the event of extraordinary influences on a company's financial results (avoiding windfall profits and high payments in a crisis). These can be in the form of an absolute cap or of a bonus increasing degressively.

Under proposed reforms of the German Corporate Governance Codex (published in February 2013, and likely to be adopted in May 2013), companies should define caps for all individual variable compensation payments and for the total aggregate remuneration payable to an executive board member.

Where variable compensation is paid to board members of banks there are additional requirements, which are very similar to those which apply in the financial sector in the UK. For example, it is required that board members may not be significantly dependent on their variable compensation and that there is an appropriate balance between fixed and variable remuneration components. For board members of significant banks:

- the variable compensation must not be entirely dependent on the success of the bank, and must take into account the individual's stake therein (*Anteil am Erfolg*);
- payment of 60% or more of the variable compensation must be deferred for at least 3-5 years;
- 50% or more of the immediately payable and of the deferred variable compensation must be made subject to the sustainable economic development of the bank, and adequate holding periods must be agreed during which such compensation is not at the disposal of the board member; and
- in the event of negative performance of the individual, of his area of responsibility or of the bank as a whole, the variable compensation payable to him must be reduced.

Similar rules regarding dependency on sustainable development, deferral and reduction apply to the granting of discretionary company pension claims to board members of banks.

## Recovery of payments in breach

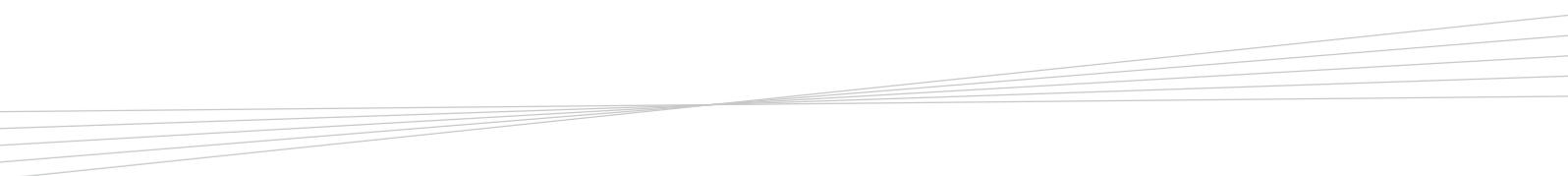
In **the UK**, if a payment is made in breach of the current or prospective new requirements for shareholder approval of remuneration payments, the payment will be held on trust for the company (or other person who paid it). In addition, the directors who approved the payment will be jointly and severally liable to indemnify the company for any loss.

In the financial sector, any payments in breach of the Remuneration Code will be void and recoverable by the company (unless they are made under certain pre-existing provisions). The firm cannot then make any further payment of variable remuneration to that employee unless it has obtained a legal opinion stating that the new payment complies with the Code. The firm must also report the breach to the relevant regulatory authority (the FCA or the PRA).

In **Germany**, members of a supervisory board who authorise the payment of excessive executive remuneration are liable to the company for damages. However, there are difficulties under German law with reclaiming money from former members of the board. Unless the granted remuneration is obviously excessive (which is unlikely, in light of other legal restrictions), the executive board member will usually be able to argue that he relied on the adequacy of the remuneration and that it has been spent. This argument could be avoided by declaring part of the remuneration payments voluntary (*Freiwilligkeitsvorbehalt*) or subject to revocation (*Widerrufsvorbehalt*). However, given the strict requirements for general terms and conditions established by the Federal Labour Court, there usually is a risk that such clauses will be deemed void if brought to court.

## Drafting of clawback clauses

In the UK and Germany, the use of clawback clauses is becoming more and more prevalent, particularly in the financial sectors. 'Clawback' in this sense refers to the ability of the company to recover a payment or benefit which has already vested and been made to the director. It should be contrasted with a 'malus' adjustment, which would apply before the remuneration has actually vested or been paid (with the result that the director never actually receives anything at all).



In **the UK**, there are a number of drafting issues to consider when implementing clawback clauses:

- The clause may be challenged as unenforceable under the penalties doctrine. However, recent case law suggests that such a challenge would be difficult to mount, provided that the payment or benefit is expressly made subject to the clawback condition, and that the amount reclaimed is not in excess of the loss which the company has suffered.
- The clause may be challenged as an unenforceable restraint of trade, if the clawback condition is related to the employee undertaking competitive activity, such as leaving to join a competitor. Although there are strong arguments to suggest that the restraint of trade doctrine would not apply in this scenario, this issue is currently subject to conflicting decisions under UK case law, and much will depend on the individual factual circumstances.
- The director may be able to invoke the ‘change of position’ defence, where he has already disposed in good faith of the amount which the company is seeking to claw back. However, the defence is less likely to succeed where, at the time of receipt, it is made clear to the director (in the contract or otherwise) that he may be required to repay it at some stage in the future.
- Finally, there are tax issues to consider on clawback which may affect the drafting. If the clause is not appropriately drafted, the employee could be taxed on the initial payment but unable to reclaim the tax paid if some or all of the payment is subsequently clawed back.

Under **German** law, a distinction has to be made between the commonly used clawback clauses applicable at termination of a service or employment relationship (which are not at issue here) and clawback clauses aimed at reclaiming (particularly bonus) payments if it turns out after payment that the preconditions for such payment were not met to begin with. This could, for example, be the case if the achievements of an executive which seemed to fulfil his bonus objectives later turn out to be of temporary nature rather than sustainable, or achieved by improper means. Clawback clauses for these purposes will generally be permissible, but have to satisfy the high transparency requirements of German general terms and conditions law. Namely, they will have to clearly state the prerequisites, scope and timeframe for a recovery of bonus payments from the executive board member. Achieving these standards, particularly in defining the circumstances in which payments can be reclaimed in a sufficiently broad and yet concise and understandable manner, will constitute a legal challenge. While precedent

had limited the portion of remuneration which could be rescinded to 25-35% of the aggregate remuneration of an individual, it seems unlikely that these limits will be found to apply to clawback clauses of the kind described here. However, this is disputed among legal writers and there does not seem to be any higher-court precedent on this issue yet.

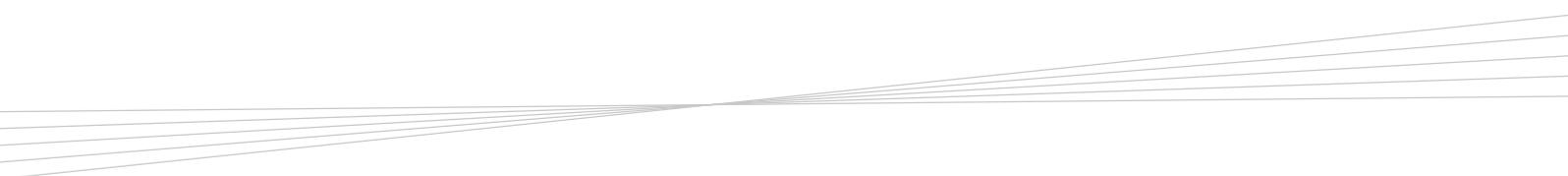
### Single total figure of remuneration

In **the UK**, one of the key elements of the proposed new executive remuneration regime is the requirement for listed companies to disclose in their remuneration report a single total figure of remuneration for each director. This figure should represent the total remuneration earned by each director in the relevant financial year (including salary, taxable benefits, pension-related benefits, bonuses awarded in relation to that year, and long-term incentive plan (LTIP) awards and share options). The calculation which has been proposed for some elements of the single total figure has proven controversial. For example:

- *Pension benefits*: for a defined contribution scheme, the valuation is the cash value of the company's contributions to the scheme in the relevant year. For a defined benefit scheme, the valuation is the additional value of benefits using the 'HMRC method'<sup>5</sup>.
- *LTIPs and share options*: the single total figure is intended to include an amount in respect of LTIP awards and share options which vest in that year. The valuation is the market value of the shares at the date of vesting (less any option exercise price). A significant issue with this approach is that it values the award or option at vesting, rather than on exercise. As the director may not exercise the option when it vests, the value of the option on exercise (when the director actually receives the benefit) may be very different to the value of the option at the point of vesting (when the calculation is carried out).

In the financial sector, firms have additional disclosure obligations. However, firms are only required to disclose the aggregate amounts of remuneration paid to senior employees, broken down into fixed and variable remuneration. There is no requirement to publish a single total figure of remuneration for each employee.

<sup>5</sup> This valuation method places a notional current value on a future benefit at a particular point in time. The value is calculated by applying statutory valuation assumptions that (i) the person becomes entitled to the benefit at the relevant point in time; (ii) there is no reduction in benefits for early payment; and (iii) there is no increase in benefits for ill health. There is some controversy about using the HMRC method, on the basis that it may result in figures which are not comparable between the defined benefit pension schemes of different companies, and/or result in inaccuracies in the figures reported.



In **Germany**, different rules apply to listed companies and banks. A rule requiring listed companies to disclose remuneration by individual board member and the aggregate value of all benefits granted during the financial year in their annual accounts was established in 2005. By the 2009 reforms, this rule was extended to require a statement by individual of all benefits granted in the event of (i) a regular and (ii) an early termination of the service relationship, any changes to those amounts agreed during the relevant financial year, and benefits promised and granted in connection with the termination of a board member during the financial year. Benefits granted in the event of a regular termination must be stated with their net present value (*Barwert*). This can cause difficulty, particularly where pension expectancies are concerned (which as a rule do not have a net present value).

These requirements can be waived by a 75% majority vote of the shareholders at the AGM, in which case, only an aggregate number for the entire board has to be disclosed.

For banks, *InstitutsVergV* requires the annual (or more frequent) publication of the aggregate remuneration of board members and the number of such members on the website of the company. Significant banks additionally have to state the aggregate amounts of the variable compensation payable to board members, including amounts which are dependant on the economic development of the bank, retained and paid out portions of variable compensation and the total aggregate and highest amount of an individual severance payment paid in the relevant year. These requirements are additional to those described for listed companies.

To increase the transparency of and allow comparison between published remuneration information, the proposed 2013 amendments to the German Corporate Governance Codex include the setting of standards by establishing sample reporting tables.



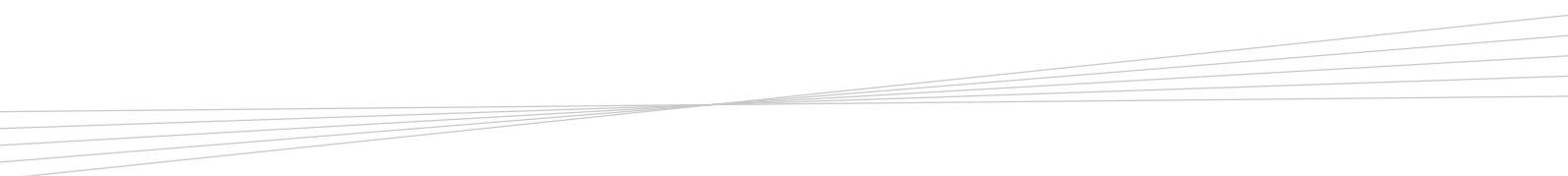
## Future reform

The proposed reforms of executive remuneration in the UK, and to DCGK in Germany, which are outlined in this briefing are expected to take effect later this year. However, there are still more changes on the horizon.

At the end of February 2013 the European Parliament and the Council reached a political agreement on a cap on bankers' annual bonuses which was affirmed by EU member states and the European Parliament in March 2013. Under the agreement, annual bonuses will be capped at a year's base salary. The cap could be increased to twice base salary with the approval of shareholders (requiring the votes of at least 65% of shareholders owning half the shares represented, or of 75% of votes if there is no quorum). In addition, if the cap is increased above a year's base salary, then 25% of the bonus must be deferred for at least five years.

The political agreement must yet be formally adopted by the European Parliament plenary, in which a vote is expected at the 15-18<sup>th</sup> April session (although this is expected to be a formality). Once approved, Member States would need to implement the new rules by 1<sup>st</sup> January 2014 and these will have to be adhered to with respect to bonuses paid from 2015 onwards.

In addition, the German government has initiated a new law which would make institutional and negligent violations of management obligations by board members of banks which lead to a crisis threatening the existence of the bank (*Bestandsgefährdung*) subject to criminal law punishment of up to five years imprisonment. And in March 2013, following a Swiss referendum on the same subject, the German Federal Minister of Justice has launched a draft law which would make AGM decisions on executive remuneration mandatory. As the political pressure on the subject is increasing with German federal elections due in September 2013, we are likely to see further restrictive proposals on executive remuneration soon.



## Conclusions/practical implications

- The proposed reforms in the UK will give shareholders significantly more power to shape executive remuneration. Companies must be prepared to set out their policy on executive remuneration in more detail, and will need to reach agreement with their shareholders on that policy before it can be validly implemented. The position of employees, although secondary, will require greater consideration under the new regime, with peer comparison remaining less important.
- In Germany, the balance of power in setting executive remuneration rests primarily with the supervisory board. Shareholder influence is largely confined to debate and potentially a negative vote at the AGM. Employee influence is limited to (up to 50%) representation on the supervisory board of larger companies. Nonetheless this puts employees in Germany in a better position to influence executive remuneration than their colleagues in the UK. In addition, peer comparison is of key importance in restraining levels of executive pay.
- The granting of variable remuneration is subject to greater legal restrictions in Germany than in the UK, although both jurisdictions have very similar regimes for financial sector companies.
- The mechanism for reclaiming executive pay is also more difficult in Germany, in light of the requirements applicable to general terms and conditions.
- Finally, the reporting in both the UK and Germany of a single total figure may create an impression which is not entirely representative of the remuneration which a director actually receives. In Germany, the proposed amendments to the German Corporate Governance Codex are intended to address this issue. In the UK, it is expected that in many cases additional explanations may be required in order to ensure that shareholders can interpret the single figure. Despite any such explanations, companies must expect that investors (and the press) will focus on the single total figure of remuneration, as it provides a simple headline statement (if not a wholly accurate summary) of the way in which the company rewards its executives.

## Summary

Issue	UK position	German position
Shareholder voting	<p>Currently, advisory vote on remuneration report. No legal consequences of negative vote.</p> <p>Proposal for binding vote on remuneration policy, and on payments which are not consistent with the approved policy.</p>	<p>Advisory vote only on remuneration system for board members. Binding vote was considered but rejected (and now is reconsidered). No legal consequences of negative vote.</p> <p>No binding vote on payments to members of the board.</p>
Comparison with peers	<p>No legal requirement to benchmark pay against peers. However, the ABI recommends that this benchmarking takes place and is disclosed.</p> <p>Most companies seek to position remuneration in upper quartile.</p>	<p>Remuneration may not exceed the remuneration "customarily paid" (i.e. by companies in the same trade, of the same size and within Germany) unless there are special reasons for doing so.</p>
Employee involvement	<p>No requirement for any employee involvement in setting executive remuneration.</p> <p>Proposal for companies to disclose comparisons between executive remuneration and employee pay, and whether employee consultation has taken place on executive pay.</p>	<p>In companies with 500 or more employees, employee representatives on the supervisory board are involved in setting executive remuneration.</p> <p>No strict legal requirement to compare executive pay with employee pay, but comparison routinely forms part of remuneration discussions in supervisory boards.</p>
Variable remuneration	<p>No laws prescribing amount and structure of variable remuneration, except in the financial sector.</p>	<p>No legal requirement to pay variable remuneration, but if it is paid, it should be on a multi-year assessment basis and capped to exclude extraordinary influences.</p> <p>Special restrictive rules for the financial sector.</p>
Recovery of payments in breach	<p>Payments are held on trust by the director for the company. Directors who authorised the payment are also jointly and severally liable to indemnify the company for any loss.</p>	<p>Difficulties with reclaiming money from directors under German law. Members of the supervisory board who authorised payment of excessive remuneration are liable to the company for damages.</p>
Drafting of clawback clauses	<p>Drafting issues include avoiding the penalties doctrine, restraint of trade arguments, change of position defence and tax issues.</p>	<p>Difficulty of drafting legally effective clawback clauses due to general terms and conditions law.</p>
Single total figure of remuneration	<p>Proposal to require reporting of a single total figure of remuneration for each director. Valuation difficulties in practice, particularly for pension benefits and LTIPs/ share options.</p>	<p>Reporting of a figure of remuneration by individual is required unless waived by AGM vote. Valuation difficulties in practice, particularly for pension commitments.</p>

## Further information

If you would like to find out more about any of the issues raised in this briefing, or require advice in relation to a specific matter, please contact:

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