

Moving out of uncertainty*

New trends in equity rewards



Foreward

In a relatively short period of time, equity compensation has moved from the shadows of footnote disclosure, to center stage in both corporate financials and corporate governance. As intense as the focus on equity compensation was during the months preceding the recognition of expense for all forms of equity compensation that scrutiny has continued to intensify in the aftermath of this change in accounting. As shareholders, Board members, corporate executives and employee groups evaluate the impact of equity compensation on the bottom line, a host of issues have come up regarding the relative expense and benefit of each type of equity compensation award. Far from staging the demise of equity compensation, the requirement to recognize and expense all forms of equity awards has freed companies to explore new equity designs, and has increased the number of internal and external stakeholders charged with designing, managing and delivering compensation as a critical aspect of executing a company's business strategy.

Understanding the emerging (and continuing) trends in equity compensation among other multinational companies is essential as companies continue to work through issues related to their overall compensation programs. To this end, PricewaterhouseCoopers ("PwC") is pleased to provide "Moving out of Uncertainty: New Trends in Equity Rewards." This Executive Summary provides a sneak peak of the major findings from PwC's 2006 Global Equity Incentives Survey Report. Our Report is one of the most comprehensive studies available on the design and administration of equity incentive compensation plans for multinational companies.

It is an exceedingly challenging yet interesting time in the world of compensation and benefits. We hope you find the 2006 Global Equity Incentives Survey Executive Summary of assistance as you look to creating the employee incentives that will help your company achieve its business objectives.

Scott Olsen
Principal
Leader, Remuneration Network
Human Resource Services

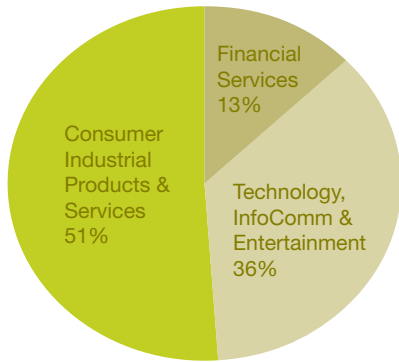
Introduction & methodology

This Executive Summary provides an overview of the trends observed in our 2006 Global Equity Incentives Survey. PricewaterhouseCoopers (“PwC”) has prepared this Summary to illustrate how various companies are handling the ever-developing array of tax, accounting and legal regulations related to strategic human capital issues and how responses have evolved since our last survey.

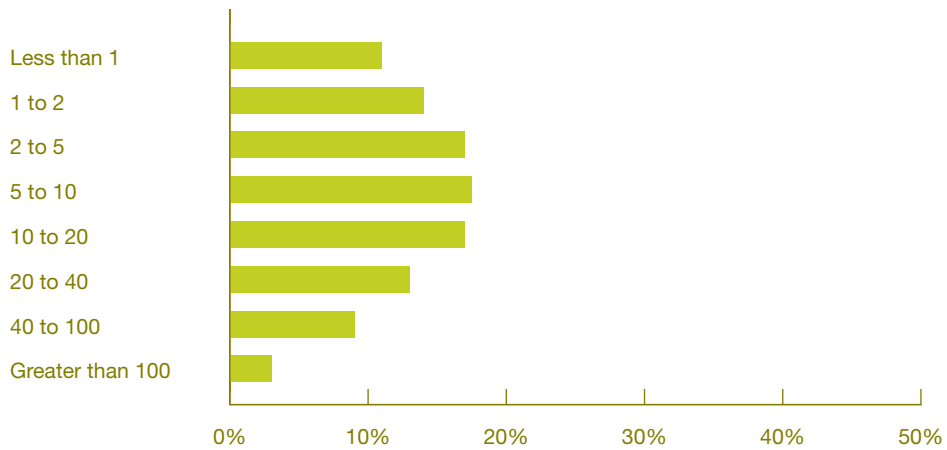
The Survey was conducted in April, 2006. Internet questionnaires were completed by 151 multinational companies headquartered in one of 16 countries worldwide. Our survey requested information on different types of equity plans, such as stock option plans, stock appreciation right plans, restricted stock/unit plans and employee stock purchase plans. We inquired about the design and administration of these plans throughout the world by asking more than 200 multiple choice questions.

We believe the Survey results are statistically significant for publicly held multinationals that offer equity incentive compensation plans to executives and employees in the 38 countries identified on the following pages. The full spectrum of revenues and employee sizes are represented, and at least 13 companies with employees in each country participated. The largest number, 150 companies, have employees in the US. The least, 13 companies, have employees in Uzbekistan.

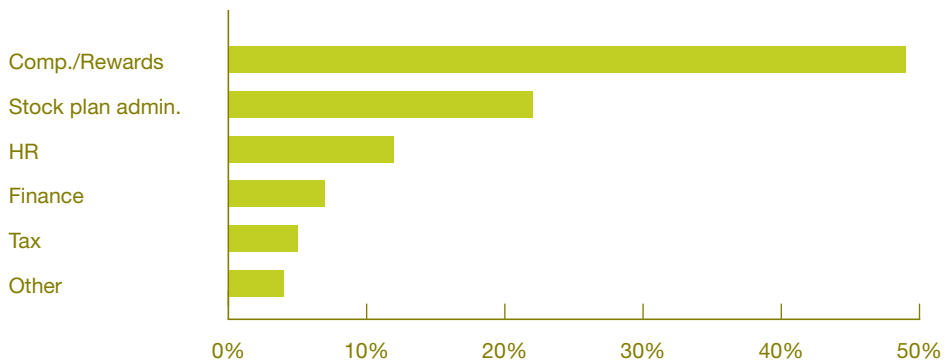
Percentage of participants by industry cluster



Percentage of participants by revenue (in USD billions)

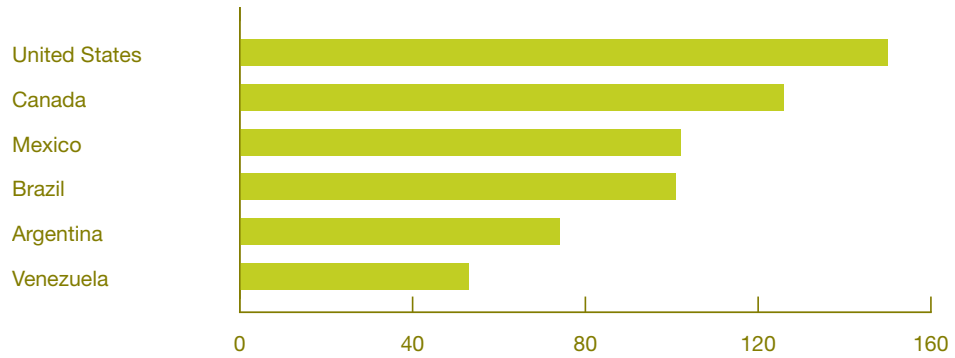


Role of the participant or respondent

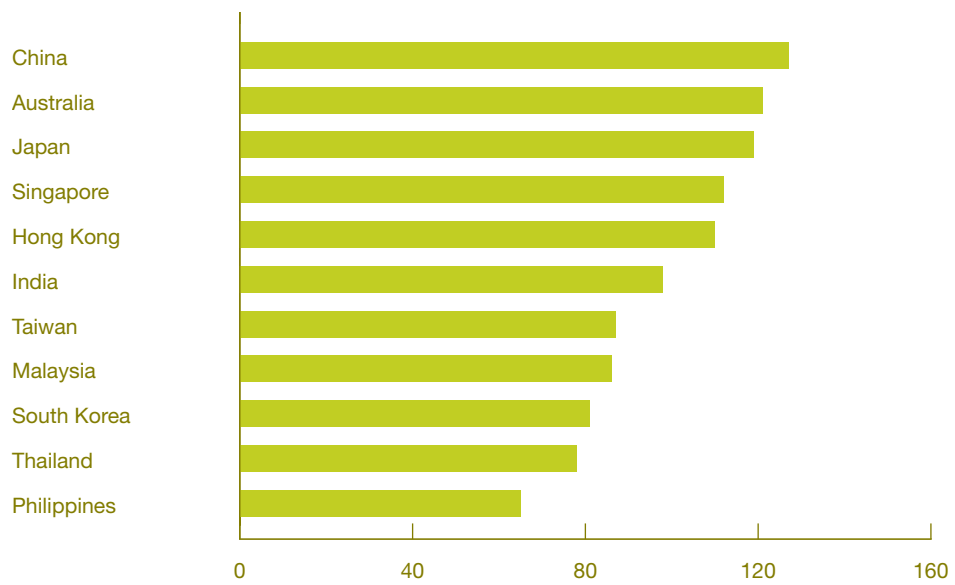


Number of participants by country

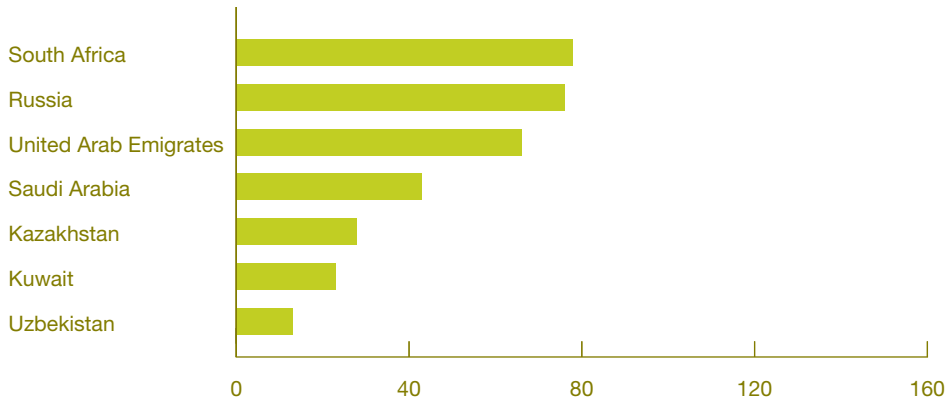
Americas



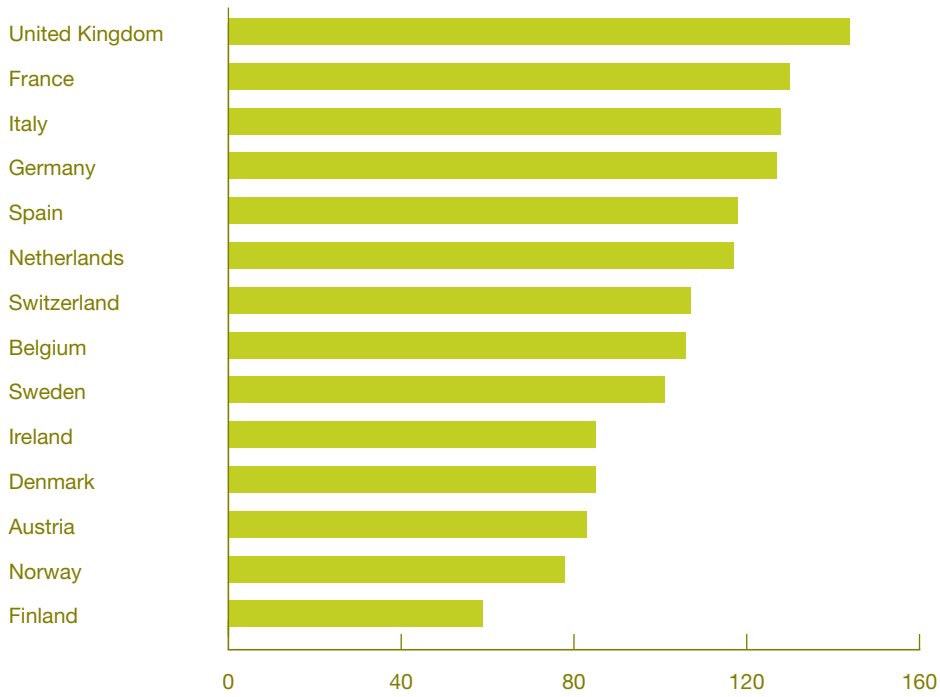
Asia-Pacific



Central Europe, Middle East and Russia



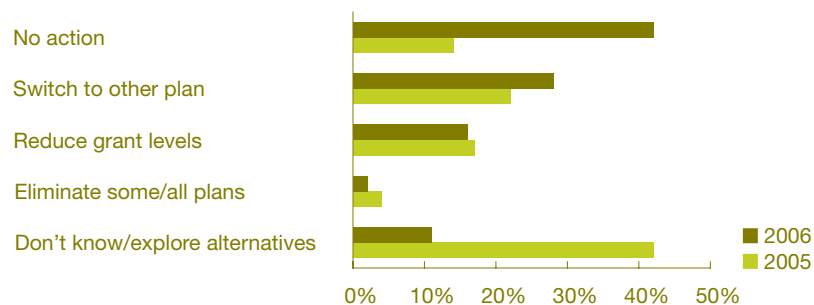
Western Europe



Expensing equity compensation is a reality

The requirement to expense equity compensation is now a reality, reducing one source of the uncertainty reflected in last year's report on global equity rewards from PricewaterhouseCoopers (2005). Whereas initial reactions to this change in accounting tended to be negative, companies are now adapting to this reality by beginning to tailor overall incentive compensation strategies to suit specific employee demographics and company goals. Whether companies are simply carrying forward their old stock option plans into the era of expensing, "tweaking" their plans, or replacing them with new equity and/or cash-based incentive plans, the use of "plain vanilla" options as a "one-size-fits-all" form of equity compensation—because they were the "cheapest"—is over.

What is the impact of expensing on your stock option plan?



The PricewaterhouseCoopers 2006 Global Equity Incentives Survey shows that companies are taking advantage of new opportunities and rethinking their compensation strategies by focusing on how they deliver compensation. For the last decade, companies wanting to achieve a variety of compensation goals have relied on stock options as the vehicle for those goals. Whether your goal was to attract, retain or motivate employees to deliver a particular result, the fact that stock options did not have an expense associated with them tended to tip the cost/benefit analysis of different types of equity compensation in favor of options. Perhaps chief among these opportunities presented, now that almost all forms of equity compensation must be expensed and reported in the same manner, is the wider variety of plans that can be customized to attract, retain and motivate employees.

The 2006 Global Equity Incentives Survey was conducted in the spring of 2006, just a year after companies based outside the United States began to recognize expense for stock options under IFRS 2, and a few months after U.S.-based companies began to do so under

FAS 123R. The results of the 2006 Survey show the following new and continuing trends as multinational companies move out of uncertainty with their equity compensation plans:

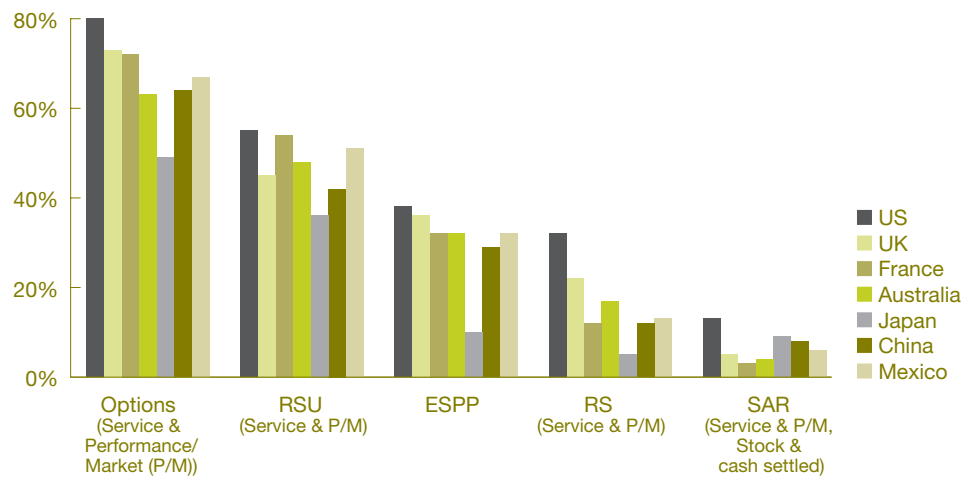
- A continuation of the three-year trend indicating a decline in “plain vanilla” stock options (both prevalence and size of grants), along with a new attention to which countries outside company headquarters participate in stock option grants
- More diversity in plan design, with a greater emphasis on full value shares and performance-based compensation
- Increased diversification in the design of service-based equity plans among various staff levels
- Continued challenges and sophistication in equity compensation plan design related to tax planning, compliance, administration and communication

The decline in “plain vanilla” options

Options are not likely to disappear entirely. While the 2005 Global Equity Incentives Survey showed that nearly half of respondents were uncertain or exploring alternatives with respect to the effect expensing has on their stock option plans, the 2006 Survey results show that many of those who were uncertain have, at least for the time being, simply rolled their existing “plain vanilla” option plans forward. Indeed, more than 40% of this year’s participants indicated that they have taken no action to change their option plan in 2006 as a result of expensing.

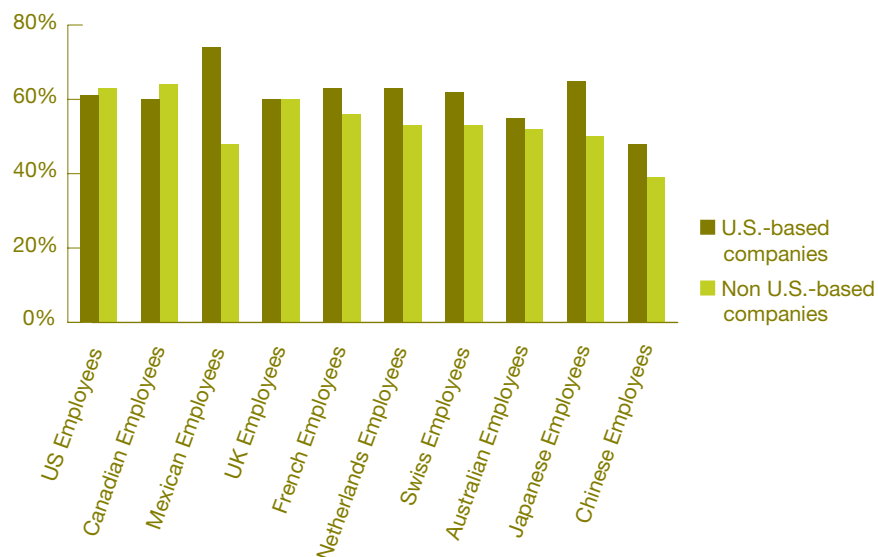
When we look at the mix of types of equity compensation, stock options (service-based and performance- or market-based) remain the single most prominent vehicle, regardless of the country where employees are located or where the company is headquartered.

The equity mix in seven countries



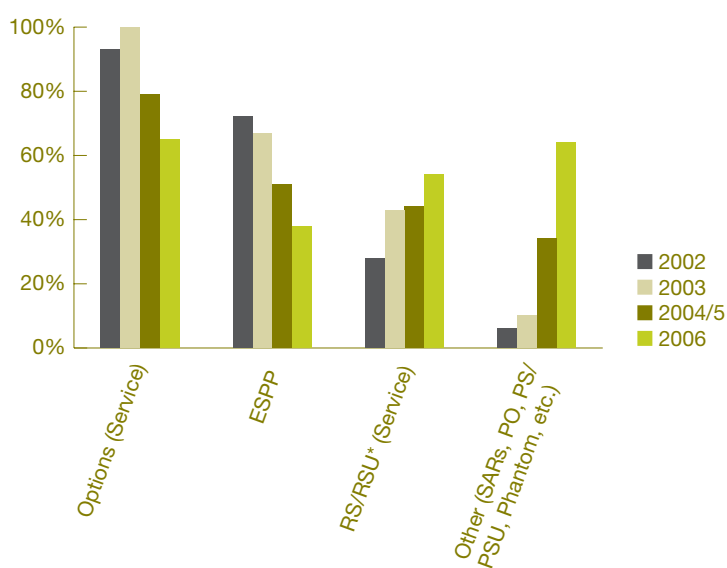
Prevalence of service-based options in ten countries

By country of company headquarters



While stock options continue to be the type of equity compensation that is most heavily relied upon by U.S. and non U.S.-based companies in all countries, we do see an overall decline in the prevalence of stock options in our 2006 Survey results, continuing a trend we have observed over the last three years. In 2003, virtually every participating company offered service-based stock options to employees in the United States. In 2004, when expensing was on the horizon, that number decreased to 80%. This year, just over 60% of participating companies with employees in the United States indicate that they offer service-based stock options to their U.S. employees.

US equity plan mix 2002-2006

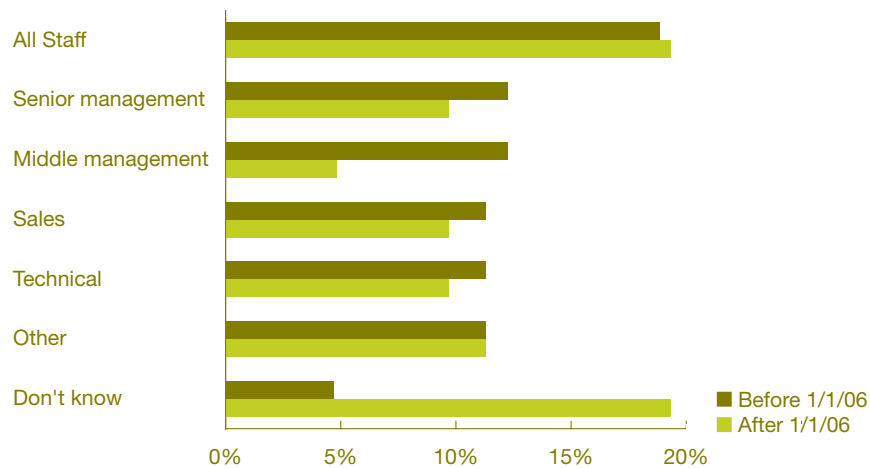


Historically, options may not have been the best way to provide equity compensation to employees for all of a company's varied compensation objectives. However, under previous accounting rules stock options were often a company's first choice because, unlike other forms of equity compensation, at-the-money stock options did not result in an expense on the income statement. Now that companies must recognize an expense for stock options, they are analyzing the cost/benefit relationship of stock options relative to other forms of compensation, and re-thinking how and when to use them. Indeed, barring significant legal and/or regulatory changes, we will probably never again see 100% of companies offering "plain vanilla" stock options like we saw in our 2003 Survey results.

A similar trend can be seen in the prevalence of employee stock purchase plans (ESPPs) offered by companies based in the United States. The majority of these plans provided benefits to participants in the form of a discount on the fair market value of the stock at the beginning or the end of the purchase period, whichever was lower. Under the old rules, these plans were not considered compensatory and, therefore, did not result in an expense for the sponsoring company. Under FAS 123R, however, most of these plans are now considered compensatory and result in an expense in the P&L. Not surprisingly, the percentage of companies offering ESPPs to employees in the United States has declined from 70% of U.S.-based companies in 2002 to 46% of U.S.-based companies in 2006, compared to 23% among companies based outside the United States. Unlike the case with options, companies based in the United States are nearly twice as likely to provide ESPPs as are companies whose headquarters are elsewhere.

Companies that plan to continue to offer stock options report reducing grant levels or restricting eligibility. Where grant levels have been cut, they are typically being cut at all employee staff levels, with 19% of participants reporting cutting grants to all staff, and over 10% of companies reporting that grants were cut to the following employee groups: senior management, middle management, sales and technical staff. Furthermore, companies report that cuts are not over. Indeed, participants expect to see similar reductions in grant levels for nearly all employee groups after January 2006.

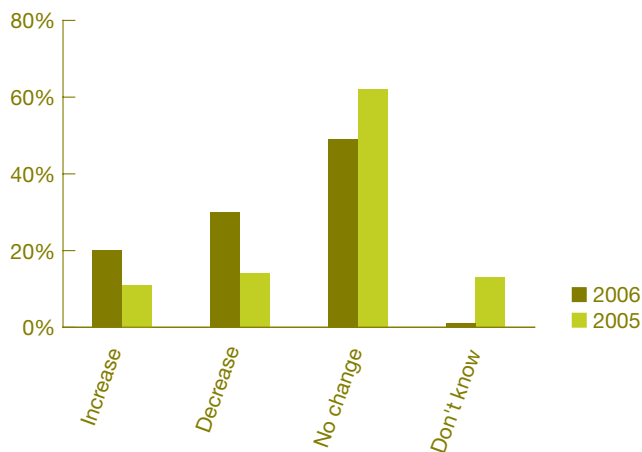
Staff levels whose option grant levels have been or will be cut



Nonetheless, while options are losing their ubiquitous role in the portfolio of equity compensation, they continue to be the single most relied-upon vehicle in every country where participants grant equity to employees. Furthermore, as companies gain more experience in global administration, tax, accounting and securities requirements related to equity compensation in the countries where they operate, they are adjusting the levels of participation among foreign affiliates in their equity compensation plans. The 2005 Survey indicated that the majority of participants did not anticipate making any changes where equity compensation is offered. This year, however, 50% of participants report that they have made some changes to where equity compensation is offered, with nearly equal numbers increasing the number of affiliates that participate as the number that are decreasing the number of affiliates that participate.

Further, overall prevalence of equity-based compensation remains—and should continue to remain—high. With employee satisfaction with equity plans at 85%, it is not surprising that 75% of respondents continue to believe that the benefits of a global equity plan outweigh the costs.

Changes in foreign affiliates that participate in equity compensation

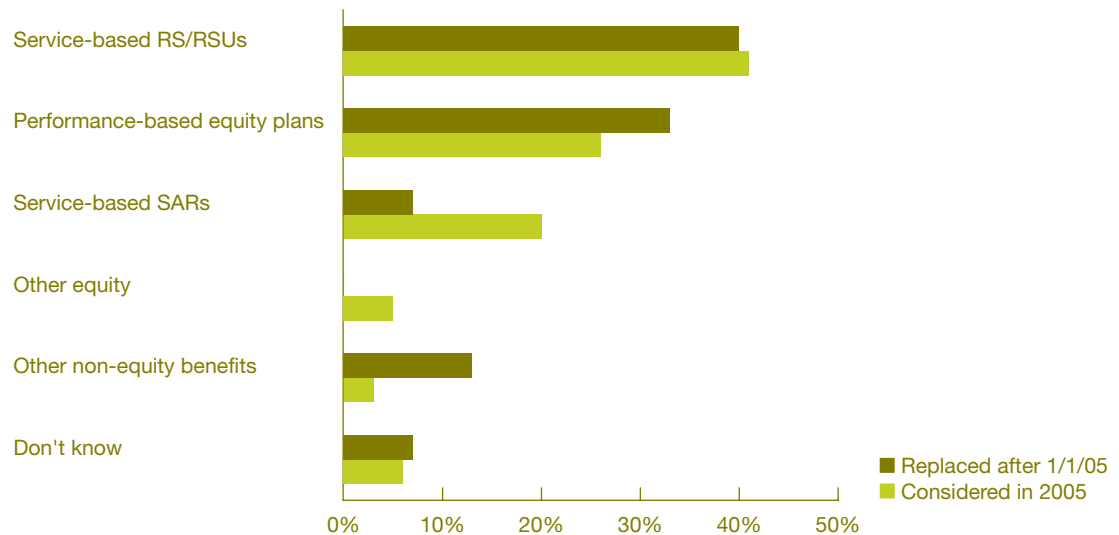


Variety in plan design, more performance-based compensation

The second significant finding of this year's equity compensation survey is manifested in two ways. First, now that expense must be recognized for all equity compensation plans, companies are beginning to more fully explore the range of possibilities and to tailor equity compensation plans to specific employee demographics and specific company needs or goals. We expect that the broad diversity of combinations reflected in this year's survey will, over time, settle into trends unique to specific employee populations, business strategies, company maturity levels and competitive landscapes.

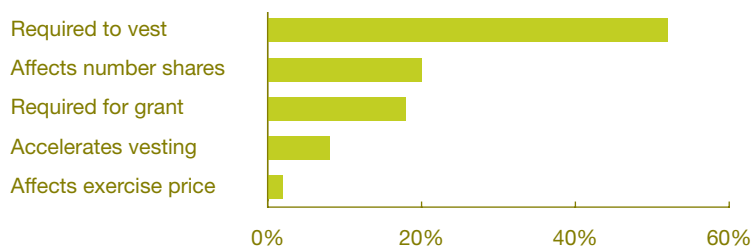
Second, as a result of this exploration, there is a noticeable shift to performance-based compensation, particularly for executive level employees, whose performance has a measurable impact on the company's bottom line. Last year's report showed almost half of all companies that were planning to replace their option plans with something else were considering replacing them with performance-based equity arrangements. This year's report shows that nearly one-third of participants actually have replaced their option plan with a performance-based plan. This trend is reflected in responses by companies based in the United States, and those based outside the United States alike.

If you are replacing your option plan with something else, what are you replacing it with?



Performance-based incentives can take a variety of forms. Options, which create a benefit for employees only if the company's stock price increases after the grant date, can be designed so employees vest upon reaching individual or company-specified goals. Restricted stock (RS) and restricted stock units (RSU), however, are currently more commonly used vehicles for performance-based equity compensation plans. Performance can be based on company-wide results, division or segment performance, or individual productivity. Company-wide results may be market-based, represented by a rise in share price over a specific period of time or based on operating metrics. Division performance is typically tied to division specific metrics, projects or priorities. Results can also be correlated with external factors or can, instead, be tied to productivity as measured by factors such as increased sales or a new product design. Insofar as recent accounting developments allow greater fine tuning of compensation delivery to what motivates each employee group to select features tailored to that group, this customization of equity incentives is a positive outcome of recent changes.

How do your performance and market targets work?

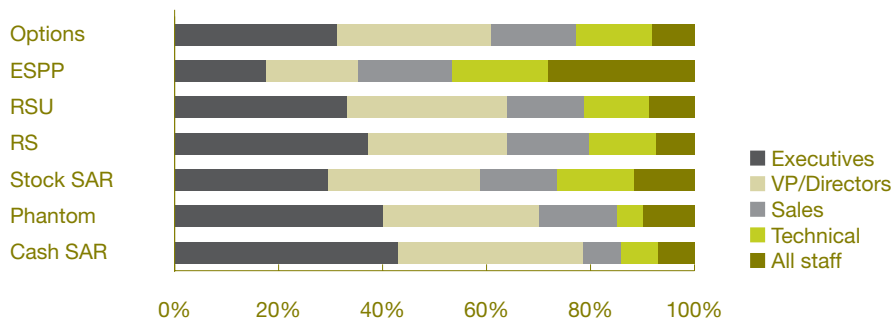


More variety in service-based plans

Performance-based plans may be increasing in popularity, but service-based plans are still very much part of the scene. Used in combination with performance-based plans, service-based equity compensation plans can provide strong attraction and retention incentives to top talent in today’s competitive recruiting environment. Survey results indicate that many companies are increasing the use of service-based equity compensation such as restricted stock, restricted stock units and stock-settled stock appreciation rights. The key finding in this arena is the diversification of service-based plans. Since the beginning of 2005, about 45% of companies replacing their option plans have replaced option grants with service-based restricted stock and restricted stock unit grants. By January 1, 2007, nearly 40% expect to do so. Restricted stock and restricted stock units continue to increase in the overall mix of equity compensation design.

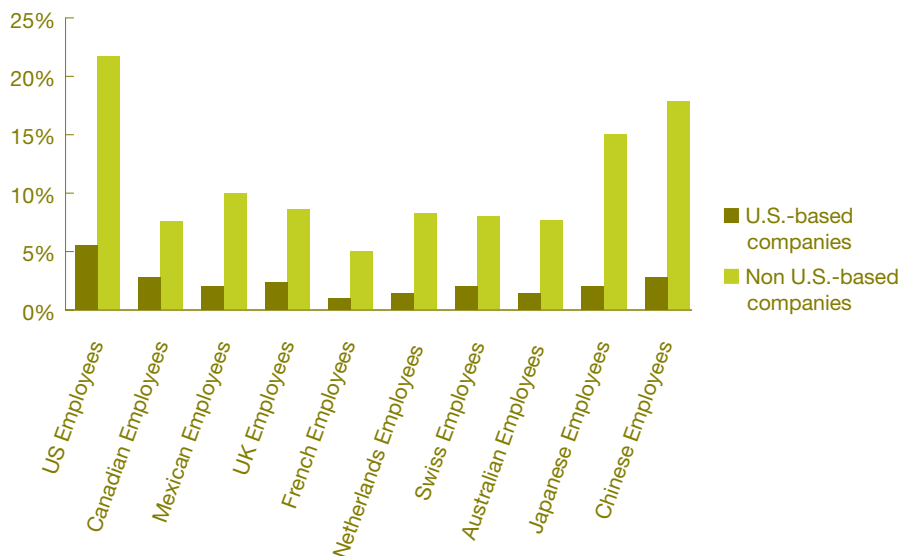
Where performance-based plans are focused more on the executive suite and sales and technical staff, service-based plans often apply to a broader range of employee groups—from executives through all staff levels. While over 60% of respondents indicate that executives and upper management participate in service-based RS and RSU plans, 10% report that “all staff” participate in such plans, with the rest fairly evenly divided between sales and technical staff. This year we also asked participants how they use equity and cash for their broad-based plans. One in ten companies report replacing options with cash bonuses, typically below the managerial level.

Which employees participate in your service-based equity compensation plans?



A somewhat new trend shows a growing segment of companies (7-8% in 2006) that are replacing stock options are moving to service-based stock appreciation rights (SARs). When we look at where companies that offer SARs are headquartered, we see that companies based outside the United States are more than twice as likely as companies headquartered in the United States to include SARs in the mix of equity compensation. SARs are like stock options in that they tie individual reward to company performance in a clear, easy way to understand. Unlike options, however, SARs do not dilute shareholder earnings by requiring that individuals pay a purchase price. We will be closely monitoring whether this trend favoring the use of SARs among non-US based companies is replicated among U.S.-based companies, who began complying with FAS 123R a year later than non U.S.-based companies began complying with IFRS 2.

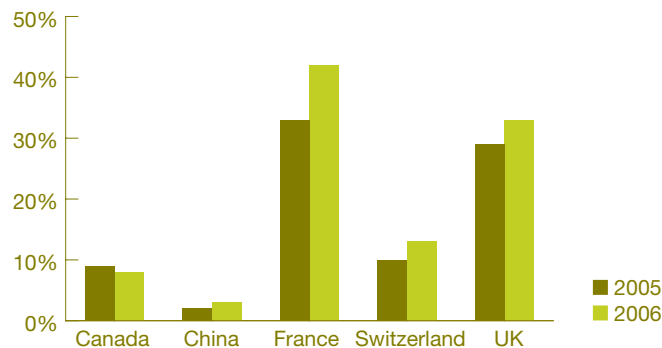
Prevalence of stock appreciation rights among U.S.-based and non U.S.-based companies



Continued challenges in plan design and compliance

The requirement to expense equity compensation is reflected in the flurry of changes related to compensation design and valuation strategies and international compensation design. A corollary to these changes is the increase in the number of companies that report taking advantage of various tax planning strategies related to equity compensation expense. Soon after IFRS 2 and FAS 123R were released, companies were aware that they would be required to track expense for all forms of equity compensation grant by grant, employee by employee and country by country. Many of these same companies began to look for ways to allocate this expense to departments and local (foreign) operations. Companies also began to look more closely at introducing qualified plans where possible.

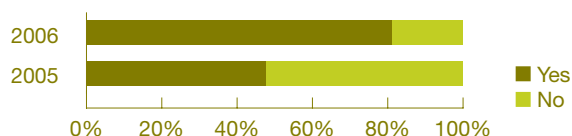
Chart 11: Does your company offer a locally tax-favored plan?



Perhaps because the new accounting requirements mandate that record keeping is done at the individual and grant specific levels, the cost/benefit analysis of implementing locally tax qualified equity compensation plans has shifted for many global companies. Because this trend is apparent in both headquarter countries and foreign locations, additional cross-border coordination is anticipated in the future.

Meanwhile, increasing attention is being paid to country-specific tax planning, as in the growing use of charge-backs which can create corporate tax deductions that offset income lost to expensing. In 2005, fewer than 48% of respondents charged back the costs associated with equity stock-based compensation plans to their foreign subsidiaries. By 2006, 61% of companies did so. We expect this increasing trend to continue as companies continue to look for ways to reduce the impact of stock-based compensation expense.

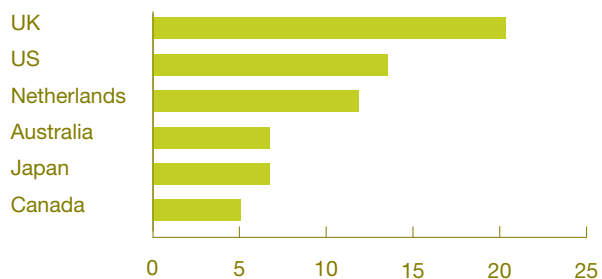
Does your company charge back the costs affiliated with your equity/stock-based compensation plan(s) to your foreign subsidiaries?



Note: 2006 responses do not include 14 "don't know" responses

Tax authorities worldwide have stepped up the number of audits they perform related to equity compensation. For example, South Korea has announced its intention to audit all the equity plans of all companies that do business there. In Japan, tax authorities are investigating whether individual executives have characterized equity compensation correctly and whether they are paying appropriate tax. In the United States, it has recently been discovered that a significant number of companies have, in one way or another, backdated options. The SEC has announced that it will investigate this practice which, in effect, results in the granting of discounted options that are accounted for as if they were fair market value stock options. It is expected that these companies will have to take action to recognize additional expense. In this context, it is not surprising that compliance was cited as a significant challenge faced by over two-thirds of Survey participants.

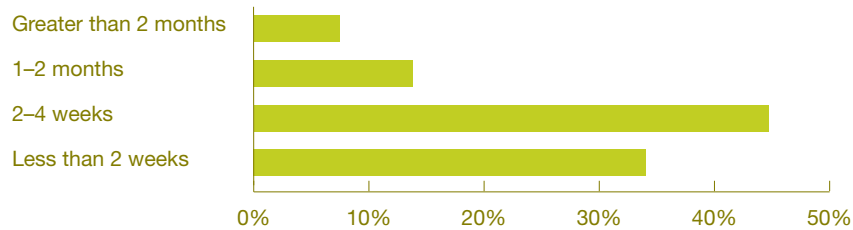
Has your company been audited by local tax authorities during the last three years?
(Most frequent responses only)



The complexity entailed in the new regulatory environment has resulted in more challenges in the areas of stock plan administration and employee communications. A sizable number

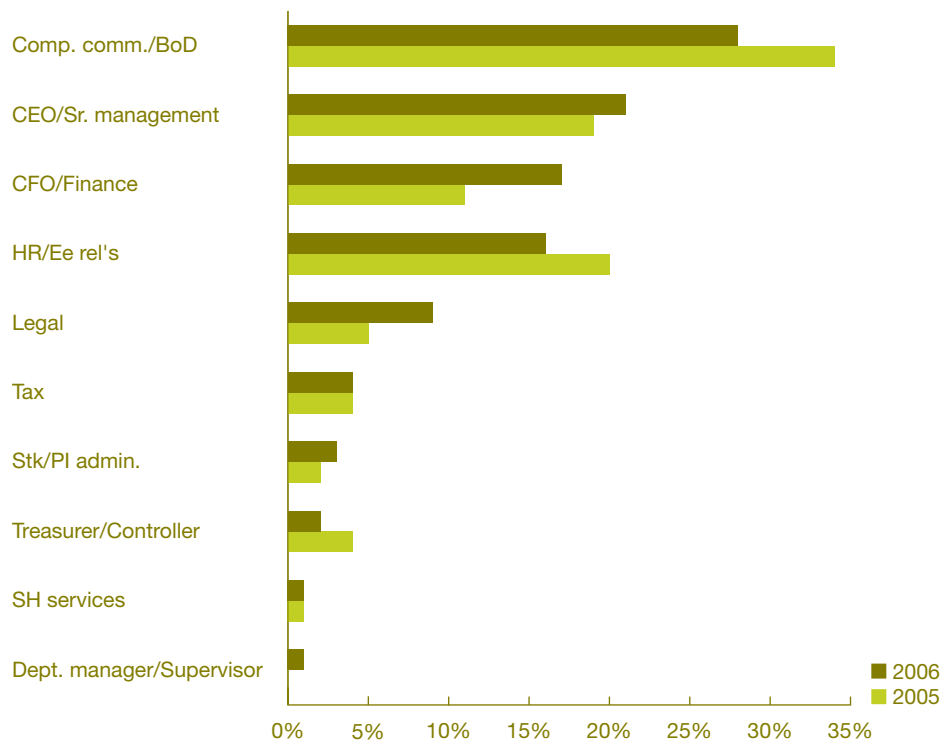
of companies, almost 45%, report a lag time of two-to-four weeks related to communication of equity compensation awards. More than 15% of companies' communication processes take more than a month. Further, companies reported a slight decline in satisfaction with both stock plan administrators and stock plan software from 2005 to 2006.

What is the general lag time between the Board's approval and the company's communication of the plan to employees?



However, on a positive note, there is more cross-department collaboration as human resources, accounting and tax departments are all increasingly involved in the design and administration of equity compensation plans. Equity compensation now generates reporting and budgeting responsibilities throughout the organization, bringing many new stakeholders into collaboration regarding equity compensation strategy, design and delivery.

Which five are the most influential decision-makers for your employee stock-based compensation plans?



Conclusion

In general, in reviewing this year's findings on equity compensation, two points are abundantly clear. First, the most critical element in plan design is identifying company objectives. If the primary goal is retain employees for three years (or more), then a service-based plan may be most appropriate. If the goal is to reach a given target, then the best choice may be a performance-based plan. Combination plans based on both service and performance can also be designed. In today's compensation marketplace, equity incentive plans can be tailored to reach specific objectives and to recruit and retain specific employee groups.

The second point is that despite complex and changing accounting, regulatory and tax requirements, equity in the company remains something employers want in the hands of employees. Companies across industries and borders will continue to explore the newly leveled playing field of equity compensation vehicles with respect to their particular business and talent management goals. Although leading practices in the design of these plans are in a state of flux, the one currency that is constant is the perceived value of employees owning company stock.

To obtain the full report

To receive a copy of the 2006 PwC Global Equity Incentives Survey report free of charge, please send an email to SurveyAdmin@us.pwc.com, or call +1 720 931 7341. Contents of the 2006 Report include:

Part I

Section 1

Organization and Participant Information

Section 2

General Information (Equity Plan Design, Participation, etc.)

Section 3

Accounting for Equity/Stock-Based Compensation

Section 4

Global Aspects of Equity/Stock Plans

Section 5

Tax Planning and Compliance for Equity Plans

Section 6

Process and Administration
of Global Equity/Stock-Based Compensation

Section 7

Employee Communication

Part II

Country-specific questions pertaining to equity-based compensation in the following countries:

Australia	Ireland	Spain
Belgium	Italy	Switzerland
Canada	Japan	Thailand
China	Netherlands	United Kingdom
France	Singapore	United States
Germany	South Africa	
India	South Korea	

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It is this combination of experience which sets us apart.

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