



**GAO'S SIXTH ANNUAL CONFERENCE**  
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**Companies' Reactions to Changes in the Global Share Plan Environment**

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**Changes in the Global Share Plan Environment**

- Market conditions
- Institutional investors
- Regulations
- Tax
- Accounting

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**Typical Traditional Global Share Plan Model**

	Top executives	Other senior managers	All employees
Home country	Share options (and often performance shares)	Share options	Share purchase plan (eg ESPP, SAYE)
Overseas/global	Home country practice	Share options (modified as necessary for tax, regulatory reasons)	Share purchase plan (where feasible)

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### Market Conditions

- Low inflation
- Stock market volatility:
  - reduced probability of payout from options
  - lower perceived value by employees
- Pensions crisis



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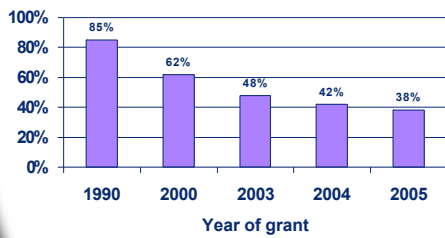
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### Reducing Attractiveness of Share Options

Probability of option pay-out in UK



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### Increased Power of Institutional Investors

- Pressure globally for:
- increased disclosure, value for money
  - reduced dilution (overhang) / size of awards
  - effective performance conditions



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### Increased Regulation

- EU Prospectus Directive
- US Sarbanes-Oxley
- NYSE, NASDAQ listing rules reviewed
- Corporate governance codes: eg
  - EU – recommendations on directors' pay and on role of independent directors
  - Australia – ASX code
  - UK Combined Code



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### Tax – Changing Rules

- Anti-avoidance and reporting: eg
  - American Jobs Creation Act 2004
  - UK Finance Act 2003
- International perspective of tax authorities
  - OECD cross-border recommendations
  - trailing liabilities
  - transfer pricing
- Compliance / audits



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### Ongoing Tax Developments

- Australia – tax treatment of employees who change residency
- France – new tax regime for granting of free shares
- Mexico – new rules governing taxation of stock options
- Netherlands – taxation of options at date of exercise
- Singapore – waiver tax treatment of departing employees
- South America – availability of deductions locally
- US - Jobs Creation Act treatment of deferred compensation
- Many others



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### New Accounting Rules for Share-Based Payments

IFRS2 / FAS123(R):

- New charge for share options where there was not one
- Removal of accounting bias for share options
- Performance conditions:
  - no longer a 'variable accounting' disadvantage
  - reduce expense
  - problems with traditional accounting measures



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### Performance conditions: Market vs. Non-Market example of company with volatile earnings



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### Other accounting issues around performance measures

- Main standards:
  - IFRS 2: Share plans
  - IAS 19: Employee remuneration and benefits
  - IAS 27/ IFRS 3: Business combinations
  - IAS 32/ IAS 39: Financial instruments, treasury operations
  - IAS 38: Intangible assets
- Short-term transition issues
- Long-term concerns about suitability of EPS
- EPS vs TSR vs other



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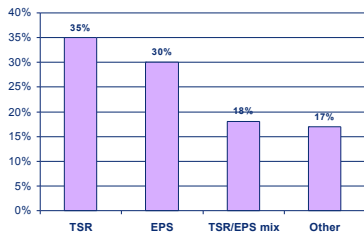
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### UK Equity Plan Trends

Performance conditions for plans approved by shareholders in UK in 2004



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### Other Criticisms of Share Options

- Encourage excessive risk taking
- Do not lead to share ownership
- Do not take relative performance into account



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### Implications of Changes for Global Share Plans

- Pressure to reduce accounting costs and dilution
- Options perceived less attractive – both for investors and for employees
- Need for capital accumulation
- Increased compliance burden
- More disclosure, resulting in greater press coverage
  - executives moving from listed companies to private equity



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### Predicted Responses to These Changes

- Cut size and frequency of grants
- Cut number of participants
- Cut broad-based / all-employee plans
- Cut foreign plans
- Use cash instead




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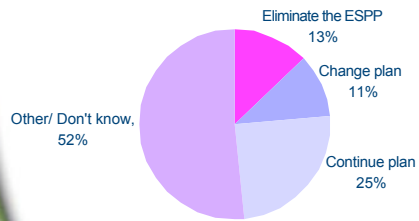
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### Global Equity Incentives Survey\* Results

If accounting rules result in increased expense for share purchase plan/ESPP what will your company do?




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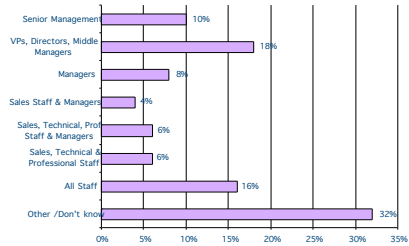
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### Global Equity Incentives Survey\* Results

How staff are selected to have grants reduced after expensing?:




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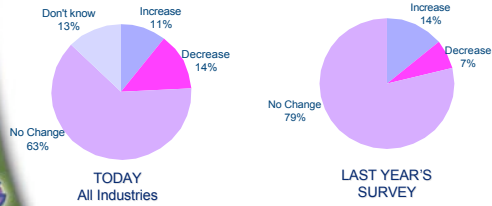
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### Global Equity Incentives Survey\* Results

Is your company planning on increasing or decreasing the number of foreign subsidiaries that participate in share plans in near future?



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### More Sophisticated Responses

Revisit role of share plans:

- tax-effective reward
- competitive total reward package
- method of wealth accumulation (pension supplement)
- motivational impact
- educational role
- global unifier

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### Alternative Approaches We Have Seen

- More sophisticated grant policy – tailored by:
  - line of business
  - job role
  - location / competitive forces
- Changes in option plan design:
  - premium options/caps/earlier expiry
  - performance conditions
  - longer vesting periods

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### Alternative Approaches (continued)

- Changes in types of plan
  - move towards share awards – performance/restricted shares/deferred shares, all-employee share awards
  - more use of share-settled SARs
- Shareholding guidelines
- Key role for share plans in employee communication



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### Recent Global Share Plan Trends

- Reasons for operating
- Perceived value
- Performance conditions
- Types of plan



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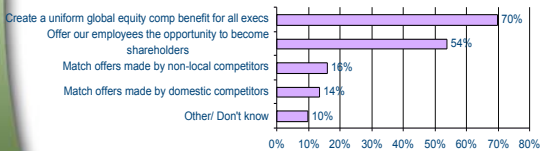
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### Global Equity Incentives Survey Results

What were the reasons for offering share-based plans to your international employees?



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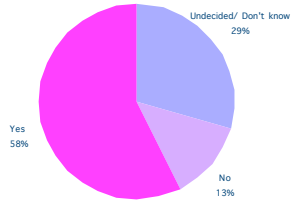
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### Global Equity Incentives Survey Results

Are costs of global plans worth the benefits?



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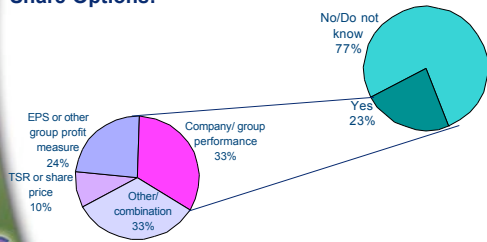
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### Global Equity Incentives Survey Results

Do your share plans have performance measures?  
**Share Options:**



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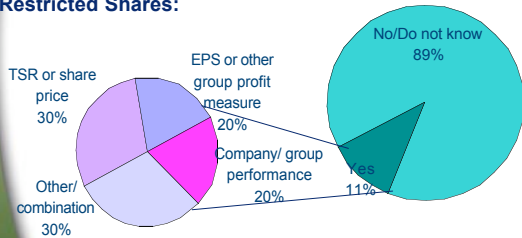
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### Global Equity Incentives Survey Results

Do your plans have performance measures?  
**Restricted Shares:**



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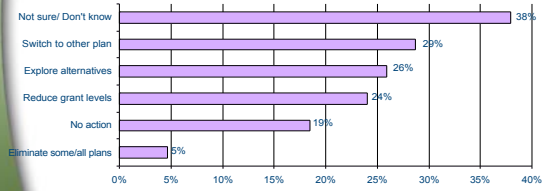
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### Global Equity Incentives Survey Results

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




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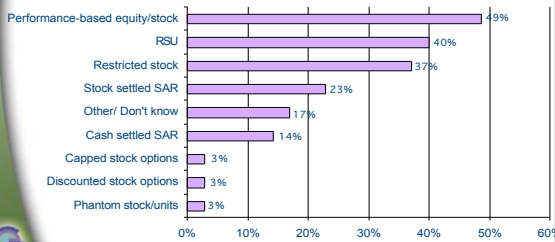
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### Global Equity Incentives Survey Results

Please select the vehicles you are considering moving to:




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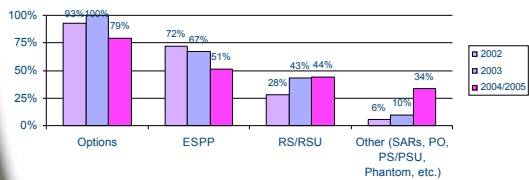
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### US Share Plan Trends

Types of share incentive plans offered in the US over the last three years.




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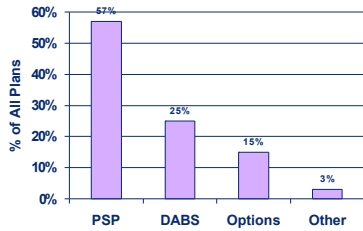
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### UK Share Plan Trends

Types of share incentive plans approved by shareholders in UK in 2004



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### Tax and compliance issues

- Local modifications to plans
- Charge-backs to local affiliates
- Degree of compliance with tax and other regulatory provisions

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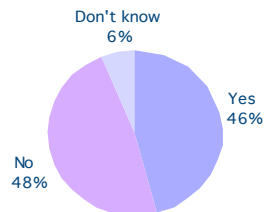
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### Global Equity Incentives Survey Results

Have you modified your share plans plan(s) in any way, specifically for grants in other countries?



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**Case study**

- US-based multinational operating stock plans in excess of countries
- Old policy:
  - Restricted stock
  - Stock options



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**Case study (continued)**

Company undertook review of stock plans globally

- Drivers for the review were:
  - stock options regarded as ineffective
  - accounting charge creating more transparency around stock plans
  - restricted stock creating tax issues in certain territories
  - Sarbanes-Oxley
  - corporate tax deductions



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**Case study (continued)**

Findings:

- most stock options underwater
- flat share price meant options did not represent value vis a vis accounting charge
- restricted stock created issues around timing of tax charge in certain countries
- numerous tax compliance failures around the globe
- inefficient internal processes led to delays in information being passed to local territories



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**Case study (continued)**

Outcome:

- redesign stock plan to RSUs
- cease granting stock options and restricted stock
- improve processes to ensure better flow of information
- seek local tax clearances
- ensure correct tax compliance for local nationals
- looking at systems to deal with tax compliance for internationally mobile employees
- implementing recharges




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**Typical response of UK-based multinational**

- Performance share plans/restricted share plans –using deferred bonus plans for top executives
  - Support minimum share holding requirement
- Restricted shares to other senior managers
  - on selective basis
  - annual performance link
- Restricted share awards to all employees
  - communication tool
  - simpler to understand
  - No reduction in perceived value




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**Emerging global share plan model**

	Top executives	Other senior managers	All employees
Home country	Restricted/ deferred shares/ RSUs with stringent performance conditions	Restricted shares / RSUs (modified by function and/or sector) More varied performance conditions	Restricted shares
Overseas countries/global	Home country practice	Restricted shares / RSUs (modified by function and/or sector and/or region)	Restricted shares (or phantom)




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**Questions?**

Thank you for your participation



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**PwC's 2005 Global Equity Incentives Survey**

- The 2005 survey researched the global share incentive practices of multinational companies
- The survey was completed in September-November, 2004
- 131 multinationals participated. All revenue/turnover and employee sizes were well represented in this year's Survey
  - 300-100,000+ employees
  - annual revenues from \$64 Million to \$232 Billion



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