

## What Happens When Your Company Decides to Change From Stock Options to RSUs?

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### Today's Presenters

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## Agenda

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- Global Dynamics
- CBS Environment and Driving Force for Change
- Existing Options
- Restricted Stock and RSUs - CBS Key Features
- The Exchange
- Global Implementation
  - Tax
  - Legal
  - Accounting
  - Communication
- Lessons Learned/Leading Practices

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## Global Dynamics

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- Compliance under US Sarbanes Oxley 404 Rules
- FAS123R and IFRS 2
- More Extensive Disclosure Requirements
- S409 A Regulations in the US
- Corporate Governance Environment
- Creativity of Executive Compensation Directors
- Planning to align Long Term Incentives with Business and Human Capital strategies
- Shareholder focus on anything related to equity

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## Overall Environment

- Recognition of options expense – cost/benefit analysis
- Decline in prevalence of stock options in the US
- Replacement of options with service-based, performance-based, or market based-plans
- Viacom moved away from options model to RSU model

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## CBS Environment

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- The “Separation” of former Viacom Inc. into CBS Corporation and Viacom Inc.
- Perceived growth potential of new companies necessitated a revamping of equity compensation planning
  - Prospective: Stock options vs. RSUs?
  - Historical: What about those underwater options?



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## CBS Demographics – Local Population

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<i>Country</i>	<i>Headcount</i>
Australia	50
Canada	500
France	200
Germany	100
Italy	200
Mexico	150
Netherlands	300
Spain	150
UK	500
US	22,500
<b>Total</b>	<b>24,650</b>



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## **The Option Plans – The Viacom Inc 2004 Long Term Management Incentive Plan**

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- Non Qualified Stock Options
- Time-based vesting in 4 equal installments
- Class B Common Stock
- January 2005 grant
  - Any employee eligible
  - Exercise Price \$37.38
  - Expiration of exercise period in 8 years from date of grant
  - Non transferable
  - Options terminated if employment terminated for cause
  - Cashless exercise, net share settlement
  - Ability to cancel stock options in exchange for Restricted Stock or other equity award if in connection with a corporate transaction

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## **Options – Why not?**

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- Purchase of shares at a predetermined price
- Tied to future performance
- Mandatory Stock Option Expensing, FAS123R
- Greater Market Price Risks
- Underwater
- Dilution
- Key Executives kept mix of stock options and RSUs
- Retention in new landscape of CBS

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## CBS- The Driving Force for Change

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- The Voluntary Exchange Offer intended to accomplish a number of important objectives:
  - Reintroducing vesting restrictions where the vast majority of options are fully vested,
  - Improve the retentive effects of long-term incentives to ensure the continuity of its employees.
  - Reinforce the “ownership culture” among its employees; and
  - More closely align employees’ interests with those of the CBS stockholders.
- The Voluntary Exchange Offer should reduce the overhang and potential dilution associated with long-term incentive plans.



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## CBS- The Driving Force for Change

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- What was the impetus for change?
  - Corporate “separation”
  - CBS profile post split
- Approval Process?
- How?
  - Tender Offer
- Multi-disciplinary Approach:
  - Human Resources
  - Legal
  - Tax
  - Treasury
  - Accounting



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## Features of Restricted Stock and RSUs

Restricted Stock	RSUs
Receipt of Stock	Promise to pay
Participant does not have to pay	Participant does not have to pay
Not necessarily tied to performance	Not necessarily tied to performance
Treatment on Financial Statements	Treatment on Financial Statements
Less Dilution	Less Dilution
Dividends accrued	Dividend Equivalents
Vesting provisions	Vesting provisions

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## CBS Strategy

- Roll out Restricted Stock in ALL locations
- Assessed US Tax Implications
- S409A
- RSUs subject to disadvantageous tax treatment
- Participant loses flexibility of choosing when to receive proceeds
- May be difficult to communicate that replacement awards are equal in value to the replaced stock options
- Administration more complex

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## CBS Revised Strategy

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- Continue to use Restricted Stock in US
- Award RSUs in ALL other locations
- Tax treatment pivotal in shaping the strategy
- Restricted stock subject to disadvantageous tax treatment
- Participant loses flexibility of choosing when to receive proceeds
- May be difficult to communicate that replacement awards are equal in value to the replaced stock options
- Administration more complex



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## The CBS RSU Plan

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- Represent the right to receive shares of CBS Class B Common Stock upon vesting
- Subject to forfeiture prior to vesting, and may not be transferred
- Dividend equivalents accrue on the RSUs and are subject to the same vesting conditions as the underlying restricted shares
- Vesting in two equal 50% installments on the second and third anniversaries of the grant date
- Golden Handcuffs.



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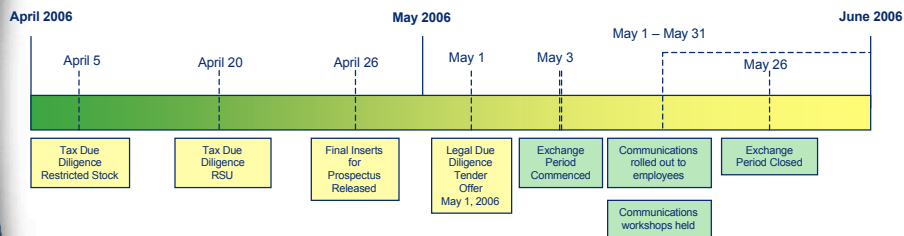
## The CBS RSU Plan (cont.)

- Accrued dividends and dividend equivalents are paid to the holder of RSUs in cash when the underlying restricted shares or RSUs vest and will be forfeited if the underlying restricted shares or RSUs do not vest
- Performance conditions for certain CBS senior executives - *Section 162(m)*
- Shares of CBS Class B Common Stock do not have voting rights - *Sumner Redstone's ownership.*



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## Global Implementation Issues - Timeline



*Total Time Period – Start to Finish – 3 \_ Months*



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## The Exchange – Not one for one

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- “Eligible Employees” – an active employee continuously employed throughout the Voluntary Exchange Offer
- The exercise prices of all eligible options were adjusted to take account the Separation:
  - “**Out-of-the-money**” options are those that have a per share exercise price equal to or greater than \$24.9340
  - “**In-the-money**” options are those that have a per share exercise price less than \$24.9340
  - “All or nothing” exchange within each category
- Eligible Employees receive a number of RSUs that have in aggregate a fair value equal to 75% of the aggregated tendered options.

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## The Exchange

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- The number of restricted shares or RSUs received was calculated by applying the following equation to each of the outstanding awards of eligible options:

$$RS = \frac{0.75 \times N \times AV}{REF}$$

- “RS” is the number of restricted shares or RSUs received in respect of the particular award of eligible options for which the calculation is made
- “N” is the number of eligible options included in the particular award for which the calculation is made, rounded down to the nearest whole number
- “AV” is the “attributed value” of an eligible option included in the particular award for which the calculation is made. The “attributed value” of each eligible options was calculated using the Black-Scholes option pricing model, which is a commonly used model for valuing stock options
- “REF” is the “reference price” of the CBS Class B Common Stock, \$24.9340 per share. This was the average of the closing prices of the CBS Class B Common Stock on the NYSE for the five consecutive trading days ending on April 26, 2006(which was the fifth trading day preceding the date Voluntary Exchange Offer was commenced)

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## Global Implementation Issues – Tax

- Individual Income Tax Implications of the Exchange
- Taxation upon exchange:

Country	Income Tax due on Exchange	Capital gains Tax event on Exchange	Company Withholding Obligations upon grant of RSUs	Company Reporting Obligations upon grant of RSUs
Australia	No	Yes	None other than in respect of dividend equivalents	None other than in respect of dividend equivalents
Canada	Out the money options - Yes In the money options - Possibly	No	No	Yes
France	No	No	No	No
Germany	No	No	No	No
Italy	No	No	No	No
Mexico	No	No	No	No
Netherlands	Yes	No	No	No
UK	No	No	No	No

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## Global Implementation Issues – U.S.

- §409A issue: risk of adding deferral feature, subjecting the awards to §409A
- Would be adding deferral feature if fully vested options were exchanged for unvested RSUs
- Restricted stock not subject to §409A - exchanging options for restricted stock not addition of a deferral feature

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## Global Implementation Issues - Canada

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- Taxation dependent upon the intrinsic value of the outstanding options immediately before exchange and the FMV of the shares underlying the RSUs immediately after exchange
- “In the money” options – **May** be subject to income and social tax at exchange
- FMV of shares underlying RSUs exceeds the intrinsic value of the stock options – roll-over not available – double taxation
- “Out of the money” options – **Will** be subject to income and social tax at exchange
- Roll-over not available as intrinsic value is zero. Recognize employment income equal to the FMV of the RSUs immediately after the exchange.
- Preferential tax treatment – offset 50% (25% Quebec)
- Systems Issues:
  - Withholding tax set to withhold on stock options at capital gain rates
    - Potential under-withholding for employees

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## Global Implementation Issues - Legal

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- Tender Offer Process
- SEC Filing
  - 14(e)(5) Relief
- SEC Exemptive Order Reliance
- UK Exclusionary Offer
  - Who can facilitate?

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## Global Implementation Issues - Accounting

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- Fully vested- No Compensation Expense
  - Early adopter of FAS 123R
- Unvested- Compensation Expense
  - Grant date FMV over the remaining vesting period



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## Global Implementation Issues – Communication: General Overview

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- Method of Communication: Webcast, Group Workshops, Written Documents, One-on-One, Helpline
- Timing: Is there an Offer Period?
- Jurisdictions: US vs. Worldwide
- Special Groups: Top Executives, Individual Talents, VIPs



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## **Global Implementation Issues – Communication: CBS Specific**

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- Typical Communication Structure
- US: Live Workshops, Telephone Conferences, 1-800 Helpline
- Worldwide: Written Communication, Telephone Conferences
- Special Groups: One on One
- Timing: 30 day offer period



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## **Global Implementation Issues – CBS Internal Coordination**

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- 409A: RSU's
  - RSUs subject to 409A unless “short-term deferral”
- SEC documents: Communication to employees
- Systems: Payroll withholding/reporting process?
  - Systems issues



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## **Post Implementation Issues**

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- Update Tax and Legal Due Diligence Annually
- Update Communications Annually
- Update Systems



## **Leading Practices from Our Process**

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- Strong Communication Strategy
- Workshops & Written Communication
- Design Features
- Global Tax Strategy
- Inclusion of Multi-discipline team



## CBS – Lessons Learned

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- What would CBS do differently?
  - Provide more time to implement:
    - Avoid Crisis Mode



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## One Year On – What Next?

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- Disparate Plan Structures
  - Need to Standardize
    - DBP?
    - ESOP?
    - Enhanced DCP?
- Evaluate Equity Awards annually – stock options?



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## Questions?

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Thank you for your participation



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