

Global Warming:

Regional Overview of Tax and Legal Changes Affecting Share Plans

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Agenda

- General Trends
 - From a legal perspective
 - From an issuer perspective
- Breakdown by Region
 - From cool to warm to HOT!



Global Warming: General Trends

- Reduction of option grants due to accounting expense
- Shift to Restricted Stock Units due to lower accounting expense compared to perceived benefit and lower dilution/share usage
- Increased focus on tax optimization due to FAS 123R/IFRS2
- Increased audit activity

Global Warming: Lilly Background

- Eli Lilly and Company
 - 40,000+ employees
 - Issue equity in 90+ countries
 - Shifted to expense oriented award guidelines in 2006
 - Shifted to regional award guidelines in 2006
 - Eliminated stock options from our award portfolio in 2007
 - Currently focused on:
 - Indian Fringe Benefit Tax implementation
 - Chinese foreign exchange and tax regulations
 - Updating employee-focused, country-specific tax supplements
 - Evaluating the effectiveness of our new award portfolio

Lilly

Answers That Matter.

Global Warming: Issuer Trends

- **Changing Design Portfolios**
 - Mandatory expensing of stock options continuing to drive companies to utilize more full value share awards
 - Shareholder pay for performance concerns driving award criteria (performance vesting, award adjustments, etc)
 - Companies beginning to design award guidelines based on expense instead of setting guidelines based on share counts
- **Award Values**
 - Equity award values being adjusted for local market conditions (regional or country-driven award sizes)
 - Reliance on quality local and/or global LTI survey data increasing (global guidelines based on headquarter's country diminishing)

Global Warming: Issuer Trends

- **Tax Liabilities especially for the Mobile Workforce**
 - Local tax implications forcing corporations to review the effectiveness of equity programs in certain jurisdictions
 - Detailed tracking of global workforce movement improving
 - Application of trailing and/or exit tax a concern, but difficult to manage (outside of company sponsored mobile employees whose taxes are usually managed by a large accounting firm)
- **Managing Compliance**
 - Securities, tax, and foreign exchange regulations constantly evolving
 - Companies are keenly interested in being compliant, but struggling with complexity and/or vagueness of regulatory guidelines

Global Warming: Breakdown by Region



- Africa
- The Americas
- Europe
- Asia-Pacific



Global Warming: Africa



-  South Africa: Exchange control approval for equity plans no longer required

Global Warming: The Americas

-  Mexico: New securities law and impact on equity awards
-  Costa Rica: New tax rules for options and ESPP (again!)

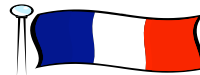


Global Warming: Europe

-  Netherlands: No longer corporate tax deduction
-  Russia: Exchange control laws liberalized



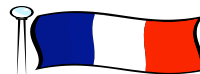
Global Warming: France



- New restrictions/guidelines for French-qualified awards:
 - Law on profit sharing and employee equity plans dated December 30, 2006
 - Tax guidelines published November 10, 2006



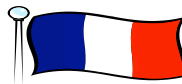
Global Warming: France



- Good news:
 - No requirement to comply with 2-year share holding requirement for French-qualified RSUs in case of death or disability (as defined under French law)
 - If 4-year cliff vesting, 2-year share holding requirement does not have to be *imposed* for French-qualified RSUs (i.e., can be left to awardee to comply), but still has to be met to obtain qualifying treatment
 - Possible to require payment for RSUs/underlying shares if price does not exceed 5% of value of shares at grant



Global Warming: France



- **Bad news:**
 - Closed period restriction continues to apply to sale of shares for French-qualified RSUs
 - Corporate officer restriction (applies to both French-qualified options and RSUs)
 - Covers certain enumerated executives at French entity (but not if local entity organized as SARL)
 - Requires that “certain” percentage of shares not be sold until expiration of corporate duties
 - Recommendation: Modify sub-plan and/or agreement to provide for restriction
 - No dividend equivalents permissible, even if paid in shares at vesting

Global Warming: Italy



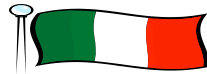
- Modification of fair market value (FMV) exemption for options granted/exercised on or after 7/5/06
- “Old” FMV exemption easy to comply with:
 - Exercise price must be no less than Italian FMV of stock on grant date (i.e., one-month average price prior to and including grant date)
 - Optionee may not hold more than 10% of outstanding shares of issuer
- Grandfathering provision for options granted before but exercised on or after July 5, 2006, but only with respect to social security contributions

Global Warming: Italy



- First changes to FMV exemption proposed on July 5, 2006, but replaced by changes proposed on October 2, 2006
- Modified FMV exemption introduces several *additional* requirements:
 - Option cannot be exercisable prior to third anniversary of grant date
 - Shares must be listed on regulated stock exchange at time option is exercisable
 - After exercise, optionee must hold number of shares having value not lower than spread at exercise for at least five years

Global Warming: Italy




- Possible to amend outstanding options to comply with modified FMV exemption?
 - Probably, provided granted less than three years ago
 - Amend vesting schedule or restrict exercisability for three years from grant date and impose 5-year share holding requirement
 - Requires employee consent
 - Alternatively, leave it up to employees to comply (by voluntarily not exercising options for three years from grant date and not sell certain number of shares for five years)
- Consider financial intermediary rules
 - If company is restricting options to cashless exercise to avoid rules, compliance with modified FMV exemption impossible

Global Warming: Europe

- EU age discrimination legislation
 - Prohibits that employees of certain age be treated less favorably than others, unless objectively justified by legitimate aim and means of achieving that aim are appropriate and necessary
 - Impact on Equity Awards: No preferential treatment for employees based on age (e.g., accelerated vesting or longer post-termination period for employees attaining certain age)
- EU prospectus directive updates

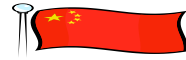


Global Warming: Asia-Pacific

-  Taiwan: Ruling on taxation of ESPPs



Global Warming: China

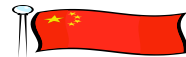


“Liberalization” of exchange control laws

- Central SAFE issued “Implementation Rules Regarding Individual Foreign Exchange Administration” on January 5, 2007
- Effective February 1, 2007
- But still waiting for implementing regulations



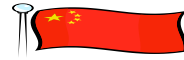
Global Warming: China



- Remittances for purchase of shares of foreign companies under equity compensation plans now possible
 - Potential ESPP participation for PRC nationals
- Prior approval of SAFE required
- Possible to file “pooled” application by one affiliate covering all affiliates in China
- Application submitted to local SAFE office (which will then correspond with Central SAFE)

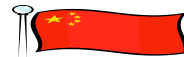


Global Warming: China



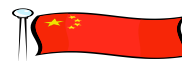
- Annual quota on conversion of RMB to USD for purchase of shares
 - Applicant will need to request as part of the application; no minimum or maximum amounts specified in the regulations
- Need for dedicated foreign exchange account to manage inward and outward flow of currency attributable to PRC participants
 - Preliminary guidance: Sales proceeds must also be repatriated through account

Global Warming: China



- Applications under “pilot test program” currently in process for handful of U.S. issuers
- Will approval requirement apply to options (even if restricted to cashless) and RSUs?
- Other requirements?

Global Warming: China



- Individual currency remittance/conversion limit increased from \$10,000 to \$50,000
- **But:** No real improvement because \$10,000 was per-transaction-limit, while \$50,000 limit is annual limit

Global Warming: India



- New Fringe Benefit Tax (FBT) for equity awards introduced by 2007 Finance Bill
 - Enacted on May 11, 2007, but effective as of April 1, 2007
- Prior Rule:
 - Employee tax at exercise (option), vesting (RSU), purchase (ESPP)
 - Tax-qualified treatment for grants made under Guidelines
 - Tax deferred until sale
 - Capital gains treatment
- No employer-paid tax

Global Warming: India



- New Rule:
 - No employee tax
 - FBT (employer-paid tax) due at exercise (options), vesting (RSUs), purchase (ESPP) at rate of 33.99%
 - Tax-qualified Guideline treatment no longer applicable
 - FBT can be transferred to employee

Global Warming: India



- Questions:
 - Does FBT apply to grants made by a U.S. company to employee of an Indian subsidiary?
 - How can FBT be transferred to employee?
 - For outstanding grants
 - For future grants
 - How is FBT calculated and paid?
 - Advance tax paid on a quarterly basis
 - Need to estimate exercises/vesting/purchases for the entire year

Questions?

Thank you for your participation



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