

Why have long-term incentives?

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Three questions

Q1: How many of you consider your annual bonus plan to be highly valued by executives and a driver of behaviour?

Three questions

Q2: How many of you consider your long-term incentive plan to be highly valued by executives and a driver of behaviour?

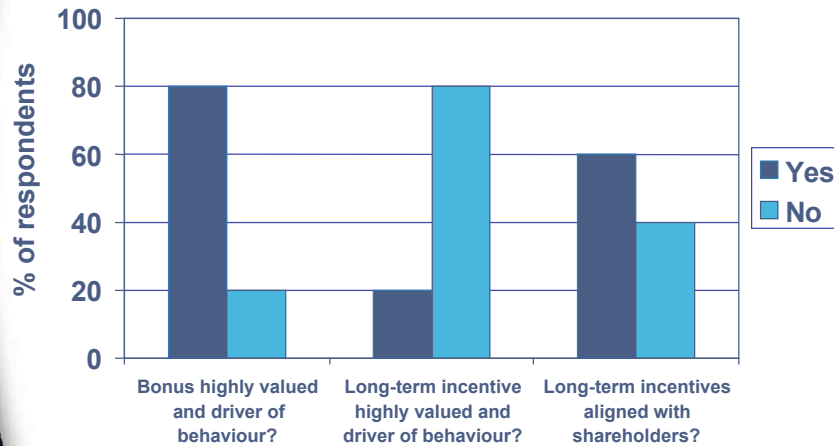


Three questions

Q3: Do you think that your long-term incentives are well aligned with shareholder outcomes?



Three questions



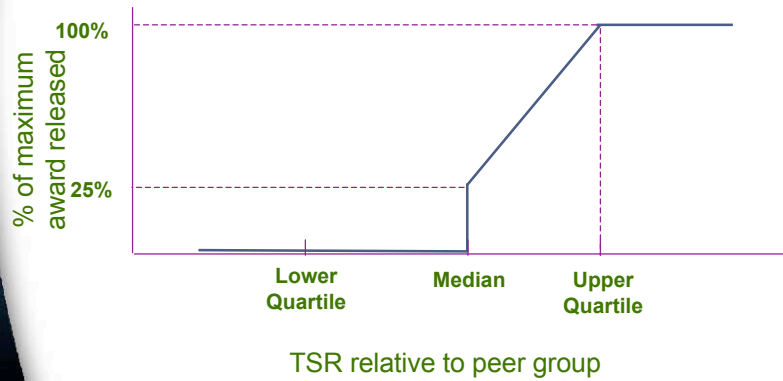
Source: very unscientific informal client survey

Issues with long-term incentives

- Generally high degree of dissatisfaction with LTIs
- Frustrations over:
 - Perceived poor connection with actions
 - Lottery-type nature
 - Low levels of understanding
 - Perceived governance constraints
- Should we have long-term incentives at all?
- Is there a better way of designing them?

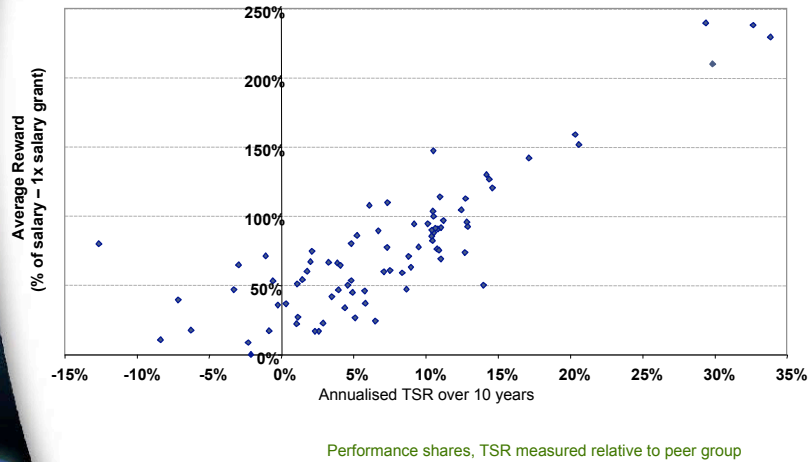
Alignment with shareholder value

- Typical TSR measure



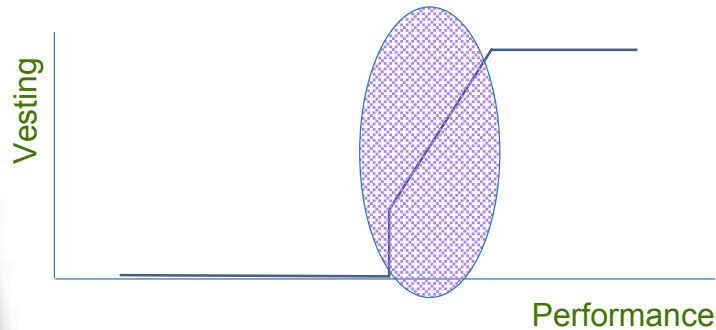
Alignment with shareholder value

Reward versus Performance over 10 years
- Traditional TSR Measure



Alignment with shareholder value

- Problems with out-performance philosophy



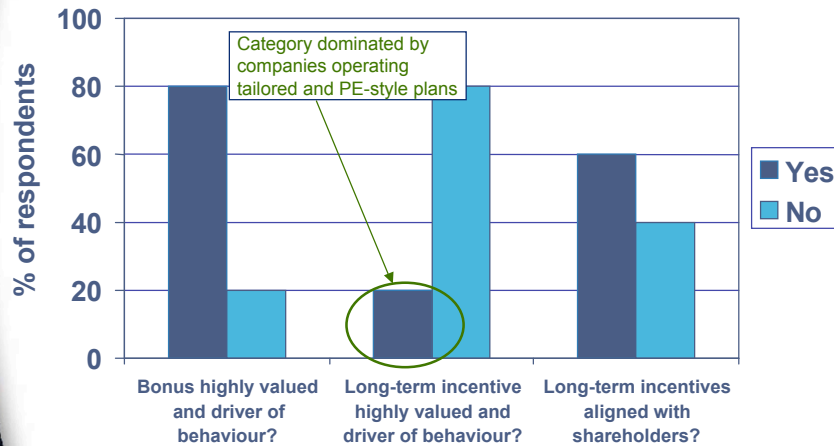
- Zone of discrimination too narrow
- Rewards volatile rather than sustained performance

Why have long-term incentives?

- Alignment
- Motivation
- Retention
- Wealth accumulation
- Market competitiveness

- ...but not clear that traditional models are delivering anything but the last of these
- How could things be better?

Private-equity style plans



Source: very unscientific informal client survey

Private-equity style plans

- WH Smith, J Sainsbury, Cable & Wireless etc
- Significant upside, with concentrated quantum
- Measures tailored to business transformation
- Non-standard periods / pay-out profiles
- Co-investment often a feature

Private-equity style plans

- Are they effective?
- [Some initial evidence to be presented]



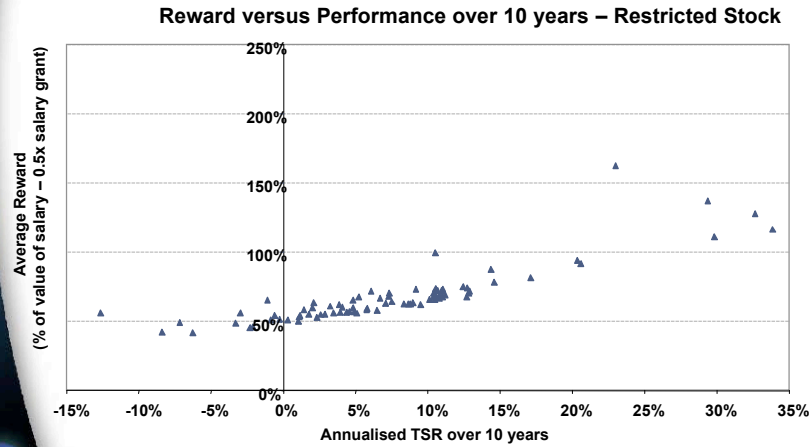
Alternative reward structures

- Is PE-style reward always the answer?
- Risk profile not for all executives
- Could encourage excessive risk-taking within company
- In strongly performing company in stewardship, there may be a lack of clear agreed strategic timeframe
- Concentrated reward may cause unhealthy focus on fixed timeframes



Alignment with shareholder value

- Is holding stock better than performance conditions?



An alternative model (for example!)

	Traditional design	Alternative design
Base salary	€800,000	€800,000
Bonus	150% of salary, 33% deferral	200% of salary 50% deferral
LTI	300% of salary maximum TSR / EPS scale	None
Restricted stock	None	150% of salary pa
Pension	40% of salary	None
Shareholding requirement	100% of salary	350% of salary
Total value	c. € 3m	c. €3m

Where does this leave us?

- Simplification
- Tailoring to business needs
- Lessons from private equity
- Increased focus on shareholding rather than complex performance conditions to achieve alignment
- Improved communication

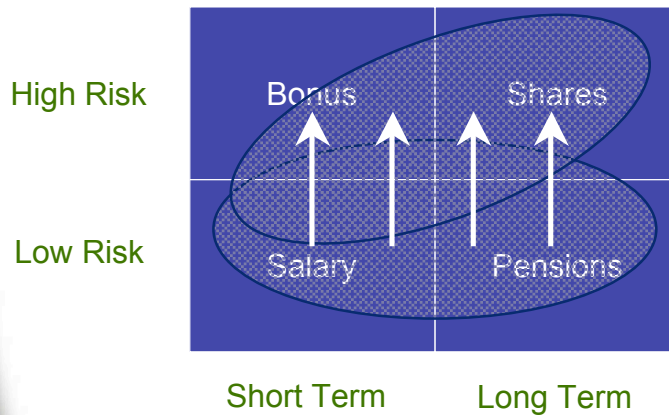


Wealth creation and capital accumulation

- Growth in incentive opportunities
- Toughening performance requirements
- Increased company equity exposure
- Move towards defined contribution pensions



Wealth creation and capital accumulation

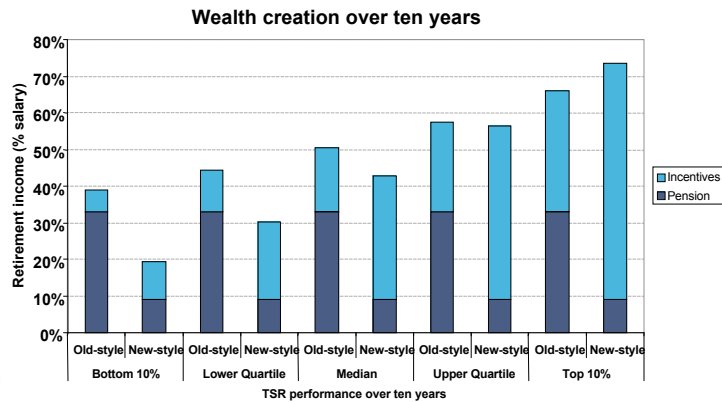


Wealth creation and capital accumulation

% of salary	Old-Style	New-Style
On-target Bonus	30% of base	60% of base
LTI	100% of base	200% of base
Pension	1/30 th DB accrual	30% of base DC

- Suppose all LTI and Pension saved
- Consider wealth created over 10 year career as board member

Wealth creation and capital accumulation



- Only for upper quartile performers do enhanced incentives replace the lost value of moving away from defined benefit pensions

Where does this leave us?

- Long-term incentives often not meeting needs of either company or executives
- Current middle ground arguably not working
- Case for move to one-off tailored arrangements (PE-style)...
- ...or move to bonus model, combined with stock-ownership to deliver alignment

Questions?

Thank you for your participation

