

Trends & Challenges in Equity Compensation in Asia

GEO Hong Kong Chapter Meeting

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Topics Covered

- Hong Kong
 - Alternatives to Stock Option Plans
 - Decrease in Grant Sizes
 - Infrequent Grant Patterns
- Mainland China
 - Local Firms: Performance-based Plans
 - Multinational Companies: More Compliance Procedures
 - Challenges
- Taiwan
 - The demise of "profit-sharing" stock?
 - What's next?
- Japan & India
 - Restricted Stock (Japan)
 - Fringe Benefits Tax (India)
- Summary

Trends: Equity Vehicles

Alternatives to stock options are proliferating



- There are a growing number of companies adopting full value share vehicles (including the 29 companies listed at right)
- A growing number of companies are also using performance metrics in their LTI plans (including the 14 companies listed below)
- But, there are challenges:
 - No treasury shares
 - Grants to directors constitute a connected transaction
 - Tax deductibility issues

Hong Kong Companies using Full Value Share Incentives

AMVIG	Hopewell Holdings	Pacific Andes
Asia Satellite	HSBC	Pacific Basin Shipping
ASM Pacific Technology	Johnson Electric	PCCW
BYD	Ju Teng	SMIC
China Insurance	Lenovo	Stella International
China Vanguard	Li Ning	Techtronic
Foxconn International	Meadville Holdings	Walker Shop
HKC	Moiselle	Wing Hang Bank
HKEx	Next Media	ZTE
Hopewell Highway	Noble Group	

Hong Kong Companies using Performance Metrics in Equity Incentives

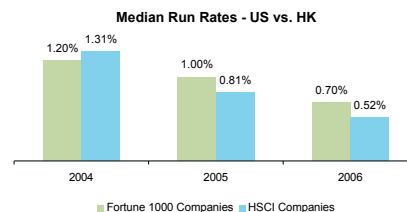
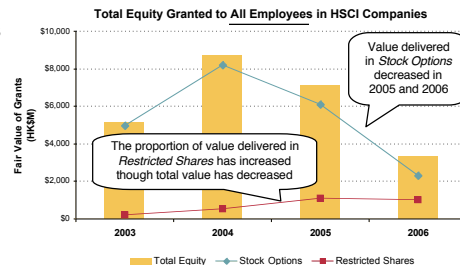
Beijing Enterprises	Hang Seng Bank	Link REIT
China Mengniu Dairy	HKEx	Sa Sa
China.com	HSBC	Solomon Systech
Clear Media	i-CABLE	ZTE
CLP	Lenovo	

Trend: Grant Size

Total grant sizes have recently decreased



- In 2005, new accounting regulations were introduced that require option grants to be expensed
- The decrease in option value granted was somewhat offset by an increase in value delivered to employees through full value restricted shares
- Internationally, stock options remain common for top-level executives though eligibility has narrowed
- Number of options granted as a percentage of total outstanding shares remains modest when compared to the US



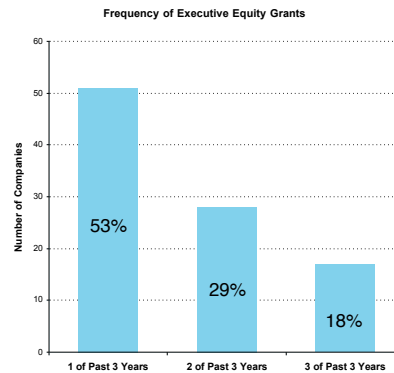
Note: Data from Equilar and Watson Wyatt Database of Directors' Remuneration

Trends: Grant Frequency

Equity incentive grants from analyzed HSCI companies remains discretionary



- Approximately 50% of HSCI companies made equity grants in the three-year period from 2004 to 2006
- Among those companies, only 18% made equity grants to executives in each of the three years
- Internationally, most companies make annual grants
 - To provide continuous retention as well as performance incentives
 - To reduce the risk for participants, mitigate the possibility of windfall payouts, and avoid the unattainable goals due to chance market timing
 - That are often smaller and less volatile in relation to size, therefore allow the investors to better estimate the cost and dilution impact



Hong Kong: In Summary



- Declining option grants (in terms of eligibility and grant sizes)
- Moderate increase in restricted shares & performance shares - but beset with regulatory hurdles
 - No treasury stock & need to establish a trust
 - Connected transactions & grants to directors
 - Complications on tax deductibility of stock awards that use newly issued shares (even though there is an accounting expense!)
- No all-employee stock purchase programs among companies listed exclusively in Hong Kong

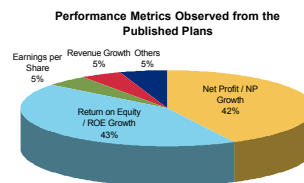
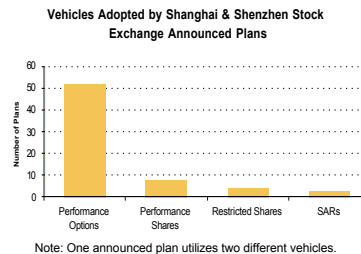


Trend: Local Firms

Performance plans are the dominant type for domestically listed companies



- By late January 2008, we identified 171 companies making announcements on equity incentive related issues and 66 published plans
 - Most of the published plans are performance based
 - Net Profit and Return on Equity are the most commonly used metrics
- Seems to be driven by regulatory requirements
 - Nearly 1/3 of the published plans have performance conditions attached to both grant and vesting



Trend: Multinational Companies

More compliance procedures are required as new regulations were promulgated



- For Stock Option Plans ("SOP")
 - File initial foreign exchange quota and application for opening the special account with the **local** SAFE
 - Register with local tax bureaus ("LTB")
 - Report each grant under SOP to the LTB
 - Use the registered special account for fund transfer
 - For Employee Stock Purchase Plans ("ESPP")
 - File initial foreign exchange quota and application for opening the special account with the **central** foreign exchange control authorities (State Administration of Foreign Exchange, "SAFE")
 - Use the registered special account for fund transfer
- ↓
- Recent NASPP survey:
 - 55% of Cos. impose mandatory cashless exercise (45% do not)
 - No longer necessary in light of regulatory changes
 - 11% of Cos. operate an ESPP
 - This figure likely to increase somewhat



Mainland China: Challenges



- State-owned Assets Supervision and Administration Commission (“SASAC”) is planning to make more specific requirement on plan design features for State Owned Enterprises (“SOEs”)
 - Performance metrics should apply to both grant and vesting
 - Realizable gain to be capped at 50% of total compensation
- The new Labor Contract Law may bring new complication to the process of implementing equity incentive plans, especially that of ESPP
 - The law requires significant matters in direct relation to remuneration be discussed at the workers' congress or by all the workers
- Equity incentive plan design needs to take a total reward approach and pay close attention to the pay mix of the whole compensation package
 - Under current regulatory framework, equity award with huge realizable gain disproportional to other compensation elements could “motivate” executives to resign to “cash-in”

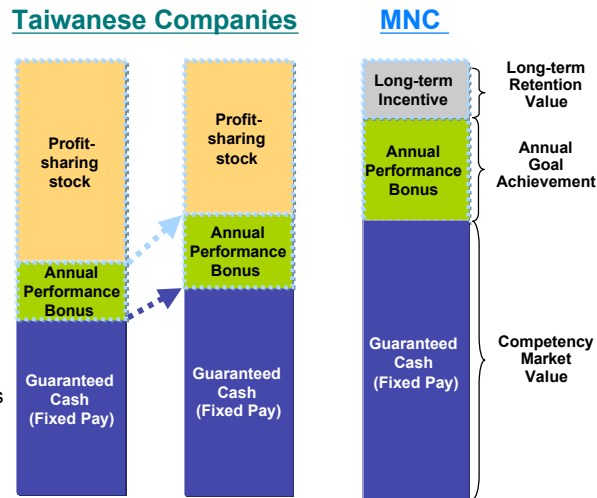


Trends: Profit-sharing Stocks

The historical prevalent usage of profit-sharing stocks will likely decline



- In the past, stock-settled profit sharing plan are commonly used in Taiwan, especially by those high-tech companies
 - X% of profit is allocated (5-10%)
 - Converted into shares at par (NT10)
- From 1 January 2008, companies should follow international accounting standard
 - Treat the fair value of the profit-sharing stocks as expense
 - Thus there will likely be a substantial reduction in this practice



Trends: Japan & India



- Stock option is still the most prevalent tool
 - Option is first introduced only 13 years ago (1995) by Sony
- Pace of increasingly using options is slowing down
 - Due to expensing requirement under accounting rules
- Move towards “Restricted Stock”
 - In form of deeply discounted options (exercise price of 1 Yen)
 - Less generous retirement benefit, more in restricted stock
- There will likely be a reduction in use of stock compensation due to the Fringe Benefit Tax (“FBT”)
- FBT is having major impact on stock plans in India
- Tax is being shifted from employee to employer
- Likely reduction of grant sizes and / or move to cash-settled payments



QUESTIONS?

**Thank you
for your interest in GEO**

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