

Long-term Incentives vs. Short-term Incentives

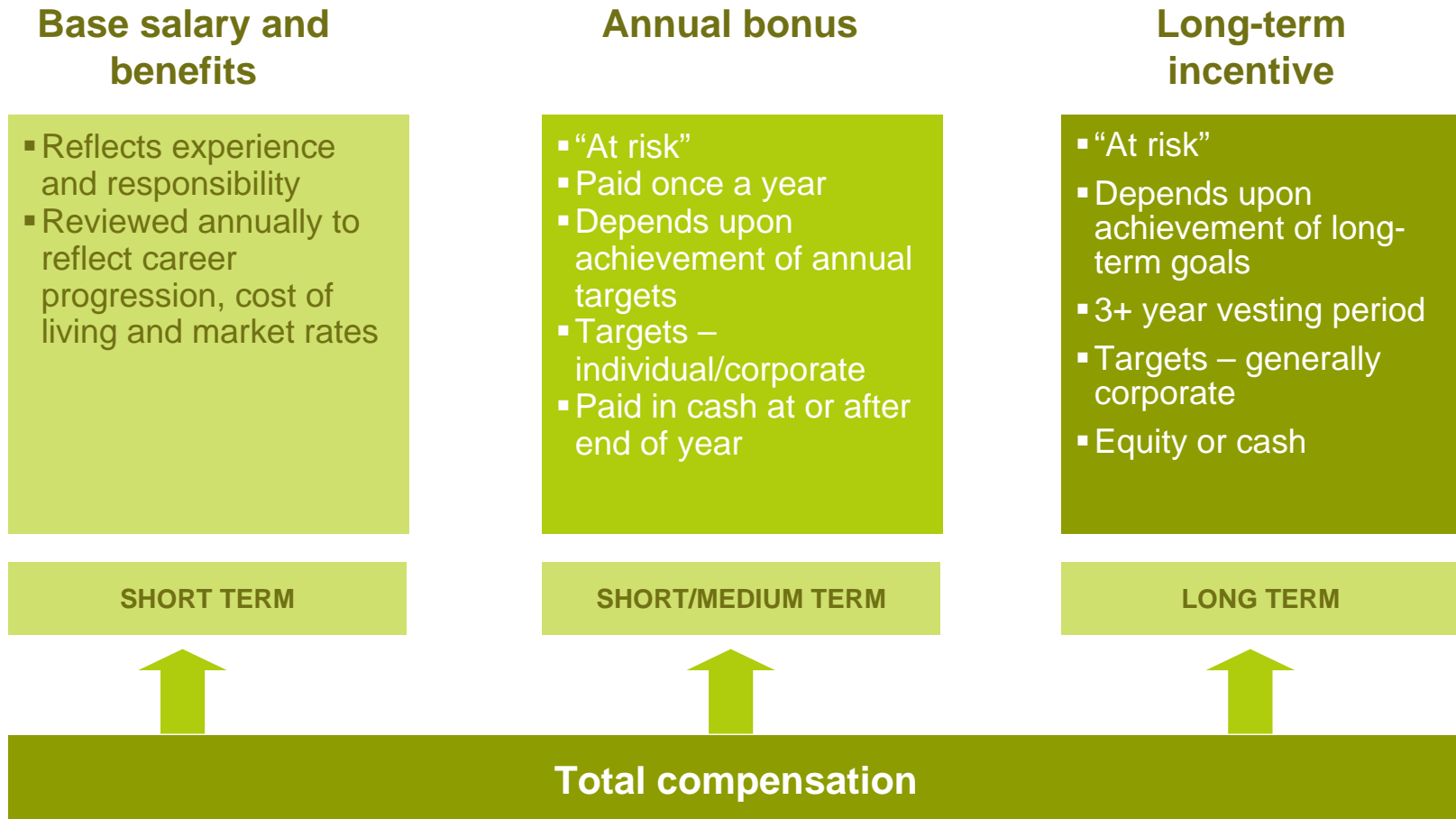
Stephen Quick
Director
Human Resource Consulting

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Long-term Incentives vs. Short-term Incentives

- Defining long-term and short-term
- Why provide long-term incentives?
- Typical Long-term Incentive Plan (LTIP) design
- Use of LTIPs by companies - some statistics
- Implementing an LTIP
- The future

Defining long-term and short-term



Why provide long-term incentives?

The business case: to encourage executives to deliver on strategic business objectives



Typical LTIP design

Share-based	Cash-based	
<p>Options, restricted shares, restricted stock units</p>	<p>Phantom options, stock appreciation rights</p>	
Strategic HR considerations		
✓	Sense of ownership	X
✓	Investor risk for executives	X
X	Protection for shareholders from dilution	✓
Practical considerations		
X	Simplicity of implementation	✓
X	Ease of communication with executives	✓
✓	Cash and accounting costs	✓

Use of long-term incentive plans in Russia

Major Russian companies *

- 47% have implemented LTIPs
- Average face value at grant as a percentage of base pay is 100%
- 47% of Russian companies provide LTIP to top management
- 24% of Russian companies provide LTIP to middle management

FTSE 100 listed UK companies**

- All have LTIPs of one form or another – at least one for each company will generally be share-based
- Face value at grant as a percentage of base pay is often 200% - 300%
- All companies provide LTIP to top management and almost all to middle management

**PwC Top Management Survey: 2007. The Survey contains analyses of 34 major Russian companies.*

***PwC Executive compensation FTSE 100 Review of the year 2007.*

Use of long-term incentive plans in Russia - Finance Sector as an example*

Russian financial companies

- 17% provide LTIPs to employees
- 11% are planning introduce LTIP next year

Foreign financial companies operating in Russia

- 45% provide LTIPs to employees
- Average face value at grant as a percentage of base pay is 75%

Employee eligibility for LTIPs:

	Russian Companies	Foreign Companies in Russia
	%	%
Top management	17%	45%
Middle Management	17%	38%

*PwC Financial Sector Compensation Survey: 2007. The Survey contains analyses of 80 finance companies in 49 Russian cities.

Implementing a LTIP – issues to address

Russian company

- No history of employee share ownership: practical and legal issues
- Cash plans
- Specific legal structuring often used, depending on plan design
- Labour law

Foreign company plan

- Similar issues to Russian company
- Restrictions on Russian nationals holding foreign shares now lifted
- Consider:
 - Currency restrictions
 - Corporate tax deductibility
 - Limits on value of securities used
 - Securities law – offerings of new issue foreign company shares
 - Labour law

Implementation an LTIP in developing markets - experience of Russian companies

To help ensure success:

- Goals and main parameters of plan:
 - establish early
 - agree with key stakeholders e.g. shareholders and/or management at initial stage of plan development
- Structuring of plan:
 - balancing interests/risks of company and participants
- Consideration of all aspects before final approval of plan design
 - financial costs, legal, tax, accounting, practical etc
- Communication and education of executives
 - how plan works
 - value of plan
 - “line of sight” – performance conditions, share price

The future

Some speculation

- Market trends and global job market - more companies likely to implement LTIPs:
 - market trends
 - increasingly global recruitment market
 - IPOs of companies
- Increased sophistication of performance conditions
- Development of Russian legislation to ease LTIP implementation
- Link with short/medium-term plans
 - deferred bonuses

Contacts



William Schofield, Partner
William.Schofield@ru.pwc.com
+7 (495) 967-6460



Stephen Quick, Director
Stephen.Quick@ru.pwc.com
+7 (495) 967-6040



Natalia Akhmina, Manager
Natalia.Akhmina@ru.pwc.com
+7 (495) 967-6177



Olga Shestakova, Manager
Olga.Shestakova@ru.pwc.com
+7 (495) 223-5119