

FREDERIC W. COOK & CO., INC.

FVAT

FAIR VALUE TRANSFER

*Measuring the Costs of Aggregate Long-Term
Incentive Grant Practices*

AUGUST 2008

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We are pleased to present our fourth survey of aggregate fair value transfer (“FVT”), measuring the total value transferred from shareholders to employees through grants of long-term incentive compensation. Our research of 240 companies, spread across four broad industry sectors, revealed that aggregate FVT rates leveled off in 2006 and 2007 following previous declines from 2003 to 2005. In the following pages, we present a detailed explanation of our analysis, along with other key findings.

BACKGROUND

With ever increasing focus on executive compensation levels, it is vital for compensation committees and Boards of Directors to ask themselves:

- What should we be spending, in the aggregate, on long-term incentive grants?
- What total equity usage is competitive for a company of our size and in our industry?

Compensation committees traditionally answered these questions in two ways. The first method was to compare the company’s annual share usage rate measured as a percentage of average outstanding company shares, i.e., the “run rate” or “burn rate,” against those of its peers or general industry practices. The second was to look at the company’s “overhang,” i.e., the number of shares represented by outstanding grants and available shares remaining for future grants as a percentage of fully diluted company shares at year end, also versus peers or general industry practices.

These traditional approaches were appropriate when most companies’ long-term incentive grants consisted largely of stock options. With the release of the Financial Accounting Standards Board’s (“FASB”) accounting mandate for stock option expensing, known as “Statement 123R, Share-Based Payment” (“FAS 123R”) in 2004, companies were forced to rethink their evaluation methods. Starting with fiscal years beginning after June 15, 2005, companies have been required to record an income statement expense for stock options, along with all other equity awards. As a result, stock options are no longer considered “free,” and other grant types now have a level playing field.

This led to a shift away from long-term compensation programs consisting solely of stock options to programs using portfolios of several different types of equity and cash award vehicles. Share usage and dilution analyses have taken a backseat to the more important question of how to best award long-term incentive value in a competitive and cost-effective manner.

OUR ALTERNATIVE: FVT

In order to more accurately evaluate the aggregate cost of long-term incentive programs, we encourage our clients to examine the company's annual FVT, which measures the aggregate grant value and potential cost of long-term incentive ("LTI") compensation awards for a given fiscal year.

The FVT method:

- Measures the aggregate pre-tax compensation cost of grants made in a given year (the cost of which will likely be spread over multiple years for profit and loss purposes)
- Facilitates trade-offs between various LTI vehicles since all award types are expressed on an economically equivalent basis
- Provides a better way of comparing the proportionate costs of various grant types in an option-expensing environment
- Differentiates the dilutive impact of various grant types, i.e., recognizes that an option has less immediate dilution than a full value share

For comparisons across companies, annual FVT can be measured as a percentage of a company's total market capitalization or as a percentage of an internal financial measure, such as revenue or net income.

The benefits of measuring FVT as a percentage of market capitalization / revenue are:

- Allows comparisons to be made across companies to assess competitiveness and reasonableness of a given company's aggregate LTI budget
- Eliminates distortion from stock price fluctuation, especially for companies establishing grant guidelines based on competitive LTI values
- Is generally consistent with the way investor advisory groups, such as RiskMetrics (formerly known as Institutional Shareholder Services ("ISS")) and Glass Lewis, primarily assess the reasonableness of company aggregate grant practices and new share authorizations
 - RiskMetrics recognized the issues associated with traditional measures of potential dilution long ago and switched its primary methodology for evaluating the reasonableness of new share authorization requests from traditional potential dilution to shareholder value transfer ("SVT"); SVT measures outstanding and potential grant value as a percentage of market capitalization
 - Although similar in concept to RiskMetrics' SVT calculation, our FVT analysis focuses on annual usage (as opposed to total potential dilution), and uses a different valuation methodology
 - Coincidentally, following the publication of our inaugural FVT survey in 2005, RiskMetrics added a similar value-based test for analyzing annual usage; RiskMetrics' burn rate test applies a multiplier to full-value awards to recognize their greater economic costs over stock options. This multiplier is based on a company's historical share price volatility
 - Glass Lewis examines the annual accounting cost of long-term incentive awards as compared to income statement line items, a methodology similar to our FVT analyses

The implementation of the revised Securities and Exchange Commission executive compensation disclosure rules for fiscal years ending after December 15, 2006, added to the focus on the economic value of equity awards granted to named executive officers. In the Grants of Plan-Based Awards table of the proxy statement, companies are required to disclose the grant-date fair value of each stock option and other equity award, as well as cash-denominated LTI awards, made to each named executive officer. Though this information is presented on an individual as opposed to aggregate basis, these rules confirmed the importance of considering equity award value.

METHODOLOGY

FVT measures the pre-tax “fair value” of equity awards granted during the year. For the purposes of this report, pre-tax fair value of equity awards was calculated for the most recent three fiscal years available using each company’s Form 10-K disclosure, supplemented with information from proxy statements as necessary. Year 2007 data is defined as any fiscal year ending during the 12 months ended February 29, 2008.

Fair value is calculated as follows:

- Options are valued using the weighted-average fair value of options granted during the year. If fair value was not disclosed in public filings, it was calculated using the Black-Scholes option pricing model and the company’s reported FAS 123R input assumptions
 - Restricted shares are valued at fair market value on grant date
 - Performance shares are valued at grant date fair value; cash-based LTI awards are valued at grant date target value
- Note: if aggregate data for restricted shares, performance shares, or cash-based LTI awards are not disclosed, aggregate grants made to the named executive officers disclosed in each company’s proxy statement are used, under the assumption that these executives received the majority of the awards

FVT as a percentage of market capitalization is calculated using an approximation of the weighted-average market capitalization at the time the grants were made:

$$\text{FVT \%} = \frac{\text{Pre-Tax Fair Value of Equity Awards Granted During the Year}}{\text{Weighted-Average Market Capitalization}}$$

AN EXAMPLE CALCULATION OF FVT IS SHOWN BELOW:

Options Granted	1,000,000
Weighted-Average Exercise Price	\$100.00
Weighted-Average Fair Value of Options	\$25.00
<i>Aggregate Pre-Tax Fair Value</i>	<i>\$25,000,000</i>
Restricted/Performance Shares Granted	200,000
Weighted-Average Grant Date Fair Value	\$100.00
<i>Aggregate Pre-Tax Fair Value</i>	<i>\$20,000,000</i>
<i>FVT</i>	<i>\$45,000,000</i>
Weighted-Average Basic Shares Outstanding	50,000,000
Weighted-Average Market Capitalization	\$5,000,000,000
<i>FVT % of Market Capitalization</i>	<i>0.90%</i>

A simple example illustrates the need to focus on the fair value of LTI awards, highlighting the fact that while one stock option and one share of restricted stock are comparable on a share usage / run rate basis, they are clearly different in terms of value. The example below shows that granting half the number of option shares as restricted stock reduces the run rate, but actually doubles the FVT and the amount being “spent” by the company:

ASSUMPTIONS:

Shares Outstanding	100,000
Stock Price	\$10.00
Black Scholes % of Stock Price	25%

	Stock Options	Restricted Shares	Change
Number Granted	1,000	500	-50%
Run Rate	1.00%	0.50%	—
Pre-Tax Value	\$2,500	\$5,000	+100%
Fair Value Transfer	0.25%	0.50%	—

METHODOLOGY

RESEARCH SAMPLE

To identify patterns in FVT rates among companies of different sizes and industry sectors, we selected 240 publicly-traded companies based on market capitalization as of February 28, 2008 and industry classification according to Standard & Poor's Global Industry Classification Standard Industry Group codes:

	Small Cap (Mkt. Cap. < \$1B)	Mid Cap (Mkt. Cap. \$1B-\$5B)	Large Cap (Mkt. Cap. > \$5B)	Total
Financial	20	20	20	60
Industrial	20	20	20	60
Retail	20	20	20	60
Technology	20	20	20	60
Total	80	80	80	240

This year, the scope of the research was expanded to include companies in the financial services sector, along with the three sectors included in previous studies. Due to acquisitions and company growth, the list of companies was recreated from a random sample for this year's report. Recent IPOs and delinquent-filers were removed during the screening process. Approximately 30% of the companies in the most recent 2006 report are included. A complete list of the research sample is included in the *Appendices*.

Market capitalization as of June 30, 2008 and trailing four quarters' revenue for the research sample companies are as follows:

	Market Capitalization as of 6/30/08 (\$ Millions)			Trailing 4-Qtrs. Revenue as of 6/30/08 (\$ Millions)			Market Capitalization as Multiple of Revenue		
	25P	Median	75P	25P	Median	75P	25P	Median	75P
<i>Size Categories</i>									
Small	\$213	\$462	\$635	\$198	\$488	\$996	0.37	0.83	2.07
Mid	\$1,431	\$2,272	\$3,442	\$985	\$2,141	\$4,303	0.54	1.01	2.49
Large	\$6,593	\$9,611	\$19,006	\$4,460	\$9,333	\$19,888	0.73	1.14	1.93
<i>Industry Sectors</i>									
Financial	\$696	\$1,959	\$6,355	\$372	\$958	\$4,582	0.84	1.23	2.61
Industrial	\$722	\$3,212	\$7,834	\$993	\$3,434	\$6,527	0.54	0.95	1.57
Retail	\$591	\$2,035	\$6,518	\$1,520	\$3,863	\$9,221	0.38	0.55	0.77
Technology	\$733	\$2,602	\$6,355	\$396	\$1,378	\$3,262	1.05	2.23	3.62
Total Sample	\$645	\$2,272	\$6,579	\$691	\$2,285	\$6,169	0.55	1.02	2.19

The charts on the following pages summarize historical median FVT as a percentage of market capitalization results from this year's study in the aggregate and by various categories:

- By Size
 - Small, Mid, and Large Cap companies
- By Industry
 - Financial, Industrial, Retail, and Technology (“Tech”) companies

For additional comparisons, we have also shown FVT as a percentage of revenue.

The data illustrate a generally flat trend in FVT rates as a percent of market capitalization across most size and industry cuts. Small and Mid Cap and Tech companies continue to show a decreasing trend, which was seen among Large Cap companies from 2002 to 2005. Overall, the absence of the strong declines shown in our previous reports implies that companies completed most cutbacks to LTI budgets during the year before and in the first year after FAS 123R became effective. Minor downward adjustments presumably reflect compensation committees' continued awareness and responsibility for the income statement effects of their LTI programs.

Other key findings include:

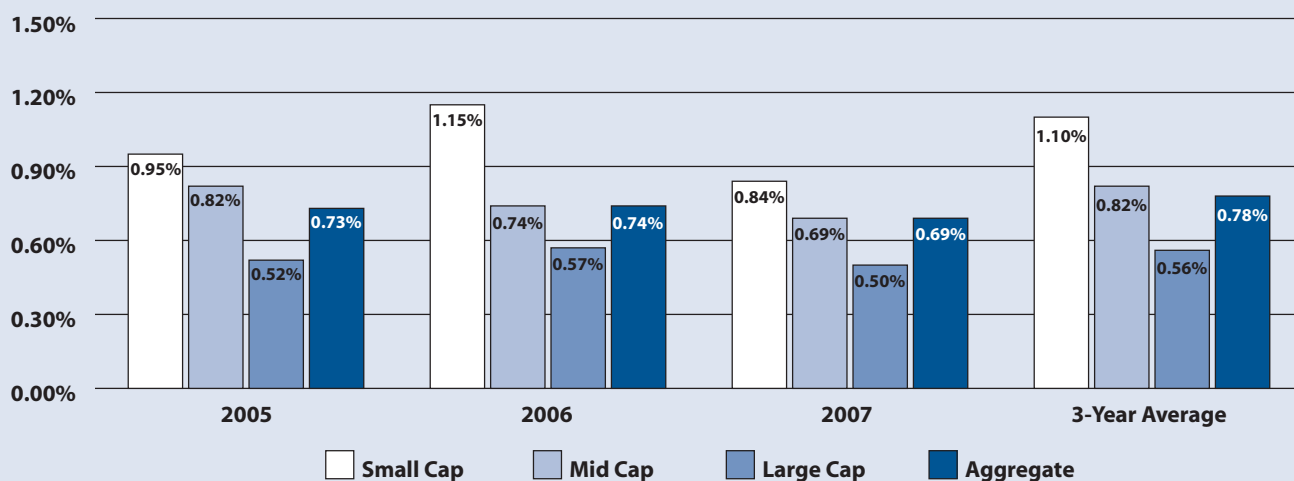
- Median share usage for the entire sample decreased from 1.6% to 1.2%, reflecting additional movement away from stock options and towards a more varied mix of LTI awards that includes full-value awards (i.e., restricted shares, performance shares, and cash-denominated performance units)
- There continues to be a negative correlation between company size and aggregate FVT granted as a percentage of market capitalization; smaller companies need to use a larger proportion of their total equity to deliver competitive compensation programs
- Tech companies continue to have significantly higher FVT than companies in other industry sectors
 - Human capital-intensive companies, such as those in the Tech industry, are expected to need larger aggregate LTI budgets as compared to asset-intensive companies, such as the Financials and the Industrials
- Financial services companies show the lowest aggregate FVT
 - Investment banks, also human capital-intensive companies, show very high FVT as a percentage of market capitalization, but they comprise only a small percentage of the financial sector sample
- FVT as a percentage of revenue is highest in the Finance and Tech sectors; this is due primarily to higher market capitalization to revenue ratios in these two sectors, and the market capitalization-based methodology for constructing the research sample

We expect that continued shareholder scrutiny of executive compensation levels and practices will force compensation committees to continue to trim both participation in equity award programs and overall equity budgets. However, absent future regulatory changes affecting long-term incentive grant practices, we expect that future market capitalization-based FVT rates will remain flat or trend slightly positive due to the combination of fixed dollar grant guidelines and decreasing market capitalizations.

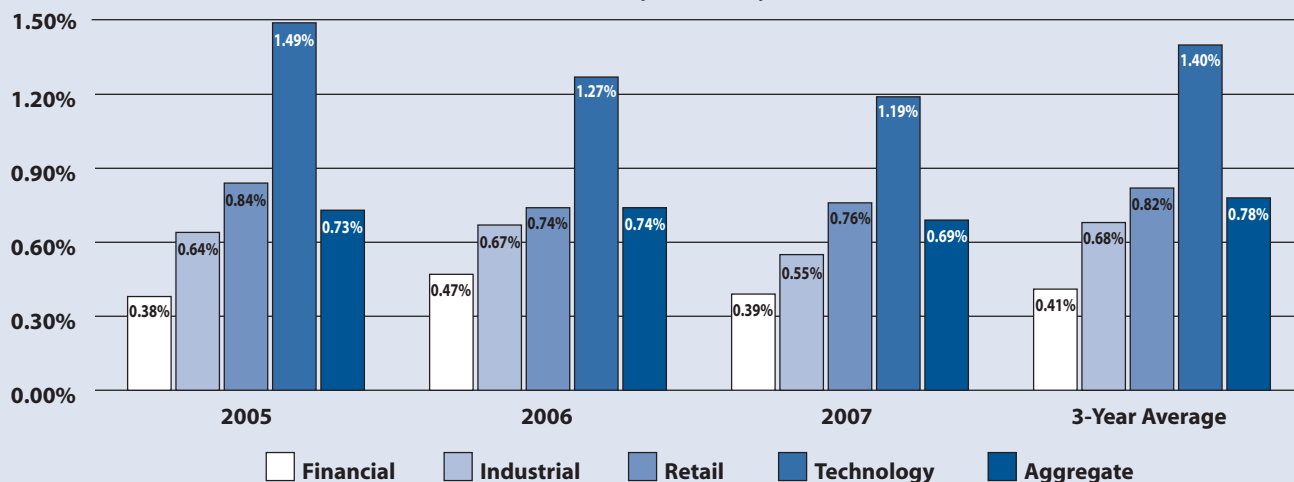
SUMMARY FINDINGS

MEDIAN FVT % OF MARKET CAPITALIZATION

By Size

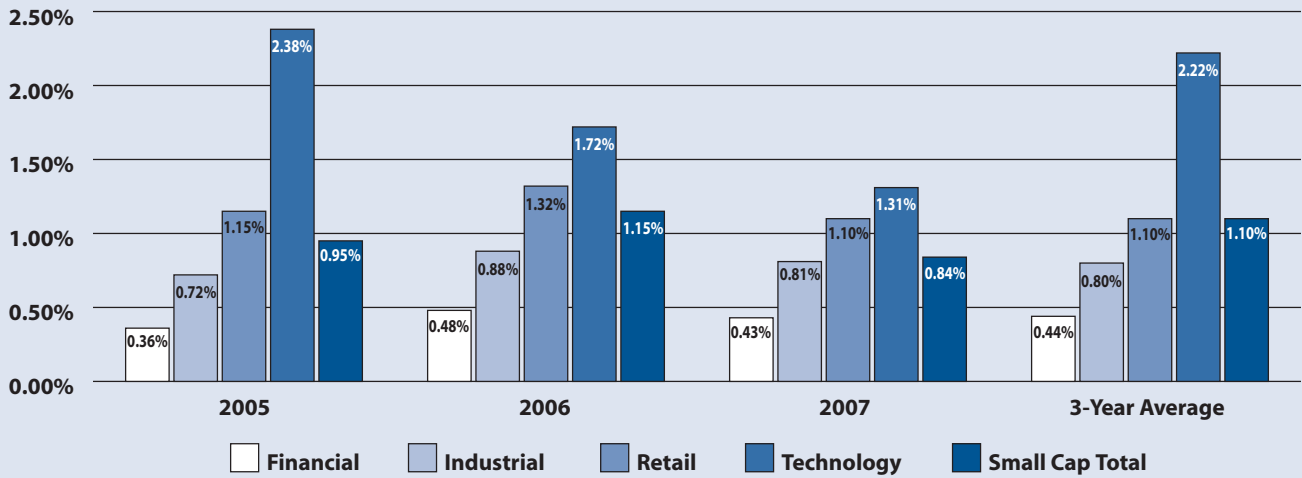


By Industry

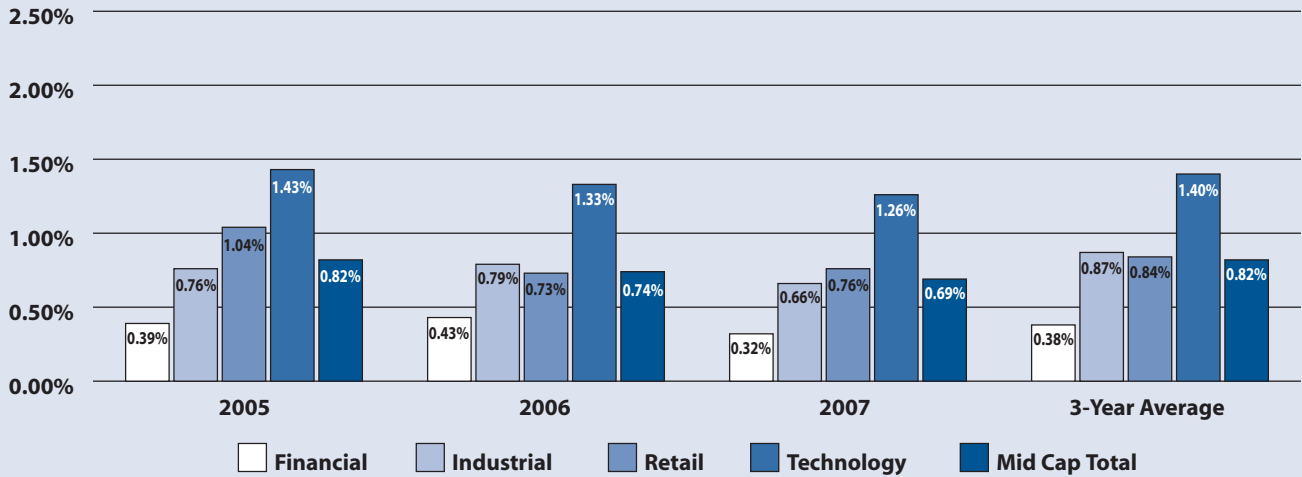


MEDIAN FVT % OF MARKET CAPITALIZATION – DETAIL BY SIZE

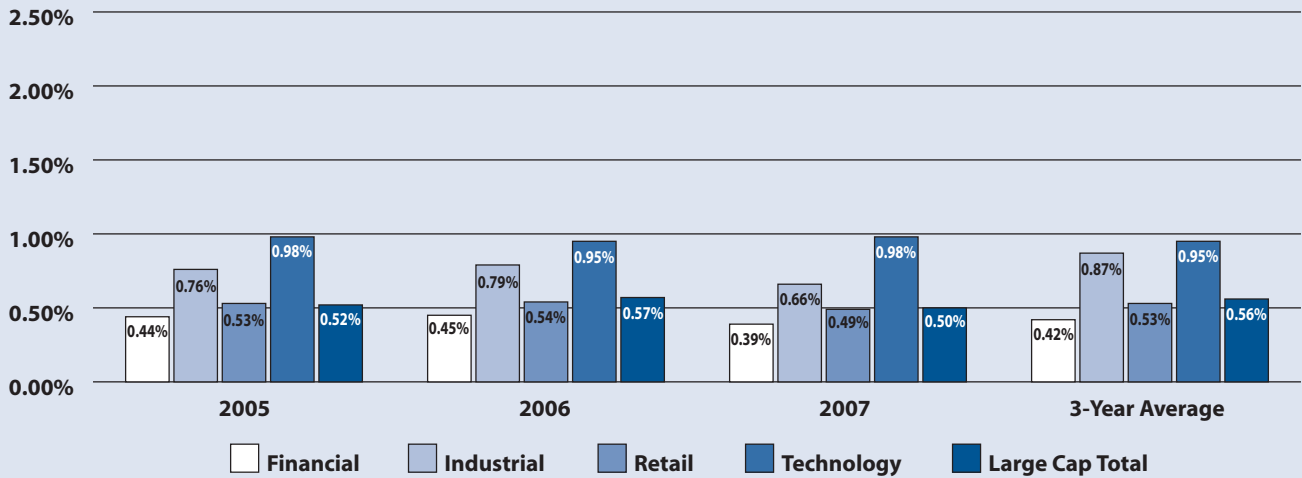
Small Cap Companies



Mid Cap Companies



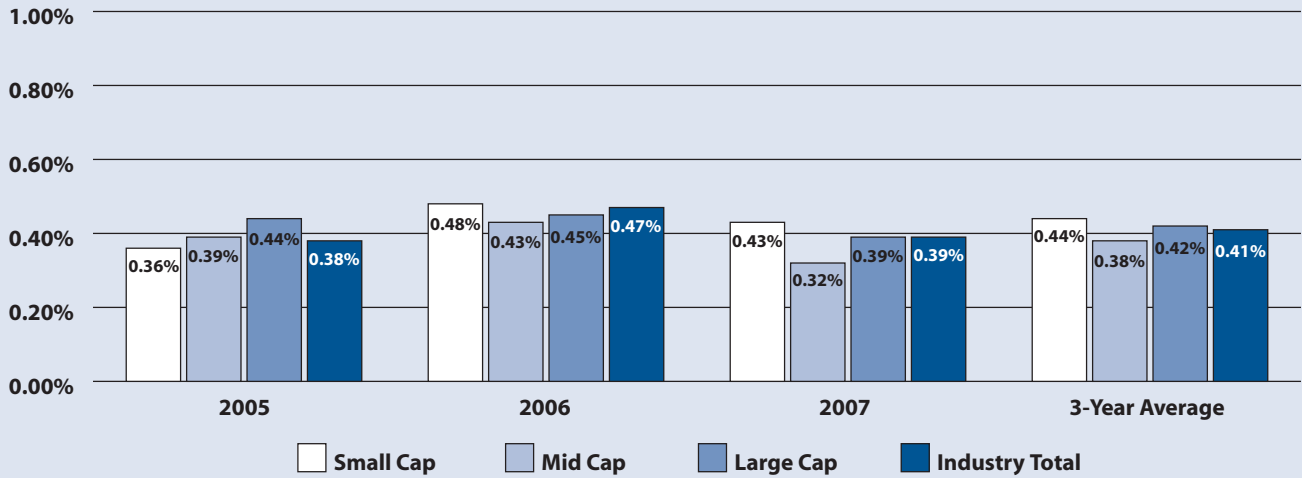
Large Cap Companies



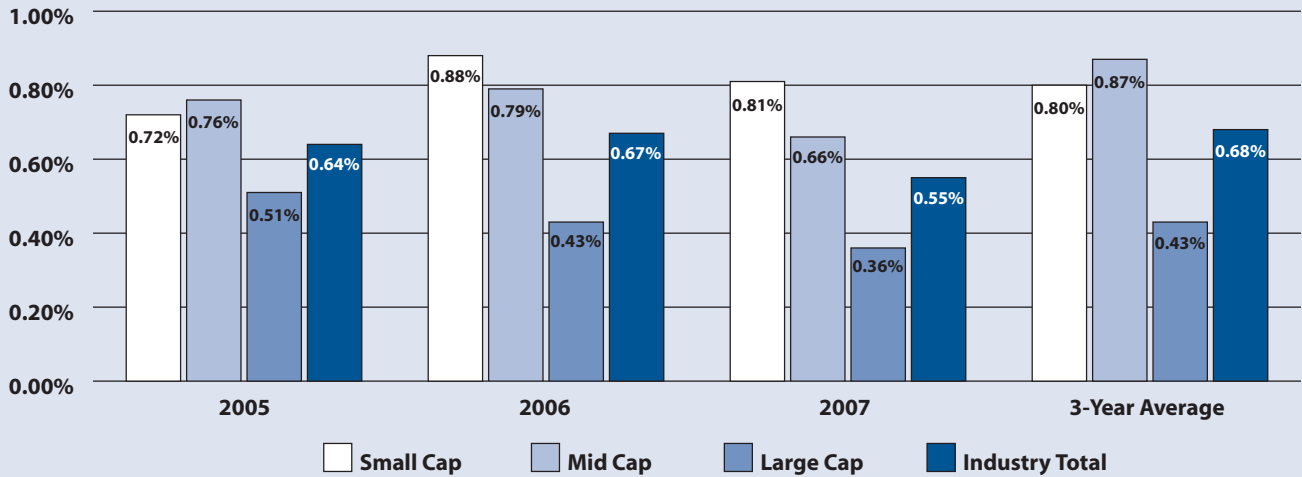
SUMMARY FINDINGS

MEDIAN FVT % OF MARKET CAPITALIZATION – DETAIL BY INDUSTRY

Financial

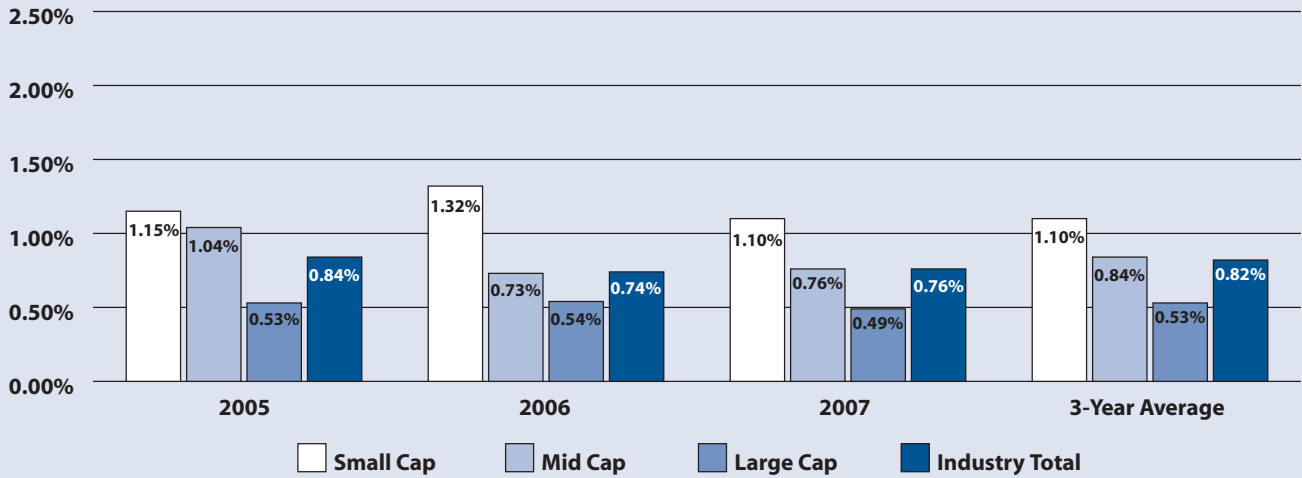


Industrial

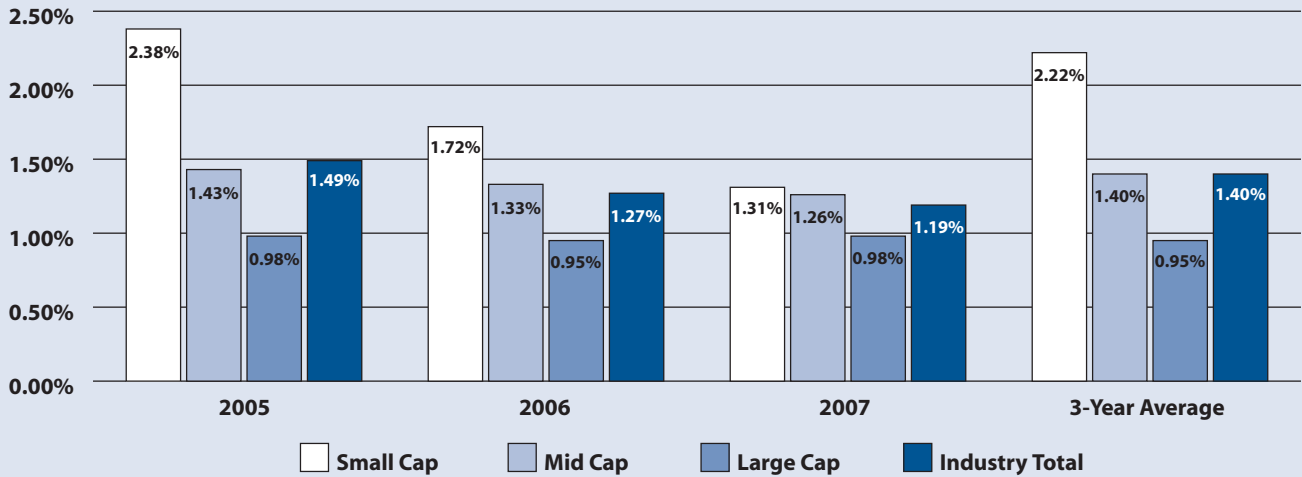


MEDIAN FVT % OF MARKET CAPITALIZATION – DETAIL BY INDUSTRY

Retail



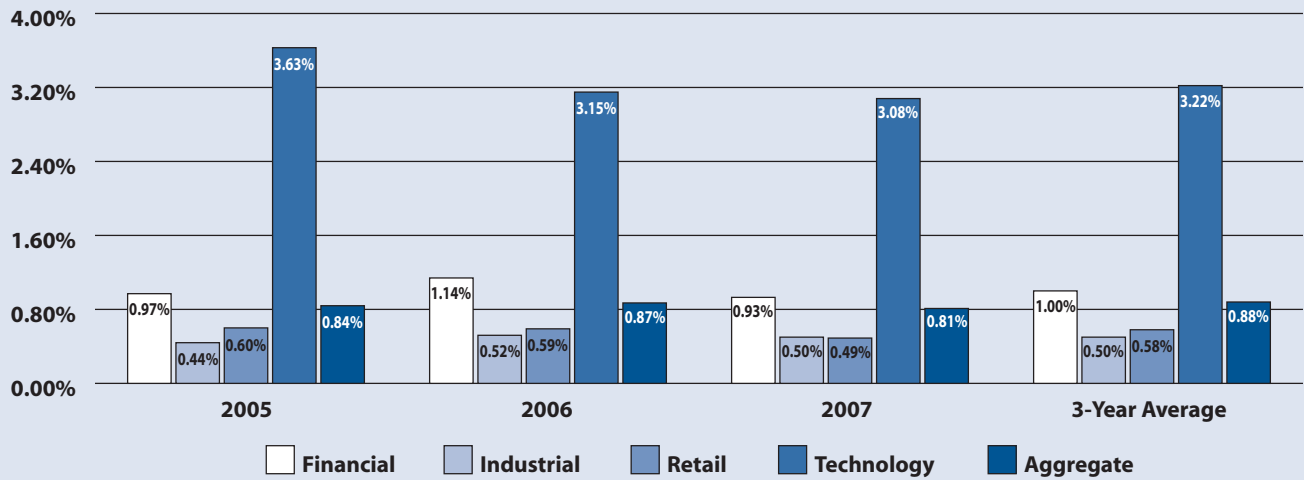
Technology



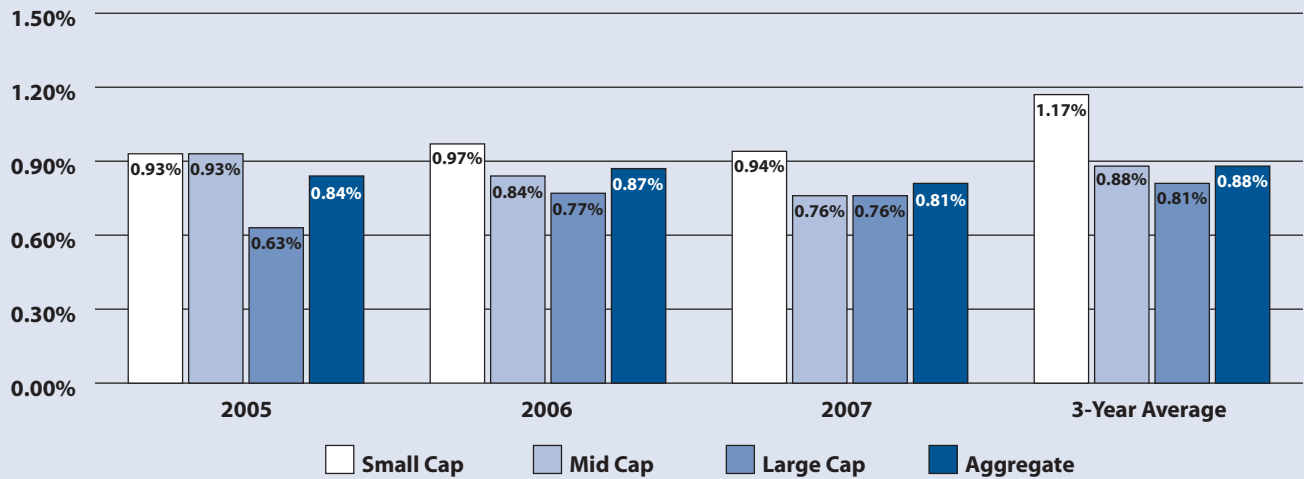
SUMMARY FINDINGS

MEDIAN FVT % OF REVENUE

By Industry



By Size



APPENDIX: RESEARCH SAMPLE COMPOSITION

3M	Cache	E-Trade Financial
A.C. Moore	CACI Intl	Expeditors Intl Of Washington
Abercrombie & Fitch	Cadence Design Systems	F5 Networks
Adobe Systems	Capital One Financial	Fairchild Semiconductor
Advance Auto Parts	Cascade Bancorp	FalconStor Software
Aeropostale	Caterpillar	FBL Financial
Affiliated Computer Services	CBIZ	Financial Federal
Alamo Group	Centennial Bank Holdings	Finish Line
Allied Capital	Cenveo	First Acceptance
Allied Waste Industries	Ceradyne	First Charter
Altera	Charlotte Russe Holding	First Defiance Financial
Amazon.com	Children's Place Retail Stores	FirstMerit
AMB Property	ChoicePoint	Fluor
Analog Devices	Cincinnati Financial	FuelCell Energy
Ann Taylor Stores	Cintas	GAMCO Investors
ANSYS	Citizens Republic Bancorp	GameStop
Aon	Citrix Systems	Gap
Apartment Invt & Mgmt	CNA Surety	General Dynamics
Applied Materials	Cognex	General Electric
Applied Micro Circuits	Cognizant Tech Solutions	Genesco
Applied Signal Technology	Coldwater Creek	Genesee & Wyoming
Argon ST	Colonial BancGroup	Genuine Parts
Arkansas Best	Comerica	Goldman Sachs
Assurant	Computer Sciences Corp	Goodrich
Atlas Air Worldwide Holdings	Conseco	GrafTech Intl
Audible	Con-Way	Greenfield Online
AutoNation	Cost Plus	Guess
AutoZone	Cree	Hancock Holding
Avery Dennison	CTS	Harris
Barnes & Noble	Cummins	Harris & Harris
BB&T	Deere & Co	Hartford Financial Services
Bed Bath & Beyond	Dick's Sporting Goods	Healthcare Realty Trust
Best Buy	Digital River	Home Depot
Big Lots	Dillard's	Hub Group
Bon-Ton Stores	Dress Barn	Informatica
Borders Group	DRS Technologies	Ingram Micro
Briggs & Stratton	Drugstore.com	Integrated Device Tech
Broadcom	Duke Realty	Intel
Brown & Brown	EDS	Internet Capital Group
Brown Shoe Co	Emcore	Iron Mountain

APPENDIX: RESEARCH SAMPLE COMPOSITION

Jabil Circuit	Oracle	Sybase
Jacobs Engineering Group	Overstock.com	Sypris Solutions
JCPenny	Pacer Intl	T. Rowe Price
Jefferies Group	Pacific Sunwear	Tanger Factory Outlet
Jo-Ann Stores	Pentair	Target
Joy Global	PetSmart	TCF Financial
Juniper Networks	Pier 1 Imports	TD AMERITRADE
Kelly Services	Plug Power	Tekelec
KLA-Tencor	PMA Capital	Tennant
Kohl's	Power-One	TIBCO Software
Lam Research	Presidential Life Corp	Tiffany & Co
LandAmerica Financial	Priceline.com	Timken
LaSalle Hotel Properties	ProLogis	TJX Cos
Legg Mason	PS Business Parks	Tompkins Financial
Lexmark Intl	Quanta Services	Tractor Supply
Limited Brands	Quantum	Trane
Lincoln National Corp	RadioShack	Travelers Cos
Lowe's	Radyne	Trimble Navigation
LSI	Regal-Beloit	TTM Technologies
M&T Bank	Resources Connection	UAP Holding
Mack-Cali Realty	Rimage	Umpqua Holdings
Macy's	Robert Half Intl	Union Pacific
Markel	Rockwell Collins	United PanAm Financial
MAXIMUS	Ross Stores	United Rentals
McDermott Intl	RR Donnelley	Urban Outfitters
Mentor Graphics	Ryder	URS
MetLife	Saia	Valley National Bancorp
Mettler-Toledo Intl	Saks	Wabash National
Micron Technology	Sherwin Williams	Walter Industries
Midas	Sigma Designs	Washington Banking Co
Molex	SkyWest	Washington Mutual
MPS Group	Sonus Networks	Waste Connections
MSC Software	SourceForge	Waste Management
National City	Sovran Self Storage	WebSense
NetApp	SPX	Wells Fargo
Netflix	StanCorp Financial	Whitney Holding
Nordstrom	Standard Parking	Williams-Sonoma
Northrop Grumman	Staples	Xilinx
Office Depot	Stratasys	Zale
OfficeMax	Sun Microsystems	Zions Bancorporation

APPENDIX: SUMMARY STATISTICS

	2005 FVT % of Market Cap			2006 FVT % of Market Cap			2007 FVT % of Market Cap			3-Year Average FVT % of Market Cap		
	25P	Median	75P	25P	Median	75P	25P	Median	75P	25P	Median	75P
	<i>Size Categories</i>											
Small	0.39%	0.95%	1.89%	0.43%	1.15%	1.71%	0.41%	0.84%	1.44%	0.46%	1.10%	1.72%
Mid	0.49%	0.82%	1.33%	0.49%	0.74%	1.16%	0.45%	0.69%	1.07%	0.52%	0.82%	1.10%
Large	0.38%	0.52%	0.81%	0.38%	0.57%	0.90%	0.36%	0.50%	0.94%	0.39%	0.56%	0.90%
<i>Industry Sectors</i>												
Financial	0.24%	0.38%	0.66%	0.21%	0.47%	0.75%	0.25%	0.39%	0.67%	0.29%	0.41%	0.72%
Industrial	0.42%	0.64%	0.84%	0.40%	0.67%	1.06%	0.36%	0.55%	0.96%	0.41%	0.68%	1.01%
Retail	0.48%	0.84%	1.34%	0.46%	0.74%	1.24%	0.45%	0.76%	1.12%	0.58%	0.82%	1.12%
Technology	0.94%	1.49%	2.16%	0.75%	1.27%	1.88%	0.82%	1.19%	1.72%	0.86%	1.40%	1.94%
Total Sample	0.40%	0.73%	1.37%	0.41%	0.74%	1.31%	0.38%	0.69%	1.17%	0.43%	0.78%	1.26%

	2005 FVT % of Revenue			2006 FVT % of Revenue			2007 FVT % of Revenue			3-Year Average FVT % of Revenue		
	25P	Median	75P	25P	Median	75P	25P	Median	75P	25P	Median	75P
	<i>Size Categories</i>											
Small	0.42%	0.93%	2.64%	0.37%	0.97%	3.21%	0.41%	0.94%	2.32%	0.50%	1.17%	2.82%
Mid	0.39%	0.93%	1.62%	0.42%	0.84%	1.75%	0.43%	0.76%	1.66%	0.46%	0.88%	1.63%
Large	0.42%	0.63%	1.69%	0.38%	0.77%	1.89%	0.39%	0.76%	1.76%	0.37%	0.81%	1.79%
<i>Industry Sectors</i>												
Financial	0.37%	0.97%	1.45%	0.39%	1.14%	1.96%	0.50%	0.93%	1.52%	0.49%	1.00%	1.83%
Industrial	0.28%	0.44%	0.98%	0.33%	0.52%	1.02%	0.34%	0.50%	0.78%	0.34%	0.50%	0.87%
Retail	0.38%	0.60%	1.05%	0.36%	0.59%	0.79%	0.34%	0.49%	0.92%	0.39%	0.58%	0.97%
Technology	1.42%	3.63%	7.59%	1.40%	3.15%	6.09%	1.30%	3.08%	6.28%	1.44%	3.22%	6.64%
Total Sample	0.41%	0.84%	1.80%	0.39%	0.87%	2.23%	0.41%	0.81%	1.90%	0.42%	0.88%	1.96%

Frederic W. Cook & Co., Inc. is an independent consulting firm specializing in executive and director compensation and related corporate governance matters. Formed in 1973, our firm has served more than 2,000 corporations, including 28 percent of the Fortune 500 during the past two years, in a wide variety of industries from our offices in New York, Chicago, Los Angeles, San Francisco, Atlanta, and Tarrytown. Our primary focus is on performance-based compensation programs that help companies attract and retain business leaders, motivate and reward them for improved performance, and align their interests with shareholders. Our range of consulting services includes:

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- Compensation Committee Advisor
- Competitive Assessment
- Corporate Governance Matters
- Corporate Transactions
- Directors' Remuneration
- Incentive Grants and Guidelines
- Long-term Incentive Design
- Ownership Programs
- Performance Measurement
- Recruitment/Retention Incentives
- Regulatory Services
- Restructuring Incentives
- Shareholder Voting Matters
- Specific Plan Reviews
- Strategic Incentives
- Total Compensation Reviews

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