PROLOGIS
Form 10-Q
May 10, 2006

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended March 31, 2006

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from ____________________ to ____________________
Commission File Number 01-12846
PROLOGIS
(Exact name of registrant as specified in its charter)

Maryland	**74-2604728**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
4545 Airport Way, Denver, Colorado	**80239**
(Address or principal executive offices)	**(Zip Code)**

(303) 567-5000
(Registrant s telephone number, including area code)
14100 East 35th Place, Aurora, Colorado 80011
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing for the past 90 days.

Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934).

Yes o No þ

The number of shares outstanding of the Registrant s common shares as of May 4, 2006 was 244,975,819.

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PROLOGIS
CONSOLIDATED STATEMENTS OF
EARNINGS AND COMPREHENSIVE INCOME
(Unaudited)
(In thousands, except per share data)

	Three Months Ended March 31,	
	2006	**2005**
Revenues:		
Rental income	$ 233,033	$ 131,203
CDFS dispositions proceeds	305,010	282,591
Property management and other fees and incentives	38,568	16,527
Development management and other income	4,168	131
Total revenues	580,779	430,452
Expenses:		
Rental expenses	64,171	37,521
Cost of CDFS dispositions	238,286	227,250
General and administrative	33,788	23,934
Depreciation and amortization	72,554	41,470
Merger integration and relocation expenses	2,372	2,751
Other expenses	2,526	1,913
Total expenses	413,697	334,839
Operating income	167,082	95,613
Other income (expense):		
Earnings from unconsolidated property funds	56,445	11,771
Earnings from CDFS joint ventures and other unconsolidated investees	3,517	498
Interest expense	(70,853)	(36,493)
Interest income on long-term notes receivable	5,036	
Interest and other income	4,574	1,147
Total other income (expense)	(1,281)	(23,077)
Earnings before minority interest	165,801	72,536
Minority interest	(1,125)	(1,341)
Earnings before certain net gains (expenses/losses)	164,676	71,195
Gains recognized on dispositions of certain non-CDFS business assets, net	13,709	
Foreign currency exchange expenses/losses, net	(1,322)	(114)
Earnings before income taxes	177,063	71,081

Income taxes:		
Current income tax expense	13,197	1,173
Deferred income tax expense	169	839
Total income taxes	13,366	2,012
Earnings from continuing operations	163,697	69,069

(Continued)

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PROLOGIS
CONSOLIDATED STATEMENTS OF
EARNINGS AND COMPREHENSIVE INCOME (CONTINUED)
(Unaudited)
(In thousands, except per share data)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Discontinued operations:		
Income attributable to disposed properties and assets held for sale	4,369	1,961
Losses related to temperature-controlled distribution assets		(11,370)
Gains (losses) recognized on dispositions, net:		
Non-CDFS business assets	16,428	2,207
CDFS business assets	5,019	(439)
Total discontinued operations	25,816	(7,641)
Net earnings	189,513	61,428
Less preferred share dividends	6,354	6,354
Net earnings attributable to common shares	183,159	55,074
Other comprehensive income items:		
Foreign currency translation adjustments	(4,473)	(15,196)
Unrealized gains (losses) on derivative contracts, net	(420)	400
Comprehensive income	$ 178,266	$ 40,278
Weighted average common shares outstanding Basic	244,282	186,154
Weighted average common shares outstanding Diluted	255,146	196,180
Net earnings (loss) per share attributable to common shares Basic:		
Continuing operations	$ 0.64	$ 0.34
Discontinued operations	0.11	(0.04)
Net earnings per share attributable to common shares Basic	$ 0.75	$ 0.30
Net earnings (loss) per share attributable to common shares Diluted:		
Continuing operations	$ 0.62	$ 0.33
Discontinued operations	0.10	(0.04)
Net earnings per share attributable to common shares Diluted	$ 0.72	$ 0.29
Distributions per common share	$ 0.40	$ 0.37

The accompanying notes are an integral part of these Consolidated Financial Statements.

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PROLOGIS
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	March 31, 2006 (Unaudited)	December 31, 2005
ASSETS		
Real estate	$ 12,002,993	$ 11,875,130
Less accumulated depreciation	1,149,705	1,118,547
	10,853,288	10,756,583
Investments in and advances to unconsolidated investees	1,189,097	1,049,743
Cash and cash equivalents	254,095	191,716
Accounts and notes receivable	301,861	327,214
Other assets	808,042	788,840
Discontinued operations assets held for sale	258,236	
Total assets	$ 13,664,619	$ 13,114,096
LIABILITIES AND SHAREHOLDERS EQUITY		
Liabilities:		
Debt	$ 7,054,628	$ 6,677,880
Accounts payable and accrued expenses	328,208	332,339
Other liabilities	600,343	557,210
Discontinued operations assets held for sale	46,652	
Total liabilities	8,029,831	7,567,429
Minority interest	53,546	58,644
Shareholders equity:		
Series C Preferred Shares at stated liquidation preference of $50.00 per share; $0.01 par value; 2,000,000 shares issued and outstanding at March 31, 2006 and December 31, 2005	100,000	100,000
Series F Preferred Shares at stated liquidation preference of $25.00 per share; $0.01 par value; 5,000,000 shares issued and outstanding at March 31, 2006 and December 31, 2005	125,000	125,000
Series G Preferred Shares at stated liquidation preference of $25.00 per share; $0.01 par value; 5,000,000 shares issued and outstanding at March 31, 2006 and December 31, 2005	125,000	125,000
Common Shares; $0.01 par value; 244,817,298 shares issued and outstanding at March 31, 2006 and 243,781,142 shares issued and outstanding at December 31, 2005	2,448	2,438
Additional paid-in capital	5,618,632	5,606,017
Accumulated other comprehensive income	144,693	149,586

Distributions in excess of net earnings	(534,531)	(620,018)
Total shareholders equity	5,581,242	5,488,023
Total liabilities and shareholders equity	$ 13,664,619	$ 13,114,096

The accompanying notes are an integral part of these Consolidated Financial Statements.

PROLOGIS
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Three Months Ended March 31,	
	2006	**2005**
Operating activities:		
Net earnings	$ 189,513	$ 61,428
Minority interest share in earnings	1,125	1,341
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Straight-lined rents	(8,821)	(1,731)
Cost of share-based compensation awards	5,199	4,773
Depreciation and amortization	74,829	43,782
Amortization of deferred loan costs and net premium on debt	(1,815)	1,179
Gains recognized on dispositions of non-CDFS business assets, net	(30,137)	(2,207)
Impairment charge on assets held for sale		13,084
Equity in earnings from unconsolidated investees	(59,962)	(12,269)
Distributions from and changes in operating receivables of unconsolidated investees	29,084	14,488
Purchases of derivative contracts	(1,007)	(965)
Adjustments to foreign currency exchange amounts recognized	1,811	285
Deferred income tax expense	169	839
Increase in accounts receivable and other assets	(61,784)	(20,565)
Increase (decrease) in accounts payable and accrued expenses and other liabilities	37,008	(4,481)
Net cash provided by operating activities	175,212	98,981
Investing activities:		
Real estate investments	(870,651)	(538,841)
Purchase of ownership interests in property funds	(259,248)	
Tenant improvements and lease commissions on previously leased space	(18,407)	(12,495)
Recurring capital expenditures	(4,460)	(2,706)
Proceeds from dispositions of real estate assets	540,936	255,871
Proceeds from repayment of notes receivable related to dispositions of assets	36,855	59,991
Net investments in unconsolidated investees	(102,188)	(16,764)
Net cash used in investing activities	(677,163)	(254,944)
Financing activities:		
Net proceeds from sales and issuances of common shares under various common share plans	13,233	12,403
Distributions paid on common shares	(97,672)	(68,894)
Minority interest redemptions and distributions	(6,231)	(2,128)
Dividends paid on preferred shares	(6,354)	(6,354)
Debt and equity issuance costs paid	(5,377)	
Net (payments on) proceeds from lines of credit and short-term borrowings	(148,589)	351,893
Proceeds from issuance of senior notes `	844,428	

Payments on senior notes, secured debt and assessment bonds	(29,108)	(20,046)
Net cash provided by financing activities	564,330	266,874
Net increase in cash and cash equivalents	62,379	110,911
Cash and cash equivalents, beginning of period	191,716	236,529
Cash and cash equivalents, end of period	$ 254,095	$ 347,440

See Note 12 for information on non-cash investing and financing activities and other information.

The accompanying notes are an integral part of these Consolidated Financial Statements.

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PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. General:

Business. ProLogis, collectively with our consolidated subsidiaries (we, our, us, the Company or Prologis), is a publicly held real estate investment trust (REIT) that owns, operates and develops (directly and through our unconsolidated investees) primarily industrial distribution properties in North America, Europe and Asia. Our business consists of three reportable business segments: (i) property operations, (ii) fund management and (iii) corporate distribution facilities services and other real estate development business (CDFS business). Our property operations segment represents the direct long-term ownership, and the management and leasing of industrial distribution and retail properties, both directly and indirectly owned. Our fund management segment represents the long-term investment management of unconsolidated property funds and the properties they own. Our CDFS business segment primarily encompasses our development or acquisition of real estate properties that are generally contributed to an unconsolidated property fund, in which we have an ownership interest and act as manager, or sold to third parties. See Note 11 for further discussion of our business segments.

Basis of Presentation. The accompanying consolidated financial statements, presented in the U.S. dollar, are prepared in accordance with U.S. generally accepted accounting principles (GAAP). GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as of the date of the financial statements and revenue and expenses during the reporting period. Our actual results could differ from those estimates and assumptions. All material intercompany transactions with consolidated entities have been eliminated.

The accompanying unaudited interim financial information has been prepared according to the rules and regulations of the U.S. Securities and Exchange Commission (the SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted in accordance with such rules and regulations. Our management believes that the disclosures presented in these financial statements are adequate to make the information presented not misleading. In our opinion, all adjustments and eliminations, consisting only of normal recurring adjustments, necessary to present fairly our financial position as of March 31, 2006 and our results of operations and cash flows for the three months ended March 31, 2006 and 2005 have been included. The results of operations for such interim periods are not necessarily indicative of the results for the full year. The accompanying unaudited interim financial information should be read in conjunction with our December 31, 2005 audited Consolidated Financial Statements, as filed with the SEC on Form 10-K.

Certain amounts included in the accompanying consolidated financial statements for 2005 have been reclassified to conform to the 2006 financial statement presentation. These amounts include reclassifications in the consolidated statement of cash flows resulting in an increase to operating cash flows of $13.2 million, a decrease to investing cash flows of $14.2 million and an increase to financing activities of $1.0 million, which we believe are immaterial to 2005.

Adoption of New Accounting Pronouncements. The Emerging Issues Task Force (EITF) reached a consensus in June 2005 regarding EITF Issue 04-5, Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity when the Limited Partners Have Certain Rights. The EITF agreed on a framework for evaluating when a general partner controls a limited partnership and whether the partnership should be consolidated. The Financial Accounting Standards Board (the FASB) ratified the consensus that was effective June 29, 2005 for all new or modified partnerships and effective January 1, 2006 for all existing partnerships. We adopted EITF 04-5 on January 1, 2006. As such, we performed an evaluation of each of our unconsolidated investees. We first determined whether or not the entity needed to be evaluated under EITF 04-5 based on the ownership and legal structure. Next, we evaluated whether the limited partners had substantive kick-out rights or participating rights, both as defined under EITF 04-5. We concluded that the unconsolidated investees that were subject to EITF 04-5 and needed to be evaluated should be accounted for under the equity method of accounting based on the rights provided to the limited partners under the governing documents of the respective entity.

On December 16, 2004, the FASB issued Statement of Financial Accounting Standards No. 123R Share Based Payment (SFAS 123R) that required companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the award s fair value on the grant date and recognize the cost over the period during which an employee is required to provide service in exchange for the award, generally the vesting period. We

PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

adopted SFAS 123R on January 1, 2006 using the modified prospective application. Prior to that date, we recognized the costs of our share-based compensation plans under SFAS No. 123 Accounting and Disclosure of Stock Based Compensation that allowed us to continue to account for these plans under Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25). The impact of adoption of SFAS 123R is the inclusion of compensation expense within our statements of earnings, which were previously disclosed as pro forma amounts within the notes to our financial statements. See Note 4.

2. Mergers and Acquisitions:

On September 15, 2005, Catellus Development Corporation, a publicly traded REIT, (Catellus) merged with and into Palmtree Acquisition Corporation, one of our subsidiaries, pursuant to an Agreement and Plan of Merger dated as of June 6, 2005 (the Merger Agreement), as amended (the Catellus Merger). At the time of the Catellus Merger, Catellus owned or held an ownership interest in 41.8 million square feet of industrial, office and retail properties of which approximately 92% was industrial space.

In connection with the Catellus Merger, we incurred merger integration costs, such as employee transition costs and severance costs for certain of our employees whose responsibilities became redundant after the Catellus Merger. We expect to incur integration costs through the first half of 2006, although the majority of these costs have already been incurred.

Under the terms of the Merger Agreement, Catellus stockholders had the opportunity to elect to receive cash or our common shares for their Catellus stock. As a result of the Catellus Merger, we issued approximately 55.9 million of our common shares to former Catellus stockholders. We financed the cash portion of the Catellus Merger primarily through borrowings of $1.5 billion on a short-term bridge facility (the Bridge Facility). As of March 31, 2006, the Bridge Facility had been repaid with proceeds from the issuance of senior notes, $900 million issued in November 2005 and $850 million issued in March 2006, borrowings under our revolving credit facilities and the disposition of certain real estate properties. See Note 9 for details of our March 2006 debt issuance.

The allocation of the purchase price of $5.3 billion was based upon estimates and assumptions. We engaged a third party business valuation expert to assist primarily with the fair value assessment of real estate. The current allocations are substantially complete; however, there are certain items that may be subject to revision if additional information becomes available. We do not expect future revisions to have a significant impact on our financial position or results of operations.

The following unaudited pro forma financial information for the three months ended March 31, 2005, gives effect to the Catellus Merger as if it had occurred on January 1, 2005. The pro forma results (in millions, except per share amounts) are based on historical data and are not intended to be indicative of the results of future operations.

	Three Months Ended March 31, 2005
Total revenues	$ 543.1
Operating income	$ 114.7
Net earnings attributable to common shares	$ 53.2
Weighted average common shares outstanding basic	241.8
Weighted average common shares outstanding diluted	251.8
Net earnings per share attributable to common shares basic	$ 0.22
Net earnings per share attributable to common shares diluted	$ 0.22

PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

3. Unconsolidated Investees:

Summary of Investments and Income

Our investments in and advances to unconsolidated investees, which are accounted for under the equity method, are summarized by type of investee as follows (in thousands):

	March 31, 2006	December 31, 2005
Property funds	$ 826,206	$ 755,320
CDFS joint ventures and other investees	362,891	294,423
Totals	$ 1,189,097	$ 1,049,743

We recognize earnings or losses from our investments in unconsolidated investees consisting of our proportionate share of the net earnings or losses of these investees and interest income on advances made to these investees, if any. In addition, we earn fees for providing services to the property funds, CDFS joint ventures and certain other investees. The amounts we have recognized from our investments in unconsolidated investees are summarized as follows (in thousands):

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Earnings (losses) from unconsolidated investees (including interest income):		
Property funds:		
North America	$ 42,482	$ 5,408
Europe	11,199	4,721
Asia	2,764	1,642
Total property funds	56,445	11,771
CDFS joint ventures and other investees:		
North America	3,306	113
Europe	(172)	41
Asia	383	344
Total CDFS joint ventures and other investees	3,517	498
Total equity in earnings	$ 59,962	$ 12,269
Property management and other fees and incentives:		
North America	$ 28,629	$ 8,094
Europe	7,399	7,393
Asia	2,540	1,040

Total property management and other fees and incentives	$ 38,568	$ 16,527

Property Funds

Contributions of developed properties to a property fund allow us to realize, for financial reporting purposes, a portion of the profits from our development activities while at the same time allowing us to maintain a long-term ownership interest in our developed properties. This business strategy also provides liquidity to fund our future development activities and generates fee income. The property funds generally own operating properties that we have contributed to them, although certain of the property funds have also acquired properties from third parties. We may receive additional ownership interests in the property funds as part of the proceeds generated by the contributions of properties to the property funds. We recognize our proportionate share of the earnings or losses of each property fund. We earn fees for acting as the manager of each of the property funds and the fund properties, and we may earn additional fees by providing other services including, but not limited to, acquisition, development and leasing activities. We may also earn incentive performance participation based on the investors returns.

On January 4, 2006, we purchased the 80% ownership interests in each of ProLogis North American Properties Funds II, III and IV (collectively Funds II-IV) from our fund partner. On March 1, 2006, we contributed substantially all of these assets and associated liabilities to the ProLogis North American Industrial Fund (the North American Industrial Fund), which was formed in February 2006 (see below). In connection with these transactions, we recognized the

PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

following amounts in the respective financial statement line items for the three months ended March 31, 2006, after deferral of $17.9 million due to our 20% ownership interest in the North American Industrial Fund (in thousands):

CDFS disposition proceeds (1)	$ 12,492
Property management and other fees and incentives (2)	$ 21,958
Earnings from unconsolidated property funds (3)	$ 37,113

(1) Represents the recognition of proceeds that we had previously deferred as part of CDFS income upon the initial contributions of the properties to Funds II-IV.

(2) Represents an incentive return we earned due to certain return levels achieved by our fund partner upon the termination of Funds II-IV.

(3) Represents our proportionate share of the gain on termination recognized by Funds II-IV.

Information about our property funds is as follows:

	Ownership percentage		Investment in and advances to	
Property Fund	**March 31, 2006**	**December 31, 2005**	**March 31, 2006**	**December 31, 2005**
ProLogis California (1)	50.0%	50.0%	$ 114,549	$ 115,743
	41.3%	41.3%	33,159	33,241

ProLogis North American Properties Fund I (1)				
ProLogis North American Properties Fund II-IV (2)		20.0%		12,410
ProLogis North American Properties Fund V (3)	11.2%	11.3%	56,190	53,104
ProLogis North American Properties Fund VI (1)	20.0%	20.0%	41,070	42,227
ProLogis North American Properties Fund VII (1)	20.0%	20.0%	32,275	32,543
ProLogis North American Properties Fund VIII (1)	20.0%	20.0%	15,463	15,602
ProLogis North American Properties Fund IX (1)	20.0%	20.0%	14,191	14,274
ProLogis North American Properties Fund X (1)	20.0%	20.0%	15,950	15,968
ProLogis North American Properties Fund XI (1)	20.0%	20.0%	32,188	33,094
ProLogis North American Industrial Fund (4)	20.0%		69,139	
ProLogis European Properties Fund (5)	21.2%	21.0%	287,456	283,435
ProLogis Japan Properties Fund I (1)	20.0%	20.0%	94,447	103,679
ProLogis Japan Properties Fund II (1)(6)	20.0%		20,129	
Totals			$ 826,206	$ 755,320

(1) We have one fund partner in each of these property funds.

(2) As discussed earlier, on January 4, 2006, we purchased the 80% ownership interests of our fund partner in each of these property funds and subsequently contributed substantially all of the assets and associated liabilities into the ProLogis North American Industrial Fund.

(3) We refer to the combined entities in which we have ownership interests as one property fund named ProLogis North American Properties Fund V. Our ownership percentage is based on our levels of ownership interest in these different entities. We are committed to offer to contribute certain existing industrial distribution properties in the United States and Mexico to ProLogis North American Properties Fund V, prior to offering for contribution or sale to any third party, subject to certain conditions, through December 31, 2006. During the three months ended March 31, 2006, we contributed certain assets for approximately $95 million to ProLogis North

American Properties Fund V. We estimate our remaining commitment under this arrangement to be $255.0 million at March 31, 2006. On January 9, 2006, a preferred unit holder in a subsidiary of ProLogis North American Properties Fund V exercised its option to put its interest to us for $55.0 million, which we acquired and include in other investees below. We have an agreement with ProLogis North American Properties Fund V that would enable us to put this interest to ProLogis North American Properties Fund V at the same price after June 30, 2006.

(4) In February 2006, we formed the North American Industrial Fund, with several institutional investors, which will primarily own recently

developed industrial distribution properties in major distribution markets throughout the United States and Canada. We refer to the combined entities in which we have ownership interests as one property fund named ProLogis North American Industrial Fund. We are committed to offer to contribute substantially all of our stabilized industrial development properties in Canada and the United States to the North American Industrial Fund. The North American Industrial Fund has equity commitments, which expire in February 2009, aggregating approximately $1.5 billion from third party investors, of which $1.2 billion was unfunded at March 31, 2006. We

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PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

have a 20% ownership interest in the North American Industrial Fund. We receive property and asset management fees and will also have the potential for incentive performance participation based on the investors returns.

(5) We and 21 third parties, primarily institutional investors, own units in the ProLogis European Properties Fund. ProLogis European Properties Fund has equity commitments from nine investors through subscription agreements aggregating 636.6 million (the currency equivalent of approximately $767.4 million at March 31,

2006) of which 140.8 million (the currency equivalent of approximately $169.7 million at March 31, 2006) was unfunded at March 31, 2006. The subscription agreements expire on August 29, 2006. We are committed to offer to contribute all of the properties that we develop and stabilize in specified markets in Europe to ProLogis European Properties Fund as long as the fund has capital to invest, subject to the property meeting certain leasing and other criteria.

(6) ProLogis Japan Properties Fund II was formed on September 1, 2005. We are committed to offer to contribute all of the properties that we develop and stabilize in Japan through August 2008 to this property fund, subject to

the property meeting certain leasing and other criteria. During the three months ended March 31, 2006, we made our first contribution of a property to this property fund and the property fund acquired four properties from third parties. ProLogis Japan Properties Fund II has equity commitments aggregating $600.0 million from our fund partner, which expire in August 2008, of which $523.4 million was unfunded at March 31, 2006.

Summarized financial information of the property funds (for the entire entity, not our proportionate share) and our investment in such funds is presented below (dollars in millions):

	2006			
	North America	Europe	Asia	Total
For the three months ended March 31, 2006:				
Revenues	$ 111.0	$ 97.7	$ 24.9	$ 233.6
Net earnings (1)	$ 204.2	$ 50.7	$ 11.6	$ 266.5
As of March 31, 2006:				
Total assets	$ 5,129.3	$ 4,233.5	$ 1,553.4	$ 10,916.2
Amounts due to ProLogis	$ 13.7	$ 7.2	$ 62.6	$ 83.5
Third party debt (2)	$ 2,774.7	$ 2,082.9	$ 634.0	$ 5,491.6
Total liabilities	$ 3,051.2	$ 2,490.6	$ 832.8	$ 6,374.6
Equity	$ 2,077.3	$ 1,737.8	$ 720.6	$ 4,535.7
Our weighted average ownership (3)	23.2%	21.2%	20.0%	22.0%
Our investment balance (4)	$ 424.1	$ 287.5	$ 114.6	$ 826.2
Deferred proceeds, net of amortization	$ 81.8	$ 119.2	$ 46.2	$ 247.2

	2005			
	North America	Europe	Asia	Total
For the three months ended March 31, 2005:				
Revenues	$ 126.1	$ 91.4	$ 14.5	$ 232.0
Net earnings	$ 26.9	$ 19.4	$ 7.1	$ 53.4
As of December 31, 2005:				
Total assets	$ 4,786.6	$ 4,052.0	$ 1,230.1	$ 10,068.7
Amounts due to ProLogis	$ 9.0	$ 15.7	$ 71.3	$ 96.0
Third party debt (2)	$ 2,690.7	$ 1,991.2	$ 535.1	$ 5,217.0
Total liabilities	$ 2,921.0	$ 2,409.6	$ 639.8	$ 5,970.4
Equity	$ 1,864.1	$ 1,637.9	$ 590.3	$ 4,092.3
Our weighted average ownership (3)	23.5%	21.0%	20.0%	22.1%
Our investment balance (4)	$ 368.2	$ 283.4	$ 103.7	$ 755.3
Deferred proceeds, net of amortization	$ 77.7	$ 105.5	$ 44.1	$ 227.3

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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(1) Included in net earnings for North America is $185.7 million representing the net gain recognized by the Funds II-IV termination.

(2) Of the total third party debt of the property funds, we had guaranteed $42.0 million and $12.5 million of debt at March 31, 2006 and December 31, 2005, respectively, all of which relate to borrowings ProLogis North American Properties Fund V has outstanding, which mature in September 2006.

(3) Represents the weighted average of our ownership interests in all property funds based on each entity s contribution to total assets, before depreciation, net of other

liabilities.

(4) The difference between our percentage ownership interest of the property fund s equity and our investment balance results from three types of transactions: (i) deferring a portion of the proceeds we receive from a contribution of one of our properties to a property fund as a result of our continued ownership in the property; (ii) recording additional costs associated with our investment in the property fund; and (iii) advances to the property funds.

CDFS joint ventures and other investees

At March 31, 2006, we had investments in entities that perform some of our CDFS business activities (the CDFS joint ventures) and certain other investments. These joint ventures include entities that develop and own industrial operating properties and also include entities that perform land, multi-use and residential development activity. The other operating joint ventures include entities that own a hotel property and office properties. Our investments in and advances to these entities were as follows (in thousands):

	March 31, 2006	December 31, 2005
CDFS joint ventures:		
United States	$ 119,850	$ 113,008
Europe	13,042	12,238
China	62,322	57,165
Total CDFS joint ventures	$ 195,214	$ 182,411

Other investees:				
Operating joint ventures	$	85,331	$	84,731
Other (1)		82,346		27,281
Total other investees		167,677	$	112,012
Total	$	362,891	$	294,423

(1) On January 9, 2006, a preferred unit holder in a subsidiary of ProLogis North American Properties Fund V exercised its option to put its interest to us for $55.0 million, which we acquired. We have an agreement with ProLogis North American Properties Fund V that would enable us to put this interest to ProLogis North American Properties Fund V at the same price after June 30, 2006.

4. Long-Term Compensation:

Share Options

We have granted various share options to our employees and trustees with graded vesting at various rates over periods from one to 10 years, subject to certain conditions. Each share option is exercisable into one common share. The holders of share options granted before 2001 earn dividend equivalent units (DEUs) each year until the earlier of the date the underlying share option is exercised or the expiration date of the underlying share option. Share options granted generally vest over a four-year period.

PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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Share options outstanding at March 31, 2006 were as follows:

	Number of Options	Exercise Price(1)	Expiration Date	Weighted Average Remaining Life (in years)
Outside Trustees Plan	121,250	$19.75 - $43.80	2009-2015	6.4
Share options:				
1997 grants	157,464	$21.22	2007	1.4
1998 grants	678,895	$20.94 - $21.09	2008	2.6
1999 grants	666,038	$17.19 - $18.62	2009	3.5
2000 grants	660,242	$21.75 - $24.25	2010	4.5
2001 grants	603,575	$20.67 - $22.02	2011	5.5
2002 grants	1,091,164	$22.98 - $24.75	2007, 2012	6.2
2003 grants	1,351,345	$24.90 - $31.26	2013	7.5
2004 grants	1,792,863	$29.41 - $41.50	2014	8.5
2005 grants	1,110,093	$40.86 - $45.46	2015	9.7
2006 grants	7,518	$54.51	2016	10.0
Total	8,240,447			

(1) The exercise price is equal to the average of the high and low market prices on the date of grant for each issuance.

The weighted average fair value of the share options granted during the three months ended March 31, 2006 was $9.61 per option. There were no options granted during the corresponding period in 2005. We calculated the fair value of the options granted in 2006 using a Black-Scholes model with the following assumptions: i) risk free interest rate of 4.69%; ii) dividend yield of 3.59%; iii) volatility of 20.25%; and iv) weighted-average option life of 5.8 years.

Restricted Share Units

Restricted share units (RSUs), in the form of common shares, are granted at a rate of one common share per RSU from time to time to our employees and our trustees. The RSUs are valued on the grant date based upon the market price of a common share on that date. We recognize the value of the RSUs granted as compensation expense over the applicable vesting period which generally is four or five years. The RSUs do not carry voting rights during the vesting period, but do generally earn DEUs that vest according to the underlying RSU.

Performance Shares

Certain employees are granted performance share awards (PSAs). The grants are based on performance criteria, established in advance, for each employee eligible for the grant. If, based on the performance criteria, a PSA is earned,

the recipient must continue to be employed by us until the end of the vesting period before any portion of the grant is vested. The PSAs carry no voting rights during this vesting period, but do earn DEUs that are vested at the end of the vesting period, which is generally two or three years. The PSAs are valued on the grant date, based upon the market price of a common share on that date. We recognize the value of the PSAs granted as compensation expense over the vesting period.

Included in the PSAs outstanding at March 31, 2006 were certain PSAs that will be earned based on our ranking in a defined subset of companies in the National Association of Real Estate Investment Trust s (NAREIT s) published index. These PSAs will vest over a three-year period. The amount of PSAs to be issued will be based on our ranking at the end of the three-year period, and may range from zero to 255,000 shares. For purposes of calculating compensation expense, we consider the PSAs to have a market condition and therefore we estimate the amount of PSAs to be earned.

Dividend Equivalent Units

DEUs in the form of common shares are earned at a rate of one common share per DEU for certain share options granted through 2001, RSUs and PSAs. The DEUs are valued on the grant date, generally December 31st, based on the market price of a common share on that date. Prior to the adoption of SFAS 123R, we recognized the value of the DEUs issued as compensation expense over the vesting period of the underlying share award. With the adoption of SFAS

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123R, we now treat the DEUs as dividends, which are charged to retained earnings and factored into the computation of the fair value of the underlying share award at grant date.

Summary of Activity

The activity for the three months ended March 31, 2006, with respect to our share options is presented below.

	Options Outstanding		Options Exercisable		
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price	Weighted Average Life (in years)
Balance at December 31, 2005	8,873,820	$ 29.19			
Granted	7,518	$ 54.51			
Exercised	(579,203)	$ 25.57			
Forfeited	(61,688)	$ 35.02			
Balance at March 31, 2006	8,240,447	$ 29.42	4,427,383	$ 24.09	6.6

Activity with respect to our RSUs and PSAs is as follows:

	Number of Shares	Weighted Average Original Value	Number of Shares Vested
Balance at December 31, 2005	1,792,335		
Granted	3,567		
Exercised	(277,625)		
Forfeited	(6,933)		
Balance at March 31, 2006	1,511,344	$ 37.36	367,899

During the three months ended March 31, 2006, we recognized $5.2 million of compensation expense, net of $0.7 million that was capitalized due to our development activities, under the provisions of SFAS 123R. During the three months ended March 31, 2005, under the provisions of APB 25, we recognized $4.8 million of compensation expense, net of $0.9 million that was capitalized due to our development activities. With the adoption of SFAS 123R, we now recognize the compensation cost associated with stock options that was previously disclosed in our footnotes and we no longer recognize compensation cost associated with dividend equivalent units, which are now treated as dividends, which are charged to retained earnings and factored into the computation of the fair value of the underlying share award at grant date. Had we not adopted SFAS 123R, our net earnings attributable to common shares would have been approximately $182.5 million and our net earnings per share attributable to common shares would not have

changed.

Had we adopted SFAS 123R on January 1, 2005, our net earnings attributable to common shares would have changed as follows:

	Three Months Ended March 31, 2005
Net earnings attributable to common shares:	
As reported	$ 55,074
Pro forma	$ 55,765
Net earnings per share attributable to common shares:	
As reported Basic	$ 0.30
As reported Diluted	$ 0.29
Pro forma Basic	$ 0.30
Pro forma Diluted	$ 0.29

Total compensation cost related to unvested share options, RSUs and PSAs was $52.4 million as of March 31, 2006 and will be recognized over a weighted average period of 1.8 years, prior to adjustments for capitalized amounts due to our development activities and forfeited awards.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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5. Discontinued Operations:

Discontinued operations represent a component of an entity that has either been disposed of or is classified as held for sale if both the operations and cash flows of the component have been or will be eliminated from ongoing operations of the entity as a result of the disposal transaction and the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. The results of operations of the component of the property or a business are also reported as discontinued operations for all periods presented. A property is classified as held for sale when certain criteria are met. At such time, the respective assets and liabilities are presented separately on our balance sheet and depreciation is no longer recognized. Assets held for sale are reported at the lower of their carrying amount or their estimated fair value less the costs to sell.

Properties disposed of to third parties are considered discontinued operations unless such properties were developed under a pre-sale agreement. Properties contributed to property funds in which we maintain an ownership interest and act as manager are not considered discontinued operations due to our continuing involvement with the properties. Discontinued operations recognized directly by our unconsolidated investees, if any, are not reflected separately from our investment balance or separately from the net earnings or losses of those equity investees.

Income attributable to discontinued operations is summarized as follows (in millions):

	Three Months Ended March 31,	
	2006	2005
Rental income	$ 14.0	$ 5.7
Rental expenses	(6.7)	(1.8)
Depreciation and amortization	(2.3)	(1.8)
Interest expense	(0.6)	(0.1)
Income attributable to disposed properties and assets held for sale	$ 4.4	$ 2.0

Assets Disposed Of

The following information relates to properties disposed of to third parties that are recorded as discontinued operations (in millions, except number of properties):

	Three Months Ended March 31,	
	2006	2005
Non-CDFS business assets:		
Number of properties	29	4
Net proceeds from dispositions	$ 137.7	$ 6.9
Net gains from dispositions	$ 16.4	$ 2.2
CDFS business assets:		
Number of properties	2	1
Net proceeds from dispositions	$ 47.8	$ 2.9
Net gains (losses) from dispositions	$ 5.0	$ (0.4)

Our temperature-controlled distribution assets in France were sold in July 2005. In connection with the sale, we received total proceeds of 30.8 million including a note receivable of 23.9 million that was paid in full in January 2006. We recognized impairment charges of $13.1 million in the first quarter of 2005, to reflect our investment in this business at its estimated fair value less costs to sell. These charges are included in Losses related to temperature-controlled distribution assets in our Consolidated Statements of Earnings.

Assets Held For Sale

As of March 31, 2006, we had 19 office properties and one hotel property that were classified as held for sale and accordingly, the operations of these properties were included in discontinued operations and the respective assets and liabilities are presented separately in our Consolidated Balance Sheets.

PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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6. Distributions and Dividends:

Common Share Distributions

Cash distributions of $0.40 per common share for the first quarter of 2006 were paid on February 28, 2006 to holders of common shares on February 15, 2006. Quarterly common share distributions paid in 2006 are based on the annual distribution level for 2006 of $1.60 per common share (as compared to $1.48 per common share in 2005) set by the Board of Trustees (Board) in December 2005. The payment of common share distributions is subject to the discretion of the Board and is dependent upon our financial condition and operating results, and may be adjusted at the discretion of the Board during the year.

Preferred Share Dividends

The annual dividends on our cumulative redeemable preferred shares are $4.27 per share (Series C) and $1.6875 per share (Series F and Series G). On March 31, 2006, we paid quarterly dividends of $1.0675 per share (Series C) and $0.4219 per share (Series F and Series G). Such dividends are payable quarterly in arrears on the last day of March, June, September and December. Dividends on preferred shares are payable when, and if, they have been declared by the Board, out of funds legally available for the payment of dividends.

7. Earnings Per Common Share:

We determine basic earnings per share based on the weighted average number of common shares outstanding during the period. We determine diluted earnings per share based on the weighted average number of common shares outstanding combined with the incremental weighted average common shares that would have been outstanding assuming all potentially dilutive instruments were converted into common shares at the earliest date possible. The following table sets forth the computation of our basic and diluted earnings per share (in thousands, except per share amounts):

	Three Months Ended March 31,	
	2006	**2005**
Net earnings attributable to common shares	$ 183,159	$ 55,074
Minority interest share in earnings	1,125	1,341
Adjusted net earnings attributable to common shares	$ 184,284	$ 56,415
Weighted average common shares outstanding Basic	244,282	186,154
Incremental weighted average effect of conversion of limited partnership units	5,363	5,543
Incremental weighted average effect of potentially dilutive instruments (1)	5,501	4,483
Weighted average common shares outstanding Diluted	255,146	196,180
Net earnings per share attributable to common shares Basic	$ 0.75	$ 0.30
Net earnings per share attributable to common shares Diluted	$ 0.72	$ 0.29

(1) Total weighted average potentially dilutive instruments outstanding were 11,116 and 11,180 for the three months ended March 31, 2006 and 2005, respectively. Substantially all were dilutive for both the three months ended March 31, 2006 and 2005.

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8. Real Estate:

Real estate assets owned directly by us primarily consist of income producing properties, properties under development and land held for future development. Our real estate assets, presented at cost, include the following (in thousands):

	March 31, 2006	December 31, 2005
Industrial operating properties (1):		
Improved land	$ 1,878,867	$ 1,774,923
Buildings and improvements	7,140,425	6,955,983
Retail operating properties (2):		
Improved land	67,357	66,848
Buildings and improvements	215,540	221,405
Land subject to ground leases and other (3)	452,399	792,668
Properties under development, including cost of land (4)	1,041,465	884,345
Land held for development (5)	1,022,971	1,045,042
Other investments (6)	183,969	133,916
Total real estate assets	12,002,993	11,875,130
Less accumulated depreciation	1,149,705	1,118,547
Net real estate assets	$ 10,853,288	$ 10,756,583

(1) At March 31, 2006 and December 31, 2005, we had 1,409 and 1,432 industrial operating properties consisting of 187.4 million square feet and 185.6 million square feet, respectively.

(2) At March 31, 2006 and December 31, 2005, we had 27 and 29 retail

operating properties, both consisting of 1.1 million square feet.

(3) At March 31, 2006, our office properties and one hotel property were classified as assets held for sale. See Note 5.

(4) Properties under development consisted of 96 properties aggregating 27.7 million square feet at March 31, 2006 and 72 properties aggregating 23.2 million square feet at December 31, 2005. Our total expected investment upon completion of these properties is approximately $2.2 billion at March 31, 2006.

(5) Land held for future development consisted of 5,870 and 6,568 acres at March 31, 2006 and December 31, 2005, respectively.

(6)

Other investments primarily include: (i) restricted funds that are held in escrow pending the completion of tax-deferred exchange transactions involving operating properties; (ii) earnest money deposits associated with potential acquisitions; (iii) costs incurred during the pre-acquisition due diligence process; (iv) costs incurred during the pre-construction phase related to future development projects; and (v) costs related to our corporate office buildings.

We directly own real estate assets in North America (Canada, Mexico and the United States), Europe (Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Romania, Spain, Sweden, and the United Kingdom) and Asia (China, Japan, Korea and Singapore).

For our direct-owned properties, the largest customer and the 25 largest customers accounted for 2.3% and 18.5%, respectively, of our annualized collected base rents at March 31, 2006.

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9. Debt:

Our debt consisted of the following (dollars in thousands):

	March 31, 2006		December 31, 2005	
	Weighted Average Interest Rate	Amount Outstanding	Weighted Average Interest Rate	Amount Outstanding
Unsecured lines of credit and short-term borrowings	2.43%	$ 1,835,643	3.28%	$ 2,240,054
Senior notes	6.02%	3,589,137	6.16%	2,759,675
Secured debt	6.50%	1,595,431	6.50%	1,643,586
Assessment bonds	3.89%	34,417	3.87%	34,565
Totals	5.18%	$ 7,054,628	5.27%	$ 6,677,880

On March 27, 2006, we issued $450.0 million of 5.5% senior notes due April 1, 2012 and $400.0 million of 5.75% senior notes due April 1, 2016. We received net proceeds of $838.7 million, after all offering costs, of which $390.0 million was used to repay the balance under the Bridge Facility with the remainder to repay borrowings under our global senior credit facility (Global Line).

Our Global Line is a $2.6 billion global senior credit facility from which funds may be drawn in U.S. dollar, euro, Japanese yen, British pound sterling, Chinese renminbi, South Korean won and Canadian dollar. The commitments for $40 million of borrowings in Chinese renminbi have been received but the facilities are not yet available pending the completion of certain conditions that are expected to be resolved this year. The weighted average interest rate represents the weighted average base interest rates using local currency rates on borrowings outstanding at the end of the period.

10. Shareholders Equity:

During the three months ended March 31, 2006, we sold and/or issued common shares under various common share plans, including share-based compensation plans, as follows (in thousands):

	Shares	Proceeds
1999 Dividend Reinvestment and Share Purchase Plan	19	$ 967
Continuous Equity Offering Plan (1)	135	$ 7,018
Long-term Incentive Plan and Share Option Plan for Outside Trustees	845	$ 14,579

(1) Proceeds were received in April 2006.

11. Business Segments:

We have three reportable business segments:

Property operations representing the direct long-term ownership, management and leasing of industrial distribution and retail properties, both directly and indirectly owned. Each operating property is considered to be an individual operating segment having similar economic characteristics that are combined within the reportable segment based upon geographic location. Included in this segment are properties we developed and properties we acquired and rehabilitated or repositioned within the CDFS business segment with the intention

of contributing the property to a property fund or selling to a third party. Our operations in the property operations business segment are in North America (Mexico and the United States), Europe (properties are located in the Czech Republic, France, Germany, Hungary, Italy, Poland and the United Kingdom and are generally pending contribution to a property fund or sale to a third party) and Asia (properties are located in China, Japan and Singapore and are generally pending contribution to a property fund or sale to a third party).

Fund management representing the long-term investment management of unconsolidated property funds and the properties they own, generate a high level of returns to us and our fund partners. Along with the income recognized under the equity method from our investments in the property funds, we include fees and incentives earned for services performed on behalf of the property funds and interest earned on advances to the property

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
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funds, if any. We utilize our leasing and property management expertise in our property operations segment for managing the properties owned by property funds in this segment, and we report the costs as part of rental expenses in the property operations segment. Each investment in a property fund is considered to be an individual operating segment having similar economic characteristics that are combined within the reportable segment based upon geographic location. Our operations in the fund management segment are in North America (Mexico and the United States), Europe (Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Spain, Sweden, and the United Kingdom), and Asia (Japan).

CDFS business primarily encompasses our development of properties that generally are either contributed to an unconsolidated property fund, in which we have an ownership interest and act as manager, or sold to third parties. Additionally, we acquire properties with the intent to rehabilitate and/or reposition the property in the CDFS business segment prior to being contributed to a property fund. We engage in commercial mixed-use development activities generally with the intention of selling the land or completed projects to third parties. We also have investments in several unconsolidated entities that perform development activities and we include our proportionate share of their earnings or losses in this segment. Additionally, we include fees earned for development activities on behalf of customers or third parties, interest income earned on notes receivable related to asset sales and gains or losses on the disposition of land parcels when our development plans no longer include the parcels. The separate activities in this segment are considered to be individual operating segments having similar economic characteristics that are combined within the reportable segment based upon geographic location. Our CDFS business segment operations are in North America (Canada, Mexico and the United States), in Europe (Belgium, the Czech Republic, France, Germany, Hungary, Italy, the Netherlands, Poland, Romania, Spain, and the United Kingdom) and in Asia (China, Japan and Korea).

We have other operating segments that do not meet the threshold criteria to disclose as a reportable segment, primarily the management of land subject to ground leases. Each operating property and activity is located in the United States and is considered to be an individual operating segment.

The assets of the CDFS business segment generally include properties under development and land held for development. During the period between the completion of development, rehabilitation or repositioning of a property and the date the property is contributed to a property fund or sold to a third party, the property and its associated rental income and rental expenses are included in the property operations segment because the primary activity associated with the property during that period is leasing. Upon contribution or sale, the resulting gain or loss is included in the income of the CDFS business segment.

We present the operations and net gains and losses associated with properties sold to third parties generally as discontinued operations. In addition, as of March 31, 2006, we had 19 office properties and one hotel property classified as assets held for sale, with the operations included in discontinued operations. Accordingly, these amounts are excluded from the segment presentation. See Note 5.

Reconciliations are presented below for: (i) each reportable business segment s revenue from external customers to our total revenues; (ii) each reportable business segment s net operating income from external customers to our earnings before minority interest; and (iii) each reportable business segment s assets to our total assets. Our chief operating decision makers rely primarily on net operating income and similar measures to make decisions about allocating resources and assessing segment performance. The applicable components of our revenues, earnings before minority interest and assets, excluding discontinued operations, are allocated to each reportable business segment s income, net operating income and assets. Items that are not directly assignable to a segment, such as certain corporate income and expenses, are reflected as reconciling items. The following reconciliations are presented in thousands:

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	Three Months Ended March 31,	
	2006	**2005**
Revenues:		
Property operations (1):		
North America	$ 207,373	$ 127,876
Europe	11,662	1,182
Asia	2,590	2,145
Total property operations segment	221,625	131,203
Fund management (2):		
North America	71,111	13,502
Europe	18,598	12,114
Asia	5,304	2,682
Total fund management segment	95,013	28,298
CDFS business (3):		
North America	100,913	131,605
Europe	152,060	86,170
Asia	61,241	64,947
Total CDFS business segment	314,214	282,722
Total segment revenue	630,852	442,223
Other North America	11,408	-
Reconciling item (4)	(61,481)	(11,771)
Total revenues	$ 580,779	$ 430,452
Net operating income (loss):		
Property operations (5):		
North America	$ 153,860	$ 92,188
Europe	6,882	(188)
Asia	2,167	1,682
Total property operations segment	162,909	93,682
Fund management (2):		
North America	71,111	13,502
Europe	18,598	12,114
Asia	5,304	2,682

Total fund management segment	95,013	28,298
CDFS business (6)(7):		
North America	34,810	28,169
Europe	32,113	13,729
Asia	9,650	12,424
Total CDFS business segment	76,573	54,322
Total segment net operating income	334,495	176,302
Other North America	5,953	-
Reconciling items:		
Income from other unconsolidated investees	461	41
General and administrative expenses	(33,788)	(23,934)
Depreciation and amortization expense	(72,554)	(41,470)
Merger integration and relocation expenses	(2,372)	(2,751)
Other expenses	(115)	(306)
Interest expense	(70,853)	(36,493)
Interest and other income	4,574	1,147
Total reconciling items	(174,647)	(103,766)
Total earnings before minority interest	$ 165,801	$ 72,536

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	March 31, 2006	December 31, 2005
Assets:		
Property operations (8):		
North America	$ 7,667,237	$ 7,530,062
Europe	667,402	673,342
Asia	260,147	106,069
Total property operations segment	8,594,786	8,309,473
Fund management (9):		
North America	424,174	368,206
Europe	287,456	283,435
Asia	114,576	103,679
Total fund management segment	826,206	755,320
CDFS business:		
North America	1,161,145	1,142,319
Europe	1,089,390	1,062,338
Asia	655,140	535,190
Total CDFS business segment	2,905,675	2,739,847
Total segment assets	12,326,667	11,804,640
Other North America	481,080	901,281
Reconciling items:		
Investments in and advances to other unconsolidated investees	167,677	27,281
Cash and cash equivalents	254,095	191,716
Accounts and notes receivable	24,574	38,864
Other assets	152,290	150,314
Discontinued operations assets held for sale	258,236	
Total reconciling items	856,872	408,175
Total assets	$ 13,664,619	$ 13,114,096

(1) Includes industrial and retail property rental income.

(2) Includes fund management revenues and our share of the income or loss recognized under the equity method from our investment in the property funds along with interest earned on advances to the property funds, if any.

(3) Includes proceeds received on CDFS property dispositions, fees earned from customers and third parties for development activities and interest income on long-term notes receivable related to asset dispositions.

(4) Amount represents income from unconsolidated property funds and interest income on long-term notes receivable that are not presented as a component of revenues in our Consolidated Statements of Earnings.

(5)

Includes rental income less rental expenses of our industrial and retail properties. Included in rental expenses are the costs of managing the properties owned by the property funds.

(6) Includes net gains or losses associated with CDFS property dispositions, fees earned from customers and third parties for development activities, interest income on notes receivable related to asset dispositions and our share of the earnings or losses recognized under the equity method on our investments in CDFS joint ventures.

(7) Excludes proceeds of $47.8 million and $2.9 million for the three months ended March 31, 2006 and 2005, respectively and net gains of $5.0 million and a loss of

$0.4 million for the three months ended March 31, 2006 and 2005, respectively, associated with CDFS properties sold to third parties and presented as discontinued operations in our Consolidated Statements of Earnings. See Note 5.

(8) Includes properties that were developed or acquired in the CDFS business segment that have not yet been contributed or sold of $1.7 billion and $1.4 billion as of March 31, 2006 and December 31, 2005, respectively.

(9) Represents our investment in and advances to the property funds.

12. Supplemental Cash Flow Information:

Non-cash investing and financing activities for the three months ended March 31, 2006 and 2005 are as follows:

In connection with the purchase of the 80% ownership interests from our fund partner in Funds II-IV, we assumed $418.0 million of secured debt. See Note 3.

As partial consideration for properties we contributed to the North American Industrial Fund, we received ownership interests of $62.1 million, representing a 20% ownership interest, and the property fund assumed $677.2 million of secured debt and short-term borrowings. See Note 3.

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PROLOGIS
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(Unaudited)

We received $35.4 million and $15.1 million of equity interests in property funds from the contribution of properties to these property funds during the three months ended March 31, 2006 and 2005, respectively.

As partial consideration for certain property contributions, we received $1.9 million and $32.6 million in the form of notes receivable from ProLogis North American Properties Fund V in 2006 and 2005, respectively. The outstanding balance of the notes at March 31, 2006 was $1.9 million.

The amount of interest paid in cash, net of amounts capitalized, for the three months ended March 31, 2006 and 2005 was $57.6 million and $46.5 million, respectively.

13. Derivative Financial Instruments:

We use derivative financial instruments as hedges to manage our risk associated with interest and foreign currency exchange rate fluctuations on existing or anticipated obligations and transactions. We do not use derivative financial instruments for trading purposes.

At March 31, 2006, the only outstanding derivative contracts were foreign currency put option contracts. The activity relating to these contracts for the three months ended March 31, 2006 was as follows (in millions):

New contracts	$ 92.9
Settled contracts	(13.9)
Notional amounts at March 31, 2006	$ 79.0

The foreign currency put option contracts are paid in full at execution and are related to our operations in Europe and Japan. The put option contracts provide us with the option to exchange euro, pound sterling and yen for U.S. dollars at a fixed exchange rate such that, if the euro, pound sterling or yen were to depreciate against the U.S. dollar to predetermined levels as set by the contracts, we could exercise our options and mitigate our foreign currency exchange losses. The notional amounts of the put option contracts represent the U.S. dollar equivalent of 18.9 million, £12.2 million and ¥4.9 billion at March 31, 2006.

These contracts generally do not qualify for hedge accounting treatment and are marked-to-market through results of operations at the end of each period. Upon expiration of the contract, the mark-to-market adjustment is reversed, the total cost of the contract is expensed and any proceeds are recognized as a gain. We recognized net losses/expenses of $113,000 and net gains of $277,000 for the three months ended March 31, 2006 and 2005, respectively, on various put option contracts. These amounts include mark-to-market losses of $22,000 and mark-to-market gains of $304,000 for the three months ended March 31, 2006 and 2005, respectively.

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Report of Independent Registered Public Accounting Firm

The Board of Trustees and Shareholders
ProLogis:

We have reviewed the accompanying consolidated balance sheet of ProLogis and subsidiaries as of March 31, 2006 and the related consolidated statements of earnings and comprehensive income and consolidated statements of cash flows for the three-month periods ended March 31, 2006 and 2005. These consolidated financial statements are the responsibility of ProLogis management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of ProLogis and subsidiaries as of December 31, 2005, and the related consolidated statements of earnings, shareholders equity and comprehensive income, and cash flows for the year then ended (not presented herein); and in our report dated March 14, 2006, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2005, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

KPMG LLP
Los Angeles, California
May 8, 2006

ITEM 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with our Consolidated Financial Statements and the related notes included in Item 1 of this report and our 2005 Annual Report on Form 10-K.

Certain statements contained in this discussion or elsewhere in this report may be deemed forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as expects , anticipates , intends , plans , believes , seeks , estimates , variations of such words and similar expressions are int identify such forward-looking statements, which generally are not historical in nature. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future including statements relating to rent and occupancy growth, development activity and changes in sales or contribution volume of developed properties, general conditions in the geographic areas where we operate and the availability of capital in existing or new property funds are forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Although we believe the expectations reflected in any forward-looking statements are based on reasonable assumptions, we can give no assurance that our expectations will be attained and therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Some of the factors that may affect outcomes and results include, but are not limited to: (i) national, international, regional and local economic climates, (ii) changes in financial markets, interest rates and foreign currency exchanges rates, (iii) increased or unanticipated competition for our properties, (iv) risks associated with acquisitions, (v) maintenance of real estate investment trust (REIT) status, (vi) availability of financing and capital, (vii) changes in demand for developed properties, and (viii) those additional factors discussed in Item 1A. Risk Factors of our 2005 Annual Report on Form 10-K. Unless the context otherwise requires, the terms we , us and our refer to ProLogis and our consolidated subsidiaries.

Management s Overview

We are a self-administered and self-managed REIT that operates a global network of real estate properties, primarily industrial distribution properties. The primary business drivers across the globe continue to be the need for greater distribution network efficiency and the growing shift to third-party logistics providers. Our focus on our customers expanding needs has enabled us to become a leading global provider of distribution space in three continents.

Our business is organized into three reportable business segments: (i) property operations, (ii) fund management and (iii) corporate distribution facilities services and other real estate development business (CDFS business). The property operations segment represents the direct long-term ownership and the management and leasing of industrial distribution and retail properties, both directly and indirectly owned. The fund management segment represents the long-term investment management of unconsolidated property funds and the properties they own, to generate a high level of returns to us and our fund partners. The CDFS business segment primarily encompasses our development or acquisition of properties that are rehabilitated or repositioned, which are generally contributed to an unconsolidated property fund in which we have an ownership interest and act as manager or sold to third parties.

We generate and seek to increase revenues, earnings, funds from operations (FFO), as defined below, and cash flows through our segments primarily as follows:

Property Operations Segment

We earn rent from our customers under long-term operating leases, including reimbursements of certain operating costs, in our industrial distribution and retail properties that we own directly in North America, Europe and Asia. We expect to grow our revenue through increases in occupancy rates and rental rates in both our industrial distribution and retail properties. Our strategy is to achieve these increases primarily through continued focus on our customers global needs for distribution space in the three continents in which we operate and use of the ProLogis Operating System®, an

organizational structure and service delivery system that we built around our customers and the selective acquisition of industrial distribution properties.

Fund Management Segment

We recognize our proportionate share of the earnings or losses from our investments in unconsolidated property funds operating in North America, Europe and Asia. Along with the income recognized under the equity method, we include fees and incentives earned for services performed on behalf of the property funds and interest earned on advances to the property funds, if any. We also earn certain other fees for services provided to the property funds, such as acquisition, financing and development fees. We expect growth in income recognized to come from newly created property funds, as discussed below, growth in existing property funds, as well as increased fees and incentives. The growth in the existing property funds is expected to come primarily from additional properties the funds will acquire, generally from us, and increased rental revenues in the property funds due, in part, to our leasing and property management efforts by our property operations segment.

CDFS Business Segment

We recognize income primarily from the contributions of developed, rehabilitated and repositioned properties to the property funds and from dispositions to third parties. In addition, we earn fees from our customers or other third parties for development activities that we provide on their behalf, recognize interest income on notes receivable related to asset dispositions, recognize net gains from the disposition of land parcels that no longer fit into our development plans and recognize our proportionate share of the income generated by development joint ventures in which we have an investment. We expect increases in this segment to come primarily from the continued development of high-quality industrial distribution properties in our key markets in North America, Europe and Asia, resulting in the contribution to property funds or sale to third parties. In addition, we expect to increase our land and other commercial development activities for development fees and sales to third parties.

In September 2005, we completed a merger whereby Catellus Development Corporation was merged into one of our subsidiaries (the Catellus Merger). The total purchase price of $5.3 billion was financed through the issuance of 55.9 million ProLogis common shares, the assumption of $1.7 billion of liabilities and cash of $1.3 billion. We financed the cash portion through borrowings on a short-term bridge facility that has been fully repaid as of March 31, 2006.

Summary of the three months ended March 31, 2006

The fundamentals of our business were strong in the first three months of 2006. We increased our total operating portfolio of industrial distribution and retail properties owned or managed, including direct-owned properties, and properties owned by the property funds and CDFS joint ventures, to 359.7 million square feet at March 31, 2006 from 349.7 million square feet at December 31, 2005. We increased our same store net operating income (as defined below) by 3.7% in the first quarter of 2006 over the same period in 2005. Our same store average occupancy increased by 4.0% for the first quarter of 2006 as compared to the first quarter of 2005. Same store rent growth was a negative 1.1% in the first quarter of 2006, compared with a negative 2.1% in the first quarter of 2005. The stabilized leased percentage (as defined below) was 95.2% at March 31, 2006, compared with 94.5% at December 31, 2005.

Net operating income of the CDFS business segment increased 41.0% in the three months ended March 31, 2006 as compared to the same period in 2005, primarily due to increased development fees and interest income due in part to activities acquired in the Catellus Merger, as well as the recognition of previously deferred proceeds from contributions. During the quarter, we started the development of projects with a total expected cost at completion of $887.4 million and completed development projects at a total cost of $461.6 million. This compares with the first quarter of 2005 when we started development projects with a total expected cost at completion of $732.2 million and completed development projects at a total cost of $178.6 million. The increased development activity was spurred by increased demand for industrial distribution properties in North America, Europe and Asia. We believe

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the strong development activity, along with the access to capital through the property funds and positive leasing activity, will continue to support increased contribution activity.

Key Transactions during the three months ended March 31, 2006

We formed the ProLogis North American Industrial Fund (the North American Industrial Fund), which will primarily own recently developed industrial properties in the United States and Canada.

During the quarter, we generated net proceeds of $305.0 million from contributions and sales of CDFS assets, excluding discontinued operations. This includes our first contribution of assets to the ProLogis Japan Properties Fund II, which was formed in late 2005 and in which we have a 20% ownership interest.

On January 4, 2006, we purchased the 80% ownership interests in each of ProLogis North American Properties Funds II, III and IV (Funds II-IV) from our fund partner. In March 2006, we contributed substantially all of the assets and associated liabilities we obtained in this acquisition to the North American Industrial Fund. In connection with this transaction, we recognized: (i) our proportionate share of the gain on termination of Funds II-IV of $37.1 million; (ii) an incentive return fee of $22.0 million due to certain return levels achieved by our fund partner, and (iii) $12.5 million of disposition proceeds that had previously been deferred. These amounts are net of an aggregate $17.9 million, which was deferred due to our 20% ownership in the North American Industrial Fund.

During the quarter, we disposed of 31 CDFS and non-CDFS properties to third parties, which are included in discontinued operations and generated net proceeds of $185.5 million and resulted in the recognition of $21.4 million of gains.

On March 27, 2006 we issued $850.0 million of senior notes and used the proceeds to repay borrowings under the short-term bridge facility that was used to fund the Catellus Merger and borrowings under our global credit facility (Global Line).

Results of Operations

Net earnings attributable to common shares was $183.2 million and $55.1 million for the three months ended March 31, 2006 and 2005, respectively. Basic and diluted net earnings attributable to common shares was $0.75 and $0.72 per share, respectively, for the three months ended March 31, 2006 and $0.30 and $0.29 per share, respectively, for the three months ended March 31, 2005. The increase in net earnings in 2006 over 2005 is primarily due to the Catellus Merger, the termination of Funds II-IV, improved property operating performance, and gains on dispositions of assets to third parties.

Portfolio Information

In the discussion that follows, we present the results of operations by reportable business segment. The following table summarizes our total operating portfolio of industrial and retail properties, excluding properties under development, and including properties owned by us, the properties funds and CDFS joint ventures (square feet in thousands):

	March 31, 2006		**December 31, 2005**		**March 31,2005**	
Reportable Business Segment	**Number of Properties**	**Square Feet**	**Number of Properties**	**Square Feet**	**Number of Properties**	**Square Feet**
Property operations	1,436	188,520	1,461	186,663	1,220	131,679
Fund management	780	166,869	752	159,769	722	153,308
CDFS business	26	4,314	23	3,283	17	2,411
Totals	2,242	359,703	2,236	349,715	1,959	287,398

The stabilized operating properties owned by us, the property funds and CDFS joint ventures were 95.2% leased at March 31, 2006, 94.5% leased at December 31, 2005 and 92.2% leased at March 31, 2005. The stabilized properties are those properties where the capital improvements, repositioning efforts, new management and new marketing programs for acquisitions or the marketing programs in the case of newly developed properties, have

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been completed and in effect for a sufficient period of time to achieve stabilization. A property generally enters the stabilized pool at the earlier of 12 months from acquisition or completion or when it becomes substantially occupied, which we define generally as 93.0%.

Same Store Analysis

We evaluate the operating performance of the properties included in each of our three reportable business segments using a same store analysis because the population of properties in this analysis is consistent from period to period, thereby eliminating the effects of changes in the composition of the portfolio on performance measures. We include properties owned directly and indirectly, by the property funds and by the CDFS joint ventures, in the same store analysis. Accordingly, we define the same store portfolio of operating properties for each period as those properties that have been in operation throughout the full period in both the current and prior year. When a property is disposed of to a third party, it is removed from the population for the full quarter in which it is disposed and the corresponding period of the prior year. The same store portfolio aggregated 274.4 million square feet at March 31, 2006 and included only industrial distribution properties.

Same store results were as follows:

Net operating income generated by the same store portfolio (defined for the same store analysis as rental income, excluding termination and renegotiation fees, less rental expenses) increased 3.7% for the three months ended March 31, 2006 over the same period in 2005, due to a 4.1% increase in rental income and a 5.4% increase in rental expenses.

Average occupancy in the same store portfolio increased 4.0% for the three months ended March 31, 2006 over the same period in 2005.

The same store portfolio s rental rates, associated with leasing activity for space that has been previously leased by us, decreased for the three months ended March 31, 2006 by 1.1% over the same period in 2005.

We believe the factors that impact net operating income, rental rates and average occupancy in the same store portfolio are the same as for the total portfolio. The percentage change presented is the weighted average of the measure computed separately for us and each entity individually with the weighting based on each entity s proportionate share of the combined component on which the change is computed. In order to derive an appropriate measure of period-to-period operating performance, the percentage change computation removes the effects of foreign currency exchange rate movements by computing each property s components in that property s functional currency.

Rental income computed under GAAP applicable to the properties included in the same store portfolio is adjusted to remove the net termination and renegotiation fees recognized in each period. Net termination and renegotiation fees excluded from rental income for the same store portfolio (including properties directly owned and properties owned by the property funds and CDFS joint ventures) were $0.8 million and $5.6 million for the three months ended March 31, 2006 and 2005, respectively. Net termination and renegotiation fees represent the gross fee negotiated to allow a customer to terminate or renegotiate their lease, offset by the write-off of the asset recognized due to the adjustment to straight-line rents over the lease term, if any. Removing the net termination fees from the same store calculation of rental income allows us to evaluate the growth or decline in each property s rental income without regard to items that are not indicative of the property s recurring operating performance.

In computing the percentage change in rental expenses, the rental expenses applicable to the properties in the same store portfolio include property management expenses for our direct-owned properties. These expenses are based on the property management fee that is provided for in the individual agreements under which our wholly owned management company provides property management services to each property (generally, the fee is based on a percentage of revenues). On consolidation, the management fee income earned by the management company and the management fee expense recognized by the properties are eliminated and the direct costs of providing property management services are recognized as part of our rental expenses reported under GAAP.

Operational Outlook

Changes in economic conditions will generally impact customer leasing decisions and absorption of new distribution properties. Since late 2004, we have experienced strong customer demand and continued strengthening in occupancies across our global markets. Leasing activity continues to improve with our stabilized portfolio reaching 95.2% leased at March 31, 2006. Market rental rates are beginning to increase and the negative gap between our current rental rates on expiring leases and market rents has started to decrease. As a result, we have experienced positive rental rate growth or only modestly negative rental rate growth over the past several quarters. Growth in global trade continues to support strong market fundamentals, which in turn, supports the acceleration of our global development pipeline. We executed 31 million square feet of leases during the three months ended March 31, 2006, an increase of 45% over the same period in 2005. We expect absorption of available space to continue to be strong throughout 2006. One of the most important fundamentals to our long term growth is repeat business with our global customers. Nearly half of the leases in our newly developed space is being leased to repeat customers.

Property Operations Segment

The net operating income of the property operations segment consists of rental income and rental expenses from the industrial distribution and retail operating properties that we directly own. The costs of our property management function for both our direct-owned portfolio and the properties owned by the property funds are all reported in rental expenses in the property operations segment. The net earnings or losses generated by operating properties that were developed or acquired in the CDFS business segment are included in the property operations segment during the interim period from the date of completion or acquisition through the date the properties are contributed or sold. See Note 11 to our Consolidated Financial Statements in Item 1 for a reconciliation of net operating income to earnings before minority interest. The net operating income from the property operations segment, which does not include rental income and rental expenses associated with the industrial distribution and retail properties that are presented as discontinued operations in our financial statements, was as follows (in thousands).

	Three Months Ended March 31,	
	2006	**2005**
Rental income	$ 221,625	$ 131,203
Rental expenses	58,716	37,521
Total property operations segment	$ 162,909	$ 93,682

The number and composition of operating properties that we own throughout the periods and the timing of contributions impact rental income and rental expenses for each period. Rental income includes net termination and renegotiation fees and rental expense recoveries of $44.9 million and $25.8 million for the three months ended March 31, 2006 and 2005, respectively.

When a property is contributed to a property fund, we begin reporting our share of the earnings of the property under the equity method in the fund management segment. However, the overhead costs incurred by us to provide the management services to the property fund continue to be reported as part of rental expenses. The increases in rental income and rental expenses, in 2006 over 2005, are due primarily to the increase in properties owned through the Catellus Merger and other acquisitions and increases in the same store properties we directly own. The increase in the number of properties under management has also contributed to the increase in rental expenses.

Fund Management Segment

The net operating income of the fund management segment consists of: (i) earnings or losses recognized under the equity method from our investments in the property funds; (ii) fees and incentives earned for services performed on behalf of the property funds; and (iii) interest earned on advances to the property funds, if any. The net earnings or losses of the property funds include the following income and expense items of the property funds, in addition to rental income and rental expenses: (i) interest income and interest expense; (ii) depreciation and amortization expenses; (iii) general and administrative expenses; (iv) income tax expense; (v) foreign currency exchange gains and

losses; and (vi) gains on dispositions of properties. See Notes 3 and 11 to our Consolidated Financial Statements in Item 1 for additional information on the property funds and for a reconciliation of net operating income to earnings before minority interest.

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The net operating income from the fund management segment was as follows (in thousands):

	Three Months Ended March 31,	
	2006	2005
Earnings from property funds (1):		
North American property funds (2)	$ 71,111	$ 13,502
ProLogis European Properties Fund (3)	18,598	12,114
Japan property funds (4)	5,304	2,682
Total fund management segment	$ 95,013	$ 28,298

(1) The earnings from the property funds includes fees and incentives earned by us for providing services to the property funds. Fees earned for providing services to the property funds for other than property management and asset management services can fluctuate from year to year. The costs of the property management function for the properties owned by the property funds are reported in the property operations segment and the costs of the fund management function are included in

general and administrative expenses.

(2) Represents the income earned by us from our investments in property funds in North America, including our proportionate share of the earnings or losses of the property funds and property management and other fees and incentives. We had interests in 13 and 15 funds at March 31, 2006 and 2005, respectively. Our ownership interests ranged from 11.2% to 50.0% as of March 31, 2006. With respect to the income from these funds, fluctuations between years in the amount that we recognize under the equity method are generally due to the number of property funds, the number of properties owned by the property funds, occupancy levels and the

amount of termination and renegotiation fees earned by the property funds. These property funds on a combined basis owned 780 and 722 properties at March 31, 2006 and 2005, respectively.

In January 2006, we purchased the 80% ownership interests from our fund partner in Funds II-IV and subsequently contributed substantially all of the assets and associated liabilities to the North American Industrial Fund. In connection with this transaction, we earned an incentive return of $22.0 million and recognized $37.1 million in income, representing our proportionate share of the net gain recognized by Funds II-IV upon termination.

(3) ProLogis European Properties Fund has continued to acquire properties, primarily from us, and increase its portfolio size since it began operations. This property fund owned 271 and 234 properties at March 31, 2006 and 2005, respectively. Our ownership interest in ProLogis European Properties Fund was 21.2% at both March 31, 2006 and 2005. The fluctuations in income recognized from our ownership interest in this property fund are primarily the result of the following factors: (i) the size of the portfolio and occupancy levels in each period; (ii) increases in the fees earned for services provided to the property fund due to the increase in the number of properties managed; (iii) higher interest costs associated with the higher debt levels that primarily result from the use of debt to acquire the additional properties; (iv) changes in our ownership interest in each year; and (v) variances in the average foreign currency exchange rate at which we translate our share of the net earnings of the property fund to U.S. dollars.

(4) Amounts represent our investments in two property funds in Japan. ProLogis Japan Properties Fund I has increased its portfolio to 18 properties at March 31, 2006 from 14 properties at March 31, 2005. Our ownership interest in ProLogis Japan Properties Fund I has been 20.0% since inception. The increases in the amounts recognized under the equity method from our ownership in this property fund correspond with the growth in the portfolio over the three years. In September 2005, we formed a second fund in Japan, ProLogis Japan Properties Fund II. Our ownership interest in ProLogis Japan Properties Fund II was 20% at March 31, 2006. During the three months ended March 31, 2006, we made our first contribution of a property to this fund, which did not own any properties in 2005, and the fund acquired four properties from third parties.

CDFS Business

Net operating income from the CDFS business segment consists primarily of: (i) gains and losses resulting from the contributions and dispositions of properties, generally developed by us or acquired with the intent to rehabilitate or reposition; (ii) gains and losses from the dispositions of land parcels; (iii) fees earned for development services

provided to customers and third parties; (iv) interest income earned on notes receivable related to property dispositions; (v) our proportionate share of the earnings or losses of CDFS joint ventures; and (vi) certain costs associated with potential acquisition of CDFS business assets and land holding costs. See Note 11 to our Consolidated Financial Statements in Item 1 for a reconciliation of net operating income to earnings before minority interest.

For the three months ended March 31, 2006, our net operating income in this segment was $76.6 million, as compared to $54.3 million for the same period in 2005, an increase of $22.3 million, or 41.0% (an increase of $27.7 million or 51.4% when the gains from CDFS business transactions recognized as discontinued operations are included). In 2006, 45.5% of the net operating income of this operating segment was generated in North America, 41.9% was generated in Europe and 12.6% was generated in Asia.

The CDFS business segment s net operating income includes the following components (in thousands):

	Three Months Ended March 31,	
	2006	2005
CDFS transactions:		
Disposition proceeds, prior to deferral (1)	$ 315,786	$ 293,849
Proceeds deferred and not recognized (2)	(23,608)	(11,258)
Recognition of previously deferred amounts (2)	12,832	-
Cost of CDFS dispositions (1)	(238,286)	(227,250)
Net gains	66,724	55,341
Development management and other income (3)	4,168	131
Interest income on long-term notes receivable (4)	5,036	-
Net earnings from CDFS joint ventures (5)	3,056	457
Other expenses and charges (6)	(2,411)	(1,607)
Total CDFS business segment	$ 76,573	$ 54,322
CDFS transactions recognized as discontinued operations (7):		
Disposition proceeds	$ 47,765	$ 2,936
Cost of dispositions	(42,746)	(3,375)
Net CDFS gains (losses) in discontinued operations	$ 5,019	$ (439)

(1) During the three months ended March 31, 2006, we contributed 15 buildings to the property funds (five in North America, nine in Europe and one in Japan) generating a net gain of

$44.0 million, compared with 16 buildings contributed during the same period in 2005 (10 in North America, five in Europe and one in Japan) generating a net gain of $51.8 million. In addition, we recognized net gains of $10.5 million and $2.2 million from the disposition of land parcels during the three months ended March 31, 2006 and 2005, respectively.

(2) When we contribute a property to a property fund in which we have an ownership interest, we do not recognize a portion of the proceeds in the computation of the gain resulting from the contribution, based on our continuing ownership interest in the contributed

property that arises due to our ownership interest in the property fund that acquires the property. We defer this portion of the proceeds by recognizing a reduction to our investment in the respective property fund. We adjust our proportionate share of earnings or losses that we recognize under the equity method from the property fund in later periods to reflect the property fund s depreciation expense as if the depreciation expense was computed on our lower basis in the contributed property rather than on the property fund s basis in the contributed property. If a loss results when a property is contributed to a property fund, the entire loss is recognized.

When a property that we originally contributed to a property fund is disposed of to a third party by the property fund, we recognize in earnings the net amount of proceeds we had previously deferred in the period that the disposition to the third party occurs, in addition to our proportionate share of the net gain or loss recognized by the property fund. Further, during periods when our ownership interest in a property fund decreases, we recognize gains to the extent that previously deferred proceeds are recognized to coincide with our new ownership interest in the property fund. This amount includes $12.5 million in 2006 related to the termination of Funds II-IV.

(3) Amounts include fees we earned for the performance of development activities. The increase in 2006 is due primarily to development undertaken since the Catellus Merger and increased development management activity in Europe.

(4) Amount in 2006 represents interest income earned on notes receivable related to previous property sales that were acquired in the Catellus Merger.

(5) Represents the net earnings we recognized under the equity method from our investments in CDFS joint ventures. The increase in 2006 is due primarily to earnings recognized in our investments in joint ventures acquired in connection with the Catellus Merger.

(6) Includes land holding costs and charges for previously capitalized pursuit costs related to potential CDFS business segment projects when the acquisition is no longer probable.

(7) Includes two CDFS business properties aggregating 0.2 million square feet and one CDFS business property aggregating 0.1 million square feet that were sold to third parties during the three months ended March 31, 2006 and 2005, respectively, that met the criteria to be presented as discontinued operations.

Income from the CDFS business segment is dependent on several factors, including but not limited to: (i) our ability to develop and timely lease properties, (ii) our ability to acquire properties that eventually can be contributed to property funds after rehabilitating or repositioning, (iii) our ability to generate a profit from these activities and (iv) our success in raising capital to be used by the property funds to acquire the properties we developed or repositioned. There can be no assurance we will be able to maintain or increase the current level of net operating income in this segment and we continue to monitor leasing activity and general economic conditions as it pertains to the CDFS business segment.

Other Components of Income

General and Administrative Expenses

General and administrative expenses were $33.8 million and $23.9 million for the three months ended March 31, 2006 and 2005, respectively. Fluctuations in general and administrative expenses are influenced by the various business initiatives we are undertaking in a given period. The increase in general and administrative expenses in 2006 over 2005 is primarily due to the overall growth of the company resulting from the continuing international expansion of our operating platform, the Catellus Merger and the formation of additional property funds.

On December 16, 2004, the Financial Accounting Standards Board (the FASB) issued Statement of Financial Accounting Standards No. 123R Share Based Payment (SFAS 123R) that required companies to measure the cost of employee services received in exchange for an award of an equity instrument based on the award s fair value on the grant date and recognize the cost over the period during which an employee is required to provide service in exchange for the award, generally the vesting period. We adopted SFAS 123R on January 1, 2006. The adoption did not have a significant impact on our results of operations. See Notes 1 and 4 to our Consolidated Financial Statements in Item 1.

Depreciation and Amortization

Depreciation and amortization expenses were $72.6 million and $41.5 million for the three months ended March 31, 2006 and 2005, respectively. The increase in 2006 over 2005 is due primarily to the increased level of real estate assets and intangible lease assets acquired in the Catellus Merger and other acquisitions and improvements of properties in our property operations segment during this period.

Merger Integration and Relocation Expenses

Merger integration costs are indirect costs associated with the Catellus Merger, such as employee transition costs as well as severance costs for certain of our employees whose responsibilities became redundant after the merger. We expect to incur integration costs associated with the Catellus Merger through the first half of 2006, although the majority of these costs have already been incurred.

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The relocation expenses relate to the move of our corporate headquarters in the first quarter of 2006 and the relocation of our information technology and corporate accounting functions from El Paso, Texas to Denver, Colorado in the first quarter of 2005.

Interest Expense

The following table presents the components of interest expense (in thousands):

	Three Months Ended March 31,	
	2006	**2005**
Gross interest expense	$ 96,485	$ 47,563
Amortization of (premium) discount, net	(3,224)	10
Amortization of deferred loan costs	998	1,360
Interest expense before capitalization	94,259	48,933
Less: capitalized amounts	(23,406)	(12,440)
Net interest expense	$ 70,853	$ 36,493

The increase in interest expense for the three months ended March 31, 2006 as compared with the same period in 2005, is due to increases in our borrowings, primarily as a result of the Catellus Merger, our increased investments in property funds and CDFS joint ventures, individual and portfolio acquisitions and increased development activity, offset somewhat by a decline in weighted average interest rates and additional capitalized interest. The increase in capitalized interest for the three months ended March 31, 2006, as compared with the same period in 2005, is due to the significant increase in our development activities.

Foreign Currency Exchange Gains (Expenses/Losses), Net

We and certain of our foreign consolidated subsidiaries have intercompany or third party debt that is not denominated in that entity s functional currency. When the debt is remeasured against the functional currency of the entity, a gain or loss can result. To mitigate our foreign currency exchange exposure, we borrow in the functional currency of the borrowing entity when possible. Certain of our intercompany debt is remeasured with the resulting adjustment recognized as a cumulative translation adjustment in accumulated other comprehensive income in shareholders equity. This treatment is applicable to intercompany debt that is deemed a permanent source of capital to the subsidiary or investee. If the intercompany debt is deemed not permanent in nature, when the debt is remeasured, we recognize a gain or loss in earnings. Additionally, we utilize derivative financial instruments to manage certain foreign currency exchange risks, primarily put option contracts with notional amounts corresponding to a portion of our projected net operating income from our operations in Europe and Japan. See Note 13 to our Consolidated Financial Statements in Item 1.

Income Taxes

We and one of our consolidated subsidiaries have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended, (the Code), and are not generally required to pay federal income taxes if we make distributions in excess of taxable income and meet the REIT requirements of the Code. Certain of our consolidated subsidiaries in the United States are subject to federal income taxes and we are taxed in certain states in which we operate. In addition, the foreign countries where we have operations do not recognize REITs under their respective tax laws. Accordingly, we recognize income taxes for these jurisdictions, as necessary.

Current income tax expense is generally a function of the level of income recognized by our taxable subsidiaries operating primarily in the CDFS business segment, state income taxes, taxes incurred in foreign jurisdictions and interest associated with our income tax liabilities. Current income taxes were $13.2 million and $1.2 million for the three months ended March 31, 2006 and 2005, respectively. The increase in 2006 over 2005 is due primarily to disposition activity in the United Kingdom, interest expense on tax liabilities and additional income in our taxable subsidiaries due to the Catellus Merger.

The deferred income tax component of total income taxes is generally a function of the period s temporary differences (items that are treated differently for tax purposes than for book purposes), the utilization of tax net operating losses generated in prior years that had been previously recognized as deferred tax assets and deferred tax liabilities related to indemnification agreements related to certain contributions to property funds.

Discontinued Operations

Discontinued operations represent a component of an entity that has either been disposed of or is classified as held for sale if both the operations and cash flows of the component have been or will be eliminated from ongoing operations of the entity as a result of the disposal transaction and the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction. The results of operations of the component of the entity that has been classified as discontinued operations are reported separately as discontinued operations in the statements of earnings. From time to time, we dispose of properties to third parties that are included in our property operations segment. The results of operations for these properties, as well as the gain or loss recognized upon disposition, are included in discontinued operations. In addition, as of March 31, 2006, we had 19 office properties and one hotel property classified as held for sale and therefore, the results of operations of those properties are also included in discontinued operations. See Note 5 to our Consolidated Financial Statements in Item 1 for further discussion of discontinued operations.

Environmental Matters

A majority of the properties acquired by us were subjected to environmental reviews either by us or the previous owners. While some of these assessments have led to further investigation and sampling, none of the environmental assessments have revealed an environmental liability that we believe would have a material adverse effect on our business, financial condition or results of operations.

In connection with the Catellus Merger, we acquired certain properties in urban and industrial areas that may have been leased to or previously owned by commercial and industrial companies that discharged hazardous materials. In accordance with purchase accounting, we recorded a liability for the estimated costs of environmental remediation to be incurred in connection with certain operating properties acquired and properties previously sold by Catellus. This liability was established to cover the environmental remediation costs, including cleanup costs, consulting fees for studies and investigations, monitoring costs and legal costs relating to cleanup, litigation defense, and the pursuit of responsible third parties. In addition, we will incur environmental remediation costs associated with certain land parcels in connection with the future development of the land and have recorded a liability for the estimated costs of remediation. We purchase various environmental insurance policies to mitigate our potential exposure to environmental liabilities. We are not aware of any environmental liability that we believe would have a material adverse effect on our business, financial condition or results of operations.

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Liquidity and Capital Resources

Overview

We consider our ability to generate cash from operating activities, contributions and disposition of properties and from available financing sources to be adequate to meet our anticipated future development, acquisition, operating, debt service and shareholder distribution requirements.

Our credit facilities, primarily the Global Line, provide liquidity and financial flexibility, which allows us to efficiently respond to market opportunR SIZE=1 COLOR=BLACK NOSHADE>

(1) We calculated the value of unexercised options using the difference between the option exercise price and the closing price of Alcoa common stock on the New York Stock Exchange on December 31, 2003 of $38.00 per share, multiplied by the number of shares underlying the option.

(2) Alcoa paid cash dividend equivalents in 2003 on a portion of the exercisable options held by plan participants. Dividend equivalents are equal in amount to the company s common stock dividend. The total amount of dividend equivalents paid in 2003 to all plan participants was approximately $1.8 million.

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PENSION PLANS

Alcoa s pension plans cover a majority of salaried employees. Alcoa pays the full cost of these plans, which include both tax-qualified and non tax-qualified excess plans. This table shows the annual benefits payable for the majority of salaried employees at executive compensation levels.

PENSION PLAN TABLE

Average Annual Compensation	Annual Benefits for Years of Service Indicated					
	15	20	25	30	35	40
$ 100,000	$ 19,650	$ 26,200	$ 32,750	$ 39,300	$ 46,270	$ 54,420
250,000	52,840	70,450	88,060	105,680	123,290	140,900
500,000	108,150	144,200	180,250	216,300	252,350	288,400
750,000	163,460	217,950	272,440	326,930	381,410	435,900
1,000,000	218,780	291,700	364,630	437,550	510,480	583,400
1,250,000	274,090	365,450	456,810	548,180	639,540	730,900
1,500,000	329,400	439,200	549,000	658,800	768,600	878,400
2,000,000	440,030	586,700	733,380	880,050	1,026,730	1,173,400
2,500,000	550,650	734,200	917,750	1,101,300	1,284,850	1,468,400
3,000,000	661,280	881,700	1,102,300	1,322,550	1,542,980	1,763,400
3,500,000	771,900	1,029,200	1,286,500	1,543,800	1,801,100	2,058,400

The company bases the employee s amount of pension upon the average compensation for the highest five years in the last 10 years of service. For the executive level, covered compensation includes base salary and annual cash incentive. We calculate the amounts in the table using salary at target and annual incentive at target. We also make payments as a straight life annuity, reduced by 5% when an employee elects the surviving spouse feature. The table shows benefits at age 65, before any reduction for surviving spouse coverage. The amounts shown do not include social security benefits.

At December 31, 2003, pension service for the named officers was: Mr. Belda, 35 years; Mr. Coleman, 6 years; Mr. Kelson, 29 years; Mr. Leahey, 13 years; and Mr. Pizzey, 33 years.

EQUITY COMPENSATION PLAN INFORMATION

The following table gives information about Alcoa s common stock that could be issued under the company s equity compensation plans as of December 31, 2003.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders[1]	77,944,680	$ 33.37	13,097,943(2)
Equity compensation plans not approved by security holders[3][4]	0	0	0
Total	77,944,680	$ 33.37	13,097,943(2)

(1) Includes the Alcoa Stock Incentive Plan (approved by shareholders in 1999) (the ASIP) and the former Alcoa Long Term Stock Incentive Plan (last approved by shareholders in 1992 and amendments thereto approved by shareholders in 1995).

(2) The ASIP authorizes, in addition to stock options, other types of stock-based awards in the form of stock appreciation rights, contingent stock, performance shares and performance units and stock or other awards valued by reference to Alcoa stock. The shares that remain available for issuance under the ASIP may be issued in connection with any one of these awards. The ASIP has a provision that permits shares repurchased by Alcoa and designated by the Board of Directors to be added to the number of shares available for future issuance under the ASIP. In addition, the following are available to grant under the ASIP: (i) shares subject to awards under the ASIP or prior plan that are forfeited, settle for cash, expire or otherwise terminate without issuance of shares and (ii) shares tendered in payment of the purchase price of an option award under the ASIP or prior plan or tendered or withheld to pay required withholding taxes. As of February 20, 2004, as a result of grants made in January 2004, the remaining number of securities available for future issuance under the ASIP is approximately 5.1 million. As discussed in Item 2 of this proxy statement (Proposal to Approve the 2004 Alcoa Stock Incentive Plan), the Board of Directors has approved a new 2004 Alcoa Stock Incentive Plan, subject to approval by shareholders. If approved, the 2004 plan will replace the ASIP.

(3) In connection with its acquisitions of Alumax, Cordant, Howmet and Reynolds, Alcoa assumed stock options outstanding under these companies stock option plans. An aggregate of 9,893,248 shares of Alcoa common stock are to be issued upon exercise of the outstanding options. The options have a weighted average exercise price of $25.67. No grants of stock options under these plans have been made since the year of Alcoa s acquisition of the particular company, nor will any such grants be made in the future.

(4) The Alcoa Fee Continuation Plan for Non-Employee Directors, adopted in 1990, provided fee continuation payments for persons who met a minimum service requirement as a non-employee director. Each of the eleven eligible participants receives (or will receive) such cash and stock payments for life upon retirement from the Board, or age 65 (whichever is later), based upon the cash retainer fee for directors and an annual stock grant under the company s former Stock Plan for Non-Employee Directors. In 1995, the Board froze future annual payments to eligible directors at a maximum of $30,000 and 2,000 shares (or a lesser proportion based on service). The Plan was otherwise terminated at that time. Alcoa s practice has been to use treasury shares for such share payments. All current fees and other compensation for directors are outlined under Directors Compensation on page 10 of this proxy statement.

ITEM 2 PROPOSAL TO APPROVE THE 2004 ALCOA STOCK INCENTIVE PLAN

In February 2004, Alcoa s Board of Directors approved the 2004 Alcoa Stock Incentive Plan (the Plan), subject to approval by shareholders at the 2004 annual meeting. If approved, the Plan will become effective on May 1, 2004 and will replace the Alcoa Stock Incentive Plan (the Prior Plan) under which Alcoa has primarily made stock option awards. The Board recommends that you vote for approval of the Plan.

In the following pages we have summarized the principal features of the Plan. This summary does not purport to be complete and is qualified in its entirety by reference to the specific language of the Plan. A copy of the Plan is appended to this proxy statement as Attachment G.

Purpose of the Plan

In reviewing the Prior Plan against current and emerging competitive practices, new legal and regulatory developments and good corporate governance trends, management and the Board determined that changes to the long-term incentive design were desirable. The Plan authorizes the Board of Directors, or an authorized committee or subcommittee of the Board, to make stock-based awards to company employees. The purpose of the Plan is to attract, motivate, retain and reward employees by giving them an ownership interest in Alcoa and a proprietary and vested interest in the company's growth and financial success, thereby aligning the interests of management employees with the company s shareholders. The Board believes that the Plan will enhance the company s ability to attract and retain individuals of exceptional managerial, technical and professional talent upon whom, in large measure, the sustained progress, growth and profitability of Alcoa depend.

Differences Between the Plan and the Prior Plan

The Plan offers a number of features differentiating it from the Prior Plan. Those features include:

There is a greater emphasis on granting awards other than stock options. Under the Prior Plan, grants were predominantly stock options, with only a very small portion of the awards made as contingent stock or other stock unit awards. Under this Plan, 25% of the total shares authorized are designated for contingent stock, performance shares or other stock unit awards.

The maximum term of an original option (meaning any option other than a reload option) granted under the Plan will be six years, rather than 10 under the Prior Plan.

The reload feature is limited to option grants made in 2003 and before. Options granted in 2004 and after will not have a reload feature. With respect to any options granted in 2002 or prior years, only one reload option will be granted on or after January 1, 2004, which grant can occur anytime during the remaining term of the underlying option. With respect to the 2003 original option grant, a reload option will be granted only on the first one-third of the grant (vesting in 2004), and that grant must be accomplished on or before December 31, 2004.

As a result of eliminating multiple reloads on prior years grants, and prohibiting reloads on grants made in 2004 and after, the company s stock overhang should be reduced.

The replenishment feature of the Prior Plan is eliminated; any increase in the total number of shares approved for grant under the Plan (beyond the addition of any forfeited awards in the event of retirement, expiration, etc.) will require shareholder approval.

The term of the Plan is five years rather than the Prior Plan s 10 year term.

The Plan provides for a minimum one year vesting period for stock options.

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Other Sound Corporate Governance Practices Continued under the Plan:

No discount stock options. Except in very limited circumstances (see Substitute Awards on page 42), all stock options granted must have an exercise price equal to or greater than the fair market value of the company stock on the date of grant of the option.

No stock option repricings. The prohibition on repricing contained in the Prior Plan is continued under the Plan.

Compensation recognized on exercise of options granted under the Plan should be fully deductible to the company.

Shares Authorized and Award Limits

We are asking you to authorize 30 million shares of Alcoa common stock for issuance under this Plan in connection with options and stock appreciation rights, and 10 million shares of Alcoa common stock for issuance under the Plan in connection with awards of contingent stock, performance shares or other stock unit awards. In addition to those 40 million shares, the following also would be available for grant under the Plan:

Shares subject to awards under the Plan or the Prior Plan that are forfeited, settled for cash, expire or otherwise terminate without share issuance;

Shares tendered in payment of the purchase price of an option award under the Plan or the Prior Plan or tendered or withheld to pay required withholding taxes;

Shares available on the effective date of the Plan for issuance as stock options under the Prior Plan, but not issued thereunder, which shares amounted to approximately 5.1 million shares as of February 20, 2004.

The Plan also contains annual limits on awards to individual participants. In any calendar year, no participant may be granted stock options or stock appreciation rights covering more than 2,000,000 shares or contingent stock or performance shares covering more than 300,000 shares. The maximum dollar value payable to an individual with respect to performance unit awards and other stock unit awards (valued with reference to property other than Alcoa shares) granted in any calendar year is $2,000,000.

Administration

The Compensation and Benefits Committee of the Board, or a subcommittee of that committee, will administer the Plan. Committee members must be independent directors and outside directors to satisfy applicable regulatory requirements. This means that they cannot be current or former Alcoa officers or employees, and they may not receive compensation from Alcoa except in their capacity as directors. The Board may assume responsibilities otherwise assigned to the committee, and it may amend, alter or discontinue the Plan at any time. The Board or the committee may amend the terms of any award previously granted, provided, however, that none of the foregoing actions may impair the existing rights of a participant without the participant s consent, and neither the Board nor the committee may amend the terms of any option to reduce its exercise price. The Board may not amend the Plan without shareholder approval if: a) such amendment would materially increase the benefits received by participants, materially increase the maximum number of shares that may be issued under the Plan, or materially modify the Plan s eligibility requirements; or b) such amendment requires shareholder approval pursuant to tax or regulatory requirements.

The committee has the authority, subject to the terms of the Plan, to select employees to whom it will grant awards, to determine the types of awards and the number of shares covered, to set the terms and conditions of the awards and to cancel or suspend awards. The committee also has authority to interpret the Plan, to establish, amend and rescind rules applicable to the Plan or awards under the Plan, to approve the terms and provisions of any agreements relating to Plan awards and to make all determinations relating to awards under the Plan.

The Plan permits delegation of certain authority to senior officers in limited instances to make, cancel or suspend awards to employees who are not Alcoa directors or executive officers.

Eligibility and Participation

All employees of Alcoa and its subsidiaries are eligible to be selected as participants. About 2,500 current and former employees hold stock option awards under the Prior Plan.

Term

If shareholders approve the Plan, it will become effective on May 1, 2004. No award may be granted under the Plan after April 30, 2009.

Types of Awards

The following types of awards can be granted under the Plan:

Nonqualified stock options (without reload features);

Stock appreciation rights;

Contingent (forfeitable) stock;

Performance shares and performance units conditioned upon meeting performance criteria over a period of time; and

Stock or other awards valued by reference to or based on Alcoa stock or other property.

Stock Option Awards

The committee may grant nonqualified stock option awards under the Plan. Stock option awards entitle a participant to purchase shares of Alcoa stock at a fixed price during the option term. The committee determines the option grant price, but the price may not be less than the fair market value per share on the grant date. The minimum vesting period for stock options is one year. The maximum term of original stock options granted in 2004 and after is six years.

The participant must pay the option grant price in full upon exercise. The participant may pay the price in cash, or by surrendering shares of Alcoa common stock the value of which equals the option price, or by a combination of cash, shares or other consideration approved by the committee.

Options with a reload feature will not be granted under the Plan. However, since grants under the Prior Plan having a reload feature are still outstanding, and all grants under the Prior Plan will be administered under the Plan if the Plan is approved by shareholders, the Plan does permit grant of a reload option in limited circumstances on those options granted under the Prior Plan. With respect to options granted in 2002 or any year prior to that, a participant may, beginning January 1, 2004, be granted a reload option only once during the remaining term of the underlying option. For original options granted in 2003, a participant may be granted only one reload option, and only with respect to the first one-third of the grant vesting in 2004, and that grant must occur on or before December 31, 2004. The term of a reload option will be the same as the remaining term of the underlying option. As a condition to the grant of a reload option, a participant must elect that one-half of the profit shares issued upon exercise of the underlying option may not be sold or transferred for the shorter of five years from the issuance date of the shares or the remainder of the participant s career with Alcoa. The participant then receives a new option having a grant price equal to the current market price, with the same expiration date as the underlying option. The new option covers the number of shares exercised, less the net number of profit shares delivered to the optionee after withholding for taxes. Reload options may be granted where the exercise price of the underlying option is paid using shares owned for a minimum period set by the committee or, in limited instances, using cash.

The committee may permit participants to transfer stock option awards to family members or family trusts. Otherwise, stock option awards are not transferable during the participant s lifetime.

Stock Appreciation Rights

A stock appreciation right (SAR) entitles the holder to receive, on exercise, the excess of the fair market value of the shares on the exercise date (or, if the committee so determines, as of any time during a specified period before the exercise date) over the SAR grant price. The committee may grant SAR awards as stand-alone awards or in combination with a related option award under the Plan. The SAR grant price is set by the committee and may not be less than the fair market value of the shares on the date of grant. Payment upon exercise will be in cash, stock or other property or any combination of cash, stock or other property as the committee may determine. Unless otherwise determined by the committee, any related option will no longer be exercisable to the extent the SAR has been exercised, and the exercise of an option will cancel the related SAR.

Due to current accounting treatment, SAR awards likely will be granted only to non-U.S. residents in locales where option awards have less favorable tax or security law implications for participants.

Contingent Stock

Contingent stock means shares issued with conditions or contingencies and, until the conditions or contingencies are satisfied or lapse, the stock is subject to forfeiture. The committee establishes the terms and conditions applicable to a contingent stock award. The minimum contingency period for a contingent stock award that is not subject to performance conditions is three years from the date of grant, except that the committee may approve contingent stock awards covering up to 200,000 shares with contingency periods of less than three years.

A recipient of a contingent stock award has the right to vote the shares and receive dividends on them unless the committee decides otherwise. If the participant ceases to be an employee before the end of the contingency period, the award is forfeited, subject to such exceptions as authorized by the committee.

Performance Awards

A performance award may be in the form of performance shares (units valued by reference to shares of stock) or performance units (units valued by reference to cash or property other than stock). The committee may select periods of at least one year during which performance criteria chosen by the committee are measured for the purpose of determining the extent to which a performance award has been earned. The committee decides whether the performance levels have been achieved, what amount of the award will be paid and the form of payment, which may be cash, stock or other property or any combination.

Other Stock Unit Awards

The committee may make other awards of shares or of units valued by reference to shares or other property. The committee determines all conditions and terms that apply to these awards. A participant may not sell, assign, transfer, pledge or encumber any award issued with conditions or contingencies until after those conditions lapse. If the only condition to vesting is passage of time, the minimum vesting period is three years.

Deferrals of Awards; Dividends

The committee may permit participants to defer the distribution of all or part of an earned award. The committee also may provide that payments will be made in installments and that dividends or dividend equivalents will be paid on shares covered by outstanding awards.

Substitute Awards

The committee may grant awards to employees of companies acquired by Alcoa or a subsidiary in exchange for or assumption of outstanding stock-based awards issued by the acquired company. Shares covered by substitute awards will not reduce the number of shares otherwise available for award under the Plan. Substitute awards may be granted at a discount rate to the fair market value of Alcoa stock since those awards will be replacing awards that may be in the money .

Option and SAR Repricing Prohibited

The Plan prohibits repricing of options or SARs. Repricing means the grant of a new option, SAR or other award in return for the cancellation, exchange or forfeiture of an award that has a higher grant price than the new award, or the amendment of an outstanding award to reduce the grant price. The grant of a substitute award is not a repricing.

Adjustments

The Plan provides for adjustments of awards and shares authorized for issuance under the Plan in the event of stock splits, recapitalizations, mergers, consolidations, and other changes in the stock. In that event, the committee will make such substitutions or adjustments in the aggregate number or class of shares that may be distributed under the Plan (including the substitution of similar awards denominated in the shares of another company) and in the number, class and option price or other price of shares subject to outstanding awards as it believes equitable or appropriate to maintain the purpose of the original grant.

Change in Control Provisions

In order to preserve the value of outstanding awards for participants in the event of a change in control of Alcoa, unless the committee determines otherwise at the time of grant of a particular award:

- all outstanding option and SAR awards vest and are immediately exercisable;
- any restrictions, conditions or deferral limitations on contingent stock awards or other stock unit awards lapse;
- all shares restricted as a result of exercise of the reload feature become fully transferable; and
- all performance awards will be earned at the target amount of shares covered by the award if the change in control event occurs during the performance period, or at the actual amount of the award if the change in control event occurs thereafter.

Holders of options and SARs may elect to receive a cash settlement of their awards in the event of a change in control. The cash settlement per share is equal to the excess of the highest sales price during the 60-day period leading up to a change in control or, if the change in control event is a merger or tender offer or similar transaction, the highest price paid in that transaction over the grant price per share of the option or SAR.

Change in control of Alcoa means any of the following events:

- the acquisition of a 20% ownership position by any person or group, other than:
  - (i) acquisitions by or from Alcoa;
  - (ii) acquisitions by an Alcoa benefit plan; and
  - (iii) corporate reorganizations in which no person or group becomes a 20% owner or in which the relative equity interests of current shareholders are the same before and after the reorganization
- a change in a majority of the members of the Alcoa Board (other than by individuals whose nomination for director is approved by at least 75% of the incumbent Board members)

a merger, consolidation, or similar transaction, except for:

i) mergers and other corporate transactions in which Alcoa common stock converts into or continues to represent at least 55% of the voting securities of the combined or surviving entity or

(ii) reorganizations in which no entity becomes a 20% holder

a sale of substantially all assets of Alcoa, except to an entity owned at least 55% by the holders of Alcoa common stock in the same proportion as their Alcoa holdings or

a shareholder-approved dissolution or liquidation of Alcoa.

Performance-Based Compensation

Section 162(m) of the Internal Revenue Code limits the amount of the deduction that the company may take on its U.S. federal tax return for compensation paid to any of the named officers in the proxy statement (the Code refers to these officers as covered employees). The limit is $1 million per covered employee per year, with certain exceptions. This deductibility cap does not apply to performance-based compensation, if approved by shareholders. We believe that awards under the Plan will qualify as performance-based compensation if shareholders vote to approve the Plan and it is otherwise administered in compliance with Code section 162(m).

The Plan contains a number of measurement criteria that the committee may use to determine whether and to what extent any covered employee has earned a contingent stock award, performance award or other stock unit award. The measurement criteria that the committee may use to establish specific levels of performance goals include any one or a combination of the following: cumulative net income or cumulative net income per share; return on sales; return on assets; return on capital; return on shareholders equity; cash flow; economic value added; cumulative operating income; total shareholders return; cost reductions; or achievement of environment, health and safety goals. The committee may set performance goals based on the achievement of specified levels of corporate-wide performance or performance of the Alcoa subsidiary or business unit in which the participant works. The committee may make downward adjustments in the amounts payable under an award, but it may not increase the award amounts or waive the achievement of a performance goal.

Tax Aspects of the Plan

The grant of a nonqualified stock option or SAR under the Plan has no U.S. federal income tax consequences for the participant or the company. Upon exercise of a stock option or SAR, Alcoa may take a tax deduction, and the participant realizes ordinary income. The amount of this deduction and income is equal to the difference between the fair market value of the shares on the date of exercise and the grant price of the stock option or SAR. The committee may permit participants to surrender Alcoa shares in order to satisfy the required withholding tax obligation.

Regarding Plan awards (other than options or SARs) that are settled either in cash or in stock or other property that is either transferable or not subject to substantial risk of forfeiture, the participant will generally recognize ordinary income equal to the cash or the fair market value of shares or other property received. Alcoa may take a deduction for the same amount.

Regarding Plan awards (other than options or SARs) that are settled in stock or other property that is subject to contingencies restricting transfer and to a substantial risk of forfeiture, the participant will generally recognize ordinary income equal to the fair market value of the shares or other property received (less any amount paid by the participant) when the shares or other property first become transferable or not subject to substantial risk of forfeiture, whichever occurs first. Alcoa may take a deduction at the same time and for the same amount.

The committee may adjust awards to employees who are not U.S. citizens or U.S. residents to recognize differences in local law or tax policy and may impose conditions on the exercise or vesting of awards to minimize tax equalization obligations for expatriate employees.

Recent Share Price

On February 20, 2004, the closing market price for Alcoa common stock on the New York Stock Exchange was $36.83 per share.

Awards to Named Officers and Other Employees

The Plan is new and no awards have been made under it. The committee has not yet established guidelines or standards on the types of awards it may grant under the Plan to the named officers or other participants or the number of shares that the awards will cover.

Share Repurchases to Prevent Dilution

To prevent or minimize the dilutive effect of stock-based compensation plans, Alcoa s practice has been to repurchase shares in the open market in amounts at least equal to the number of shares issued under employee stock option and other stock incentive plans. Alcoa intends to use the proceeds of stock option award exercises under the Plan for this purpose as well as other funds available from time to time. The continuation of this practice is subject to the company s capital needs and resources and compliance with corporate, securities and regulatory requirements that apply to share repurchases.

Vote Required for Approval

For this proposal to be adopted, a majority of the votes cast by shareholders must be voted for approval.

The Board of Directors recommends a vote FOR ITEM 2. The proxy committee will vote your proxy for this item unless you give instructions to the contrary on the proxy.

ITEM 3 SHAREHOLDER PROPOSALS

ITEM 3(a) SHAREHOLDER PROPOSAL RELATING TO PAY DISPARITY

The Catholic Funds, 1100 West Wells Street, Milwaukee, Wisconsin 53233, owning 2,300 shares of common stock, have notified Alcoa that they intend to present the following proposal at the annual meeting. The names, addresses and shareholdings of the proposal s co-filers will be supplied upon oral or written request. The proposal, as submitted, reads as follows:

WHEREAS:

Commentators note that U.S. CEO compensation is excessive,[1] an occasion of sin tempting CEO s to undertake self-serving ventures[2] that often degrade long-term stock performance.[3] Often CEO pay is driven mainly by what other companies pay. As a result, bosses pay spirals upward,[4] creating a Lake Wobegon effect (where all children have to be above average[5]).

CEO pay once bore a reasonable relationship to the pay of the average or lowest-paid worker. Now the ratio of CEO pay to average-worker pay has skyrocketed from about 40 in 1980 to several hundred currently.[6] The ratio is only 15 to 20 in Japan and Germany today.[7] A huge CEO-to-worker pay gap not only degrades worker and therefore company performance but also violates common moral principles of the common good, love of neighbor, and the dignity and worth of every human being.

Alcoa appears to be part of this national problem. *Business Week* again gave Alcoa a ranking of 1 (the worst) in its 2003 study of CEO compensation versus stock performance.[8] Another study shows Alcoa s 2002 CEO compensation to be 1,358 times the pay of a minimum-wage worker,[9] compared to the S&P500 median of 625 times.[10]

If Alcoa has an unjustifiable gap between the pay of the CEO and the lowest paid worker, the CEO and board should, as New York Fed President William J. McDonough urged, simply reach the conclusion that executive pay is excessive and adjust it to more reasonable and justifiable levels.[11]

RESOLVED: shareholders request the Board s Compensation Committee to initiate a review of our company s executive compensation policies and to make available, upon request, a report of that review by January 1, 2005 (omitting confidential information and processed at a reasonable cost). We request the report include:

1. A comparison of the total compensation package of top executives and our company s lowest paid workers in the United States in July, 1994 and July, 2004.

2. An analysis of changes in the relative size of the gap between the two groups and the rationale justifying this trend.

3. An evaluation of whether our top executive compensation packages (including, but not limited to, options, benefits, perks, loans and retirement agreements) are excessive and should be modified.

4. An explanation of whether the issues of sizable layoffs or the level of pay of our lowest paid workers should result in an adjustment of executive pay to to more reasonable and justifiable levels as suggested by William J. McDonough above.

Notes:

1. Conference Board, 9/17/02 (quoting Greenspan: infectious greed), *Business Week* 4/22/02 (simply out of hand).

2. Edward M. Welch, Justice In Executive Compensation , America 5/19/03

3. Graef Crystal, *Bloomberg* 8/13/03 (high pay destroys high performance).

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4. Economist.com, 10/9/03 *http://www.economist.com/opinion/displayStory.cfm?story_id=2121856*

5. Retired Medtronics CEO Bill George, *Fortune* 9/29/03.

6. Economist.com, *Executive Pay,* 10/9/03

7. Justice In Executive Compensation , *America* 5/19/03

8. April 21, 2003, *http://bwnt.businessweek.com/exec_comp/2003/index.asp*

9. AFL/CIO Executive Paywatch, *www.aflcio.org*

10. Our calculations

11. *WSJ,* 09/12/03

POSITION OF THE BOARD OF DIRECTORS

The Board of Directors recommends a vote **Against** the proposal.

We believe Alcoa s compensation is established in a fair and equitable manner, and that the proposed study would not yield any relevant or meaningful data. Last year, we recommended a vote against a similar proposal. While this year s proposed study is more limited in scope, our objection remains that such a study would not produce any meaningful information to help the Board judge whether Alcoa s current compensation policies and pay levels for the company s management are appropriate.

The Compensation and Benefits Committee of Alcoa s Board of Directors, comprised entirely of independent directors, regularly reviews the company s compensation design. In 2002, the Committee used its own independent compensation consultant to review the results of a comprehensive study of executive compensation that had been completed by management. At the completion of that study, the Board changed the company s total cash compensation targets for executives from above the median down to the median, as compared with an expanded database of approximately 150 comparable companies. In 2003, the Board made significant changes to the company s long-term incentive compensation design to place more executive compensation at risk and link it directly to the attainment of specific transparent financial goals. For 2004, we concluded that both salary and incentive compensation targets for the company s executives are competitive, so both are being held firm at 2003 levels.

The Board believes that the company s executive compensation design is competitive, fair and appropriate and helps the company attract, motivate and retain individuals who can successfully manage a complex, multinational enterprise. Alcoa s compensation framework is designed to reward executives for performance against both financial and non-financial goals, thereby delivering superior value to its shareholders.

We are a values-based company, and we believe that all employees should be treated fairly. We work to ensure that all employees are compensated fairly in accordance with their accountabilities, the relevant regional labor market and individual performance.

The Board of Directors therefore recommends a vote AGAINST ITEM 3(a). The proxy committee will vote your proxy against this item unless you give instructions to the contrary on the proxy.

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ITEM 3(b) SHAREHOLDER PROPOSAL RELATING TO CHANGE IN CONTROL SEVERANCE PLAN

The American Federation of Labor and Congress of Industrial Organizations, 815 Sixteenth Street, N.W., Washington, D.C. 20006, owning 500 shares of common stock, has notified Alcoa that it intends to present the following proposal at the annual meeting. The proposal, as submitted, reads as follows:

Shareholder Proposal

Resolved: Shareholders of Alcoa Inc. (Alcoa or the Company) urge the Board of Directors to seek shareholder approval of the Alcoa Inc. Change in Control Severance Plan (the Severance Plan), or modify the Severance Plan to provide benefits, not to exceed 2 times the sum of any participating executive s base salary plus bonus.

Supporting Statement

At the 2003 annual shareholder meeting, almost 65 percent of Alcoa shareholders casting votes voted in favor of requiring shareholder approval of future executive severance benefits, commonly known as golden parachutes. In response to this vote, the Board of Directors adopted a policy to require shareholder approval of future severance agreements when any such agreement would result in a payment in excess of 2.99 times the salary and bonus of the executive.

However, the Board of Directors did not modify the existing Alcoa Inc. Change in Control Severance Plan. The Severance Plan was adopted by the Board of Directors in 2002 without first seeking shareholder approval. Under the Severance Plan, senior executives are entitled to the equivalent to three years salary, bonus, benefits, pension credit, as well as reimbursement of excise taxes, and six months of outplacement assistance.

In addition to these benefits, stock options granted to Alcoa executives on or after June 1, 1999 provide for acceleration of vesting and become immediately exercisable upon a change in control of Alcoa. We believe that the immediate vesting of stock option compensation, combined with generous severance benefits, may reward underperformance leading up to a change in control and is unnecessary given the high levels of executive compensation at our Company.

In the event of a change in control, we are concerned that the potential cost of the Severance Plan may reduce the value ultimately received by shareholders. We also believe that golden parachutes can encourage senior executives to support a takeover that may not be in the best interests of shareholders because executives know that they will be rewarded if a takeover occurs.

If payments are made under Alcoa s Severance Plan as it is currently structured, the Company will be penalized under the Tax Reform Act of 1984. When severance benefits exceed 3 times an executive s average W-2 compensation, all benefits in excess of one year s compensation are subject to a 20 percent golden parachutes excise tax. Not only has Alcoa promised to reimburse executives for these taxes, but the Company will lose its tax deduction for the cost of these benefits.

The Council of Institutional Investors, a coalition of over 130 pension funds whose assets exceed $2 trillion, believes that Boards of Directors should take actions recommended in shareholder proposals that receive a majority of votes cast for and against. In 2003, several other companies including Tyco, Sprint, Union Pacific, International Paper, and Hewlett Packard revised their severance policies after a majority of their shareholders voted in favor or similar proposals.

For the above reasons, please vote FOR this proposal.

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POSITION OF THE BOARD OF DIRECTORS

The Board of Directors recommends a vote **Against** the proposal.

The proponents 2003 shareholder proposal, favored by less than a majority of the total voting shares outstanding, but 65% of the votes cast, was that the Board of Directors seek shareholder approval for future severance agreements with senior executives that provide benefits in an amount exceeding 2.99 times the sum of the executive s base salary and bonus. Following the annual shareholders meeting, the Compensation and Benefits Committee of the Board (Compensation Committee) took the matter under advisement, and in September 2003, the full Board passed a resolution requiring submission of any such agreement to shareholders for approval.

The Board originally approved a Change in Control plan in 2002 after careful review by the Compensation Committee, which consulted with its own outside compensation expert. The plan would become effective in very limited circumstances, and is designed to ensure that the Board receives steady and objective advice from executive management if faced with the prospect of a change in the company s ownership. By providing executives with financial security when their jobs may be threatened, the plan is designed to protect the interests of shareholders by

keeping key employees focused on negotiating the best possible value for the company in a change in control situation. Payments under the plan would occur only after a change in control occurred. The plan would not pay a windfall to a voluntarily departing executive.

The Board concluded from its study that the majority of comparable companies have in place change in control plans, or they put one in place when the prospect of a change in ownership arises. The Board also determined that the terms of the plan, which are essentially three times salary and bonus, three years of continuation of benefits, three years of pension credits, outplacement assistance and reimbursement of excise taxes and gross-up, were appropriate. Approval of the plan was appropriately disclosed.

The accelerated vesting of stock options upon the occurrence of a change in control, which the proponents mention in their statement, is a specific provision in the Alcoa Stock Incentive Plan that was approved by the shareholders in 1999.

Although the proponents last year favored a 2.99 cap on severance agreements prior to requiring them to be submitted for shareholder approval, this year they ve deemed a 2.0 cap to be appropriate. We believe that arbitrarily selected caps are not the issue. The Board is very aware of its fiduciary responsibilities to the company (for the benefit of the shareholders), and its obligation to exercise its business judgment in the decisions it makes. We are confident that in approving this plan we have satisfied both obligations.

The Board of Directors therefore recommends a vote AGAINST ITEM 3(b). The proxy committee will vote your proxy against this item unless you give instructions to the contrary on the proxy.

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OTHER INFORMATION

LEGAL PROCEEDING INVOLVING DIRECTORS AND CERTAIN ALCOA OFFICERS

As previously reported, on October 15, 1999, Victoria Shaev, who represents that she is an Alcoa shareholder, filed a purported derivative action on behalf of the company in the United States District Court for the Southern District of New York, naming as defendants the company, each member of Alcoa s Board of Directors, certain officers of the company and PricewaterhouseCoopers LLP, Alcoa s independent accountants. The lawsuit alleged, among other things, that Alcoa s proxy statement dated March 8, 1999 contained materially false and misleading statements and omissions regarding the proposed Alcoa Stock Incentive Plan. On March 19, 2001, the court granted without prejudice the defendants motion to dismiss the plaintiff s claims. On May 31, 2001, Ms. Shaev served an amended complaint making the same allegations as in the previous complaint but styling the complaint as a class action on behalf of shareholders. The company served a motion to dismiss on June 25, 2001. On October 25, 2002, the amended complaint was dismissed on the factual and legal merits of the matter. The plaintiff filed a notice of appeal, and on September 17, 2003, the Second Circuit Court of Appeals affirmed the dismissal of the amended complaint.

CHANGE IN CONTROL PLAN

In 2002, the Board approved a change in control severance plan for key executives designated by the Compensation and Benefits Committee. The severance plan entitles these executives to termination compensation if the executive s employment is terminated without cause or terminated by the executive in certain circumstances, in either case within three years after a change in control of the company. Termination compensation includes: a cash payment equal to three times annual salary plus target annual variable compensation; continuation of benefits for three years; growth on pension credits for three years; reimbursement of excise taxes and gross-up, and six months outplacement.

HOUSEHOLDING INFORMATION

We have adopted a procedure approved by the Securities and Exchange Commission called householding. Under this procedure, shareholders of record who have the same last name and address will receive only one copy of our Annual Report for 2003. This procedure will reduce our printing costs and postage fees. Shareholders who participate in householding will continue to receive separate proxy statements this year, as well as proxy cards. Also, householding will not in any way affect dividend check mailings.

If you participate in householding and wish to receive a separate copy of the 2003 Annual Report, please call 1 (800) 522-6757, or request a copy in writing from Alcoa, Corporate Communications, 201 Isabella Street, Pittsburgh, Pennsylvania 15212-5858, and a copy will be provided to you promptly.

If you do not wish to continue participating in householding and prefer to receive separate copies of future Annual Reports and other shareholder communications, please notify Alcoa in writing at the following address: Corporate Election Services, P.O.Box 1150, Pittsburgh Pennsylvania 15230-1150.

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ATTACHMENT A

DIRECTOR INDEPENDENCE STANDARDS

1. In no event will a Director be considered independent unless the Board of Directors affirmatively determines that the Director has no material relationship with Alcoa Inc. (Alcoa) or any subsidiary in the consolidated group (together with Alcoa, the Company), either directly or as a partner, shareholder or officer of an organization that has a relationship with the Company, other than the Director s relationship with Alcoa as a Director. In each case, the Board shall consider all relevant facts and circumstances and shall apply these Director Independence Standards.

2. If, within the preceding three years:

   The Director was employed by the Company; or

   An immediate family member of the Director was employed by the Company as an executive officer; or

   The Director received, or his or her immediate family member received, more than $100,000 a year in direct compensation from the Company, other than Director and Committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service) (Compensation received by an immediate family member for service as a non-executive employee of the Company need not be considered in determining independence under this test.); or

   The Director was affiliated with or employed by the Company s present or former external auditor; or

   An immediate family member of the Director was affiliated with or employed in a professional capacity by the Company s present or former external auditor; or

   A current executive officer of the Company served on the compensation committee of the board of directors of a company that employed as an executive officer either the Director or an immediate family member of the Director; or

   The Director is an employee or executive officer, or his or her immediate family member is an executive officer of another company that made payments to, or received payments from, the Company for property or services in an amount that, in any single fiscal year, exceeded the greater of $1 million or 2% of such other company s consolidated gross revenues (for purposes of this clause, charitable organizations will not be considered companies);

   then that Director will be deemed to have a material relationship with the Company and will be deemed not to be independent.

3. It would not be considered to be a material relationship that would impair a Director s independence if, in any year within the preceding three years:

   A Director of Alcoa served as an employee or executive officer of a charitable or other not-for-profit organization, or his or her immediate family member served as an executive officer of a charitable or

   not-for-profit organization, and the Company s or the Alcoa Foundation s charitable contributions to the organization, in the aggregate, were less than two percent (or $250,000, whichever is greater) of that organization s consolidated gross revenues.

A Director of Alcoa served as an executive officer of another company that was indebted to the Company, or to which the Company was indebted, and the amount of either company s indebtedness to the other at the end of the year was less than 5% of the total consolidated assets of the Company or of the company the Director serves as an executive officer.

4. The Board will annually review all commercial and charitable relationships of Directors. The determination as to whether Directors meet these Independence Standards will be disclosed in the proxy statement.

5. In addition to the Independence Standards applicable to independent Directors generally, Audit Committee members may not accept, directly or indirectly, any consulting, advisory, or other compensatory fee from the Company, other than director fees and any regular benefits that other Directors receive for services on the Board or Board Committees. For purposes of this Paragraph 5, prohibited indirect payments include payments received by an Audit Committee member s spouse, minor children or stepchildren, or children or stepchildren sharing a home with the Director, as well as payments received by an entity in which the Director is a partner, member, managing director, executive officer or in which the Director holds a similar position, which entity provides accounting, consulting, legal, investment banking or financial advisory services to the Company. In addition, no Audit Committee member can be an affiliated person of the Company, meaning that no Audit Committee member can beneficially own, directly or indirectly, more than 10% of the voting securities of the Company.

6. For any relationships not covered by the guidelines in paragraphs 2 or 3 above, the determination of whether the relationship is material or not, and therefore whether the Director is independent or not, will be made by the Directors who satisfy the independence standards contained in paragraphs 2 and 3 above. Alcoa will explain in its next proxy statement the basis for any Board determinations regarding such relationships.

7. For purposes of the determination of a Director s independence, immediate family member means a Director s spouse, parents, children, siblings, mother-in-law and father-in-law, sons-in-law and daughters-in-law, brothers-in-law and sisters-in-law, and anyone (other than domestic employees) who shares the Director s home. When applying the three-year look-back provision in paragraph 2 and the test in paragraph 3, individuals will not be considered who are no longer immediate family members as a result of legal separation, divorce, death or incapacity.

8. As used herein, executive officer means the CEO or president, the principal financial officer, the principal accounting officer, any officer in charge of a principal business unit or function and any other individual who performs a policy-making function. Executive officers of subsidiaries may be deemed executive officers of a corporation or other entity if they perform such policy-making functions for the corporation or other entity.

9. If a Director is determined by the Board not to be independent under these Standards, he or she cannot serve on the Audit Committee, the Governance and Nominating Committee or the Compensation and Benefits Committee of the Board.

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ATTACHMENT B

AUDIT COMMITTEE CHARTER

Mission Statement

The primary purpose of the Audit Committee (the Committee) of the Board of Directors (the Board) of Alcoa Inc. (the Company) is:

(A) to assist the Board of Directors to fulfill its oversight of the integrity of the Company s financial statements, the Company s compliance with legal and regulatory requirements, the independent auditor s qualifications and independence, and the performance of the Company s internal audit function and independent auditors; and

(B) to prepare the audit committee report required by the rules of the Securities and Exchange Commission (the SEC) to be included in the Company s annual proxy statement.

Membership

The Committee shall consist of at least three directors, the exact number to be determined from time to time by the Board.

The members of the Committee shall meet the independence requirements imposed by the listing standards of the New York Stock Exchange (the NYSE), law or regulation. At least one member of the Committee shall be an audit committee financial expert, as determined by the Board.

The members of the Committee shall be appointed by a majority vote of the Board from among its members based on the recommendations of the Governance and Nominating Committee and shall serve until such member s successor is duly appointed and qualified or until such member s resignation or removal by a majority vote of the Board.

No member of the Committee may serve simultaneously on the audit committees of more than two other public companies, unless the Board determines that such simultaneous service would not impair such director s ability to serve effectively on the Committee and such determination is disclosed in the Company s annual proxy statement.

Authority and Responsibilities

The Committee s function is not to replace the Company s management, internal auditors and outside auditors, but rather one of oversight. It is the responsibility of the Company s management to prepare the Company s financial statements and to develop and maintain adequate systems of internal accounting and financial controls, and it is the internal and outside auditors responsibility to review, and when appropriate, audit these financial statements and internal controls. The Committee recognizes that the financial management and the internal and outside auditors have more knowledge and information about the Company than do Committee members. Consequently, in carrying out its oversight responsibilities, the Committee cannot provide any expert or special assurance as to the Company s financial statements or internal controls or any professional certification as to the outside auditors work.

In carrying out its oversight responsibilities, the Committee shall undertake the following activities and have the following authority (in addition to any others that the Board may from time to time delegate to the Committee):

Relationship with Auditors

1. The Committee shall have sole authority and be directly responsible for the retention, compensation, oversight, evaluation and termination (subject, if applicable, to shareholder ratification) of the work of the Company s outside auditors for the purpose of preparing or issuing an audit report or related work. The Company s outside auditors shall report directly to the Committee.

2. The Committee shall review and pre-approve (a) auditing services (including those performed for purposes of providing comfort letters and statutory audits) and (b) non-auditing services that exceed a *de minimis* standard established by the Committee, which are rendered to the Company by its outside auditors (including fees).

3. The Committee shall:

   (a) receive from the outside auditors, at least annually, a written report describing: (i) the outside auditors internal quality-control procedures; (ii) any material issues raised by the most recent internal quality-control review or peer review of the outside auditors, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, with respect to one or more independent audits carried out by the outside auditors, and any steps taken to deal with any such issues; and (iii) (to assess the outside auditors independence) all relationships between the outside auditors and the Company, including the matters covered by Independence Standards Board Standard Number 1; and

   (b) review and discuss with the outside auditors any relationships or services that may impact the objectivity and independence of the outside auditors.

4. After reviewing the foregoing report and the outside auditors work throughout the year, the Committee shall evaluate the outside auditors qualifications, performance and independence. This evaluation shall include the review and evaluation of the lead partner(s) of the outside auditors. In making its evaluation, the Committee may take into account the opinions of management and the Company s internal auditors (or other personnel responsible for the internal audit function) and shall take appropriate action in response to the outside auditors report and the opinions of those the Committee consults to satisfy itself of the outside auditors independence and adequate performance.

5. The Committee should further consider whether, in order to assure the continuing independence of the outside auditors, there should be regular rotation of the lead audit partner (in addition to what may already be required by law or regulation).

6. The Committee shall establish clear hiring policies with respect to employees and former employees of the outside auditors.

7. The Committee shall review and discuss with management, the outside auditors and the internal auditors the performance and adequacy of the Company s internal audit function, including the internal auditors responsibilities, budget, staffing, the Internal Audit Statement of Responsibilities and any proposed changes in the audit scope, plan or procedures from the prior period.

Financial Reporting Process and Financial Statements

8. The Committee shall meet regularly with management. In addition, the Committee shall meet separately, and without management present (and, in any event, not less than four times a year) with (a) the General Counsel of the Company; (b) the Chief Financial Officer of the Company; (c) the Company s internal auditors; and (d) the Company s outside auditors.

9. The Committee shall review and discuss with management and the outside auditors on a quarterly basis prior to filing quarterly or annual financial statements:
   (a) the audited financial statements to be included in the Company s Annual Report on Form 10-K (or the Annual Report to Shareholders if distributed prior to the filing of the Form 10-K);

   (b) the quarterly financial statements to be included in Form 10-Q;

   (c) the Company s disclosures in the related Management s Discussion and Analysis of Financial Condition and Results of Operations;

   (d) the Company s disclosure controls and procedures (including any significant internal control deficiencies or material weaknesses and any changes implemented in light of material control deficiencies or weaknesses); and

   (e) any fraud that involves management or other employees who have a significant role in the Company s internal controls.

10. In connection with the annual audit and review by the outside auditors of the financial information included in the Company s Quarterly Reports on Form 1 0-Q, the Committee shall, prior to the filing of the Form 10-K or Form 10-Q, as applicable, discuss with the outside auditors the results of their audit or review and the matters required to be discussed by Statement on Auditing Standards No. 61 (SAS 61), as amended or supplemented. In addition, the Chairman or his designee shall, before the quarterly earnings press releases are released, discuss with the outside auditors the results of their review of quarterly earnings press releases and the matters required to be discussed by SAS 61.

11. The Committee shall receive from the Company s outside auditors and, where applicable, the Company s internal auditors, timely reports concerning:
   (a) major issues regarding accounting principles and financial statement presentations, including all critical accounting policies and practices and any changes in the selection or application of accounting principles;

   (b) all significant financial reporting issues and judgments, including all critical accounting estimates and alternative treatments of financial information within generally accepted accounting principles that have been discussed with the management of the Company, the ramifications of the use of such alternative estimates or treatments and the estimate/treatment preferred by the auditors;

   (c) the effect of regulatory or accounting initiatives, as well as off-balance sheet transactions, on the financial statements; and

   (d) any material written communications between the auditors and the management of the Company (such as any management letter or schedule of unadjusted differences).

12. The Committee shall review with the outside auditors and the internal auditors any audit problems or difficulties encountered (including any restrictions on the scope of the independent auditor s activities or on access to requested information, and any significant disagreements with management) and management s response. The Committee shall be responsible for the resolution of disagreements among the Company s management, the outside auditors and the internal auditors regarding financial reporting.

13. The Committee shall review with the internal auditor and the external auditor their annual audit plans and the degree of coordination of such plans.

14. Based on the above review and discussions, the Committee shall determine whether to recommend to the Board that the Company s audited financial statements be included in the Company s Annual Report on Form 10-K.

15. The Committee shall prepare the report of the audit committee required by the rules of the SEC to be included in the Company s annual proxy statement.

16. The Committee shall periodically discuss with management the types of information to be disclosed and the types of presentations to be made in quarterly earnings press releases and with respect to financial information and earnings guidance provided to analysts and rating agencies or otherwise made public.

Risk Management

17. The Committee shall discuss with management, the internal auditors and the outside auditors the Company s policies with respect to risk assessment and risk management. This discussion should cover the Company s major financial risk exposures and the steps management has taken to monitor and control these exposures.

18. The Committee shall review the annual audit report regarding officers expense accounts and perquisites and the results of the annual survey of compliance with the Company s Business Conduct Policies.

Compliance with Laws, Regulations and Ethics Codes

19. The Committee shall review with the Company s general counsel, the internal auditors and other appropriate parties legal matters that may have a material impact on the Company s financial statements, the Company s compliance policies and procedures and any material reports received from or communications with regulators or government agencies.

20. The Committee shall
    (a) regularly receive reports from management regarding compliance with the Business Conduct Policies and the Code of Ethics for the CEO, CFO and Other Financial Professionals and the procedures established to monitor compliance with the Business Conduct Policies and the Code of Ethics for the CEO, CFO and Other Financial Professionals;

    (b) review requests for waivers from (i) the Code of Ethics for the CEO, CFO and Other Financial Professionals; and (ii) from the Business Conduct Policies with respect to directors and executive officers; and

    (c) promptly disclose any waivers that are required by regulation or listing standards to be disclosed publicly.

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21. The Committee shall oversee and regularly review the adequacy and performance of established procedures for:
    (a) the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls and/or auditing matters; and

    (b) the confidential, anonymous submission by Company employees of concerns regarding questionable accounting or auditing matters.

Performance Evaluation

22. The Committee shall review its own performance and reassess the adequacy of this Charter at least annually in such manner as it deems appropriate, and submit such evaluation, including any recommendations for change, to the full Board for review, discussion and approval.

Access to Advisors

23. The Committee shall have the authority to engage and obtain advice and assistance from internal or external legal, accounting or other advisors, without having to seek Board approval.

24.

The Committee shall make determinations with respect to funding by the Company with respect to the payment of the Company s outside auditors and any other advisors retained by the Committee.

Structure and Operations

The Board shall designate one member of the Committee to act as its chairperson. The Committee shall meet in person or telephonically at least four times per year at such times and places determined by the Committee chairperson, with further meetings to occur, or actions to be taken by unanimous written consent, when deemed necessary or desirable by the Committee or its chairperson. The chairperson, with input from the other members of the Committee, shall set the agendas for Committee meetings; such agendas shall be distributed to the full Board. Two members of the Committee shall constitute a quorum; when more than two members are present, the act of a majority of such members at a meeting at which a quorum exists shall be the act of the Committee, and when only two members are present, the unanimous vote of the two members shall constitute the act of the Committee.

The Committee may request that any directors, officers or other employees of the Company, or any other persons whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests. The Committee may exclude from its meetings any persons it deems appropriate in order for it to fulfill its responsibilities.

The Committee may form and delegate authority to subcommittees when appropriate. In particular, the Committee may also delegate to one or more of its members the authority to pre-approve audit and/or non-audit services, provided that the decisions of any member(s) to whom pre-approval authority is delegated shall be presented to the Committee at the next Committee meeting.

The Committee shall maintain minutes or other records of its meetings and shall give regular reports to the Board on these meetings, including the Committee s actions, conclusions and recommendations and such other matters as required by this Charter or as the Board may from time to time specify.

Except as expressly provided in this Charter, the Company s by-laws or the Company s Corporate Governance Guidelines, or as required by law, regulation or NYSE listing standards, the Committee shall set its own rules of procedure.

Compensation

No member of the Committee may receive, directly or indirectly, any compensation from the Company other than (i) fees paid to directors for service on the Board (including customary perquisites and other benefits that all directors receive), (ii) additional fees paid to directors for service on a committee of the Board (including the Committee) or as the chairperson of any committee and (iii) a pension or other deferred compensation for prior service that is not contingent on future service on the Board.

ATTACHMENT C

COMPENSATION AND BENEFITS COMMITTEE CHARTER

Mission Statement

The purpose of the Compensation and Benefits Committee (the Committee) of the Board of Directors (the Board) of Alcoa Inc. (the Company) is to (i) discharge the Board s responsibilities relating to the compensation of the Company s officers, (ii) oversee the administration of the Company s compensation and benefits plans, in particular the incentive compensation and equity-based plans of the Company (and, to the extent appropriate, the significant subsidiaries of the Company) and (iii) prepare the annual report on executive compensation required by the rules and regulations of the Securities and Exchange Commission (the SEC) to be included in the Company s annual proxy statement.

Membership

The Committee shall consist of no fewer than three members, the exact number to be determined from time to time by the Board.

Each member of the Committee shall meet the independence requirements imposed by the listing standards of the New York Stock Exchange (the NYSE).

The members of the Committee shall be appointed by a majority vote of the Board from among its members based on the recommendations of the Governance and Nominating Committee and shall serve until such member s successor is duly appointed and qualified or until such member s

resignation or removal by a majority vote of the Board.

Authority and Responsibilities

The Committee shall have the following specific authority and responsibilities (in addition to any others that the Board may from time to time delegate to the Committee):

1. The Committee shall periodically review and approve general compensation and benefit policies of the Company and its significant subsidiaries.

Executive Compensation

2. The Committee shall at least annually (a) review and approve the corporate goals and objectives relevant to the compensation of the Company s Chief Executive Officer (the CEO), (b) evaluate the CEO s performance in light of these goals and objectives and (c) set the CEO s compensation level based on this evaluation.

3. The Committee shall at least annually review and approve the compensation for the other officers of the Company, including (a) the annual base salary, (b) the annual incentive opportunity, (c) the long-term incentive opportunity, and (d) any special or supplemental benefits.

4. The Committee shall approve any employment agreements, consulting arrangements, severance or retirement arrangements and/or change-in-control agreements or provisions covering any current or former officer of the Company, including without limitation, the approval of all contracts of the Company with any officer for remuneration (whether in the form of a pension, deferred compensation or otherwise) to be paid from the general funds of the Company after the termination of regular employment of such officer.

5. The Committee shall review and approve the Company s policies and procedures with respect to officers expense accounts, special one-time payments and loans to officers made, arranged or guaranteed by the Company.

Director Compensation

6. The Committee shall periodically review and make recommendations to the Board regarding director compensation.

Compensation Plans

7. The Committee shall oversee the implementation and administration of the compensation plans of the Company (and, to the extent appropriate, the significant subsidiaries of the Company), including pension, savings, incentive and equity-based plans; provided that, the Committee shall not exercise any of its authority with respect to any of its members.

8. The Committee shall review and make recommendations to the Board with respect to, or approve, any incentive compensation plans and equity-based plans for the Company (and, to the extent appropriate, the significant subsidiaries of the Company) to be adopted or submitted to shareholders for approval.

9. The Committee shall periodically review the investment management of the Company s principal retirement and savings plans.

10. The Committee shall review and make recommendations to the Board with respect to, or approve, all awards of shares or share options pursuant to the Company s (and, to the extent appropriate, the Company s significant subsidiaries) equity-based plans; provided that, the Committee shall not exercise any of its authority with respect to any of its members.

SEC Report

11. The Committee shall produce the annual report on executive compensation required to be included in the Company s annual proxy statement in accordance with applicable SEC rules and regulations.

Performance Evaluation

12. The Committee shall review its own performance and reassess the adequacy of this Charter at least annually in such manner as it deems appropriate, and submit such evaluation, including any recommendations for change, to the full Board for review, discussion and approval.

Retention of Consultants and Advisors

13.

The Committee shall have authority to retain and terminate any compensation consultant to be used to assist in the evaluation of CEO or officer compensation and shall have authority to approve the consultant s fees and other retention terms.

Structure and Operations

The Board shall designate one member of the Committee to act as its chairperson. The Committee shall meet in person or telephonically at least three times a year at such times and places determined by the Committee chairperson, with further meetings to occur, or actions to be taken by unanimous written consent, when deemed necessary or desirable by the Committee or its chairperson. The chairperson, with input from the other members of the Committee, shall set the agendas for Committee meetings;

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such agendas shall be distributed to the full Board. Two members of the Committee shall constitute a quorum; when more than two members are present, the act of a majority of such members at a meeting at which a quorum exists shall be the act of the Committee, and when only two members are present, the unanimous vote of the two members shall constitute the act of the Committee.

The Committee may request that any directors, officers or other employees of the Company, or any other persons whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests. The Committee may exclude from its meetings any persons it deems appropriate in order for it to fulfill its responsibilities.

The Committee may form and delegate authority to subcommittees when appropriate.

The Committee shall maintain minutes or other records of its meetings and shall give regular reports to the Board on these meetings, including the Committee s actions, conclusions and recommendations and such other matters as required by this Charter or as the Board shall from time to time specify. Reports to the Board may take the form of oral reports by the chairperson of the Committee or any other member of the Committee designated by the Committee to give such report.

Except as expressly provided in this Charter, the Company s by-laws or the Company s Corporate Governance Guidelines, or as required by law, regulation or NYSE listing standards, the Committee shall set its own rules of procedure.

ATTACHMENT D

GOVERNANCE AND NOMINATING COMMITTEE CHARTER

Mission Statement

The purpose of the Governance and Nominating Committee (the Committee) of the Board of Directors (the Board) of Alcoa Inc. (the Company) is to (i) identify individuals qualified to become Board members and recommend such individuals to the Board for nomination for election to the Board, (ii) make recommendations to the Board concerning committee appointments other than this Committee, (iii) develop, recommend and annually review corporate governance guidelines for the Company and oversee corporate governance matters and (iv) coordinate an annual review of the Board s performance.

Membership

The Committee shall consist of no fewer than three members, the exact number to be determined from time to time by the Board.

Each member of the Committee shall meet the independence requirements imposed by the listing standards of the New York Stock Exchange (the NYSE).

The members of the Committee shall be appointed by a majority vote of the Board from among its members and shall serve until such member s successor is duly appointed and qualified or until such member s resignation or removal by a majority vote of the Board.

Authority and Responsibilities

The Committee shall have the following specific authority and responsibilities (in addition to any others that the Board may from time to time delegate to the Committee):

Board Nominees; Committee Appointments; Continued Service

1. The Committee shall determine the criteria, objectives and procedures for selecting Board members. The Committee shall consider factors such as independence, diversity, age, integrity, skills, expertise, breadth of experience, knowledge about the Company s business or industry and willingness to devote adequate time and effort to Board responsibilities in the context of the existing composition and needs of the Board and its committees.

2. The Committee shall (a) review potential candidates for the Board suggested to it and report to the Board regarding the results of such review; (b) recommend nominations for election and re-election to the Board and (c) recommend appointments to the Board to fill vacancies.

3. In the case of an individual recommended to fill a Board vacancy created by an increase in the size of the Board, the Committee shall make a recommendation to the Board as to the class of directors in which the individual should serve.

4. The Committee shall review the appropriateness of continued service on the Board of members whose business or professional affiliations or responsibilities have changed or who contemplate accepting a directorship on another public company board or an appointment to an audit or compensation committee of another public company board.

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5. The Committee shall identify Board members qualified to fill vacancies on any committee of the Board (other than the Committee) and recommend that the Board appoint the identified member or members to the respective committee. In recommending a candidate for appointment to a committee, the Committee shall consider any required qualifications as set forth in the committee s charter, the needs of the committee in light of its purpose and responsibilities and the existing composition of the committee, the benefits of periodic rotation of committee members and any other factors the Committee deems appropriate.

Corporate Governance

6. The Committee shall review the effectiveness of orientation process for newly elected members of the Board. The Committee shall also regularly assess the adequacy of and need for additional continuing director education programs.

7. The Committee shall recommend to the Board corporate governance guidelines for the Company, assess those guidelines at least annually and review any requests for waivers of those guidelines.

Board Performance

8. The Committee shall coordinate the annual evaluation of the structure, organization, policies, performance and effectiveness of the Board.

Performance Evaluation

9. The Committee shall review its own performance and reassess the adequacy of this Charter at least annually in such manner as it deems appropriate, and submit such evaluation, including any recommendations for change, to the full Board for review, discussion and approval.

Retention of Consultants and Advisors

10. The Committee shall have authority to retain and terminate any search firm to be used to identify director candidates, including authority to approve the search firm s fees and other retention terms.

Structure and Operations

The Board shall designate one member of the Committee to act as its chairperson. The Committee shall meet in person or telephonically at least two times a year at such times and places determined by the Committee chairperson, with further meetings to occur, or actions to be taken by unanimous written consent, when deemed necessary or desirable by the Committee or its chairperson. The chairperson, with input from the other members of the Committee, shall set the agendas for Committee meetings; such agendas shall be distributed to the full Board. Two members of the Committee shall constitute a quorum; when more than two members are present, the act of a majority of such members at a meeting at which a quorum exists shall be the act of the Committee, and when only two members are present, the unanimous vote of the two members shall constitute the act of the Committee.

The Committee may request that any directors, officers or other employees of the Company, or any other persons whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests. The Committee may exclude from its meetings any persons it deems appropriate in order for it to fulfill its responsibilities.

The Committee may form and delegate authority to subcommittees when appropriate.

The Committee shall maintain minutes or other records of its meetings and shall give regular reports to the Board on these meetings, including the Committee s actions, conclusions and recommendations and such other matters as required by this Charter or as the Board shall from time to time specify. Reports to the Board may take the form of oral reports by the chairperson of the Committee or any other member of the Committee designated by the Committee to give such report.

Except as expressly provided in this Charter, the Company s by-laws or the Company s corporate governance guidelines, or as required by law, regulation or NYSE listing standards, the Committee shall set its own rules of procedure.

ATTACHMENT E

PUBLIC ISSUES COMMITTEE CHARTER

Mission Statement

The purpose of the Public Issues Committee (the Committee) of the Board of Directors (the Board) of Alcoa Inc. (the Company) is to provide advice and guidance on public issues that may affect the Company.

Membership

The Committee shall consist of no fewer than three members, the exact number to be determined from time to time by the Board.

The members of the Committee shall be appointed by a majority vote of the Board from among its members based on the recommendations of the Governance and Nominating Committee and shall serve until such member s successor is duly appointed and qualified or until such member s resignation or removal by a majority vote of the Board.

Authority and Responsibilities

The Committee shall have the following specific authority and responsibilities (in addition to any others that the Board may from time to time delegate to the Committee):

1. The Committee shall oversee the Company s policies and procedures on corporate charitable giving.
2. The Committee shall make recommendations to the Board on significant shareholder issues.
3. The Committee shall identify and bring to the attention of the Board as appropriate, current and emerging political, social and environmental trends and public policy issues that may affect the business operations, performance or public image of the Company.
4. The Committee shall provide oversight of the Company s reports on social and environmental issues under the Global Reporting Initiative.

Performance Evaluation

The Committee shall review its own performance and reassess the adequacy of this Charter at least annually in such manner as it deems appropriate, and submit such evaluation, including any recommendations for change, to the full Board for review, discussion and approval.

Structure and Operations

The Board shall designate one member of the Committee to act as its chairperson. The Committee shall meet in person or telephonically at least two times a year at such times and places determined by the Committee chairperson, with further meetings to occur, or actions to be taken by unanimous written consent, when deemed necessary or desirable by the Committee or its chairperson. The chairperson, with input from the other members of the Committee, shall set the agendas for Committee meetings; such agendas shall be distributed to the full Board. Two members of the Committee shall constitute a quorum; when more than two members are present, the act of a majority of such members at a meeting at which a quorum exists shall be the act of the Committee, and when only two members are present, the unanimous vote of the two members shall constitute the act of the Committee.

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The Committee may request that any directors, officers or other employees of the Company, or any other persons whose advice and counsel are sought by the Committee, attend any meeting of the Committee to provide such pertinent information as the Committee requests. The Committee may exclude from its meetings any persons it deems appropriate in order for it to fulfill its responsibilities.

The Committee may form and delegate authority to subcommittees when appropriate.

The Committee shall maintain minutes or other records of its meetings and shall give regular reports to the Board on these meetings, including the Committee s actions, conclusions and recommendations and such other matters as required by this Charter or as the Board shall from time to time specify. Reports to the Board may take the form of oral reports by the chairperson of the Committee or any other member of the Committee designated by the Committee to give such report.

Except as expressly provided in this Charter, the Company s by-laws or the Company s Corporate Governance Guidelines, or as required by law, regulation or NYSE listing standards, the Committee shall set its own rules of procedure.

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ATTACHMENT F

PRE-APPROVAL POLICIES AND PROCEDURES ADOPTED BY THE AUDIT COMMITTEE IN APRIL 2003 FOR AUDIT AND NON-AUDIT SERVICES

I. Statement of Policy

The Audit Committee is required to pre-approve the audit and non-audit services performed by the independent auditor in order to assure that the provision of such services does not impair the auditor s independence. Unless a type of service to be provided by the independent auditor has received general pre-approval under this policy, it will require specific approval by the Audit Committee before the service is provided. Any proposed services exceeding pre-approved cost levels under this policy will require specific approval by the Audit Committee before the service is provided.

The appendices to this Policy describe the Audit, Audit-related, Tax and All Other Services that have the general pre-approval of the Audit Committee. The term of any general pre-approval is 12 months from the date of pre-approval, unless the Audit Committee specifically provides for a different period. The Audit Committee will annually review and pre-approve the services that may be provided by the independent auditor without obtaining specific pre-approval from the Audit Committee. The Audit Committee will revise the list of general pre-approved services from time to time, based on subsequent determinations. The Audit Committee does not delegate its responsibilities to pre-approve services performed by the independent auditor to management.

II. Delegation

The Audit Committee delegates pre-approval authority to the Chairman of the Committee. In addition, the Chairman may delegate pre-approval authority to one or more of the other members of the Audit Committee. The Chairman or member or members to whom such authority is delegated shall report any pre-approval decisions to the Audit Committee at its next scheduled meeting.

III. Audit Services

The annual Audit services engagement terms and fees will be subject to the specific pre-approval of the Audit Committee. The Audit Committee will approve, if necessary, any changes in terms, conditions and fees resulting from changes in audit scope, Company structure or other matters.

In addition to the annual Audit services engagement specifically approved by the Audit Committee, the Audit Committee may grant general pre-approval for other Audit services, which are those services that only the independent auditor reasonably can provide. The Audit Committee has pre-approved the Audit services listed in Appendix A. All other Audit services not listed in Appendix A must be specifically pre-approved by the Audit Committee.

IV. Audit-Related Services

Audit-related services are assurance and related services that are reasonably related to the performance of the audit or review of the Company s financial statements or that are traditionally performed by the independent auditor. The Audit Committee believes that the provision of Audit-related services does not impair the independence of the auditor, and has pre-approved the Audit-related services listed in Appendix B. All other Audit-related services not listed in Appendix B must be specifically pre-approved by the Audit

Committee.

V. Tax Services

The Audit Committee believes that the independent auditor can provide Tax services to the Company such as tax compliance, tax planning and tax advice without impairing the auditor s independence. However, the Audit Committee will not permit the retention of the independent auditor in connection with a transaction initially recommended by the independent auditor, the sole purpose of which may be tax avoidance and the tax treatment of which may not be supported in the Internal Revenue Code and related regulations. The Audit Committee has pre-approved the Tax services listed in Appendix C. All Tax services involving large and complex transactions not listed in Appendix C with aggregate fees over $200,000 must be specifically pre-approved by the Audit Committee.

VI. All Other Services

The Audit Committee may grant general pre-approval to those permissible non-audit services classified as All Other Services that it believes are routine and recurring services, and would not impair the independence of the auditor. Permissible All Other Services not listed in Appendix D must be specifically pre-approved by the Audit Committee.

A list of the SEC s prohibited non-audit services is attached to this policy as Exhibit 1. The SEC s rules and relevant guidance should be consulted to determine the precise definitions of these services and the applicability of exceptions to certain of the prohibitions.

VII. Pre-Approval Fee Levels

Pre-approval fee levels for all services to be provided by the independent auditor will be established annually by the Audit Committee. Any proposed services exceeding these levels will require specific pre-approval by the Audit Committee.

VIII. Procedures

Requests or applications to provide services that require specific approval by the Audit Committee will be submitted to the Audit Committee by both the independent auditor and the Chief Financial Officer and must include a joint statement as to whether, in their view, the request or application is consistent with the SEC s rules on auditor independence.

Appendix A

Pre-Approved Audit Services for Fiscal Year 2003

Dated: April 2003

Service	Range of Fees
The Base Audit Fee: Financial audits of the Company including statutory audits or financial audits of subsidiaries or affiliates	$6,500,000
Adjustments to the Base Audit Fee due to impacts of foreign currency exchange rates and changes in scope of audits for the addition of subsidiaries or affiliates	Not to exceed $750,000
Accounting and audit services associated with the adoption of new financial accounting standards, consultation on the accounting or disclosure treatment of completed transactions, SEC registration statements or other SEC filings (e.g., comfort letters, consents), and assistance in responding to SEC comment letters	Not to exceed $500,000
Audits of businesses to be divested as required by the purchasers	Not to exceed $250,000 per divestiture
Internal control reviews and assistance with internal control reporting requirements as required	Pending Final Rules

by final rules under Sarbanes-Oxley Section 404

Appendix B

Pre-Approved Audit-Related Services for Fiscal Year 2003
Dated: April 2003

Service	Range of Fees
Due diligence services pertaining to potential business acquisitions/dispositions	Not to exceed $650,000 per transaction
Financial statement audits of employee benefit plans, net of amounts paid from the plan assets	Not to exceed $300,000
Agreed-upon or expanded audit procedures related to accounting and/or billing records required to respond to or comply with financial, accounting or regulatory reporting matters	Not to exceed $200,000
Consultations by the Company s management as to the accounting or disclosure treatment of potential or proposed transactions or events or the potential impact of proposed rules, standards or interpretations by the SEC, FASB, or other regulatory or standard-setting bodies	Not to exceed $500,000

Appendix C

Pre-Approved Tax Services for Fiscal Year 2003
Dated: September 2003

Service	Range of Fees
U.S. federal, state and local tax planning, advice, tax audit support and compliance	Not to exceed $1,000,000*
International tax planning, advice, tax audit support and compliance	Not to exceed $2,000,000
Preparation of tax returns for executives	Not to exceed $400,000
Preparation of tax returns for expatriate employees	Not to exceed $2,100,000**
Review and preparation of federal, state, local and international income, franchise, and other tax returns	Not to exceed $1,000,000

* Original Pre-Approved limit was $2,000,000, effective April 2003.
* * Original Pre-Approved limit was $1,600,000, effective April 2003. Actual amount expended was $1,600,000.

Appendix D

Pre-Approved All Other Services for Fiscal Year 2003
Dated: April 2003

Service/Range of Fees
None approved for 2003

Exhibit 1

Prohibited Non-Audit Services

Bookkeeping or other services related to the accounting records or financial statements of the audit client

Financial information systems design and implementation

Appraisal or valuation services, fairness opinions or contribution-in-kind reports (other than tax transfer pricing advice allowable under SEC rules)

Actuarial services

Internal audit outsourcing services

Management functions

Human resources

Broker-dealer, investment adviser or investment banking services

Legal services

Expert services unrelated to the audit

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ATTACHMENT G

2004 ALCOA STOCK INCENTIVE PLAN

SECTION 1. PURPOSE.

The purposes of the 2004 Alcoa Stock Incentive Plan are to encourage selected employees of the Company and its Subsidiaries to acquire a proprietary and vested interest in the long-term growth and financial success of the Company, to generate an increased incentive to promote its well-being and profitability, to link the interests of such employees to the long-term interests of shareholders and to enhance the ability of the Company and its Subsidiaries to attract and retain individuals of exceptional managerial, technical and professional talent upon whom, in large measure, the sustained progress, growth and profitability of the Company depend.

SECTION 2. DEFINITIONS.

As used in the Plan, the following terms have the meanings set forth below:

Award means any Option, Stock Appreciation Right, Contingent Stock Award, Performance Share, Performance Unit, Other Stock Unit Award, or any other right, interest, or option relating to Shares or other property granted pursuant to the provisions of the Plan.

Award Agreement means any written agreement, contract, or other instrument or document evidencing any Award granted by the Committee hereunder, which may, but need not, be executed or acknowledged by both the Company and the Participant.

Beneficial Owner means beneficial owner as defined in Rule 13d-3 under the Exchange Act.

Board means the Board of Directors of the Company.

Change in Control means the first to occur of any of the following events:

(a) an Entity, other than a trustee or other fiduciary of securities held under an employee benefit plan of the Company or any of its Subsidiaries, is or becomes a Beneficial Owner, directly or indirectly, of stock of the Company representing 20% or more of the total voting power of the Company s then outstanding stock and securities; *provided, however,* that for purposes of this subsection (a), the following acquisitions shall not constitute a Change of Control: (i) any acquisition directly from the Company, (ii) any acquisition by the Company, (iii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company or (iv) any acquisition by any corporation pursuant to a transaction that complies with clauses (i)

or (ii) of subsection (c) of this definition;

(b) individuals who, as of the date hereof, constitute the Board (the Incumbent Board), cease for any reason to constitute a majority thereof; *provided, however,* that any individual becoming a director whose election, or nomination for election by the Company s shareholders, was approved by a vote of at least 75% of the directors then comprising the Incumbent Board shall be considered as though such individual was a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of an Entity other than the Board;

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(c) there is consummated a merger, consolidation or other corporate transaction, other than (i) a merger, consolidation or transaction that would result in the voting securities of the Company outstanding immediately prior to such merger, consolidation or transaction continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving Entity or any parent thereof) at least 55% of the combined voting power of the stock and securities of the Company or such surviving Entity or any parent thereof outstanding immediately after such merger, consolidation or transaction, or (ii) a merger, consolidation or transaction effected to implement a recapitalization of the Company (or similar transaction) in which no Entity is or becomes the Beneficial Owner, directly or indirectly, of stock and securities of the Company representing more than 20% of the combined voting power of the Company s then outstanding stock and securities;

(d) the sale or disposition by the Company of all or substantially all of the Company s assets other than a sale or disposition by the Company of all or substantially all of the assets to an Entity at least 55% of the combined voting power of the stock and securities of which is owned by Persons in substantially the same proportions as their ownership of the Company s voting stock immediately prior to such sale; or

(e) the shareholders of the Company approve a plan of complete liquidation or dissolution of the Company.

Change in Control Price means the higher of (a) the highest reported sales price, regular way, of a Share in any transaction reported on the New York Stock Exchange Composite Tape or other national exchange on which Shares are listed or on NASDAQ during the 60-day period prior to and including the date of a Change in Control or (b) if the Change in Control is the result of a tender or exchange offer or a merger, consolidation or other corporate transaction, the highest price per Share paid in such tender or exchange offer or corporate transaction. To the extent that the consideration paid in any such transaction described above consists all or in part of securities or other non-cash consideration, the value of such securities or other non-cash consideration shall be determined in the sole discretion of the Board.

Code means the Internal Revenue Code of 1986, as amended from time to time, and any successor thereto.

Committee means the Compensation and Benefits Committee of the Board, or any successor to such committee, or a subcommittee thereof, composed of no fewer than two directors, each of whom is a Non-Employee Director and an outside director within the meaning of Section 162(m) of the Code, or any successor provision thereto.

Company means Alcoa Inc., a Pennsylvania corporation.

Contingent Stock means any Share issued with the contingency or restriction that the holder may not sell, transfer, pledge or assign such Share and with such other contingencies or restrictions as the Committee, in its sole discretion, may impose (including, without limitation, any contingency or restriction on the right to vote such Share and the right to receive any cash dividends), which contingencies and restrictions may lapse separately or in combination, at such time or times, in installments or otherwise, as the Committee may deem appropriate.

Contingent Stock Award means an award of Contingent Stock under Section 8 hereof.

Covered Employee means a covered employee within the meaning of Section 162(m)(3) of the Code, or any successor provision thereto.

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Employee means any employee of the Company or of any Subsidiary.

Entity means any individual, entity, person (within the meaning of Section 3(a)(9) of the Exchange Act) or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act), other than (a) any employee plan established by the Company, (b) any affiliate (as defined in Rule 12b-2 promulgated under the Exchange Act) of the Company, (c) an underwriter temporarily holding securities pursuant to an offering of such

securities, or (d) a corporation owned, directly or indirectly, by shareholders of the Company in substantially the same proportions as their ownership of the Company.

Exchange Act means the Securities Exchange Act of 1934, as amended.

Fair Market Value means, with respect to any property, the market value of such property determined by such methods or procedures as shall be established from time to time by the Committee.

Non-Employee Director has the meaning set forth in Rule 16b-3(b)(3) under the Exchange Act, or any successor definition adopted by the Securities and Exchange Commission.

Option means any right granted to a Participant under the Plan or predecessor plan allowing such Participant to purchase Shares at such price or prices and during such period or periods as the Committee shall determine. All Options granted under the Plan or predecessor plan are intended to be nonqualified stock options for purposes of the Code.

Other Stock Unit Award means any right granted to a Participant by the Committee pursuant to Section 10 hereof.

Original Option means any Option other than a Reload Option granted by the company in connection with the Prior Plan or the predecessor plan.

Participant means an Employee who is selected by the Committee to receive an Award under the Plan.

Performance Award means any Award of Performance Shares or Performance Units pursuant to Section 9 hereof.

Performance Period means that period established by the Committee at the time any Performance Award is granted or at any time thereafter during which any performance goals specified by the Committee with respect to such Award are to be measured. A Performance Period may not be less than one year.

Performance Share means any grant pursuant to Section 9 hereof of a unit valued by reference to a designated number of Shares, which value may be paid to the Participant by delivery of such property as the Committee shall determine, including, without limitation, cash, Shares or any combination thereof, upon achievement of such performance goals during the Performance Period as the Committee shall establish at the time of such grant or thereafter.

Performance Unit means any grant pursuant to Section 9 hereof of a unit valued by reference to a designated amount of property other than Shares, which value may be paid to the Participant by delivery of such property as the Committee shall determine, including, without limitation, cash, Shares or any combination thereof, upon achievement of such performance goals during the Performance Period as the Committee shall establish at the time of such grant or thereafter.

Person means any individual, corporation, partnership, association, joint stock company, trust, unincorporated organization or government or political subdivision thereof.

Plan means this 2004 Alcoa Stock Incentive Plan.

Prior Plan means the Alcoa Stock Incentive Plan adopted by the Company shareholders at the Company s 1999 annual meeting.

Reload Option means an Option described in Section 6(e) of the Plan, granted in connection with the exercise of an option under the Prior Plan or predecessor plan (an antecedent award). As a condition to the grant of a Reload Option, a Participant must elect at the time of exercise of the antecedent award that a designated portion, as determined by the Committee, of the Shares issued upon exercise of the antecedent award shall be restricted in terms of transfer for the shorter of five years from the issuance date of the shares or the remainder of the participant s career with Alcoa.

Shares means the shares of common stock of the Company, $1.00 par value.

Stock Appreciation Right means any right granted to a Participant pursuant to Section 7 hereof to receive, upon exercise by the Participant, the excess of (a) the Fair Market Value of one Share on the date of exercise or, if the Committee shall so determine, at any time during a specified period before the date of exercise over (b) the grant price of the right on the date of grant, or if granted in connection with an outstanding Option

on the date of grant of the related Option, as specified by the Committee in its sole discretion, which, except in the case of Substitute Awards or in connection with an adjustment provided in Section 4(g), shall not be less than the Fair Market Value of one Share on such date of grant of the right or the related Option, as the case may be. Any payment by the Company in respect of such right may be made in cash, Shares, other property or any combination thereof, as the Committee, in its sole discretion, shall determine.

Subsidiary means any corporation in which the Company owns, directly or indirectly, stock possessing 50 percent or more of the total combined voting power of all classes of stock in such corporation, and any corporation, partnership, joint venture, limited liability company or other business entity as to which the Company possesses a significant ownership interest, directly or indirectly, as determined by the Committee.

Substitute Awards means Awards granted or Shares issued by the Company in assumption of, or in substitution or exchange for, awards previously granted, or the right or obligation to make future awards, by a company acquired by the Company or any of its Subsidiaries or with which the Company or any of its Subsidiaries combines.

SECTION 3. ADMINISTRATION.

The Plan shall be administered by the Committee. The Committee shall have full power and authority, subject to such orders or resolutions not inconsistent with the provisions of the Plan as may from time to time be adopted by the Board, to: (i) select the Employees of the Company and its Subsidiaries to whom Awards may from time to time be granted hereunder; (ii) determine the type or types of Award to be granted to each Participant hereunder; (iii) determine the number of Shares to be covered by each Award granted hereunder; (iv) determine the terms and conditions, not inconsistent with the provisions of the Plan, of any Award granted hereunder; (v) determine whether, to what extent and under what circumstances Awards may be settled in cash, Shares or other property or canceled or suspended; (vi) determine whether, to what extent and under what circumstances cash, Shares and other property and other amounts payable with respect to an Award under this Plan shall be deferred either automatically or at the election of the Participant;

(vii) interpret and administer the Plan and any instrument or agreement entered into under the Plan; (viii) establish such rules and regulations and appoint such agents as it shall deem appropriate for the proper administration of the Plan; and (ix) make any other determination and take any other action that the Committee deems necessary or desirable for administration of the Plan. Decisions of the Committee shall be final, conclusive and binding upon all persons, including the Company, any Participant, any shareholder and any Employee.

SECTION 4. SHARES SUBJECT TO THE PLAN.

(a) Subject to the adjustment provisions of Section 4(g) below and the provisions of Section 4(b) through (f), commencing May 1, 2004, up to 30 million Shares may be issued in connection with Options and Stock Appreciation Rights under the Plan.

(b) In addition to the Shares authorized by Section 4(a), the following Shares may be issued under the Plan:

(i) Shares available for future awards under the Prior Plan as of the effective date of this Plan, and any shares that are not issued under the Prior Plan because of the cancellation, termination or expiration of awards under the Prior Plan or the predecessor plan.

(ii) If a Participant tenders, or has withheld, Shares in payment of all or part of the option price under a stock option granted under the Plan, the Prior Plan, or the predecessor plan, or in satisfaction of withholding tax obligations thereunder, the Shares tendered by the Participant or so withheld shall become available for issuance under the Plan.

(iii) If Shares that are issued under the Plan are subsequently forfeited in accordance with the terms of the Award or an Award Agreement, the forfeited Shares shall become available for issuance under the Plan.

(c) Subject to the adjustment provisions of Section 4(g), commencing May 1, 2004, up to 10 million Shares may be issued under Awards other than Options and Stock Appreciation Rights.

(d) If an Award may be paid only in Shares or in either cash or Shares, the Shares shall be deemed to be issued hereunder only when and to the extent that payment is actually made in Shares. However, the Committee may authorize a cash payment under an Award in lieu of Shares if there are insufficient Shares available for issuance under the Plan.

(e) Any Shares issued hereunder may consist, in whole or in part, of authorized and unissued shares, treasury shares or shares purchased in the open market or otherwise.

(f) Shares issued or granted in connection with Substitute Awards shall not reduce the Shares available for issuance under the Plan or to a Participant in any calendar year.

(g) In the event of any merger, reorganization, consolidation, recapitalization, stock dividend, stock split, reverse stock split, spin-off or similar transaction or other change in corporate structure affecting the Shares, such adjustments and other substitutions shall be made to the Plan and to Awards as the Committee in its sole discretion deems equitable or appropriate, including, without limitation, such adjustments in the aggregate number, class and kind of securities that may be delivered under the Plan, in the aggregate or to any one Participant, in the number, class, kind and option or exercise price of

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securities subject to outstanding Options, Stock Appreciation Rights or other Awards granted under the Plan, and in the number, class and kind of securities subject to Awards granted under the Plan (including, if the Committee deems appropriate, the substitution of similar options to purchase the shares of, or other awards denominated in the shares of, another company) as the Committee may determine to be appropriate in its sole discretion; *provided* that the number of Shares subject to any Award shall always be a whole number.

SECTION 5. ELIGIBILITY.

Any Employee shall be eligible to be selected as a Participant.

SECTION 6. STOCK OPTIONS.

Options may be granted hereunder to Participants either alone or in addition to other Awards granted under the Plan. Any Option granted under the Plan may be evidenced by an Award Agreement in such form as the Committee from time to time approves. Any such Option shall be subject to the terms and conditions required by this Section 6 and to such additional terms and conditions, not inconsistent with the provisions of the Plan, as the Committee may deem appropriate in each case.

(a) **Option Price.** The purchase price per Share purchasable under an Option shall be determined by the Committee in its sole discretion; provided that, except in connection with an adjustment provided for in Section 4(g), such purchase price shall not be less than the Fair Market Value of the Share on the date of the grant of the Option.

(b) **Option Period.** The term of each Original Option granted hereunder shall not exceed six years from the date the Option is granted.

(c) **Exercisability.** Options shall be exercisable at such time or times as determined by the Committee at or subsequent to grant, provided, however, that the minimum vesting period of an Option shall be one year.

(d) **Method of Exercise.** Subject to the other provisions of the Plan, any Option may be exercised by the Participant in whole or in part at such time or times, and the Participant may make payment of the Option price in such form or forms, including, without limitation, payment by delivery of cash, Shares or other consideration (including, where permitted by law and the Committee, Awards) having a Fair Market Value on the exercise date equal to the total Option price, or by any combination of cash, Shares and other consideration as the Committee may specify in the applicable Award Agreement.

(e) **Reload Options.** A Reload Option entitles the Participant to purchase Shares (i) that are covered by an antecedent award at the time of its exercise, but are not issued upon such exercise, or (ii) whose aggregate grant price equals the purchase price of the exercised antecedent award and any related tax withholdings. The grant price per Share of the Reload Option shall be the Fair Market Value per Share at the time of grant. The duration of a Reload Option shall not extend beyond the expiration date of the antecedent award. No Options with a reload feature can be granted under the Plan in 2004 or anytime thereafter. Options and Reload Options granted under the Prior Plan or predecessor plan in 2002, or prior thereto, will be eligible for grant of a Reload Option only once on and after January 1, 2004, which grant of a Reload Option must occur anytime prior to the expiration of the antecedent award. For Original Options granted under the Prior Plan in 2003, only that portion of the grant that vests in 2004 will be eligible for grant of only one Reload Option, which grant must occur on or before December 31, 2004.

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(f)

Transferability of Options. Notwithstanding the provisions of Section 14(a) of the Plan, at the discretion of the Committee and in accordance with rules it establishes from time to time, Participants may be permitted to transfer some or all of their Options to one or more family members as such term is defined in Form S-8 (or any successor form) promulgated under the Securities Act of 1933, as amended.

SECTION 7. STOCK APPRECIATION RIGHTS.

Stock Appreciation Rights may be granted hereunder to Participants either alone or in addition to other Awards granted under the Plan and may, but need not, relate to a specific Option granted under Section 6. The provisions of Stock Appreciation Rights need not be the same with respect to each recipient. Any Stock Appreciation Right related to an Option may be granted at the same time such Option is granted or at any time thereafter before exercise or expiration of such Option. In the case of any Stock Appreciation Right related to any Option, the Stock Appreciation Right or applicable portion thereof shall terminate and no longer be exercisable upon the termination or exercise of the related Option, except that a Stock Appreciation Right granted with respect to less than the full number of Shares covered by a related Option shall not be reduced until the exercise or termination of the related Option exceeds the number of Shares not covered by the Stock Appreciation Right. Any Option related to any Stock Appreciation Right shall no longer be exercisable to the extent the related Stock Appreciation Right has been exercised. The Committee may impose such conditions or restrictions on the exercise of any Stock Appreciation Right as it shall deem appropriate.

SECTION 8. CONTINGENT STOCK.

(a) **Issuance.** A Contingent Stock Award shall be subject to contingencies or restrictions imposed by the Committee during a period of time specified by the Committee (the Contingency Period). Contingent Stock Awards may be issued hereunder to Participants, for no cash consideration or for such minimum consideration as may be required by applicable law, either alone or in addition to other Awards granted under the Plan. The provisions of Contingent Stock Awards need not be the same with respect to each recipient.

(b) **Registration.** Any Contingent Stock issued hereunder may be evidenced in such manner as the Committee in its sole discretion shall deem appropriate, including, without limitation, book-entry registration or issuance of a stock certificate or certificates. In the event any stock certificate is issued in respect of shares of Contingent Stock awarded under the Plan, such certificate shall be registered in the name of the Participant and shall bear an appropriate legend referring to the terms, conditions, contingencies and restrictions applicable to such Award.

(c) **Forfeiture.** Except as otherwise determined by the Committee at the time of grant or thereafter, upon termination of employment for any reason during the Contingency Period, all Shares of Contingent Stock still subject to any contingency or restriction shall be forfeited by the Participant and reacquired by the Company. Noncontingent Shares, evidenced in such manner as the Committee shall deem appropriate, shall be issued to the Participant promptly after the Contingency Period, as determined or modified by the Committee, shall expire.

(d) **Minimum Vesting Condition.** The minimum Contingency Period applicable to any Contingent Stock Award that is not subject to performance conditions restricting transfer shall be three (3) years from the date of grant; *provided, however,* that a Contingency Period of less than three (3) years may be approved for such Awards with respect to up to 200,000 Shares under the Plan.

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SECTION 9. PERFORMANCE AWARDS.

Performance Awards may be granted hereunder to Participants, for no cash consideration or for such minimum consideration as may be required by applicable law, either alone or in addition to other Awards granted under the Plan. The performance criteria to be achieved during any Performance Period and the length of the Performance Period shall be determined by the Committee upon the grant of each Performance Award. Except as provided in Section 11, Performance Awards will be paid only after the end of the relevant Performance Period. Performance Awards may be paid in cash, Shares, other property or any combination thereof in the sole discretion of the Committee at the time of payment. The performance levels to be achieved for each Performance Period and the amount of the Award to be paid shall be conclusively determined by the Committee. Performance Awards may be paid in a lump sum or in installments following the close of the Performance Period or, in accordance with procedures established by the Committee, on a deferred basis.

SECTION 10. OTHER STOCK UNIT AWARDS.

(a) Other Awards of Shares and other Awards that are valued in whole or in part by reference to, or are otherwise based on, Shares or other property (Other Stock Unit Awards) may be granted hereunder to Participants, either alone or in addition to other Awards granted under the Plan. Other Stock Unit Awards may be paid in Shares, cash or any other form of property as the Committee shall determine. Subject to the provisions of the Plan, the Committee shall have sole and complete authority to determine the Employees of the Company and its Subsidiaries to whom, and the time or times at which, such Awards shall be made, the number of Shares to be granted pursuant to such Awards and all other conditions of the Awards. The provisions of Other Stock Unit Awards need not be the same with respect to each

recipient.

(b) Subject to the provisions of this Plan and any applicable Award Agreement, Awards and Shares subject to Awards granted under this Section 10, may not be sold, assigned, transferred, pledged or otherwise encumbered prior to the date on which the Shares are issued, or, if later, the date on which any applicable contingency, restriction, performance or deferral period lapses. For any Award or Shares subject to any Award granted under this Section 10 the transferability of which is conditioned only on the passage of time, such restriction period shall be a minimum of three (3) years. Shares (including securities convertible into Shares) subject to Awards granted under this Section 10 may be issued for no cash consideration or for such minimum consideration as may be required by applicable law. Shares (including securities convertible into Shares) purchased pursuant to a purchase right granted under this Section 10 thereafter shall be purchased for such consideration as the Committee shall in its sole discretion determine, which shall not be less than the Fair Market Value of such Shares or other securities as of the date such purchase right is granted.

SECTION 11. CHANGE IN CONTROL PROVISIONS.

(a) **Impact of Event.** Notwithstanding any other provision of the Plan to the contrary, unless the Committee shall determine otherwise at the time of grant with respect to a particular Award, in the event of a Change in Control:

(i) any Options and Stock Appreciation Rights outstanding as of the date such Change in Control is determined to have occurred, and which are not then exercisable and vested, shall become fully exercisable and vested to the full extent of the original grant;

(ii) the contingencies, restrictions and deferral limitations applicable to any Contingent Stock shall lapse, and such Contingent Stock shall become free of all contingencies, restrictions and limitations and become fully vested and transferable to the full extent of the original grant;

(iii) all Performance Awards shall be considered to be earned and payable at the target amount of Shares covered by the Award, to the extent that the Change in Control occurs during the Performance Period, or at the calculated award level, to the extent that the Change in Control occurs after the Performance Period, and shall be immediately settled or distributed. Any deferral, contingency or other restriction applicable to such Performance Awards shall lapse; and

(iv) the contingencies, restrictions and deferral limitations and other conditions applicable to any Other Stock Unit Awards or any other Awards shall lapse, and such Other Stock Unit Awards or such other Awards shall become free of all contingencies, restrictions, limitations or conditions and become fully vested and transferable to the full extent of the original grant; and

(v) the restrictions applicable to any Shares received in connection with the grant of a Reload Option shall lapse and such Shares shall be freely and fully transferable.

(b) **Change In Control Settlement.** Notwithstanding any other provision of the Plan, during the 60-day period from and after a Change in Control (the Change in Control Election Period), a Participant holding an Option or Stock Appreciation Right shall have the right, whether or not the Option or Stock Appreciation Right is fully exercisable and in lieu of the payment of the purchase price for the Shares being purchased under the Option or Stock Appreciation Right and by giving notice to the Company, to elect (within the Change in Control Election Period) to surrender all or part of the Option or Stock Appreciation Right to the Company and to receive cash, within 30 days of such notice, in an amount equal to the amount by which the Change in Control Price per Share on the date of such election shall exceed the purchase price per Share under the Option or Stock Appreciation Right multiplied by the number of Shares granted under the Option or Stock Appreciation right as to which the right granted under this Section 11(b) shall have been exercised.

(c) **Other Forms of Settlement.** The foregoing provisions of this Section 11 shall not preclude other forms of settlement of outstanding Awards in the event of a Change in Control, including a conversion or exchange of Awards for awards or securities of any person that is a party to or initiates the Change in Control transaction; provided that no Participant shall be required to accept any such substituted or exchanged award or security without such Participant s written consent.

SECTION 12. CODE SECTION 162(m) PROVISIONS.

(a)

Notwithstanding any other provision of this Plan, if the Committee determines at the time Contingent Stock, a Performance Award or an Other Stock Unit Award is granted to a Participant that such Participant is, or is likely to be as of the end of the tax year in which the Company would claim a tax deduction in connection with such Award, a Covered Employee, then the Committee may provide that this Section 12 is applicable to such Award.

(b) If an Award is subject to this Section 12, then the lapsing of contingencies or restrictions thereon and the distribution of cash, Shares or other property pursuant thereto, as applicable, shall be subject to the achievement by the Company or any Subsidiary, or any division or business unit thereof, as appropriate, of one or more objective performance goals established by the Committee, which shall be based on the attainment of specified levels of one or any combination of the following: cumulative net income or cumulative net income per share during the performance period; return on sales; return on assets; return on capital; return on shareholders equity; cash flow; economic value added; cumulative operating income; total shareholders return; cost reductions; or achievement of environment, health

& safety goals of the Company or the Subsidiary or business unit of the Company for or within which the Participant is primarily employed. Performance goals may be based upon the attainment of specified levels of Company, Subsidiary or unit performance under one or more of the measures described above relative to the performance of other comparator companies or groups of companies, and may include a threshold level of performance below which no Award will be earned, levels of performance at which an Award will become partially earned, and a level of performance at which an Award will be fully earned. Performance goals shall be set by the Committee within the time period prescribed by, and shall otherwise comply with, the requirements of Section 162(m) of the Code, or any successor provision thereto, and the regulations thereunder.

(c) Notwithstanding any provision of this Plan other than Section 11, with respect to any Award that is subject to this Section 12, the Committee may adjust downwards, but not upwards, the amount payable pursuant to such Award, and the Committee may not waive the achievement of the applicable performance goals.

(d) The Committee shall have the power to impose such other restrictions on Awards subject to this Section 12 as it may deem necessary or appropriate to ensure that such Awards satisfy all requirements for performance-based compensation within the meaning of Section 162(m)(4)(C) of the Code, or any successor provision thereto.

(e) Notwithstanding any provision of this Plan other than Section 4(g), no Participant may be granted Options and/or Stock Appreciation Rights in any calendar year with respect to more than two million (2,000,000) Shares, or Contingent Stock Awards or Performance Share Awards covering more than 300,000 Shares. The maximum dollar value payable with respect to Performance Units and/or Other Stock Unit Awards that are valued with reference to property other than Shares and granted to any Participant in any one calendar year is $2,000,000.

SECTION 13. AMENDMENTS AND TERMINATION.

The Board may amend, alter, suspend, discontinue or terminate the Plan or any portion thereof at any time; provided that no such amendment, alteration, suspension, discontinuation or termination shall be made without (i) shareholder approval if: (x) such approval is necessary to qualify for or comply with any tax or regulatory requirement for which or with which the Board deems it necessary or desirable to qualify or comply; or (y) a proposed amendment or alteration would materially increase the benefits accruing to Participants, materially increase the maximum number of shares which may be issued under the Plan or materially modify the Plan s eligibility requirements: or (ii) the consent of the affected Participant, if such action would impair the rights of such Participant under any outstanding Award. Notwithstanding anything to the contrary herein, the Committee may amend the Plan in such manner as may be necessary so as to have the Plan conform to local rules and regulations in any jurisdiction outside the United States.

The Committee may amend the terms of any Award theretofore granted, prospectively or retroactively, but no such amendment shall impair the rights of any Participant without his or her consent.Notwithstanding any provision of this Plan, the Committee may not amend the terms of any Option to reduce the option price.

SECTION 14. GENERAL PROVISIONS.

(a) **Nontransferability of Awards.** Unless the Committee determines otherwise at the time the Award is granted or thereafter, and except for transfers of Options permitted by Section 6(f) of the Plan: (i) no Award, and no Shares subject to Awards described in Section 10 that have not been issued, or as to which any applicable contingency, restriction, performance or deferral period has not lapsed, may be sold,

assigned, transferred, pledged or otherwise encumbered, except by will or by the laws of descent and distribution; *provided* that, if so determined by the Committee, a Participant may, in the manner established by the Committee, designate a beneficiary to exercise the rights of the Participant with respect to any Award upon the death of the Participant, and (ii) each Award shall be exercisable, during the Participant s lifetime, only by the Participant or, if permissible under applicable law, by the Participant s guardian or legal representative.

(b) **Award Term.** Except to the extent already established in Section 6 (b), the term of each Award shall be for such period of months or years from the date of its grant as may be determined by the Committee.

(c) **Award Entitlement.** No Employee or Participant shall have any claim to be granted any Award under the Plan and there is no obligation for uniformity of treatment of Employees or Participants under the Plan.

(d) **Requirement of an Award Agreement.** The prospective recipient of any Award under the Plan shall not, with respect to such Award, be deemed to have become a Participant, or to have any rights with respect to such Award, until and unless such recipient shall have executed an agreement or other instrument evidencing the Award and delivered a copy thereof to the Company and otherwise complied with the then applicable terms and conditions.

(e) **Award Adjustments.** Except as provided in Section 12, the Committee shall be authorized to make adjustments in Performance Award criteria or in the terms and conditions of other Awards in recognition of unusual or nonrecurring events affecting the Company or its financial statements or changes in applicable laws, regulations or accounting principles. The Committee may correct any defect, supply any omission or reconcile any inconsistency in the Plan or any Award in the manner and to the extent it shall deem desirable to carry it into effect.

(f) **Committee Right to Cancel.** The Committee shall have full power and authority to determine whether, to what extent and under what circumstances any Award shall be canceled or suspended. In particular, but without limitation, all outstanding Awards to any Participant shall be canceled if the Participant, without the consent of the Committee, while employed by the Company or after termination of such employment, becomes associated with, employed by, renders services to or owns any interest in (other than any nonsubstantial interest, as determined by the Committee) any business that is in competition with the Company or with any business in which the Company has a substantial interest as determined by the Committee or otherwise takes any action that in the judgment of the Committee is not in the best interests of the Company.

(g) **Stock Certificate Legends.** All certificates for Shares delivered under the Plan pursuant to any Award shall be subject to such stock transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Shares are then listed and any applicable Federal or state securities law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

(h) **Compliance with Securities Laws.** No Award granted hereunder shall be construed as an offer to sell securities of the Company, and no such offer shall be outstanding, unless and until the Committee in its sole discretion has determined that any such offer, if made, would be in compliance with all applicable requirements of the U.S. Federal securities laws and any other laws to which such offer, if made, would be subject.

(i) **Award Deferrals; Dividends.** The Committee shall be authorized to establish procedures pursuant to which the payment of any Award may be deferred. Subject to the provisions of the Plan and any Award Agreement, the recipient of an Award (including, without limitation, any deferred Award) may, if so determined by the Committee, be entitled to receive, currently or on a deferred basis, cash dividends, or cash payments in amounts equivalent to cash dividends on Shares (Dividend Equivalents), with respect to the number of Shares covered by the Award, as determined by the Committee, in its sole discretion, and the Committee may provide that such amounts (if any) shall be deemed to have been reinvested in additional Shares or otherwise reinvested.

(j) **Consideration for Awards.** Except as otherwise required in any applicable Award Agreement or by the terms of the Plan, recipients of Awards under the Plan shall not be required to make any payment or provide consideration other than the rendering of services.

(k) **Delegation of Authority by Committee.** The Committee may delegate to one or more executive officers (as that term is defined in Rule 3b-7 under the Exchange Act) or a committee of executive officers the right to grant Awards to Employees who are not executive officers or directors of the Company and to cancel or suspend Awards to Employees who are not executive officers or directors of the Company.

(l) **Withholding Taxes.** The Company shall be authorized to withhold from any Award granted or payment due under the Plan the amount of withholding taxes due in respect of an Award or payment hereunder and to take such other action as may be necessary in the opinion of the Company to satisfy all obligations for the payment of such taxes. The Committee shall be authorized to establish procedures for election by Participants to satisfy such obligations for the payment of such taxes by delivery of or transfer of Shares to the Company or

by directing the Company to retain Shares otherwise deliverable in connection with the Award.

(m) **Other Compensatory Arrangements.** Nothing contained in this Plan shall prevent the Board from adopting other or additional compensation arrangements, subject to shareholder approval if such approval is required; and such arrangements may be either generally applicable or applicable only in specific cases.

(n) **Governing Law.** The validity, construction, and effect of the Plan and any rules and regulations relating to the Plan shall be determined in accordance with the laws of the Commonwealth of Pennsylvania and applicable Federal law.

(o) **Severability.** If any provision of this Plan is or becomes or is deemed invalid, illegal or unenforceable in any jurisdiction, or would disqualify the Plan or any Award under any law deemed applicable by the Committee, such provision shall be construed or deemed amended to conform to applicable laws or if it cannot be construed or deemed amended without, in the determination of the Committee, materially altering the intent of the Plan, it shall be stricken and the remainder of the Plan shall remain in full force and effect.

(p) **Awards to Non U.S. Employees.** Awards may be granted to Employees who are foreign nationals or employed outside the United States, or both, on such terms and conditions different from those applicable to Awards to Employees employed in the United States as may, in the judgment of the Committee, be necessary or desirable in order to recognize differences in local law or tax policy. The Committee also may impose conditions on the exercise or vesting of Awards in order to minimize the Company s obligation with respect to tax equalization for Employees on assignments outside their home countries.

(q) **Repricing Prohibited.** The repricing of Options or Stock Appreciation Right Awards under the Plan is expressly prohibited. Repricing means the grant of a new Option, Stock Appreciation Right or other Award in consideration of the exchange, cancellation or forfeiture of an Award that has a higher grant price than the new Award or the amendment of an outstanding Award to reduce the grant price; provided, that the grant of a Substitute Award shall not be considered to be repricing.

SECTION 15. TERM OF PLAN.

The Plan shall be effective as of May 1, 2004. No Award shall be granted pursuant to the Plan after April 30, 2009, but any Award theretofore granted may extend beyond that date.

SECTION 16. TERMINATION OF PRIOR PLAN.

No stock options or other awards may be granted under the Prior Plan or any predecessor plan after April 30, 2004, but all such awards theretofore granted shall extend for the full stated terms thereof and be administered under this Plan.

Alcoa

201 Isabella St. at 7th St. Bridge
Pittsburgh, PA 15212-5858

Alcoa Annual Meeting of Shareholders
9:30 a.m. Friday, April 30, 2004
Carnegie Music Hall
4400 Forbes Avenue
Pittsburgh, Pennsylvania 15213-4080

Admission Ticket
This ticket is not transferable.

Please keep this ticket to be admitted to the annual meeting.

â Fold and detach here **â**

THREE WAYS TO VOTE

VOTE BY MAIL
Return your proxy in the **postage-paid** envelope provided.

VOTE BY INTERNET
Access this **Web site** to cast your vote.

www.votefast.com

VOTE BY TELEPHONE
Call toll-free using a touch-tone telephone.
1-800-542-1160

Control Number Ø

Vote By Mail Please mark, sign and date your proxy card and return it in the postage-paid envelope provided.

Vote By Internet Have your proxy card available when you access the Web site **www.votefast.com** and follow the simple directions presented to record your vote.

Vote By Telephone Have your proxy card available when you call toll-free **1-800-542-1160** using a touch-tone phone and follow the simple directions presented to record your vote.

Vote 24 hours a day, 7 days a week. Your telephone or Internet vote must be received by 11:59 p.m. EDT on April 29, 2004 to be counted. If you vote by Internet or by telephone, please do not mail your proxy card. If you vote by mail, your proxy card must be received before the meeting for your vote to be counted.

Alcoa
201 Isabella St. at 7th St. Bridge
Pittsburgh, PA 15212-5858

THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS

I authorize Ronald D. Dickel, Charles D. McLane, Jr. and Dale C. Perdue, together or separately, to represent me at the Annual Meeting of Shareholders of Alcoa Inc. scheduled for Friday, April 30, 2004, and at any adjournment of the meeting. I authorize them to vote the shares of stock that I could vote if attending the meeting, in accordance with the instructions on the reverse side of this card. The representatives are authorized in their discretion to vote upon other business that might properly come before the meeting, and they may name others to take their place.

As described more fully in the proxy statement, this card votes or provides voting instructions for shares of common stock held under the same registration in any one or more of the following: as a shareholder of record, in the Alcoa Dividend Reinvestment and Stock Purchase Plan, the Alcoa Employee Stock Purchase Plan and in employee savings plans sponsored by Alcoa, its subsidiaries or affiliates.

Comments: _______________________________

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(Vote on the other side)

(continued from the other side) (RETURN IN THE ENCLOSED ENVELOPE IF VOTING BY MAIL) (fold and detach here)

Please mark your choices clearly in the appropriate boxes.

Unless specified, the proxy committee will vote FOR items 1 and 2 and AGAINST items 3a and 3b.

P R O X Y

DIRECTORS RECOMMEND A VOTE FOR THESE DIRECTORS / CANDIDATES	**1.**	**Election of Directors** Nominees to serve a three-year term: 1. Alain J.P. Belda 2. Carlos Ghosn 3. Henry B. Schacht 4. Franklin A. Thomas o FOR all listed nominees o WITHHOLD vote for all listed nominees o WITHHOLD vote only from ____
DIRECTORS RECOMMEND A VOTE FOR THIS ITEM (#2)	**2.**	**Proposal to Approve the 2004 Alcoa Stock Incentive Plan** o VOTE FOR o VOTE AGAINST o ABSTAIN
DIRECTORS RECOMMEND A VOTE AGAINST THIS ITEM (#3a)	**3a.**	**Shareholder Proposal Relating to Pay Disparity** o VOTE FOR o VOTE AGAINST o ABSTAIN
DIRECTORS RECOMMEND A VOTE AGAINST THIS ITEM (#3b)	**3b.**	**Shareholder Proposal Relating to Change in Control Severance Plan** o VOTE FOR o VOTE AGAINST o ABSTAIN

If you plan to attend the annual meeting, please check the box on the right. q **I will attend the 2004 annual meeting.**

PLEASE VOTE, SIGN, DATE AND RETURN Ø ____ Date ________________________, 2004

(Sign exactly as name appears on the reverse side, indicating position or representative capacity, where applicable)

Alcoa Annual Meeting of Shareholders **Admission Ticket**

9:30 a.m. Friday, April 30, 2004
Carnegie Music Hall
4400 Forbes Avenue
Pittsburgh, Pennsylvania 15213-4080

This ticket is not transferable.

Please keep this ticket to be admitted to the annual meeting.

â Fold and detach here **â**

Dear Preferred Shareholder:

We invite you to attend the 2004 Alcoa Annual Meeting of Shareholders on Friday, April 30, at 9:30 a.m. at the Carnegie Music Hall, 4400 Forbes Avenue, Pittsburgh, Pennsylvania 15213-4080. All shareholders are welcome to attend, although only holders of Alcoa common stock are eligible to vote at this meeting.

If you plan to attend this meeting, please check the box below. Then detach and return the card in the enclosed postage-paid envelope by April 15, 2004.

Shareholder comments about any aspect of company business are welcome, and we provide space on the card for this purpose. Although we do not answer these comments on an individual basis, they do assist management in determining and responding to your needs as shareholders.

Judith L. Nocito
Secretary

â Fold and detach here **â**

Alcoa Annual Meeting Attendance
If you plan to attend the annual meeting, please check the box below.

q **I will attend the 2004 annual meeting.**

For your comments . . .