XOMA LTD /DE/
Form DEF 14A
April 13, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

Filed by the Registrant x

Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-12

XOMA LTD.

(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if Other Than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

¨ Fee paid previously with preliminary materials.

¨ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

XOMA LTD.

2910 Seventh Street

Berkeley, California 94710

(510) 204-7200

April 13, 2006

To Our Shareholders:

You are cordially invited to attend the annual general meeting of shareholders of XOMA Ltd. on May 23, 2006 at 9:00 a.m. local time, which will be held at The Claremont Hotel, Ashby and Domingo Avenues, Berkeley, California.

Details of business to be conducted at the annual general meeting are provided in the enclosed Notice of Annual General Meeting of Shareholders and Proxy Statement. Also enclosed for your information is a copy of our Annual Report to Shareholders for 2005. Some of our shareholders will be accessing these materials and appointing a proxy through the Internet and may not be receiving a paper proxy card by mail.

We hope that you will attend the annual general meeting. In any event, please promptly sign, date and return the enclosed proxy in the accompanying reply envelope or appoint a proxy by telephone or through the Internet.

Sincerely yours,

John L. Castello

Chairman of the Board,

President and Chief Executive Officer

Enclosures

XOMA LTD.

NOTICE OF ANNUAL GENERAL MEETING OF SHAREHOLDERS

TO BE HELD AT 9:00 A.M. ON MAY 23, 2006

To the Shareholders of XOMA Ltd.:

Notice is hereby given that the annual general meeting of shareholders of XOMA Ltd. (the Company) will be held at The Claremont Hotel, Ashby and Domingo Avenues, Berkeley, California, on May 23, 2006, at 9:00 a.m. local time, for the following purposes:

1. To elect directors;

2. To appoint Ernst & Young LLP to act as the Company s independent auditors for the 2006 fiscal year and authorize the Board to agree to such auditors fee;

3. To receive the Company s audited financial statements for the 2005 fiscal year;

4. To approve an amendment to the Company s Restricted Share Plan to eliminate the provisions thereof that permit the issuance of shares at a price, and the granting of options with an exercise price, representing a discount to the fair market price of the common shares on the date of issuance or grant, as the case may be;

5. To approve amendments to the Company s 1981 Share Option Plan and Restricted Share Plan to increase the number of shares issuable over the terms of the two plans by 3,450,000 shares to 14,600,000 shares in the aggregate;

6. To approve an amendment to the Company s Restricted Share Plan to increase the number of shares issuable over the term of the plan by 750,000 shares (which shares will come out of the 3,450,000 share increase referred to in item 5 above) to 2,250,000 shares in the aggregate; and

7. To consider and transact such other business as may properly come before the meeting or any adjournment or postponement thereof.

The Board of Directors has fixed the close of business on March 30, 2006, as the record date for the determination of shareholders entitled to notice of, and to vote at, this meeting and at any adjournment or postponement thereof.

By Order of the Board of Directors

Christopher J. Margolin

Secretary

April 13, 2006

Berkeley, California

YOUR VOTE IS IMPORTANT

You are cordially invited to attend the meeting in person. Whether or not you plan to attend the meeting, please promptly mark, sign and date the enclosed proxy and mail it in the accompanying postage pre-paid envelope or appoint a proxy by telephone or through the Internet.

XOMA LTD.

PROXY STATEMENT

TO THE SHAREHOLDERS:

The enclosed proxy is solicited on behalf of the Board of Directors of XOMA Ltd., a company organized under the laws of Bermuda (XOMA or the Company), for use at the annual general meeting of shareholders to be held at The Claremont Hotel, Ashby and Domingo Avenues, Berkeley, California, on May 23, 2006, at 9:00 a.m. local time, or any adjournment or postponement thereof, at which shareholders of record holding Common Shares on March 30, 2006, will be entitled to vote. On March 30, 2006, the Company had issued and outstanding 95,366,184 common shares, par value US$.0005 per share (Common Shares). Holders of Common Shares are entitled to one vote for each share held.

All registered shareholders can appoint a proxy by paper proxy or by telephone by following the instructions included with their proxy card. Shareholders whose Common Shares are registered in the name of a bank or brokerage firm should follow the instructions provided by their bank or brokerage firm on voting their Common Shares. Shareholders whose Common Shares are registered in the name of a bank or brokerage firm participating in the ADP Investor Communication Services online program may appoint a proxy electronically through the Internet. Instruction forms will be provided to shareholders whose bank or brokerage firm is participating in ADP s program. Signing and returning the proxy card or submitting the proxy by telephone or through the Internet does not affect the right to vote in person at the annual general meeting.

In the case of registered shareholders, a proxy may be revoked at any time prior to its exercise by (a) giving written notice of such revocation to the Secretary of the Company at the Company s principal office, 2910 Seventh Street, Berkeley, California 94710, (b) appearing and voting in person at the annual general meeting, (c) properly completing and executing a later-dated proxy and delivering it to the Company at or before the annual general meeting or (d) retransmitting a subsequent proxy by telephone before the annual general meeting. Presence without voting at the annual general meeting will not automatically revoke a proxy, and any revocation during the meeting will not affect votes previously taken. Shareholders whose Common Shares are registered in the name of a bank or brokerage firm should follow the instructions provided by their bank or brokerage firm on revoking their previously appointed proxies. Abstentions and broker non-votes are each included in the number of Common Shares present and entitled to vote for purposes of establishing a quorum but are not counted in tabulations of the votes cast on proposals presented to shareholders.

The Company will bear the entire cost of solicitation, including preparation, assembly, printing, and mailing of this proxy statement, the proxy card, and any additional material furnished to shareholders. Copies of solicitation material will be furnished to brokerage houses, fiduciaries, and custodians holding in their names Common Shares that are beneficially owned by others to forward to such beneficial owners. The solicitation of proxies may be supplemented by one or more of telephone, telegram, or personal solicitation by directors, officers, or employees of the Company for no additional compensation. We have also engaged Georgeson Shareholder Communications Inc. to assist in such solicitation at an estimated fee of $7,500 plus disbursements. Shareholders appointing a proxy through the Internet should understand that there may be costs associated with electronic access, such as usage charges from Internet access providers and telephone companies, that must be borne by the shareholder.

The Company intends to mail this proxy statement and make it available on the Internet on or about April 13, 2006.

SHARE OWNERSHIP

The following table sets forth certain information regarding all shareholders known by the Company to be the beneficial owners of more than 5% of the Company s outstanding Common Shares and regarding each director, each executive officer and all directors and current executive officers as a group, together with the approximate percentages of outstanding Common Shares owned by each of them. Unless otherwise indicated, amounts are as of March 30, 2006 and each of the shareholders has sole voting and investment power with respect to the Common Shares beneficially owned, subject to community property laws where applicable.

Name of Beneficial Owner	Number of Common Shares Beneficially Owned	Percentage of Common Shares Beneficially Owned
OrbiMed Group(1)	12,938,227	13.6%
Platinum Asset Management Limited(2)	7,830,313	8.2%
Joseph L. Harrosh(3)	6,935,182	7.3%
D.E. Shaw(4)	4,946,412	5.2%
James G. Andress(5)	68,000	*
William K. Bowes, Jr.(6)	98,069	*
J. David Boyle II(7)	30,406	*
John L. Castello(8)	699,223	*
Peter Barton Hutt(9)	20,000	*
Arthur Kornberg, M.D.(10)	78,000	*
Christopher J. Margolin(11)	363,790	*
Patrick J. Scannon, M.D., Ph.D.(12)	346,765	*
W. Denman Van Ness(13)	102,611	*
Patrick J. Zenner(14)	42,500	*
All executive officers and directors as a group as of the record date (10 persons)(15)	1,849,364	1.9%

* Indicates less than 1%.

(1) As reported by the group comprised of OrbiMed Capital LLC, OrbiMed Advisors LLC and Samuel D. Isaly (collectively, the OrbiMed Group) on Schedule 13G/A filed with the Securities and Exchange Commission on February 10, 2006. Members of the OrbiMed Group are investment advisors and hold the securities on behalf of other persons who have the right to receive or the power to direct the receipt of dividends from, or proceeds from sale of, such securities. None of such other persons have an interest in the securities whose ownership is reported on the Schedule 13G that relates to more than 5% of the class. Information is as of December 31, 2005.

(2) As reported by Platinum Asset Management Limited on Schedule 13G filed with the Securities and Exchange Commission on February 14, 2006. Amount is as of December 31, 2005.

(3) As reported by Joseph L. Harrosh on Schedule 13G/A filed with the Securities and Exchange Commission on January 10, 2006, consists of Common Shares issuable upon conversion of $13,000,000 aggregate principal amount of 6.50% Convertible Senior Notes due 2012 (Convertible Notes). Amount is as of December 31, 2005.

(4) As reported by D.E. Shaw Valence Portfolios, L.L.C. (D.E. Shaw Valence), D.E. Shaw & Co., L.P. and David E. Shaw on Schedule 13G filed with the Securities and Exchange Commission on January 24, 2006, (a) consists of 1,745,559 Common Shares in the name of D.E Shaw Valence, 533,475 Common Shares issuable in the name of D.E. Shaw Valence upon conversion of $1,000,000 aggregate principal amount of Convertible Notes and 2,667,378 Common Shares issuable in the name of a swap counterparty to which D.E. Valence has exposure upon conversion of $5,000,000 aggregate principal amount of Convertible Notes and (b) each of these reporting persons has shared voting power over 2,279,034 of such Common Shares and shared dispositive power over all 4,946,412 of such Common Shares. Information is as of January 23, 2006.

(5) Includes 66,000 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.

(6) Includes 67,000 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.

(7) Includes 16,667 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.
(8) Includes 25,778 Common Shares held by The John L. and Katherine C. Castello Trust, of which Mr. Castello is a trustee. Includes 566,250 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date. Does not include 20,421 Common Shares that have vested pursuant to the Company s Deferred Savings Plan.
(9) Includes 20,000 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.
(10) Includes 67,000 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.
(11) Includes 294,375 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date. Does not include 20,828 Common Shares that have vested pursuant to the Company s Deferred Savings Plan.
(12) Includes 60,805 Common Shares held by The Patrick J. Scannon Separate Property Trust. Includes 229,375 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date. Does not include 21,291 Common Shares that have vested pursuant to the Company s Deferred Savings Plan.
(13) Includes 49,481 Common Shares held by The Van Ness 1983 Revocable Trust, of which Mr. Van Ness is a trustee. Includes 52,000 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.
(14) Represents 42,500 Common Shares issuable upon the exercise of options exercisable as of 60 days after the record date.
(15) Includes 1,706,167 Common Shares issuable upon exercise of options exercisable as of 60 days after the record date. Does not include 75,848 Common Shares that have vested pursuant to the Company s Deferred Savings Plan.

COMPENSATION OF EXECUTIVE OFFICERS

The following table sets forth the compensation of the named executive officers for the last three completed fiscal years of the Company:

SUMMARY COMPENSATION TABLE

					Long-Term	
		Annual Compensation			Compensation	
				Other Annual	Securities	All Other
			Bonus	Compensation	Underlying	Compensation
Name and Principal Position	**Year**	**Salary ($)**	**($)(1)**	**($)(2)**	**Options (#)**	**($)(3)**
John L. Castello (Chairman of the Board, President	2005	$ 500,000	$ 147,000	$ 8,854	100,000	$ 32,182
	2004	$ 500,000	N/A	$ 956	100,000	$ 30,692
and Chief Executive Officer)	2003	$ 500,000	N/A	$ 12,080	100,000	$ 30,182
Patrick J. Scannon, M.D., Ph.D.	2005	$ 350,000	$ 120,190	$ 1,471	30,000	$ 11,838
	2004	$ 340,000	$ 79,127	$ 3,615	30,000	$ 10,838
(Senior Vice President and Chief Scientific and Medical Officer)	2003	$ 340,000	$ 69,022	$ 2,615	30,000	$ 9,787
J. David Boyle II	2005	$ 223,519	N/A	$ 40,000	80,000	$ 1,097
	2004	N/A	N/A	N/A	N/A	N/A
(Vice President, Finance and Chief Financial Officer)	2003	N/A	N/A	N/A	N/A	N/A
Peter B. Davis	2005	$ 145,000	$ 91,185	$ 32,169	30,000	$ 10,316
	2004	$ 280,000	$ 76,661	$ 0	30,000	$ 10,081
(Retired Vice President, Finance and Chief Financial Officer)	2003	$ 270,000	$ 36,899	$ 0	40,000	$ 8,806

Christopher J. Margolin	2005	$ 290,000	$ 98,359	$ 13,308	55,000	$ 11,679
(Vice President, General Counsel	2004	$ 280,000	$ 67,519	$ 12,846	30,000	$ 10,563
and Secretary)	2003	$ 270,000	$ 56,696	$ 12,384	50,000	$ 9,348

3

(1) The amount in the column for 2005 for Mr. Castello represents an award under the Company s CEO Incentive Compensation Plan in the amount of $73,500 and 31,784 Common Shares (relating to performance in 2004). Each amount in this column for 2005, 2004 and 2003 for Dr. Scannon, Mr. Davis and Mr. Margolin represents awards under the Company s Management Incentive Compensation Plan in the following amounts: Dr. Scannon $40,630 and 18,319 Common Shares in 2005 (relating to performance in 2004); $21,771 in each of 2005 and 2004 and 2,167 Common Shares in 2004 (relating to performance in 2003); $17,160 in each of 2005, 2004 and 2003 and 3,382 Common Shares in 2003 (relating to performance in 2002); $18,426 in each of 2004 and 2003 (relating to performance in 2001); and $16,277 in 2003 (relating to performance in 2000); Mr. Davis $32,834 and 13,290 Common Shares in 2005 (relating to performance in 2004); $19,018 in each of 2005 and 2004 and 1,700 Common Shares in 2004 (relating to performance in 2003); $13,900 in 2003 and 2,299 Common Shares in each of 2005, 2004 and 2003 (relating to performance in 2002); 737 Common Shares in each of 2004 and 2003 (relating to performance in 2001); and 742 Common Shares in 2003 (relating to performance in 2000); and Mr. Margolin $32,253 and 13,661 Common Shares in 2005 (relating to performance in 2004); $19,693 in each of 2005 and 2004 and 1,684 Common Shares in 2004 (relating to performance in 2003); $14,160 in each of 2005, 2004 and 2003 and 2,449 Common Shares in 2003 (relating to performance in 2002); $13,972 in each of 2004 and 2003 (relating to performance in 2001); and $14,403 in 2003 (relating to performance in 2000).

(2) Mr. Castello s amounts in this column for 2005, 2004 and 2003 include financial services provided to Mr. Castello in the amount of $4,176, $400 and $4,888, respectively. Mr. Castello s amounts in this column for 2005, 2004 and 2003 represent taxes paid by XOMA on Mr. Castello s behalf in the amounts of $2,755, $556 and $3,347, respectively. All of Dr. Scannon s amount for 2005 and 2003 and $2,615 of the amount for 2004, $24,654 of Mr. Davis amount for 2005, all of Mr. Margolin s amounts in this column for 2005, 2004 and 2003 and the balance of Mr. Castello s amounts for 2005 and 2003 represent cash payments in lieu of earned vacation and/or personal holidays. Dr. Scannon s amount for 2004 includes $1,000 for patent awards. Mr. Boyle s amount for 2005 represents a sign on bonus. The remainder of Mr. Davis amount for 2005 represents a retirement gift.

(3) Amounts in this column for 2005, 2004 and 2003 include the Company s Common Shares contributed to accounts under the Company s Deferred Savings Plan, valued at fiscal year-end formula prices of $1.6900, $2.611 and $6.6392 , respectively, per share, in the following amounts: Mr. Castello 5,326 Common Shares for 2005, 2,876 Common Shares for 2004 and 1,054 Common Shares for 2003; Dr. Scannon and Mr. Margolin 5,326 Common Shares each for 2005, 3,064 Common Shares each for 2004 and 1,054 Common Shares each for 2003; and Mr. Davis 3,064 Common Shares for 2004 and 1,054 Common Shares for 2003. Amounts for 2005, 2004 and 2003 also include group term life insurance premiums in the following amounts: Mr. Castello $5,182 for each of 2005, 2004 and 2003; Dr. Scannon $2,838 for each of 2005, 2004 and 2003; Mr. Boyle $1,097 for 2005; Mr. Davis $1,316 for 2005, $2,081 for 2004 and $1,806 for 2003; and Mr. Margolin $2,679 for 2005, $2,563 for 2004 and $2,348 for 2003. Mr. Castello s amounts in this column include life insurance premiums paid in the amount of $18,000 for each of 2005, 2004 and 2003. Dr. Scannon s amount for 2003 includes $(51) which represents the difference between (i) the amount of interest Dr. Scannon would have been required to pay in interest for such year had the loan made to him by the Company pursuant to his employment agreement been made at the then-prevailing market rate and (ii) the amount of interest payable on the loan for such year in accordance with its terms. See Employment Contracts and Termination of Employment and Change-in-Control Arrangements.

The following table contains information concerning the grant of options under the Company s option plans to the named executive officers as of the end of the last completed fiscal year of the Company. No share appreciation rights (SARs) were granted during the last fiscal year and none were held at the end of the fiscal year.

OPTION GRANTS IN LAST FISCAL YEAR

	Individual Grants				Potential Realized Value of Assumed Annual Rates of Share Price Appreciation For Option Term(1)		
Name	Number of Securities Underlying Options Granted (#)	% of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price ($/SH)	Expiration Date	0% ($)	5% ($)	10% ($)
John L. Castello	100,000	7.7%	$ 1.40	02/23/2015	0	$ 88,045	$ 223,124
Patrick J. Scannon, M.D., Ph.D	30,000	2.3%	$ 1.40	02/23/2015	0	$ 26,414	$ 66,937
J. David Boyle II	50,000	3.8%	$ 2.40	01/04/2015	0	$ 75,467	$ 191,249
	30,000	2.3%	$ 1.81	07/20/2015	0	$ 34,149	$ 86,540
Peter B. Davis	30,000	2.3%	$ 1.40	02/23/2015	0	$ 26,414	$ 66,937
Christopher J. Margolin	30,000	2.3%	$ 1.40	02/23/2015	0	$ 26,414	$ 66,937
	25,000	1.9%	$ 1.78	10/25/2015	0	$ 27,986	$ 70,922

(1) The amounts set forth in the three columns represent hypothetical gains that might be achieved by the optionees if the respective options are exercised at the end of their ten-year option terms. These gains are based on assumed rates of share price appreciation of 0%, 5% and 10% compounded annually from the dates the respective options were granted. Options granted with exercise prices equal to the market price of the underlying Common Shares on the date of grant will have no value unless the Company s share price increases above the exercise prices as a result of actions by the executives that improve the Company s performance and/or other factors affecting such price.

The following table sets forth information with respect to the named executive officers concerning the exercise of options during the last completed fiscal year of the Company and unexercised options held as of the end of the fiscal year. No SARs were exercised during the last fiscal year and none were held at the end of the fiscal year.

AGGREGATE OPTION EXERCISES IN LAST FISCAL YEAR AND FY-END OPTION VALUES

Name	Shares Acquired On Exercise (#)	Value Realized	Number of Securities Underlying Unexercised Options at FY-End Exercisable	Unexercisable	Value of Unexercised in-the-Money Options at FY-End ($)(1) Exercisable	Unexercisable
John L. Castello	0	$ 0	585,000	100,000	$ 0	$ 20,000
Patrick J. Scannon M.D., Ph.D	0	$ 0	270,000	30,000	$ 0	$ 6,000
J. David Boyle	0	$ 0	0	80,000	$ 0	$ 0
Peter B. Davis	0	$ 0	310,000	0	$ 6,000	$ 0
Christopher J. Margolin	0	$ 0	310,000	55,000	$ 0	$ 6,000

(1) The amounts listed in the two columns are based on the closing price per share of $1.60 on December 31, 2005, as reported on The Nasdaq Stock Market, less the applicable option exercise prices.

Employment Contracts and Termination of Employment and Change-in-Control Arrangements

The Company has entered into an employment agreement with Mr. Castello, dated as of April 29, 1992, that provides for his employment as President and Chief Executive Officer at a salary of $500,000 per year. Under this agreement, Mr. Castello also receives all standard Company employee benefits and supplemental life insurance for the amount that an annual premium of $18,000 provides. The agreement also provides for a grant of options for 500,000 Common Shares under the Company s 1981 Share Option Plan (the Option Plan), which was made in 1992.

Mr. Castello s employment may be terminated, with or without cause, at the will of either party. If terminated by the Company for any reason other than due cause or by Mr. Castello for good reason, Mr. Castello must be paid his then current base salary and benefits for one year. If terminated for due cause, he is entitled to no further compensation. Good reason includes, in the context of a change of control, the assignment to Mr. Castello of duties inconsistent with his prior duties; his removal from, or failure to re-elect him to, any position he held immediately prior to the change in control; any termination by the Company within three years of the change of control other than for due cause or upon disability or death; a good faith determination by Mr. Castello that changes in circumstances resulting from the change in control leave him substantially unable to perform his duties, after notice; the failure of the Company s successor or the transferee of its assets or business to assume its obligations under the agreement; or, a significant relocation of the Company s executive offices. Good reason also includes any reduction in base pay or benefits or any breach of the agreement by the Company.

The Company has entered into an employment agreement with Dr. Scannon, dated as of March 26, 2006, that provides for his employment as Senior Vice President and Chief Scientific and Medical Officer at a salary of $350,000 per year. Under this agreement, Dr. Scannon is entitled to participate in any benefit plan for which key executives of the Company are eligible, including the Management Incentive Compensation Plan established effective July 1, 1993 (as amended, the MICP). Upon termination of his employment for any reason other than cause, or upon resignation, Dr. Scannon must be paid his then current base salary and benefits for one year.

The Company had an employment agreement with Mr. Davis dated as of April 1, 1994 that provided for his employment as Chief Financial Officer at an initial salary of $200,000 per year. Under this agreement, Mr. Davis received a one-time transition allowance in the amount of $35,000 and was entitled to participate in any benefit plan for which executives of the Company were eligible. In addition, the agreement provided for an initial grant of options for 60,000 Common Shares under the Option Plan, which was made in 1994, as well as participation in the MICP. Mr. Davis employment agreement provided no additional compensation in the event of a change of control but provided a minimum severance amount equal to six months of base salary at the time of termination.

The Company has entered into an employment agreement with Mr. Margolin, dated as of February 23, 2005, that provides for his employment as Vice President, General Counsel and Secretary at a salary of not less than $290,000 per year. Under the agreement, Mr. Margolin will be entitled to participate in any benefit plan for which key executives of the Company are eligible, including the MICP. Upon termination of his employment by the Company for any reason other than cause or upon his resignation from the Company for good reason, Mr. Margolin will be entitled to his then current base salary and benefits for nine months. The agreement will continue until February 22, 2006, and will be automatically extended (without further action by the parties) for one year thereafter and again on each subsequent anniversary thereof, unless terminated by mutual written consent of the parties.

The Company has entered into an employment agreement with Mr. Boyle, effective as of July 1, 2005, that provides for his employment as Vice President, Finance and Chief Financial Officer at a salary of not less than $240,000 per year. Under the agreement, Mr. Boyle is entitled to participate in any benefit plan for which key executives of the Company are eligible, including the MICP. Upon termination of his employment by the Company for any reason other than cause or upon his resignation from the Company for good reason, Mr. Boyle will be entitled to his then current base salary and benefits for six months. The agreement will continue until June 30, 2006, and will be automatically extended (without further action by the parties) for one year thereafter and again on each subsequent anniversary thereof, unless terminated by mutual written consent of the parties.

Compensation Committee Report on Executive Compensation

The Company s compensation program for officers (including the named executive officers) is administered by the Compensation Committee of the Board of Directors (the Committee), which is composed of three independent directors. Following review and approval by the Committee, all issues pertaining to officer compensation are submitted to the full Board of Directors for approval. The primary objectives of the Company s compensation program are to enable the Company to attract, motivate and retain outstanding individuals and align their success with that of the Company s shareholders through the creation of shareholder value and achievement of strategic corporate objectives.

The level of compensation paid to an officer is determined on the basis of the individual s overall experience, responsibility, performance and compensation level in his or her prior position (for newly hired officers), the individual s overall performance and compensation level at the Company during the prior year (for current employees), the compensation levels of similarly situated individuals in the pharmaceutical and biotechnology industries (including, but not limited to, the biotechnology companies included in the AMEX Biotechnology Index) and other labor markets in which the Company competes for employees, the performance of the Company s Common Shares during the prior fiscal year and such other factors as may be appropriately considered by the Board of Directors, by the Committee and by management in making its initial proposals to the Committee.

Mr. Castello s compensation for 2005 was determined after considering the general factors described above and the terms of his existing employment contract. In 1992, the Committee approved, and recommended that the Board approve, the terms of Mr. Castello s employment contract, as more fully described under Employment Contracts and Termination of Employment and Change-in-Control Arrangements, because it felt that the terms thereof were necessary in order to attract a candidate of Mr. Castello s experience and reputation in the pharmaceutical industry, which in turn was deemed necessary in order to enable the Company to advance toward its long-range goal of becoming a pharmaceutical company with commercially viable products. In 2004, the Committee, the Board and the shareholders approved the CEO Incentive Compensation Plan (the CICP) in order to make Mr. Castello s compensation more commensurate with that of his peers and because the Committee believed that it was not appropriate to include Mr. Castello in the Management Incentive Compensation Plan given his active role in administering that plan.

Only the chief executive officer of the Company (CEO) is eligible to participate in the CICP, and depending on his or her performance and that of the Company, earn incentive compensation. The determination of the incentive compensation awarded for each fiscal year is as follows: The target award opportunity for the CEO is set at 50% of his or her base salary. As soon as practicable after the end of each fiscal year (the Plan Period), the Committee will recommend to the Board and the Board will determine whether and to what extent certain Company objectives (Company Objectives) have been met. Company Objectives may be based on financial goals, scientific or commercial progress, profits, return on investments or any other criteria established by the Board. For each Plan Period, unless 70% of the Company Objectives have been met, no incentive compensation will be awarded.

The incentive compensation will be weighted based 70% on meeting Company Objectives and 30% based on discretionary objectives. The award opportunity range for the CEO expressed as a percentage of his or her base salary is as follows: minimum award opportunity 25%; target award opportunity 50%; and maximum award opportunity 75%.

The performance of the CEO will be rated as soon as practicable following the conclusion of the Plan Period. Distribution of incentive compensation will be established by the Board, and will generally be in February or March of the succeeding year after the Plan Period. The incentive awards will be comprised 50% of cash and 50% of common shares (based on the average market value of the common shares for the 10 trading days prior to the date of the award).

For 2005, the Committee and the Board determined that Mr. Castello had met a percentage of the Company Objectives in excess of the 70% minimum required by the CICP in order to make an award thereunder.

The principal methods for long-term incentive compensation are the Option Plan and Restricted Share Plan (the Restricted Plan), and compensation thereunder principally takes the form of incentive and non-qualified option grants. These grants are designed to promote the convergence of long-term interests between the Company s key employees and its shareholders; specifically, the value of options granted will increase or decrease with the value of the Company s Common Shares. In this manner, key individuals are rewarded commensurately with increases in shareholder value. These grants also typically include a 4-year vesting period to encourage continued employment. The size of a particular option grant is determined based on the individual s position with and contribution to the Company. For grants during 2005, the number of options granted were determined based on the numbers of options granted to such individuals in the previous fiscal year, the aggregate number of options held by each such individual, the number of options granted to similarly situated individuals in the pharmaceutical and biotechnology industries, the price of the Company s Common Shares relative to other companies in such industries and the resulting relative value of such options; no specific measures of corporate performance were considered.

Certain employees are also compensated through the MICP, in which management employees (other than the Chief Executive Officer), as well as certain additional discretionary participants chosen by the Chief Executive Officer, are eligible to participate. Under the MICP, at the beginning of each fiscal year, the Board of Directors (with advice from the Committee) establishes a target incentive compensation pool, which is then adjusted at year-end to reflect the Company s performance in achieving its corporate objectives.

After each fiscal year, the Board of Directors and the Committee make a determination as to the performance of the Company and MICP participants in meeting corporate objectives and individual objectives, which are determined from time to time by the Board of Directors in its sole discretion and which included for 2005: a target level of cash at year end; generation of current income; progress toward collaborations, potential partnerships or financing arrangements; and various objectives tied to development of the Company. Awards to MICP participants vary depending upon the level of achievement of corporate objectives, the size of the incentive compensation pool and the MICP participants base salaries and performance during the fiscal year as well as their expected ongoing contribution to the Company. The Company must meet a minimum percentage of its corporate objectives (currently 70%) before any awards are made under the MICP.

Awards under the MICP granted on or prior to December 31, 2004 vest over a three-year period with 50% of each award payable during the first quarter of the following fiscal year, and 25% payable on each of the next two annual distribution dates, so long as the participant remains an employee of the Company. The 50% on each distribution date is payable half in cash and half in Common Shares. Awards under the MICP granted after December 31, 2004, including grants made in 2005 for performance in 2004, are made in one payment soon after the end of the relevant fiscal year, rather than three payments over three years, and are payable half in cash and half in Common Shares. All share issuances under the MICP are made pursuant to the Restricted Plan.

For 2005, the Committee and the Board of Directors determined that management had met a percentage of the corporate objectives summarized above in excess of the 70% minimum required by the MICP in order to make awards thereunder. For 2005, 83 individuals were determined to be eligible to participate in the MICP, including all of the executive officers named in the Summary Compensation Table above other than Mr. Castello.

Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code), generally limits the deductible amount of annual compensation paid to certain individual executive officers (i.e., the chief executive officer and the four other most highly compensated executive officers of the Company) to no more than $1 million. However, qualifying performance-based compensation will be excluded from the $1 million cap on deductibility, and the Committee believes, based on information currently available, that the Company s options issued to its executive officers qualify for this exclusion. Considering the current structure of executive officer compensation and the availability of deferral opportunities, the Committee believes that the Company will not be denied any significant tax deduction for 2005. The Committee will continue to review tax consequences as well as other relevant considerations in connection with compensation decisions.

W. Denman Van Ness

William K. Bowes, Jr.

Peter Barton Hutt

PERFORMANCE GRAPH

Comparison of Five Year Cumulative Total Return Among XOMA,

Nasdaq Composite Index and AMEX Biotechnology Index

As of December 31,	XOMA Ltd.	Nasdaq Composite Index	AMEX Biotechnology Index
2000	100.00	100.00	100.00
2001	101.03	78.95	91.53
2002	43.38	54.06	53.32
2003	67.69	81.09	77.26
2004	26.56	88.06	85.80
2005	16.41	89.27	107.34

The comparison assumes $100 invested on December 31, 2000 in the Company s Common Shares, the Nasdaq Composite Index, and the AMEX Biotechnology Index. Total return assumes reinvestment of dividends although the Company has never paid cash dividends. Returns for the Company are not necessarily indicative of future performance.

ITEM 1 ELECTION OF DIRECTORS

The Company s directors are elected annually to serve until the next annual general meeting of shareholders and until their successors are elected, or until their death, resignation or removal. The nominees for the Board of Directors are set forth below. Unless otherwise instructed, the proxy holders will vote all proxies received by them in the accompanying form for the nominees for directors listed below. In the event any nominee should become unavailable for election due to an unexpected occurrence, the proxies will be voted for any such substitute nominee as may be designated by the present Board of Directors to fill the vacancy. In the event that additional persons are nominated for election as directors, the proxy holders intend to vote all proxies received by them for the nominees listed below. Each person nominated for election has agreed to serve if elected, and management has no reason to believe that any of the nominees listed below will be unable to serve. The eight candidates receiving the highest number of affirmative votes of the Common Shares entitled to vote at the annual general meeting will be elected as directors of the Company.

NOMINEES TO BOARD OF DIRECTORS

Name	Title	Age
John L. Castello	Chairman of the Board, President and Chief Executive Officer	69
Patrick J. Scannon, M.D., Ph.D.	Senior Vice President, Chief Scientific and Medical Officer and Director	