



Through the Looking Glass: Proxy Disclosures – How to Avoid the Challenges

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Agenda

- Proxy Disclosure Challenges
 - ◆ Compensation Discussion & Analysis
 - ◆ Executive Compensation Tables
 - ◆ Termination Payments and Benefits
 - ◆ Director Compensation
 - ◆ Other Challenges
- Avoiding SEC Comments
- Best Proxy Disclosure Practices



Proxy Disclosure Challenges

Proxy Disclosure Challenges

- The SEC Staff of the Division of Corporation Finance conducted an Executive Compensation Disclosures Review project after the 2007 proxy season
- The Review focused on approximately 350 companies' executive compensation disclosures under the new proxy disclosure rules during the first proxy season they applied, 2007
- We have reviewed publicly available SEC comments for about 90 of these companies, as well as the 2008 proxy disclosures, where available



Proxy Disclosure Challenges

- Most companies exchanged letters with the SEC staff on the comments 2 or 3 times
- Why should you care?
 - ◆ 2009 disclosures likely to receive even greater scrutiny
 - ◆ The SEC has indicated companies needed to follow the rules, especially in regard to
 - Providing analysis in the CD&A
 - Disclosure or non-disclosure (assuming the requirements are met) of performance goals, and
 - Presentation



Proxy Disclosure Challenges

- “As we enter the second season, we will expect companies to have taken our guidance to heart, and I anticipate that you will see that heightened expectation reflected in the type and focus of our comments and reactions next year”
 - John White, Director,
Division of Corporation Finance, U.S. SEC





Proxy Disclosure Challenges

Compensation Discussion & Analysis

Compensation Discussion & Analysis

- Analysis
- Compensation Policy
- Role of Executive Officers in Determining Compensation
- Role of Compensation Consultants in Determining Compensation
- Use of Discretion
- Internal Equity
- Benchmarking



Compensation Discussion & Analysis

- Allocation between Cash and Equity
- Performance Goals
- Annual Incentive Compensation
- Long-Term Incentives & Equity Awards





Proxy Disclosure Challenges

Executive Compensation Tables

Executive Compensation Tables

- Summary Compensation Table
 - ◆ Alternative Tables
 - ◆ Bonus
 - ◆ Perquisite Allowances
 - ◆ Corporate Aircraft



Executive Compensation Tables

- Grants of Plan-Based Awards Table
 - ◆ Full footnote description of awards
 - ◆ Dividends paid?
 - ◆ Threshold, Target, and Maximum
 - ◆ Size of Awards – How Determined & Why



Executive Compensation Tables

- Outstanding Equity Awards at Fiscal Year End Table
 - ◆ Footnote vesting dates of awards
- Pension Benefits Table
 - ◆ Difference in number of years of credited service
 - ◆ Difference between years of service & years of credited service



Executive Compensation Tables

- Non-Qualified Deferred Compensation Table
 - ◆ How interest or earnings is calculated
 - ◆ Footnote regarding amount of previously reported compensation shown
 - ◆ Succinct narrative of material factors





Proxy Disclosure Challenges

Termination Payments and Benefits

Termination Payments and Benefits

- Explain how appropriate payment and benefit levels determined
- Consider using a table
- Define terms used, *e.g.* “Cause,” “Good Reason,” “Change in Control”
- Consider including a total for each executive for each triggering event
- Describe and explain material conditions or obligations to receive payments or benefits





Proxy Disclosure Challenges

Director Compensation

Director Compensation


- Disclose all assumptions in valuing awards
- Footnote grant date fair value of equity awards
- How amount of equity grants determined
- Include any matching gifts/charitable contributions
- Policy regarding mix of cash/equity



Proxy Disclosure Challenges

Other Challeges

Other Challenges

- Material differences in compensation policies for individual NEOs
 - Changes/actions after FYE
 - Actual vs. Targeted Percentiles
 - Over reliance on abbreviations
 - Using too many defined terms
 - Use of jargon
 - ◆ Stretch goal
 - ◆ Earnings kicker
 - Overly legalistic disclosure
- 

Avoiding SEC Comments

Avoiding SEC Comments

- Comply with the rules
- Know what the SEC has focused on in other companies' disclosures
- Consider whether a comment indicating that the company does not offer particular types of compensation would be useful
- Disclose performance goals – or – have a well thought out reason for not disclosing them that complies with the “competitive harm” requirements



Avoiding SEC Comments

- If disclosure indicates a change in your compensation programs going forward, consider whether current year compensation actions should be disclosed



Avoiding SEC Comments

■ Questions to ask before drafting disclosures from Director John White:

- ◆ What is material to my shareholders, to my investors, as they examine the compensation of our executives and make their voting decisions for our board of directors and investment decisions with respect to our company?
- ◆ What are the material elements of individual executive and corporate performance that are considered in setting executive compensation?
- ◆ What is the relationship between the objectives of our compensation program and the different elements of compensation?
- ◆ What are the material factors that relate to our compensation decisions-making process?



Avoiding SEC Comments

- Then focus on two important aspects of your disclosure:
 - ◆ Analysis – Focus on how and why you reached the compensation decisions you made in your CD&A.
 - ◆ Presentation matters – Focus on being clear, concise and understandable. Consider:
 - Ways to present your information in a manner that helps people understand it




Best Proxy Disclosure Practices

Best Proxy Disclosure Practices

■ CD&A

◆ Overview of **Compensation Elements** chart

- Fiserv (element & description)
 - Kimberly Clark (element, objectives, purpose, target competitive position)
 - United Parcel Service – multiple (program & award type, payment form & program type, target amount, performance measures, performance objectives)
 - USG Corp. (program, description, participants, objectives achieved)
 - Verizon (element, primary objective, relative weight)
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Best Proxy Disclosure Practices

- ◆ Where appropriate, provide **totals by executive**
- ◆ **Avoid** using **too many** defined terms
- ◆ **Avoid jargon** and overly **legalistic** disclosure
- ◆ Include **analysis** - the *how* and the *why* behind the compensation figures that are disclosed
- ◆ Use **charts** and **graphs** to aid understanding
- ◆ **Overview** of the company's **compensation policies** and programs and discussion of *how* each element supports those policies and programs



Best Proxy Disclosure Practices

- ◆ Better disclose **performance goals** and **actual performance achieved**
- ◆ Explain (if applicable) *how* **individual performance** and/or **Tally Sheets** impacted the determination of compensation
- ◆ If there is a **significant difference** between the **compensation reported for one NEO** and the rest of the NEOs, consider affirmatively addressing whether this was the result of a **material difference in compensation policies with respect to individual NEOs** or some other reason



Best Proxy Disclosure Practices

- ◆ Detail any **subjective** factors considered
- ◆ Detail *how* **Internal Pay Equity** (if considered) impacted the compensation decisions that were made
- ◆ Provide a **summary of compensation decisions made** – last FY and current FY (if applicable)
- ◆ **After FYE Compensation Actions** –
Performance Targets, Change to Plans/Programs,
New Plans/Programs



Best Proxy Disclosure Practices

- ◆ **Stock Ownership Guidelines** – explain what amounts executives must hold, how calculated, if executives are in compliance, how long they have to comply, and consequence of failing to comply
- ◆ Explain *how* and *why* the company has **employment contracts** with NEOs (if applicable)
- ◆ Explain *how* the **amounts** and **levels** were **determined** for purposes of any severance or change in control payment or benefit



Best Proxy Disclosure Practices

- Summary Compensation Table / Director Compensation Table
 - ◆ Include footnotes that detail all the **valuation assumptions** and detail the **grant date fair value** (under FAS 123R) used for each equity award
 - ◆ Include a sub-table to the Summary Compensation Table that outlines the components of Non-Equity Incentive Compensation (if figures are totals of multiple items)
 - ◆ Include a sub-table to the Summary Compensation Table that outlines the components of All Other Compensation, by items and executive



Best Proxy Disclosure Practices

- Grants of Plan-Based Awards Table
 - ◆ Include a description of the various grants in the table
- Termination and Change in Control Payments and Benefits
 - ◆ Consider using a chart to help explain termination or change in control payments and benefits
 - ◆ Explain how payment and benefit amounts were determined



Best Proxy Disclosure Practices

■ Director Compensation

- ◆ Ensure your narrative to the Director Compensation Table offers a succinct explanation of the compensation provided to directors – consider using tables to help improve understandability
- ◆ Detail any matching gift or charitable contribution programs in the narrative and in a footnote to the Director Compensation Table if programs used



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A special thanks to Equilar for assisting us in our review of the CD&As of the approximately 90 companies, www.equilar.com

