

**The Effect of Proxy Issues on
Executive Compensation**
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**A Review of the Recent Proxy Season and
What You Should Be Considering Now**

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Agenda

- Review of 2009 proxy season
- Review of RMG/ISS policies
- Recent developments

Review of 2009 Proxy Season

- Stakeholder proposals
 - Social/environmental
 - Governance: board-related
 - *Independent chairman*
 - *Elimination of poison pills*
 - *Right to call special meetings*
 - *Majority voting*

Review of 2009 Proxy Season (Cont'd)

- Governance: compensation-related
 - *Say on pay*
 - *Golden parachutes*
 - *Golden coffins*
 - *Share retention*
 - *Gross-up on perks*

Shareholder Proposal – Say on Pay

	<u>2007#</u>	<u>2007%</u>	<u>2008#</u>	<u>2008%</u>	<u>2009YTD#</u>	<u>2009YTD%</u>
Total	51	100%	76	100%	71	100%
RMG AGAINST	2	3.92%	0	0.00%	0	0.00%
RMG FOR	49	96.08%	76	100.00%	71	100.00%
FAIL	41	80.39%	64	84.21%	9	12.68%
PASS	5	9.80%	8	10.53%	4	5.63%
Pending/Not Disclosed ¹	5	9.80%	4	5.26%	58	81.69%
Average Support (F / (F+A+ABS))		38.04%		39.09%		46.23%

*Data from ISS voting analytics

¹Based on reports in 10-Qs of voting results

Management Proposal – Say on Pay

	<u>2007#</u>	<u>2007%</u>	<u>2008#</u>	<u>2008%</u>	<u>2009YTD#</u>	<u>2009YTD%</u>
Total	7	100%	11	100%	138	100%
RMG AGAINST	0	0.00%	1	9.09%	39	28.26%
RMG FOR	7	100.00%	7	63.64%	97	70.29%
FAIL	0	0.00%	0	0.00%	0	0.00%
PASS	3	42.86%	8	72.73%	21	15.22%
Pending/Not Disclosed ¹	4	57.14%	3	27.27%	117	84.78%
Average Support (F / (F+A+ABS))		78.37%		88.48%		84.17%
NOTE: 2008, 2009 RMG made no recommendation on its own agenda items						

*Data from ISS voting analytics

¹Based on reports in 10-Qs of voting results

Review of 2009 Proxy Season (Cont'd)

- Equity plan proposals
 - New plan/amendments
 - Repricings
- Withhold/no votes for directors/compensation committee members

Who is RMG/ISS?

- Preeminence of RMG/ISS Franchise
- Consulting vs. Advisory Function
- Access to RMG/ISS Review
 - COMPASS Product
 - Fee for consultation review
- Increase in use of RMG/ISS “pre-review”

Equity Plan Proposal Stats (2007-2009 YTD)

	<u>2007#</u>	<u>2007%</u>	<u>2008#</u>	<u>2008%</u>	<u>2009YTD#</u>	<u>2009YTD%</u>
Total	750	100%	843	100%	767	100%
RMG AGAINST	217	28.93%	207	24.56%	198	25.81%
RMG FOR	533	71.07%	636	75.44%	569	74.19%
FAIL	12	1.60%	19	2.25%	1	0.13%
PASS	640	85.33%	752	89.21%	106	13.82%
Pending/Not Disclosed¹	95	12.67%	70	8.30%	660	86.05%
Withdrawn	3	0.40%	2	0.24%	0	0.00%
Average Support (F / (F+A+ABS))		81.29%		82.04%		81.62%
NOTE: 2009 data is through 7/17/2009						
Many vote results for 2009 are not known yet						

*Data from ISS voting analytics

¹Based on reports in 10-Qs of voting results

RMG/ISS Policy Overview

- How much will the plan cost?
 - Shareholder Value Transfer (SVT): Binomial (proprietary) model that measures the amount of wealth flowing out of the company to plan participants as awards exercise and vest.
 - SVT is expressed as a dollar value and as a percent of company's market cap.
 - Considers proposed new shares, unvested full value shares and all outstanding options (even out-of-the money)
 - Unless restricted to use as options, counts all new shares as full value.
 - Use of fungible share approach.

RMG/ISS Policies—SVT Test

- Is the plan cost reasonable?
 - Compare SVT (%) to allowable cap.
 - The allowable cap is industry-specific, market cap-based, and pegged to the average amount paid by companies performing in the top quartile of their peer groupings.
 - If SVT cost is above the allowable cap RMG will recommend a vote against the plan.
 - Mechanical test--- business rationales (e.g., reduction in use of cash compensation) don't help.
 - Option overhang a killer.

RMG/ISS Policy Overview

- Burn Rate:
 - RMG will recommend a vote against plans if burn rate exceeds one standard deviation from industry mean and 2%.
 - Full-value awards (restricted stock, performance awards, etc) will count as more than one in burn rate depending on company's stock price volatility.
 - Companies that fail the RMG burn rate test may make public commitment to future burn rate and RMG will not apply the burn rate test.

RMG/ISS Policy Overview

- Pay for Performance:
 - Measure of total shareholder returns versus CEO total direct compensation for companies in lower half of TSR performance.
 - RMG will recommend a withhold/against vote on the compensation committee members if there is a pay for performance disconnect. Also, RMG could recommend a vote against the equity plan if increase in TDC is at least 50 percent based on equity.
 - Company may make a public commitment and RMG may override the PfP test.
 - Exceptions for “pay for performance” policies embedded in programs: ability to “argue your case”

RMG/ISS Policy Overview

- Poor pay practices – 2009 version:
 - Poor pay practices may result in a “withhold” or “against” recommendation for directors
 - Excessive severance or change in control arrangements now include:
 - *Payments for termination in connection with performance failures*
 - *Any new or materially amended arrangements that include:*
 - **gross-up provisions**
 - **modified single triggers**
 - **liberal change in control definitions**
 - Tax reimbursements of perquisites
 - Dividends or dividend equivalents on unearned performance awards

RMG/ISS Policy Overview

- Repricing: RMG will recommend a vote against any plan that permits repricing of underwater stock options.
 - Bullet proof repricing language: *"Except in connection with a corporate transaction involving the company (including, without limitation, any stock dividend, stock split, extraordinary cash dividend, recapitalization, reorganization, merger, consolidation, split-up, spin-off, combination, or exchange of shares), the terms of outstanding awards may not be amended to reduce the exercise price of outstanding Options or SARs or cancel outstanding Options or SARs in exchange for cash, other awards or Options or SARs with an exercise price that is less than the exercise price of the original Options or SARs without stockholder approval."*

Option Exchange Programs

	<u>2008</u>	<u>2009 (YTD)</u>
# of proposals	18	69
RMG Recommendation (FOR / AGAINST)	5 / 13	25 / 40

- Data from ISS Voting Analytics
- RMG recommendation pending at 4 companies in 2009

Repricing Programs

- Shareholder friendly programs include
 - Value for value exchange (must have)
 - Exclusion of NEOs and directors (must have)
 - Exercise price of surrendered options must be above the 52-week high in stock price (must have)
 - Reset the vest
 - Explanation of rationale

Option Exchange Programs – 2009 YTD

Company	Meeting Date	ISS Rec	Result	Industry
TRW Automotive Holdings Corp	5/19/2009	Against	Pending	Automobiles and Components
EnergySolutions, Inc.	5/29/2009	Against	Pending	Commercial Services and Supplies
iRobot Corporation	5/28/2009	Against	Pending	Consumer Durables and Apparel
Cherokee, Inc.	6/3/2009	Against	Pending	Consumer Durables and Apparel
LeapFrog Enterprises, Inc.	8/26/2009		Pending	Consumer Durables and Apparel
Starbucks Corp.	3/18/2009	For	Pass	Consumer Services
Dominos Pizza Inc.	4/28/2009	Against	Pending	Consumer Services
Pinnacle Entertainment, Inc.	5/5/2009	Against	Pending	Consumer Services
Calamos Asset Management, Inc.	5/22/2009	Against	Pending	Diversified Financials
MF Global Ltd	8/13/2009		Pending	Diversified Financials

*Data from ISS voting analytics

Option Exchange Programs – 2009 YTD (Cont'd)

Company	Meeting Date	ISS Rec	Result	Industry
Delek US Holdings Inc	5/5/2009	Against	Pending	Energy
Ion Geophysical Corp.	5/27/2009	Against	Pending	Energy
Geokinetics, Inc.	5/27/2009	Against	Pending	Energy
Sirona Dental Systems Inc.	2/25/2009	Against	Pass	Health Care Equipment

*Data from ISS voting analytics

Corporate Governance and Disclosure Changes That May Affect the 2010 Proxy Season

1. **Elimination of brokers' discretionary authority to vote in uncontested elections of directors**
2. **Possible changes in the proxy solicitation process**
 - a. Delivery of management's proxy card
 - b. Rounding out of slate of nominees for directors
 - c. Proxy access
3. **Possible corporate governance changes**
 - a. Annual elections with a majority vote
 - b. Independent chairman of the board
 - c. Independent risk committee of the board
4. **Compensation-related corporate governance changes**
 - a. Independent compensation committees and compensation consultants, counsel and advisors
 - b. Say on pay
 - c. Limits on compensation

Corporate Governance and Disclosure Changes That May Affect the 2010 Proxy Season (Cont'd)

5. Changes in disclosure

a. SEC's proposal

- i. Risks relating to compensation policies and practices*
- ii. Disclosure of grant date fair value*
- iii. Expanded disclosure about director qualifications and background and about legal proceedings involving directors, nominees and executive officers*
- iv. Disclosures about leadership structure*
- v. Disclosures about fees paid to and services provided by compensation consultants*
- vi. Accelerated disclosure of the results of proxy votes*

b. Draft legislation

- i. Disclosure about retention of compensation consultants*
- ii. Improved disclosure of compensation targets*

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