

How to Create More Effective Compensation Committees



December 5, 2007

■ Agenda

- **Introduction**
- **Objectives**
- **Structure, Process and Knowledge**
- **Approaching IPO**
- **Public Company Hot Topics**
- **Stages of Development Summary**

■ Compensation Committee Objectives

- **Build trust in process**
- **Foster strong working relationship with management**
- **Management feels treated fairly**
- **Create a regular forum to discuss pay matters**
- **Support management in developing programs and setting pay**
- **Ensure that management can represent to others that the process is fair, considered and even-handed**

■ Compensation Committee Structure and Process

- Annual calendar
- Name a Committee or acknowledge it's the full Board
- Consider guiding principles early on for items like competitiveness target, pay for performance link, pay mix and grant frequency
- Receive materials at least a week before a meeting
- Consider once, then decide
- Keep accurate minutes with alternatives considered, decisions and rationale for decisions

■ Compensation Committee Knowledge

- **Unless within a year of an offering, generally don't need a consultant**
 - Might need assistance with specific events or technical issues:
 - » Restructuring equity after a recap
 - » Contracts for senior “marquee” hires
 - » Options vs. restricted stock – 409A
- **Educational opportunities for Board members**
 - NACD
 - Roundtables
- **Spend the time to understand current programs**
 - Private company data generally not good
- **Create a concise summary of all pay programs, contracts, etc.**

Approaching IPO

- **Time to consider public company practices more seriously**
- **Implement more structured decision-making**
- **Formalize incentive plans**
- **Formalize pay comparisons**
- **Consider severance and CIC protections**
- **May need professional help for CD&A, compensation comparisons and independent guidance**
- **Impact of FAS expense**

■ Public Company Hot Topics to Consider

- **Broad-based equity distribution declining**
- **Restricted stock use increasing at the expense of options**
- **Peer Groups and pay comparison methodologies under scrutiny**
- **Pay-for-performance emphasis**
- **Disclosure, disclosure, disclosure**
- **Severance and certain CIC provisions under attack**
- **Perquisites under attack and disappearing**

Areas of Focus Based on Stage of Development

Professional Investment

- May implement Guiding Principles
- No separate Compensation Committee
- No formal incentive plans
- Ad-hoc equity allocation process
- No formal compensation review

Market Validation Depending on length in stage

- Guiding Principles
- May have independent directors
- May implement Compensation Committee
- Keep in mind equity grant prices (may effect reporting at future date)
- May implement formal incentive plans

Preparing for an Offering

- Formal Charter
- Independent Directors
- Separate Compensation Committee
- Reserve necessary equity prior to IPO
- May have formal review of compensation
- Formal Incentive Plans
- Ensure plans are in compliance
- FAS 123(R)

Post Offering

- Formal Charter
- Independent Directors
- Separate Compensation Committee
- Formal review of compensation
- Develop Peer Group of Public Firms
- Formal Incentive Plans
- Ensure plans are in compliance
- FAS 123(R)
- Employment contracts
- CIC / Severance
- Prepare for proxy disclosures