

# The Early Returns: A Look at 2008 Executive Pay Disclosures

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## Our Speakers

### **Michael D. Enos**

#### ***Managing Director***

Michael Enos is a Managing Director in the Boston office, where his areas of expertise include executive compensation, long-term incentive compensation strategy and design, and market practices benchmarking.

### **Deborah Lifshey**

#### ***Managing Director***

Deborah Lifshey, a Managing Director in the New York office, specializes in advising clients on compensation matters from a legal perspective, including securities disclosure, taxation and corporate governance issues, as well as contract negotiation and reasonableness opinion letters.

- Methodologies and Research
- “Proxies that Make the Grade” Survey Results -- What the “Players” said
- Study Results – The “Early 50 Filers”
- Comment Letters and Responses
- Closing Remarks

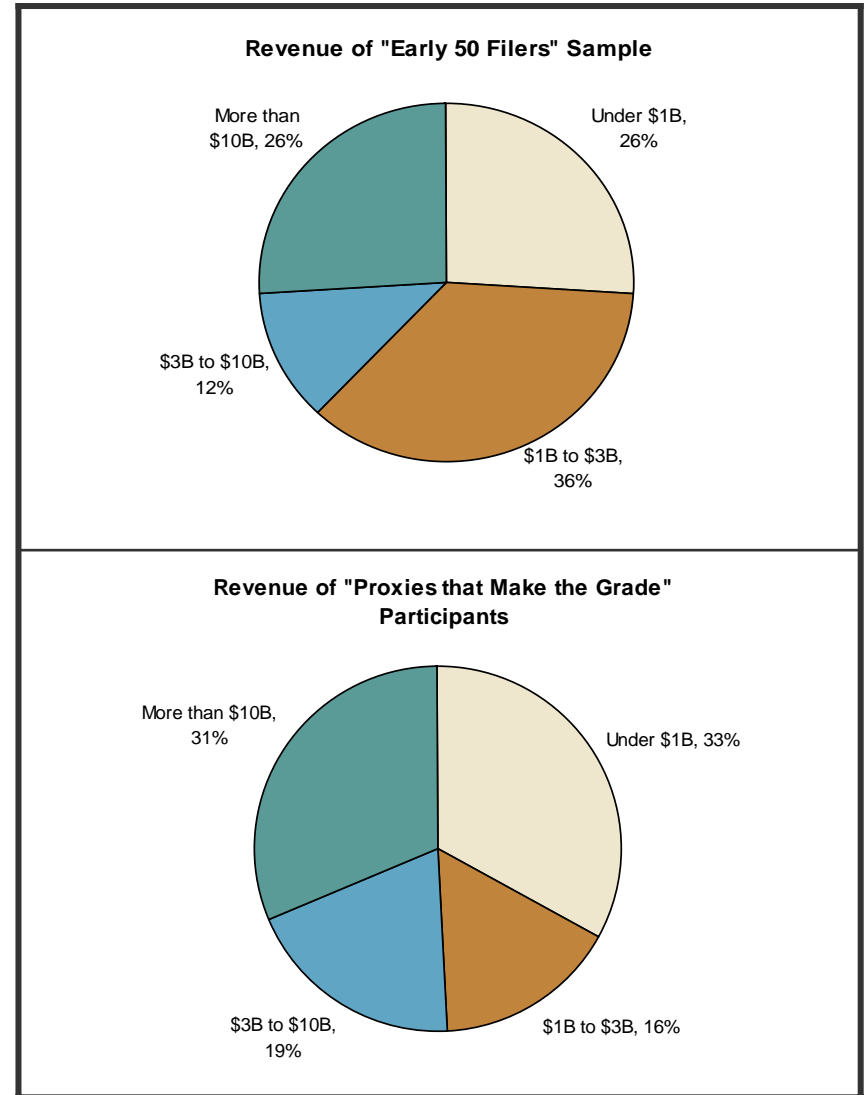
## The “Early 50 Filers” Study

- Reviewed 2008 proxies of 50 companies that are in their second year of filing under expanded SEC disclosure rules
- Compared each firm’s 2008 and 2007 CD&As
- Cross-industry sample

**And**

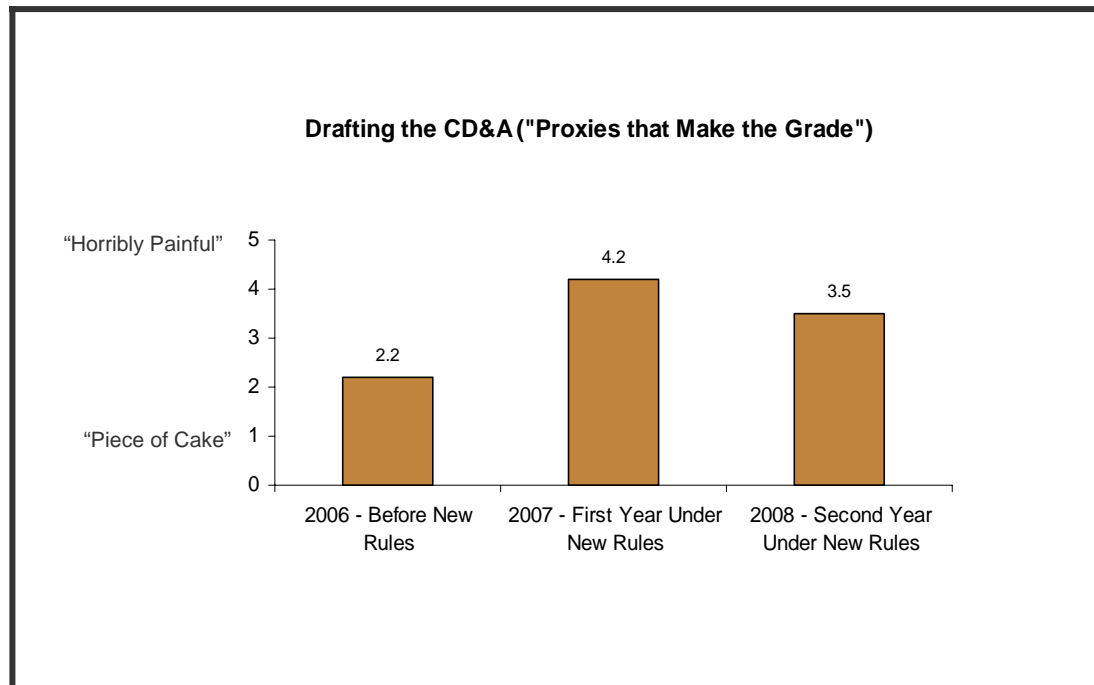
## “Proxies that Make the Grade” Study

- Second annual survey of companies’ views on pay disclosures
- Includes questions about their own firm’s 2008 CD&A and views on the new rules
- 124 participants
- Cross-industry sample



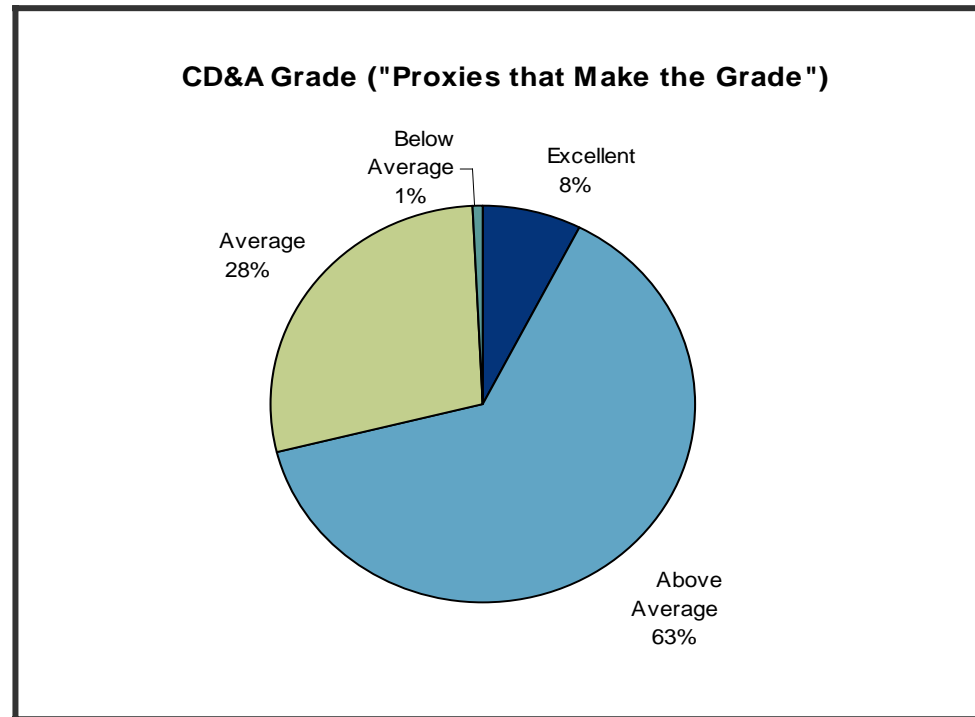
## How Painful Was This Year's CD&A Process?

- Asked to rank the entire CD&A process on a scale of 1 to 5 (1 being “a piece of cake” and 5 being “horribly painful”), respondents gave a combined average rating of 3.5 – slightly easier than the 4.2 rating given in 2007



## How did Firms Grade their CD&A?

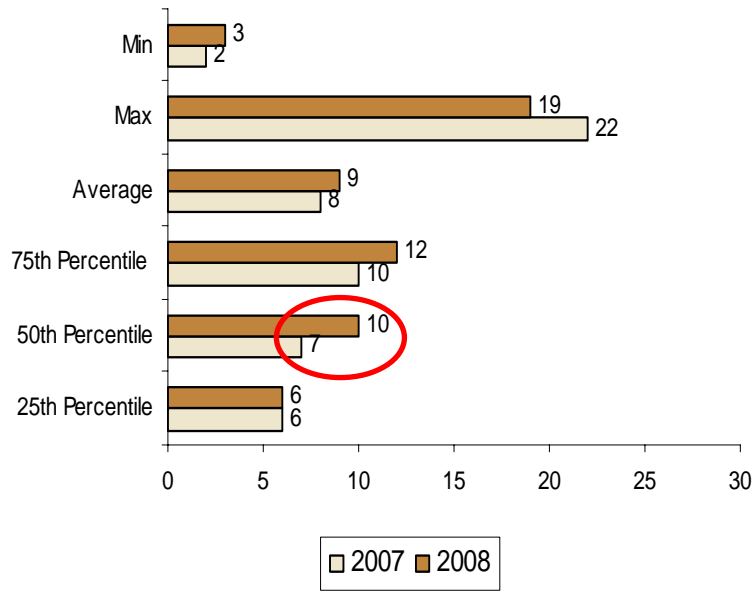
- A majority of participants (63.6%) gave their own company's CD&A a grade of "Above Average," while only 7.6% awarded themselves an "Excellent" rating



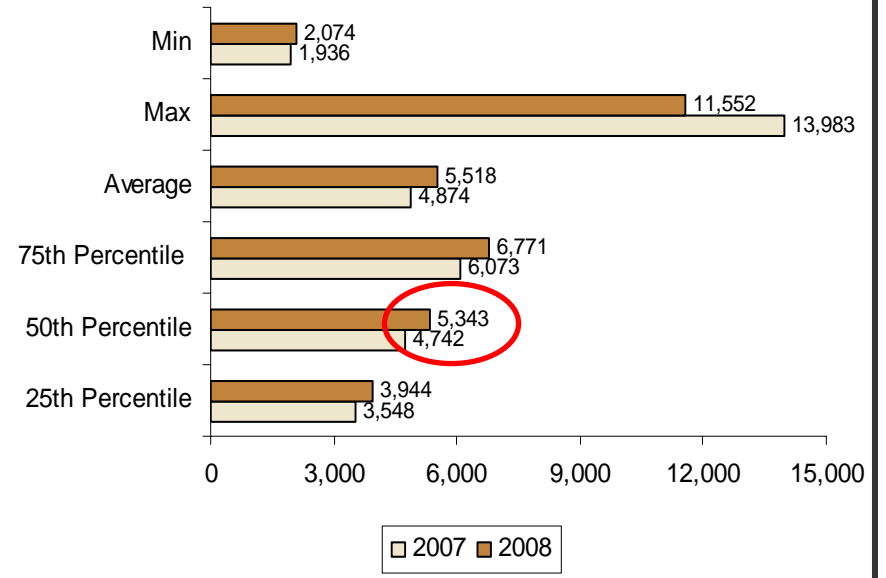
# How Long was the CD&A?

- CD&As in 2008 were longer and more wordy...

### # of Pages in CD&A "Early 50 Filers"

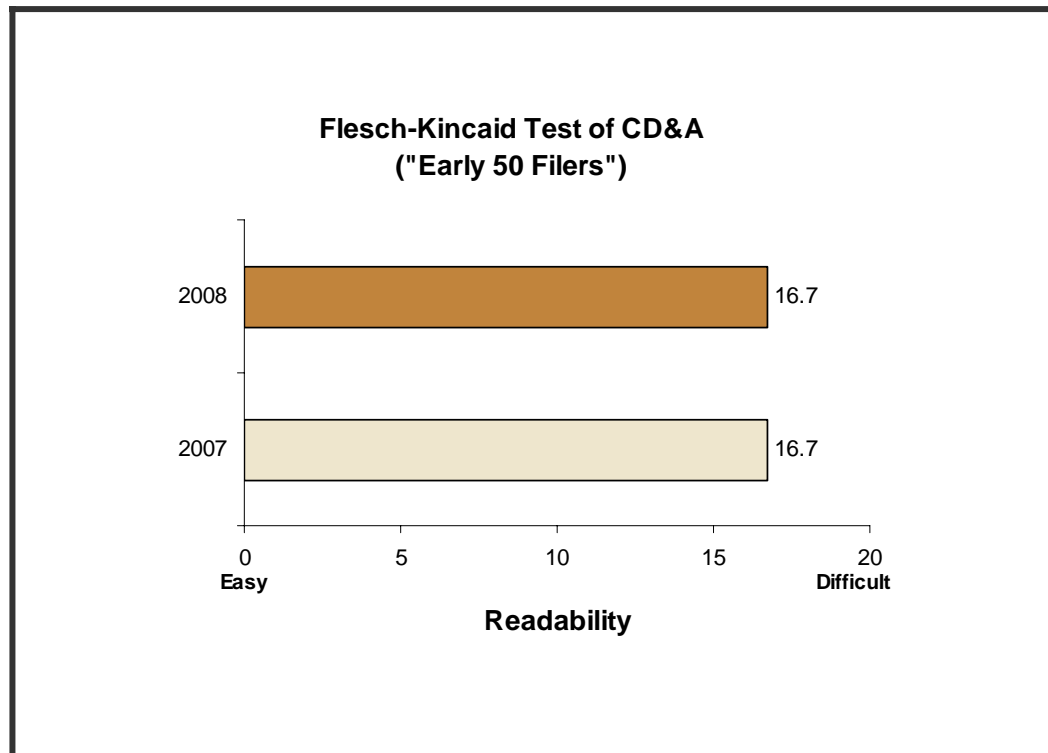


### # of Words in CD&A "Early 50 Filers"



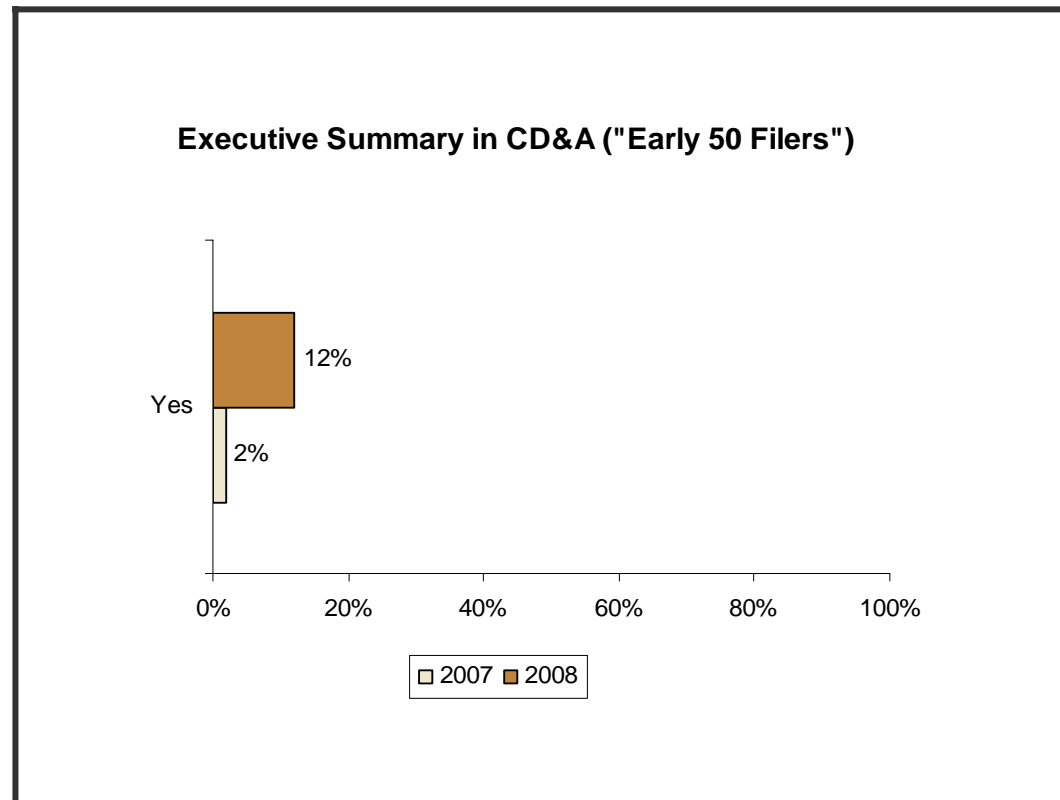
## Were CD&A's Written in "Plain English"?

- ...and not any easier to read than a year earlier



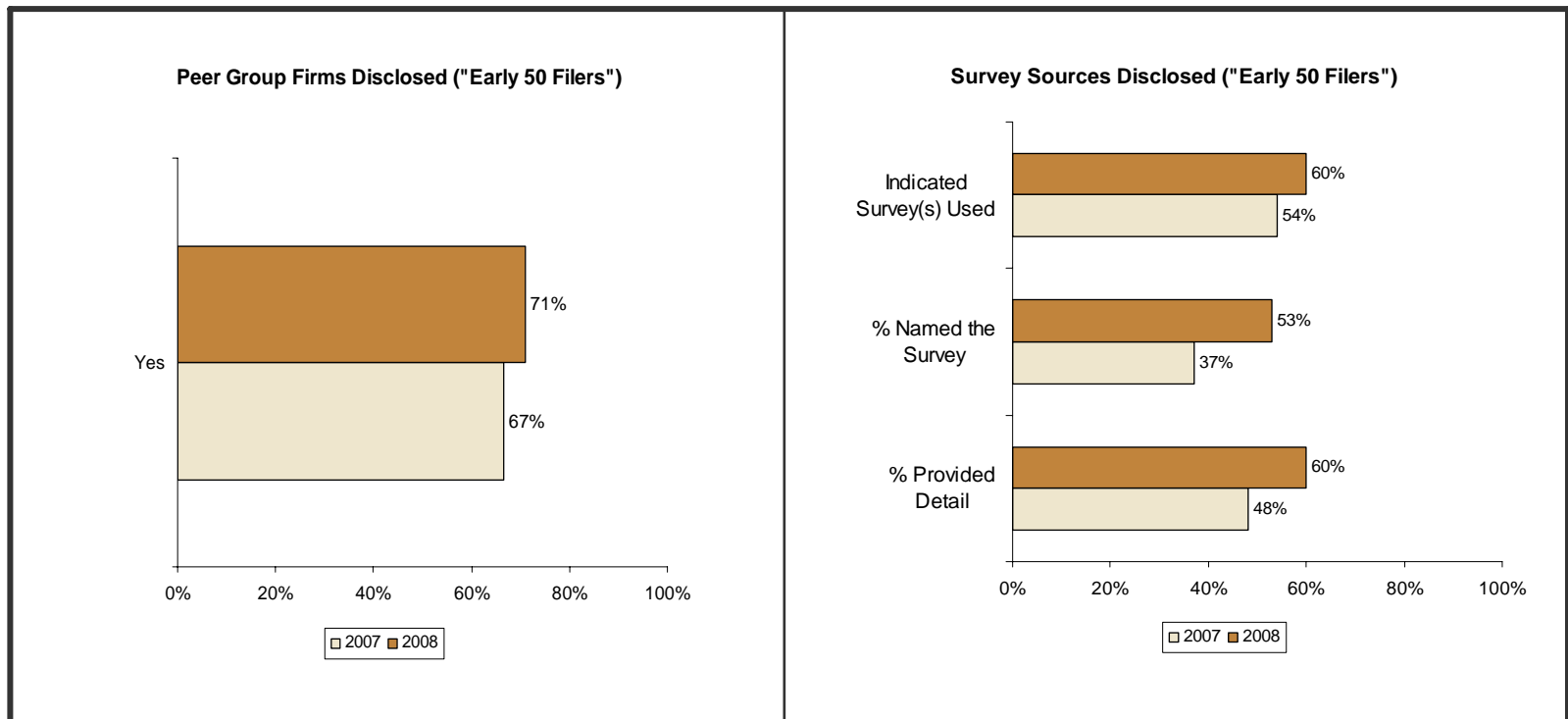
## Have Steps Been Taken to Help Understand the CD&A?

- While significantly more companies provided an executive summary of the CD&A in 2008, the vast majority did not



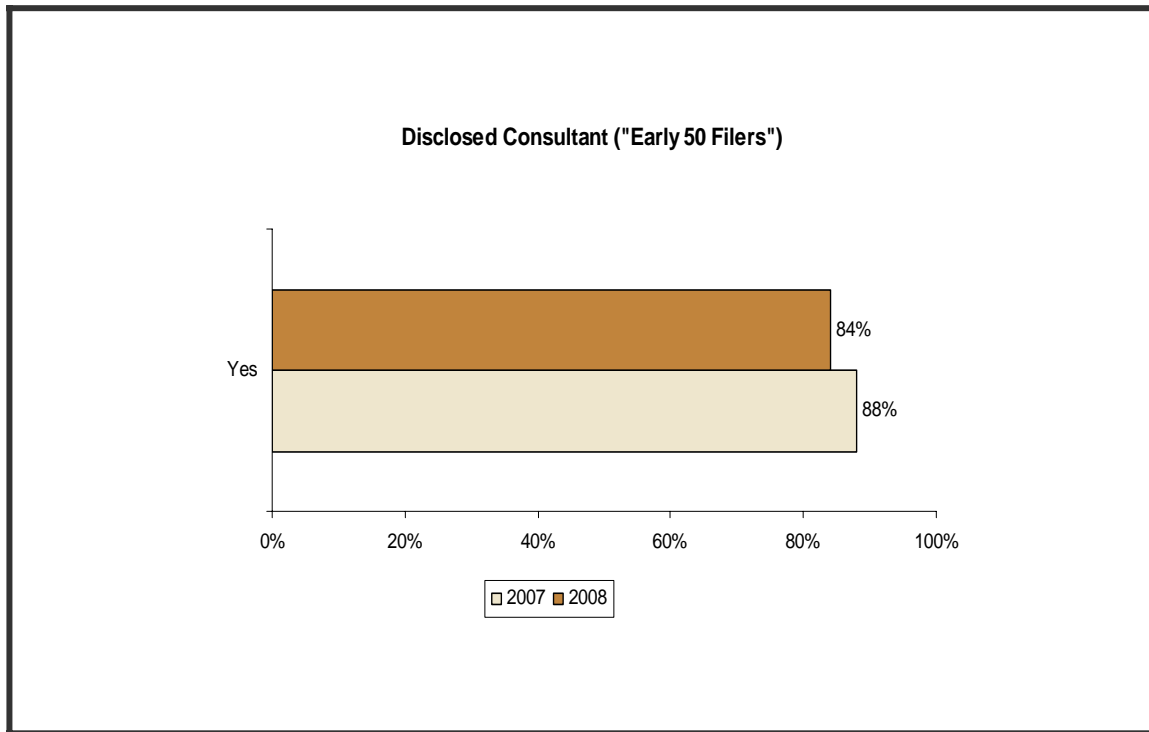
# Were Peer Group Firms and Survey Information Disclosed?

- More companies provided details about peer group use and survey sources



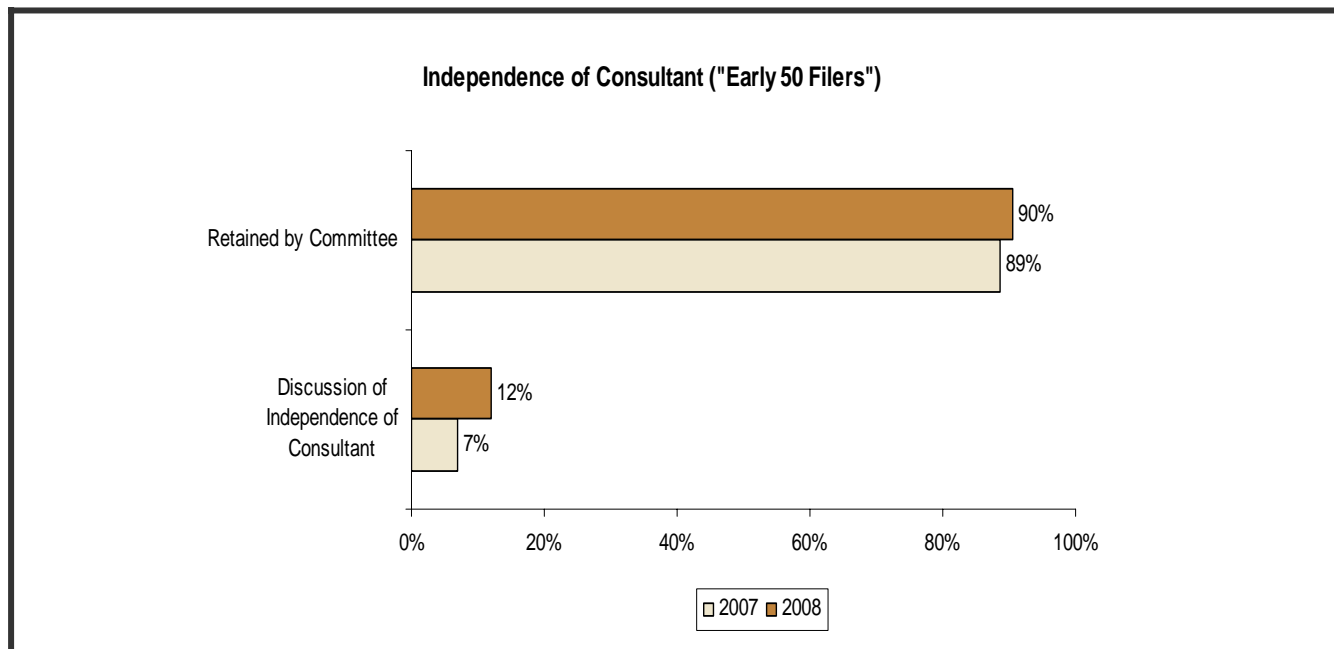
## Who is using a Consultant?

- Information about the use of consultants was similar to a year earlier



## Was the Independence of the Consultant Disclosed?

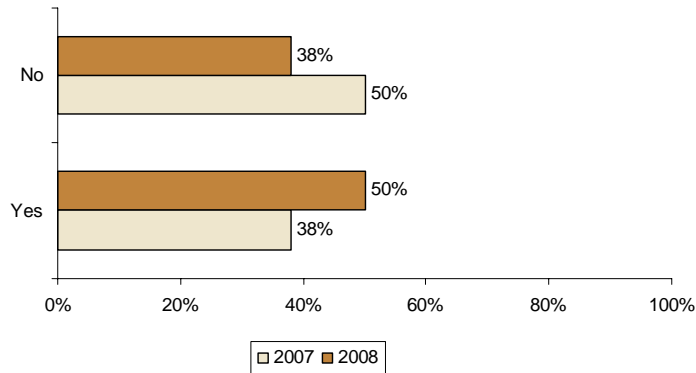
- Many companies in both years accompanied disclosure of consultant use with a discussion of whether the firm was working exclusively for the committee
- Slightly more firms discussed the independence of their consulting firm



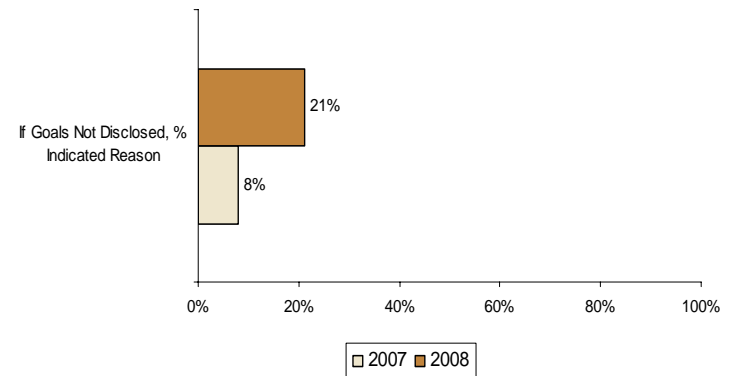
# Were Specific Corporate Performance Goals and Targets Disclosed?

- There was significantly more disclosure of specific corporate goals and targets in 2008
- Firms that did not disclose specific corporate goals were more likely to explain why

Disclosed Specific Corporate Goals ("Early 50 Filers")

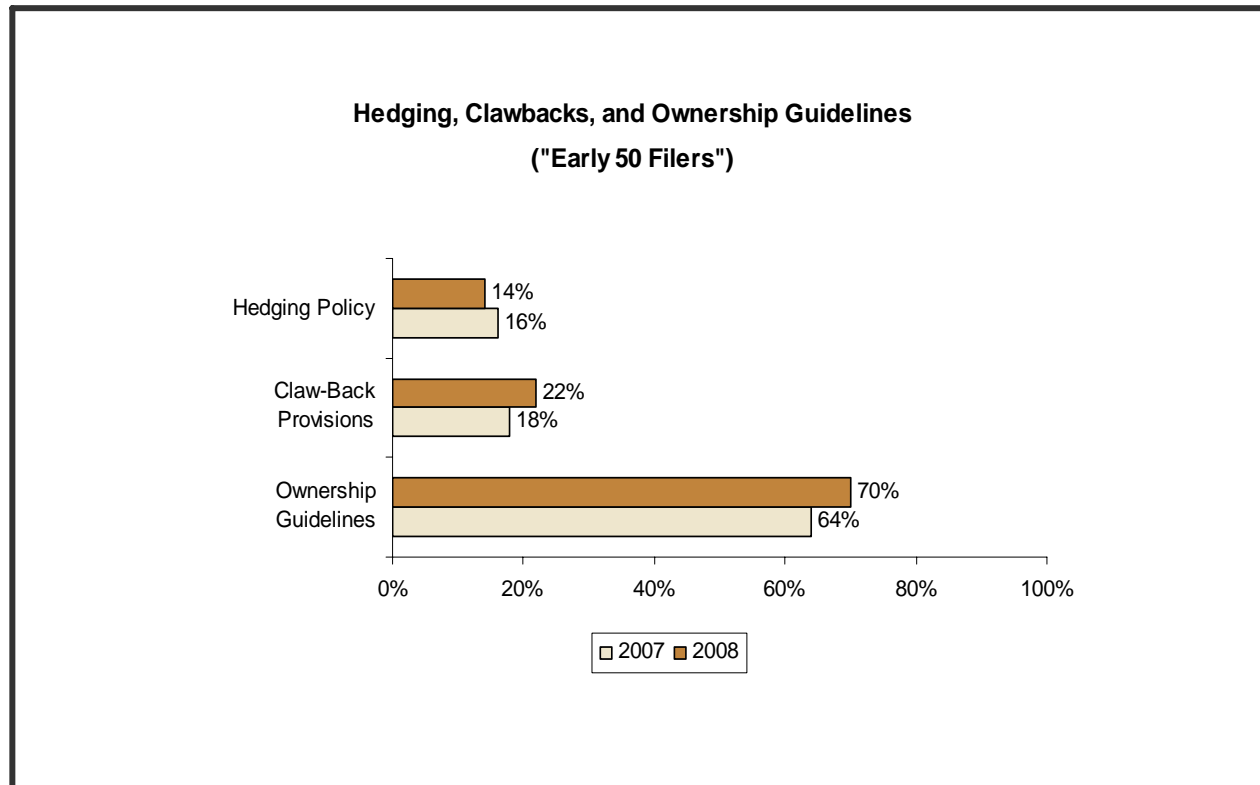


Provided Reason Why Corporate Goals Not Disclosed ("Early 50 Filers")



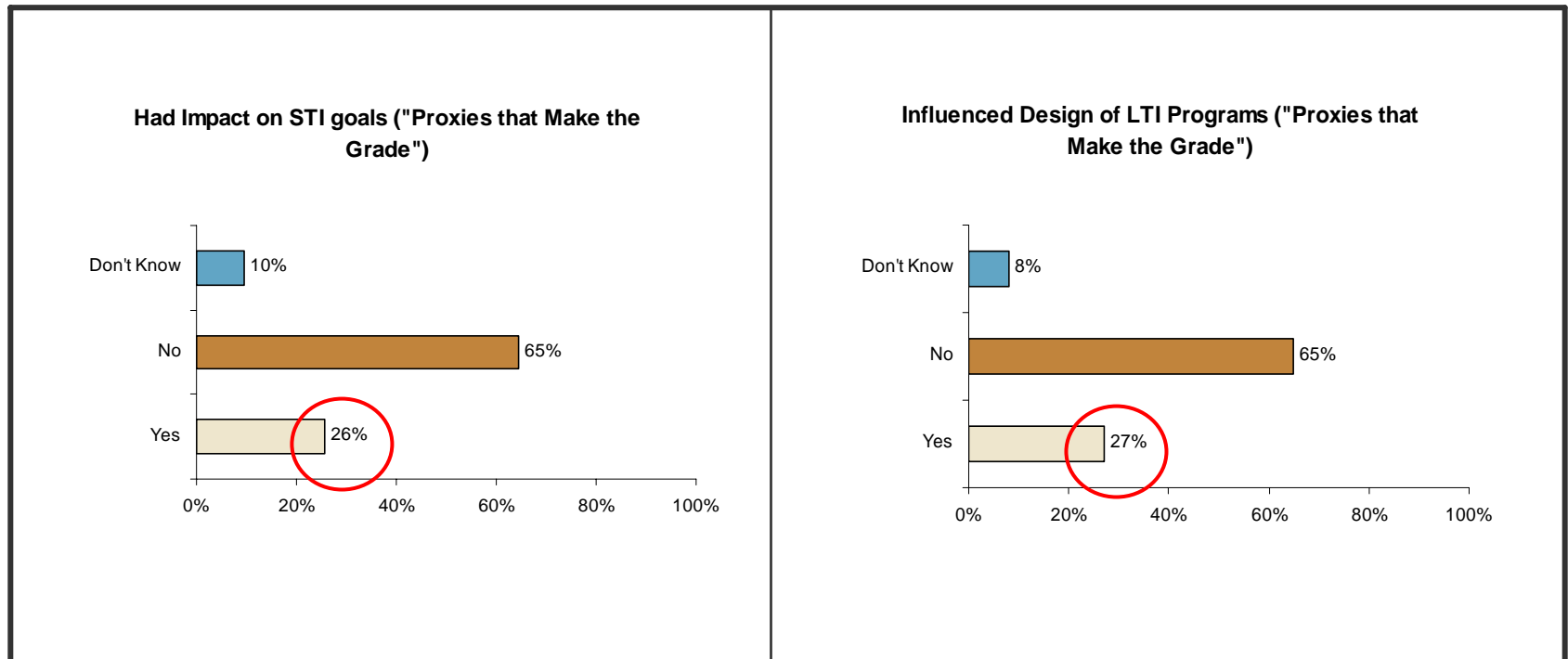
# Are the New SEC Disclosure Having an Impact on the Disclosure of “Favorable” Corporate Governance Practices?

- There was a slight increase in disclosure of claw-back provisions and ownership guidelines



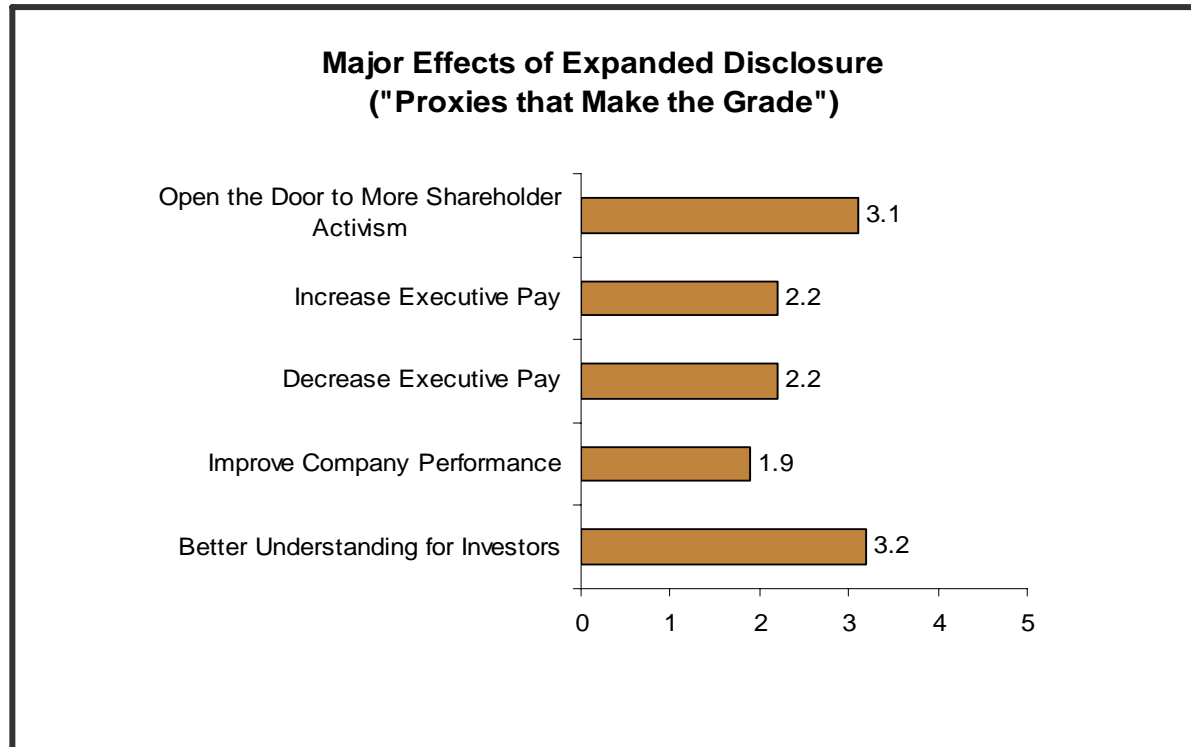
# Are SEC Disclosure Impacting STI Goals and LTI Design?

- About one-quarter of participants said the SEC disclosure rules influenced how individual/corporate performance goals were set, with about an equal number saying the rules affected the design of long-term incentives



## What are Other Potential Effects of the Expanded Disclosure?

- Asked to assess possible effects of expanded disclosure on a scale of 1 to 5 (with 1 having the least effect and 5 having the greatest effect), respondents rated “Better Understanding for Investors” the highest

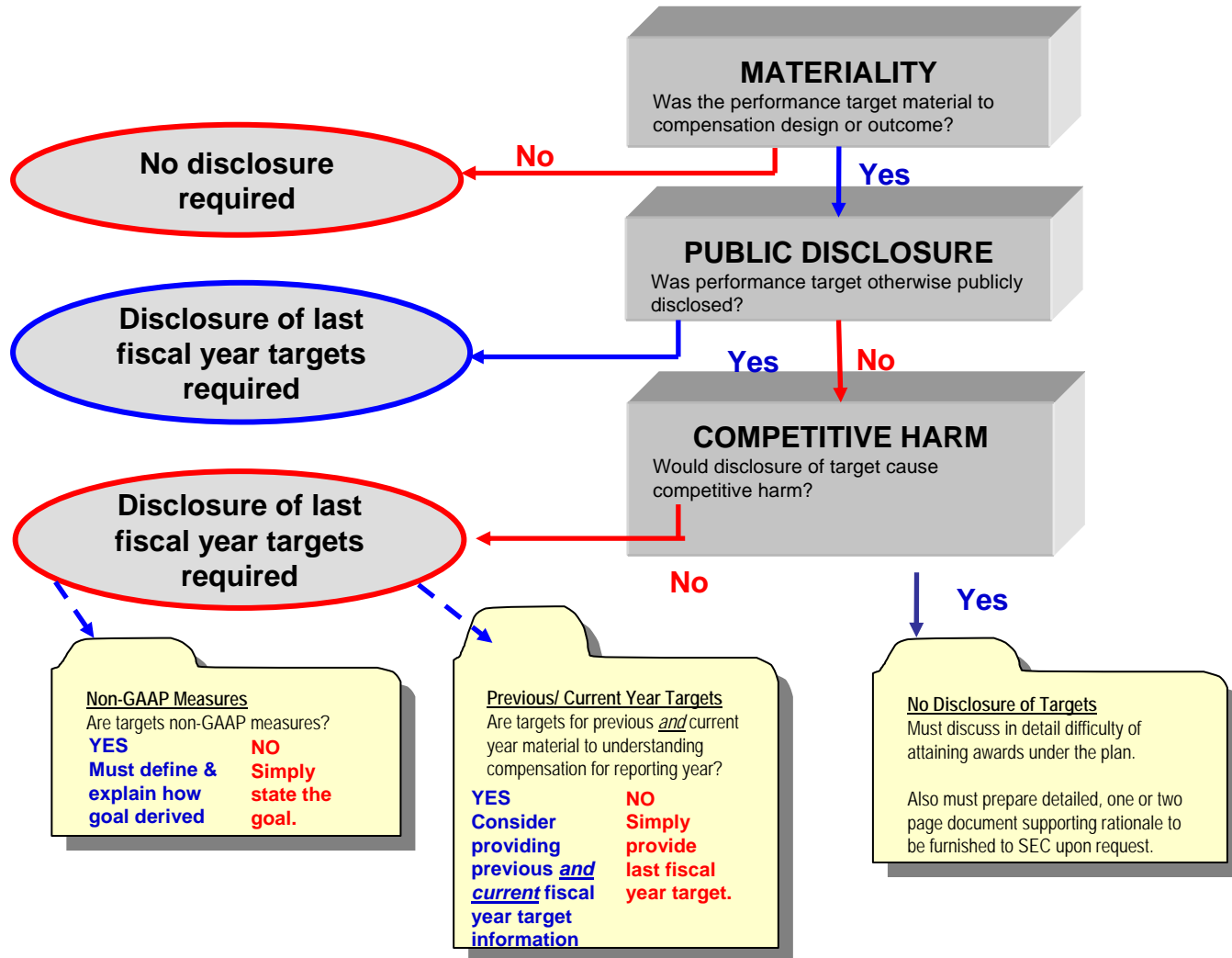




## Comment Letters – Overview

- Approximately 350 sent
- Letters were posted ad hoc 45 days after “all clear” letter was received
- Hot topics: performance targets and benchmarking
- Treasure hunt to find the comment letters
- Averaged 8-15 questions each
- Very repetitive
- Most companies responded that they will comply in future
- Majority of initial responses required a follow-up
  - Ironically, follow-up requested mostly from companies that volunteered additional info

# The Great Performance Target Decision Tree





## Comment Letters – What we Learned about Performance Target Disclosure

- Operational vs. Financial Targets
- Retroactive vs. Prospective Targets
- Current Performance Targets
- Competitive Harm
  - Get the line people involved
  - Nexus argument is critical
- Degree of Difficulty Argument
  - Philosophy
  - History
  - Avoid boilerplate

## **The questions:**

- Exactly what is included in individual performance?
- What were the corporate and business unit goals?
- How difficult were the performance goals for executives to achieve?
  - What is the meaning of “stretch” goal?
- What are executives’ targets for the current year?

## **Examples:**

### ***Valley National Bancorp***

- SEC asked for quantitative details regarding performance targets and measures
- Comment letter response: Company response provided extensive details for individual and corporate-wide performance targets
- 2008 Proxy: Continued excellent and specific disclosure about financial and individual performance goals

### ***Public Service Enterprise Group***

- SEC asked for prospective financial, operational and strategic targets
- Comment letter response: Company will disclose prospective targets to the extent they are material to understanding prior year or to the CD&A
- 2008 Proxy: Disclosed new measures for CEO, but stated that it would not discuss measures for other NEOs because the structure of their arrangements had not changed from 2007



## Comment Letters – What we Learned about Benchmarking

- Companies must identify the benchmark and the component companies
- If the list is extensive, companies can use an appendix
- Focus should be on materiality
  - Peer Groups
  - Surveys

## The questions:

- What companies were in the peer group?
- What companies were in the survey?
- At what percentage was total pay, and each element, targeted?
- At what percentage did company fall relative to peers in terms of performance?
- What were specifics of the compensation practice and benchmark use?

## Examples:

### ***Electronic Data Systems Corp.***

- SEC asked which companies were used to benchmark pay in 2007 – proxy referred only to two peer groups
- Comment letter response: We will comply in future filings
- 2008 proxy: Listed all companies in the two peer groups, plus companies in a new peer group to be used in this year's pay decisions

### ***SunTrust Banks, Inc.***

- SEC asked for further explanation about how banking industry data as a whole influenced compensation – 2007 proxy stated only that it “considered” industry data
- Comment letter response: Surveys are used to validate peer group data; provided the number of companies underlying the survey as well as the survey scope. It did not disclose the companies in the survey
- 2008 Proxy: Reiterated that survey data is used to validate and sometimes supplement specific position matches, but did not name specific surveys or companies that participated in the surveys.



## Comment Letters – Role of Compensation Consultant

### **The questions:**

- What are the specifics of the compensation process and the roles of executives and consultants?
- What role is defined for the compensation consultant?
- How did the committee use the data provided by the consultant?
- If multiple consultants were used, what was each consultant's role?

### **Example:**

#### *Electronic Data Systems Corp.*

- SEC asked for more information about the scope of engagements with two consulting firms, in addition to more disclosure regarding multiple business arrangements
- Comment letter response: We will comply in the future
- 2008 Proxy: Stated the first consultant was retained by the committee for periodic review of compensation and specific recommendations for two NEOs, and that the consultant also provided non-executive compensation services. Indicated that the company would discontinue the non-executive compensation consulting services to avoid conflict. Indicated that the second firm was retained by management to provide broad-based employee services and provide survey data for executives



# Comment Letters – Executive Employment Agreements

## **The questions:**

- Why does the company maintain these agreements?
- Why is one executive's benefit greater than the others?
- How were terms negotiated in the employment agreements?
- Define the triggering events?

## **Example:**

*Electronic Data Systems Corp.*

- SEC asked for elaboration of rationale behind employment agreement severance payouts
- Comment letter response: We will comply in the future
- 2008 Proxy: Company states that agreements help with retention of needed executive officers during unforeseen events when the executive's future is uncertain. Company finds it beneficial for agreements to specify the exact terms and benefits an executive would receive and periodically benchmarks all elements of payouts



## Closing Remarks

- 2007 vs. 2008
- Problematic areas
- What to expect in 2009
- Unintended consequences



# Complimentary NACD Compensation Series Webcast

**April 23, 2008 - 2:00 pm ET**

## **Design by Disclosure: The Unintended Consequences of SEC Proxy Rules**

Experts from the National Association of Corporate Directors and compensation consultancy Pearl Meyer & Partners will discuss how Boards' concerns over how programs will be perceived by investors are driving major changes in program designs - sometimes in ways that can undermine their effectiveness and transparency. Guidance will be provided on reconciling meaningful performance-based practices with more detailed disclosure of sensitive and complex pay programs, including design alternatives that do not sacrifice good design for good optics.

### **Presenters**

**Mark J. Rosen, Managing Director, Pearl Meyer & Partners, Charlotte**  
**Ronnie LaBorde, Lead Director, Amedisys, Inc.**

**More information and registration at [www.nacdonline.org](http://www.nacdonline.org)**