

For audio participation, dial 866.256.9239 and follow the prompt. If assistance is needed please ask to be connected to Foley's NDI Web Conference.

2012 Proxy Season Preview

December 8, 2011

NATIONAL DIRECTORS INSTITUTE | NDI Checkpoint

FOLEY
FOLEY & LARDNER LLP

CO-SPONSORS
AON

D. F. King

EVERSHEDS

F. T. I.
CONSULTING

Deloitte.

IN-KIND SPONSORS

Boardroom Bound
Helping Corporate Boards Overlook & Thrive

inFORUM
BOARDACCESS

NASDAQ OMX

©2011 Foley & Lardner LLP

2

NATIONAL DIRECTORS INSTITUTE | NDI Checkpoint

Today's Presenters



■ **John K. Wilson**
Partner
Foley & Lardner LLP



■ **Carolyn T. (Carrie) Long**
Partner
Foley & Lardner LLP



■ **Joshua A. Agen**
Associate
Foley & Lardner LLP



■ **Richard H. Grubaugh**
Senior Vice President
D.F. King & Co., Inc.

©2011 Foley & Lardner LLP

Housekeeping

- Call **866.493.2825** for technology assistance
- Dial ***0** (star/zero) for audio assistance
- Questions can be entered via the Q&A tab located on your menu bar at the top of your screen. We will address questions at the end of the program.
- We encourage you to maximize the PowerPoint to full screen usage:
 - Hit F5 on your keyboard; or
 - Select "View" from the toolbar menu and click "Full Screen"
- To print a copy of this presentation:
 - Click on the printer icon in the lower right-hand corner
 - Convert the presentation to PDF and print as usual
- Foley will apply for CLE credit after the Web conference. If you did not supply your CLE information upon registration, please e-mail it to eharris@foley.com

Today's Topics

- Status of Dodd-Frank Rules Applicable to Proxy Statements
- Say on Pay: Lessons Learned and Best Practices
- Shareholder Proposals

Status of Dodd-Frank Rules Applicable to Proxy Statements

New Rules Applicable for 2012 Proxy Season

- New say on pay disclosure in CD&A
 - Whether and, if so, how the company considered the results of the most recent say on pay vote in determining compensation policies and decisions
 - If so, how that consideration affected the company's executive compensation decisions and policies
- No other new SEC disclosure requirements

Rules to Be Adopted in December 2011

- SEC proposed rules on March 30, 2011
 - Exchanges to adopt listing standards regarding independence of compensation committee members
 - Consider updating D&O questionnaires to take into account proposed independence standard
 - Exchanges will still need to propose and adopt standards after SEC final rules adopted
 - Exchanges to adopt listing standards regarding compensation committee authority to engage compensation consultants, independent legal counsel and other advisers, and funding for and independence of such advisers
 - Exchanges will still need to propose and adopt standards after SEC final rules adopted

©2011 Foley & Lardner LLP

Rules to Be Adopted in December 2011

- Additional disclosure in proxy statements regarding whether a compensation consultant has been retained, the terms of the engagement, and conflicts of interest related to compensation consultants
 - Dodd-Frank required for annual meetings on and after July 21, 2011 – SEC has stated not required until final rules adopted
 - Open question as to whether will become effective at same time as exchange listing standards

©2011 Foley & Lardner LLP

Rules to Be Adopted by June 2012

- Compensation clawback policies
 - Exchanges to adopt listing standards to require companies to adopt a policy that, if a company is required to prepare an accounting restatement due to material noncompliance with any financial reporting requirement under the federal securities laws, it must recover incentive-based compensation paid to any executive officer on the basis of erroneous data
 - Although not yet required, many companies are adopting policies proactively to support their say on pay vote

Rules to Be Adopted by June 2012

- Proxy statement disclosures
 - Relationships between executive compensation and financial performance of the company
 - Ratio of median employee total compensation vs. CEO total compensation
 - Whether employees and directors may purchase financial instruments designed to hedge or offset decreases in market value of equity compensation awards

Say on Pay: Lessons Learned and Best Practices

2011 Proxy Season Say on Pay Results

- The vast majority of companies received majority shareholder support for their “say on pay” votes
- For the frequency of future “say on pay” votes, shareholders favored annual say on pay votes
- Withhold vote campaigns against compensation committee members decreased in 2011 compared to 2010
- There was a correlation between failed “say on pay” votes and negative vote recommendations from proxy advisory services
 - Several companies issued supplemental proxy materials in response to negative recommendations; some made substantive changes

2011 Proxy Season Say on Pay Results

- Leading factors contributing to failed “say on pay” votes in 2011 included:
 - A perceived disconnect between pay and performance
 - For example, poor stock price performance combined with increasing pay or mediocre stock price performance combined with extraordinary pay increases
 - The presence of disfavored pay practices
- “Say on golden parachute” votes relatively rare
- Advent of shareholder “say on pay” litigation

©2011 Foley & Lardner LLP

Lessons from Say on Pay in 2011 – Tactics

- Be familiar with your significant shareholders, their voting policies and how they evaluate pay and performance
- Communicate specifically with the governance/voting personnel at your significant shareholders
 - At many institutional investors, the investment and governance/voting functions are divided
 - The mere fact that investment personnel are pleased with your financial performance does not ensure a “yes” vote on governance matters such as “say on pay”
- Communicate with significant shareholders about say on pay well in advance of proxy season
 - It becomes increasingly difficult to reserve time for calls or meetings once proxy season activities commence

©2011 Foley & Lardner LLP

Lessons from Say on Pay in 2011 – Disclosure

- Most important: demonstrating pay for performance
- What is meant by “pay for performance?”
 - How to measure pay?
 - “Real” or “realizable” pay versus Summary Compensation Table
 - Relative – selection of peers
 - How to measure performance?
 - Total shareholder return
 - Financial measures used for incentive compensation
 - Other measures
 - Relative – selection of peers

Lessons from Say on Pay in 2011 – Disclosure

- Demonstrating pay for performance (continued)
 - Use of charts or other graphics
 - Location in proxy statement
 - Establishing workable precedent
 - SEC requirements:
 - GAAP presentation or reconciliation (including Reg G and Item 10(e) if required)
 - Not materially misleading (balance)
 - Effect of future Dodd-Frank mandated pay for performance disclosure

Lessons from Say on Pay in 2011 – Disclosure

- Other disclosure takeaways
 - Transparent disclosure can diminish the role of proxy advisors by enhancing direct communications with shareholders
 - Executive summary
 - Streamline
 - Plain English
 - Sequence should reflect priority of information
- Process considerations
 - Start early
 - Analyze vote from first year
 - Which shareholders voted “no” and why
 - Proxy solicitor analysis

Lessons from Say on Pay in 2011 – Disclosure

- SEC Compliance
 - Even as a “sales” document, the CD&A must cover the SEC’s required elements
 - The SEC staff continues to review CD&A disclosures and issue comment letters
 - In 2012, the required elements will include a discussion of the effect of the most recent say on pay result
- Litigation Defense – Be specific about what is meant by “pay for performance” so that it is demonstrably accurate

Institutional Shareholder Services (ISS) Update

- ISS published its 2012 voting policy updates in November
- ISS's new approach to its pay for performance analysis will involve an initial, quantitative "screen" that will consider:
 - "Peer group alignment," consisting of
 - The degree of alignment between the company's total shareholder return rank and the CEO's total pay rank within a peer group, as measured over one- and three-year periods (with the one-year period weighted 40% and the three-year period weighted 60%)
 - The multiple of the CEO's total pay relative to the peer group median
 - "Absolute alignment" between the trend in CEO pay and company total shareholder return over the prior five fiscal years
- Companies that do not pass this initial screen will be evaluated in a second, qualitative analysis before ISS recommends an "against" vote in say on pay

©2011 Foley & Lardner LLP

ISS Update (Continued)

- ISS will recommend "against" or "withhold" votes in the case of boards that adopt a say on pay frequency less frequent than the alternative supported by a majority of shareholders
 - If no say on pay frequency achieved a majority and the company elects a lesser frequency than received a plurality, ISS will recommend on a case by case basis
- ISS will generally recommend "against" or "withhold" votes in the case of compensation committees (or full boards in exceptional cases) failing to take adequately responsive measures after a say on pay vote receiving the support of less than 70% votes cast
 - ISS wants companies receiving less than 70% support for say on pay to determine responsive changes through engagement with shareholders, and to disclose the changes early on a voluntary basis

©2011 Foley & Lardner LLP

Say on Pay Shareholder Litigation

- 2011 saw a number of shareholder lawsuits based in part on significant “no” votes in say on pay
- Two notable examples:
 - Cincinnati Bell
 - Alleged breaches of fiduciary duty of loyalty by the board and officers, aiding and abetting by the consultants and unjust enrichment of named executive officers (NEOs)
 - Federal district court applying Ohio law denied defendants’ motion to dismiss
 - Beazer Homes
 - Alleged breaches of fiduciary duty by directors, aiding and abetting and breach of contract by consultants and unjust enrichment of NEOs
 - State (Georgia) court applying Delaware law dismissed the suit against all defendants

©2011 Foley & Lardner LLP

Disclosure in View of Say on Pay Litigation

- Artful disclosure will not prevent a lawsuit in the event of a failed say on pay vote, but may increase chances of success
- Some suggestions:
 - Do not rely on unsupported statements that “we pay for performance”
 - Rather, tie specific pay elements to specific measures of performance and analyze why the measures were selected for the pay element
 - Identify and analyze non-performance elements of pay as such
 - Review the CD&A from the perspective of a potential plaintiff

©2011 Foley & Lardner LLP

Shareholder Proposals

SEC Staff Legal Bulletin

- SEC staff issued staff legal bulletin on October 18, 2011 with changes to handling of no-action requests for shareholder proposals
 - Revised proof of ownership requirements to verify whether a beneficial owners is eligible to submit a proposal
 - Common errors in submitting proof of ownership
 - Clarifications on submission of revised proposals
 - Procedures for withdrawing no-action requests for proposals submitted by multiple shareholders
 - Use of email to transmit no-action responses

Proxy Access – Private Ordering

- In July 2011, U.S. Court of Appeals overturned SEC mandatory proxy access rule, which would have required companies to include shareholder nominees in company proxy materials in certain circumstances
- SEC did not challenge court ruling, but amendments to Rule 14a-8 became effective in September 2011 that permit proxy access “private ordering”
 - Rule 14a-8(i)(8) no longer permits companies to exclude from their proxy materials shareholder proposals to amend governing documents to specify procedures by which shareholder nominees may include director nominees in the company’s proxy materials
- Shareholder proposals for 2012 meetings seeking proxy access on company-by-company basis

Proxy Access – Private Ordering

- Binding vs. precatory proposals
- Follow SEC rule thresholds (3% for 3 years) vs. lower thresholds (e.g., 1% for 1 year)
- Strategies if receive proxy access proposal
- ISS – vote case-by-case on proxy access proposals
 - Company-specific factors
 - Proposal-specific factors, including ownership thresholds, maximum proportion of directors shareholders may nominate and method of determining which nominations should appear on the ballot

Anti-Takeover Defenses

- Eliminate classified Board
 - Proposals receive very high levels of support
 - Ability to negotiate timing of declassification
- Ability to act by written consent
 - New and increasing interest in this subject receiving high levels of support
- Ability to call special meeting
 - Proposals at 15% threshold garnering more support
- Eliminate supermajority voting provisions

Other Governance Proposals

- Majority voting
 - Most common proposal for 2011 meetings
 - While most S&P 500 companies have adopted in some form, most mid and small cap companies have not
- Independent Board Chairman
- Officer succession planning
- Exclusive Venue

Political Contributions

- Heightened attention after U.S. Supreme Court *Citizens United* decision in 2010
- Second most common proposal submitted for 2011 meetings
- Proposals request reports on corporate political spending and policies, including spending through trade associations
- 2012 election year likely to increase interest

Environmental and Social Proposals

- Environmental issues
- Issue sustainability report
- Adopt sexual orientation anti-bias policy
- Health and safety Issues

Key Takeaways

Questions & Answers

Contact Information

- **John K. Wilson**
Foley & Lardner LLP
414.297.5642
jkwilson@foley.com
- **Carolyn T. (Carrie) Long**
Foley & Lardner LLP
619.685.4635
ctlong@foley.com
- **Joshua A. Agen**
Foley & Lardner LLP
414.297.5535
jagen@foley.com
- **Richard H. Grubaugh**
D.F. King & Co., Inc.
212.493.6950
RGRUBAUGH@dfking.com

Mark Your Calendar

- **2012 NDI Checkpoint Sessions**
 - February 22, 2012
 - May 23, 2012
 - August 22, 2012
 - December 5, 2012
- **Save the Date! NDI Executive Exchange**
 - November 15, 2012 – Chicago, IL – Invitation-only

Thank You

- A copy of the PowerPoint presentation and a multimedia recording will be available on our Web site within 2-3 days:

http://www.foley.com/news/event_detail.aspx?eventid=3595

- We welcome your feedback. Please take a few moments before you leave the Web conference today to provide us with your feedback:

<http://www.zoomerang.com/Survey/WEB22E4JJEQMS5>