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## 2014 Proxy Season Wrap-Up

June 25, 2014

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## Today's Presenters

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## Management Say on Pay in 2014

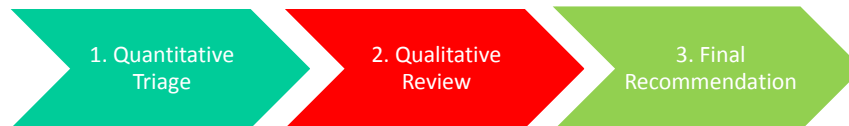
- Highest number of companies are having say on pay votes in 2014 since the advent of the rules
  - “Triennial” say on pay companies having their second say on pay votes
  - Smaller reporting companies having their second votes, depending on frequency
- ISS voting policy change for 2014
  - Changes were introduced to the calculation of the first peer group alignment measure, the relative degree of alignment (RDA), from a 40/60 weighted average of 1- and 3-year RDA measures to a single, annualized RDA measure for the 3-year measurement period (or shorter period if pay and performance data are not available for all three years)

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## Background information: ISS’ high-level Management Say on Pay process



Three formulaic screens are used to identify companies that may have Pay-for-Performance problems

Tests include:

- RDA (Relative Degree of Alignment): Tests relative pay-for-performance alignment versus peers over three years
- MOM (Multiple of Median): Absolute size of pay package relative to peers
- PTA (Pay-TSR Alignment): Trend of pay changes relative to shareholder value creation trend over five years

All companies are subjected to a qualitative review, with the initial depth set by the quantitative tests

Qualitative review includes:

- Response to last year’s MSoP
- Peer selection & benchmarking
- STI / LTI program design
- Rationale behind compensation actions taken
- Realized / Realizable Pay
- Equity pay mix
- Leadership changes
- Absolute pay levels

Based on a combination of the quantitative and qualitative review results, a final recommendation is made

Final decision based on factors including:

- Explanation of pay package
- Company-specific circumstances
- Shareholder engagement
- Performance orientation of pay package
- Rationale for performance metrics
- Rigor of performance goals

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## The Dangerous Seven: The most common reasons for negative recommendations

**ISS' most commonly cited reasons for voting against Say-on-Pay Proposals**

- Significant time-vesting equity awards
- Problematic pay benchmarking practices
- Significant discretionary grants or payments
- Lack of rigor on incentive targets
- Performance criteria duplicated in STI and LTI
- Guaranteed multi-year awards
- Excessive perquisites

**The key to overcoming these issues is effectively explaining the reasoning to shareholders in your CD&A**

These factors are likely beyond the control of the person responsible for drafting the CD&A – but, in most cases, they should be addressed

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## In 2014, ISS expanded its Realizable Pay evaluations to the full S&P 1500

Realizable Pay focuses on the value of compensation in the middle of the compensation lifecycle – after the compensation is granted, but before it's realized

**Improvements Over Granted and Target Pay**

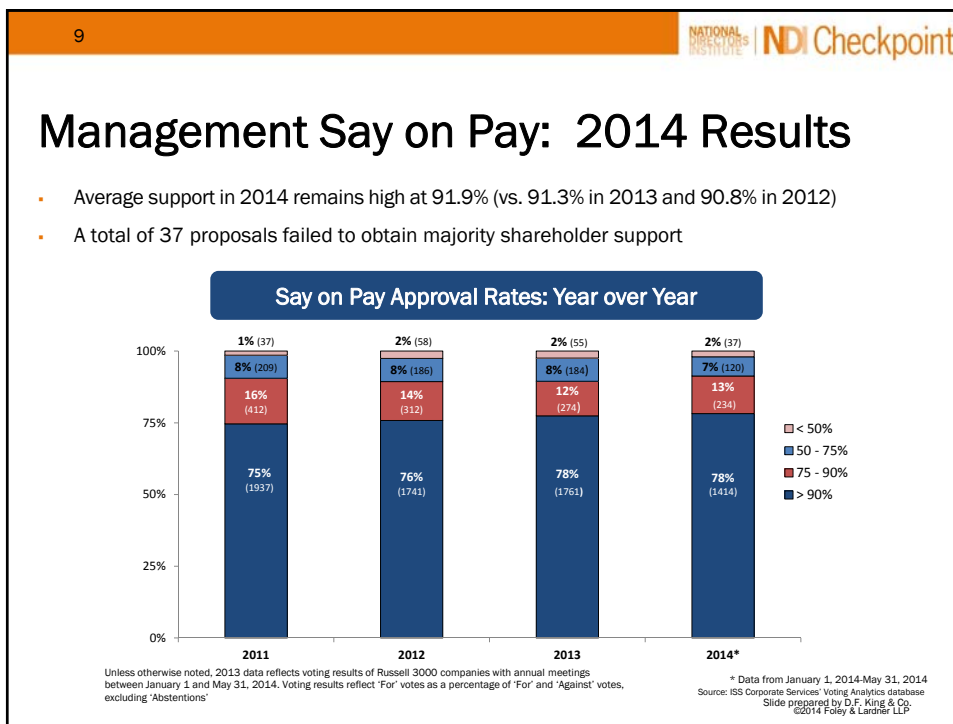
- Takes metric construction and actual company performance into consideration

**Improvements Over Realized Pay**

- Takes investment decisions out of the mix
- Takes holding restrictions off the table
- Takes compensation realized but not earned in the performance period off the table

**Realizable Pay measures compensation based on the actual outcomes of performance-based awards earned and equity award appreciation**

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## Say on Pay Year over Year

- Companies that failed Say on Pay in 2013 received significantly more support in 2014
- Biggest changes in 2014 are from companies that received the lowest support in 2013
- In 2014, companies made efforts to increase engagement, strengthen the link between pay and performance, and bolster the rigor of performance goals
- Overwhelming majority of companies (94%) have passed Say on Pay in all three years
- 5% passed two years, failed one

2013 Support	Average Change in 2014
< 50%	+39%
50 - 75%	+13%
75 - 90%	+4%
> 90%	-3%

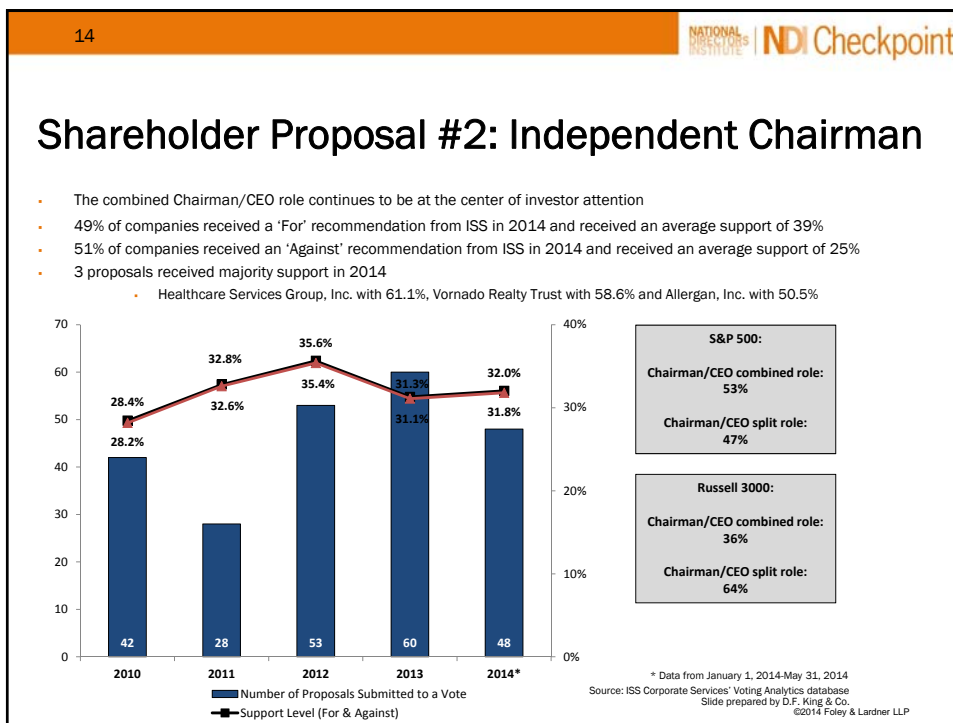
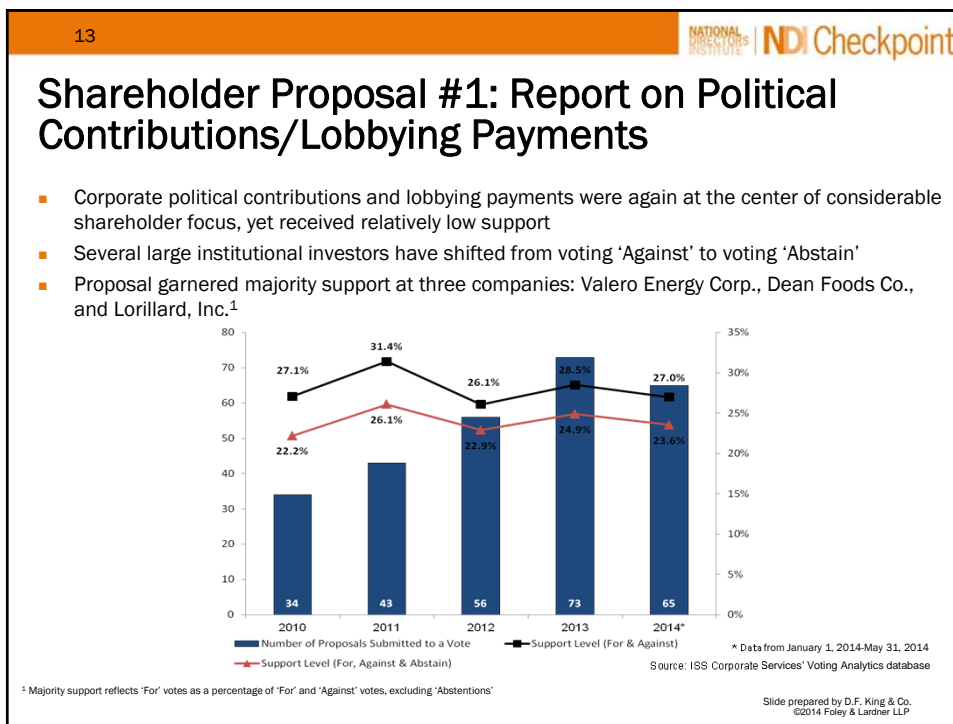
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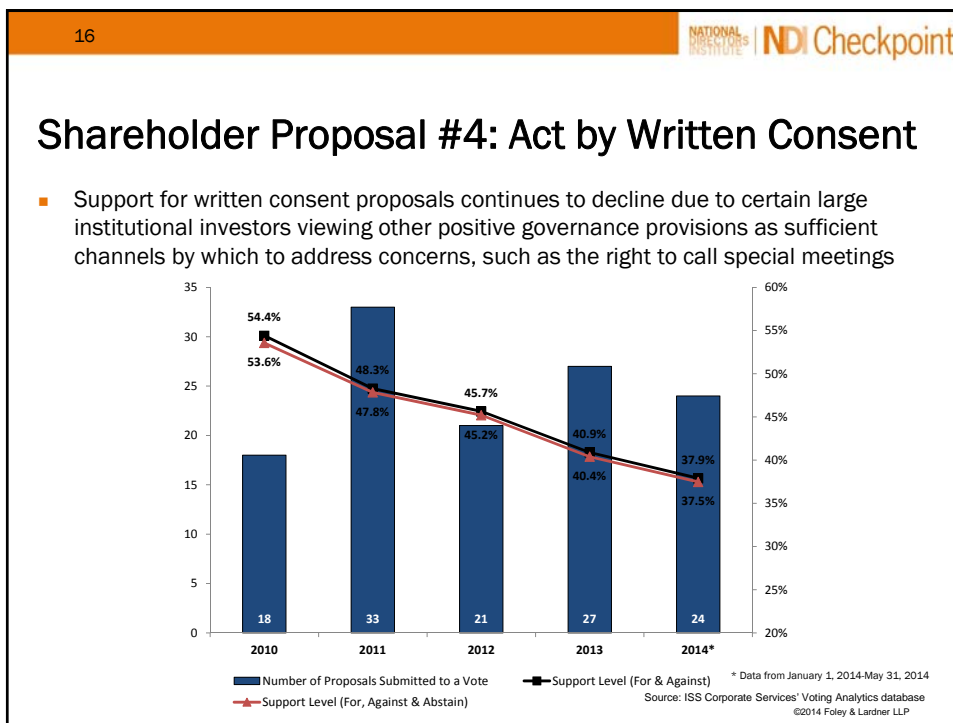
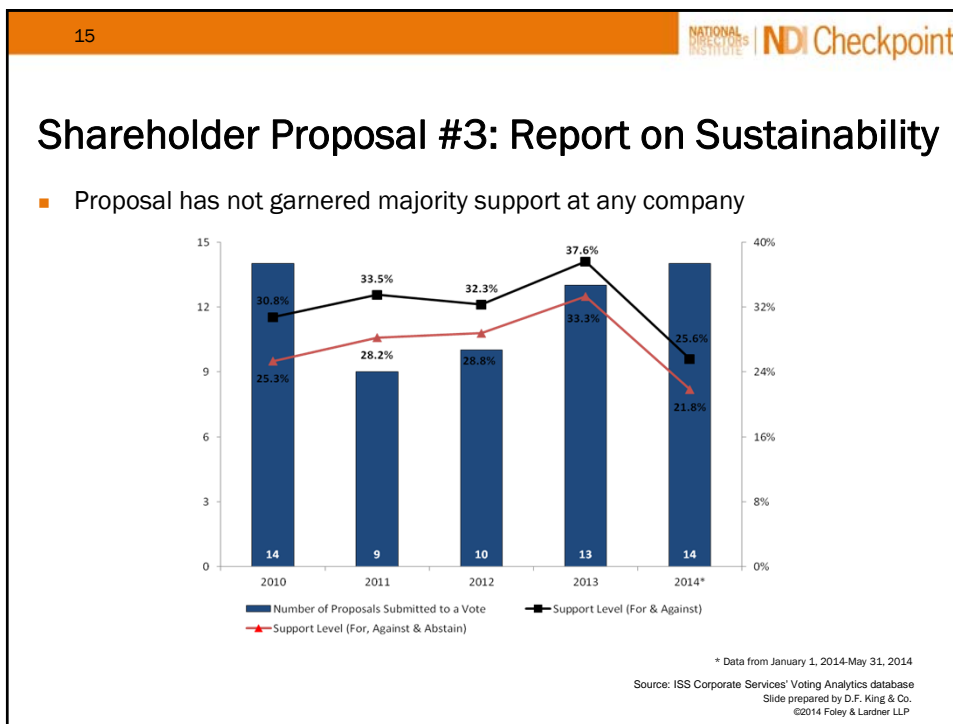
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## 2014 - Top 10 Proposals Submitted

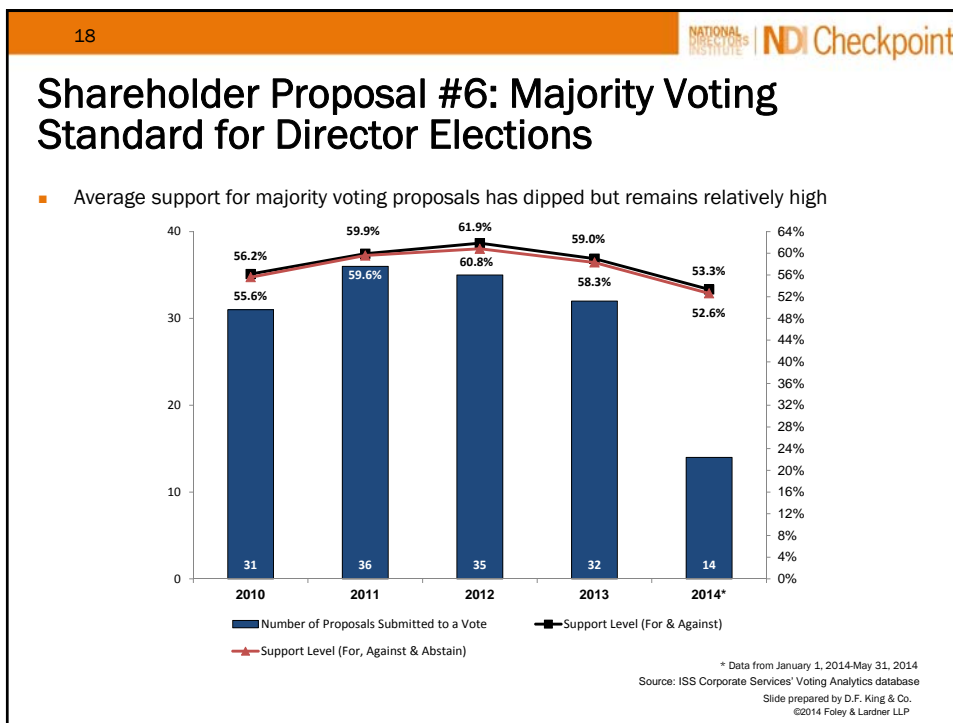
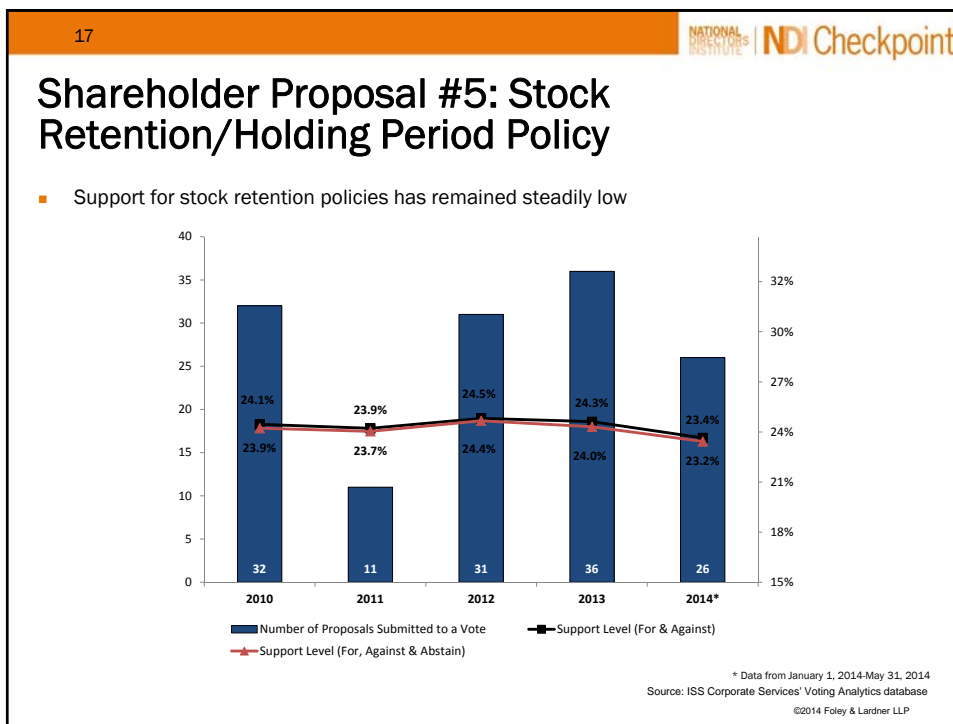
Proposal Category	Number of Proposals Submitted	Number of Proposals Submitted to a Vote
Report on Political Contributions / Lobbying	85	65
Independent Chairman	62	48
Report on Sustainability	37	14
Act by Written Consent	30	24
Stock Retention Policy	27	26
Majority Voting	25	14
Call Special Meeting	24	12
Eliminate Supermajority Provision	19	11
Pro-Rata Vesting of Equity Awards	19	6
Report on Board Diversity	16	2

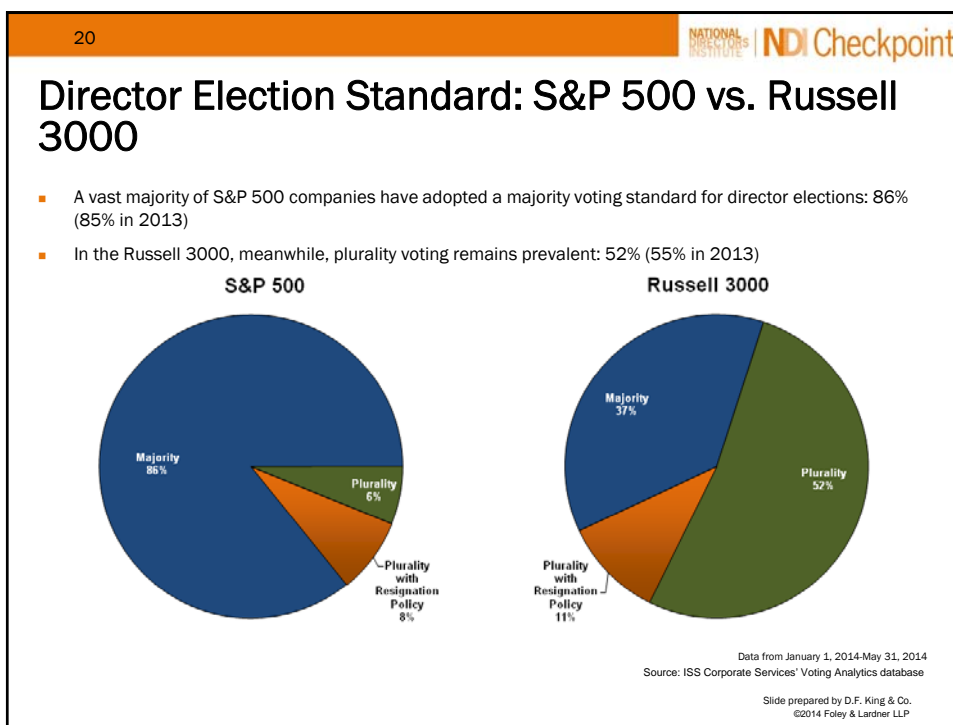
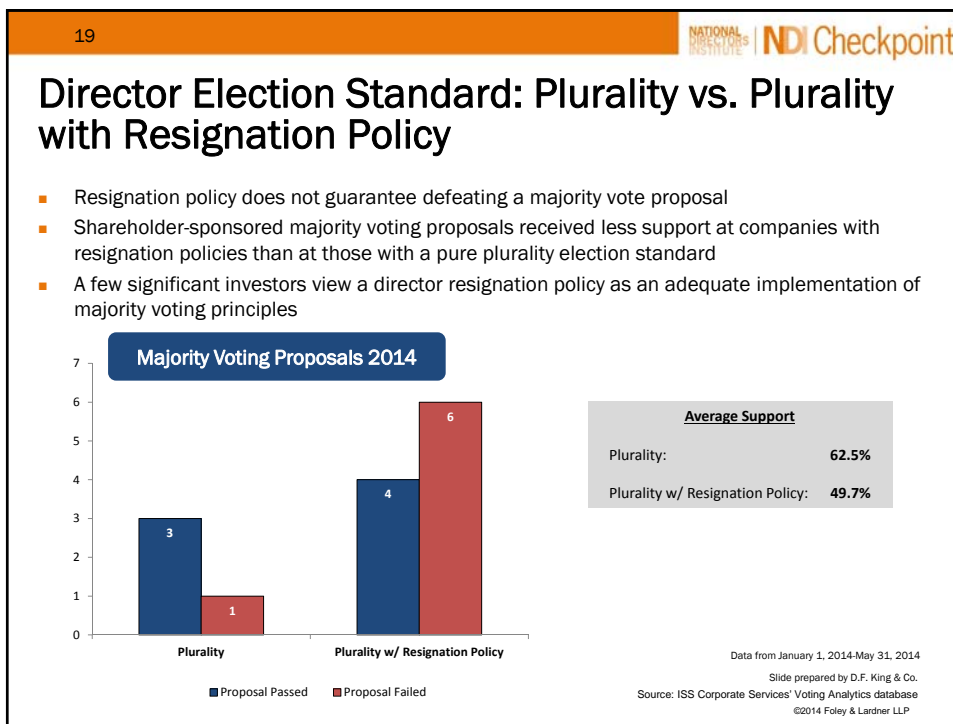
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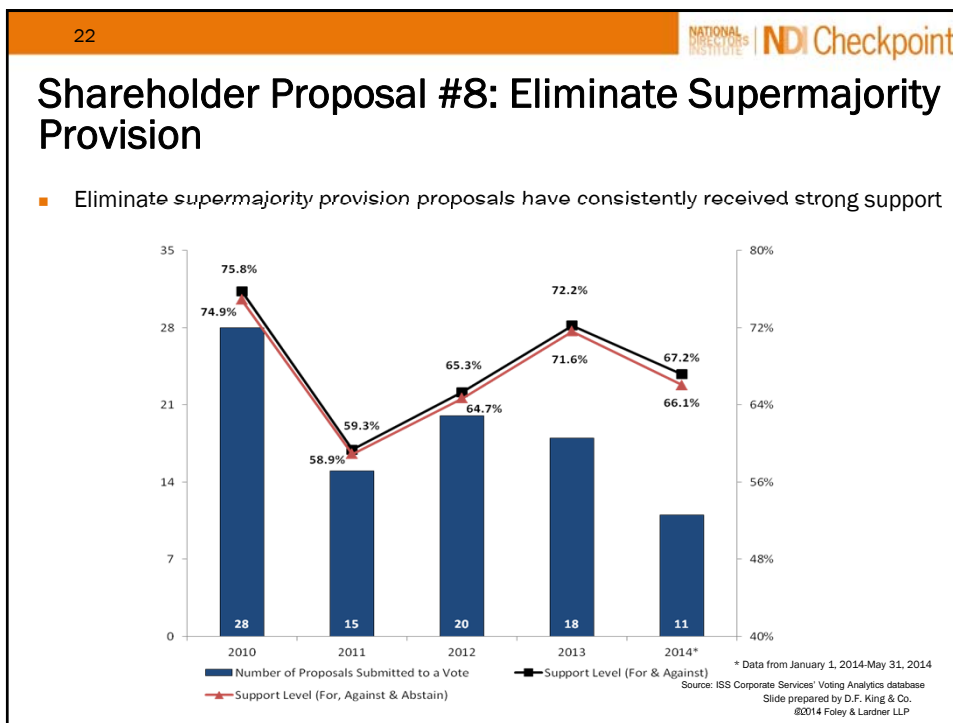
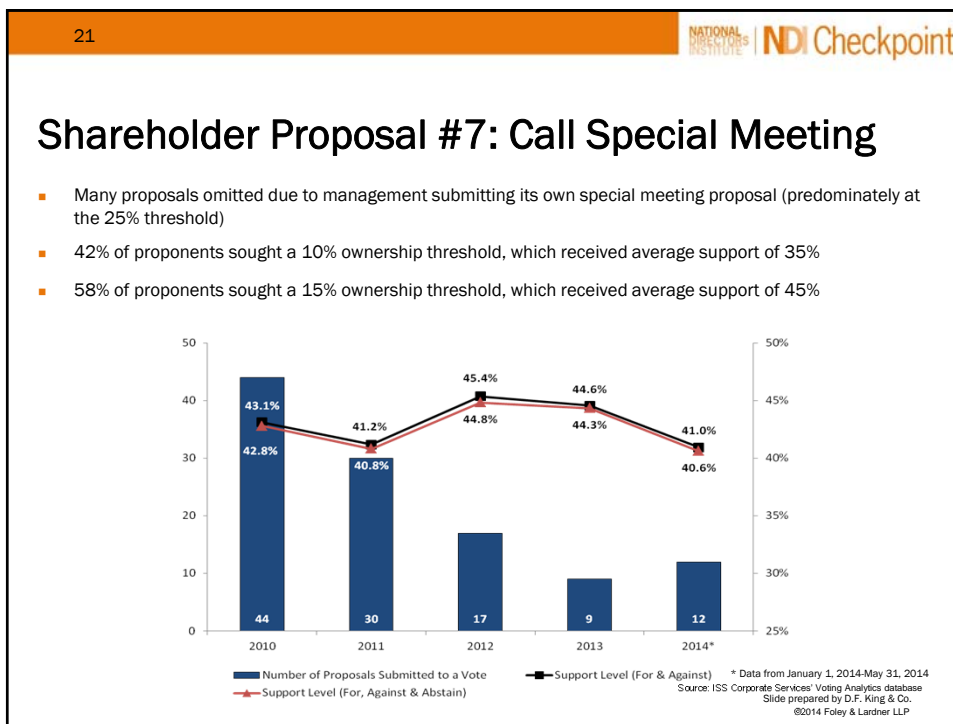


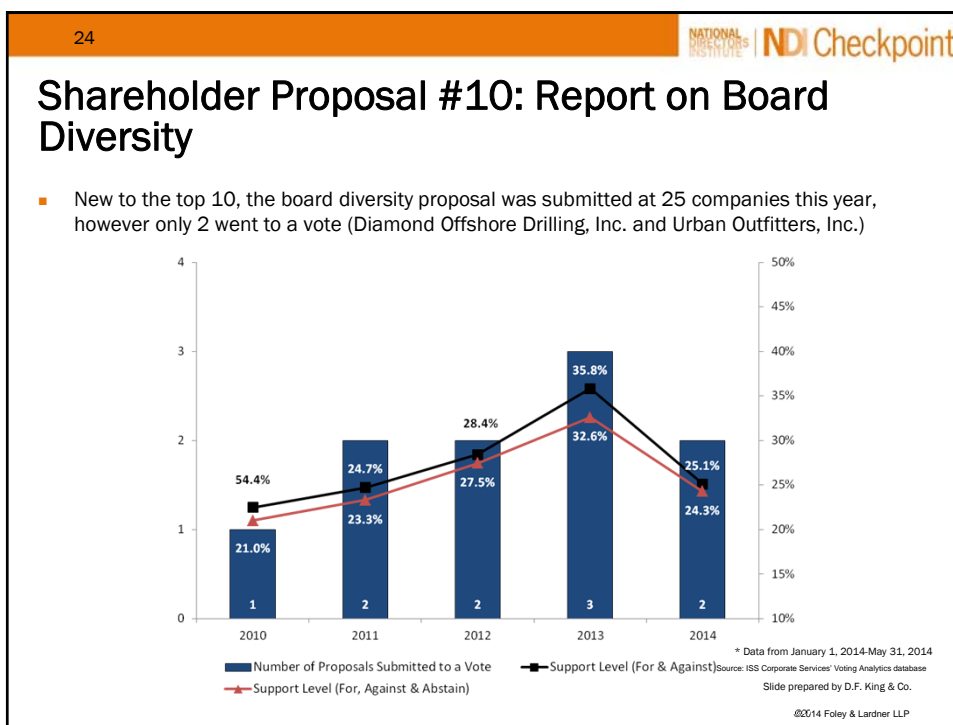
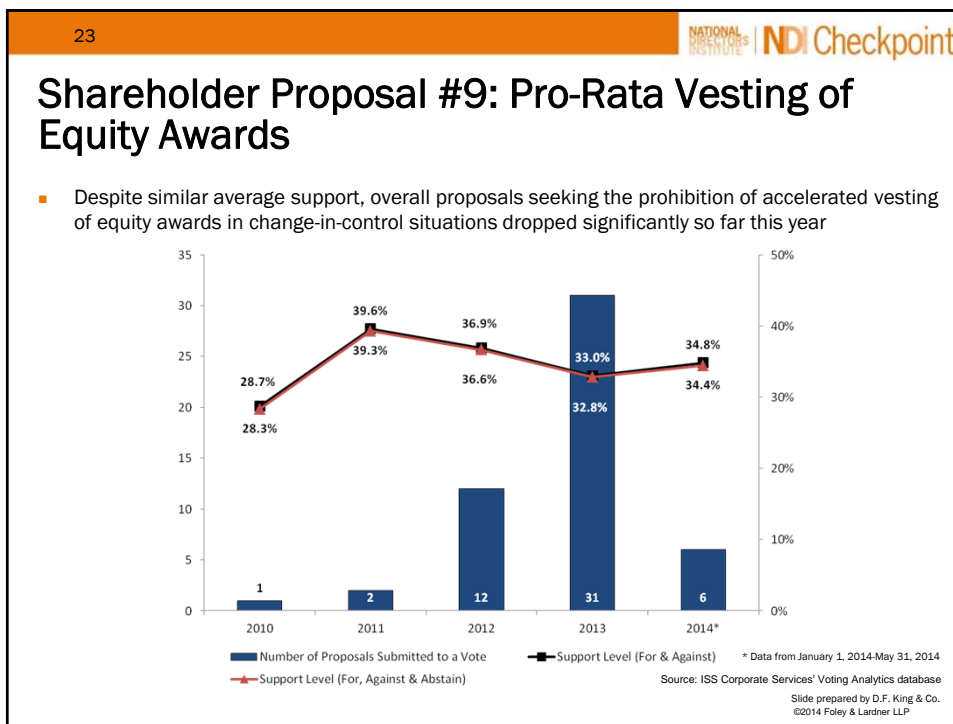


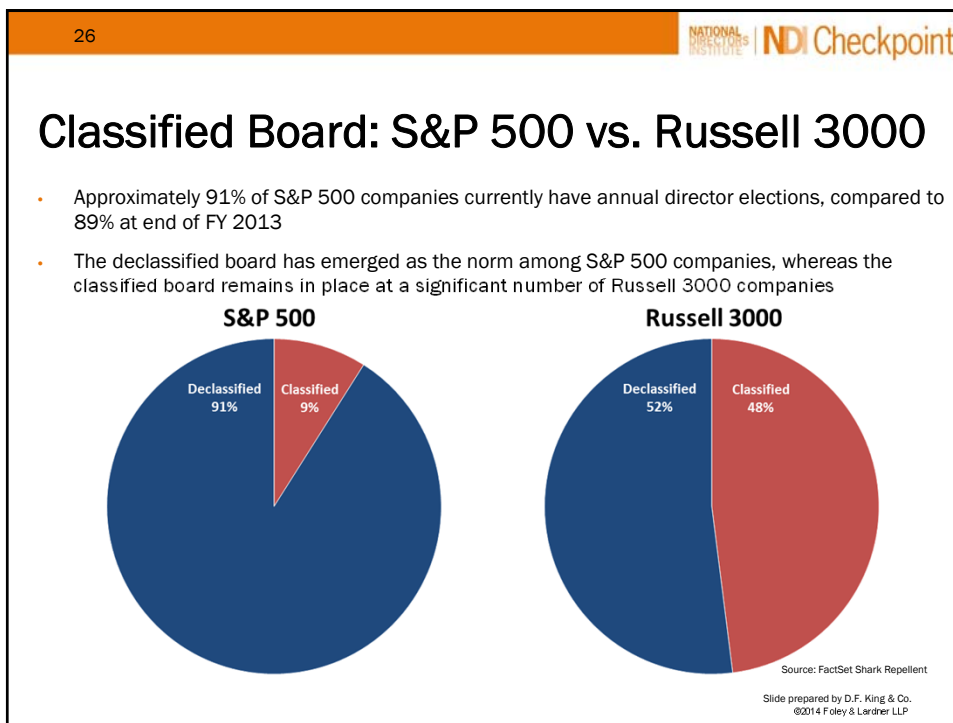
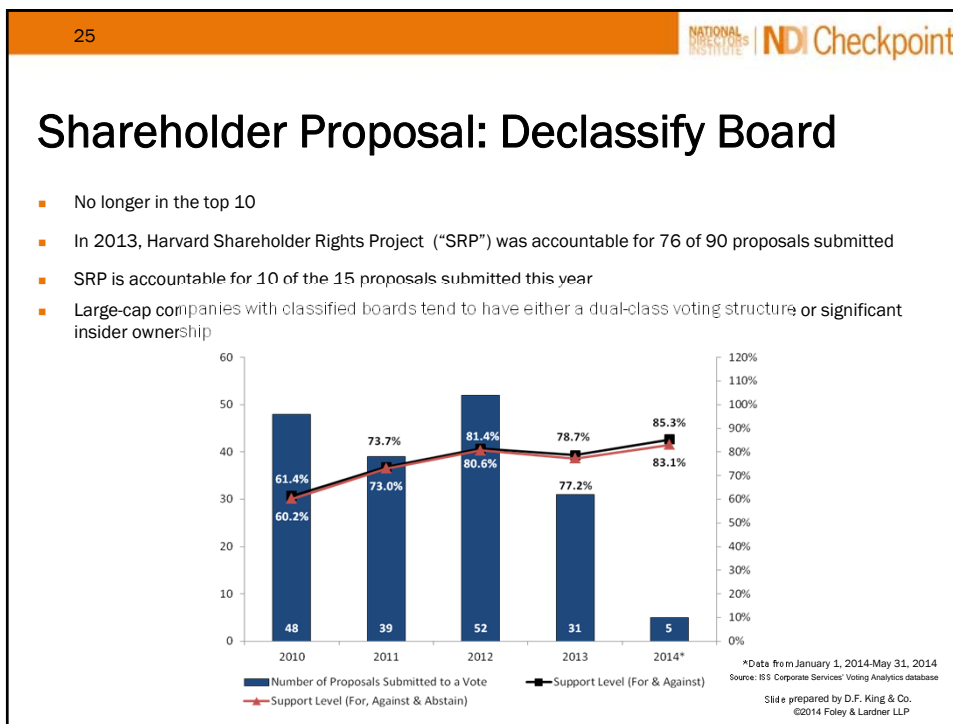












27

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## Shareholder Proposal: Proxy Access

- Companies receiving majority support for proxy access proposals
  - 2014 - Big Lots, Inc., International Game Technology and Boston Properties, Inc.
  - 2013 - Verizon, CenturyLink and Darden Restaurants
  - 2012 - Nabors Industries and Chesapeake Energy
- SEC-style proposal (3% for 3 years, 20/25% cap on seats) continues to garner greatest support
- A total of 13 proxy access proposals were submitted in 2014 (9 voted, 4 withdrawn)
- Average support overall: 31.7% (2013: 32.1%)

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## Shareholder Litigation on Compensation

- Several shareholder derivative lawsuits involving compensation-related claims have been filed or threatened since the advent of say on pay
  - Typically occur following a failed say on pay vote and/or in advance of a shareholder meeting at which shareholder approval for an equity compensation plan is sought
  - Dodd-Frank expressly stated that it did not impose new or enhanced fiduciary duties in connection with the requirement to hold say on pay votes
  - Lawsuits based on failed say on pay votes generally have not been successful, but plaintiff firms continue some activity in this area
- Cheniere Energy, Inc. postponed its 2014 annual meeting due to a lawsuit filed four days earlier alleging deficiencies in the Cheniere equity incentive plan and the proxy statement disclosures concerning the plan

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## Shareholder Litigation on Compensation (con't.)

- Director pay, as well as executive pay, has also been the subject of shareholder litigation
  - An excessive compensation lawsuit was filed in June 2014 against the officers and directors of Facebook
    - Alleges directors received excessive compensation
    - Argues that the “demand” requirement is excused “Because . . . all the non-employee Director Defendants . . . received the challenged compensation pursuant to an incentive plan that contains no limits on their compensation, let alone meaningful ones, the Director Defendants stand on both sides of the compensation awards.”
  - The Facebook complaint follows the 2012 Delaware case, *Seinfeld v. Slager*, which likewise alleged that directors had paid themselves excessive compensation
    - The court allowed plaintiffs to proceed without making a demand because the directors were not considered disinterested
  - **Recommendation:** consider establishing separate director plan for equity awards to non-employee directors

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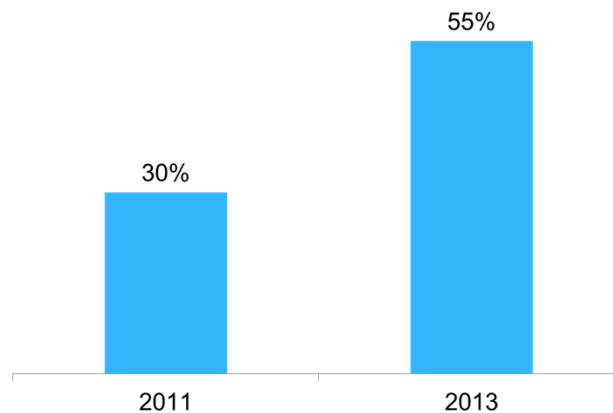
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## Shareholder Engagement

Companies have worked to increase shareholder engagement

Percentage of public companies reporting initiating at least 10 shareholder engagements

- Overall shareholder engagement is up more than 50% compared to 4 years ago
- Almost 80% of companies are conducting shareholder outreaches



Source: "Defining Engagement: An Update on the Evolving Relationship Between Shareholders, Directors and Executives" – IRRC Institute and ISS.  
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## Even though this year's campaigns are just winding down, it's time to plan for next year

### Boston Properties (BXP) 2014 Proxy Disclosure

**May 17, 2011**  
2011 Say-on-Pay  
Stockholders overwhelmingly support NEO compensation with a 96% vote FOR Say-on-Pay.

**May 15, 2012**  
2012 Say-on-Pay  
For the second straight year, stockholders strongly support NEO compensation with a 96% vote FOR Say-on-Pay.

**March 11, 2013**  
Succession Announced  
BXP announces the firing of Mr. Thomas as CEO and the transition of Mr. Zuckerman to Executive Chairman. Corresponding compensation arrangements (including TBA) are disclosed on Form 8-K.

**April 5, 2013**  
2013 Proxy Statement Filed  
Discloses compensation awarded for 2012 performance and includes summary of TBA.

**May 21, 2013**  
2013 Say-on-Pay Vote  
Although the philosophy and design of NEO compensation remained consistent with the prior two years and had been endorsed by stockholders, 80.6% vote AGAINST Say-on-Pay due primarily to TBA.

**July-November 2013**  
Stockholder Engagement  
Compensation Committee undertakes a significant outreach effort to better understand stockholder concerns.

**January 2014**  
Compensation Decisions Made for 2013 Performance  
Compensation Committee takes meaningful steps in response to Say-on-Pay vote to address key concerns expressed by stockholders (items discussed throughout the CD&A).

**April 4, 2014**  
2014 Proxy Statement Filed  
Discloses compensation awarded for 2013 performance. However, due to SEC requirements, the Summary Compensation Table contains items from last year's actions, particularly contractual obligations under TBA.

**Prime shareholder engagement season is July through your Comp Committee's fall strategy meeting**

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## A potential wrinkle: Differing views on engagement

### Survey question: How Long Does an Engagement Typically Last?


Group	More than one month	Two weeks to one month	A week or less
Issuers	12%	22%	66%
Investors	61%	14%	25%

- Survey results show that companies think of engagement similar to a road show
- The majority of investors, on the other hand, are expecting a longer-term dialogue


Source: "Defining Engagement: An Update on the Evolving Relationship Between Shareholders, Directors and Executives" – IRRC Institute and ISS.

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# CLE Code Announcement



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34



## Looking Ahead to 2015

- Exclusive Forum Provisions
  - Delaware court upheld validity of exclusive forum bylaws adopted by Chevron and FedEx
  - Glass Lewis policy recommends 'Withhold' / 'Against' vote on governance committee chair if bylaw is adopted without shareholder approval
- Debate over third party director compensation
  - Approximately 30 companies have adopted bylaws restricting such arrangements
  - ISS considers the adoption of restrictive director qualification bylaws without shareholder approval as a material failure of governance; ISS recommended 'Withhold' / 'Against' votes on members of the nominating committee
  - Some companies put bylaw restrictions to a vote (Wynn Resorts), other companies enacted bylaws stating that directors cannot be paid until after they are elected as directors

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## Looking Ahead to 2015 (con't.)

- Director Tenure / Board Refreshment
  - Some contend that directors serving on boards for long periods of time may lack independence and objectivity
  - Only 16 companies [as of 2013] in the S&P 500 index have established specific term limits for directors, down from 25 companies in 2009<sup>1</sup>
  - Board turnover at S&P 500 companies hit a 10-year low [in 2012], with more than two-thirds of those directors serving terms of 10 to 15 years, Bloomberg reported. An additional 5% had tenures longer than 15 years<sup>1</sup>
  - In the S&P 500, 3% specify a term limit for directors in their corporate governance guidelines. 65% of boards explicitly state that they do not have term limits, and 32% do not mention term limits at all<sup>2</sup>
  
- Board Diversity
  - Women hold just 16.9% of Fortune 500 board seats<sup>3</sup>
  - Among the largest 200 S&P 500 companies, minorities account for only 15% of all directors<sup>3</sup>
  - The board diversity proposal was submitted at 25 companies this year

Sources: <sup>1</sup>Wall Street Journal, <sup>2</sup>American Progress, and <sup>3</sup>Spencer Stuart  
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## Status Update on Dodd-Frank Rules

- Compensation Committee Independence
  - Dodd-Frank imposed heightened independence requirements for Compensation Committees and their advisers
  - Rules became effective in 2013 and required changes to committee charters
  - One deadline is still approaching: NASDAQ companies must certify to NASDAQ within 30 days after the later of their annual meeting in 2014 or October 31, 2014 that they meet the new Compensation Committee requirements
- CEO pay ratio disclosure
  - Rules proposed in 2013
  - May become effective in 2015 or 2016
- Other rules still to come
  - Policy on recovery of erroneously awarded compensation (“clawbacks”)
  - Disclosure of hedging by employees and directors
  - Disclosure of pay versus performance

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**Questions & Answers**

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39

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## Mark Your Calendar

- 2014 NDI Checkpoint Sessions
  - August 20, 2014
  - December 3, 2014
  
- Save the Date! NDI Executive Exchange
  - November 6, 2014 – Chicago, IL – Invitation-only

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40

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## Thank You

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