

# **Board-Shareholder Communications: Speak Now or Forever Wish You Had**

## **NACD New England**

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**November 9, 2010**



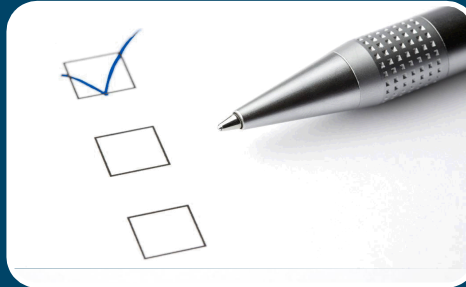
# Agenda

- ◆ Moderator: Maureen T. Wolff
- ◆ Panelists:
  - ◆ Louis A. Goodman
  - ◆ Fred K. Foulkes
  - ◆ Fletcher H. “Flash” Wiley
- ◆ Questions and Answers

## Maureen T. Wolff

- ◆ Maureen is president of Sharon Merrill Associates, a critical communications consulting firm focused on investor relations, reputation and issues management, and crisis and transaction communications. In addition to her leadership and long-term vision role, Maureen supports clients with strategic counsel, directs the agency's operations and is active in business development. A nationally recognized leader in the fields of investor relations and corporate communications, Maureen is a past chairman and board member of the National Investor Relations Institute (NIRI). She is a frequent speaker on IR issues, including shareholder activism and board-shareholder communications, and has authored numerous articles for business publications.

# Key Board Communications Issues



**Proxy  
Access**

**Say on  
Pay**

**Activist  
Investors**

# Current Environment



- ◆ Activism expected to escalate dramatically in 2011
- ◆ Belief that management and Board not accountable
- ◆ Stock price usually key trigger for activism
- ◆ Fights typically center on financial, strategic or governance issues
- ◆ Proxy advisory companies key in proxy battles

# Potential Triggers

- ◆ Poor stock price performance (absolute performance) and relative to peers
- ◆ Excessive compensation packages
- ◆ High operating expenses relative to peers
- ◆ Less than optimal capital structure
- ◆ Poor accounting practices

# Potential Triggers

- ◆ Poor bylaws and structural defenses
- ◆ Entrenched board; possible conflicts of interest
- ◆ Corporate strategy not supported or understood
- ◆ Significant asset sales
- ◆ Acquisitions – “The Bain Problem”

# Board Communication Concerns

- ◆ Shareholders increasingly reaching out directly to directors
- ◆ Most Boards have no formal communication policy in place
- ◆ No best practice established
- ◆ Directors often untrained in Regulation Fair Disclosure
- ◆ Directors uninformed on company's public disclosures



# Benefits of Communications

- ◆ Strengthen Board's role as an active, informed and engaged fiduciary to shareholders
- ◆ Some Boards may not have a good balance of information coming from external and internal sources
- ◆ Boards who meet with shareholders will increase their understanding of the risks faced by a corporation
- ◆ More communication (including more *listening*) can enhance a Board's reputation/credibility
- ◆ Board-shareholder communications may forestall regulation and shareholder resolutions

# Board Communications Initiatives

- ◆ Understand your shareholder base
- ◆ Know who is unhappy and develop a consistent dialogue with all major shareowners
- ◆ Become familiar with proxy voting guidelines and assess where your company may be at risk
- ◆ Include proxy solicitation in year-round investor outreach and communications programs
- ◆ Schedule communications training
- ◆ Monitor activist triggers and be proactive

# Proxy and Corporate Governance Update

National Association of Corporate Directors

Board-Shareholder Communications: Speak Now or Forever Wish You Had

November 9, 2010

Louis A. Goodman



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# Agenda

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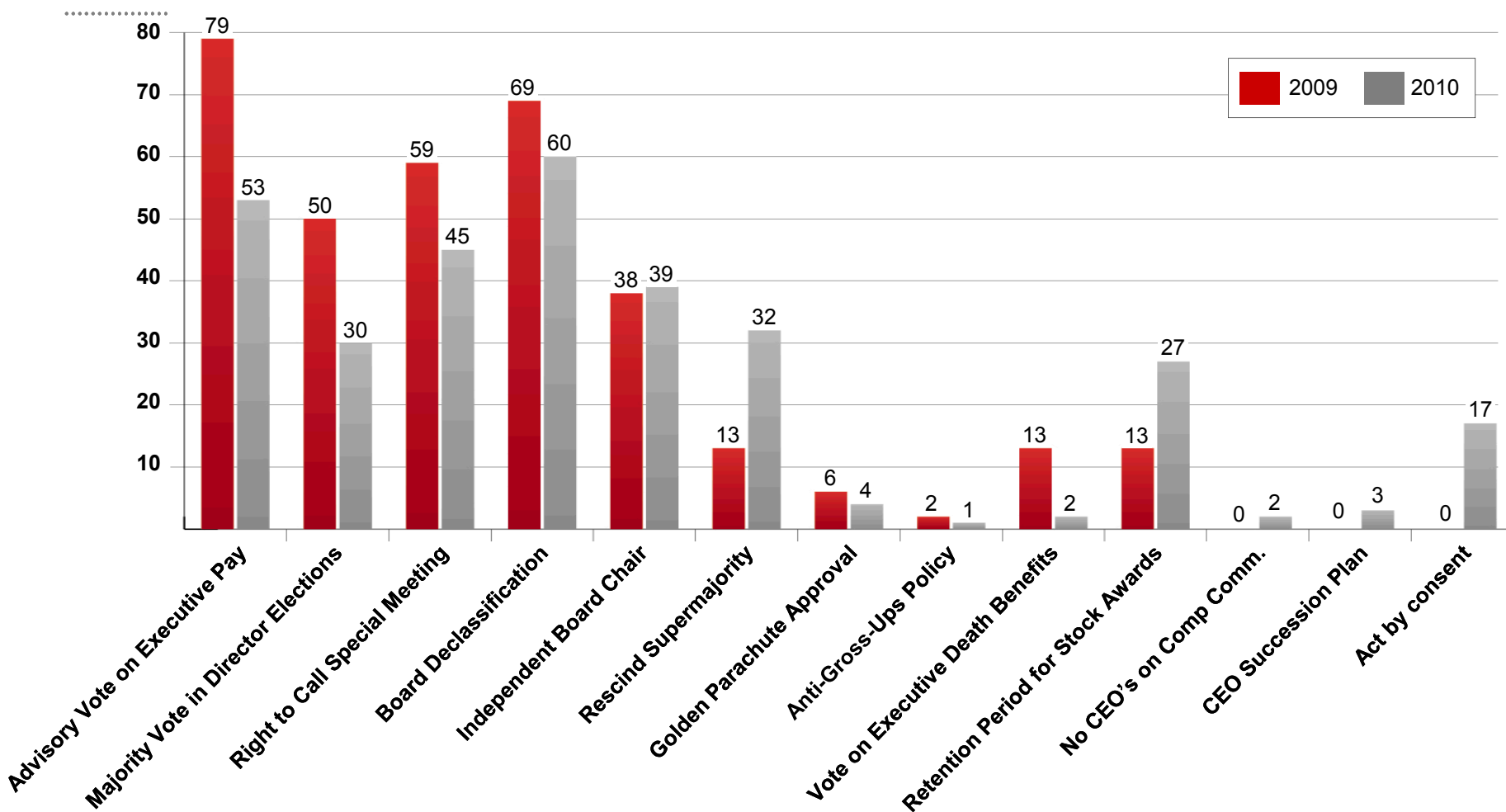
- Overview of Current Environment
- 2010 Proxy Season Review
- Proxy System Reform
- Say-on-Pay
- Other Executive Compensation Reforms
- SEC Whistleblower Bounty
- Proxy Access
- Action Items

# Overview of Current Environment

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- Increasing federal role in corporate governance
  - Dodd-Frank Act
  - SEC rulemaking
  - Impact of 2010 elections?
- Continued governance campaigns and robust activism
  - Board seats (short slates)
  - Executive compensation
  - Removal of takeover defenses
  - For/against transactions
- Rule changes continue to facilitate activism and governance campaigns

# Shareholder Proposals on Key Governance Issues



Source: ISS      Note: Data for 2010 is partial year through July 1, 2010

# 2010 Director Elections

- According to ISS, as of September 1, 2010, 88 directors failed to win majority support, down from 93 for the same period in 2009
  - At S&P 500 companies, only one director failed to win majority support, down from 12
- Number of S&P 500 companies with one or more directors receiving at least 10% against/withhold votes:

2010	158
2009	171
2008	121
2007	118
2006	95

# Proxy System Reform

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- SEC is undertaking a comprehensive review of the U.S. proxy system, including:
  - Role of proxy advisory firms, such as ISS, and whether they should be subject to enhanced regulation
  - “Empty voting” – obtaining voting rights without a corresponding economic interest in the company
  - Ability of companies to communicate with shareholders and ways to improve retail investor voting
  - Mechanics of proxy voting, including accuracy, transparency and efficiency of the voting process

# Dodd-Frank: Annual Meeting Say-on-Pay

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- At the 2011 annual meeting, shareholders will have two separate, non-binding votes:
  - “Say-on-pay”: a vote to approve the compensation of executive officers as disclosed in the proxy statement
  - “Frequency”: a vote on whether future say-on-pay votes should occur every one, two or three years
    - Frequency vote is required at least once every six years
- Although non-binding, a “no” vote is likely to have future consequences if underlying concerns are not addressed

# Say-on-Pay: 2010 Experience

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- Average say-on-pay vote in 2010 (voluntary + TARP companies) was 89.6% in favor of disclosed executive compensation, compared to 87.4% in 2009
  - Executive compensation failed to receive majority support in say-on-pay votes at Motorola, Occidental Petroleum and KeyCorp

# Say-on-Pay: SEC Proposed Rules

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- Although say-on-pay takes effect without SEC rulemaking, SEC has proposed rules to implement say-on-pay and frequency votes:
  - No specific form of say-on-pay resolution
  - Disclose that votes are being provided by law and are not binding on the company
  - Preliminary proxy filing is not required
  - Future CD&A disclosure on whether and how compensation decisions were impacted by previous say-on-pay votes

# Say-on-Pay: SEC Proposed Rules

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- Frequency vote will be a choice of one, two or three years or abstain
- Disclose in Form 10-Q the company's decision regarding how frequently to provide say-on-pay votes in light of frequency vote result
- If company adopts a policy consistent with the plurality of votes cast in the most recent frequency vote, company may exclude Rule 14a-8 proposals on say-on-pay or frequency

# Dodd-Frank: Merger-Related Say-on-Pay

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- When shareholders are voting on a merger or similar transaction, companies must:
  - Include proxy disclosure describing agreements or understandings concerning compensation of any Named Executive Officer based on or related to the transaction
  - Provide shareholders a separate non-binding vote to approve those merger-related compensation agreements or understandings
- Vote is not required if the merger-related agreements or understandings previously were the subject of a required say-on-pay vote

# Merger-Related Say-on-Pay: SEC Proposed Rules

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- Merger-related say-on-pay votes are not required until SEC adopts final rules
- SEC has proposed:
  - New table and narrative disclosure on merger-related compensation
  - Disclosure would include arrangements among target company, acquiring company and their NEOs
  - Disclosure regarding “single trigger” or “double trigger” and other material terms
  - Disclosure would be required in various business combination-related filings (*e.g.*, tender offer documents)

# Merger-Related Say-on-Pay: SEC Proposed Rules

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- As proposed, merger-related compensation would have been subject to a previous say-on-pay vote only if the new disclosure is included voluntarily in an annual meeting proxy statement and there are no new or revised arrangements
  - In the event of new or revised terms, a second table is required and the vote relates only to those new or revised terms
  - Open questions around what constitutes a new arrangement – *e.g.*, new grant of options subject to the same acceleration terms – may limit utility of this exception

# Dodd-Frank: Provisions Related to Say-on-Pay

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- No broker discretionary voting authority with respect to executive compensation
- Institutional investment managers who file Form 13F have to disclose at least annually how they voted on say-on-pay proposals with respect to companies in their portfolios

# Dodd-Frank: Enhanced Independence for Compensation Committees

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- Enhanced independence requirements for listed company compensation committee members:
  - Whether a committee member receives consulting, advisory or other compensatory fees paid by the company
  - Whether a committee member is affiliated with the company or any subsidiary
- Requires SEC rulemaking within 360 days of enactment; proposed rules expected by year-end

# Dodd-Frank: Enhanced Independence for Compensation Committees

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- Listed company compensation committees may select a compensation consultant, legal counsel or other advisor only after “taking into consideration” independence factors to be identified by the SEC
- Requires SEC rulemaking within 360 days of enactment; proposed rules expected by year-end

# Dodd-Frank: Clawback Policies

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- Requires listed companies to implement a policy to recoup executive compensation in the event of a restatement
  - Restatement due to material noncompliance with any financial reporting requirement under the securities laws
  - Applies to all current and former executive officers who received incentive-based compensation (including stock options) during the three years preceding the restatement
  - Recoup difference between incentive-based compensation paid on the basis of erroneous data and amount of incentive-based compensation that would have been paid based on the corrected data
- SEC rulemaking required; proposed rules expected April-July 2011

# Dodd-Frank: Additional Executive Compensation Disclosures

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- Pay versus performance:
  - Annual meeting proxy disclosure comparing executive compensation and the company's financial performance, taking into account changes in the value of the company's shares and dividends paid
- Internal pay ratio:
  - Median of the annual total compensation of all company employees other than the CEO;
  - Annual total compensation of CEO; and
  - Ratio of the two amounts
- SEC rulemaking required; proposed rules expected April-July 2011

# Dodd-Frank: Disclosure Regarding Hedging

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- Annual meeting proxy disclosure on whether employees and directors are permitted to purchase financial instruments designed to hedge or offset any decrease in the market value of company equity securities
- SEC rulemaking required; proposed rules expected April-July 2011

## **Dodd-Frank: SEC Whistleblower Bounty**

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- Whistleblowers receive an award if they provide original information that leads to a successful SEC enforcement action resulting in monetary sanctions exceeding \$1 million
- Award amount is 10% to 30% of the monetary sanctions (including recoveries in related actions by DOJ, state or foreign regulators, SROs)
- Immediate effectiveness
- Dovetails with recent SEC Enforcement initiative to encourage individual cooperation

- SEC-mandated proxy access: new Exchange Act Rule 14a-11
- An eligible shareholder (or group of shareholders)
  - Holding at least **3%** voting power
  - For at least **3 years**
  - May include in the company's proxy materials candidates for up to **25% of the company's board seats**
- Rule 14a-8 was amended so that shareholders may submit proposals for **additional** proxy access

# Proxy Access

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- Business Roundtable and U.S. Chamber of Commerce petitioned for court review of Rule 14a-11
  - Explicitly did not challenge amendment to Rule 14a-8
- SEC issued an order staying the effectiveness of both Rule 14a-11 and amendment to Rule 14a-8 pending outcome of litigation
- Effectively pushes proxy access into 2012 for most companies (assuming rules upheld)

- “Within a few years, we can expect to see 100s of proposals calling for more reasonable thresholds and holding periods, as well as allowing a greater proportion of shareowner nominees. Corporate governance activists have been given a new focus . . . [W]e will now be fighting for more reasonable nomination requirements. To the John Cheveddens and Ken Steiners of the world I say, ‘Time to gear up; may a thousand access proposals bloom.’”

— Blog post from James McRitchie, CorpGov.net

# Action Items

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- Director Action
  - Review bylaw provisions to determine appropriate vote for Board action
- Board Confidentiality and Authority
  - Review policies and procedures regarding director confidentiality and director authority to speak on behalf of the company
- Advance Notice Bylaws
  - Review advance notice bylaws related to director nominations to ensure effectiveness
  - Consider disclosure regarding derivative holdings
- Director Qualification Provisions
  - Consider adopting qualification provisions that could relate to, among other things, minimum age, experience or stock ownership

- Board Composition
  - Ensure that directors have necessary qualifications, skills and experience, as a group, to exercise effective oversight
- Voting Standards
  - Review voting standards in light of NYSE rule changes eliminating broker discretionary voting on certain matters
- Exceptions to Majority Voting in Contested Elections
  - Review majority voting standard to ensure it contains appropriate exceptions, including in the event of an election contest
- Number of Directors
  - Evaluate appropriate size of the Board

- Say-on-Pay
  - Review compensation policies to anticipate issues in achieving a favorable say-on-pay vote and consider what recommendation, if any, the company wishes to make regarding the frequency of the say-on-pay vote
- Compensation Clawbacks
  - Review employment agreements with executive officers and consider whether to provide for a clawback mechanism



## Louis A. Goodman

*Partner*

Corporate, Securities and Finance Law

Louis Goodman is a senior partner in the Boston office of Skadden, Arps. He works on a wide range of corporate matters, from restructurings, financings and acquisitions to white collar criminal defense.

Mr. Goodman has represented clients in some of their most significant transactions — many that have industry-wide and sometimes worldwide significance. He also has represented start-up companies and investors in smaller transactions.

He frequently represents companies in mergers and acquisitions, including BJ Services Company in its \$5.5 billion acquisition by Baker Hughes Incorporated; Tele Atlas N.V. in its approximately \$4.2 billion acquisition by TomTomNV; and Textron Inc. in its approximately \$1.1 billion acquisition of United Industrial Corporation.

Recently, he successfully defended TravelCenters of America LLC and RMR Hospitality and Real Estate Fund in two separate proxy contests brought on by activist hedge funds.

Mr. Goodman represented clients on various aspects of federal lending, capital and liquidity support programs, including those established pursuant to the Emergency Economic Stabilization Act of 2008.

Mr. Goodman is a member of the Massachusetts Business Roundtable. He also is included on numerous best-lawyer lists and is a frequent speaker on legal and financial topics.

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### Bar Admissions

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# Fred K. Foulkes



- ◆ Fred has served as a director of Panera Bread since 2003 and is currently a member of the audit, compensation and management development, and the nominations and corporate governance committees. Professor Foulkes is a Professor of Organizational Behavior and the Director of the Human Resources Policy Institute at Boston University School of Management and has taught courses in human resource management and strategic management at Boston University since 1980. From 1968 to 1980, Professor Foulkes was a member of the Harvard Business School faculty. Dr. Foulkes formerly served on the board of directors of Bright Horizons Family Solutions, the Society for Human Resource Management and the National Academy of Human Resources.

## Fletcher H. “Flash” Wiley

- ◆ Flash has served on The TJX Companies, Inc. board since 1990 and is currently a member of the audit and corporate governance committees. Mr. Wiley was Executive Vice President and General Counsel of PRWT Services, Inc., a technology-oriented products and services firm, from 1996 to 2008. Since 2003, Mr. Wiley has been “Of Counsel” to Bingham McCutchen LLP, one of the nation’s largest law firms, where he specializes in corporate and commercial law. Previously, Mr. Wiley was of counsel to the law firm Schnader Harrison Goldstein & Manello and a partner of the law firms Goldstein & Manello and Fitch, Wiley, Richlin & Tourse, P.C. Mr. Wiley formerly served on the board of directors for Boston Acoustics, Inc. and Moyco, Inc.

# Summary

Review corporate governance policies for problem areas

Review compensation policies and develop defensible disclosures

Include proxy solicitation in year-round outreach

Maintain active dialogue with shareholders and develop board-shareholder communications plan

# Questions?