



# PROXY DISCLOSURE AND GOVERNANCE IN AN INCREASINGLY TRANSPARENT WORLD

## Risk Management, Governance and Transparency - Key Issues in 2010 Disclosures

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The ongoing march toward greater disclosure of, and investor engagement in, key pay and governance issues at US public companies is accelerating again in 2010. With the proposal and/or adoption of substantive legislative, regulatory and policy changes, Congress, the Securities Exchange Commission (SEC) and investor advisory groups have transformed the landscape on which company decisions about pay and governance are made.

In some respects, the regulatory and policy shifts occurring at the end of 2009 represent a simple refinement of rule changes that were introduced with the Compensation Discussion and Analysis (CD&A) in 2007. Other changes, however, are more fundamental in nature, and far-reaching in implication. These rules will both invite increased investor scrutiny, and necessitate significant expenditures of company resources in order to meet compliance requirements. The aggregate effect of these changes is a new standard for detailed disclosure, which will likely lead to new levels of investor activism and engagement.

This Radford White Paper reviews the recent and proposed legislative and regulatory changes, as well as revisions to proxy advisor policies that will both shape how companies craft their 2010 proxy disclosures, and determine how those pay and governance practices are likely to evolve in the year to come. This paper is divided into four sections, including:

- > SEC Regulation and Disclosure Changes
  - Compensation Risk Assessment
  - Director Qualifications and Board Leadership
  - Compensation Consultants
  - Summary Compensation Table
- > Proxy Advisor and Investors
  - Shareholder Voting Activity
  - RiskMetrics Group Policy Updates
- > Legislative Update
  - Say on Pay
- > Key Takeaways

## SEC Regulation and Disclosure Changes

The most significant and pressing development for the 2010 proxy season is the SEC's adoption of new disclosure rules, which take effect for proxy statements filed on or after Feb. 28, 2010 (for calendar-year-end companies).

The new rules have widened the scope of existing proxy disclosure requirements by adding regulations pertaining to compensation risk assessment, compensation consultants, Board structure and leadership, and the Summary Compensation Tables. (See Radford Alert "SEC Adds New Disclosure Requirements," from December 2009, at [www.radford.com/home/press\\_room/index.asp](http://www.radford.com/home/press_room/index.asp) for a more detailed discussion of the regulatory changes).

### *Compensation Risk Assessment*

In introducing requirements related to compensation risk assessment, the SEC is attempting to provide investors a more detailed evaluation of how compensation philosophies (in particular those related to short- and long-term incentive compensation) can impact the risk inherent to any company. The proximate impetus for this new disclosure is the recent meltdown of the financial sector, which many believe was tied to inappropriate risk-taking spurred by pay practices at those companies. But concern over the perceived risks in compensation plans has been voiced by investors and legislators for years.

The compensation risk assessment section has been structured to: (1) prompt companies to adopt a formal process for evaluating the potential for compensation philosophies to create adverse risk; and (2) ensure shareholders are apprised of any risks that are identified, and of steps taken by the company to mitigate and/or manage the risk.

Highlights of the compensation risk assessment disclosure rules include the following:

- > It applies to *all employees*, not executives alone; *any* compensation arrangement/plan for *any* employee is covered.
- > There is a threshold for triggering the disclosure of risk. Only risks that are "reasonably likely" to have a "material adverse impact" on the company require disclosure. (This is functional equivalent of the threshold for disclosure of company risks in the MD&A section of the 10-K).
- > There is no obligation for a company to affirmatively state that it has evaluated its compensation-related risks and determined that there are no problems. In other words, companies that have identified no material adverse risk may omit the risk assessment section from their proxies entirely. As a practical matter, however, and as a matter of good governance and prudence in crafting a thorough and transparent proxy statement, we believe and recommend that companies provide a brief summary of the compensation risk analysis process, and consider stating the Board's conclusion that no material risk exists, at least in the year of the disclosure.

The compensation risk assessment rules apply to all companies, including technology and life sciences companies, most of which traditionally employ compensation strategies that are less susceptible to the kind of enterprise risks that existed in the financial services industry. Although technology and life sciences companies tend to have limited compensation risk exposure, their compensation plans should nonetheless be reviewed for the following types of potentially risk-encouraging features:

- > Uncapped bonuses
- > Commission payouts associated with long delivery schedules
- > Incentives based on a percent of revenue/profit
- > Short-term awards with no clawbacks or deferred payout structure

Companies should note that the above list is not exhaustive and is intended to be illustrative only. In addition, the listed compensation structures/practices should not be regarded as those that necessarily create inappropriate or unacceptable risks. The SEC stated that its new disclosure rules are not intended to impact companies'

compensation practices in any specific, pre-defined manner. Instead, it expects and hopes by way of the new compensation risk disclosure to ensure that Boards have a formal, regular process for the identification, evaluation, disclosure and mitigation of potentially meaningful risks associated with employee compensation programs. The ideal compensation risk disclosure should discuss how a company’s overall risk profile is addressed through its compensation practices, how compensation policies can drive particular employee behaviors, how the company has identified the risks of those behaviors, and whether/how those risks have been mitigated.

Examples of common features of compensation programs that may mitigate compensation-related risks include the following:

- > Clawbacks
- > Payout caps
- > Practices aligned to those of peers
- > Stock ownership requirements
- > Appropriate balance of: equity vehicles, terms of the awards (short- vs. long-term), cash and equity
- > Limited payouts disassociated from performance (e.g., severance, sign-on bonus, etc.)

The risk assessment process is likely to include members of the Audit and Compensation Committees, and Human Resources, legal and finance leaders, as well as compensation consultants. Additionally, those within the company who already have responsibility for assessing and reporting risk can be called upon for their expertise.

Following is an example of an assessment tool that can be used to inventory and assess compensation programs, both for the current reporting period, as well as for ongoing analysis.

**Figure 1: Compensation-Related Risk Matrix Assessment Tool**

Program	Eligibility	Measurement Factors	Limits/ Controls	Cycle/Period	Approval/ Oversight
<b>Management Incentive Plan</b>	Senior executive team	Pipeline/development milestones EPS, revenues	200%	Annual	· Compensation Committee approval of plan structure/ funding
<b>Employee Incentive Plan</b>	Non-sales employees below senior executive level	20% Corporate 80% Individual	150%	Annual	· Individual manager approval of payout · Compensation Committee approval of plan structure and funding
<b>Sales Incentive Plan</b>	Global sales force	Product revenue Team and individual goals	Uncapped Quarterly review of outliers	Annual	· Individual manager approval of payout · Compensation Committee plan oversight/ approval
<b>Performance Share Plan</b>	VPs+	EPS, net income, revenue	150% maximum opportunity 50% threshold	Three year	· Compensation Committee approval
<b>Equity Controls</b>	Timing of grants, review of grants, limits on pledging/hedging				

For recent examples of compensation risk disclosures that were voluntarily provided by Microsoft and ev3, Inc. prior to the effective date of the new rules, please see Appendix A at the end of this paper.

## *Director Qualifications and Board Leadership*

The second area of focus in the SEC's enhanced disclosure rules is on the composition and structure of the Board of directors. The objectives of the rules are to improve transparency and facilitate accountability of the Board to shareholders. The new disclosure rules cover several topics, including:

- > Qualifications and experience of individual directors
- > Past directorships held by directors and nominees
- > Legal proceedings involving directors, nominees, and executive officers
- > Consideration of diversity in the overall composition of Board
- > Board leadership structure (including separation/combination of Chairman and CEO roles and a discussion of the lead director role, if applicable)

With respect to individual directors, companies now must disclose the director/nominee skills, attributes and experiences that led the Board to conclude s/he was qualified to serve as a director that year. (For a sample disclosure filed before the new rules became effective please see Parametric Technology disclosure in Appendix B).

This new requirement will potentially be of particular interest to the many technology and life sciences companies that are venture-backed and have Board seats occupied by representatives of the venture companies. While the presence of venture firm representatives on the Board does not signify a qualifications-disconnect, it does place a special emphasis on disclosure of the qualifications of current and nominated members, and discussion of go-forward plans, if any, to address any critical skills gaps. (See Appendix C for a sample director skills matrix).

In addition to qualifications details, the SEC is requiring disclosure of any directorship held by a director/nominee during the past five years, whether currently active or not. Companies should also consider reviewing the disclosed biographies of directors that serve on the Boards of other companies, as the SEC will likely review these bios for consistency.

The new rules also require disclosure of any legal proceedings in which the director/nominee is/was involved during the past 10 years (expanded from the current requirement, which looks back only five years). The definition of legal proceeding has also been expanded to include judicial/administrative proceedings resulting from mail or wire fraud, violations of financial laws (securities, insurance, etc), or any disciplinary sanctions/orders from a stock, commodities, derivatives, or self-regulatory organization.

Moving beyond the qualifications of individual directors, the SEC has also focused on increased disclosure of the leadership structure of the Board; specifically, it now requires a discussion of whether there are separate Chairman and CEO roles, as well as the role of a lead director. In response, companies and their Boards will need to annually review the Board leadership structure, document the results of that discussion, and disclose and discuss the Board's thinking on the appropriate leadership structure in the proxy statement.

While the SEC has not signaled a preference for one structure over another, investor and advisor groups have, with a clear bias toward the separation of the roles. This preference is reflected in the changes that have occurred at public company Boards; about 37% of the S&P 500 companies had split CEO and Chair roles last year, as compared to about 21% in 1999, according to Spencer Stuart's 2009 Board Index.

Nonetheless, the exercise in front of companies in disclosure is not one primarily of laying a path to split roles, rather it is one primarily of ensuring that the rationale for the current structure is strong and well-communicated, meaning that a clear line is drawn between the needs of the organization and how its leadership structure supports those needs. That said, the question of how independence is maintained within that structure should also be addressed; disclosure can, for example, include examples of demonstrated Board independence on given issues.

In cases where a lead director role exists, companies should focus on reporting the specific duties of the lead director that encourage independence, such as setting meeting agendas, holding the authority to call meetings of the independent directors and the ability to communicate directly with shareholders. (See Analog Devices discussion in Appendix D for a sample disclosure of Board leadership structure).

Finally, with respect to the Board, the SEC is also requiring additional disclosure on the role of the Board in managing enterprise level risk (e.g., investment risk, business risk, etc). Disclosure should focus on the company’s overall risk management philosophy and approach, and how risk management processes are communicated to, and managed, at the Board level. For those companies with risk management officers, disclosure will focus on the relationship between that officer and the Board. (See Covidien plc disclosure in Appendix E for a sample disclosure of one company’s Board-related risk oversight process).

*Compensation Consultants*

The third area of focus in the enhanced disclosure rules is the independence of compensation consultants. Over the past several years, investors and other governance groups have increasingly questioned the role of compensation consultants in determining executive pay. In particular, they suggest that inappropriate conflicts of interest may arise when a compensation consultant provides both executive and/or Board compensation consulting, and additional professional (HR, benefits, broad employee compensation, etc) services to a company. In response to these concerns, the SEC’s enhanced disclosure rules now require that companies provide more detailed disclosure of the nature of services rendered, the fees associated with them, and the respective roles of management and the Board in retaining the consultant.

In defining the particulars of this enhanced disclosure obligation, the SEC has struck a balance between the benefits of additional disclosure and the legitimate interests of both companies and consultants to preserve confidentiality on these issues. The new disclosure rules are triggered only for consultants providing both executive/Board compensation consulting *and* consulting on additional areas, and only if fees paid for the latter exceed a \$120,000 threshold. Figure 2 breaks down the disclosure triggers.

**Figure 2: Compensation Consultant Disclosure Triggers**

Compensation Consultant Reporting Relationship	Executive/Board Work Only	Executive/Board Work + “Additional Services”
Hired by Board	No disclosure	Fee disclosure <i>if</i> non-executive consulting fees exceed \$120,000 Additional disclosure around selection/qualification of consultant <sup>2</sup>
Hired by Management > When Board has independent consultant	No disclosure	No disclosure
Hired by Management > Board does <u>not</u> have independent consultant	No disclosure	Fee disclosure <i>if</i> non-executive consulting fees exceed \$120,000

In cases where disclosure is required, the aggregate fees for both the Board/executive compensation consulting and additional services must be reported. In effect, two figures will be reported: (1) the cumulative value of all executive and Board compensation consulting work; and (2) the aggregate fees paid for the various “additional services.” When fee disclosure is triggered, companies must also report whether management played any role in retaining or recommending the retention of the consultant, and whether the Board approved the additional (not executive- or Board-related) services.

Disclosure is not required in cases where the ‘consulting’ is confined to participation in a compensation consultant’s executive compensation survey, or where any executive compensation analysis is performed as part of a non-discriminatory, broad-based compensation consulting engagement.

### Summary Compensation Table (SCT)

The SEC did an about-face on the question of how equity awards are valued for the purpose of disclosure; going forward, the SCT will report aggregate equity amounts based on the face value (Black-Scholes for stock options) of the equity delivered in the year. This change applies to the reporting of equity for all prior periods shown in the effected tables (in both the SCT and the Directors Compensation Table).

The new rules can precipitate a change in the Named Executive Officer (NEO) list, and companies are allowed to have more than the standard five NEOs in order to preserve continuity of reporting from one year to the next. Companies should be aware however that if a new officer is added to the NEO list by virtue of this new reporting requirement, equity grant values must be reported as calculated under the fair value rule for the past three years.

With respect to performance-based awards, the SEC now requires the reporting of the target value of those awards in cases where the performance metrics were absolute (i.e., revenue, profit), and the probable value of those awards in cases where the performance metrics were relative (i.e., share price). Irrespective of the metric, maximum potential values will need to be reported in a footnote.

One other note with respect to the SCT: any foregone compensation must be reported, even if it was traded for equity, with a footnote explaining the reason for the trade.

### Proxy Advisors and Investors

While the recent economic decline ushered in additional disclosure requirements and tighter governance standards, it also presented opportunities for companies to increase the size of their equity pools. Companies both seized the opportunity and received shareholder support in doing so. (See Figure 3 below).

**Figure 3: 2009 Shareholder Voting Activity: Management Proposals**

Type of Proposal		2008		2009	
		Number of Proposals	Average "For" Vote	Number of Proposals	Average "For" Vote
<b>Management Proposals</b>					
<b>Equity Compensation Plans</b>	> RiskMetrics recommendations for	1,221	64%	<b>1,279</b>	<b>64%</b>
	> Proposal pass rate		99%		<b>99%</b>
<b>Repricings</b>	> RiskMetrics recommendations for	22	23%	<b>126</b>	<b>36%</b>
	> Proposal pass rate		64%		<b>88%</b>

Source: RiskMetrics Voting Analytics Database

While likely a one-year phenomenon, share reserves for new equity plans nonetheless increased some 50 percent in 2009 over 2008 levels, according to research conducted by RiskMetrics Group (RMG). The increase was more dramatic for existing plans, wherein pools increased by a factor of 2x-3x.

However, shareholders are also increasingly making their voices heard on key compensation issues, such as tax gross-ups, golden parachutes, Say-on-Pay, etc, many of which would had previously been viewed as unworthy of investor attention. See Figure 4 on the next page.

**Figure 4: 2009 Shareholder Voting Activity: Shareholder Proposals**

Type of Proposal		2008		2009	
		Number of Proposals	Average "For" Vote	Number of Proposals	Average "For" Vote
<b>Shareholder Proposals</b>					
<b>Executive Compensation</b>	> Say-on-Pay	73	42%	<b>76</b>	<b>46%</b>
	> Vote on Golden Parachutes	5	51%	<b>7</b>	<b>36%</b>
	> Anti-gross ups	4	46%	<b>2</b>	<b>51%</b>
	> Retention period for stock awards	-	-	<b>16</b>	<b>25%</b>
	> Death benefits	-	-	<b>12</b>	<b>36%</b>

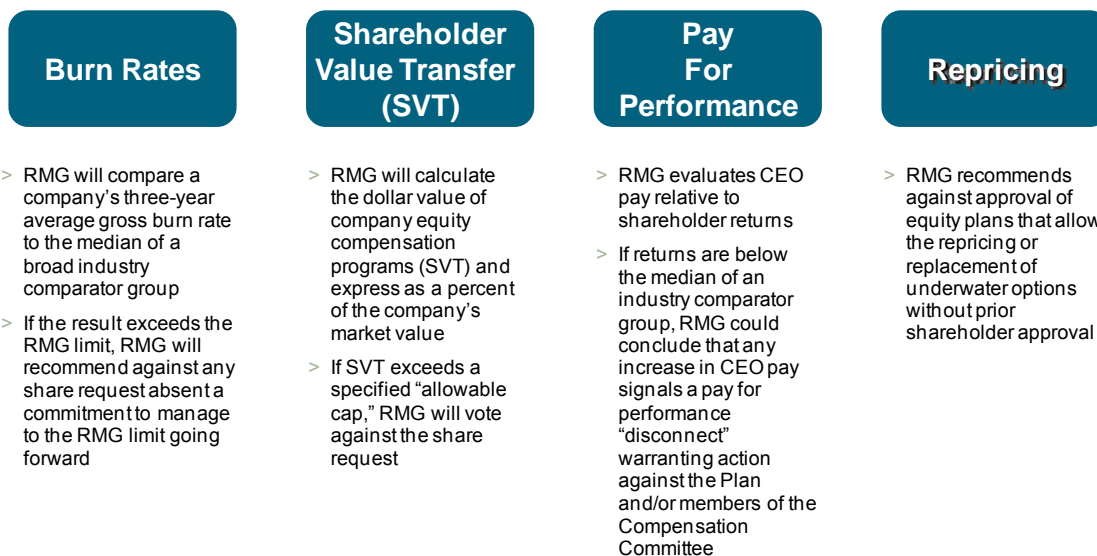
Source: RiskMetrics Voting Analytics Database

*Risk Metrics Policy Updates*

Within the context of increased shareholder involvement and SEC disclosure requirements, and broad public scrutiny, RMG updated the policies it follows in analyzing and providing vote recommendations on key executive compensation and governance issues. (For a detailed discussion of these policy changes, please see Radford Alert, "Risk Metrics Group Updates Annual Proxy Voting Policies and Processes for 2010 for Key Compensation Matters," from November, 2009, at [www.radford.com/home/press\\_room/index.asp](http://www.radford.com/home/press_room/index.asp)).

With respect to its view on equity plans, RMG will apply a four-part test to new equity plans or proposals to add shares in an existing plan, as detailed in Figure 5 below.

**Figure 5: RMG Four-Pronged Equity Plan Test**



Burn rate and SVT limits are detailed in Appendices F and G below. The new burn rate limits likely came as an unwelcome surprise for many companies, as they represent a meaningful drop in many cases, in particular for Russell 3000 companies. RMG did provide some measure of relief however by allowing companies to manage to the higher of either the 2010 burn rate limits or the three-year (2012) limits.

RMG introduced other key changes to its policies for 2010, signaling an increase in the scrutiny it will place on executive compensation issues. In many respects, these new policies are a consolidation and restatement of many years of policies regarding executive pay. And in many respects they anticipate, and coalesce with the steady march toward investor Say-on-Pay. In brief, the advisor group will be evaluating company practices against standards for:

- > Pay and performance alignment
- > Avoidance of “failure pay” practices (long-term contracts, guaranteed compensation, excessive severance)
- > Compensation Committee independence and effectiveness
- > Clarity and completeness of disclosure
- > Reasonable Board pay

RMG also modified its pay/performance alignment methodology. In 2009 and before, RMG looked for disconnects based on one-year CEO pay changes relative to one- and three-year shareholder returns; beginning in 2010, RMG will look at five-year shareholder return performance, within in the context of CEO pay changes over the five years. This represents a more holistic view and perhaps a somewhat more generous yardstick; however, the group is expected to be much more aggressive in applying repercussions (in the form of “against” vote recommendations) in cases of pay/performance misalignment.

More broadly, RMG has introduced policy changes for what it calls “problematic pay practices.” (See Appendix H for details on those practices). Of special note to many technology and life sciences companies are severance practices highlighted by RMG, in particular single trigger severance and 280G gross up payments. According to recent Radford research, about 70% of life sciences and one-half to two-thirds of technology companies provide 280G gross-up payments to CEOs. Meanwhile single-trigger equity payments are made to CEOs at about one-third of technology companies and between 40% and 50% of life sciences companies. The trend is moving away from both of these practices, and this added scrutiny by RMG is likely to accelerate that process.

In any event, where RMG detects a problematic pay practice it will likely vote against management on pay ratification measures, and vote against the Compensation Committee and/or the full Board in companies where no Say-on-Pay vote is on the ballot.

## **Legislative Update**

### *Say-on-Pay*

Most observers predicted that Say-on-Pay would be mandated for US public companies in 2010, and that did not come to pass. However, two Say-on-Pay bills are currently circulating through Congress, and adoption of some kind of legislation governing shareholder say on compensation is expected within the next year. Both bills have similar aims, namely mandating Say-on-Pay, shareholder approval of golden parachutes, Compensation Committee independence, compensation consultant independence and fee disclosure. The Senate bill goes a step further, requiring a discussion and graphical representation of the connection between executive pay and five-year firm performance, adoption of clawbacks with three-year lookbacks, majority election of directors, annual Board elections and discussion of Chairman/CEO structure.

The outcome of this proposed legislation is uncertain; however, in the meantime, companies are increasingly moving toward voluntary adoption of Say-on-Pay provisions. (See Appendix I for a list of technology and life sciences companies that have done so.) Thus far, these companies largely have not experienced significant investor push-back on compensation plans; five of the six companies for which there are data received greater than 90% approval from shareholders of their compensation plans.

That said, we are still in the early days of investor engagement in pay and governance decisions. The historical trend has been for ever-greater exercise of “say” over time, and it is reasonable to expect that shareholders will increasingly scrutinize the issues on which they vote.

## **Key Takeaways**

The bar for clear and complete communication of pay and governance practices has been raised, as has the bar for acceptable governance and pay practices. More than ever, it is incumbent upon companies to clearly articulate their policies and the rationale behind those policies. There is, for example, less willingness on the part of the SEC to accept a company’s claim that disclosing performance metrics will constitute competitive harm, as there is less willingness on the part of shareholders and proxy advisors to accept pay/performance disconnects and certain types of severance/change-in-control practices like single triggers, tax gross-ups and vesting acceleration.

While the CD&A and other key reporting sections of the proxy discussed in this article rely largely on principles-based reporting practices, the fog commonly intrinsic in principles-based reporting has lifted significantly. When viewed in the aggregate, policy and regulation change, as well as legislative activity in the past year have painted a relatively clear picture with respect to the obligation of companies to manage risk, to clearly and fully disclose key compensation and governance practices, and to allow greater shareholder engagement in compensation and governance policy.

The newest and perhaps most complicated new wrinkle in 2010 reporting – compensation risk management – will perhaps present the greatest opportunity for confusion when it comes to disclosure. But this is not because risk management – both enterprise and compensation-related – has not been of issue in corporate Boards. In 2008, 11% of the S&P 500 Boards reported that risk was a subject of intense focus; that figure rose to 50% in 2009 (Spencer Stuart, 2009). Rather, the hurdle will be one of how to develop adequate risk analysis and reporting processes, and how to work the findings of those analyses into ongoing development of increasingly transparent pay practices.

## Appendix A – Sample Compensation Risk Disclosures

Microsoft (2010)

	<ul style="list-style-type: none"> <li>&gt; <u>Assessment of Risk</u></li> <li>&gt; By design our compensation program for executive officers does not incentivize excessive risk taking. Our base salary component of compensation does not encourage risk-taking because it is a fixed amount. The current Incentive Plan awards have the following risk-limiting characteristics:</li> </ul>
<b>Capped Payouts</b>	<ul style="list-style-type: none"> <li>→ - Awards to each executive officer are limited by the terms of the Incentive Plan to a fixed maximum specified in the Plan or a fixed percentage of an incentive pool, and Mr. Ballmer's awards are further limited to 200% of his base salary;</li> <li>- Awards are made based on a review of a variety of indicators of performance, thus diversifying the risk associated with any single indicator of performance;</li> <li>- Awards are not made in the form of stock options, which may provide an asymmetrical incentive to take unnecessary risks to increase Company stock price;</li> <li>- Incentive Plan awards are not tied to formulas that could focus executives on specific short-term outcomes;</li> </ul>
<b>Committee Oversight</b>	<ul style="list-style-type: none"> <li>→ - Members of the Compensation Committee, or in the case of Mr. Ballmer, the independent members of the Board, approve the final Incentive Plan awards in their discretion, after the review of executive and corporate performance;</li> </ul>
<b>Clawbacks</b>	<ul style="list-style-type: none"> <li>→ - Incentive Plan awards are subject to the Executive Compensation Recovery Policy, described on page 26;</li> </ul>
<b>Long-Term Focus</b>	<ul style="list-style-type: none"> <li>→ - For executive officers other than Mr. Ballmer (who is a significant Microsoft shareholder), the majority of the award value is delivered in the form of stock that vests over a multiple of years, which aligns the interests of executive officers to long-term shareholder interests; and</li> </ul>
<b>Ownership Guidelines</b>	<ul style="list-style-type: none"> <li>→ - Executive officers are subject to our executive stock ownership and holding guidelines, described on pages 26 and 27</li> </ul>

eV3, Inc (2009)

	<ul style="list-style-type: none"> <li>&gt; <u>Consideration of Risk and Recoupment Policy</u></li> <li>&gt; ...we specifically analyze whether there is excessive pressure on our management to meet financial targets set up by our Board of Directors, such as too high a percentage of executives' compensation tied to sales targets and profitability incentives, and whether management's personal financial situation is threatened by our financial performance arising from significant portions of their compensation, such as annual bonuses and equity compensation, being contingent upon achieving aggressive targets for stock price, operating results, financial position or cash flow.</li> <li>&gt; ...our compensation committee believes that our executive incentive compensation arrangements do not encourage our executives to take unnecessary or excessive risks that could threaten the value of our company. While performance-based compensation constitutes a significant percentage of our executives' overall total compensation and thereby the compensation committee believes motivates our executives to help fulfill our corporate mission and vision, including specific and focused company performance objectives, the non-performance based compensation, for most executives for most years, is also a sufficiently high percentage of overall total compensation that the compensation committee does not believe that unnecessary or excessive risk taking is encouraged by the performance-based compensation. In addition, a significant portion of executives' performance-based compensation is in the form of long-term equity incentives which do not encourage unnecessary or excessive risk because they generally vest over a three to four year period of time thereby focusing the executives on our company's long-term interests.</li> </ul>
<b>Long-Term Focus</b>	<ul style="list-style-type: none"> <li>→</li> </ul>
<b>Clawbacks</b>	<ul style="list-style-type: none"> <li>→ &gt; Nonetheless, our compensation committee determined that it was prudent to review and adopt certain compensation practices that discourage unnecessary or excessive risk taking, such as a recoupment or "clawback" policy.</li> </ul>
<b>Committee Oversight</b>	<ul style="list-style-type: none"> <li>→ &gt; As a matter of best practice, we will continue to monitor our executive compensation program to ensure that it continues to align the interest of our executives with those of our long-term stockholders while avoiding unnecessary or excessive risk.</li> </ul>

## Appendix B – Sample Director/Nominee Qualifications Disclosures

### Parametric Technology (2010)

<ul style="list-style-type: none"> <li>&gt; Mr. Schechter and Mr. Lacy were elected to the Board of Directors effective in September and December of 2009, respectively, as a result of our search for two new directors. The Nominating &amp; Corporate Governance Committee selected each of Mr. Schechter and Mr. Lacy after an extensive search process conducted with the assistance of a professional search firm retained by the Committee.</li> <li>&gt; <b>The search firm used the criteria provided by the Committee, which included financial expertise and technology industry experience, to identify potential candidates. Members of the Committee, the Board and the PTC executive team met with each of the candidates selected by the Committee to assess whether the candidate would be a valuable addition to the Board.</b> Upon conclusion of the process, the Committee nominated each of Mr. Schechter and Mr. Lacy for election to the Board.             <ul style="list-style-type: none"> <li>- <b>The nomination of Mr. Schechter was based on his leadership experience as Chairman and Chief Executive Officer of NMS Communications Corporation, his strength in the area of business strategy, his knowledge of and experience in the technology market, and his financial acumen.</b> Earlier in his career, Mr. Schechter was a Partner at Coopers &amp; Lybrand LLP, an accounting firm.</li> <li>- <b>The nomination of Mr. Lacy was based on his legal and financial background, his experience as President and as Chief Financial Officer of Kronos Incorporated, his experience transforming Kronos from a small hardware company to a large global enterprise software company, and his international experience.</b></li> <li>- Professor Porter has served on the PTC Board since 1995. <b>The nomination of Professor Porter for re-election was based on his credentials and expertise in the areas of business and corporate strategy and international competitiveness, his contributions as a member of the Corporate Development Committee and of the Board of Directors as a whole, and his expected future contributions.</b></li> </ul> </li> </ul>
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## Appendix C – Sample Director Skills Matrix

Area(s) of Expertise	Board Member 1	Board Member 2	Board Member 3	Board Member 4	Board Member 5
Senior Leadership Expertise	■	■			
Business Development/M&A Expertise		■		■	
Financial Expertise	■		■		■
Public Board Expertise			■		
Advisory/Strategic Planning Expertise			■		■
Diversity		■			■
Independence	■	■		■	■
Operational/Mfg Expertise		■		■	
Global Expertise		■		■	
Technology/Science Expertise	■		■		
Human Capital Expertise				■	■

## Appendix D – Sample Board Leadership Structure Discussion

Analog Devices (2009)

- > **Board Leadership Structure**
- > We separate the roles of CEO and Chairman of the Board in recognition of the differences between the two roles. The CEO is responsible for setting the strategic direction for the Company and the day to day leadership and performance of the Company, while the Chairman of the Board provides guidance to the CEO and sets the agenda for Board meetings and presides over meetings of the full Board.
- > Because Mr. Stata, our Chairman, is an employee of the Company and is therefore not “independent,” our Board of Directors has appointed the Chairman of our Nominating and Corporate Governance Committee, John Doyle, as “presiding director” to preside at all executive sessions of “non-management” directors, as defined under the rules of the NYSE. The Board generally holds executive sessions twice a year.

## Appendix E – Sample Risk Oversight Discussion

Covidien Plc (2010)

- > **Risk Oversight**
- > Our Board of Directors oversees an enterprise-wide approach to risk management, designed to support the achievement of organizational objectives, including strategic objectives, to improve long-term organizational performance and enhance shareholder value. A fundamental part of risk management is not only understanding the risks a company faces and what steps management is taking to manage those risks, but also understanding what level of risk is appropriate for the company. The involvement of the full Board of Directors in setting the Company's business strategy is a key part of its assessment of management's appetite for risk and also a determination of what constitutes an appropriate level of risk for the Company. **The full Board of Directors participates in an annual enterprise risk management assessment, which is led by the Company's general counsel. In this process, risk is assessed throughout the business, focusing on three primary areas of risk: financial risk, legal/compliance risk and operational/strategic risk.**
- > **While the Board of Directors has the ultimate oversight responsibility for the risk management process, various committees of the Board also have responsibility for risk management.** In particular, the Audit Committee focuses on financial risk, including internal controls, and receives an annual risk assessment report from the Company's internal auditors. The Company's Compliance Committee assists the Board of Directors in fulfilling its oversight responsibility with respect to regulatory, healthcare compliance and public policy issues that affect the Company and works closely with the Company's legal and regulatory groups. In addition, in setting compensation, the Compensation Committee strives to create incentives that encourage a level of risk-taking behavior consistent with the Company's business strategy. Finally, the Company's Nominating and Governance Committee conducts an annual assessment of the risk management process and reports its findings to the Board.

## Appendix F – RMG Burn Rate Limits for Technology and Life Sciences Companies

Burn Rate	Industry	Russell 3000			Non-Russell 3000		
		RMG Limit		Change	RMG Limit		Change
		2009	2010		2009	2010	
<b>Life Sciences</b>							
	Pharmaceuticals and Biotechnology	5.76%	5.16%	▼	9.46%	8.58%	▼
	Health Care Equipment and Services	4.39%	3.65%	▼	6.64%	7.92%	▲
<b>Technology</b>							
	Software/Services	6.76%	5.47%	▼	10.12%	7.58%	▼
	Hardware	5.52%	4.79%	▼	6.30%	7.08%	▲
	Semiconductors	5.72%	4.82%	▼	7.79%	7.31%	▼

## Appendix G – RMG Shareholder Value Transfer Limits

SVT	Industry	2010 SVT Limits
	<b>Life Sciences</b>	
	Pharmaceuticals and Biotechnology (GICS 3520)	10% to 18%
	Health Care Equipment and Services (GICS 3510)	6% to 14%
<b>Technology</b>		
	Software/Services (GICS 4510)	12% to 20%
	Hardware (GICS 4520)	8% to 14%
	Semiconductors (GICS 4530)	10% to 18%

## Appendix H – RMG Problematic Pay Practices

Category	Problematic Pay Practices
> Employment Contracts	<ul style="list-style-type: none"> <li>&gt; Multi-year guarantees (that is, beyond first year of employment) of salary increase, bonus payment, or equity compensation</li> <li>&gt; Severance payment &gt; 3x base + bonus</li> <li>&gt; <b>Single trigger severance provisions</b></li> <li>&gt; <b>New or materially amended contracts with “modified single triggers”</b></li> <li>&gt; <b>New or materially modified contracts with 280G gross-ups</b> <ul style="list-style-type: none"> <li>- Change in CEO's <u>one-year</u> pay levels</li> <li>- In context of <u>one- and three-year</u> total shareholder returns</li> </ul> </li> </ul>
> Specific Elements of Pay	<ul style="list-style-type: none"> <li>&gt; SERP payouts including additional years of service; inclusion of equity awards in pension calculation</li> <li>&gt; Perquisites for former/retired executives</li> <li>&gt; Perquisite-related tax gross-ups</li> </ul>
> Other Practices	<ul style="list-style-type: none"> <li>&gt; Executive use of company stock in hedging activities</li> <li>&gt; Repricing without shareholder approval (includes cash buyouts of underwater options)</li> <li>&gt; <b>Guaranteed bonuses</b>, single metrics for long- or short-term incentive plans, lucrative severance packages, high pay relative to industry peers, disproportionate supplemental pensions, mega equity grants</li> <li>&gt; Mitigating factors include clawback provisions and stock ownership/retention guidelines</li> </ul>

## Appendix I – Say-on-Pay Early Adopters’ First Year Vote Results

Technology/Life Sciences Companies	
Company	Date of First Vote
Forest Labs	2009 (97%)
Intel	2009 (96%)
Logitech	2009 (97%)
Microsoft	2009 (99%) Triennial vote
Motorola	2009 (64%)
Par Pharmaceutical	2009 (93%)
Tech Data	2009 (not disclosed)
Apple	2010
Intuit	2010
Pfizer	2010 (biennial)
Hewlett-Packard	2011 (proposed)

## Contact Us

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## Locations

Atlanta, Austin,  
Boston, Chicago,  
Denver, Hong Kong,  
London, New York,  
Philadelphia, San  
Diego, San Francisco,  
San Jose,  
Washington, DC.

### Edward J. Speidel

Senior Vice President

Ed has nearly 20 years of experience in executive and equity compensation, corporate governance and employee benefits consulting. His clientele consists of companies of varying size and complexity, in a wide array of industries. He maintains a strong focus on the high technology communities, with emphasis in e-commerce, semiconductors, software, and life sciences firms. Prior to joining Radford, Ed was principal and national executive compensation practice leader for Mellon Human Resources & Investor Solutions (formerly Buck Consultants). Before Mellon, Ed was managing director of the Northeast compensation practice for PricewaterhouseCoopers. Ed earned a bachelor of arts in economics/government from University of Delaware, a master of business administration from Lehigh University, a juris doctorate from New England Law, and a master of laws in taxation from Boston University School of Law. In addition, he is a certified compensation; benefits; and equity professional, respectively. Ed writes and speaks frequently on executive and equity compensation issues. He is based in Boston.

### Ram Kumar

Assistant Vice President

Ram has nearly 10 years of experience in the governance and compensation industry. He is primarily focused on helping companies evaluate and resolve compensation plan design issues in the context of emerging standards of corporate governance and the perspectives of investors and proxy advisors. Prior to joining Radford, Ram was an assistant vice president in the executive compensation practice of Aon Consulting. Prior to Aon, Ram worked in the corporate governance industry for more than six years, including four years at the prominent proxy advisory firm, Institutional Shareholder Services (ISS). While at ISS, he led the US research group charged with analyzing all public US companies and making proxy recommendations to institutional investors. Ram earned a bachelor of arts from Johns Hopkins University. He is based in New York.

## About Radford

For more than 35 years, Radford has provided compensation market intelligence to the technology and life sciences industries. Global survey databases, which include 3.6 million incumbents, offer current, reliable data to nearly 2,000+ clients. Leveraging Radford survey data, our thought-leading global Radford Consulting team creates tailored solutions for the toughest global business and compensation challenges facing companies at all stages of development. In addition to our consulting team, we also offer equity valuation assistance via Radford Valuation Services, and leading-edge market analyses and survey services with Radford Analytic Services. Radford's suite of surveys includes the Global Technology, Life Sciences, and Sales Surveys, as well as the US Benefits Survey. For more information on Radford, please visit <http://www.radford.com/>.

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