



# **“Tackling Your 2008 Compensation Disclosures: The 2<sup>nd</sup> Annual Proxy Disclosure Conference”**

Michael S. Kesner, Principal  
Deloitte Consulting LLP

Scott Spector, Partner  
Fenwick & West, LLP

October 9, 2007

# Summary of Findings – Dow Jones Index Companies

- Reviewed proxies of Dow Jones Industrial Companies
- 27 of the 30 companies among the Dow Jones Industrials have filed under the new SEC rules
- 23 companies used a tabular format
  - 7 of these provided totals
- The following companies provided complete termination payment disclosure in easy to read tabular form:
  - American Express
  - Boeing
  - Caterpillar
  - Honeywell
  - Merck
  - IBM
  - Pfizer

# Summary of Findings - Tech Companies

- Reviewed proxies of 25 Bay Area Technology Companies
- 15 of the 25 companies among the Bay Area Technology Company group have filed under the new SEC Rules
- 8 companies used a tabular format
  - 2 of these provided totals
- Of this group, the following companies provided complete termination payment disclosure in easy to read tabular form:
  - Atmel
  - Cadence
  - National Semiconductor

# Summary of Findings - CIC Disclosures

## Dow Jones Companies

- 16 companies (59%) have no CIC plans or agreements
- 9 companies (33%) do not accelerate vesting of equity upon CIC,
- 12 companies (44%) do not provide severance for non-CIC terminations
- 9 companies (33%) disclosed single trigger vesting of equity upon a CIC
- 13 companies (48%) reported the value of accelerated options equaled the intrinsic value

## Tech Companies

- 5 companies (33%) have no CIC plans or agreements
- 2 companies (13%) do not accelerate vesting of equity upon CIC,
- 8 companies (50%) do not provide severance for non-CIC terminations
- 5 companies (33%) disclosed single trigger vesting of equity upon a CIC
- 13 companies (81%) reported the value of accelerated options equaled the intrinsic value

## Summary of Findings - Termination Events

### Dow Jones Companies

- The highest number of termination events reported:
  - 6 (Boeing, Verizon, Coca-Cola)
- The next highest number of termination events reported:
  - 5 (American Express, Honeywell, and DuPont)
- 16 companies (59%) disclosed payments upon death
- 14 companies (52%) disclosed payments for disability

### Tech Companies

- The highest number of termination events reported:
  - 6 (AMD and National Semiconductor)
- The next highest number of termination events reported:
  - 5 (Cadence and Atmel)
- 6 companies (40%) disclosed payments upon death
- 5 companies (33%) disclosed payments for disability

# Proxy Disclosure of Termination Payments - Presentation

Dow Jones Companies	Tabular Presentation	Totals Shown
3M		
Alcoa	✓	✓
Altria	✓	
AIG	✓	✓
American Express	✓	✓
AT&T	✓	
The Boeing Company	✓	✓
Caterpillar	✓	
Citigroup		
Coca Cola	✓	
E.I. DuPont de Nemours	✓	
Exxon Mobil Corp.		
General Electric	✓	
General Motors	✓	✓
Intel	✓	

# Proxy Disclosure of Termination Payments - Presentation

Dow Companies	Tabular Presentation	Totals Shown
Home Depot	✓	
Honeywell	✓	✓
Merck	✓	✓
McDonalds	✓	✓
JPMorgan Chase	✓	
IBM	✓	
Johnson & Johnson		
Pfizer	✓	
Proctor & Gamble	✓	
United Technologies	✓	
Verizon	✓	
Wal Mart	✓	
<b>TOTALS</b>	<b>23</b>	<b>8</b>

# Proxy Disclosure of Termination Payments - Presentation

Tech Companies	Tabular Presentation	Totals Shown
Advanced Micro Devices	✓	
Atmel	✓	
Autodesk	✓	
Cadence	✓	✓
Cypress	NA	
Genetech	NA	
Google	NA	
Juniper	✓	
National Semiconductor	✓	
Network Appliance	NA	
Nvidia		

# Proxy Disclosure of Termination Payments - Presentation

Tech Companies	Tabular Presentation	Totals Shown
Salesforce.com		
Sybase	✓	✓
Yahoo		
<b>TOTALS</b>	<b>7</b>	<b>2</b>

# Proxy Disclosure of Termination Payments

## Companies without special termination payments

Dow Companies	No CIC Agreements	No Executive Severance	No Accelerated Equity Vesting for CIC
3M			
Alcoa			
Altria	✓	✓	
AIG	✓		✓
AT&T			
The Boeing Company			
Caterpillar	✓	✓	
Citigroup	✓	✓	
Coca Cola	✓	✓	
E.I. DuPont de Nemours	✓	✓	✓
Exxon Mobil Corp	✓	✓	✓
General Electric	✓	✓	✓
General Motors	✓	✓	
Intel	✓	✓	✓

# Proxy Disclosure of Termination Payments

## Companies without special termination payments

Dow Companies	No CIC Agreements	No Executive Severance	No Accelerated Equity Vesting for CIC
Home Depot	✓		
Honeywell			
Merck			
McDonalds			
JPMorgan Chase	✓		✓
IBM	✓	✓	✓
Johnson & Johnson	✓	✓	✓
Pfizer			
Proctor & Gamble	✓	✓	
United Technologies			
Verizon			✓
Wal Mart	✓		✓
<b>TOTALS</b>	<b>16</b>	<b>12</b>	<b>10</b>

# Proxy Disclosure of Termination Payments

## Companies without special termination payments

Tech Companies	No CIC Agreements	No Executive Severance	No Accelerated Equity Vesting for CIC
Advanced Micro Devices			
Atmel			
Autodesk			
Cadence			
Cypress	✓	✓	✓
Genentech	✓	✓	✓
Google	✓	✓	
Juniper			
National Semiconductor		✓	
Network Appliance	✓	✓	
Nvidia	✓	✓	

# Proxy Disclosure of Termination Payments

## Companies without special termination payments

Tech Companies	No CIC Agreements	No Executive Severance	No Accelerated Equity Vesting for CIC
Salesforce.com		✓	
Sybase			
Yahoo		✓	
<b>Totals</b>	<b>5</b>	<b>8</b>	<b>2</b>

## Reasons Disclosed for CIC Policies

- 7 companies (out of 11 that provide severance or accelerated vesting of equity upon a CIC) in the Dow Jones group explained the reason for the policy.
- Most of the companies provided only one or two sentences to explain the rationale for their policy
- Companies that only had accelerated vesting of equity provisions typically did not the rationale for acceleration. These companies simply noted that the equity plan provided accelerated vesting upon CIC.
- Merck provided the most in-depth explanation of the reasons behind their termination policies which is included in this report.

# SEC Comment Letters on Termination Payments

Based on a review of a sampling of SEC comment letters, companies have been asked to:

- “Disclose why vesting of equity awards is accelerated under various triggering events”
- “Explain how the appropriate payment and benefit levels are determined...”
- “Please discuss why you have chosen to pay certain multiples of the components of compensation...”
- “Please distill this information into concise disclosure of the material concepts...and present your disclosure in a fashion that is readily understandable.”

## SEC Comment Letters on Termination Payments

- “Please discuss how these arrangements fit into your overall compensation objectives and affect the decisions you made regarding other compensation elements.”
- “Please add a table.”
- “Please define ‘cause,’ ‘good reason’, and ‘without cause.’”
- “Please explain why you pay severance for a termination for poor performance.”

# Proxy Examples

## Example

American Express Co - Potential Payments Upon Termination or Change-in-Control

Potential Payments Upon Termination of Employment/CIC as of 12/31/06					
K.I. Chenault					
	Death	Disability	Voluntary Resignation (Retirement)	Termination w/o Cause not in Connection with CIC	Termination w/o Cause or Constructive Term. in Connection with CIC
<i>Incremental Benefits Due to Termination Event</i>					
Severance (1)	\$ 0	\$ 0	\$ 0	\$ 26,953,180	\$ 26,953,180
Pro Rata Bonus (2)	\$ 12,376,590	\$ 12,376,590	\$ 12,376,590	\$ 0	\$ 9,640,997
Value of Accelerated LTIA (3)	\$ 43,576,753	\$ 43,576,753	\$ 12,370,550	\$ 49,220,510	\$ 44,005,920
Deferred Compensation (4)	\$ 0	\$ 0	\$ 0	\$ 5,393,596	\$ 4,259,515
Incentive Savings Plan (5)	\$ 0	\$ 0	\$ 0	\$ 430,599	\$ 0
Retirement Plan (6)	\$ 0	\$ 147,225	\$ 0	\$ 486,165	\$ 2,156,254
Other Benefits (7)	\$ 1,500,000	\$ 255,634	\$ 255,634	\$ 389,621	\$ 283,986
Gross-Up on Excise Taxes (8)	n/a	n/a	n/a	n/a	\$ 22,102,506
<i>Total Value of Incremental Benefits</i>	\$ 57,453,343	\$ 56,356,202	\$ 25,002,773	\$ 82,873,671	\$ 109,402,357

Potential Payments Upon Termination of Employment/CIC as of 12/31/06					
G.L. Crittenden					
	Death	Disability	Voluntary Resignation	Termination w/o Cause not in Connection with CIC	Termination w/o Cause or Constructive Term. in Connection with CIC
<i>Incremental Benefits Due to Termination Event</i>					
Severance (1)	\$ 0	\$ 0	\$ 0	\$ 8,399,399	\$ 8,399,399
Pro Rata Bonus (2)	\$ 3,624,699	\$ 3,624,699	\$ 0	\$ 0	\$ 2,534,850
Value of Accelerated LTIA (3)	\$ 12,741,134	\$ 12,741,134	\$ 0	\$ 9,577,640	\$ 12,881,134
Deferred Compensation (4)	\$ 1,178,635	\$ 1,178,635	\$ 0	\$ 1,474,505	\$ 2,137,311
Incentive Savings Plan (5)	\$ 0	\$ 0	\$ 0	\$ 63,772	\$ 0
Retirement Plan (6)	\$ 0	\$ 119,813	\$ 0	\$ 50,753	\$ 482,965
Other Benefits (7)	\$ 1,500,000	\$ 0	\$ 0	\$ 57,234	\$ 126,850
Gross-Up on Excise Taxes (8)	n/a	n/a	n/a	n/a	\$ 9,153,543
<i>Total Value of Incremental Benefits</i>	\$ 19,044,469	\$ 17,664,282	\$ 0	\$ 19,623,302	\$ 35,716,051

Potential Payments Upon Termination of Employment/CIC as of 12/31/06					
E.P. Gilligan					
	Death	Disability	Voluntary Resignation	Termination w/o Cause not in Connection with CIC	Termination w/o Cause or Constructive Term. in Connection with CIC
<i>Incremental Benefits Due to Termination Event</i>					
Severance (1)	\$ 0	\$ 0	\$ 0	\$ 8,136,981	\$ 8,136,981
Pro Rata Bonus (2)	\$ 3,493,490	\$ 3,493,490	\$ 0	\$ 0	\$ 2,469,245
Value of Accelerated LTIA (3)	\$ 12,317,270	\$ 12,317,270	\$ 0	\$ 9,100,372	\$ 12,455,375
Deferred Compensation (4)	\$ 180,098	\$ 214,016	\$ 0	\$ 524,691	\$ 565,617
Incentive Savings Plan (5)	\$ 0	\$ 0	\$ 0	\$ 143,248	\$ 0
Retirement Plan (6)	\$ 0	\$ 206,198	\$ 0	\$ 111,330	\$ 650,958
Other Benefits (7)	\$ 1,500,000	\$ 0	\$ 0	\$ 57,170	\$ 110,401
Gross-Up on Excise Taxes (8)	n/a	n/a	n/a	n/a	\$ 6,763,046
<i>Total Value of Incremental Benefits</i>	\$ 17,490,858	\$ 16,230,974	\$ 0	\$ 18,073,791	\$ 31,151,623

[Table of Contents](#)

Potential Payments Upon Termination of Employment/CIC as of 12/31/06					
A.F. Kelly, Jr.					
	Death	Disability	Voluntary Resignation	Termination w/o Cause not in Connection with CIC	Termination w/o Cause or Constructive Term. in Connection with CIC
<i>Incremental Benefits Due to Termination Event</i>					
Severance (1)	\$ 0	\$ 0	\$ 0	\$ 8,735,844	\$ 8,735,844
Pro Rata Bonus (2)	\$ 3,792,922	\$ 3,792,922	\$ 0	\$ 0	\$ 2,793,961
Value of Accelerated LTIA (3)	\$ 13,842,942	\$ 13,842,942	\$ 0	\$ 10,509,344	\$ 13,982,942
Deferred Compensation (4)	\$ 466,836	\$ 793,804	\$ 0	\$ 539,644	\$ 972,202
Incentive Savings Plan (5)	\$ 0	\$ 0	\$ 0	\$ 138,833	\$ 0
Retirement Plan (6)	\$ 0	\$ 179,769	\$ 0	\$ 106,380	\$ 502,311
Other Benefits (7)	\$ 1,500,000	\$ 0	\$ 0	\$ 60,272	\$ 111,782
Gross-Up on Excise Taxes (8)	n/a	n/a	n/a	n/a	\$ 8,096,173
<i>Total Value of Incremental Benefits</i>	\$ 19,602,700	\$ 18,609,437	\$ 0	\$ 20,090,317	\$ 35,195,215

Potential Payments Upon Termination of Employment/CIC as of 12/31/06					
L.M. Parent					
	Death	Disability	Voluntary Resignation (Retirement)	Termination w/o Cause not in Connection with CIC	Termination w/o Cause or Constructive Term. in Connection with CIC
<i>Incremental Benefits Due to Termination Event</i>					
Severance (1)	\$ 0	\$ 0	\$ 0	\$ 4,407,763	\$ 4,407,763
Pro Rata Bonus (2)	\$ 1,703,882	\$ 1,703,882	\$ 1,703,882	\$ 0	\$ 1,401,941
Value of Accelerated LTIA (3)	\$ 7,993,564	\$ 7,993,564	\$ 2,380,941	\$ 8,455,085	\$ 8,091,722
Deferred Compensation (4)	\$ 0	\$ 0	\$ 0	\$ 1,115,617	\$ 1,030,827
Incentive Savings Plan (5)	\$ 0	\$ 0	\$ 0	\$ 262,401	\$ 0
Retirement Plan (6)	\$ 0	\$ 142,428	\$ 0	\$ 170,583	\$ 352,621
Other Benefits (7)	\$ 1,500,000	\$ 245,358	\$ 245,358	\$ 349,137	\$ 270,228
Gross-Up on Excise Taxes (8)	n/a	n/a	n/a	n/a	\$ 0
<i>Total Value of Incremental Benefits</i>	\$ 11,197,446	\$ 10,085,232	\$ 4,330,180	\$ 14,760,587	\$ 15,555,102

(1) *Severance*. Reflects two times current base salary plus two times cash AIA awarded for 2005 performance plus two times the value of RSAs/LOIs issued in recognition of 2005 performance (and as an incentive for future performance).

(2) *Pro Rata Bonus*.

Under Death, Disability and Retirement: Reflects cash AIA awarded for 2005 performance plus the value of RSAs/LOIs issued in recognition of 2005 performance (and as an incentive for future performance).

Under Change in Control: Reflects the average of the value awarded in 2006 for 2005 performance and the value awarded in 2005 for 2004 performance (cash AIA plus the value of RSAs/LOIs issued in recognition of performance and as an incentive for future performance).

(3) *Value of Accelerated LTIA*. For stock options, reflects the acceleration of “in the money” stock options.

## Table of Contents

(4) *Deferred Compensation.*

executives.

Under Death: Reflects vesting of the unvested interest for non-retiree eligible

Under Disability: Reflects vesting of the unvested interest for non-retiree eligible executives and additional interest crediting on the account until paid.

Under Involuntary Termination: Reflects two years of interest crediting plus the portion of the account balance that continues to vest during the two year severance period.

Under Change in Control: Reflects two years of interest crediting plus the vesting of the unvested portion of the account balance.

(5) *Incentive Savings Plan.* Under Involuntary Termination: Reflects two years of interest on account balances.

(6) *Retirement Plan.*

Under Disability: Reflects value of future accruals assuming executive elects to retire at age 65.

Under Involuntary Termination: Reflects two years of interest on account balances.

Under Change in Control: Reflects crediting two years of age and service under the SRP.

(7) *Other Benefits.*

Outplacement

Under Involuntary Termination and Change in Control: Reflects an estimated value of \$11,000.

Health and Welfare Continuation

Under Involuntary Termination and Change in Control: Reflects continuation of medical, dental and Health Savings Account contributions over the two year severance period.

Perquisite Allowance

Under Involuntary Termination: Reflects continuation of flexible cash allowance of \$35,000 for one year.

Key Life Surrender Value

Under Death: Reflects the benefit under the Key Executive Life Insurance Plan payable to the beneficiary.

Under Disability, Retirement and Involuntary Termination: Reflects the cash surrender value under the Key Executive Life Insurance Plan if the NEO is retirement eligible.

Under Change in Control: Reflects the cash surrender value under the Key Executive Life Insurance Plan.

(8) *Gross-Up on Excise Taxes.* Calculations to estimate the excise tax due under 280G are complex and reflect a number of assumptions. We assume that a change in control occurred on December 31, 2006 at a stock price of \$60.67 and that each executive's employment is terminated. We also assume certain performance outcomes for AIA and PG, along with assumptions about interest and tax rates.

The following is a summary of the various termination scenarios and how potential payments are determined.

*Death.*

In the event of the death of an NEO:

- a pro rata portion of the AIA for the year of death, based on the amount of the NEO's prior year's AIA, is paid to the NEO's designated beneficiary or estate;
- the NEO's options, RSAs and LOIs become 100% vested, and options remain exercisable for five years (but not to exceed their original ten-year term);
- a pro rata portion (based on a 38-month vesting period) of the NEO's outstanding PG awards are paid to the NEO's designated beneficiary or estate;
- if the NEO is not already retirement eligible (at least age 55 with ten or more actual or deemed years of service to the Company), all earnings at the ROE rate on the NEO's balance under our deferred compensation programs become 100% vested;
- the total balance of the NEO's account under our deferred compensation programs is paid to the NEO's designated beneficiary or estate in a lump sum;
- the NEO's benefits under our Incentive Savings Plan and our Retirement Plan become 100% vested; and
- the NEO's designated beneficiary receives the coverage amount under our Key Executive Life Insurance Plan (and the Company is entitled to receive any excess cash value under the life insurance policy on the NEO).

*Disability.*

Disability generally means the inability to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months. For purposes of the Retirement Plan, disability generally means a physical or mental condition that renders the participant eligible for disability benefits under the federal Social Security Act.

In the event of the disability of an NEO:

- a pro rata portion of the AIA for the year of disability, based on the amount of the NEO's prior year's AIA, is paid to the NEO;
- the NEO's options, RSAs and LOIs become 100% vested, and options remain exercisable for five years (but not to exceed their original ten-year term);
- a pro rata portion (based on a 38-month vesting period) of the NEO's outstanding PG awards are paid to the NEO;
- if the NEO is not already retirement eligible (at least age 55 with ten or more actual or deemed years of service to the Company), all earnings at the ROE rate on the NEO's balance under our deferred compensation programs become 100% vested;
- the NEO's account balance under our deferred compensation programs is paid at the time and in the form (lump sum or installments) elected by the NEO;
- the NEO's benefits under our Incentive Savings Plan and our Retirement Plan become 100% vested;
- the NEO continues to accrue benefits under our Retirement Plan, based on the NEO's prior year compensation, through the NEO's normal retirement date (or earlier recovery from the disability or withdrawal of plan benefits); and
- if the NEO is retirement eligible, then the NEO is entitled to receive the cash surrender value of the life insurance policy on the NEO under our Key Executive Life Insurance Plan.

*Voluntary Resignation.*

The effects of a voluntary resignation by an NEO depend on whether the NEO is retirement eligible at the time of resignation. Retirement eligible means that the NEO is at least age 55 with ten or more actual or deemed years of service to the Company.

If an NEO is retirement eligible, then in the event of the voluntary resignation by the NEO:

- if the retirement occurs on or after April 1st of the year, then a pro rata portion of the AIA for the year of retirement, based on the amount of the NEO's prior year's AIA, is paid to the NEO;
- the NEO's unvested options granted before January 2005 are forfeited; for options granted beginning January 2005, 50% of unvested shares that are outstanding for more than one year vest according to their original schedule and the remaining shares are forfeited; vested options and options which become vested upon retirement remain exercisable until the end of their original ten-year term;
- the NEO's RSAs and LOIs that have been outstanding for more than two years vest in full, and those that have been outstanding for two years or less are forfeited;
- a pro rata portion (based on a 38-month vesting period) of the NEO's PG awards that have been outstanding for more than one year are paid to the NEO (on the normal payment date for such PG awards), and the NEO's PG awards that have been outstanding for one year or less are forfeited;
- the NEO's account balance under our deferred compensation programs is paid at the time and in the form (lump sum or installments) elected by the NEO; and
- the NEO is entitled to receive the cash surrender value of the life insurance policy on the NEO under our Key Executive Life Insurance Plan.

If an NEO is not retirement eligible, then in the event of the voluntary resignation by the NEO:

- the NEO's AIA for the year of resignation is forfeited;
- the NEO's options (vested and unvested), RSAs and LOIs are forfeited;
- the NEO's outstanding PG awards are canceled; and
- the NEO's account balance under our deferred compensation programs is paid in a lump sum – amounts that were earned and vested prior to December 31, 2004 are paid at the time of termination and all other amounts are paid on a date at least six months following the date of termination.

*Termination w/o Cause not in Connection w/ CIC.*

In the event of the termination without cause of an NEO, which is not in connection with a CIC:

- the NEO is entitled to receive separation pay of two years' annual compensation, which includes base salary and the amount of the last AIA paid, and separation pay is paid in installments over the two-year separation period;
- the NEO's AIA for the year of termination is forfeited;
- the NEO's options continue to vest and remain exercisable during the NEO's severance period, and are canceled on the earlier of their expiration date, the end of the NEO's severance period or the NEO's commencement of other employment;
- the NEO's RSAs and LOIs continue to vest during the NEO's severance period, and are canceled on the earlier of the end of the NEO's severance period or the NEO's commencement of other employment;
- the NEO's PG awards that remain outstanding at the end of the NEO's severance period are canceled;
- if the NEO is retirement eligible (at least age 55 with ten or more actual or deemed years of service to the Company), then the NEO's account balance under our deferred compensation programs is paid at the time and in the form (lump sum or installments) elected by the NEO; otherwise the NEO's account balance is paid in a lump sum – amounts that were earned and vested prior to December 31, 2004 are paid at the end of the two-year severance period and all other amounts are paid on a date at least six months following the date of termination;
- the NEO's account balances under our Incentive Savings Plan cannot be distributed until the end of the two-year severance period and continue to receive investment gains and losses during such period;
- the NEO's account balances under our Retirement Plan cannot be distributed until the end of the two-year severance period and continue to receive interest crediting under the terms of the plan during such period;
- the NEO is entitled to U.S. medical, dental and health savings account contributions for up to two years, generally on the same basis as prior to termination;
- the NEO is entitled to receive the perquisite allowance for the year of termination;
- the NEO is entitled to receive outplacement services; and
- if the NEO is retirement eligible, then the NEO is entitled to receive the cash surrender value of the life insurance policy on the NEO under our Key Executive Life Insurance Plan.

*Termination w/o Cause in Connection w/ CIC.*

In the event of the termination without cause of an NEO, which is in connection with a CIC:

- the NEO is entitled to receive separation pay of two years' annual compensation, which includes base salary and the amount of the last AIA paid, and separation pay is paid in a lump sum on a date at least six months following the date of termination;
- a pro rata portion of the AIA for the year of termination, based on the amount of the NEO's two prior years' AIAs, is paid to the NEO;
- the NEO's options, RSAs and LOIs become 100% vested upon the CIC, and options remain exercisable for 90 days following termination; and for retirement eligible executives, 50% of unvested options granted after January 2005 that are outstanding for more than one year become vested and remain exercisable for the original option term;
- a pro rata portion (based on a 36-month vesting period) of the NEO's outstanding PG awards, based on performance through the date of termination, are paid to the NEO;
- upon the occurrence of a CIC, if the NEO is not already retirement eligible, all earnings at the ROE rate on the NEO's balance under our deferred compensation programs become 100% vested;
- two years of additional interest (using the prior year's interest rate) are credited to the NEO's account under our deferred compensation programs;
- the NEO's account balance under our deferred compensation programs is paid in a lump sum – amounts that were earned and vested prior to December 31, 2004 are paid at the time of termination and all other amounts are paid on a date at least six months following the date of termination;
- if the termination is during the first year following the CIC, then the NEO is credited with two additional years of age and years of service for purposes of the NEO's Retirement Plan-related account under our Supplemental Retirement Plan; if the termination is during the second year following the CIC, then the NEO is credited with one additional year of age and year of service;

#### Table of Contents

- the NEO is entitled to U.S. medical, dental and health savings account contributions for up to two years, generally on the same basis as prior to termination;
- the NEO is entitled to receive outplacement services;
- the NEO is entitled to receive the cash surrender value of the life insurance policy on the NEO under our Key Executive Life Insurance Plan; and
- in the event that certain payments and benefits received by the NEO are treated as “excess parachute payments” for federal income tax purposes, and as a result the NEO is subject to excise tax on such benefits, then the NEO is entitled to receive a “tax gross-up payment” that puts the NEO in the same economic position he or she would have been in had such excise tax not applied.

## Example

Cadence Design Systems, Inc. – Potential Payments Upon Termination or Change in Control

The specific terms of each employment agreement and offer letter are described in more detail following the tables below. The tables below set forth the estimated value of the potential payments to each Named Executive Officer, assuming the executive's employment had terminated on December 30, 2006, and, for purposes of the second table below, that a change in control of Cadence had also occurred on that date. Amounts are reported without any reduction for possible delay in the commencement or timing of payments.

**Potential Payments and Benefits Upon a Termination of Employment by Cadence Without Cause or by Executive in Connection with a Constructive Termination or for Good Reason Not in Connection with a Change in Control**

Name	Transition Period Salary (\$)	Termination Payment (Salary) (\$)	Termination Payment Bonus (\$)	Company-Paid COBRA (\$)	Vesting of Stock Options (\$)(1)	Vesting of Restricted Stock Awards (\$)(2)	Pre-Tax Total (\$)
Michael J. Fister	24,000	1,800,000	1,800,000	13,659	7,112,625	5,820,732	16,571,016
Kevin Bushby	24,000	500,000	650,000	4,071	91,881	1,363,166	2,633,118
Moshe Gavrielov	—	400,000	400,000	18,154	509,087	626,850	1,954,091
James S. Miller, Jr.(3)	—	—	—	—	—	—	—
William Porter	24,000	450,000	450,000	18,154	237,766	1,343,250	2,523,170

- (1) These amounts are calculated assuming that the market price per share of Cadence's common stock on the date of termination of employment was equal to the closing price of Cadence's common stock on December 29, 2006 (\$17.91) and are based upon the difference between \$17.91 and the exercise price of the options held by the Named Executive Officer.
- (2) These amounts are calculated assuming that the market price per share of Cadence's common stock on the date of termination of employment was equal to the closing price of Cadence's common stock on December 29, 2006 (\$17.91).
- (3) Mr. Miller entered into an employment agreement with Cadence effective as of February 15, 2007 and was therefore not entitled to any payments upon termination as of December 30, 2006.

**Potential Payments and Benefits Upon a Termination of Employment by Cadence Without Cause or by Executive in Connection with a Constructive Termination for Good Reason Within 3 Months Prior to or 13 Months Following a Change in Control**

Name	Transition Period Salary (\$)	Termination Payment (Salary) (\$)	Termination Payment Bonus (\$)	Company-Paid COBRA (\$)	Vesting of Stock Options (\$)(1)	Vesting of Restricted Stock Awards (\$)(2)	Pre-Tax Total (\$)(4)
Michael J. Fister	24,000	2,000,000	2,000,000	13,659	7,484,521	8,059,482	19,581,662
Kevin Bushby	24,000	500,000	650,000	4,071	181,906	2,169,116	3,529,093
Moshe Gavrielov	—	400,000	400,000	18,154	509,087	626,850	1,954,091
James S. Miller, Jr.(3)	—	—	—	—	—	—	—
William Porter	24,000	450,000	450,000	18,154	538,641	3,059,637	4,540,432

- (1) These amounts are calculated assuming that the market price per share of Cadence's common stock on the date of termination of employment was equal to the closing price of Cadence's common stock on December 29, 2006 (\$17.91) and are based upon the difference between \$17.91 and the exercise price of the options held by the Named Executive Officer.

[Table of Contents](#)

- (2) These amounts are calculated assuming that the market price per share of Cadence's common stock on the date of termination of employment was equal to the closing price of Cadence's common stock on December 29, 2006 (\$17.91).
- (3) Mr. Miller entered into an employment agreement with Cadence effective as of February 15, 2007 and was therefore not entitled to any payments upon termination as of December 30, 2006.
- (4) Assuming a base amount under Section 280G of the Code based on taxable wages for the years 2002 through 2006 and annualized for the year in which the executive commenced employment with Cadence (if after 2001), none of the payments to the Named Executive Officers set forth in this table would be subject to the excise tax under Section 4999 of the Code.

Separate and apart from the employment agreements and offer letter described above, the award agreements governing the shares of restricted Cadence common stock granted to each of the Named Executive Officers generally provide that if the Named Executive Officer to whom the restricted stock has been granted dies while employed by Cadence, that portion of the restricted stock award that would have vested on the next following vesting date will be deemed to have vested immediately prior to the affected executive's death. In addition, the agreement governing the 600,000 shares of restricted Cadence common stock granted to Mr. Fister in connection with the commencement of his employment with Cadence provides for full vesting acceleration upon a termination of Mr. Fister's employment by reason of his death or permanent and total disability (as determined in accordance with Cadence's applicable personnel policies). The tables below set forth the estimated value of the potential payments to each Named Executive Officer, assuming the executive's employment had terminated on December 30, 2006 by reason of the executive's death or disability. Amounts are reported without any reduction for possible delay in the commencement or timing of payments.

**Potential Payments and Benefits Upon a Termination of Employment by Reason of  
Death or Disability**

Name	Vesting of Restricted Stock Awards Upon Executive's Death (\$)(1)	Vesting of Restricted Stock Awards Upon Executive's Disability (\$)
Michael J. Fister	4,701,357	3,581,982
Kevin Bushby	1,363,166	—
Moshe Gavrielov	626,850	—
James S. Miller, Jr.	895,500	—
William Porter	1,343,250	—

- (1) These amounts are calculated assuming that the market price per share of Cadence's common stock on the date of termination of employment was equal to the closing price of Cadence's common stock on December 29, 2006 (\$17.91).

**EMPLOYMENT AGREEMENT WITH MICHAEL J. FISTER**

Effective as of May 12, 2004, Cadence entered into an employment agreement with Mr. Fister. The agreement provides for Mr. Fister's employment as President and Chief Executive Officer of Cadence at an initial base salary of \$800,000 per year and for Mr. Fister to participate in Cadence's Senior Executive Bonus Plan at an annual target bonus of 100% of his base salary, with a guaranteed bonus for fiscal 2004 equal to the amount of his base salary prorated for the portion of fiscal 2004 that Mr. Fister was employed by Cadence. Mr. Fister's base salary and target bonus are subject to review by the Board or the Compensation Committee from time to time and the Board or Compensation Committee may choose, in its discretion, to approve a bonus payment in excess of 100% of Mr. Fister's base salary for any fiscal year. In 2005, the Compensation Committee increased Mr. Fister's base salary to \$1,000,000. In addition, the agreement provides for a sign-on bonus of \$1,000,000, a \$5,000 per month housing allowance for 24 months and other reasonable and actual relocation expenses agreed to by Cadence. The agreement also provides for Mr. Fister to be reimbursed for the reasonable and actual cost of moving his household goods and personal items to the San Jose, California area incurred during the first two years of Mr. Fister's employment with Cadence. If, during the first five years of Mr. Fister's employment with Cadence, Mr. Fister sells his house in

## Example

Merck & Co Inc. – Explanation of Change in Control Policy

*Change in Control.* The Board adopted the Change in Control Separation Benefits Plan in 2004. The Board adopted the plan as part of its ongoing, periodic review of the Company's compensation and benefits programs and in recognition of the importance to the Company and its shareholders of avoiding the distraction and loss of key management personnel that may occur in connection with rumored or actual fundamental corporate changes. A properly designed change in control program protects shareholder interests by enhancing employee focus during rumored or actual change in control activity through:

- Incentives to remain with company despite uncertainties while a transaction is under consideration or pending;
- Assurance of severance and benefits for terminated employees; and
- Access to equity components of total compensation after a change in control.

Merck stock options, RSUs and PSUs generally vest upon a change in control, either in whole or in part (as fully described under *Change in Control* beginning on page 54). The remainder of benefits generally requires a change in control, followed by a termination of an executive's employment. In adopting the so-called "single" trigger treatment for equity vehicles, the Company was guided by three principles:

- *Be consistent with current market practice among pharmaceutical peers.* All but one of the Peer Companies have change in control protection and all provide for single trigger equity vesting.
- *Keep employees relatively whole for a reasonable period but avoid creating a "windfall."*
  - Single trigger vesting ensures that ongoing employees are treated the same as terminated employees with respect to outstanding equity grants.
  - Single trigger vesting provides employees with the same opportunities as shareholders, who are free to sell their equity at the time of the change in control event and thereby realize the value created at the time of the deal.

### Table of Contents

- The Company that made the original equity grant will no longer exist after a change in control and employees should not be required to have the fate of their outstanding equity tied to the new company's future success.
- Single trigger vesting on performance-contingent equity, in particular, is appropriate given the difficulty of replicating the underlying performance goals.
- *Support the compelling business need to retain key employees during uncertain times.*
  - A single trigger on equity vesting can be a powerful retention device during change in control discussions, especially for more senior executives where equity represents a significant portion of their total pay package.
  - A double trigger on equity provides no certainty of what will happen when the transaction closes.

As shown under *Change in Control* beginning on page 54, the Company will provide gross-ups for the Named Executive Officers from any taxes due under Section 4999 of the Code. The effects of Section 4999 generally are unpredictable and can have widely divergent and unexpected effects based on an executive's personal compensation history. Therefore, to provide an equal level of benefit across individuals without regard to the effect of the excise tax, the Company determined that 4999 gross up payments are appropriate for the Company's most senior level executives.