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Timely “Best Practice” Disclosures for Your Compensation Discussion and Analysis

The 2009 proxy season promises to be a turning point for Compensation Discussion and Analysis and for executive pay practices in general, as rising public anger over compensation practices will focus all eyes on what companies are doing to address the growing list of concerns. In many cases, companies are grappling with unprecedented financial and economic pressures while, at the same time, their “pay for performance” programs are being fully tested. This confluence of forces occurs against a backdrop of regulatory changes in Washington, as Congress enacts legislation targeting executive compensation at companies accepting bailout funds and will likely soon take up legislation mandating an advisory vote on executive compensation.

In our January-February 2008 issue, we provided examples of “best practice” disclosures that addressed areas of concern raised by the Staff in its review of executive compensation disclosures. We are revisiting some of those examples in light of the credit crisis and economic concerns, as well as recent and expected regulatory efforts. We are also now addressing areas that have become critical concerns in the past few months and must be addressed in upcoming CD&A disclosures. While there is no “one size fits all” approach that can work for your CD&A, we hope that these examples provide critical guidance on analyses that will be expected this proxy season—and beyond.

Implementing “Hold Through Retirement” for Equity Awards

Our September-October and November-December 2008 issues described why companies should be implementing a hold-through-retirement policy for senior executives as a means for not only addressing shareholders’ valid concerns about executive compensation, but also for avoiding the creation of incentives that lead to unnecessary and excessive risks. [For a discussion of implementing a hold-through-retirement policy in the context of conducting a risk analysis of compensation programs, see the model disclosure included in the Winter 2009 issue of our *Proxy Disclosure Updates* newsletter.]

Best Practice Disclosure:

Our Hold-Through-Retirement Policy

We have long recognized the importance of stock ownership as an important means of closely aligning the interests of our senior executive officers with the interests of the company’s shareholders. As discussed on page ___ of this Compensation Discussion and Analysis under the heading “Stock Ownership Requirements” we have required that our senior executives maintain “skin in the game” with the substantial stock ownership guideline ratios of 12 times salary for our CEO and six times salary for our other named executive officers.

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This substantial stock ownership guideline alone, however, does not ensure that the interests of our senior executives are fully aligned with our shareholders' interests. While stock ownership—through both compliance with the stock ownership guidelines and through accumulation of equity awards under our compensation programs—encourages a focus on returns to shareholders through the company's stock price, that focus may, in some instances, overemphasize short-term rather than long-term returns. Without a countervailing influence, the large proportion of stock ownership—coupled with the potential for a short-term focus—could lead senior executive officers to pursue strategies that involve unnecessary or excessive risks for the company as a whole, and for the other shareholders who have a long-term investment view. The risks attendant to a short-term focus on stock price may be particularly acute in times when share prices are substantially depressed, such as we have experienced in recent months.

In 2008, the Compensation Committee considered alternatives for addressing these concerns, in particular focusing on ways to better align our executives' interests with the interests of shareholders while at the same time emphasizing to the markets in these difficult economic times that our executive team is committed to a long-term focus. At the same time, the Compensation Committee has considered ways to address the concern that our compensation programs—including our equity grants and our stock ownership guidelines—may encourage unnecessary or excessive risk-taking by the executive team.

The Compensation Committee considered implementing a policy to require that our senior executive officers (including the CEO and all of the named executive officers) hold a substantial portion of their earned equity awards until the executives retire from service with the company. The Compensation Committee recognized that this policy would address many of the concerns discussed above, however a requirement to hold a substantial portion of the equity awards only until retirement could result in executives losing their long-term focus in the critical period immediately prior to retirement, when the executive is likely to have the most influence and would likely be in a position to make significant decisions for the company. In this regard, implementing a policy requiring that a portion of the equity awards be held only until retirement could have the potential to cause an executive close to retirement to promote unnecessary or excessive risk taking, as the executive seeks to maximize the short-term stock price return to the detriment of long-term value. This potential risk may be particularly acute in periods such as we are facing today, where stock prices are depressed and executives may feel pressure to maximize the value of their retirement holdings by seeking to offset losses on broader market investments.

After performing the foregoing analysis and recognizing the potential limitations of a hold-until-retirement policy, the Compensation Committee has decided to implement a mandatory "hold-through-retirement" policy for the senior executive officers. Under this policy, the company will require that these executives hold 75% of the net after-tax portion of the op-

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erating after retirement or other termination of employment from the company, or until age 65, whichever is later. In addition, we require that 50% of our restricted stock awards do not vest until ten years from grant or two years after retirement, whichever is later. We believe that this policy most effectively addresses the possibility that our executives will unduly focus on short-term, unsustainable stock price increases that could lead to executives prematurely "cash[ing] out" of a significant portion of their equity holdings. Under this policy,

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equity compensation for the subject executives will remain a motivational force throughout their careers to promote the long term value of the company.

We are pleased to announce that our CEO and our named executive officers have also agreed to subject their already-owned, previously granted option stock and restricted stock to this new hold-through-retirement policy, thereby demonstrating their long-term commitment to the company and its shareholders.

Revisiting Perquisites

Recent economic and financial pressures are driving most companies to review every aspect of their budget—and layoffs and significant cutbacks are being experienced across the board. When a company is laying off a substantial portion of its work force or is cutting back on research and development, it becomes increasingly more difficult to justify the “need” for expensive perquisites as an element of compensation when fundamental business needs cannot be met. These heightened cost concerns come at a time when perquisites are increasingly being cut back, and federal legislation and investment policies are targeting the use or misuse by companies accepting bailout money. Given these fundamental shifts in attitude, this may be the year when many companies are compelled to “clean house” with respect to their perquisites.

Best Practices Disclosure:

Reassessment of Our Perquisites

We have provided our CEO and the other named executive officers with several perquisites, including the personal use of company aircraft and automobiles, company-paid financial planning services and country club memberships. These perquisites have historically been offered as a means of providing additional compensation to the CEO and other named executive officers through the availability of benefits that provide convenience in light of the extraordinary demands on our executive officers’ time. The Compensation Committee reviews the Company’s policies with respect to perquisites on a regular basis to consider whether the perquisites should be maintained and whether, and to what extent, it may be appropriate for the Company to discontinue particular perquisites or to require repayment of the cost of perquisites.

As described in our “Management’s Discussion and Analysis of Results of Operations and Financial Condition” in our annual report on Form 10-K, we have faced an increasingly difficult business environment as economic conditions have deteriorated while, at the same time, financing options have become limited. Given the impact on our results of operations and financial condition, the Company has implemented significant cost cutting measures that are designed to reinforce the long term strength of the Company. These measures have included reducing the number of employees, cutting back investments in a number of significant business lines and reducing costs at all operating levels.

In light of these ongoing cost concerns, the Compensation Committee has determined to eliminate the perquisites available to the CEO and the named executive officers, including the personal use of corporate aircraft. While the Compensation Committee considered providing

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for reimbursement of the costs of perquisites instead of eliminating perquisites all together. It was determined that the continued maintenance of perquisites in light of the overall cost-cutting efforts of the company would not be appropriate from the perspectives of various stakeholders, including employees and shareholders.

In determining to eliminate perquisites, the Compensation Committee considered the negative consequences from an incentive standpoint, given the perquisites' status as a component of our executive compensation program, but determined that the overall compensatory impact of eliminating perquisites is not substantial. The Compensation Committee does not believe that the elimination of perquisites will put the Company at a competitive disadvantage for the purposes of attracting or retaining executive talent, when considered in the context of the overall compensation program.

Making the Most of Clawback Provisions

Clawback policies (and such provisions in executive compensation arrangements) are being adopted with increasing frequency, as companies seek to ensure that executives are not in a position to keep compensation that was awarded based on what later turns out to be erroneous financial results. Section 304 of the Sarbanes-Oxley Act originally focused significant attention on clawback policies, and now the presence of broader clawback provisions as part of the TARP has reignited interest in clawbacks as an effective means for discouraging inappropriate conduct. In the current climate, even those companies that have already adopted clawback policies and provisions need to re-evaluate those measures, because the triggering events may be too narrow and fail to deal with circumstances where it turns out—after compensation decisions have been made—that the executive has engaged in conduct which ultimately harms the company and shareholders.

Revisiting our Compensation Recovery Policy

In 2006, the Board of Directors adopted a Compensation Recovery Policy, pursuant to which members of management (including the CEO, the CFO and the NEOs) may be required to return compensation paid based on financial results that were later restated. This policy applied only if the executive officers engaged in misconduct that contributed to the need for a restatement, or contributed to the use of inaccurate metrics in the calculation of incentive compensation. Under this policy, when the Board determined in its sole discretion that recovery of compensation was appropriate, the Company could require reimbursement of all or a portion of any bonus, incentive payment, commission, equity-based award or other compensation, to the fullest extent permitted by law.

In addition to this Compensation Recovery Policy, the Company's executive officers and other key employees have agreed to voluntarily return to the Company the forfeiture of proceeds from some or all of their termination of employment arrangements if they are involved in conduct that is material to the Company's customers, confidential information, or the Company's reputation.

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for the critical days ahead.**

In light of the risk assessment undertaken by the Compensation Committee discussed on page ___ of this Compensation Discussion and Analysis, the Compensation Committee has

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reconsidered the Company's Compensation Recovery Policy, seeking to ensure that the policy maximizes the ability of the Company to recoup compensation obtained through actions on the part of management which may ultimately prove detrimental to the Company and its shareholders. In this regard, the Compensation Committee has determined that limiting the possibility of recovery only to instances of misconduct resulting in restatement of financial results, or to certain post-termination activities, does not fully reflect the principle of potential activities which should result in a return of compensation to the company.

Based on the Compensation Committee's recommendation, the Board of Directors has adopted a revised Compensation Recovery Policy that provides for the recovery of any annual or long-term incentive compensation paid to our executives and directors in the instance where payout or vesting has been deferred (1) where recovery is necessary to reflect the longer-term results of their performance, which may not be fully known or understood immediately following the completion of the performance period, or (2) in the event that the executive subsequently engage in conduct that is detrimental to the company. Conduct considered detrimental to the Company may include, but is not limited to, the need for a restatement of results, a significant financial loss, actions, decisions or strategies that were not in the company's long-term best interests or other reputational harm to the Company. This revised policy requires reimbursement of all or a portion of any bonus, incentive payment, commission, equity-based award or other compensation that is determined by the Compensation Committee to be recoverable, to the fullest extent permitted by law, as a result of the detrimental conduct. We believe that the Compensation Recovery Policy should be sufficiently broad to allow our Compensation Committee, in its sole discretion, to address situations where executives pursued strategies and took actions that (e.g., as a result of excessive risk-taking or poor performance or what, in hindsight, were bad or flawed strategies) should not have been rewarded.

In order to ensure the enforceability of the revised Compensation Recovery Policy, appropriate language regarding the policy is to be inserted in applicable documents and award agreements. In addition, notwithstanding any current employment agreements, the board and the CEO and our management team view this as so fundamental that we are pleased to report that our CEO and NEOs have agreed to the application of these new provisions retroactively.

Evaluating the Need for Pensions and SERPs

In our January-February 2008 issue, we addressed the importance of a wealth accumulation analysis and walk-away numbers in analyzing termination and change-in-control arrangements, in particular when assessing the need for matching those arrangements. A wealth accumulation analysis and walk-away numbers are also important in assessing the continued "need" for pension and supplemental executive retirement plans for the CEO and the other named executive officers.

Our Review and Analysis of Pensions and SERPs

We provide retirement benefits to the named executive officers through both qualified and non-qualified defined-benefit and defined-contribution retirement plans. We have historically viewed our retirement benefits as a means of providing financial security to all of our salaried employees after they have spent a substantial portion of their careers with the Company. While many companies today do not provide retirement benefits in the form of a pension or

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supplemental retirement plan. We believe that pensions and similar retirement benefits remain an important part of the overall compensation approach in our industry. Our named executive officers participate in several retirement plans, including benefits that are available to all of our employees such as the Section 401(k) Savings Plan and the tax-qualified Pension Plan, as well as the Supplemental Executive Retirement Plan ("SERP"). The SERP allows executives to accrue a higher benefit than the qualified pension plan, but it vests more slowly than the pension plan. We have historically maintained the SERP as a means for attracting and retaining executive talent.

These retirement plans create significant ongoing obligations for the Company in terms of funding and administration costs. As our workforce ages, the Company could face increasing costs in the future in order to satisfy obligations under these programs. With respect to our senior executives, the Compensation Committee has, in light of these cost concerns and in reconsidering the elements of compensation, undertaken a wealth accumulation analysis, examining the total amounts that the named executive officers are entitled to receive under all of the Company's compensation programs. The following table summarizes the total accumulated wealth values as of the end of the fiscal year and projected values over the next five years and ten years for each of the named executive officers.

[Editor's Note: Includes a table summarizing, for each named executive officer, the aggregate realized and unrealized value of previously granted and projected equity awards, deferred compensation balances, pension amounts, supplemental retirement benefits and other

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benefits achieved under the SERP did not provide sufficient incentives to the named executive officers in light of the wealth that they had already accumulated, and there was thus no basis to continue increasing the costs and obligations associated with the SERP. The Compensation Committee decided to maintain the Pension Plan, but to end participation in the SERP in some circumstances such as crediting additional years of service upon the achievement of certain specified milestones. The Compensation Committee recognized that the Company's pension plan provided for some financial security which, in current economic times in particular, serves to help retain our executive talent; however, the Compensation Committee will continue to monitor the feasibility of maintaining the Company's retirement benefits for the named executive officers going forward.

Tax Implications

In our January-February 2008 issue, we provided "best practice" disclosure for addressing compliance with Internal Revenue Code Section 162(m). The Emergency Economic Stabilization Act of 2008 (the "EESA") and the US Treasury's Capital Purchase Program (the "CPP") brought Section 162(m) guidance to the forefront again, with a requirement that any participating institution agree, as a condition to participate in the CPP, that it will be subject to the \$500,000 annual deduction limit under Section 162(m)(5). Section 162(m)(5), which was added by Section 302 of the EESA, reduces the deduction threshold for the remuneration paid to senior executive officers during any taxable year from \$1 million to \$500,000, and it also eliminates the exception to the deduction limit for "performance-based compensation" as well as deferred compensation.

When the SEC's specific mandate to address the applicability of Section 162(m) in Executive Compensation Disclosure was nullified in favor of principles-based disclosure, it seems that in some cases companies just decided to drop the Section 162(m) disclosure entirely (presumably concluding that it was no longer material), and those that have decided to initiate a fully developing disclosure. (Readers should be reminded that the SEC in the adopting release for the 2006 amendments stated that the new approach "should not be construed to eliminate this [162(m)] discussion" as well as other "tax consequences to the named executive officers as well as tax consequences to the company.") Given the flexibility afforded by the rules, however, a financial institution subject to the new 30% AGI deductibility limit imposed in the HRA that chooses, nevertheless, to pay more, may (incorrectly) conclude that it does not have to disclose this fact in its proxy statement. We believe that this information is material for all companies, especially given the current economic climate—and needs to be disclosed in the CD&A—otherwise shareholders will have no idea if the boards of their companies are complying with the applicable restrictions or purposefully going outside of them. Companies should provide a separate captioned section addressing Section 162(m), which must be an actual disclosure of any amounts that exceeded the cap and a conclusion that the board considered it and nevertheless decided to exceed the deductibility limits. Companies also need to make clear that the forgone deduction is a real cost to the company.

Deductibility of Compensation for Tax Purposes

Section 162(m) of the Internal Revenue Code generally disallows a tax deduction to public corporations for compensation over \$1,000,000 paid for any fiscal year to the firm's five highest paid executive officers, however, the statute exempts qualifying performance-based compensation from the deduction limit when specified requirements are met.

In general the Compensation Committee has structured awards to executive officers under the Company's incentive programs to qualify for this exemption. However, the Compensation Committee retains the discretion to award compensation that exceeds Section 162(m)'s deductibility limit.

In fiscal 2008, the Company's compensation to the CEO, the CFO and the President

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resulting in a cost to the company of \$_____, while the President's income exceed the limit by \$_____ costing the company \$_____ due to the lost tax deduction. The aggregate cost of the Compensation Committee's decision to exceed the Section 162(m) deductibility limit in fiscal 2008 was \$_____.

The Compensation Committee believed in the past that these amounts, including the cost of the lost tax deduction, were justifiable in order to be competitive with peer companies. As part of our overall review of executive compensation in light of the current difficult economic environment and the fact that it has been necessary to lay off employees in these difficult times, the Compensation Committee has now concluded that it is not appropriate to exceed the limit. We are pleased to report that our CEO and NEOs have agreed to reductions in their compensation to remain under the IRS limit. There was no increase in qualifying "performance-based compensation" to offset these reductions.

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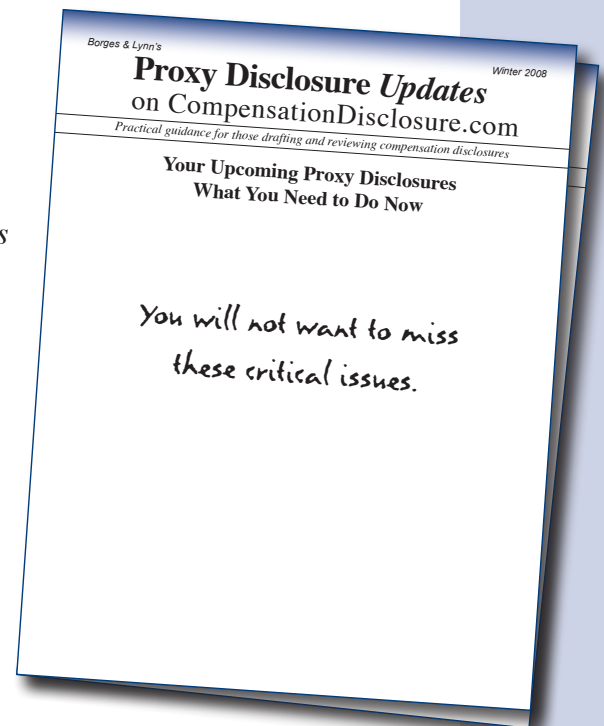
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