

MAYER • BROWN

# Preparing for the 2016 Proxy Season

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# Introduction and Overview

- Speakers
  - Laura Richman
  - Mike Hermsen
  - Jen Carlson
  - Harry Beaudry

# Agenda

- The impact of say-on-pay
- The SEC's final pay ratio disclosure rule
- The SEC proposals for clawback listing standards, pay versus performance disclosure and hedging disclosure
- Proxy access and other shareholder proposals
- Director and officer questionnaires
- Other annual meeting and annual reporting matters

## Say-on-Pay Statistics

- Average vote in 2015 for Russell 3000 companies was 91% in favor
- 54 Russell 3000 companies (2.7%) failed say on pay in 2015
- 91% of Russell 3000 companies had say-on-pay pass in all 5 years
- ISS negative recommendation generally lowers support but does not necessarily result in a failed vote

Source: Semler Brossy, *2015 Say on Pay Results*, September 28, 2015

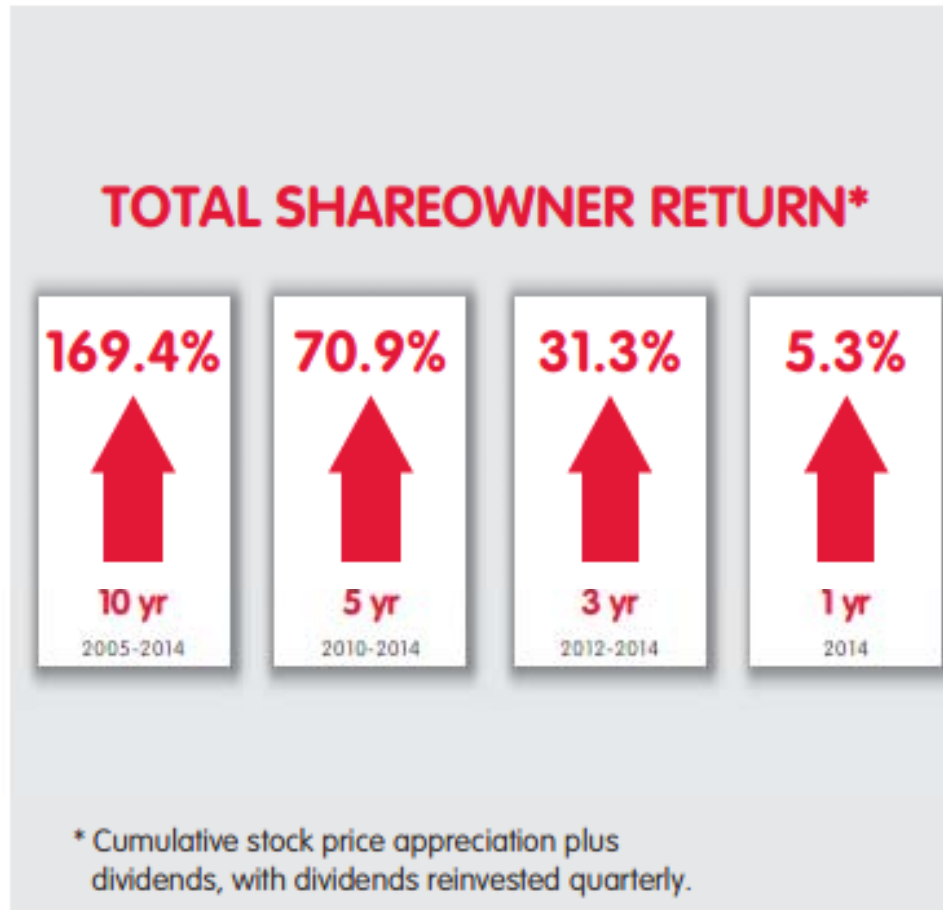
# Say-on-Pay and Shareholder Engagement

- A year round process
- Focused presentations
- Deciding who participates
- Engaging with proxy advisory firms
- Implementation of shareholder feedback
  - CD&A disclosure of how compensation committee took prior year vote into account

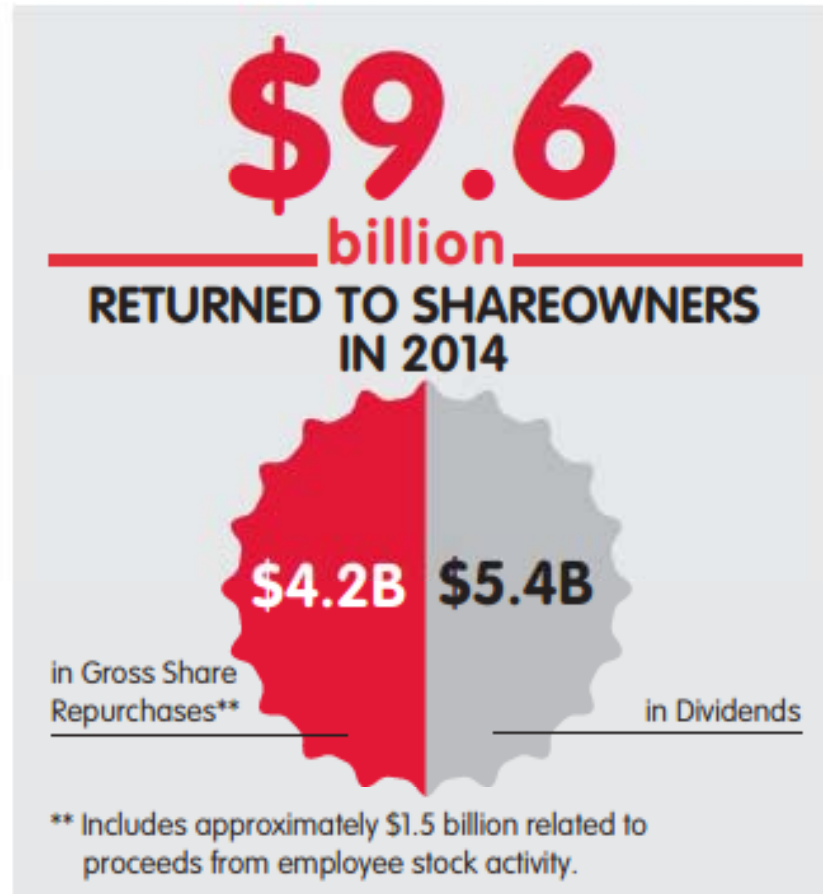
# Disclosure and Presentation Highlights

- Use of executive summaries in CD&A
- Use of proxy statements summaries to highlight say-on-pay
- Hyperlinked table of contents
- Table of contents entries for CD&A subheadings
- Use of graphics and emphasis on design
- Plain English
- Online Version
- Filing PDF as well as EDGAR copy with SEC

# Coca Cola – Proxy Graphics



## Coca Cola – Proxy Graphics (cont'd)





# Effective CD&A Disclosure for Say-on-Pay Votes

- Satisfying a disclosure obligation versus advocacy for advisory vote
- Executive Summary
  - Goals of program
  - Recent changes
- Clarifying link between pay and performance
- Use of graphics

# Goldman Sachs – First Section of CD&A

## Compensation Matters

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### Compensation Discussion and Analysis

#### Key Topics Covered in our CD&A

##### 2014 Year-End Compensation Decisions

What We Paid .....	Page 37
How Our Compensation Committee Made Its Decisions .....	Page 38
2014 Firmwide Performance .....	Page 38
2014 Individual Performance .....	Page 40

##### Importance of Discretion

Why We Avoid a Formulaic, Strictly Metrics-Based Compensation Program .....	Page 43
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##### Key Pay Practices

Key Pay Practices (What We Do and What We Don't Do) .....	Page 44
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##### Overview of Compensation Elements

Annual Variable Compensation .....	Page 48
Long-Term Performance Incentive Plan .....	Page 51

##### Other Compensation Policies and Practices

Stock Ownership Guidelines and Retention Requirements .....	Page 54
Clawback Policy .....	Page 54

# MasterCard – Excerpt from Executive Summary

## Key Features of our Executive Compensation Program

The Compensation Committee and management periodically review the compensation and benefit programs for executives and other employees to align them with the three core principles discussed above. Accordingly, we have adopted a number of practices over the last several years that affect our executive compensation program:

What We Do	
✓	Perform an annual “say-on-pay” advisory vote for stockholders
✓	Pay for performance
✓	Use appropriate peer groups when establishing compensation
✓	Balance short- and long-term incentives
✓	Align executive compensation with stockholder returns through long-term incentives
✓	Include caps on individual payouts in incentive plans
✓	Include a clawback policy in our incentive plans
✓	Set significant stock ownership guidelines for executives and non-employee directors
✓	Mandate “double-trigger” provisions for all plans that contemplate a change-in-control
✓	Condition grants of long-term incentive awards on execution of a non-solicitation, non-competition and non-disclosure agreement
✓	Mitigate undue risk taking in compensation programs
✓	Include criteria in incentive plans to maximize tax deductibility
✓	Retain an independent external compensation consultant

# MasterCard – Excerpt from Executive Summary (cont'd)

What We Don't Do	
⊘	No hedging of MasterCard stock
⊘	No new tax "gross ups" for executive officers
⊘	No tax "gross ups" for perquisites
⊘	No new "evergreen" employment agreements
⊘	No new participants in the Supplemental Executive Retirement Plan, or SERP
⊘	No repricing of options
⊘	No dividend equivalents on unvested equity awards

## 2014 Financial and Operational Highlights

In recent years, MasterCard has had strong operational and financial performance. The Company's performance has resulted in the substantial appreciation of our stock price, from a split-adjusted per share price of \$3.90 at the time of our IPO in May 2006 to a closing stock price of approximately \$86.16 per share as of December 31, 2014.

# Nabors Industries Ltd – Response to Say-on-Pay Vote

Shareholder Concern	Company Response
<b>Disconnect between Pay and Shareholder Value</b>	<ul style="list-style-type: none"> <li>• All short- and long-term incentives tied to performance-based metrics.</li> <li>• Short-term incentives directly tied to key drivers of market value.</li> <li>• Over 40% of long-term incentives tied to total shareholder return (“TSR”) versus an appropriate peer group over a 3-year period.</li> <li>• Remaining long-term equity incentives tied to achievement of financial or operational performance targets and subjected further to 3-year time-vesting requirements.</li> </ul>
<b>Rationale for Dual Peer Group Unclear</b>	<ul style="list-style-type: none"> <li>• Clarified justification for dual peer group in this Proxy Statement.</li> </ul>
<b>Limited Transparency Regarding Performance Metrics For Prior Year</b>	<ul style="list-style-type: none"> <li>• Provided more detailed disclosure on 2014 executive performance goals in this Proxy Statement, together with clearer visibility to targets and thresholds.</li> <li>• Clarified link between performance goals and Company’s long-term strategy in this Proxy Statement.</li> </ul>
<b>Size of CEO Contract Restructuring Payment</b>	<ul style="list-style-type: none"> <li>• Reduced CEO total compensation by 78% from 2013 to 2014.</li> </ul>

# Nabors Industries Ltd – Response to Say-on-Pay Vote (cont'd)

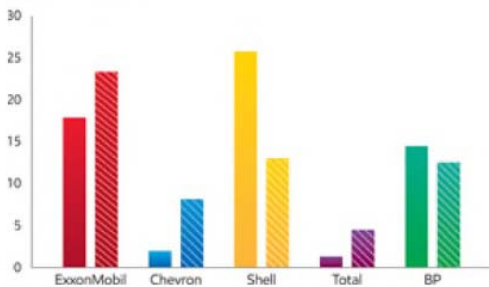
- **COMPENSATION HIGHLIGHTS**
  - **Linking Pay with Performance**
  - **CFO Employment Agreement**
  - **Reduction in Base Salaries**
  - **Updates to Compensation Practices**

# ExxonMobil – Initial Additional Materials

## 3 Free Cash Flow<sup>(4)</sup>

Industry Group

■ 2014 ■ 2010–2014 Average  
(dollars in billions)



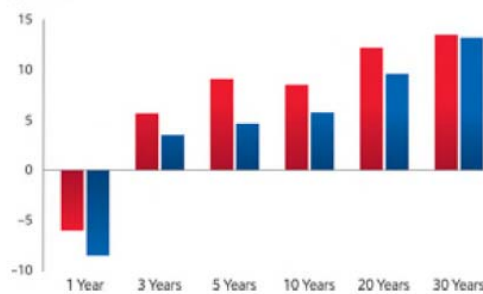
**ExxonMobil's superior cash flow preserves capacity for investments and shareholder distributions.**

- Generated \$117 billion of free cash flow since beginning of 2010.
- Reflects strong business performance and disciplined capital allocation approach.

## 5 Total Shareholder Return<sup>(6)</sup>

Industry Group

■ ExxonMobil ■ Industry Group<sup>(7)</sup>  
(percent)



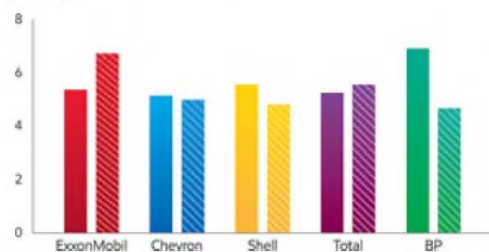
**ExxonMobil leads the industry in total shareholder return (TSR) in all performance periods.**

- The most relevant TSR comparison is across companies in the same industry of comparable size and scale.

## 4 Total Cash Distribution Yield<sup>(5)</sup>

Industry Group

■ 2014 ■ 2010–2014 Average  
(percent)



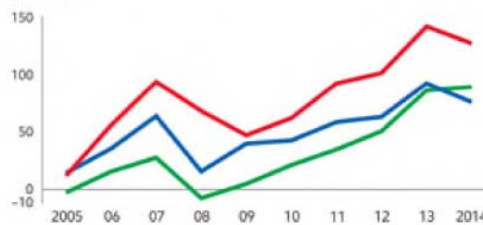
**ExxonMobil maintains industry-leading shareholder distributions through the business cycle.**

- Dividends per share up 10 percent per year over past 10 years.
- Distributed 46 cents of every dollar from operating cash flow and asset sales generated from 2010 to 2014.

## 6 10-Year Cumulative Returns<sup>(6)</sup>

Industry Group and Compensation Benchmark Companies

■ ExxonMobil ■ Industry Group<sup>(7)</sup>  
■ Compensation Benchmark Companies<sup>(8)</sup>  
(percent)



**ExxonMobil generated superior returns through a range of economic environments and business cycles.**

# ExxonMobil – Additional Materials for Updated Benchmarking

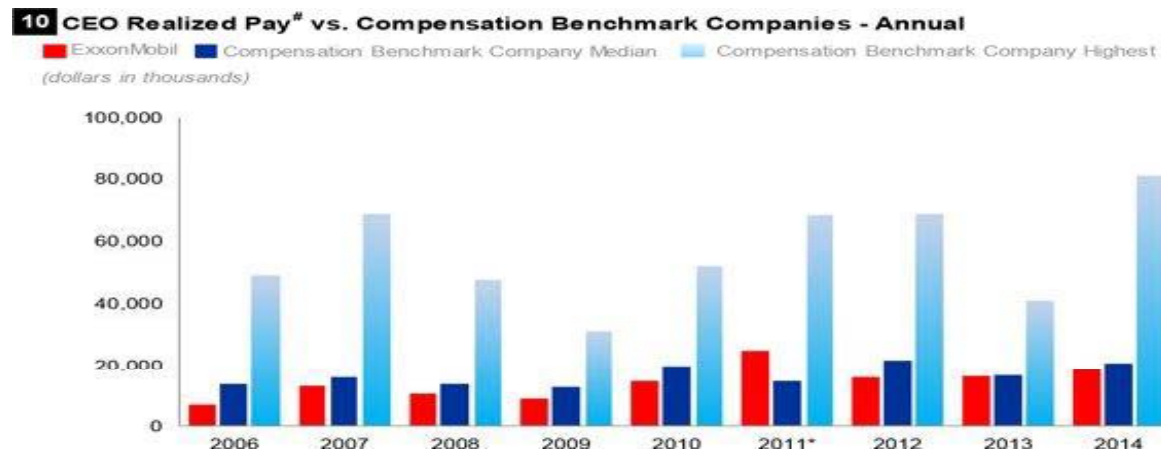
Dear Investor,

\* \* \*

The 2014 data for our compensation benchmark companies have recently become available as they have filed their 2015 proxies. Therefore we have updated Chart 10 (ExxonMobil CEO's realized pay versus our compensation benchmark companies) and Chart 11 (ExxonMobil CEO's combined realized and unrealized pay granted versus our compensation benchmark companies) to reflect this new data.

\* \* \*

As shown below in Chart 10, ExxonMobil CEO's realized pay continues to be below the median for most of his tenure as CEO.





# ExxonMobil – Additional Materials for Webinar

## Agenda

9:30am Shareholder Engagement ..... **Jeff Woodbury,**  
Vice President, Investor Relations and Secretary

Key Focus Areas

Basis for Compensation Decisions

Financial and Operating Performance

Strategic Business Results

Long-Term Business Performance

CEO Compensation ..... **Randy Powers,**  
Manager, Compensation, Benefit Plans and Policies

Annual Bonus Program

Equity Incentive Program

Determination of Equity Award Levels

Vesting Periods that Far Exceed Most Industries

ExxonMobil Program vs. Formula-Based Pay

10:10am Q&A

10:30am Webinar Concludes

# Responses to a Negative Proxy Advisory Firm Recommendation

- Triggers for a negative recommendation
- Supplemental SEC filings
- Impact of negative recommendation on shareholder approval
- Consequences of approval by less than a 70% majority

# Celanese Corporation – Additional Materials in Response to ISS Recommendation

What we heard from ISS	Our Response
Annual performance bonus targets lack rigor – performance goals set lower than last year’s actual and target goals	Annual performance bonus targets are established with year over year growth targets. 2014 target performance was 6% higher than prior year actual despite challenging global macro economic conditions. Actual performance was 20% higher than prior year
CEO bonus payout higher than table-disclosed maximum	Proxy table clearly discloses that maximum listed payout does not reflect any personal modifier. Future proxy statements will show a full (150% potential) personal modifier in annual bonus plan proxy tables
Annual performance bonus plan payouts may be adjusted upward due to a personal modifier	Our annual performance bonus plan design has included a personal modifier component since 2006. Our Board and Compensation Committee determined that the CEO’s achievements in 2014 justified a 110% personal modifier
Short- and long-term plans use the same performance measure	For 2014, both plans used Adjusted EBIT <sup>(1)</sup> as the performance measure. For 2015, we are adopting Adjusted Earnings Per Share <sup>(2)</sup> as the performance measure for the annual performance bonus plan but retaining Adjusted EBIT for the long-term plan
Retesting feature in performance-based restricted stock unit (PRSU) allows partial payout if primary threshold is not met	Many company plans have a time-based feature (restricted stock or restricted stock unit) primarily for retention of key talent. Our PRSU, while 100% performance based, permits a retesting if the primary performance threshold is not met

In addition to addressing the above concerns from ISS, our commentary below addresses our belief that ISS’s peer group methodology change for 2015 appears to have had a significant influence on their voting recommendation, and the outcome is inconsistent with our record earnings and stockholder cash returns.

# Morgan Stanley – Additional Materials in Response to ISS Recommendation

## 1. 2014 CEO Target Compensation Range

## Evaluating CEO Performance and Determining Compensation

- At the start of 2014, the CMDS Committee established a 2014 CEO target compensation range of \$13 million or less to \$23 million or more. Consistent with the approach in 2013, this range was informed by historical compensation at peer firms of similar size, scope, and complexity (i.e., five large U.S. banks as well as eight other leading financial companies in the S&P 100 index<sup>(1)</sup>), among other factors
- The matrix below provides the established framework to determine the 2014 CEO compensation, within the target range of up to \$23 million or more for superior performance and down to \$13 million or less for subpar performance

2013 Peer CEO Pay <sup>(2)</sup>			MS CEO Compensation Range	Evaluating MS CEO Performance
\$ Million	13 Financial Companies In S&P 100	5 Large U.S. Banks		
High	\$29	\$29		<ul style="list-style-type: none"> <li>CEO and Firm performance, as well as shareholder returns, substantially exceed expectations</li> </ul>
75th Percentile	\$19	\$20		<ul style="list-style-type: none"> <li>CEO performance exceeds expectations</li> <li>Strong Firm performance and shareholder returns with some room for continued progress</li> </ul>
50th Percentile	\$15	\$19		<ul style="list-style-type: none"> <li>CEO performance meets expectations</li> <li>Firm performance and shareholder returns generally in line with peers with room for continued progress</li> </ul>
25th Percentile	\$14	\$14.5		<ul style="list-style-type: none"> <li>CEO performance could be improved</li> <li>Firm performance and shareholder returns could be improved</li> </ul>
Low	\$11	\$14		<ul style="list-style-type: none"> <li>CEO and/or Firm performance, as well as shareholder returns, substantially below expectations</li> </ul>

Morgan Stanley

**Notes**

- Peer group includes (i) five large U.S. banks: Bank of America, Citigroup, Goldman Sachs, JPMorgan Chase, Wells Fargo; and (ii) other financial companies in S&P 100 index: AIG, Allstate, American Express, BNY Mellon, Capital One, Mastercard, MetLife, US Bancorp
- Includes both Annual Compensation and Long-Term Incentive Awards

4

# Quest Diagnostics – Additional Materials in Response to ISS Recommendation

## ISS Rationale and Management Response (Continued)

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ISS contends that the majority of executives' equity awards lack performance conditions, which is driven by that firm's view of executive stock options.

- Our Compensation Committee disagrees with that view, and believes that options remain an appropriate incentive, fully aligned with shareholder interests.
- Stock options provide long-term incentives to increase shareholder value and only deliver compensation if the stock price increases.
- Options are a particularly useful incentive for the Company in light of its flat stock trajectory over many years prior to 2014.
  - The Committee regularly reviews the use of different instruments (with outside consultants independent from management), after considering shareholder views and market trends; and
  - In 2012, the Committee reduced RSUs, which then constituted one-third of the total long-term incentive, to 20%, while increasing the performance share and stock option components to 40% each.

# Stifel Financial – Additional Materials in Response to ISS Recommendation

June 24, 2015

Fellow Shareholders:

Our annual shareholder meeting is currently adjourned to Tuesday, July 7, 2015 at 11:00 a.m. at our corporate headquarters in St. Louis, MO. We are sending you this letter in advance of that meeting to ask you to **vote FOR the advisory resolution approving the executive compensation of our named executive officers** (“Say on Pay”).

As described in our 2015 proxy statement, our Board of Directors unanimously recommends a vote FOR Item II, the “Say on Pay” proposal. However, during the solicitation period ISS, as independent proxy advisor, recommended against our “Say on Pay” proposal. The ISS recommendation came as a surprise to us and led to our reaching out to many shareholders to solicit their views and better explain what we seek to accomplish through our compensation program.

Based on the feedback we received from our shareholders, we intend to institute the following changes going forward:

- Our Compensation Committee will retain an independent compensation consultant to make recommendations.
- We will enhance our disclosure to more clearly describe the particular quantitative and qualitative factors used in a specific year in determining compensation for our named executive officers.
- We will expand and be more detailed with respect to the thought process and sequence of steps undertaken by the Compensation Committee as part of its process for determining compensation for our named executive officers.
- Our Compensation Committee, in consultation with the independent compensation consultant, will establish a long-term component of compensation that is based on pre-determined performance-based metrics for our named executive officers.
- We will continue to reach out to you, our shareholders, on an ongoing basis to solicit feedback on our corporate governance structures, and we will continually work to improve our public disclosure to better communicate our approach and address any concerns raised.

# Say-on-Pay Lawsuits

- First lawsuits where say-on-pay proposals failed
  - alleging breaches of fiduciary duty
- Second wave alleged insufficient compensation disclosures
  - Sought to enjoin the shareholder vote unless the company provided additional compensation disclosures
- Lawsuits challenging specific compensation actions, for example, based on failure to comply with Section 162(m) of the Internal Revenue Code
- Lawsuits were also filed regarding outside director compensation
  - Recent *Calma v. Templeton* case where the court treated the director awards as “self-dealing decisions” and held that “the operative standard of review is entire fairness
- Publicity surrounding pay-related lawsuits may have motivated more strenuous responses to negative ISS recommendations

# Say-When-on-Pay Preview

- Shareholders need to vote on the frequency of say-on-pay at least every six years
- If a company's first say-when-on-pay vote was in 2011, it will need a new one not later than at its 2017 meeting
  - Add it to the calendar for next year



# Clawback Proposal

- SEC proposed rules on July 1, 2015
- Comment period ended on September 14, 2015
- The proposal directs the stock exchanges to establish listing standards that prohibit the listing of any security of a company that does not adopt and implement a written policy requiring the recovery of certain incentive-based executive compensation
- Proposed listing standards likely will not be effective for the 2016 proxy season

## Clawback Proposal (cont'd)

- Proposed Rule 10D-1 defines ‘incentive-based compensation’ to mean any compensation that is granted, earned or vested based wholly or in part on the attainment of any financial reporting measure
- The proposed rule defines ‘financial reporting measure’ to mean a measure that is determined and presented in accordance with accounting principles used in preparing the company’s financial statements, any measure derived wholly or in part from such financial statements (including a non-GAAP measure) and stock price and total shareholder return

## Clawback Proposal (cont'd)

- The recovery would be the amount of incentive compensation that is later shown to have been paid in error, based on an accounting restatement that is necessary to correct a material error
  - To be based on the amount by which the incentive-based compensation that the executive officer received exceeds the amount the officer would have received had the incentive-based compensation been calculated following the accounting restatement
- Special situations
  - Award based on stock price or total shareholder return
  - Awards paid from a bonus pool

## Clawback Proposal (cont'd)

- The proposed recovery provisions would apply to any individual who served as an executive officer at any time during the performance period, whether or not the person is an executive officer at the time of the restatement
- The provisions would apply to any executive officer, whether or not the person engaged in misconduct or was responsible for the erroneous financial statements
- A company would be required to recover compensation paid during the three fiscal years preceding the date on which the company is required to prepare the restatement to correct a material error

## Clawback Proposal (cont'd)

- Clawback policies would be required to be filed as an exhibit to the annual report on Form 10-K
- In each proxy statements, a company must include disclosure if during its last completed fiscal year, it
  - Prepared an accounting restatement that required a clawback
  - Had an outstanding balance of unrecovered excess incentive-based compensation
- Information to be disclosed includes the name of each person subject to a clawback and any such amounts that have been outstanding for at least 180 days

## Clawback Proposal (cont'd)

- Recoverable amounts would be determined on a pre-tax basis
- A company would not have to recover excess compensation if the direct expense of recouping compensation would exceed the amount recoverable
- Foreign private issuers would not have to recover excess compensation if it obtains an opinion of home-country counsel that recovery would violate home-country law adopted prior to July 2015
- In the case of pool plans, recovery should be pro rata and a company would not be able to pursue differential recovery among executive officers

## Clawback Proposal (cont'd)

- A company would be prohibited from indemnifying their executive officers for incentive compensation recoverable pursuant to clawback policies and from paying the premiums on any insurance policy protecting against such recoveries
- Any required disclosures included in a proxy statement would be required to be block tagged using XBRL
- Summary compensation table amounts should be restated to reflect the impact of any clawbacks

# Pay-for-Performance

- SEC proposed rules on April 29, 2015
- Comment period ended on July 6, 2015
- The proposed rule would require companies to include a new table in their proxy statements showing the relationship between compensation actually paid and performance, with performance measured both by company TSR and peer group TSR
- All companies would have to provide the proposed disclosure, except foreign private issuers, registered investment companies and emerging growth companies



# Pay-for-Performance (cont'd)

## Pay Versus Performance

Year	Summary Compensation Table Total For PEO	Compensation Actually Paid to PEO	Average Summary Compensation Table Total for non-PEO Named Executive Officers	Average Compensation Actually Paid to non-PEO Named Executive Officers	Total Shareholder Return	Peer Group Total Shareholder Return
(a)	(b)	(c)	(d)	(e)	(f)	(g)

## Pay-for-Performance (cont'd)

- The chart is required to include five years of information
- The chart is to include separate line items for the compensation of the principal executive officer individually (or the aggregate if more than one person served in that role in a year) and the average compensation of the other named executive officers for each year

## Pay-for-Performance (cont'd)

- With two exceptions, the amounts are to be calculated in the same manner as for the Summary Compensation Table
  - The aggregate change in actuarial present value of the accumulated benefit included in the Summary Compensation Table would be deducted and replaced with the actuarially determined service costs for services rendered by the executive during the year
  - Equity awards would be considered actually paid on the date of vesting, whether or not exercised, and would be fair valued on that date

## Pay-for-Performance (cont'd)

- A clear description of the relationship between pay and performance must accompany the table in narrative or graphic form or a combination of both
- The required tabular disclosures included in a proxy statement would be required to be tagged using XBRL and any related footnotes would be required to be block tagged
- Phase-in of new requirements to occur over a three-year period
- Unclear whether the pay-for-performance requirements will be effective for the 2016 proxy season

# Pay Ratio Disclosure Rule: Adoption

- Section 953(b) of the Dodd-Frank Act
- Proposed in 2013; adopted on August 5, 2015
- Disclosure required for the first fiscal year commencing on or after January 1, 2017
  - Required in proxy statements for the 2018 annual meeting
  - Include in any filing that requires executive compensation disclosure
- *Exempt companies*: emerging growth companies, smaller reporting companies, foreign private issuers, MJDS filers, registered investment companies
- *Transition periods*: IPOs and business combinations or acquisitions

# Pay Ratio Disclosure Rule: Overview

- Pay Ratio Disclosure, new Item 402(u) of Regulation S-K:
  - Median annual total compensation of all company employees (except CEO);
  - Annual total compensation of CEO; and
  - The ratio of these two amounts (a ratio or a multiple)
  
- Example Disclosure:
  - Pay ratio of 50 to 1 or 50:1; or
  - The CEO's annual total compensation is 50 times the median of the annual total compensation of all company employees

# Pay Ratio Disclosure Rule: Employees Covered

- “Employee” is an individual employed by the company or any of its consolidated subsidiaries
  - U.S. employees
  - Non-U.S. employees with two exemptions:
    - Data Privacy Laws
    - *De Minimis* Exemption
  - Full-time, part-time, seasonal or temporary employees
  - Officers (other than CEO)
  - NOT independent contractors or “leased” workers

# Pay Ratio Disclosure Rule: Non-U.S. Employee Data Privacy Exemption

- May exclude employees in jurisdictions with data privacy laws that make the company unable to comply with the rule without violating those laws
- Company must exercise reasonable efforts to obtain or process the information including, at a minimum:
  - Seeking or using an exemption; and
  - Obtaining a legal opinion if no exemption granted (include as an exhibit)
- If the company uses an exemption:
  - List excluded jurisdictions and identify the specific data privacy law;
  - Exclude all non-U.S. employees in the jurisdiction and list the approximate number of employees for each excluded jurisdiction; and
  - Explain how complying with the rule violates such law, and disclose the company's efforts to seek or use the exemption



# Pay Ratio Disclosure Rule: Non-U.S. Employee *De Minimis* Exemption

- If a company's non-U.S. employees equal 5% or less of the company's total employees, the company may exclude **all** non-U.S. employees
- **or**
- If a company's non-U.S. employees exceed 5% of the company's total employees, the company may exclude **up to 5%** of its total employees who are non-U.S. employees
- A company using the *de minimis* exemption must disclose:
  - The jurisdiction(s) involved;
  - Approximate number of employees excluded in each jurisdiction;
  - Total number of U.S. and non-U.S. employees irrespective of the exemption (data privacy or *de minimis*); and
  - Total number of U.S. and non-U.S. employees used for the *de minimis* calculation
- Employees excluded pursuant to the data privacy exemption count toward the 5% *de minimis* exemption

# Pay Ratio Disclosure Rule: The Median Employee

- Identify the “median employee” using a method based on the company’s own facts and circumstances
  - Based on any consistently used compensation measure
  - A company may identify the median employee based on total compensation of the full employee population or may use a statistical sample or another reasonable method
- Disclose the date used to identify the median employee
- Identify once every three years, unless a change in employee population or compensation arrangements would result in a significant change to the pay ratio

# Pay Ratio Disclosure Rule: The Median Employee

- Median employee total compensation is calculated using the summary compensation table requirements
- Reasonable estimates
- Certain adjustments allowed
  - Annualize compensation
  - Cost-of-living adjustment
    - Disclose adjustments used to identify median employee and to calculate total compensation, including the measure used as the basis for the cost-of-living adjustment
    - Present median employee's total compensation and pay ratio without the adjustments for context
- Multiple CEOs in last fiscal year

## Pay Ratio Disclosure Rule: General Disclosure Elements

- Briefly describe and consistently apply any methodology used to identify the median employee and any material assumptions, adjustments or estimates used to identify the median employee or to determine total compensation or elements of total compensation
- Supplemental information and ratios are permitted but must be clearly identified and not misleading and not presented with greater prominence than the required ratio

# Pay Ratio Disclosure Rule: Transition Rules

- **Reporting company**
  - First fiscal year commencing on or after January 1, 2017
- **Exempt company (e.g., EGCs, SRCs, etc.)**
  - First fiscal year in which it exits exempt status but not before January 1, 2017
- **IPO company**
  - First fiscal year commencing on or after January 1, 2017 but not in an IPO prospectus or certain Form 10 registration statements
- **Business combinations/acquisitions**
  - Acquired employees may be omitted from the identification of the median employee for the fiscal year in which the transaction became effective
  - Company must disclose the approximate number of employees omitted

# Pay Ratio Disclosure Rule: Practical Considerations

- **Liability:** Pay ratio disclosures will be considered “filed,” not “furnished,” and therefore will be subject to certifications by the CEO and CFO and to potential securities law liabilities
- **Legal Challenge?** Two SEC commissioners dissented from final pay ratio rule approval
- **Assume 2018 Compliance Date**
  - Form a team (internal and external advisors)
  - Assess internal data systems
  - Develop and test a methodology
  - Address any desired compensation changes

# Proposed Hedging Policy Disclosure Rule

- Section 955 of the Dodd-Frank Act directs the SEC to issue rules requiring companies to disclose whether they permit employees and directors to hedge the company's securities
- Proposed on February 9, 2015, comment period expired
- Proposed rules would require the hedging policy disclosure in any proxy statement or information statement with respect to the election of directors
- Applicable to all companies subject to the federal proxy rules, including smaller reporting companies, emerging growth companies, business development companies and registered closed-end investment companies with shares listed and registered on a national securities exchange

# Proposed Hedging Policy Disclosure Rule

- Proposed new Item 407(i) of Regulation S-K:

(i) Employee, officer and director hedging. In proxy or information statements with respect to the election of directors, disclose whether the registrant permits any employees (including officers) or directors of the registrant, or any of their designees, to purchase financial instruments (including prepaid variable forward contracts, equity swaps, collars, and exchange funds) or otherwise engage in transactions that are designed to or have the effect of hedging or offsetting any decrease in the market value of equity securities —

- (1) Granted to the employee or director by the registrant as part of the compensation of the employee or director; or
- (2) Held, directly or indirectly, by the employee or director



# Proposed Hedging Policy Disclosure Rule

- Proposed rules are mainly in line with the Dodd-Frank Act mandate but include some expansions regarding the types of transactions covered and the location of the disclosure
- Companies are not required to prohibit hedging or to adopt practices or policies addressing hedging by any employees, officers and directors
- Proposed rules are aimed at disclosure and providing “transparency to shareholders ... about whether employees or directors are permitted to engage in transactions that mitigate or avoid the incentive alignment associated with equity ownership”

# Proposed Hedging Policy Disclosure Rule

- Many companies already discuss hedging policies in their CD&A – Item 402(b) of Regulation S-K requires disclosure of material information necessary to understand compensation policies and includes hedging policies as an example of information that should be provided, if material
- The proposed rules extend beyond the current CD&A requirement
  - Apply to all employees, officers and directors
  - Apply to all companies subject to proxy rules
- Companies should consider reviewing their hedging policies in light of the disclosure that may be required and identifying revisions to their current hedging policy disclosures that may be needed for future proxy statements

# Shareholder Proposals in 2015

- Proxy Access
- Increase in shareholder proposal activity
- More shareholder proposals received majority support
- Environmental and social policy proposals were the most commonly submitted, but not widely supported by shareholders
- Corporate governance proposals received strongest support
- Activist investors remain active and influential
- Shareholder and proxy advisor outreach continues

# Shareholder Proposal Process

- Commissioner Gallagher: move proposal process to states
- Rule 14a-8
- Initial assessment of proposal and proponent
- Check for technical deficiencies immediately
  - Verify ownership
  - 500 words or less
  - Is it late?
  - Other
- Respond to proponent within 14 days of receipt
- Opportunity to cure deficiency

# Evaluation of Shareholder Proposal

- Evaluate whether any other grounds for exclusion exist:
  - Relates to ordinary business operations
  - Not relevant to the company's business
  - Substantially implemented
  - Company lacks power or authority to implement
  - Violates proxy rules
  - Improper under state law or violates the law
  - Involves personal claim or grievance
  - Conflicts with management proposal\*
  - Other

# Preparing the No-Action Request

- Deadline for submission – 80 days before definitive proxy
  - Otherwise, must obtain a waiver from SEC
- The No-Action request letter
  - Identify all plausible arguments for exclusion
  - Cite the most recent applicable authority
  - Submit to SEC and proponent (with other documentation)
- Proponent may submit rebuttal
- SEC may give proponent opportunity to cure deficiency

# The Opposition Statement

- Must be sent to the proponent of the shareholder proposal not later than 30 days before the definitive proxy is filed
  - Prepare and send even if awaiting SEC no-action response
  - Shareholder proponent can object to false or misleading statements
- Research relevant proxy advisor voting policies and address in opposition statement
- Engage institutional shareholders and proxy advisors
- Consider whether additional soliciting materials should be prepared and filed

## Proxy Access – Background

- Proxy Access: the right of a qualifying shareholder (or group of shareholders) to include its own board candidate in the company's proxy materials, at the company's expense
- SEC Rule 14a-11 adopted in 2010:
  - 3% ownership by shareholder (or group of shareholders) for minimum of three years
  - Representing up to 25% of the company's board
  - Vacated by U.S. Court of Appeals in July 2011
- SEC amends Rule 14a-8(i)(8) to allow shareholder proposals that address director nomination process
  - Proposals modeled after vacated SEC rule received greater support



# Proxy Access Proposals – 2015

- New York City Comptroller proxy access campaign
  - Submitted 75 proxy access proposals (3%, 3 years, 25% of board)
  - Recipients were selected based on three “priority issues”: climate change, board diversity and excessive CEO pay
- Whole Foods No-Action Request
  - Requested exclusion of proxy access proposal on grounds that it directly conflicted with management proposal (9%, 5 years, 10% of board)
  - SEC initially issued no action letter concurring that Whole Foods may exclude shareholder proposal pursuant to Rule 14a-8(i)(9)
- SEC initiates review of Rule 14a-8(i)(9)
  - SEC expresses no view on directly conflicting proposals (including Whole Foods)

# Proxy Access Proposals – 2015

- Company responses to proxy access proposal:
  - Oppose shareholder proposal
  - Oppose shareholder proposal but commit to adopt proxy access bylaw
  - Include both the shareholder proxy access proposal and a management proxy access proposal in proxy materials
  - Adopt own proxy access bylaw in advance (and oppose shareholder proposal)
  - Remain neutral or recommend in favor of shareholder proxy access proposal
  - Negotiate withdrawal of shareholder proposal

# Proxy Access Proposals – 2015

- Proxy access proposal received substantial support in 2015:
  - 84 shareholder proxy access proposals came to a vote, 50 passed
  - Average vote in favor of proxy access proposal was 55%
  - ISS and Glass Lewis generally support 3%, 3-year, 25% proxy access proposal
  - Strong support among pension funds
  - Varying support among other institutional shareholders (Vanguard, Fidelity)
- Outcome of vote influenced by individual company's shareholder base

# Proxy Access Bylaw – Key Terms

- Ownership threshold – 3% vs. 5% or other
- Holding period – 3 years
- Maximum number of proxy access nominees
  - Most limit to 20% or 25% of board
  - Incumbent proxy access directors and “creeping control”
- Aggregation of shareholders
  - Limit number of shareholders that form nominating group
  - Vast majority limit to 20 shareholders
  - Funds under common control – count as single shareholder?
- Nature of ownership

## Proxy Access Bylaw – Key Terms (cont'd.)

- Information requirements
- Limits on renominations (e.g., minimum vote requirement)
- Compensation of shareholder-nominated director
- Disqualification of shareholders engaged in proxy fight for board seats

# Shareholder Proposals – Corporate Governance

- Independent chair
  - Support for this proposal continues to recede
  - If strong alternative structure, shareholders not likely to approve
- Majority voting
  - Sharp decline in number of proposals submitted and voted on in 2015
  - Those that failed were mostly at companies with plurality voting with a resignation policy
- Board declassification/annual director elections
  - Fewer proposals submitted and voted on in 2015

## Shareholder Proposal Topics – Corporate Governance (cont'd.)

- Action by written consent
  - More proposals submitted and voted on in 2015
  - Average support just under 40%, only two proposals received majority vote
- Right to call special meeting unchanged compared to 2014
- Supermajority voting
  - Overall support declined in 2015 (approximately 56% on average)

# Shareholder Proposal Topics – Compensation Issues

- Increase in number of proposals submitted and voted on in 2015
- Proposal types:
  - Limit acceleration of vesting of equity awards upon a change of control
  - Implement compensation clawback policy
  - Require disclosure of pay ratios
  - Require shareholder approval of severance payments greater than 2.99 times salary and bonus
- Not widely supported
  - Vesting and severance proposals received most support, averaging approximately 34% and 37%, respectively



# Shareholder Proposals – Political Spending / Lobbying

- *Citizens United* decision (U.S. Supreme Court – 2010)
- Proposals seek disclosure of political spending and lobbying efforts
- Fewer political activity proposals in 2015
- Only modest support for political activity proposals:
  - Approximately 35% for political spending disclosure and 25% for lobbying disclosure
  - More proposals were withdrawn in 2015

# Shareholder Proposals – Environmental Issues

- Climate change
  - Typically a report on efforts to reduce greenhouse gas emissions
  - Also, financial risks arising from climate change, adoption of principles to reduce global warming
- Sustainability
  - File reports on sustainability efforts
- Other environmental issues
  - Hydraulic fracturing, coal-related proposals, recycling, water scarcity, oil sands, toxic substances
- Modest support among shareholders

## Other Current Matters

- D&O questionnaires
- Universal proxy cards
- Online/virtual meetings
- Conflict minerals update
- Resource extraction update

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