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Executive Compensation in 2010: The Evolution Continues

A Buck Consultants Webcast
April 28, 2010

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Kathi Myers, Director
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Topics Covered in Today's Webcast

What We've Learned from the Latest Proxy Filings

- Risk Assessment Disclosures Under the New Rules
- CEO Compensation
 - Year-over-Year Changes
 - Base Salaries
 - Variable Cash Programs
 - Actual Total Direct Compensation
- Other Insights
 - Non-Equity Incentive Plan Disclosures
 - Discretionary Bonuses
 - Retentive Actions
- Breaking Out the Crystal Ball
 - Informed Projections for 2010

Today's Speakers

- **Andy Mandel, Principal**

Andy is based in the New York office of Buck's Compensation Consulting practice. He is a Certified Public Accountant and has more than 17 years experience at a Big Four accounting firm, where he served as a leader in the Transaction Advisory Services' Compensation and Benefits Practice. His expertise covers a range of issues affecting executive compensation, incentive plans, and equity award programs. Andy's consulting clients have included multinational corporations in diverse industries, private equity firms, and financial institutions.

- **Kathi Myers, Director**

Kathi is based in the San Francisco office of Buck's Compensation Consulting practice. With more than 12 years experience working in both corporate and consulting environments, she is well-versed in the design, administration, and implementation of broad-based employee and executive pay, with a focus on incentive programs. Her consulting experience has included a wide range of clients across various industries, from retail to aerospace to technology.

- **Amy Heinze, Senior Associate**

Amy is based out of the San Francisco office of Buck's Compensation Consulting practice and currently works from Tacoma, WA. With her 8 years of experience in sleuthing and analyzing the latest trends in executive compensation, she is a go-to person for collecting the most current market data available.

Risk Assessment Disclosure

SEC Proxy Disclosure Requirements Involving Risk

Generally effective for 2010 proxy filings

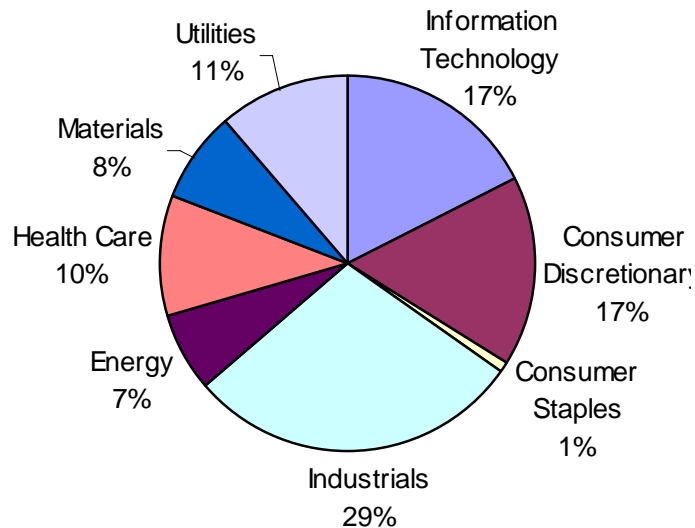
- Narrative disclosure on compensation policies and practices that:
 - Create risks that are “reasonably likely” to have a “material adverse effect” on the company
 - “Reasonably likely” standard - MD&A threshold; What will influence shareholder decisions?
 - “Material adverse effect” – unnecessary and excessive risk taking and/or manipulation of results **versus** those involving innovation and appropriate levels of risk-taking
 - Applies to all compensation arrangements not just those covering executives
 - Guidance suggests inclusion within executive compensation disclosures
 - Does NOT require affirmative statement
 - However, does not alleviate the existing requirement to disclose (within the CD&A) material risk considerations involving NEO compensation arrangements
- Must describe the Board’s role in the oversight of risk

Proxy Risk Disclosure Findings

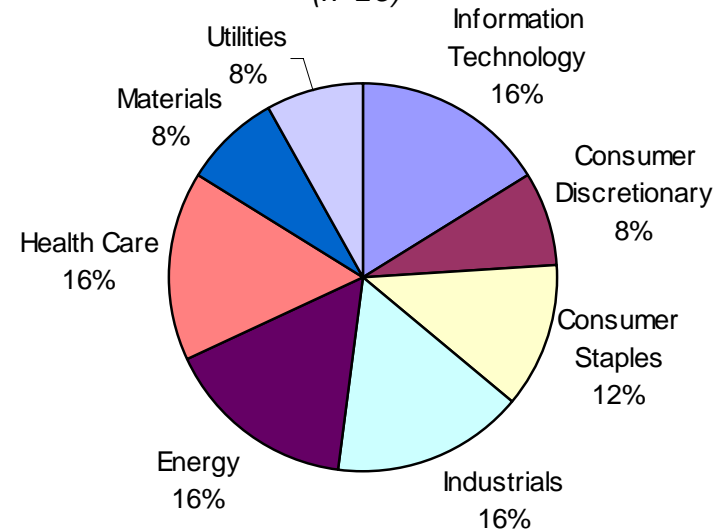
Study Demographics

- Pulled data on 115 S&P 400 and 25 S&P 100 companies
 - Financial service companies were excluded
- Reviewed for compensation-related risk disclosures
 - Also reviewed disclosures on risk oversight
- Our research is an ongoing process as proxies continue to be filed and analyzed

S&P 400 - Industry Breakout of Sample
Filing after 2/28/2010
(n=115)



S&P 100 - Industry Breakout of Sample
Filing after 2/28/2010
(n=25)

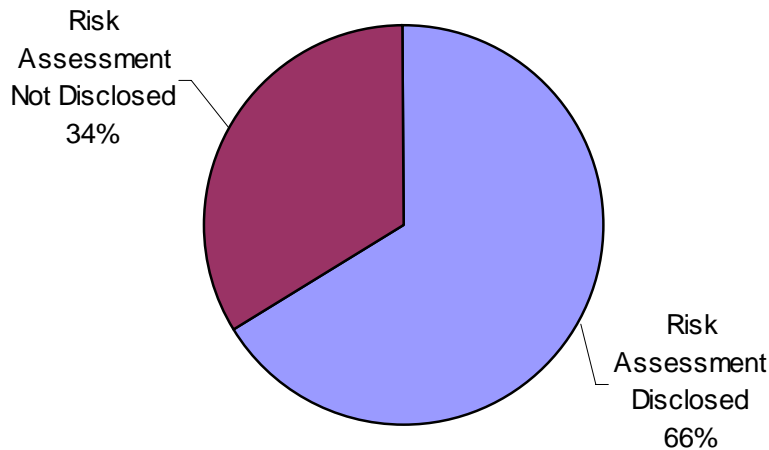


Proxy Risk Disclosure Findings (Cont'd)

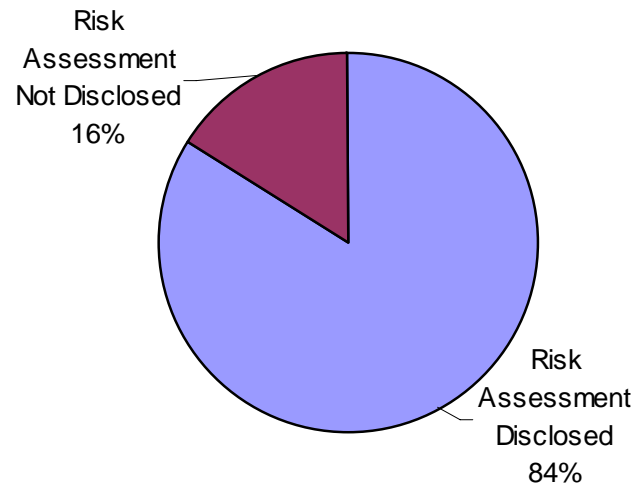
Indication of whether a risk assessment was performed

- 76 or 66% of the S&P 400 companies
- 21 or 84% of the S&P 100 companies
- Are larger companies more inclined to assess risks within their compensation plans?

**S&P 400 - Prevalence of Compensation Plan
Risk Disclosure in Proxy**
(n=115)



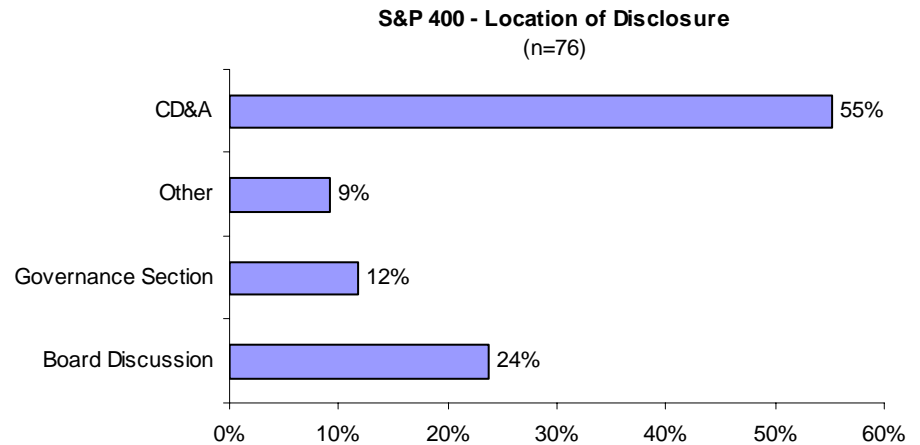
**S&P 100 - Prevalence of Compensation Plan
Risk Disclosure in Proxy**
(n=25)



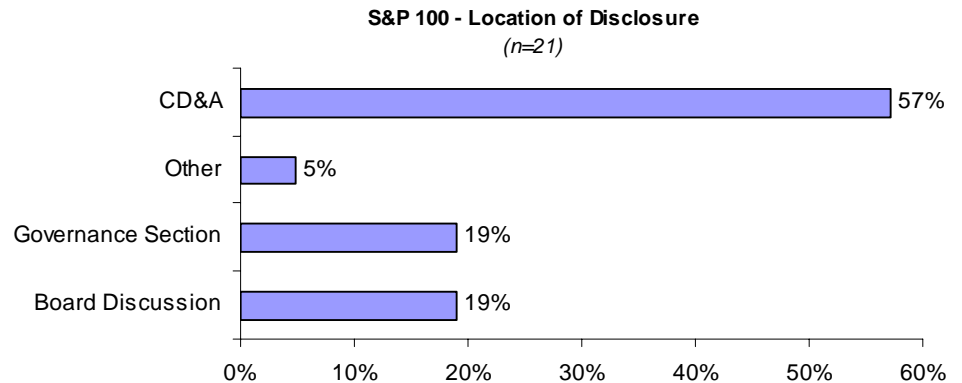
Proxy Risk Disclosure Findings (Cont'd)

Location of risk disclosure within the proxy

- Mixed results - slightly more than half included within CD&A in each case



- Is there a need for more guidance to generate greater consistency among filers?

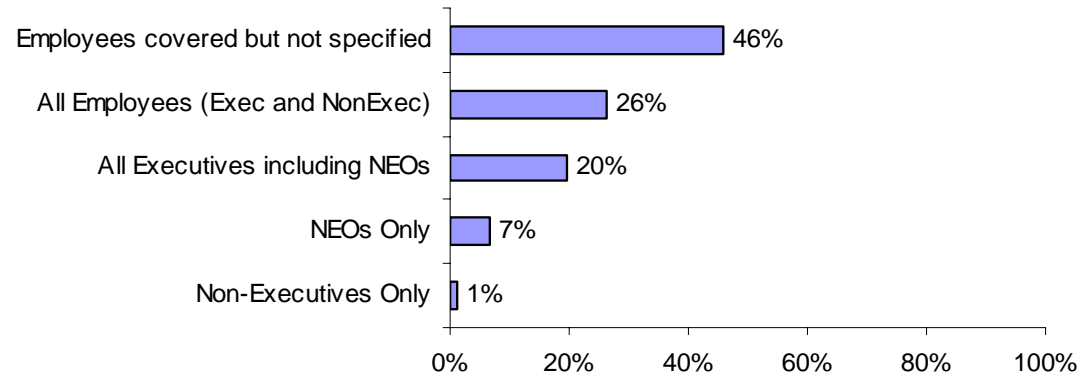


Proxy Risk Disclosure Findings (Cont'd)

Employee groups covered within the compensation risk assessment

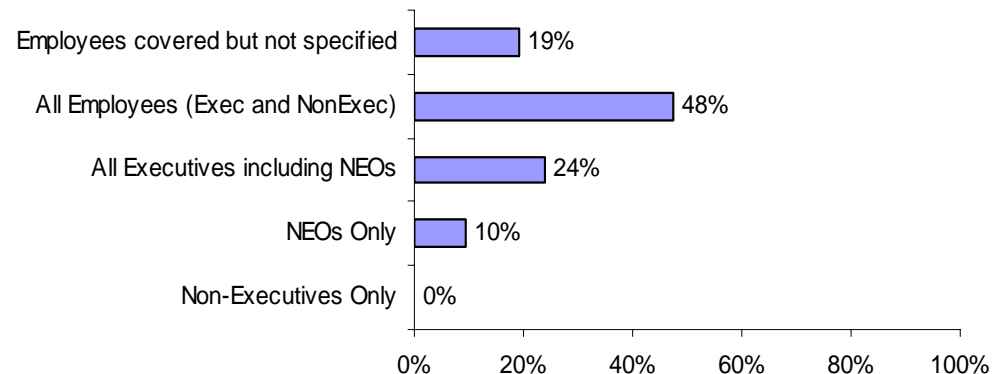
- Not entirely clear as to which employee plans were reviewed – particularly in the S&P 400 group

S&P 400- Population Covered in Risk Assessment Disclosure
(n=76)



- Are larger companies more inclined to perform a more comprehensive review of plans covering all employees?

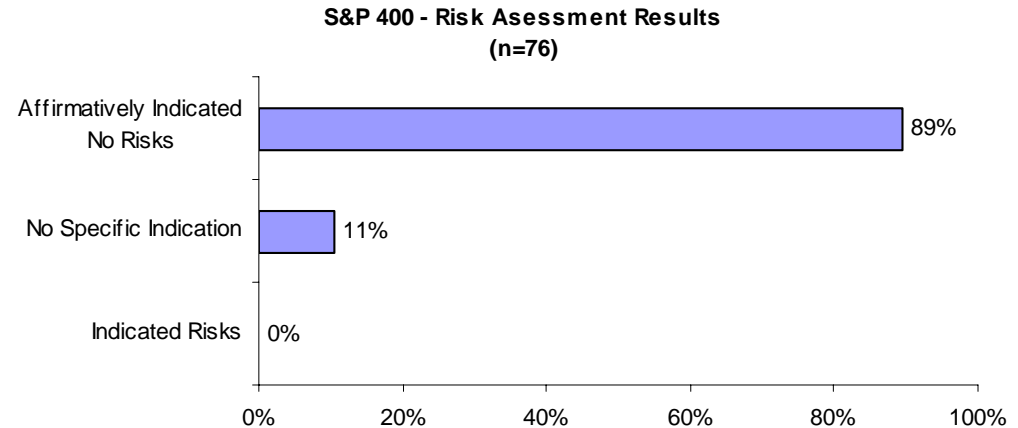
S&P 100 - Population Covered in Risk Assessment Disclosure
(n=21)



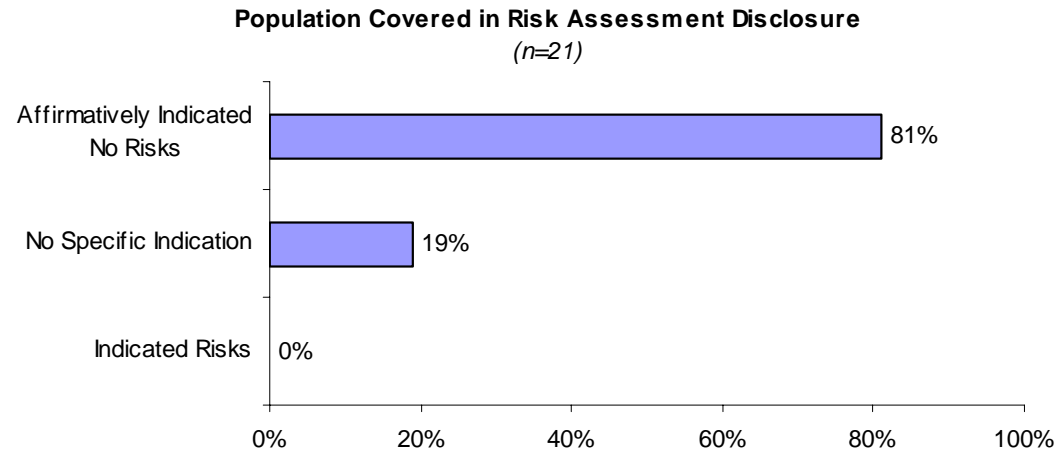
Proxy Risk Disclosure Findings (Cont'd)

For those that performed assessments, what were the “results”?

- Most companies disclosed one of several results:
 - No “excessive” risks were detected
 - No “unnecessary” risks were detected
 - No “inappropriate” risks were detected
 - No “material adverse” risks were detected



- A number of companies acknowledged that there are “appropriate” levels of risk within their plans

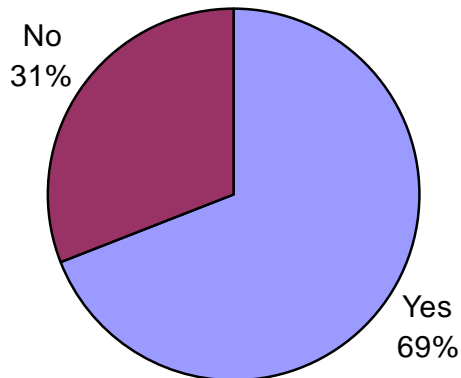


Proxy Risk Disclosure Findings (Cont'd)

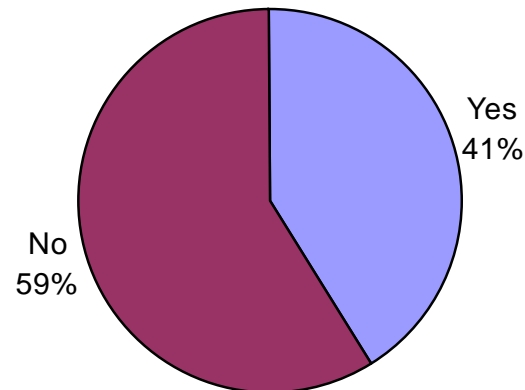
Those that incorporated the SEC's "no material adverse effect" language

- A fairly large percentage of companies that indicated there were "no risks" included this specific affirmative statement even though such statement is NOT required by the SEC

S&P 400 - Prevalence of
"No Material Adverse Effect" Statement
(n=67)



S&P 100 - Prevalence of
"No Material Adverse Effect" Statement
(n=17)

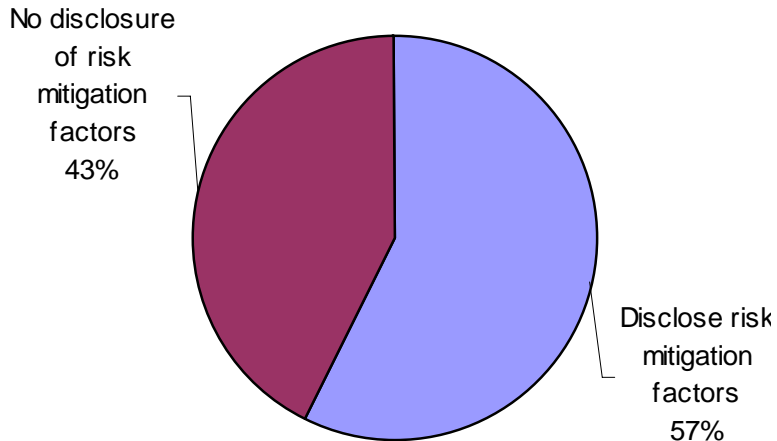


Proxy Risk Disclosure Findings (Cont'd)

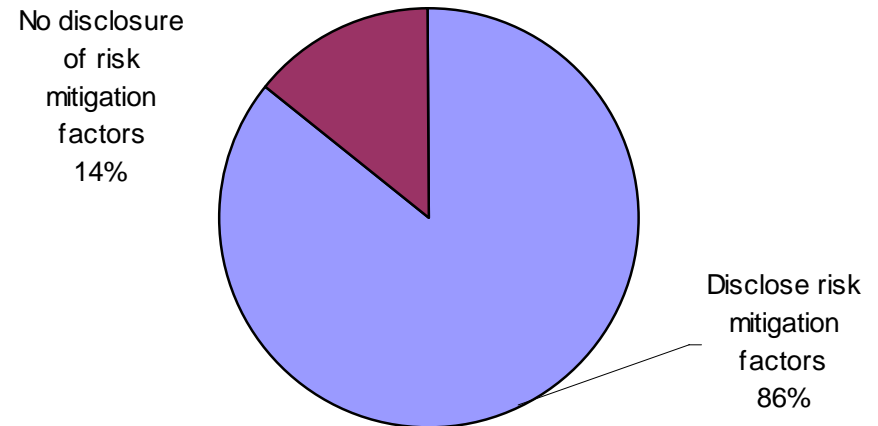
Most companies that had risk disclosures indicated their techniques

- 44 of 76 S&P 400 companies
- 18 of 21 S&P 100 companies

S&P 400 - Indication of Risk Mitigation Factors
(n=76)



S&P 100 - Indication of Risk Mitigation Factors
(n=21)

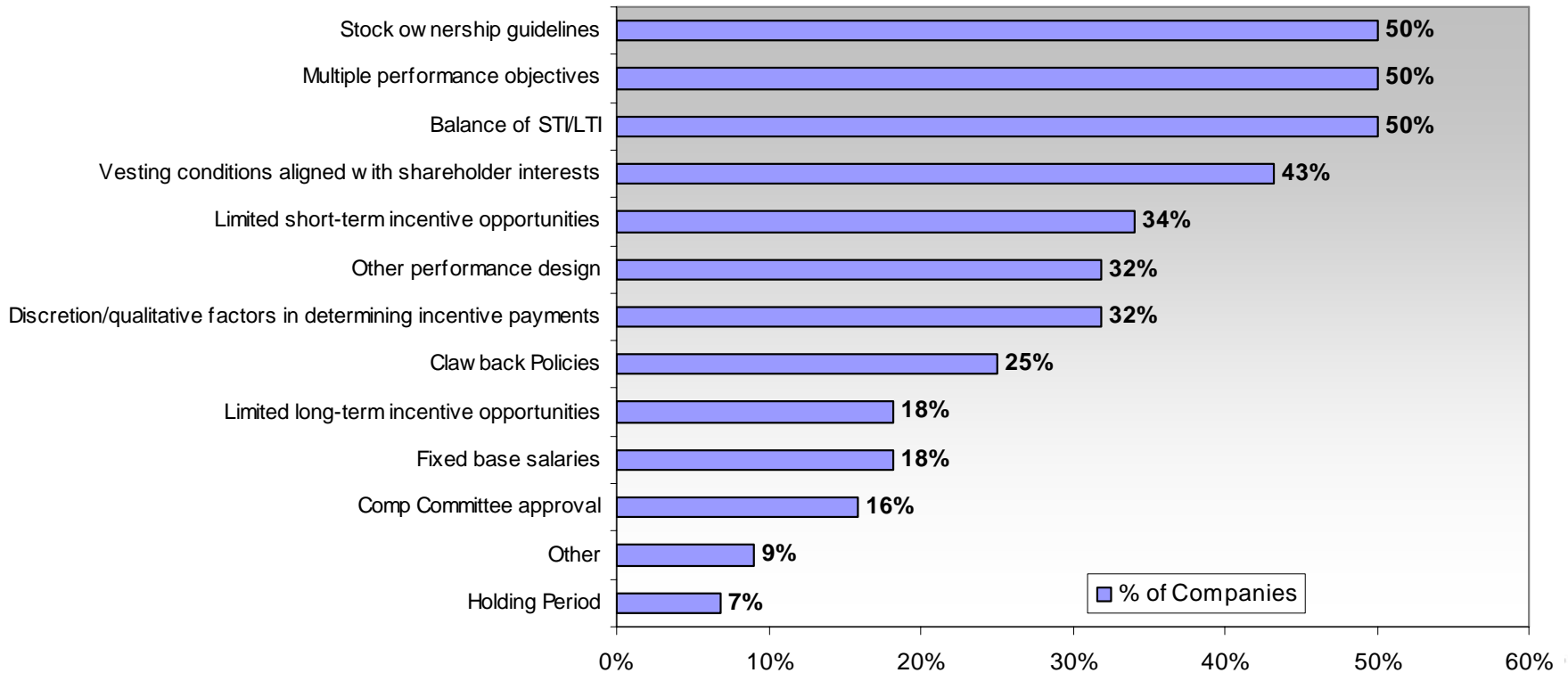


Proxy Risk Disclosure Findings (Cont'd)

Factors cited by S&P 400 companies as ways in which risks are mitigated

- Very mixed results
- No companies indicated “bonus banks”

S&P 400 - Risk Mitigation Factors Discussed in Risk Assessment Section
(n=44)

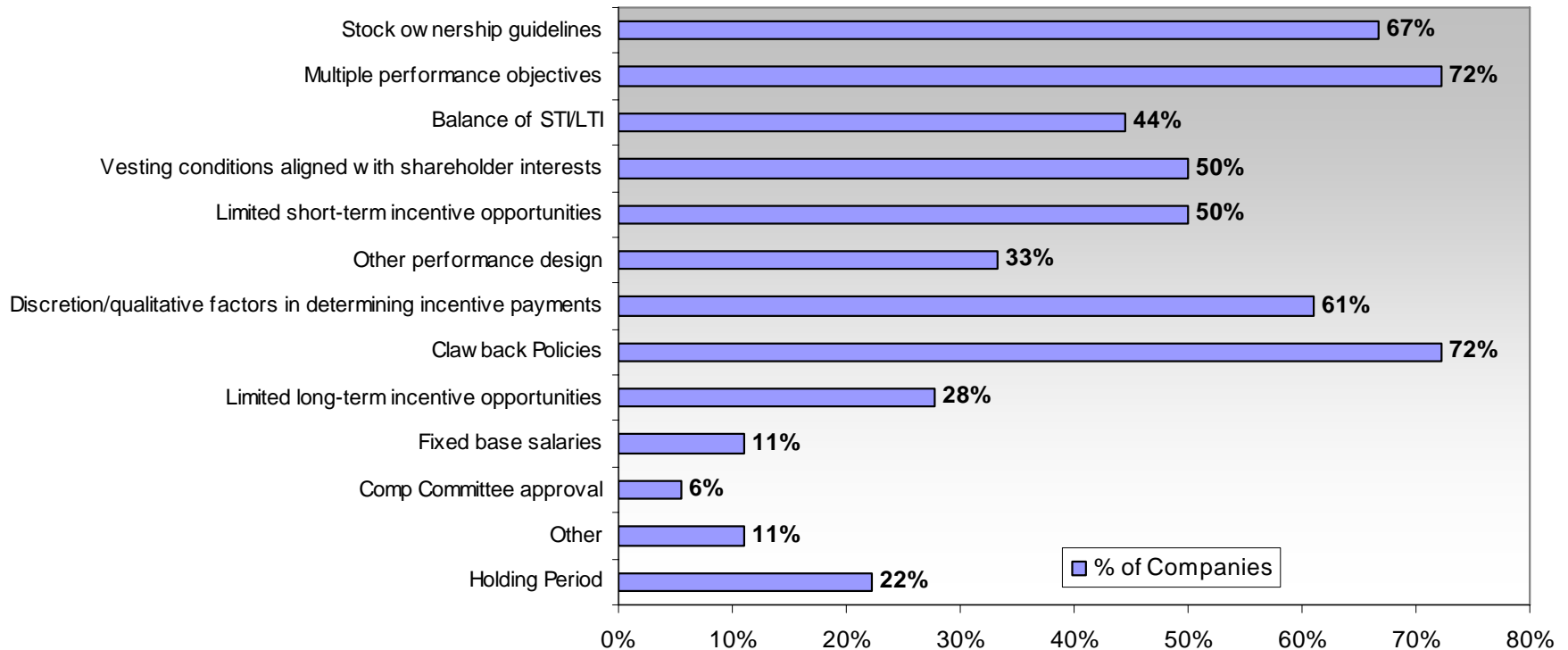


Proxy Risk Disclosure Findings (Cont'd)

Factors cited by S&P 100 companies as ways in which risks are mitigated

- S&P 100 companies were more inclined to reflect claw-back policies and discretionary features as risk mitigation factors

S&P 100 - Risk Mitigation Factors Discussed in Risk Assessment
[n=18]



Proxy Risk Disclosure Findings (Cont'd)

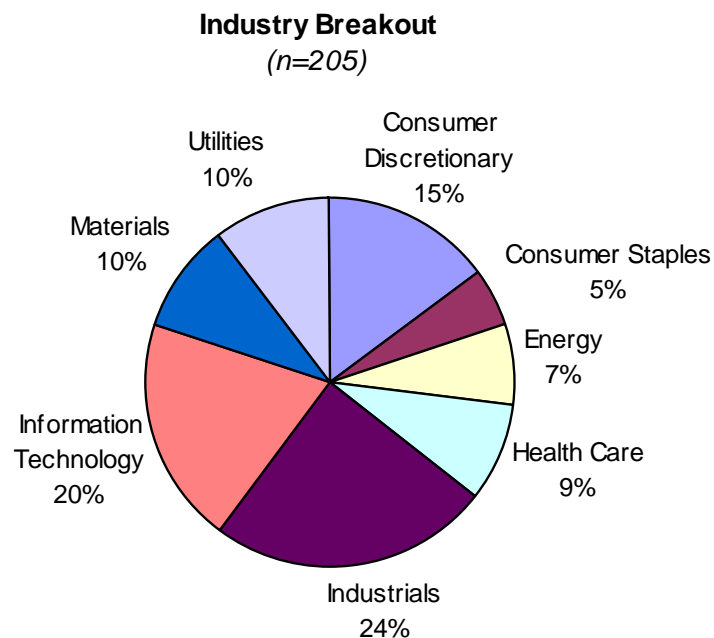
Summary of findings

- By and large companies felt the need to include disclosures about compensation risk assessments
 - How meaningful are these disclosures to investors?
- Generally, companies rationalized that their plans, by design, mitigate risks without the need for added risk mitigation procedures
 - Fewer than 5% of all companies indicated that a new risk management role was created
 - Fewer than 8% of all companies indicated that there is a separate risk committee
 - Very few companies indicated that there were substantive changes made to their policies and practices to address risks within their compensation plans
 - ***Do these design elements truly mitigate material adverse risk?***

Year-over-Year CEO Compensation *(and other insights)*

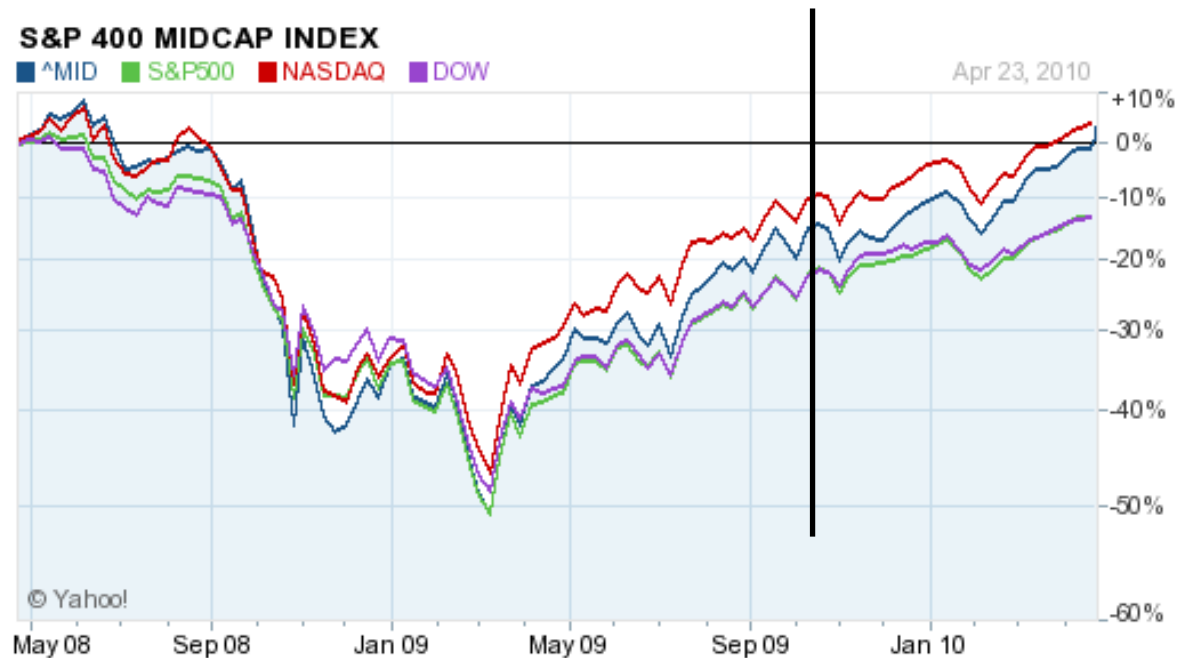
Study Demographics

- S&P 400 Midcap Companies, excluding Financial Services
 - Range of Market Cap \$2B - \$10B
- Collected quantitative data for only those companies with a new proxy filed as of early April
 - Final sample size of 205 companies



The Market's Wild Ride – A Recap

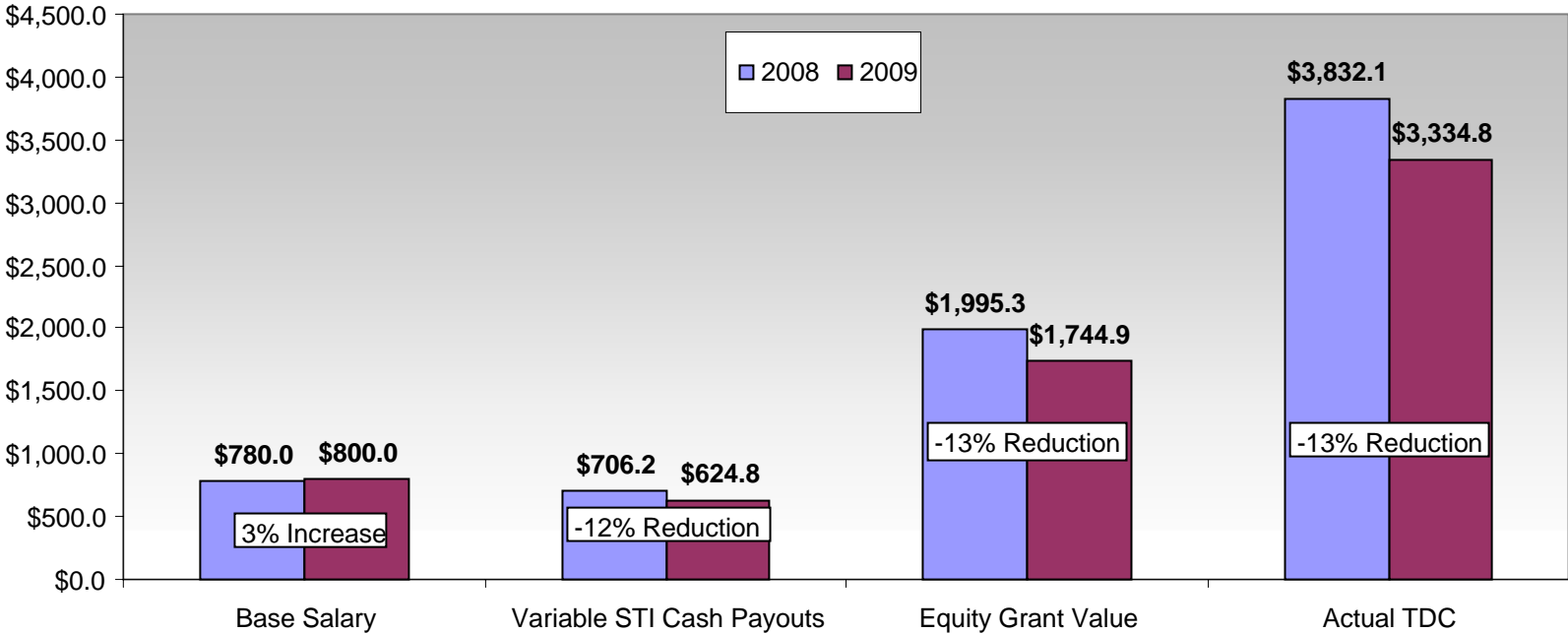
- All indices began to suffer around September of 2008
- Relatively steady march downward with some spikes mixed in....just in case you had already tried to call the bottom of the market
- By March of 2009 some companies experienced stock price drops of 50% or more



CEO Compensation Year-over-Year

- As expected, variable pay elements were down in 2009 from the prior year leading to an overall median total direct compensation reduction of 13% across all industries

CEO Compensation
(Year-over-Year)



CEO Compensation Year-over-Year Analysis

- Some industries fared better than others
- Industrials and Technology, two industries historically known for their heavy variable pay programs, experienced some of the deepest declines as stock prices fell and financial metrics were missed in cash programs

Industry	# Cos	Base Salary			Actual Total Cash		
		2008 Median	2009 Median	% Change	2008 Median	2009 Median	% Change
Consumer Discretionary	31	\$825.0	\$850.0	3%	\$1,213.0	\$1,421.4	17%
Consumer Staples	10	\$828.1	\$851.1	3%	\$1,197.6	\$1,049.5	-12%
Energy	14	\$600.0	\$628.2	5%	\$1,280.2	\$1,240.6	-3%
Health Care	18	\$781.5	\$815.4	4%	\$1,654.0	\$1,554.9	-6%
Industrials	50	\$801.6	\$797.1	-1%	\$1,496.0	\$1,043.2	-30%
Information Technology	41	\$645.0	\$650.0	1%	\$996.2	\$892.4	-10%
Materials	20	\$864.3	\$896.2	4%	\$1,598.4	\$1,780.0	11%
Utilities	21	\$744.7	\$771.8	4%	\$1,284.9	\$1,381.3	8%

Industry	# Cos	Equity Values			Actual Total Direct Comp		
		2008 Median	2009 Median	% Change	2008 Median	2009 Median	% Change
Consumer Discretionary	31	\$1,914.0	\$1,763.8	-8%	\$2,988.6	\$3,314.2	11%
Consumer Staples	10	\$876.5	\$803.7	-8%	\$2,906.2	\$2,405.2	-17%
Energy	14	\$2,695.2	\$2,258.8	-16%	\$4,532.4	\$4,110.4	-9%
Health Care	18	\$2,382.4	\$2,210.0	-7%	\$4,166.9	\$3,842.0	-8%
Industrials	50	\$1,938.2	\$1,558.1	-20%	\$3,995.1	\$3,157.4	-21%
Information Technology	41	\$2,286.2	\$1,710.0	-25%	\$4,217.6	\$3,141.2	-26%
Materials	20	\$1,964.9	\$2,038.1	4%	\$4,027.3	\$3,821.7	-5%
Utilities	21	\$1,143.9	\$1,174.9	3%	\$2,674.6	\$3,031.9	13%

Formal Non-Equity Incentive Plan

- 167 companies (82%) disclosed a target amount in the Grants-of-Plan-Based-Awards table as it relates to non-equity incentive plans
 - Approximately half of the remaining companies paid a discretionary bonus (more on that later)
- Of those companies with a formal target, the majority (83%) disclosed the actual performance targets associated with financial metrics
 - Plans are being designed to include more discretion in final payouts
- Average performance metric weighting for CEO role
 - 90% Financials or other Corporate Metric
 - 10% MBOs or other Individual Metric
 - Note: Several plan designs called for bonus pool funding at 100% based on corporate metric with discretion applied based on individual performance

Discretionary Bonuses

- FAQs we encountered this year as fiscal years were ending
 - Are other companies considering a discretionary bonus to executives where performance metrics became unachievable due to exogenous factors?
 - What is the “right” amount?
- The answer: It depends
 - Several companies delivered a discretionary bonus, either in lieu of or in addition to the formal STI payout, in the last fiscal year
 - We can safely guess that many more considered it

Discretionary Bonuses

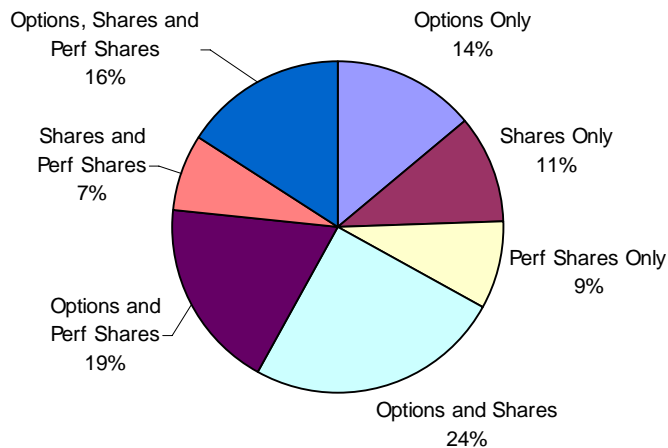
- 34 (17%) of the companies studied paid a discretionary bonus to the CEO
 - A study of the broader NEO group may yield even higher results
- Median payment equal to 76% of base salary, average payment equal to 91%
- Caution: the details behind this headline are important to understand

CEO Discretionary Bonus Detail	2009
Of those companies with a discretionary bonus payout, what is the prevalence of companies without a formal STI target?	47%
Of those companies with a discretionary bonus payout AND a formal STI plan, what was the median formal STI plan payout as a percent of target?	74%
Of those companies WITHOUT a discretionary bonus payout, what was the median formal STI plan payout as a percent of target?	79%
Of those companies with a discretionary bonus payout WITHOUT a formal STI plan, was the median discretionary bonus payout as % of base?	113%
Of those companies with a discretionary bonus payout AND a formal STI plan, what was the median discretionary bonus payout as a percent of base?	35%

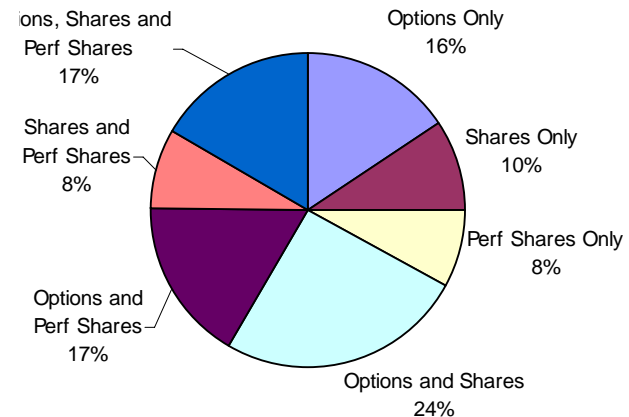
Long-Term Incentives

- Little changed in terms of the types of equity being granted to CEOs year-over-year
 - Yields a colorful pie chart, especially when painting the picture from a cross-industry perspective
- Eighteen companies (9%) provided a Cash LTIP in addition to equity in 2009 versus nineteen companies in 2008
- Only one company utilized Cash as its only form of LTIP in both 2008 and 2009

2008 Equity Vehicle Mix

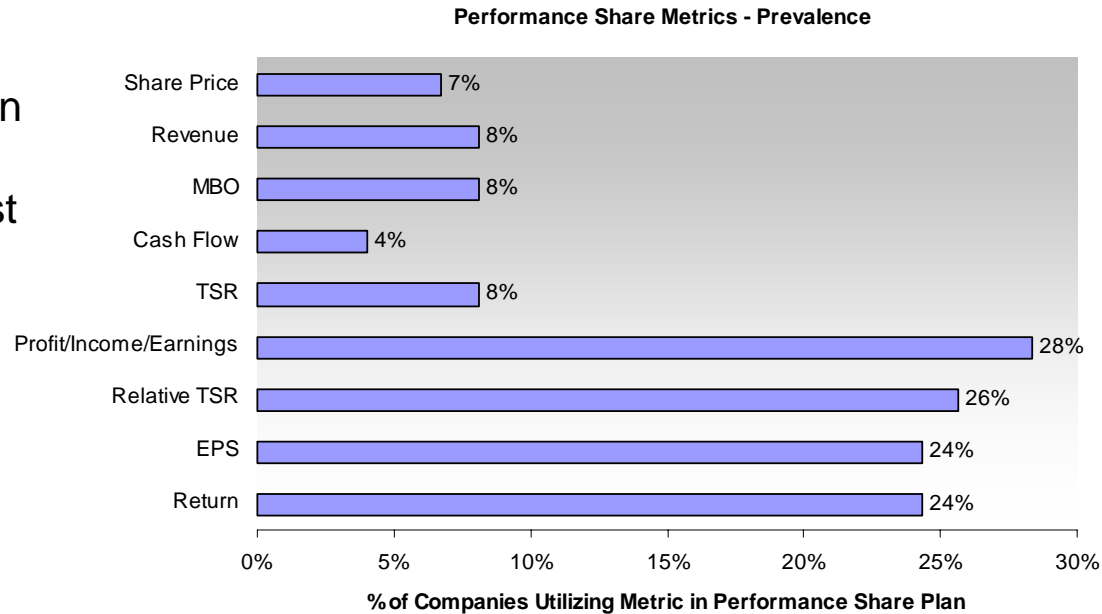


2009 Equity Vehicle Mix

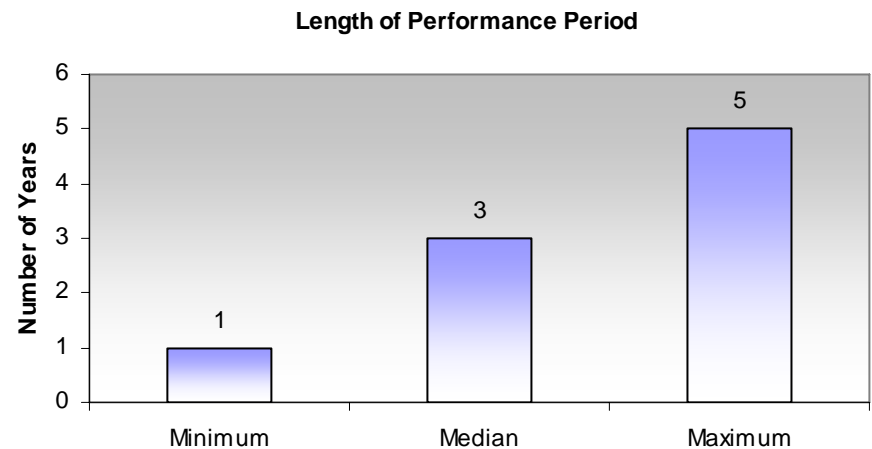


Performance Share Plans

- Almost half of the companies in our study granted performance-based shares last year, utilizing anywhere from 1 to 4 of the following metrics:



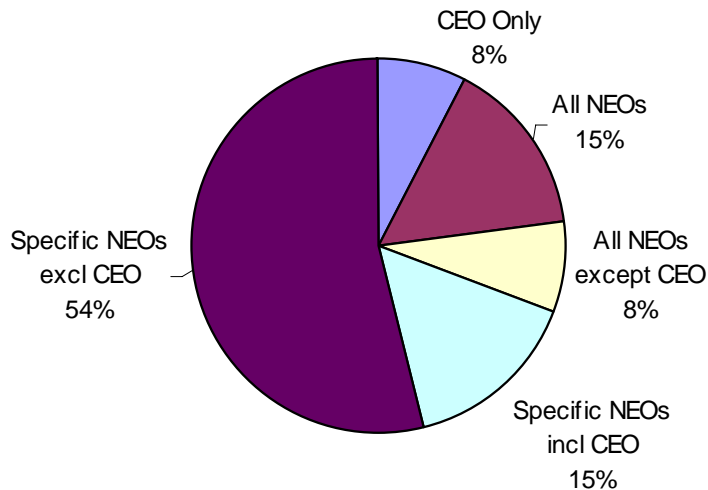
- The most common performance period is 3 years (48 companies) with several companies (14) utilizing a 1-year period and one company utilizing a 5-year period
 - Other Performance Periods
 - 2 years (3 companies)
 - 4 years (4 companies)



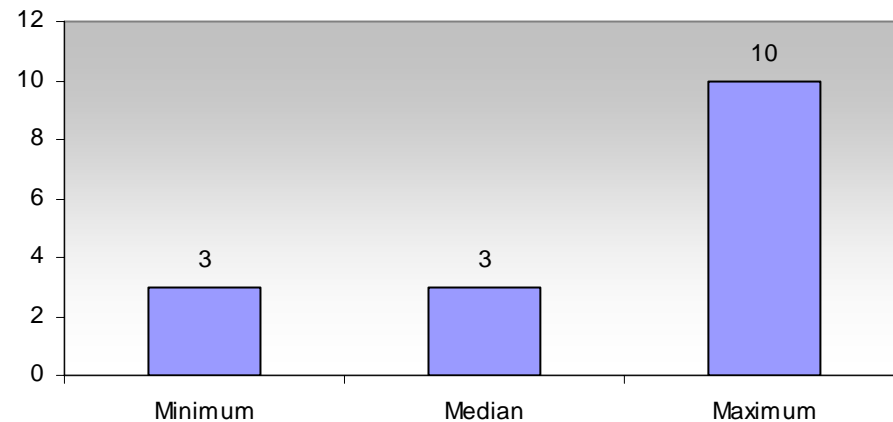
Retentive Actions

- Thirteen of the companies studied made a retention LTI grant in this last fiscal year to one or more executives
- Twelve of the companies tendered a stock option exchange some time between December 2008 and February 2010
 - 50% exchanged Options for Options
 - 50% exchanged Options for RSUs

Retention Grants - Executives Receiving



Retention Grants
Number of Years to Fully Vested



Breaking Out the Crystal Ball (Implications for 2010 and Beyond)

The Next Stage?

Assuming a continued upward climb out of the recession

- Base Salaries:
 - Freezes may be lifted
 - At executive levels, expect minimal “increases” with heightened scrutiny of pay-for-performance at the executive levels
 - Reductions may be re-instated (difference between voluntary vs. involuntary)
- Cash STI Plans:
 - We anticipate the heightened assessment of “risk” in incentive plans will cause many companies to re-evaluate metrics and the target-setting process

The Next Stage? (Cont'd)

Assuming a continued upward climb out of the recession (Cont'd)

- Long-Term Incentive Plans:
 - Any potential “windfalls” from the prior year’s activities (such as option exchanges, retention grants, granting lots of stock at the low of the market) will be closely monitored
 - New hires that came in during the downturn may now have better compensation positions than high-performing tenured employees, creating a need for a more customized approach to the annual grant process (rather than simply granting “x” number of shares to grade “y”, for example)
 - Pressure from shareholders to show ROI and effectiveness

The Next Stage?

Assuming a continued upward climb out of the recession

- Media Coverage:
 - Potential for outcry over “Big Increases” to equity grant values over last year in some sectors as stock prices rebound:
 - Preliminary research into Form 4 filings in the first part of 2010 suggests increases upwards of 40% in the Technology sector from last year
 - A deeper look shows the target grant values have merely returned to pre-recession levels with more moderate increases over that timeframe
 - Closer to 12% according to our preliminary work
 - Potential for outcry over “Big Windfalls” when executives start to become vested in their low-priced options and retention grants
 - Holding requirements may become an even bigger topic
 - The lesson: year-over-year values, when one year is an anomaly, should not be viewed in a vacuum

Be on the lookout for a Buck publication on this research in May!



Questions

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Join Us for Our Next Webcast...

- May 12, 2010
- Topic: *The Effectiveness of Equity Compensation: A Look at 2010 Practices*
- Speakers: Chris Young and Kathi Myers
- For more information about our Webcast series, contact Lorraine M. Smith at **203.352.1617** or Lorraine.M.Smith@buckconsultants.com