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Eyes Wide Open:
Global Investor Perspectives on Share Requests

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Introduction

- The following rules show convergence in these areas:
  - Increased focus on shareholder value transfer and burn rates, resulting in less than annual grants made on a merit not automatic basis for high performers
  - A premium on real performance conditions and holding requirements
  - Minimum vesting, claw backs with teeth
  - Shareholders are expanding focus beyond TSR to include operational performance conditions, with achievement of performance conditions necessary on a relative peer basis in addition to internal hurdles

Share Plan Approval Rules

Europe – ISS Share Plan Approval Voting Guidelines (except UK and Ireland)

- The shares reserved for all share plans may not exceed 5 percent of a company's issued share capital, except in the case of high-growth companies or particularly well-designed plans, in which case we allow dilution of between 5 and 10 percent: in this case, we will need to have performance conditions attached to the plans which should be acceptable under ISS criteria
- The plan(s) must be sufficiently long-term in nature/structure: the minimum vesting period must be no less than three years from date of grant
- The awards must be granted at market price. Discounts, if any, must be mitigated by performance criteria or other features that justify such discount
- If applicable, performance standard must be fully disclosed, quantified, and long-term, with relative performance measures preferred

France – ISS Share Plan Approval Voting Guidelines

- See previous slide
- The potential volume from equity-based compensation plans must not exceed 10 percent of fully diluted issued share capital
- In addition, for companies that refer to the AFEP-MEDEF Code, all awards (including stock options and warrants) to executives must be conditional upon challenging performance criteria or premium pricing. For companies referring to the Middlenext Code (or not referring to any code) at least part of the awards to executives shall be conditional upon performance criteria or premium pricing. In both cases, free shares shall remain subject to performance criteria for all beneficiaries
- For large- and mid-cap companies, the company's average three year unadjusted burn rate (or, if lower, the maximum volume per year implied by the proposal made at the general meeting) must not exceed the mean plus one standard deviation of its sector. If necessary, these sector-specific caps are adjusted so that they do not change by more than one percentage point from year to year

United Kingdom – ISS Share Plan Approval Voting Guidelines

- The LTIP is aligned with the company's strategy, is not over-complex and fosters an appropriately long-term mindset
- The proposed award levels are appropriate, and in the case of an amendment plan, any increases to the previous award levels are well-explained
- Any increase in the level of certainty of reward is matched by a material reduction in the size of awards
- The maximum payout is capped
- The vesting levels for threshold and on target performance are in line with market norms, with threshold vesting no higher than 25 percent

United Kingdom – ISS Share Plan Approval Voting Guidelines (Continued)

- The LTIP is in line with the current remuneration policy.
- Change of control, good leaver and malice/clawback provisions are present and the terms are in line with the standard practice in the UK market.
- The remuneration committee seeks to reserve a degree of discretion in line with standard UK practice.
- The company is operating within the dilution limits of the company’s share-based incentive schemes.
- There are no issues with the equity plan which would be of concern to shareholders

United States – ISS Share Plan Approval Voting Guidelines

- In the United States, public companies need to seek shareholder approval when new equity plans are adopted and materially amended per the listing exchange rules, certain tax rules and in many cases, the company’s operating documents
- Under ISS’ scorecard approach, equity pay plan proposals are evaluated using a "scorecard," which considers a host of factors that are individually weighted and then plugged into an overall assessment model
- The total maximum number of points that may be accrued under the scorecard model is 100. Absent other overriding factors, a score of 53 or higher will generally result in a positive recommendation from ISS for an equity plan proposal

United States – ISS Share Plan Approval Voting Guidelines (Continued)

- The table below summarizes the categories of factors and applicable scores for each model:

Maximum Scores by EPSC Model and Pillars

Pillar	Model	Maximum Pillar Score	Comments
Plan Cost	S&P 500, Russell 3000, Non–Russell 3000	45	All models include the same Plan Cost factors
	Special Cases – Russell 3000 / S&P 500*	50	
	Special Cases – non–Russell 3000*	60	
Plan Features	S&P 500, Russell 3000	20	All models include the same Plan Features factors
	Non-Russell 3000	30	
	Special Cases – non–Russell 3000*	35	
	Special Cases – non–Russell 3000*	40	
Grant Practices	S&P 500, Russell 3000	35	The Non–Russell 3000 model includes only Burn Rate and Duration factors. The Special Cases model for Russell 3000 / S&P 500 firms includes all Grant Practices factors except Burn Rate and Duration. The Special Cases model for non–Russell 3000 companies does not include any Grant Practices factors.
	Non-Russell 3000	25	
	Special Cases – non–Russell 3000*	15	
	Special Cases – non–Russell 3000*	0	

*Generally covers companies that recently had their IPO, were spun off, or emerged from bankruptcy that do not disclose 3 years of grant data.

United States – ISS Share Plan Approval Voting Guidelines (Continued)

- Along with the cost of administering corporate equity plans, ISS will consider numerous additional factors/practices in its scoring system, including:
  - Automatic single-trigger vesting upon a change-in-control
  - Broad discretionary vesting authority that may result in "pay for failure" or other scenarios contrary to a pay-for-performance philosophy
  - Liberal share recycling
  - The absence of a minimum required vesting period (at least one year) for grants made under the equity plan
  - The company's 3-year average burn rate relative to its industry and index peers
  - Vesting schedule(s) under the CEO's most recent equity grants during the prior three years
  - Whether dividends/dividend equivalents are only paid out if and when the underlying equity awards vest
  - The plan's estimated duration, based on the sum of shares remaining available and the new shares requested, divided by the 3-year annual average of burn rate shares
  - The proportion of the CEO's most recent equity grants/awards subject to performance conditions
  - A clawback policy that includes equity grants
  - Post-exercise/post-vesting shareholding requirements

United States – ISS Share Plan Approval Voting Guidelines (Continued)

- Some plan features will continue to automatically result in negative recommendations regardless of other factors; these items include:
  - Authority to reprice stock options without shareholder approval
  - "Liberal" change-of-control definition that could result in vesting of awards by a single trigger
  - Plans that are vehicles for "problematic pay practices"
  - Tax-gross-ups related to plan awards
  - Provisions for reload options

United States – Glass Lewis Share Plan Approval Voting Guidelines

- More of a black-box approach than ISS' approach
- Generally, Glass Lewis evaluates stock option and other equity-based compensation plans based on the following principles:
  - Program size and granting pattern
  - Program costs
  - Program features
- Overarching principles
  - Companies should only seek shares when needed
  - Focus on plan duration

United States – Glass Lewis Share Plan Approval Voting Guidelines (Continued)

- Program Size and Granting Pattern
  - Duration of existing shares
  - Pace of grants
  - Concentration ratio
- Program Costs
  - Projected Annual Costs and Expensed Costs as a % of Company Size (measured separately by Revenue, Total Book Value or OCF, and Enterprise Value)
  - Projected cost on a per employee basis
- Program Features
  - Evergreen is a deal-breaker under Glass Lewis

Key Trends in Plan Design

- ISS and Glass Lewis have become the de facto corporate governance standard setters
  - Minimum vesting and share recycling
  - Clawback and holding period requirements
  - Companies are adopting restrictive plan changes to obtain more shares under the ISS model
- Director Comp Litigation
  - Increased scrutiny around director compensation recently
  - Avoid perception of self dealing
  - Set a limit on cash and equity compensation for NED
- Section 162(m) Compliance
  - 5-yr rule!
  - Assess whether existing limit is appropriate given the Company’s future needs

Strategies and Tips for Assuring Approval

- Preparation for Share Requests
  - Analyze existing share pool and overhang levels
    - Is it necessary to seek shares at the upcoming meeting?
    - How does dilution look relative to proxy and industry peers?
  - Current and anticipated burn rate usage levels
    - How does burn rate look relative to proxy and industry peers?
  - Existing plan features
    - Is there anything that could be perceived as controversial in the plan?
    - Bring the plan to date in terms of types of awards, annual limits
- Understand Your Investors and the Proxy Advisors
  - ISS and Glass Lewis influence on your top shareholders
  - What types of investor specific guidelines exist for share requests?

Say on Pay Rules

Europe – Say on Pay (Global Principles)

- Provide shareholders with clear, comprehensive compensation disclosures
- Maintain appropriate pay-for-performance alignment with emphasis on long-term shareholder value
- Avoid arrangements that risk "pay for failure"
- Maintain independent and effective compensation committee
- Avoid inappropriate pay to non-executive directors

United Kingdom – Say on Pay (Key Considerations)

- Whether the proposals are consistent with the good practice principles set out in the voting guidelines (see next three slides)
- The linkage between the proposals and the company’s strategic objectives
- Whether or not the proposals have an appropriate long-term focus
- The extent to which the proposals help simplify executive pay
- The impact on the overall level of potential pay
- Any proposal which provides for a greater level of certainty regarding the ultimate rewards should be accompanied by a material reduction in the overall size of awards

United Kingdom – Remuneration Voting Guidelines (continued)

- The overall remuneration policy or specific scheme structures are not over-complex, have an appropriate long-term focus and have been sufficiently justified in light of the company's specific circumstances and strategic objectives
- The company's approach to fixed remuneration is appropriate
- The award levels for the different components of variable pay are capped, and the quantum is reasonable when compared to peers, and any increase in the level of certainty of reward is accompanied by a material reduction in size of awards
- Increases to the maximum award levels for the LTIP and bonus have been adequately explained
- Performance conditions for all elements of variable pay are clearly aligned with the company's strategic objectives, and vesting levels are in line with UK good practice
- Change of control, good leaver and malice/clawback provisions are in line with the standard practice in the UK market

United Kingdom – Remuneration Voting Guidelines (continued)

- The shareholding requirement for executive directors is a minimum of 200% of base salary
- Service contracts contain notice periods of no more than 12 months’ duration and potential termination payments are linked to fixed pay with no contractual entitlements to unearned bonus on termination
- Non-executive directors do not receive any performance-related remuneration beyond their standard fees
- The treatment of new joiners is appropriate, with particular attention paid to the use of buy-out awards, and that the potential for any additional awards is capped
- The remuneration committee seeks to reserve a degree of discretion in line with standard UK practice
- There are no issues in the policy which would be of concern to shareholders

United States – Say on Pay Proxy Voting Guidelines

- On January 25, 2011, the Securities and Exchange Commission adopted rule changes to implement the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act relating to shareholder approval of executive compensation
- In the United States, many companies with publicly traded stock are required to seek shareholder approval of executive compensation on an advisory based every one, two, or three years (often referred to as a "say-on-pay" vote)
- Shareholders also have the ability to cast an advisory vote on the frequency of when a say-on-pay vote occurs every six years

United States – Say on Pay Proxy Voting Guidelines (Continued)

- ISS will generally recommend in favor of annual say-on-pay votes
- If the board adopts a longer frequency for say-on-pay votes than approved by a plurality of shareholder votes, ISS will make a case-by-case recommendation
- If there is no say-on-pay or say-on-pay frequency vote on the ballot where one would otherwise be expected, and the company does not provide an explanation for the omission, ISS will generally recommend against the compensation committee chair (or full committee, as appropriate) until the company presents shareholders with an advisory vote on executive compensation

United States – Say on Pay Proxy Voting Guidelines (Continued)

- The following factors cause ISS to recommend AGAINST a say-on-pay proposal:
  - CEO pay-for-performance misalignment
  - The presence of “egregious” pay practices
  - The Board exhibits a significant level of poor communication and responsiveness to shareholders

United States – Say on Pay Proxy Voting Guidelines (Continued)

- CEO pay-for-performance misalignment is measured using certain quantitative tests
  - Relative Degree of Alignment. This relative measure compares the percentile ranks of a company's CEO pay and TSR performance, relative to an industry-and-size derived comparison group, annualized for the prior three fiscal year periods. Specifically, CEO pay is averaged for the three-year period; annualized TSR is the geometric mean of the three fiscal year TSRs in the period
  - Multiple of Median. This relative measure expresses the prior year's CEO pay as a multiple of the median pay of its comparison group for the same period
  - Pay-TSR Alignment. This absolute measure compares the trends of the CEO's annual pay and the value of an investment in the company over the prior five-year period

United States – Say on Pay Proxy Voting Guidelines (Continued)

- If the quantitative analysis determines that significant pay misalignment exists, ISS will perform a more in-depth qualitative assessment taking into consideration a number of unweighted factors to determine whether a company's pay practices mitigate or facilitate the misalignment, including:
  - The ratio of performance- to time-based equity awards
  - The overall ratio of performance-based compensation
  - The completeness of disclosure
  - The rigor of performance goals
  - The application of compensation committee discretion
  - The magnitude of pay opportunities
  - The company's peer group benchmarking practices
  - Actual results of financial/operational metrics, such as growth in revenue, profit, cash flow, etc., both absolute and relative to peers
  - Special circumstances related to, for example, CEO and executive turnovers or anomalous equity grant practices (e.g., bi-annual awards, special one-time grants)
  - Realizable and realized pay compared to granted pay

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United States – Say on Pay Proxy Voting Guidelines (Continued)

- Pay elements that are not directly based on performance are generally evaluated on a case-by-case basis.
- ISS has, however, identified certain practices that are contrary to a performance-based pay philosophy, which are listed below:
  - Egregious employment contracts
  - New CEO with overly generous new-hire package
  - Abnormally large bonus payouts without justifiable performance linkage or proper disclosure
  - Egregious pension/SERP (supplemental executive retirement plan) payouts
  - Excessive Perquisites
  - Excessive severance and/or change in control provisions
  - Tax Reimbursements
  - Dividends or dividend equivalents paid on unvested performance shares or units
  - Internal pay disparity
  - Repricing or replacing of underwater stock options/stock appreciation rights without prior shareholder approval

United States – Say on Pay Proxy Voting Guidelines (Continued)

- Under ISS's Proxy Voting Guidelines, ISS will consider the following factors when evaluating the board's responsiveness to investor input and engagement on say-on-pay issues:
  - Failure to respond to majority-supported shareholder proposals on executive pay topics
  - Failure to adequately respond to the company's previous Say on Pay proposal that received the support of less than 70% of votes cast
- When a company's prior year say-on-pay proposal received less than 70% of votes cast, ISS will determine its vote recommendation on Compensation Committee members (or, in exceptional cases, the full board) and on a company's current say-on-pay proposal, taking into account the following factors:
- The company's response to the say-on-pay vote outcome, including:
  - Disclosure of engagement efforts with major institutional investors regarding the issues that contributed to the low level of support
  - Specific actions taken to address the issues that contributed to the low level of support
  - Other recent compensation actions taken by the company
- Whether the issues raised by the say-on-pay vote are recurring or isolated
- The company's ownership structure.

United States – Glass Lewis Say on Pay Proxy Voting Guidelines

- Glass Lewis’ approach consists of two main components:
  - A qualitative assessment of the structure of a company’s compensation program and the accompanying disclosure
  - A quantitative assessment reflected in its pay-for-performance grade.
- As per Glass Lewis, a poor grade (i.e., “D” or “F”) in the pay-for-performance analysis does not automatically result in a negative vote recommendation. Conversely, a favorable grade does not guarantee a positive vote recommendation
  - A grade of “D” indicates that the company has been deficient in linking NEO pay with company performance
  - A grade of “F” indicates that a significant misalignment between pay and performance exists
  - A grade of “D” or lower for the quantitative filters generally triggers Glass Lewis’ qualitative assessment
  - A grade level of “C” generally indicates that NEO pay is sufficiently aligned with company performance

United States – Glass Lewis Say on Pay Proxy Voting Guidelines (Continued)

- Generally, companies that receive an “F” tend to get a negative vote recommendation from Glass Lewis A year-over-year “F” grade from Glass Lewis generally results in adverse vote recommendation on the Compensation Committee members for “ongoing compensation concerns” as well
- Companies that receive a “D” usually receive a “cautionary FOR” from Glass Lewis. However, a year-over-year “D” grade from Glass Lewis usually results in a negative vote recommendation on the say-on-pay proposal

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Issuer Governance Challenges

- Issuer has one global system, but has to deal with multiple regional ISS policies
- This creates challenges when operating in the US and W. Europe, especially the Bay Area, given the persistence of stock options and time-vesting RSUs
- Also problematic in one-size-fits all rules on dilution, which are applied regardless of sector
- ISS P4P system is converging with the US system, not reflective of Swiss disclosure practice

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