INTRODUCTION

Change-in-control arrangements have two key functions: attracting new management talent to a company and motivating existing executives to continue working in shareholders’ interests if leadership changes hands. By providing payments upon a change in control, these arrangements seek to relieve executives’ potential anxieties about losing their position in the event of a merger or acquisition.

Change-in-control severance packages have played a prominent role in the national conversation about executive compensation. Shareholder advisory groups are aiming to curb the use of “golden parachute” payments, delineating specific severance arrangements that could be considered “excessive payments” or “problematic pay practices.” Targeted change-in-control agreement features included cash multipliers of three times or greater, single- and modified-trigger provisions, and certain bonus definitions used to calculate the change-in-control cash payment.

In this study, Equilar examines change-in-control arrangements among Fortune 100 companies for fiscal years 2008 and 2010. This report sheds some light on recent trends in corporate-governance reform, which have been bolstered by increased public scrutiny of executive compensation. While the prevalence of change-in-control arrangements has not declined, firms are decreasing payments and instituting restrictive payment triggers related to executive termination.

The analysis includes information from corporate proxy statements, examining the following topics within change-in-control arrangements:

- Change-in-CEO multipliers from 2008 to 2010
- 2010 multipliers for CEOs and other NEOs
- Change-in-control cash payment triggers
- Definition of salary and bonus multipliers

KEY FINDINGS

- **Change-in-Control Cash Multiples Decrease for CEOs:** The prevalence of 3x salary multipliers among Fortune 100 CEOs decreased from 65.9% in 2008 to 44.2% in 2010, while the prevalence of 2x salary multipliers rose from 18.2% to 34.9%. Similarly, the prevalence of 3x bonus multipliers decreased from 65.9% in 2008 to 44.2% in 2010, while that of 2x bonus multipliers rose from 15.9% to 32.6%.

- **Over 40% of Fortune 100 Executives Receive Cash Payments upon a Change-in-Control Termination:** In 2010, 45.3% of CEOs included in the study had cash change-in-control payment arrangements in place, while 41.2% of other NEOs had such agreements.

- **Most Common Multiplier Higher for CEOs Compared to Other NEOs:** The most prevalent salary and bonus multiplier was 3x for CEOs and 2x for other NEOs.

- **Majority of Change-in-Control Payments Require “Double-Trigger” Termination Scenario:** 97.7% of companies with cash payments upon a termination related to a change-in-control required a double trigger, while the remaining 2.3% required a modified trigger.

- **Target Bonus is the Most Prevalent Bonus Definition Used in F100 Severance Formulas:** 50.8% of all change-in-control cash payments used target short-term incentives to calculate the bonus portion of the severance amount.
REPORT SCOPE AND METHODOLOGY

The information presented in Equilar’s 2011 Change-in-Control Cash Severance Analysis is derived primarily from data disclosed in SEC filings for Fortune 100 companies from fiscal years 2008 and 2010. To help put this analysis in context, the following charts summarize key financial trends for the Fortune 100 index in 2008 and 2010:

MARKET CAPITALIZATION

In 2010, publicly traded Fortune 100 companies had a median fiscal year-end market capitalization of approximately $40.8 billion. This represents a 54.5% increase from the 2008 median value of approximately $26.4 billion.

ANNUAL REVENUES

The median annual revenues for Fortune 100 companies increased by 9.8% from 2008 to 2010. In 2010, Fortune 100 companies earned median annual revenues of approximately $49.4 billion.

NET INCOME

In 2010, Fortune 100 companies earned median annual revenues of approximately $2.6 billion. The median net income for Fortune 100 companies increased by 18.2% from 2008 to 2010.
**Definitions**

- **Change-in-Control**: A change in control occurs when a company is acquired by another entity or when a threshold percentage of a company's shares are acquired by one person or group. For the purposes of change-in-control arrangements with company executives, change-in-control scenarios are further categorized into “double-trigger,” “modified-trigger,” and “single trigger” events, which define the specific terms under which payments are made in connection with a change in control.

- **Double Trigger**: A double trigger involves 1) a change in control and 2) a termination of the executive's employment by the company without cause or by the executive with good reason, as defined by each agreement. For double-trigger provisions to become payable, the termination must occur within a specified period of time before or after a change in control, also known as the termination window.

  - Prudential Financial Inc. (PRU)
    - DEF 14A filed on March 22, 2011
    - [Link to filing](#)
    - “Our executive officers, including the NEOs, except for our CEO, are eligible for severance payments in the event of an involuntary termination of employment without ‘cause.’ These officers and our CEO are also eligible for ‘double-trigger’ severance payments in the event of an involuntary termination of employment without ‘cause’ or a termination of employment with ‘good reason’ in connection with a change in control of the Company.”

- **Modified Trigger**: A modified trigger involves 1) a change in control and 2) a termination of the executive for any reason within a designated termination window before or after the change in control. This event differs from a double trigger in that the executive will receive payments regardless of the reason for termination.

  - Lowe's Companies, Inc. (LOW)
    - DEF 14A filed on April 11, 2011
    - [Link to filing](#)
    - “The agreements provide for certain benefits if the Company experiences a change-in-control followed by termination of the executive's employment:
      - by the Company's successor without cause;
      - by the executive during the 30-day period following the first anniversary of the change-in-control; or
      - by the executive for certain reasons, including a downgrading of the executive's position.

      ‘Cause’ means continued and willful failure to perform duties or conduct demonstrably and materially injurious to the Company or its affiliates.”

- **Single Trigger**: A single trigger involves only a change in control and does not require a termination of employment. Single trigger provisions become payable immediately following a change in control.

- **Cash Multiplier**: The cash multiplier is the numerical value by which an executive's salary or the sum of the executive's salary and bonus is multiplied to make up the cash portion of the change-in-control severance payment. Variations of the payment formula depend on the specific definitions of salary and bonus within each agreement.

  - AT&T Inc. (T)
    - DEF 14A filed on March 10, 2011
    - [Link to filing](#)
    - “The Change-in-Control Severance Plan offers benefits to an officer who is terminated or otherwise leaves our Company for ‘good reason’ after a change-in-control. These benefits include a payment equal to 2.99 times the sum of the executive’s most recent salary and target bonus.”
**Change-in-Control Cash Multipliers Decrease for CEOs**

For this analysis, a change-in-control provision includes cash payments made in addition to earned amounts, upon termination, in connection with a change in control. Cash payments made in connection with a change in control are generally structured as a multiple of (i) an executive’s base salary or (ii) the sum of an executive’s base salary and bonus.

In 2010, 45.3% of the Fortune 100 companies analyzed had change-in-control cash severance policies in place for their CEOs, compared to 45.8% in 2008. While the prevalence of such arrangements has remained stable over the past two years, the size of the cash multiple has dropped significantly for CEOs.

The prevalence of a 3x salary multiplier among CEOs decreased from 65.9% in 2008 to 44.2% in 2010, while that of a 2x salary multiplier rose from 18.2% in 2008 to 34.9% in 2010. Similarly, the prevalence of a 3x bonus multiplier decreased from 65.9% to 44.2% in 2010, while that of a 2x bonus multiplier rose from 15.9% to 32.6% in 2010.

The following chart compares the average cash multiples for CEOs in 2008 and 2010:

The disclosure example below highlights a company which reduced the cash multiplier in its change-in-control arrangements between 2008 and 2010, in compliance with changing market practices:

- *MetLife Inc. (MET)*
  DEF 14A filed on March 28, 2011
  Link to filing

  “Under this plan, had a change-in-control occurred on the Trigger Date, and the Named Executive Officer’s terms and conditions of employment during the three-year period beginning with the Trigger Date (Employment Period) not satisfied specified standards, the Named Executive Officer could have terminated employment and received severance pay and related benefits.

  […]

  *Effective June 14, 2010 the amount of severance pay that could be paid under the plan changed from three times to two times the sum of the executive’s annual salary rate plus the average of the executive’s annual incentive awards for the three fiscal years prior to the change-in-control.*"
Change-in-Control Cash Severance Multipliers

In 2010, 45.3% of CEOs at the Fortune 100 companies analyzed had cash change-in-control payment arrangements in place, while 41.2% of other NEOs had such agreements. Furthermore, the most prevalent salary and bonus multiplier for CEOs was 3x, while that of other NEOs was 2x. No company provided for change-in-control related severance payments with cash multiples greater than 3x.

The following charts display the prevalence of salary and bonus multipliers for CEOs and other NEOs among executives who were eligible for cash payments in connection with a change in control:

**CEO Salary and Bonus Multipliers**

**Other NEO Salary and Bonus Multipliers**
CHANGE-IN-CONTROL PAYMENT TRIGGERS BECOME MORE RESTRICTIVE

In 2010, the prevalence of double-trigger provisions among CEOs with change-in-control arrangements was 97.7%, compared to 84.1% in 2008. The prevalence of modified-trigger payments declined, from 15.9% in 2008 to 2.3% in 2010. There were no cash provisions available through a single trigger in either year.

The following disclosure example highlights the elimination of a modified-trigger feature between 2008 and 2010:

- Johnson Controls, Inc. (JCI)
DEF 14A filed on December 10, 2010
Link to filing

“The executive officer also has the right, exercisable during a 30-day period following the first anniversary of a change of control, to terminate his or her employment with us for any reason and receive the severance payments and the continued medical and welfare benefits we describe above as if the executive officer had terminated for good reason. During fiscal year 2009, the Committee eliminated this provision for any new executive officers elected after September 14, 2009.”

DISTRIBUTION OF CHANGE-IN-CONTROL BONUS DEFINITIONS

While a change-in-control payment formula is determined largely by the cash multiplier, it is also dependent upon the definition of the salary and bonus from which the cash payout is calculated. Though the majority of salary definitions cited variations of the term “annual base salary,” bonus descriptions showed more variety. The following chart displays the distribution of bonus definitions among all Fortune 100 executives with change-in-control provisions for bonus payments. “Other” includes descriptions that provide for the greater of several bonus definitions, which may include target annual bonus, the average of paid bonuses from the three years prior to termination, etc.