CAPflash
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2012 Proxy Season Update – Experience During our Second Year of Say on Pay Voting

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As of May 25, 2012, we have compiled voting results for 292 S&P 500 companies at their 2012 annual meetings, providing early insight into Say on Pay votes during the proxy season.

Say on Pay Update

2012 marks the second year of mandatory Say on Pay voting. In 2011, the SEC issued final rules implementing Section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). Dodd-Frank provides shareholders of US public companies with the right to cast three types of advisory votes related to executive compensation:

1. A vote to approve the compensation of the Named Executive Officers (NEOs), effective for shareholder meetings occurring on or after January 21, 2011;

2. A vote on the frequency with which shareholders should be entitled to cast Say on Pay votes (every one, two or three years), effective for shareholder meetings occurring on or after January 21, 2011; and

3. A vote on golden parachute arrangements for NEOs related to a sale, consolidation or merger, effective April 25, 2011.

***CAP Comment:** While these votes are non-binding, we see evidence that companies carefully evaluate their vote results, taking some action if there is low shareholder support for the company's executive compensation program. In 2011, a consensus developed that a low pass rate was a concern.*

SAY ON PAY VOTE RESULTS AMONG THE S&P 500

So far this season, Say on Pay resolutions received majority shareholder support at all but seven S&P 500 companies.[1] The seven companies where a majority of shareholders did not support the executive compensation program were International Game Technology, Citigroup, Cooper Industries PLC, Mylan, NRG Energy, Pitney Bowes and Simon Property Group.

Comparison of year-to-date results for 2012 to 2011 results shows a consistent pattern. We found that the median vote in support of a Say on Pay resolution is 93.7% s in 2012. This is almost identical to the 93.2% median support level that we observed last year.

1 Outside of the S&P 500, an additional 22 companies did not receive majority shareholder support for their NEO compensation program as of 5/25/2012: Actuant Corporation, Argo Group International, Cenveo, Charles River Laboratories, Chemed Corporation, Community Health Systems, Comstock Resources, First California Financial, FirstMerit Corp., Gentiva Health Services, Hercules Offshore, Infinera Corporation, KB Home, Knight Capital Group, Manitowoc Company, OM Group, Palomar Medical Tech., Phoenix Companies, Sterling Bancorp, The Ryland Group, Tower Group, and Viad Corp.

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2011 AND 2012 SAY ON PAY VOTE RESULTS

% in Favor	# of Companies in 2012	% of Companies in 2012	% of Companies in 2011
90% - 100%	200	69%	63%
80% - 90%	42	14%	17%
70% - 80%	17	6%	10%
50% - 70%	26	9%	9%
0% - 50%	7	2%	2%

CAP Comment: *While a company does not "fail" its Say on Pay vote unless a majority of shareholders vote against the compensation program, most companies have received 90+% shareholder support and an "acceptable" shareholder support threshold has emerged around 70% - 80%. ISS identified 70% as a minimum acceptable level of support, while Glass Lewis prefers 75%. Among institutions, CalSTRS and Black Rock identified 75% and 80%, respectively.*

Notably, all of the S&P 500 companies that failed Say on Pay in 2011 that have completed their 2012 Say on Pay votes, have received passing grades from shareholders. Some of these companies have made significant changes to pay programs. In addition, management teams at these companies have devoted considerable effort to shareholder outreach and engagement to better understand the issues that may be creating concerns.

Company Failing Say on Pay in 2011	% Support Received in 2012 Say on Pay Vote	Modifications Made to Compensation Program
Hewlett-Packard	77%	• Target compensation at the market median • Limited the use of discretion in pay decisions and provided more detailed disclosure • Redesigned the annual incentive plan • Disclosed more detailed information about historical performance targets, actual performance against targets, and payouts under the annual incentive plan • Changed the structure and design of CEO's compensation, to increase performance-based elements • Eliminated tax gross-ups for Section 16 officers except for gross-ups on relocation benefits • Amended Severance Plan for Executive Officers to reduce the need for individual agreements and the use of discretion
Jacobs Engineering	96%	• Performance-based market stock unit grants replaced grants of time-based restricted stock
Masco Corp.	95%	• Reduced stock options and introduced long-term cash incentive based on return on invested capital performance over 3 years • Changed mix of long-term awards • Eliminated excise tax gross-up feature on all equity grants beginning in 2012 • Increased CEO's stock ownership requirements • Adopted "double-trigger" vesting of equity on a change in control
Stanley Black & Decker	93%	• Modified Compensation Committee membership • Increased stock ownership requirements for executive officers and directors • Imposed a 1-year post exercise holding period on options and RSU grants to executive officers • Replaced "single-trigger" change in control provisions with "double-trigger" provisions

CAP Comment: *SEC disclosure rules require additional disclosure in the CD&A regarding whether, and if so how, companies have considered the results of the most recent Say on Pay vote.*

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Several factors impact Say on Pay Voting results. We have observed a clear link between voting outcomes and company performance as measured by Total Shareholder Return ("TSR"). Not surprisingly, companies that enjoy high levels of shareholder support tend to perform better. Companies with lower performance tend to receive lower shareholder support.

TSR VS. SAY ON PAY VOTE RESULTS

% in Favor	Average 1-Yr TSR @ 12/31/11 Prior to 2012 Annual Meetings	Average 1-Yr TSR @ 12/31/10 Prior to 2011 Annual Meetings
90% - 100%	3.4%	24.5%
80% - 90%	-5.3%	24.1%
70% - 80%	-7.6%	17.3%
50% - 70%	-5.8%	8.0%
0% - 50%	-5.9%	9.6%

The recommendations of the proxy advisory services also have an impact. For example, when ISS recommends an "Against" vote on Say on Pay, the voting outcome is normally low. To date in 2012, we found that companies receiving a "For" recommendation from ISS had average shareholder support of 93%. In contrast, companies receiving an "Against" recommendation from ISS had average shareholder support of only 60%.

Among companies where ISS recommended "Against" the Say on Pay proposal, 93% received less than 80% support.

Companies Receiving "Against" Vote Recommendation		
% in Favor	# of Companies	% of Companies
90% - 100%	0	0%
80% - 90%	3	7%
< 80%	38	93%

Given the growing influence of the proxy advisory firms, more and more companies are pushing back. Many companies have been proactive during this proxy season, with more than 50 firms filing supplementary soliciting materials. Prominent examples include Qualcom and Disney. Companies provide additional soliciting material to rebut the vote recommendations of the proxy advisory firms. While the supplemental materials do not impact the recommendation of the proxy advisory firms, they are positive in terms of investor outreach. Arguments over the appropriateness of peer groups selected by the proxy advisory firms are relatively common. In addition, a number of companies have adopted the proxy summary concept to direct attention to key messages, highlight the proposals that shareholders will be voting on and supplement the pay orientated disclosure provided in the CD&A.

SAY ON PAY FREQUENCY VOTE RESULTS

An annual vote frequency emerged as the clear shareholder preference in 2011. Among S&P 500 companies reporting vote results, a majority of shareholders supported an annual frequency at 94% of companies. This differs from vote recommendations, with only 70% of the companies recommending an annual vote.

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Board Recommendation for Vote Frequency	# of Companies
Annual	70%
Biennial	3%
Triennial	23%
No Recommendation	4%

Frequency Receiving Majority Shareholder Support	% of Companies
Annual	94%
Biennial	0%
Triennial	5%
None (only plurality)	1%

The strong support for annual votes is not a surprise. 39 institutional investors, representing more than $830 billion in assets, issued a public call for companies and investors to support annual advisory votes on executive compensation in 2011 proxy statements. Similarly, a number of major mutual funds, as well as ISS and Glass Lewis, have indicated support for annual Say on Pay votes.

CAP Comment: *Over time, we expect the prevalence of annual Say on Pay voting to increase.*

CAP Comment: *Following the frequency vote, the SEC rules mandate disclosure through an 8-K of how often the company will hold future Say on Pay votes. Issuers must also provide proxy-based disclosure of the current frequency of Say on Pay votes and when the next scheduled Say on Pay vote will occur.*

CAP Comment: *For companies that conduct Say on Pay vote frequency in line with the preference of a majority of shareholders, shareholder frequency proposals can be excluded from the proxy for six years.*

Conclusion

Last year many questioned what level of shareholder support should be viewed as "acceptable." Based on experience to date, the acceptable "threshold" will be around 80% support, a higher hurdle than simply a pass / fail test. This is somewhat higher than the minimums identified by ISS and Glass Lewis, and should be sufficient to avoid undue scrutiny of the compensation program.

Going forward, a Say on Pay vote will be an annual event at most companies. Our experience indicates that Say on Pay voting has been a catalyst for change, and certain themes have emerged:

- Companies with stronger performance generally receive higher levels of shareholder support;
- Negative vote recommendations from the shareholder advisory firms will likely reduce the vote below the "acceptable" level and companies will need to campaign to obtain a positive voting outcome;
- Many companies have increased dialogue with their largest investors by engaging early;
- Say on Pay proposals include supporting statements;
- Use of executive summaries in the Compensation Discussion and Analysis (CD&A) of the proxy statement is commonplace; and
- Use of a proxy summary or potentially filing supplemental material to rebut negative voting recommendations should be considered.

Please contact us at (212) 921-9350 if you have any questions about the issues discussed above or would like to discuss your own executive compensation issues. You can access our website at www.capartners.com for more information on executive compensation.