The Office Of
State Treasurer
Denise L. Nappier

News

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Connecticut Treasury's 2009 Proxy Year Reflects Fiscal Crisis, New Shareholder Rights and Breakthroughs on Climate and Energy Policies

HARTFORD—Connecticut State Treasurer Denise L. Nappier, principal fiduciary of the $20 billion Connecticut Retirement Plans and Trust Funds (CRPTF), announced today that the CRPTF's 2009 proxy season was marked by record agreements with portfolio companies on several corporate governance issues, including severance payments, internal pay equity, compensation consultant disclosure and sustainability. The CRPTF also continued to play an important role in shaping and advancing public policy and regulatory developments aimed at improving corporate governance for U.S. companies overall.

In commenting on the results of the proxy season, Nappier said that there was a renewed and heightened sense of awareness, determination and cooperation on the corporate governance front that brought about solid results. "The on-going financial crisis spurred greater interest in promoting responsible corporate behavior as an important element in discussions about how to rebuild and restore our economy to complete and sustainable health," Nappier said.

For the Connecticut pension fund, executive compensation topped the list of intense shareholder activism and was supported by calls from the general public to stop excessive pay that insulates corporate leaders from downside risk and rewards failure. The public's outcry was a welcome support to the active shareholders' world of long-standing concern and advocacy, prompting some directors to make immediate significant corporate governance changes, and focusing lawmakers in Washington on redesigning the federal regulatory landscape to better protect investors' interests.

In 2009, the CRPTF engaged with major U.S. companies that helped advance a number of important governance initiatives; the CRPTF:

- Engaged **Citigroup Inc.** and **AIG** on issues of systemic risk and executive compensation. Additionally, the CRPTF joined other institutional investors in voicing concern over the lack of risk management, board accountability and transparency associated with **Bank of America's** acquisition of **Merrill Lynch**.

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- Filed innovative shareholder resolutions on Say on Pay, which would allow shareholders to cast an annual advisory vote on the executive pay package. The CRPTF won majority votes at three companies—**Sun Microsystems**, **CVS Caremark**, and **Tupperware Brands**—and received high shareholder votes at two others. A sixth resolution at **Goldman** Sachs was withdrawn after the federal government compelled the company to implement Say on Pay as part of the Troubled Asset Relief Program (TARP) program.
- Garnered settlements with **The Limited Brands**, **Merck & Co., Inc.**, and **Avon Products, Inc.** that resulted in important disclosures on compensation consultant independence that exceed current Securities and Exchange Commission (SEC) requirements;
- Reached agreements with **Ameriprise Financial**, **Anadarko Petroleum Corporation**, and **Schering Plough Corporation** after asking each company's compensation committee to adopt a policy regarding severance agreements with senior executives.
- Successfully engaged with **Goodyear Tire & Rubber** and **Lockheed Martin** on the role internal pay equity, defined as the gap in pay between the chief executive officer and other named executive officers (NEOs), plays in executive pay-setting decisions.
- Struck an agreement with electric energy company **NV Energy, Inc.** in which the company agreed to issue a Sustainability Report to shareholders with specific attention to energy conservation and efficiency. The report was issued in July 2009.
- Joined with other institutional investors on innovative and "classic" corporate governance issues, including Hold 'Til Retirement and separation of the chair and CEO.

In her efforts to promote stability in the financial markets, Nappier commented extensively to regulatory agencies and members of Congress on several corporate governance issues that have a significant impact on institutional investors. She joined other major institutional investors in sending a letter to Congressional leaders and SEC Chair Mary Schapiro on principles for regulatory reform that detailed key protections investors are seeking in reform measurers. She also supported the role of a strong SEC as the preeminent agency for investor protection.

The Treasurer continued her engagement with the SEC on the disclosure of the relationships between compensation consultants, board compensation committees and company management. Through her efforts, the SEC agreed to include heightened disclosure of compensation consultant independence as part of a comprehensive proxy disclosure reform package issued for comment in July 2009. In addition, Nappier issued several additional comment letters to the SEC on other proposed rules relating to financial regulatory reform, including oversight of credit rating agencies, election of corporate directors, shareholder rights and executive pay rules.

"Federal regulatory reform combined with new shareholder rights will require our companies to lead with transparency, accountability and ethical behavior in order to rebuild investor confidence both here and abroad. That is the lesson of the unprecedented market unrest that plagued the U.S. and global economy, and whose effects reached all the way down to the general public, taxpayers, institutional investors, as well as 401(k) participants who least can afford to bear the brunt of the hardship," Nappier said.

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Summary of Proxy Season 2009 for the Connecticut Retirement Plans and Trust Funds (CRPTF)

The CRPTF filed a total of 25 shareholder resolutions in 2009 on topics including executive compensation, energy and climate and other corporate governance issues. The CRPTF filed 16 resolutions as primary sponsor, and co-filed an additional nine resolutions. Eleven proposals were withdrawn and 13 went to a vote. A resolution filed at General Motors on greenhouse gas emissions was preempted when the company filed for bankruptcy protection in June.

Say on Pay

Executive Compensation – long a focus of Treasurer Nappier's shareholder activism – received considerable attention in Washington and in the media, as the financial crisis highlighted pay practices that were unrelated to performance. When the government used taxpayer money to bail out corporate failures, shareholders and taxpayers were increasingly outraged at executives who walked away with millions.

Congress put constraints on pay at companies that received government assistance, particularly through the Troubled Asset Relief Program (TARP). All companies receiving TARP funds were required to include a non-binding advisory vote on executive compensation, or Say on Pay, on their annual proxy ballot.

The CRPTF filed or co-filed six resolutions at portfolio companies asking for Say on Pay. In an innovative turn, three of the Say on Pay resolutions focused on the need for better internal pay equity, or the relationship between compensation received by the chief executive officer and that received by other named executive officers (NEOs). (See attached background material for more information on internal pay equity.) These resolutions were filed at Tupperware Brands, ConocoPhillips, and CVS Caremark; proposals filed at Tupperware and CVS received majority votes of 63 percent and 59 percent, respectively. The proposal at ConocoPhillips received a near-majority, netting 49.9 percent shareholder support.

Other Say on Pay resolutions were filed at Sun Microsystems (67 percent) and WellPoint, Inc. (47.2 percent). The proposal filed at Goldman Sachs was withdrawn after the federal government compelled companies receiving TARP money to include an advisory vote on executive compensation on their 2009 proxy ballot. Goldman Sachs has since paid back its TARP funds – and shareholders are continuing to urge the company to include an advisory vote on their 2010 proxy as a matter of company policy, rather than in response to a federal mandate.

Compensation Consultant Disclosure

The CRPTF filed shareholder resolutions at portfolio companies asking them to provide important disclosures in their annual proxy statements on the relationships between the compensation consultant engaged by the board compensation committee and company management. The proposal specifically asks if the board compensation consultant provides any services other than executive compensation consulting to the company, and if so, for disclosure of all fees paid to the consulting firm for all services provided in the last fiscal year. It also requests information on the relationship between compensation received by individual consultants and the consulting firm's provision of other services. The proposal was based on a settlement reached with Caterpillar Inc. last year through which the company agreed to list both the fees for all services provided by its compensation consultant to the board and management, and whether the compensation consultant engaged by the board compensation committee held an equity interest in the consulting firm.

The CRPTF filed or co-filed five shareholder proposals in 2009 on compensation consultant disclosure. Three resolutions, filed at The Limited Brands, Merck & Co., Inc., and Avon Products, Inc., were withdrawn after the companies agreed to provide varying levels of disclosure relating to their use of compensation consultants. Through the settlement, The Limited included a description of all services rendered by the compensation consulting firm and the fees paid by the company to the consulting firm for non-compensation consulting services as a percentage of the consulting firm's total revenues. During the engagement period with the CRPTF, Merck switched to an independent compensation consultant; however, the company did say that it would include information on the scope of services and fees paid for such services in the annual proxy statement if it chooses to engage a non-independent compensation consulting firm in the future. Finally, Avon agreed to adopt a policy barring the use of non-independent compensation consultants similar to the language on compensation consultant independence contained in the CRPTF's Domestic Proxy Voting Policies.

Resolutions filed at Citigroup Inc. and Halliburton went to a vote in 2009. At Citigroup Inc., the proposal was backed by major proxy voting agencies RiskMetrics and Glass Lewis, and received 48 percent shareholder support. Co-filed with the AFL-CIO, the resolution at Halliburton won 47.4 percent of the vote.

Treasurer Nappier also wrote to the four largest compensation consulting firms by market share requesting that the firms provide copies of written policies and standards designed to mitigate potential conflicts of interest that may arise from engagements where the firms provide both executive and non-executive compensation consulting services. Hewitt Associates, Mercer Human Resource Consulting, Towers Perrin and Watson Wyatt all participated in the engagement.

Severance Policy

The CRPT filed three shareholder resolutions requesting compensation committees to adopt a policy on severance pay. Settlements were reached between the CRPTF and all three companies, which included Anadarko Petroleum, Ameriprise Financial, and Schering Plough.

Anadarko agreed to adopt a policy requiring periodic review of severance arrangements, including employment contracts with executives, accumulated wealth and other compensation such as pension payments, tax gross ups, and related issues. Ameriprise agreed that its compensation committee will annually review a report on severance benefits by its independent compensation consultant during the executive pay-setting process. Finally, Schering Plough agreed that its compensation and governance committee will draft a policy on severance agreements for adoption in September, and Treasurer Nappier will have the opportunity to review and directly comment on the policy prior to its ratification. Treasurer Nappier met with Schering Plough CEO Fred Hassan to discuss the issue earlier this year.

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Internal Pay Equity

The CRPTF began focusing on internal pay equity, defined as the gap in pay between the chief executive officer and other named executive officers (NEOs), as an important indicator of governance and management risk. A larger percentage of top executive pay going to the CEO may be associated with lower firm value, weaker shareholder rights, more management-entrenching governance provisions and unchanged performance when CEOs turn over.

High levels of pay disparity also may indicate a company culture that discourages teamwork and puts excessive emphasis on the CEO's contributions. A large divergence between CEO and other top executive compensation may imply that there is a chasm in ability and performance between the individuals at those two levels. This in turn suggests that the board may not be adequately planning for internal CEO succession. Because poorly planned transitions can be highly disruptive and may put the company at risk, failure to engage in succession planning has real consequences for shareholders.

The CRPTF continued its engagement on internal pay equity in the 2009 proxy season, brokering agreements with Goodyear Tire & Rubber and Lockheed Martin through which both companies will exceed SEC reporting requirements in disclosing that they will consider internal pay equity as part of the executive pay-setting process. Last year, the CRPTF reached similar settlements with Abercrombie & Fitch and supermarket conglomerate Supervalu. Resolutions with each company were withdrawn as a result of the successful dialogues.

Hold Till Retirement

The CRPTF co-filed a resolution with the American Federation of State, County and Municipal Employees (AFSCME) at Dow Chemical requesting that the company adopt a policy that a significant portion of equity compensation be held until the executive retires as a continuing link between compensation and creation of long term shareholder value. The resolution received 35.2% shareholder support.

A second resolution was co-filed with AFSCME at AIG, garnering 54 percent of the non-trustee vote. However, due to the government's control of 77.9 percent of the voting power, the resolution ultimately failed to receive a majority of the votes cast.

Corporate Governance

The CRPTF co-filed two resolutions calling for the separation of the positions of Chair and CEO at Time Warner and Exxon Mobil. The resolution at Time Warner was withdrawn when the company adopted a policy that the board would review at least annually whether it was in the best interest of the company to have a governance structure of a Lead Independent Director with the CEO also being board chairman, or whether to have an independent member of the board be the chair. The resolution at Exxon Mobil–which was drafted as a binding by-law amendment–received 29.5% shareholder support.

Climate Change and Energy Issues

The CRPTF filed five shareholder resolutions relating to climate change and energy issues. The resolution at NV Energy (the principal electric utility in Nevada) was withdrawn when the company agreed to issue a Sustainability Report to shareholders with specific attention to energy conservation and efficiency (the report was issued in July 2009). At Home Depot, the CRPTF shareholder resolution requested that the company set targets for energy use reductions and report to shareholders on progress in achieving them received a 23% vote. And a resolution filed at major electric utility Southern Company requesting it set greenhouse gas emission goals received a 10% vote.

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