IN THE NEWS

LEGISLATORS TAKE AIM AT EXECUTIVE COMPENSATION

WHAT'S HAPPENED

As the expert witness against the egregious payouts to Enron executives, Longnecker & Associates ("L&A") has observed the mounting frustration of legislators since 2002. As a result, executive compensation has been placed squarely in the sights of key legislative bodies. Specifically, the following actions have been taken:

2002

Legislators passed the Sarbanes-Oxley, which has greatly tightened the governance & reporting process for public company executives and directors.

2004

The **IRS** provided early guidance on tightening the restrictions of deferred compensation through the American Jobs Creation Act 409A.

2004

The **IRS** announced random audits of US companies' executive Compensation practices. This was done to create a template for future audits throughout the US.

2005

FASB enacted the expensing of stock options through FASB 123(R).

2005

Delaware Judicial Court rulings increased the personal liability for board directors who either knowingly approved egregious executive pay, or failed to do their job.

2006

SEC approved new regulations that require public companies to better disclose executive pay practices.

March 28, 2007

The **House of Representatives** approved the "Say on Pay" Act, whereby shareholders would have the right to cast non-binding votes on US public companies' top executives pay.

August 21 2007

The **SEC** sent comment letters to 300 publicly traded companies asking the CEO to answer 10 to 30 questions detailed in the company's Compensation, Discussion and Analysis (CD&A). More details provided below.

WHAT WILL HAPPEN

September 2007

The **SEC** announced that more executive compensation comment letters, asking for CD & A clarification, will be sent out to U.S. public companies in October 2007.

Fall 2007

The **SENATE** is expected to decide upon approving the "Say on Pay" Act.

Fall 2007

The **SENATE** is expected to consider Legislation that would impose a $1 million cap on the amount of compensation an individual could place annually into a nonqualified deferred compensation account.

Summer 2008

The **SEC** announced that they will review company responses to the comment letters on executive compensation and provide further guidance in the summer of 2008– conveniently before the election.

December 2008

The **IRS** announced in September 2007 that public and private companies now have until December 2008 to comply with new 409A deferred compensation rules. Special Note: Since 2008 is a key election year, L&A believes (1) that a good deal of this activity is politically motivated and (2) more is yet to come.

WHAT TO DO

Remember that you, not the politicians or regulators, are charged with the leadership of Corporate America. You have a fiduciary responsibility to take care of the great companies you lead. Always do what is in your company's best interests by not giving into the "tail wagging the dog" syndrome. The U.S. always responds to the challenges it faces– today we face a tough one in the area of executive pay. With that being said, Longnecker & Associates is confident that sound business practices from directors and leaders will guide American business through this transitional period.

As trusted advisors to many executives and directors, L&A has provided a list of **"TO DO"** considerations for: (1) public companies responding to comment letters, or (2) companies watching from the sidelines.

For those that have or will receive comment letters from the SEC, L&A has observed and recommends the following:

(1) The SEC letters have confusing language with regards to compensation items that call for an immediate response versus future changes in next year's proxy. **TO DO** L&A recommends companies consider styling their responses to the SEC as items they will clarify in the 2008 proxy vs. those items that appear to already be complaints with SEC regulations.

(2) The SEC letters ask for a response detailing the company's responses to comments or explaining when to expect a response by September 21, 2007. **TO DO** L&A advises companies to try to meet the 21st deadline by outlining what actions the company will take in the coming year to revise the CD&A or summary compensation table. However, be cautious in your response by taking the approach of, "We would rather be right, than right on time."

(3) The SEC letters typically ask for specific clarification about the performance of the company or an individual that justifies the executive's compensation. **TO DO** This is a complicated area where companies do not want to provide future guidance, confidential and/or competitive information. L&A has advised companies to consider better explanation for payouts where necessary but do not feel forced to usurp the wisdom and decision making authority of directors elected to govern the policies and practices of the organization. L&A believes some discretion is healthy.

(4) The tone of the SEC letters often incites emotional reactions, and the nature of many of the requests go far beyond the original "principles-based" guidance. **TO DO** Breathe first, then write. L&A advises companies to consider drafting a response coupled with a review by: (1) inside executives and legal counsel members, (2) outside legal counsel and consultants, and (3) the compensation committee.

(5) If the SEC's requests are taken literally, direct responses may actually create compensation policies where there currently are none. **TO DO** Create classifications of responses:
    (1) Responses that are clarification only and would not require compensation committee action or policy change, and
    (2) Responses that would actually change or create new compensation policies and/or practices.

For those watching on the sidelines, and all others, L&A recommends the following:

(6) **TO DO** Think ahead to the 2008 Proxy Filings. L&A does not expect the SEC to amend current requirements before 2008, so prepare now. Determine proxy best practices, watch for emerging trends in executive compensation, and keep the compensation committee as educated and up to date as possible.

(7) **TO DO** Ensure alignment of: (1) Compensation Committee Charter, (2) CD&A, (3) actual compensation practices and (4) performance of the company. Once the company has analyzed these items, ensured their alignment, and succinctly disclosed their alignment, everyone will breathe a little easier.

(8) **TO DO** Persevere. While many companies may feel like these changes are tremendous growing pains, executive compensation will ultimately be better for it. However, L&A will continue to strive to educate those involved in executive compensation to provide the thought leadership that is necessary to innovate leading edge compensation practices.

(9) **TO DO** Stay tuned. The SEC has so far declined any attempt for us at L&A, or other company counsel, to come visit them in person to discuss. Their response to us, to date, is that once they get the replies to the comment letters back, they will begin setting up personal corporate visits. This adds to the mounting frustration. However, we are working around the boundaries of the SEC by getting as much information as we can.

We at L&A are confident that Corporate America and its leaders will get through this time of over-regulation – we must, or the U.S. as we know it will fall behind other nations. It's a shame about the Enron's of the U.S. and how they allowed those with hidden "agendas" to paint all of Corporate America as greedy. Rest assured, there are still companies like that out there, but (1) they represent 1% of the total and (2) we all can play a roll in making the right decisions, so that we can ultimately make the difference we are called to make!