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Executive Compensation in Extreme Times: Advice for Companies and Their Executives

Presented by

Mark Poerio and Dan Brandenburg

The Wagner Law Group

800 Connecticut Avenue, N.W.,

Washington, D.C. 20006

Tel: (202) 969-2800 / Website: www.wagnerlawgroup.com

mpoerio@wagnerlawgroup.com

dbrandenburg@wagnerlawgroup.com

Introduction and Agenda

1. Short-term Emergency Steps regarding Key Employees
2. Providing Some Security through Rabbi Trusts.
3. Adjusting the Goals for Formula-based Incentive Plans and Awards.
4. Addressing Out-of-the-money Stock Options
5. Severance and Retention Strategies.
6. Responding to Cash Flow Disruptions.
7. Considering Claw-backs and Covenants.
8. Protecting against employer distress or bankruptcy.

1. Short-term Emergency Steps regarding Key Employees

1. Revising Incentive Plans ... and other short term strategies
2. 409A plan terminations
3. Cancellation of equity awards – or diversification
4. Refined employment agreements
 - Enhanced Change in Control Protections, including 280G
5. Indemnification and D&O insurance

2. Rabbi Trust Protections

- ❑ Origin – 1980s PLR
- ❑ Tax Rules and Safe Harbor: 1990s
- ❑ Occasions for Rabbi Trust:
 - Ordinary course for deferred compensation and other NQDC
 - “Springing” Rabbi – for M&A and special funding triggers
- ❑ Issues to consider
 - Independent trustee?
 - One for all, or one for each?
 - Investment choices – employer stock?
 - Solvency and Credit Risks

3. Adjusting the Goals for Formula-based incentive plans and awards.

- Pay-for-performance:
 - adjustments in response to downturn and volatile results
 - “better” customization
- Discretion on making adjustments as a result of extraordinary events.

4. Underwater Stock options

1. Underwater Stock Options

- 409A and tax rules
- Financial (GAAP) considerations
- Securities law requirements – federal and state
- Business and morale implications

2. Possible Adjustments

- Form of Consideration
- Vesting terms
- Number of Shares
- Long-term goals and strategies

5. Severance and Retention Strategies

- ❑ Severance:
 - Ordinary course vs. triggered by RIF or Other Event , e.g. CIC
 - Formula driven vs. discretion vs. hybrid
 - Inside or outside ERISA
- ❑ ERISA-fication
- ❑ Retention Alternatives:
 - Pay to stay
 - Event based vesting and/or payouts
 - Cash vs. Equity

6. Cash Flow disruptions

1. Mechanisms by which to protect employers if cash becomes short (or could become short).
2. Equity and other alternatives
3. 409A and 457(f) considerations

7. Claw-backs and Covenants

- ❑ Claw-back Meaning
 - Statutory vs. contractual
 - Tax implications
- ❑ Comparison to a Hold-back
 - Tax implications
- ❑ Triggers for Recovery or Forfeiture
- ❑ Implementation Alternatives
 - Velvet glove
 - Iron fist

8. Protecting against employer distress or bankruptcy

1. Customized retention and “event” incentives
2. 409A rules re unvested vs vested compensation
3. Roll-forward of restrictive covenants
4. Impact on buyer’s incentive plans

QUESTIONS?