AN OFFERING FROM BDO'S CORPORATE GOVERNANCE PRACTICE

BDO BOARD REFLECTIONS

MERGERS, SPINOFFS, CYBER SECURITY, DISASTER PLANNING AND EXECUTIVE PAY AMONG TOP ISSUES AT 2014 SHAREHOLDER MEETINGS ACCORDING TO BDO USA, LLP

As the 2014 corporate annual meeting season begins, shareholders are likely to be paying close attention to the opportunities and threats facing the companies they continue to put their faith in. After slumping through January and early February, the stock market has bounced back and is within shouting distance of new highs, but mixed economic data on hiring, exports, housing and manufacturing, coupled with worries about emerging markets are cause for potential concern. This unsettled climate should make for an interesting annual meeting season this Spring. BDO USA, LLP has compiled the following list of topics that corporate management and boards of directors should be prepared to address in connection with their 2014 annual meetings:

M&A Opportunities/Takeover Defenses

Comcast's $45 billion acquisition of Time Warner Cable may be the start of a long awaited merger boom as large businesses flush with cash look to buy growth. Shareholders will want to know if management is seeking out opportunities and that potential targets are properly vetted to avoid any buyer's remorse (Hewlett-Packard/Autonomy). By the same token, Boards should have contingency takeover defenses in place to enable them to respond quickly to fend off attacks or maximize shareholder value should a transaction be accepted.

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BDO USA CORPORATE GOVERNANCE PRACTICE

BDO USA's Corporate Governance Practice was developed to provide guidance to corporate boards. The firm works with a wide variety of clients, ranging from entrepreneurial businesses to multinational Fortune 500 corporations, on a myriad of accounting, tax, risk management and forensic investigation issues.

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Spinoffs

Trian Fund Management's campaign to get Pepsi to spin off its struggling beverage business is just one example of companies coming under fire from activist shareholders wanting to break them apart. Management should be prepared to respond to these well-funded investors who argue that businesses perform better when they aren't part of a large conglomerate.

Global Economic Concerns

Investors have become well educated on how inter-related the world's economies have become and are concerned how the crisis in the Ukraine and slowing growth in China, Brazil, Japan and other markets will impact the global recovery. Sovereign debt holders or any companies with exposure (facilities or sales operations) in these countries should be prepared for worst case scenarios. Shareholders will ask about contingency plans the company has in place should there be a major collapse.

Cybersecurity

Highly publicized data breaches at Target, Neiman Marcus, Barclays and JP Morgan Chase have put cybersecurity on the agenda for shareholders. Weaknesses in networks and data security can expose businesses to significant losses in brand and market value. Shareholders may want to know how the company is taking a proactive and preemptive approach to improve data security. BDO recently examined this topic further via the issuance of our publication "Cybersecurity – A Board Primer" along with a complimentary archived webinar "Managing Risk in Cyberspace" which featured a panel discussions on the current cyber risk environment, the roles of boards and management related to cybersecurity risk, along with action items to consider to insure assets and protect client relationships.

Executive Compensation

Proxy disclosure rules and new avenues for shareholder feedback have encouraged adoption of performance focused compensation models at public companies. This shift is one key reason that 90 percent of public companies are receiving favorable shareholder votes on their executive pay programs, however, there are still several compensation issues that shareholders are likely to raise at this year's annual meetings:

- **Pay for Performance.** Media coverage questioning pay practices at Yahoo (paying departing COO $109 million for just 15 months on job) and JP Morgan Chase (Jamie Dimon's 74 percent raise in the same year that the bank paid $20 billion in fines/legal costs) is likely to embolden shareholders to question whether executive pay levels actually reflect performance. Companies should be aware of these concerns and communicate with shareholders about compensation decisions. This is particularly important when board decisions are in the company's best long-term interests, but don't fit in the one-size-fits-all pay models that institutional investors may be using.

- **CEO-Median Employee Pay Ratio.** The SEC has issued proposed regulations on disclosure of the ratio of the CEO's pay to the median pay of employees of the company. This extremely complex calculation will likely be a required disclosure for most companies in 2016 proxies, but the question may be asked at 2014 annual meetings, so companies need to be proactive and begin thinking about how they will comply long before the first required disclosure. Refer to BDO's Flash Report for further information.

- **Voluntary Disclosure of Realizable Pay.** In the absence of regulations requiring disclosure of the relationship between pay and company performance, the emerging consensus appears to be that disclosure should track how well the company's total shareholder returns correlate with the CEO's realizable pay (salary, bonus and the value of outstanding equity awards). Most institutional investors are doing their own realizable pay modeling and incorporating it into their say-on-pay decisions. Companies should begin to develop their own models in anticipation of investor questions on the matter.

For additional topics related to executive compensation, refer to BDO's recently archived webinar "Executive Compensation: Hot Topics for Keeping Your Leaders Cool." Additionally, The BDO 600 was released this week and outlines the 2013 compensation practices of 600 mid-market public companies.

Succession Planning

As the economy continues to improve, executive movement should start to increase – including CEO turnover. CEO succession is one of the board's most important responsibilities. Shareholders will want to know that the board has a succession plan in place and candidates identified, if needed, for the CEO and other senior positions. Too often, companies are viewed as being reactive to turnover in critical leadership roles instead of being proactive. BDO continues to examine perspectives in these areas as well as best practices related to executive succession planning strategies and has issued several practice aids, including a tool to assist companies in developing success profiles for key leadership positions. BDO's Nominating Committee website contains these and other thought leadership pieces, including a new publication anticipated to be released later this month as reference for boards and management. Additionally, "Executive Succession Strategy" is available as an archived webinar from our Board series programming.

Read more

Accessing Public Equity Markets

In 2013, initial public offerings (IPOs) in the U.S. experienced a renaissance with both total offerings and proceeds raised reaching the highest levels since 2000. In 2014, IPO activity has continued to increase with offerings up 85 percent year-over-year through February. Shareholders may want to know if the favorable IPO market will translate to new securities offerings from existing public companies, as well as potential spin-offs, and whether management is considering any such offerings in the foreseeable future. Refer to a more complete summary in the "2014 BDO IPO Outlook."

Disaster Planning

Typhoons, hurricanes, earthquakes, tornadoes and other natural disasters seem to be on the rise in recent years. Beyond the terrible loss of human life, these events are a powerful demonstration of supply chain risks in a global economy. Any single failure in a business's supply chain can cause problems throughout the company. Boards should be prepared to articulate what they have done to prepare for low probability, but high impact events such as natural disasters.

New COSO Framework

Is the company in compliance with the new COSO 2013 Internal Control – Integrated Framework (2013 Framework)? If not, why not? Will major changes be necessary to comply? What is the timeframe and what are the costs? While the 2013 Framework becomes effective December 15, 2014, the SEC has stated that the longer an entity continues to use the 1992 Framework beyond the transition date, the more likely they are to receive questions from the SEC about such use. Additionally, during the transition period, COSO and the SEC have indicated that management should disclose in their annual assessment which version of the framework is used.

In general, we would expect companies to have a consistent result with the use of the 2013 Framework as compared to its predecessor the 1992 Framework. However, in the process of matching controls with the explicit 17 principles and relevant points of focus laid out in the 2013 Framework, management may identify the need for additional documentation, possible changes in controls to address gaps that were not previously apparent or eliminate or enhance certain control procedures. Therefore, BDO is encouraging companies to begin their evaluation of the impact of the 2013 Framework on their assessment of their system of internal control and develop appropriate mapping documentation to demonstrate that each principle is present and functioning. Refer to BDO's recent Flash Report for further details and aids to assist in this process. For an overview of the 2013 Framework, tune into BDO's archived webinar offering.

Conflict Minerals

The SEC has released its Form SD, a specialized disclosure form for reporting conflict mineral rule compliance. The new rule requires companies to disclose information each calendar year on the source of tantalum, tin, gold, and tungsten, minerals that have funded violent conflict in the Democratic Republic of the Congo and adjoining countries. Shareholders may want to know if companies are conducting country-of-origin inquiries to ensure that there supply chains are conflict free. For more on the SEC's frequently asked questions about conflict mineral reporting, refer to BDO's Flash Report.

Auditor Tenure

Although efforts to require mandatory audit firm rotation in the U.S. appear to have waned, as evidenced by PCAOB Chairman James Doty indicating that the PCAOB no longer has an active project on a term limit for auditors, management and audit committees should be prepared to discuss any questions regarding lengthy auditor tenures. Shareholders may want to know the process the company uses to select an audit firm, how long the current firm has been in place, when the last time the audit engagement was put out for bid and how the audit committee ensures that the audit firm performs quality work. Interestingly, the European Union reached a tentative agreement in December 2013 regarding auditor rotation reforms that calls for a rotation requirement of 10 years that could be extended up to 10 additional years if companies put the engagement out for bid; and up to 14 additional years when a company appoints more than one audit firm as a "joint audit." This may impact U.S. companies who have EU-based affiliates and how these companies manage auditing relationships globally.