

## PRIVATE POWER

**INCREASED DISCLOSURE OF EXECUTIVE PAY THIS PROXY SEASON COULD LEAD TO MORE TAKE-PRIVATES AND FOREIGN LISTING IN YEARS TO COME**

**BY CHRISTINE LAFOLLETTE**

As stockholders, potential acquirers and venture partners open the 2007 annual proxy statements of public companies, they will have to wade through even more pages of disclosure about what executives and board members are now (or could potentially be) paid. The compensation dollars in 2007, when fully calculated and disclosed, will be larger than ever before, with a host of newly required line items. These revised federal securities disclosure rules could heighten the attractiveness of “going private” strategies or listings on foreign exchanges with lighter regulatory structures.

The recent brisk pace of consolidation in the energy industry, particularly in the exploration and production (upstream) sector, makes executive compensation agreements, including severance disclosures and buy-out triggers, of particular interest to acquirers when determining the cost of a potential M&A deal.

The Securities and Exchange Commission has focused on more robust executive compensation disclosure practices. When regulators came to a decision in 2006, SEC Chairman Christopher Cox commented, “We are mounting an all-out war on needless complexity ... No shareholder should need a machete and a pith helmet to go hunting for what the CEO makes.”

New SEC rules require much more specific information about compensation, including additional tables with a total “all-in” compensation column, as well as detailed descriptions of total compensation policies and procedures. To establish a baseline for 2006, according

to Executive PayWatch Database, the average CEO of a **Standard & Poor’s** 500 company received \$14.78 million in total compensation last year, which represented more than a 9% increase over 2005 levels. The percentage increase in 2007 numbers may appear higher than ever before given the requirement for more robust disclosure.

Executive compensation agreements traditionally include a mix of direct salary and deferred compensation, such as performance-based components, the details of any severance package, and perquisites that vary largely by employer. In the past, if companies relied heavily on “perks” for executive retention, disclosure may not have been fulsome, so this may now be an eye opener for interested parties.

The new SEC disclosure rules also require a “Compensation Discussion and Analysis” to outline the objectives and metrics of compensation programs at a company, and regulators have specifically directed that the discussion be company-specific and not a “boilerplate” statement. This discussion and analysis will provide dealmakers with a unique window into the inner workings of a company.

Not all items disclosed regarding executive compensation, however, will be triggered in a given year. Certain payments subject to company performance measurers and stock price volatility may never be made. More important, to attract top management talent, boards of directors must compensate in alignment with their industry and the market for executives willing to take on high-risk, high-profile roles at leading public companies.

The requirement of Sarbanes-Oxley that executives certify financial statements places top executives in a riskier position than ever before in terms of accountability and exposure for the actions of everyone in the entire company with potential civil and criminal liability. The global nature of the energy business provides a special wrinkle in that cross-border and cross-cultural factors heighten an energy executive’s risk profile.

Despite some notable compensation numbers last year, many research studies tracking the median total compensation of the CEOs of large companies have found that the reward levels were generally consistent with the growth of the market value and shareholder returns of those companies. While these analyses support the notion that generous levels of executive compensation may be warranted and support shareholder value, some investors may wonder what their returns might have been with more conservative levels.

As the 2007 proxy season moves forward with more disclosure as well as shareholder proposals and potential legislation to vote on executive pay, the changes could ultimately contribute to a rise in take-private transactions or foreign exchange listings in the months and years to come. ■

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