Summary

“...Our central concern is the 'F' grade received by the Company in our pay-for-performance analysis. Ordinarily, this grade would suggest a major disconnect between Company performance and the compensation of its executives. However, in this case, we believe this grade is driven primarily by the value of long-term awards granted during the past year. We note that 66% of these equity awards are contingent on performance and will not pay out until the end of a five-year performance period. In December 2009, the Company cancelled the restricted stock and tandem cash awards originally awarded in 2007 and 2008 due to the Company's failure to fulfill the necessary performance conditions. As such, we are confident that performance targets have historically been set at a reasonably challenging level and that NEOs will most likely not receive the full value of these equity grants. Further, the Company states that it does not expect to award any additional equity until after the five-year performance period has expired.

We also note that during the past year, the compensation committee has adopted a number of beneficial features in its compensation program such as the elimination of excise tax gross-ups, the elimination of dividend payments on any unearned or cancelled performance-based awards, and the decision to maintain fiscal 2011 salaries for its NEOs at the fiscal 2010 level. The Company also maintains executive stock ownership guidelines, a feature which further aligns the interests of NEOs with that of shareholders. In the aggregate, these features, along with the clear disclosure provided by the Company, outweigh the unfavorable pay-for-performance grade. While shareholders should be mindful of the amount of equity being granted, they should be confident in the Company's overall compensation structure.

Accordingly, we recommend that shareholders vote FOR this proposal.” (Source: Glass Lewis Proxy Voting Report on Methode Electronics)
Online Appendix 2 Examples of company responses to negative ISS recommendations

Disagreement with ISS

Disagreement on choice of peer groups used to assess relative stock performance
“ISS’s comparative financial data is flawed. ISS’s methodology does not provide an accurate comparison of ATI’s performance to that of its true peers. ISS’s recommendation is based in part by comparing the Company’s total shareholder return with that of a group of companies selected by ISS based on the Global Industry Classification Standard (GICS). The ISS group includes companies engaged in completely different businesses than ATI, such as copper mining, iron ore mining, and consumer products packaging. The performance of those companies is not relevant to ATI and should not be compared with the performance of ATI. Those companies’ businesses are not reflective of the same cyclicality and other circumstances that our business, and the specialty metals manufacturing industry generally, encounters. More importantly, the ISS peer group does not include certain companies that are clearly recognized by the investing public as our competitors.” Allegheny Technologies Inc., DEFA14A, April 12, 2011 (Annual meeting date: April 29, 2011)

Disagreement on valuation of equity component of total pay
“ISS’s valuation of Mr. Dvorak’s 2010 stock option grant significantly overstates his total compensation and the increase in his compensation from 2009 to 2010…ISS’s report measures his total compensation at $12,014,000, whereas our 2011 proxy statement measures total CEO compensation at $9,555,210. This discrepancy is caused by a difference in the assumptions used in the calculation of the grant date fair value of Mr. Dvorak’s stock option award using the Black-Scholes option pricing model. Our proxy statement reports this award as having a grant date fair value of $3,421,600, whereas ISS values the award at $5,880,000, more than 70% higher than our valuation. ISS’s report overstates Mr. Dvorak’s 2010 compensation and the increase in his compensation from 2009 to 2010.” Zimmer Holdings, DEFA14A, April 15, 2011 (Annual meeting date: May 29, 2011)

Disagreement on definition of what constitutes performance-based pay
‘ISS asserts that ExxonMobil time-vested restricted stock is not performance-based compensation because it is not tied to a formula or targets. This analysis does not recognize the significant pay-for-performance connection that is created when an executive’s net worth is made substantially dependent on long-term share performance. We do this by combining restricted stock with the other supporting design features of stock-based compensation... Furthermore, it does not recognize the key metrics considered by the Compensation Committee in determining the share grants to the CEO and other NEOs which are fully disclosed in the CD&A…’ Exxon Mobil Corporation, DEFA14A, May 6, 2011 (Annual meeting date: May 25, 2011)

Disagreement on assessment of severance plan
“ISS has based its recommendation on only one small element of a comprehensive executive compensation program. ISS indicates…that each component of its “Executive Compensation Evaluation” is a “Low” level of concern, except for “Severance/CIC Agreements”. ISS’ recommendation against the entire executive compensation package is based solely on our inclusion of one newly hired executive in the CIC Plan. We strongly disagree with this approach… It is worthy of note that Glass Lewis…has recommended a vote “for” the resolution approving our executive compensation. [Also, the company]…has a valid business reason for allowing newly hired employees to participate in pre-existing programs for similarly situated executives, including the CIC Plan…If Mr. Ellen had been excluded from the CIC Plan, his compensation package would have been substantially less than that of our other similarly situated executives. His recruitment and retention, or the recruitment and retention of any talented executive officer, would be difficult…” Dr. Pepper Snapple Group, DEFA14A, May 6, 2011 (Annual meeting date: May 19, 2011)
Additional Disclosure – Severance

*School Specialty Inc., 8-K Form, August 8, 2011 (Annual meeting date: August 23, 2011)*

“In response to a report issued by a proxy advisory firm, School Specialty, Inc. (the "Company") is filing this report to clarify certain matters relating to the terms of the employment agreement dated June 27, 2011 (the "Employment Agreement") between the Company and David J. Vander Zanden, the Company's Chief Executive Officer and President...”

*School Specialty Inc., ISS Proxy alert (August 8, 2011; original ISS report: August 3, 2011)*

“ISS is updating the original report dated Aug. 3, 2011. In an 8-K filed on Aug. 8, 2011, the company clarified that the new employment agreement with the CEO, dated June 27, 2011, would not entitle him to a continuation of base salary or such benefits if he were to voluntarily terminate his employment upon a change in control. Based on this new information, ISS now recommends a vote FOR Item 2.”

Changes to Compensation Plans – Introduction of Performance Conditions in Equity Grants

*Collective Brands Inc., 8-K Form, May 18, 2011 (Annual meeting date: May 26, 2011)*

“Matthew E. Rubel, the Chairman, Chief Executive Officer and President of Collective Brands, Inc. offered and on May 18, 2011, the Company agreed to modify unilaterally the terms governing 50 percent of the 129,344 shares underlying the stock appreciation right ("SAR") award granted to him on March 24, 2011 (the "Award"). As a result of this modification, 64,672 SARs (the "CCG Performance SARs") will now vest on March 24, 2014, if the Company achieves the performance criteria for the three year performance period beginning on January 31, 2011 and ending on January 31, 2014 (the "Performance Period") set forth below in the Vesting Schedule. The other 64,672 SARs granted pursuant to the Award shall vest as set forth in the Vesting Schedule.”

*Collective Brands Inc., ISS Proxy Alert (May 18, 2001; original ISS report: May 10, 2011)*

“On May 18, 2011, the company filed a Form 8-K and provided additional information. Specifically, half of CEO Rubel's 2011 stock appreciation right (SAR) award (in terms of shares) will be modified to incorporate a performance condition…The Compensation Committee will also impose performance vesting requirement on 50 percent or more of grants of equity based compensation (in terms of shares) awarded in the future for the company's named executive officers in the aggregate. Finally, the company also clarified that it does not benchmark target compensation for the CEO or the remaining named executive officers at the 75th percentile. In light of the enhanced performance-based equity award for the CEO and an ongoing pay for performance commitment, a vote FOR is recommended for Item 2.”

Changes to Compensation Plans – Elimination of Excise Tax Gross-Ups

*The Walt Disney Company, 8-K Form, March 18, 2011 (Annual meeting date: March 23, 2011)*

“On March 17, 2011, the Company amended employment agreements with each of Robert A. Iger, James A. Rasulo, Alan N. Braverman and Thomas O. Staggs to remove a provision for payment to the executive to cover excise taxes incurred by the executive pursuant to Section 4999 of the Internal Revenue Code with respect to payments received by the executive upon termination following a change in control.”

*The Walt Disney Company, ISS Proxy alert (March 18, 2001; original ISS report: February 28, 2011)*

“On March 18, 2011, the company filed additional proxy materials disclosing that excise tax gross-up provisions have been eliminated from the company's employment agreements with four executives... In light of this positive action, ISS recommends that shareholders vote FOR Item 16 – Advisory Vote to Ratify Named Executive Officers' Compensation”
Online Appendix 3 Firm’s responses to the 2011 say on pay vote: excerpts from the 2012 proxy statements

“Our Response to Say on Pay Vote: A majority of the stockholders who voted on our 2011 “Say on Pay” proposal voted against the proposal. In response to that vote, our board of directors, the Committee and our executive team took immediate and thorough action:

a. The Committee engaged Towers Watson, a leading human resources consulting firm, to perform a review of our executive compensation program and make recommendations for enhancements.
b. Our executive team agreed to amend the equity grants issued in January 2011 to include a vesting condition that limits vesting to the extent that Umpqua’s total shareholder return (TSR) does not exceed the KRX total return index, a regional bank index.
c. We met with representatives of Institutional Shareholder Services (ISS) and Glass Lewis to fully understand their view of the “pay for performance” aspect of our compensation program.
d. We engaged Phoenix Advisory Partners to advise on outreach to our institutional shareholders who voted against our say on pay resolution.
e. We met with many of our large institutional shareholders who voted against our 2011 say on pay resolution to advise them of our response and to understand their concerns with our program.
f. We strengthened our stock ownership policy to require that named executive officers acquire and maintain positions in company stock with a value ranging from 150% to 400% of base salary.
g. We enhanced our policy to require that at least 50% of all equity awards to executive officers will be “performance based”. In 2011, 100% of the equity awards to executives were “performance-based”.
h. We revised our “hold to retirement” policy to remove the age 62 exemption. 75% of all net equity awards must be held to retirement.”

(Umpqua Holdings Corp., Proxy Statement, April 17, 2012)

“During fiscal 2011, the equity compensation component of the Company’s pay programs was reevaluated, taking into account the outcome of the shareholder vote on executive compensation at the 2011 Annual Meeting of Shareholders, consultations with the independent consultant of the HR&C Committee, and discussions with major institutional shareholders. As a result of these considerations, the long-term equity based incentive program now has the following features:

• Instead of time-based restricted stock grants, which were a significant portion of the 2010 equity compensation program, performance-based market stock unit (“MSU”) grants (the structure of the MSU grants is described below under “Compensation Discussion and Analysis—Compensation Elements—2011 Equity Awards”), were awarded to the NEOs;
• the CEO MSU grant includes a second performance condition based upon the Company’s total shareholder return compared to its peer group over a three-year performance period;
• The proportion of long-term incentives delivered in the form of stock options granted to the NEOs was reduced so that MSUs comprise the majority of their equity compensation in both shares and value;
• In fiscal 2011 the Company increased the required CEO Company stock ownership guideline from five times to six times base salary;
• New equity award agreements were modified in fiscal 2011 to provide for accelerated vesting after a change in control only if the executive is terminated without cause or quits for good reason (“double trigger vesting”);
• In fiscal 2011 the Company adopted a clawback policy that applies when inaccurate financial statements have affected incentive award payments to executive officers…”

(Jacobs Engineering Group Inc., Proxy Statement, December 16, 2011)
“At the 2011 Annual Meeting, our stockholders approved our Say on Pay resolution by a favorable vote of approximately 72% of the votes cast (including abstentions). In considering the prior year vote, our Compensation Committee conferred with management about the possible reasons the Company received an unfavorable vote on the prior year Say on Pay resolution of approximately 28%. Based on discussions with certain investors and rating agencies, the Company believes that a significant portion of the “no” or “abstention” vote on the prior year Say on Pay resolution related to the Company’s exchange of certain outstanding options at the end of 2010 and that the negative Say on Pay votes did not necessarily relate to the Company’s executive compensation programs in general.”

(Taser International, Proxy Statement, April 23, 2012)

“Consideration of Last Year’s Advisory Stockholder Vote on Executive Compensation
At the 2011 Annual Meeting of Stockholders, stockholders voted to approve the compensation of the Company’s named executive officers...In considering the results of the 2011 advisory vote and feedback from stockholders, the Compensation Committee concluded that our stockholders generally support the compensation paid to our executive officers and the Company’s overall compensation program and therefore determined to maintain the current program. The Compensation Discussion and Analysis in this proxy statement, however, reflects a number of revisions relative to the 2011 Proxy Statement to improve the clarity and understanding of our executive compensation program.”

(Mohawk Industries, Proxy Statement, April 3, 2012)
Online Appendix 4 Event study around compensation changes made in response to 2011 say on pay votes

We perform an event study where we treat as “events” the proxy filing dates of the 147 firms targeted by an ISS Against recommendation in 2011 that report changes to their compensation plan in the 2012 proxy statement (see Section 6.2). Since some of these changes may have been already disclosed in 8-Ks during the year, for each of the 147 firms we read all Form 8-K, Item 5.02s (where firms must report, among other things, material changes to compensation arrangements) filed between the 2011 vote and the 2012 proxy filing date, leading us to identify 71 additional events (62 distinct firms), resulting in a sample of 218 SOP-related compensation change events. For each event we calculate Abnormal Returns as size-adjusted returns calculated over the [0, +1], [0, +2] and [0, +3] trading day windows around the event date.

Table A1 shows no statistically significant stock price reaction for the pooled sample (first row). The results are similar when we drop 43 contaminated events. One possibility is that some firms might have announced (some or all of) the compensation changes in 8-Ks filed earlier in the year. However, we continue to find no significant reaction around compensation changes in proxy filings not preceded by 8Ks (third row) and around the subset of 8-K events themselves, which, by definition, do not suffer from this problem (fourth row).

We note in Section 6.2 that some of the firms reporting changes to their compensation plans continue to receive Against recommendations in 2012, suggesting that these changes may be window dressing. Also, some changes may not be material enough to have a detectable impact on firm value (e.g. removing an excise tax gross-up provision from a severance contract of an executive). To address these concerns, we proceed as follows. First, we examine separately the subset of firms with a change in ISS SOP recommendation from Against in 2011 to For in 2012 (fifth row). As noted earlier, these firms experience a dramatic drop in dissent suggesting that both shareholders and PA considered the changes as adequate and material. Second, we identify 42 events, which, based on our subjective classification, represent the most substantial changes (sixth row). An example would be a firm that revamps multiple aspects of its compensation plan (the case of Umpqua Holdings in Online Appendix 3). Yet, we fail to find a significant stock price reaction.

Another concern is that the compensation changes are the result of an engagement process with institutional investors and inputs from compensation consultants and, thus, they do not reflect the views of ISS. However, as we have already noted, there is no significant reaction for the subset of firms with an ISS For recommendation in 2012 (which suggests ISS’s approval of the changes to the compensation plan, no matter how they came into place). Also, when we focus on the sub-sample of events where at least one of the compensation changes addresses an issue raised in the ISS report (not surprisingly, given our focus on firms with a negative ISS recommendation, 190 out of 218 events fit this definition), we do not find a significant stock price reaction (seventh row). In untabulated analyses, to increase the power of the test, we expand the sample by looking at responses to 2012 SOP votes by firms with a negative ISS recommendation in 2012, resulting in additional 99 compensation change events with price data. We continue to fail to detect any significant stock price reaction.

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1 We also read the 8-K (Item 5.02) filings for the firms reporting no SOP-related compensation changes in the 2012 proxy statement and find no cases where the change was announced in an 8-K and not reported in the proxy statement.

2 We define an event as contaminated if an earnings announcement occurs within the (-5,+5) window around the event or if there are other announcements via 8-K on the same day as the event date. Since proxy filings contain other information (and, thus, they are contaminated by definition), we also run a multivariate analysis with indicators for the type of proposals on the ballot. The inferences are unchanged.
Finally, to examine whether the market perceives SOP-induced changes to be better or worse than “routine” (non-SOP-induced) compensation changes, we compare the stock price reaction documented in Table A1 to two control samples: “routine” compensation changes made by the same firms (i.e. firms with a negative ISS recommendation) during the year prior to the 2011 SOP vote (245 events) and “routine” compensation changes made after the 2011 vote by a control sample of 269 firms with positive ISS and GL recommendations in 2011 and 2012 (145 events). None of the differences are significant, and neither of the two control samples exhibits a significant stock price reaction (untabulated results).

Overall, we find no evidence that PA analyses of SOP plans lead to superior compensation practices. There is an important caveat to our event study: since the compensation changes are the result of an engagement process with key institutional investors they may have been largely anticipated by some market participants, reducing the power of the event study. Our test implicitly assumes that these changes are not anticipated by all investors and/or that there is some uncertainty as to whether the firm would follow through and implement all the changes discussed during the engagement process.
Table A1 Market reaction to compensation changes in response to SOP votes

<table>
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<th>Compensation Changes</th>
<th>All</th>
<th>Exclude Contaminated Events</th>
<th>Mean Abnormal Returns</th>
<th>N</th>
<th>[0, +1]</th>
<th>[0, +2]</th>
<th>[0, +3]</th>
<th>N</th>
<th>[0, +1]</th>
<th>[0, +2]</th>
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<td>All compensation changes</td>
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<tr>
<td>…disclosed in the 2012 proxy and not preceded by an 8-K</td>
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<td></td>
<td>98</td>
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</table>

Table A1 displays the market reaction to the announcement of compensation changes made explicitly as a response to the 2011 SOP vote for the sample of 269 Russell 3000 firms that received an against recommendation from ISS in 2011 for SOP. Abnormal Returns is size-adjusted returns calculated over the [0, +1], [0, +2] and [0, +3] trading day windows around the announcement of the compensation change (proxy filing date or 8-K). ",", ",", and " denote significance at the 0.01, 0.05, and 0.10 level, respectively, based on a two-tailed test.