Blogs

Here's a tip from the sixth edition of our popular publication ***The Public Company Handbook***, which is an easy-to-read guide that provides practical insights regarding legal and other board management issues facing public—or soon-to-be-public—companies.

In 2005, the Delaware Court of Chancery absolved directors of liability for the 1995-96 hiring and firing of former Disney president Michael Ovitz. The Board had approved a severance package for Mr. Ovitz of approximately $140 million for his 14-month tenure. While not finding Disney's directors personally liable, the court sharply criticized their action (and inaction) as falling short of best corporate governance practices.

Many lessons of what not to do, wrote the court, could be learned from the Disney Board's conduct.

1. **Engage Your Independent Directors at an Early Stage.** Do not deliver decisions on a silver platter! In Disney, half of the Compensation Committee was active in negotiations and the other half came in "very late in the game." Engage your entire Compensation Committee in the "many" early stages of critical employment negotiations.

2. **Seek Expert Advice.** In Disney, the court allowed the Compensation Committee to rely on an expert, even though the expert's analysis may have been incomplete or flawed, because the Committee selected him with reasonable care, his analysis was within his professional competence, and the directors had no reason to question his conclusions. So make sure your Committee has the authority to solicit advice, and does, from independent employment compensation experts.

3. **Provide Directors with Sufficient Notice and Materials Prior to the Meeting.** Provide notice and materials well in advance of any meeting at which an executive employment agreement is to be discussed, including:

• A plain English term sheet summarizing the key provisions of the arrangements (and, when appropriate, a full draft of the proposed agreement).

• An analysis of the cost to the company of termination of employment, change of control, etc., including information relating to reasonableness of terms. Compensation Committee members should expect a spreadsheet making different, alternative assumptions and showing the range of potential payments in the most reasonably foreseeable alternative scenarios that could arise. The court noted that an analysis for the Ovitz employment agreement should have shown the cost to Disney if Mr. Ovitz's employment terminated during each of the five years of the agreement's initial term. Show your Board each possible bottom line!

4. **Allow Sufficient Time for Discussion, and Document the Process.** The Disney court focused on the length of Board discussions, noting how helpful it would have been had the Committee minutes shown that the discussion relating to Mr. Ovitz was longer than discussion of other issues. Insist that your Compensation Committee spend sufficient time on discussion, and document it!

5. **Establish Succession Planning**. Mr. Ovitz came to Disney as the result of a too-rapid search precipitated by the unexpected death of Disney's president and the discovery of the then-CEO's heart ailment. The Compensation Committee can take the lead in implementing a robust succession-planning process so that your company does not find itself in the position of being forced to hire a CEO without having conducted a proper search or made appropriate preparations.

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