

THE KEY POINTS TO LOOK FOR IN A CORPORATE PROXY STATEMENT

By Tom Burnett

All publicly traded companies must file a proxy statement once a year in advance of their annual meeting, and these statements can contain a wealth of critical data about a company's financial health if you know where to look.

Say the word "proxy" and most investors start to nod off. A proxy statement is perceived to be a complicated document that's written for number crunchers, not average investors.

Yet a proxy statement can contain a wealth of critical data about a company's financial health—if you know where in the document to look.

Where can you find the most telling facts about a company's proxy statement and how can you interpret that data before investing?

HOW TO FIND A PROXY, FAST

All publicly traded companies—with the exception of the tiny ones that are listed on the Nasdaq Bulletin Board—must file a proxy statement once a year in advance of their annual meeting.

All U.S. companies are required to file the statement electronically. As a result, the public document is immediately available on-line to the public. Foreign companies listed on U.S. exchanges as American depositary receipts (ADRs) do not have to file electronically, although some do.

A company's proxy is easy to access by calling the company for a copy, visiting its Web site, or going to the Securities and Exchange's EDGAR site (www.sec.gov/edgarhp.htm); the form code for looking up proxy statements on the SEC database is DEF.

WHAT TO LOOK FOR

Here's what to look for in a company's proxy statement before investing in its stock:

- ***How many options do directors hold?***

Flip to the "Election of Directors" section in the front of the proxy. This section lists the names of all directors and their holdings in the company, including how many shares of common stock they hold. The table lists holdings of all classes of company stock, with options listed separately. Figure 1 provides an example from the Microsoft proxy statement for its November 9, 2000, annual meeting. [This example is provided for illustration purposes only].

What to look for: See if the directors as a group own a significant portion of the company—5% or more. Include options in this calculation. To find the total number of company shares outstanding, go to almost any on-line site offering stock research, consult Value Line, or call the company.

It's a bad sign if several directors own just a few hundred shares and have few, if any, options. You want their financial interests to be aligned with

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FIGURE 1. MICROSOFT PROXY EXAMPLE: DIRECTORS' HOLDINGS

Information Regarding Beneficial Ownership of Principal Shareholders, Directors, and Management		
The following table sets forth information regarding the beneficial ownership of the Company's common shares by the nominees for directors, the Company's Chief Executive Officer and the four other highest paid executive officers (the "Named Executive Officers"), and the directors and executive officers as a group.		
Name	Amount and Nature of Beneficial Ownership of Common Shares as of 3/3/00(1)	Percent of Class
William H. Gates	731,749,668(2)(3)	13.7%
Steven A. Ballmer	239,626,832	4.5%
David F. Marquardt	1,873,816(4)	*
Ann McLoughlin	1,000	*
W. G. Read, Jr.	611,872(5)	*
Jon A. Shirley	9,184,979(6)	*
Robert J. Herbert	963,246(7)	*
James E. Allchin	1,015,327(8)	*

yours, and you want them to have an incentive to dissuade the CEO from doing anything really dumb.

• **Who are the other large investors?**

The "Election of Directors" section also details the stock and options holdings of senior management and any holders who own more than 5% of the company.

What to look for: Investors should

want top executives to have significant stakes in the company. It's a bad sign if an executive vice president owns only 1,000 shares.

Investors should want each top manager to have more than \$1 million in stock. The only exception is if the person is a very recent hire.

You also should check to see which companies have strong positions in the company you're considering.

A case in point appeared in last year's PaineWebber proxy. If you had examined the proxy, you would have seen that General Electric at the time owned 21.7% of the company and Yasuda Mutual owned 7.7%. This kind of information can give you insight into the kinds of supporters and controlling interests a company has and the corporate relationships it has developed. The support of both General Electric and

FIGURE 2. MICROSOFT PROXY EXAMPLE: EXECUTIVE COMPENSATION

Information Regarding Executive Officer Compensation					
Cash Compensation					
The following table discloses compensation received for the three fiscal years ended June 30, 2000, by the Named Executive Officers.					
SUMMARY COMPENSATION TABLE					
Name and Principal Position	Year	Annual Compensation		Long-Term Compensation Awards	All Other Compensation(2)
		Salary	Bonus(1)	Securities Underlying Options(4)	
Steven A. Ballmer President and Chief Executive Officer; Director	2000	\$428,414	\$200,000	0	\$5,100
	1999	388,392	272,181	0	4,800
	1998	337,429	205,598	0	4,800
William H. Gates Chairman of the Board; Chief Software Architect; Director	2000	439,401	200,000	0	0
	1999	400,213	223,160	0	0
	1998	368,874	173,423	0	0

FIGURE 3. MICROSOFT PROXY EXAMPLE: OPTION GRANTS

Compensation Pursuant to Stock Options

The following table sets forth information on option grants in fiscal 2000 to the Named Executive Officers.

Name	OPTION GRANTS IN LAST FISCAL YEAR				Potential Realized Value at Assumed Annual Rate of Stock Price Appreciation for Option Term(s)		
	Number of Securities Underlying Options Granted(000)	Percent of Total Options Granted to Employees in Fiscal Year	Expiration Date	(\$/Share)	Annual Rate of Stock Price Appreciation for Option Term(s)		
					0%(0)	5%(0)	10%(0)
Steven A. Ballmer	0	0	N/A	0	0	0	0
William H. Gates	0	0	N/A	0	0	0	0
Robert J. Harbold	600,000		March, 2010	\$90.63	0	\$ 88,571,143	\$140,034,746
	300,000		April, 2010	66.63	0	32,557,531	51,842,427
	2,000,000		May, 2010	69.38	0	226,009,129	359,881,766
	2,900,000	0.93%			0	347,137,803	552,758,939

Yasuda Mutual was key when PaineWebber merged with Swiss banking giant UBS Warburg last summer.

EXECUTIVE COMPENSATION

- **Are top executives overpaid?**

Turn to the "Executive Compensation" section. There you will see exactly what the company's top officers have earned annually over the past three years. Figure 2 shows an example, again from the

Microsoft November proxy.

What to look for: Investors should check to see whether their compensation seems appropriate or whether the executives are overpaid.

Is their compensation increasing steadily, or has it taken an enormous jump recently? Does this increase relate to the company's earnings or stock price performance, or does it seem excessive?

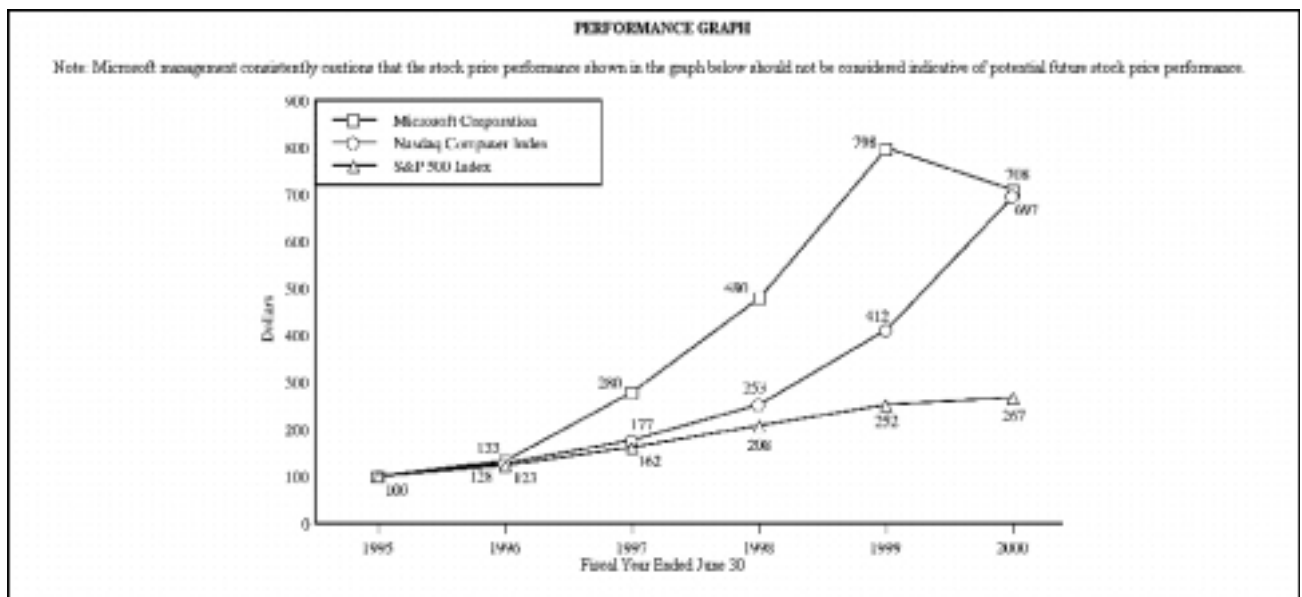
Check three companies in the same industry and compare com-

pensation packages. Consider investing in companies whose senior executives have large stakes in the company but relatively modest pay packages.

- **What's the exercise price of recent options?**

The next table in the compensation section is called "Option Grants." It reports all option grants for senior executives and the prices at which those options can be exercised. Figure 3 illustrates this

FIGURE 4. MICROSOFT PROXY EXAMPLE: THE PERFORMANCE GRAPH



section from the Microsoft November proxy.

What to look for: Investors should want to see an exercise price for the most recently granted options that is close to the current market price or, preferably, above it.

That's because investors want the executives to have a strong financial incentive to get the stock price to a higher level.

It's a bad sign if options have recently been repriced—that is, lowered—so that the stock no longer has to rise as high for the options to be profitable if exercised. Any repricing of options must be explicitly discussed in this section.

TRANSACTIONS

- ***Are executives borrowing at a fair rate?***

In the "Related Party Transactions" section, you'll find a discussion of every kind of transaction

(loans, sales, rentals, leasebacks, etc.) between company officers and the company—or between the company and certain related businesses.

What to look for: Are executives being charged a fair interest rate for any money they have borrowed from the company? Interest-free loans are a bad sign because they mean that the executives are getting sweet deals at the expense of the company.

Has a company executive recently sold real estate or a business to the company? While such a transaction could be perfectly acceptable, it is extremely troubling if there is any doubt about the true value of what was sold.

Make sure there was an external independent appraisal and, if possible, check recent prices of comparable transactions. If the transaction looks fishy, it's probably a good idea to avoid investing in the company.

THE BOTTOM LINE

- ***What's the shareholder return performance?***

Look for the "Performance Graph" section. You'll find a chart that compares the stock price performance of the company to the S&P 500 and to its peer group. Figure 4 shows the performance graph from the Microsoft November proxy.

What to look for: This chart provides a terrific visual sense of how the company has been doing compared to its market benchmark and the stocks of its competitors.

The chart is a reminder that beating the S&P 500, as impressive as it is, may not matter that much if the company has badly trailed its peers.

Ideally, investors should want a stock that has beaten its market index and is one of the leaders in its industry. ♦

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