

Public Company Boards and Compensation Committees Need to Be Careful When Setting Executive Compensation

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PRACTICES Employee Benefits and Executive Compensation

The recent invalidation of Elon Musk’s \$55.8 billion compensation package with Tesla, Inc. (“**Tesla**”) by the Delaware Court of Chancery and the dismissal by the U.S. District Court for the Southern District of New York of the lawsuit against Apple, Inc. (“**Apple**”) alleging that Apple had overpaid its executives, including Tim Cook, by tens of millions of dollars are great reminders to boards of directors and compensation committees that stockholders are watching, and directors should use care when making executive compensation decisions.

Although both cases involve high-profile executives, any public company could face a challenge to its executive compensation packages if it does not follow a prudent decision-making process. Below are some best practices for boards of directors and compensation committees to consider when reviewing executive compensation:

Control the process: The court in the Tesla case noted that the compensation process was cooperative with Elon Musk. While directors may seek input from an executive, directors have the ultimate responsibility to control the compensation decision-making process.

Compensation consultants: Boards and compensation committees should retain outside compensation consultants to advise on what is considered reasonable executive compensation. As noted in the Tesla court opinion, Tesla’s Board did not use objective compensation benchmarking data.

Preserve director independence: The court in the Tesla case focused on the directors’ interpersonal and financial relationships with Elon Musk. Directors should be independent of executives, particularly with respect to compensation matters.

Accurate disclosures: All required disclosures to stockholders must accurately describe the material terms of the executive compensation package and should be consistent with disclosures made to other parties, such as financial institutions. The court in the Apple case focused on the accuracy of the disclosures in Apple’s proxy in dismissing the plaintiff’s claims.

The opinion in [Richard J. Tornetta v. Elon Musk](#) is available [here](#), and the opinion in [International Brotherhood of Teamsters, Garage Employees Local 272 Labor Management Pension Fund v. Apple Inc. et al](#) is available [here](#).