PARKER HANNIFIN CORP
Form DEFA14A
October 12, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SCHEDULE 14A

(RULE 14a-101)

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities

Exchange Act of 1934 (Amendment No.)

Filed by the Registrant þ
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Check the appropriate box:

o Preliminary Proxy Statement
o **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))** o Definitive Proxy Statement þ Definitive Additional Materials
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PARKER-HANNIFIN CORPORATION

(Name of Registrant as Specified In Its Charter)

Not Applicable

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

þ No fee required.

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Subject: Parker Hannifin Corp. Proxy Statement Supplemental Information
Dear Shareholder,
Parker Hannifin Corporation s Annual Shareholders meeting is scheduled for October 25, 2006 and your vote on this year s proxy issues is very important to us.
The attached report recently issued by Proxy Governance Inc. provides information that may be helpful to you in making an informed decision. Proxy Governance is an independent proxy research, advisory and voting firm providing advice to institutional investors, pension plans, advisors, money managers and others with the goal of building long-term shareholder value. It evaluates proxy issues and makes voting recommendations on an issue-by-company basis, considering a company s performance, compensation practices, management strength and other corporate governance factors.
I ask that you review this report and consider the issues addressed. I strongly believe Parker s performance and the performance of the Board of Directors warrants your support with a vote against the proposal to declassify the Board of Directors and votes for the Directors nominated for re-election this year. If you would like to discuss these issues I would be happy to talk with you.
Most importantly, thank you for your continued interest in Parker. We re looking forward to another outstanding year.
Sincerely,
Donald E. Washkewicz
Chairman & CEO

PROXY Governance, Inc.

Contact: Alesandra Monaco

PROXY Governance, INC.

PARKER-HANNIFIN CORP (NYSE : PH)

Annual Meeting **Record Date:** 08/31/2006 **Meeting Date:** 10/25/2006

Classification: Fortune 500, Russell 3000, S&P 500

Fiscal Year End: 06/30/2006

Market Capitalization: $9.3B

Solicitor: Georgeson Shareholder Communications

Shareholder Proposal Deadline: 08/11/2007

Meeting Agenda

Investor Relations

Proxy Statement

SEC Filing 10k

Company Description

Proposals			**Recommendations** Management	PROXY *Governance*	
MGT	**1**	Elect Nominees	**FOR**	**FOR**	**Analysis**
	1.1	Robert J. Kohlhepp	**FOR**	**FOR**	
	1.2	Giulio Mazzalupi	**FOR**	**FOR**	
	1.3	Klaus-Peter Müller	**FOR**	**FOR**	
	1.4	Markos I. Tambakeras	**FOR**	**FOR**	
MGT	**2**	Ratify Appointment of Auditors PricewaterhouseCoopers LLP	**FOR**	**FOR**	**Analysis**
SH	**3**	Eliminate Classified Board	**AGAINST**	**AGAINST**	**Analysis**

MGT *= Management,* ***SH****=Shareholder,* ***SHB****=Shareholder binding proposal*

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Comparative Performance Analysis

PROXY Governance s Comparative Performance Analysis contains calculations and graphs that reflect a company s historical performance and that of its industry peers (listed below) based on certain key financial metrics generally over a five-year period.

Comparative Performance Analysis

Peer Companies

For the Comparative Performance Analysis, generally up to 10 peer companies are selected primarily based on industry, but also considering market capitalization.

Peer Companies

DANAHER CORP	DOVER CORP	EATON CORP	HARSCO CORP
ILLINOIS TOOL WORKS	INGERSOLL-RAND CO LTD	ITT CORP	METSO CORP -ADR
PALL CORP	PENTAIR INC		

Comparative Performance Analysis

Comparative Return to Shareholders

The graphs above depict total shareholder return and compounded annual growth rate at specific points in time over the past five years based on average monthly stock prices. The graphs should be read from left (present time) to right (60 months before present time). The graphs allow the user to determine either the company s total shareholder return or compounded annual growth rate to date based on an investment made at a specific point in time over the last five years. Assumes payment, but not reinvestment, of dividends.

Comparative Performance Analysis

Composite Performance Summary

Composite Performance:

	Percentile relative to S&P 1500		**Percentile Pts.**
	Company	Peers	Trend
Composite:	**54**	**57**	á **3**
Quarterly Shareholder Returns:	57	60	á 3
Cash Flow from Operations/Equity:	57	54	á 3
Return on Equity:	56	63	á 2
Revenue/Expenses:	35	41	á 1

Comparative Performance Analysis

Performance Summary

Governance Analysis

Executive Compensation

PROXY *Governance* evaluates a company s executive compensation over the last three years, as available, and compares that to the median compensation paid by its peers over the same time frame. For our compensation model, generally 20 peer companies are selected based on similarity of market capitalization and broad economic sector using the GICS. Only U.S. and certain U.S. reporting companies that are incorporated offshore are included in this peer group.

The graph that follows shows:

The average three-year CEO compensation paid by the company expressed as a percentage from median peer compensation.

The average three-year compensation paid to the company s other named executives (excluding the CEO) as a percentage from median peer compensation.

Domestic Peer Companies

AMERICAN STANDARD COS INC	COOPER INDUSTRIES LTD	CUMMINS INC	DANAHER CORP
DEERE & CO	DOVER CORP	EATON CORP	FLUOR CORP
GOODRICH CORP	INGERSOLL-RAND CO LTD	ITT CORP	JOY GLOBAL INC
L-3 COMMUNICATIONS HLDGS INC	PACCAR INC	PALL CORP	PRECISION CASTPARTS CORP
ROCKWELL AUTOMATION	ROCKWELL COLLINS INC	SPX CORP	TEXTRON INC

ecutive Compensation

	Salary	Bonus	Other Annual Comp.	Restricted Stock	Stock Options[1]	LTIP	All Other	1-yr Pay[2]	Avg. Pa
nald E. Washkewicz ef Executive Officer l Chairman he Board	$ 1,100,000	$ 1,901,800	$ 271,264	$ 0	$ 3,730,770	$ 4,648,550	$ 15,402	$ 8,568,752	$ 7,712,1
an D. Myslenski ecutive Vice sident-Sales, rketing and Operations pport	$ 631,000	$ 631,547	$ 184,798	$ 0	$ 2,312,782	$ 2,528,518	$ 15,012	$ 4,617,978	$ 3,964,2
nothy K. Pistell ecutive Vice sident-Finance and ministration and Chief ancial Officer	$ 589,000	$ 547,469	$ 213,992	$ 0	$ 1,271,032	$ 1,721,634	$ 12,664	$ 3,208,035	$ 2,689,1
bert P. Barker e President and	$ 400,000	$ 407,320	$ 109,238	$ 0	$ 494,075	$ 1,291,264	$ 17,000	$ 1,858,054	$ 1,913,5

sident, Parker rospace Group									
kolas W. Vande Steeg sident and Chief erating Officer	$ 733,000	$ 962,123	$ 309,604	$ 325,050	$ 1,920,678	$ 2,700,946	$ 108,967	$ 5,192,525	$ 4,521,7

[1] *Options valued using binomial formula.*

[2] *Restricted stock is annualized over the year of the award and following three years; LTIP is annualized over the year of the award and previous two years. Average pay is based on three-years of pay data, when available.*

Source: Salary.com (www.executive.salary.com)

As disclosed for fiscal year end 2006.

Governance Analysis

Director Compensation

Board Member Compensation

Annual Fees						Initial Fees	
Cash	Stock Awards / Units ($)	Stock Options ($ / # shares)	Minimum Portion Paid In Stock	Board Meeting Fee	# Board Meetings	Stock Awards / Units ($)	Stock Options ($ / # shares)
$80,000	--	-- / 2,750	--	--	5	--	-- / --

Committee Compensation

Audit					Compensation					Nominating				
# Meetings	Member Fee	Member Retainer	Chair Fee	Chair Retainer	# Meetings	Member Fee	Member Retainer	Chair Fee	Chair Retainer	# Meetings	Member Fee	Member Retainer	Chair Fee	Chair Retainer
8	--	--	--	$ 15,000	5	--	--	--	$ 5,000	3	--	--	--	$ 5,000

Governance Analysis

Board Profile

Name	Nominee	Term Ends	Not Ind.	Position	Audit	Comp.	Nom.	Age	Tenure	Other Board Seats	<75% Att.	No stock	Prev. yr withhold votes
William E. Kassling	o	2008	o	Presiding Director	þ	o	Chair	62	5	1	o	o	0.8%
Robert J. Kohlhepp	þ	2009	o	o	Chair, Financial Expert	o	o	62	4	2	o	o	--
Giulio Mazzalupi	þ	2009	o	o	o	o	þ	65	7	--	o	o	--
Klaus-Peter Muller	þ	2009	o	o	o	o	þ	62	8	1	o	o	--
Candy M. Obourn	o	2007	o	o	o	þ	þ	56	4	--	o	o	--
Joseph M. Scaminace	o	2008	o	o	o	þ	þ	53	2	1	o	o	0.8%
Wolfgang R. Schmitt	o	2008	o	o	þ	Chair	o	62	14	--	o	o	1.3%
Markos I. Tambakeras	þ	2009	o	o	o	þ	o	56	1	2	o	o	--
Nickolas W. Vande Steeg	o	2007	þ	President, COO	o	o	o	63	2	1	o	o	--

Donald E. Washkewicz	o	2007	þ	Chair, CEO	o	o	o	56	6	--	o	o	--

Independence

Board	80.0%
Audit	100.0%
Compensation	100.0%
Nominating/Governance	100.0%

PROXY Governance believes that the Self-Regulatory Organizations (SROs) standards of independence are satisfactory and does not support the use of an additional overlay of independence standards, which may vary among advisory services, institutional investors, and commentators. PROXY Governance believes that if the SROs standards are perceived to be inappropriate, interested parties should reopen the debate with the SROs or the SEC to have those standards adjusted.

Governance Analysis

Stock Ownership/Voting Structure

Type of stock	Outstanding shares	Vote(s) per share
Common Stock	119,738,081	1

Director & Officer Ownership

2.2%

Significant Shareholders

Lord, Abbett & Co. LLC	9.6%
Wellington Management Company, LLP	7.6%
Barclays Global Investors, NA	5.6%
Capital Research and Management Company	5.1%

Governance Analysis

State Law Statutory Provisions

State of incorporation	Ohio
Business combination	þ
Control share acquisition	þ
Fair price provision	þ
Constituency provision	þ
Poison pill endorsement	þ

Charter/Bylaws Provisions

Classified board	þ
Cumulative voting	þ
Dual class/unequal voting rights	o
Blank check preferred stock	þ
Poison pill	o
Directors may be removed only for cause	þ
Only directors may fill board vacancies	þ
Only directors can change board size	o
Supermajority vote to remove directors	o
Prohibit shareholders to call special meetings	o
Prohibit action by written consent	o
Fair price provision	þ
Supermajority vote for mergers/business transactions	þ
Supermajority to amend charter/bylaw provisions	þ
Constituency provision	o

Governance Analysis
Auditor Profile

Peer group includes companies listed under Executive Compensation.

PricewaterhouseCoopers LLP has served as the company s independent auditors since 1938.

Audit Fees

	Audit fees	Audit Related fees	Tax fees	Other fees	Total fees paid
PARKER-HANNIFIN CORP	$ 9,260,000	$423,127	$ 2,390,000	$ 0	$ 12,073,127

As disclosed for fiscal year end 2006.

Governance Analysis
Vote Results of Last Annual Meeting

Proposals		**% FOR Votes[1]**	**For Votes**	**Against Votes**	**Abstentions**	**Broker Non-Votes**
MGT	Elect directors[2]	98.7% - 99.2%				
MGT		97.7%	105,262,594	2,528,746	802,248	0

	Ratify Appointment of Auditors PricewaterhouseCoopers LLP					
MGT	Approve Parker-Hannifin Corporation Performance Bonus Plan	94.9%	94,686,551	5,096,465	1,367,775	7,442,797
SH	Eliminate Classified Board	78.3%	77,842,086	21,633,982	1,674,723	7,442,797

[1] *As a % of votes cast for and against; may not reflect passage of proposal.*

[2] *Low High director votes.*

Note: See the Board Profile for individual director votes.

Proposal Analysis

Management

1 Elect Nominees

PROXY Governance Vote Recommendation: FOR

Proposal:

To elect the following four nominees to the board: R. Kohlhepp, G. Mazzalupi, K. Muller, M. Tambakeras

The company has a staggered board.

Analysis:

Board size: 10

New directors since last year: 0

Independent directors: 8

Non-Independent directors: 2

Non-Independent directors: President/COO N. Vande Steeg, Chair/CEO D. Washkewicz

D. Collins, whose term expires in October 2006, and P. Likins, whose term expires in October 2008, will both retire from the board effective as of Oct. 25, 2006 due to the policy of mandatory retirement at age 70. H. Ortino, whose term was set to expire in October 2007, passed away in November 2005.

Unless there is evidence of a breakdown in board monitoring or effectiveness such as poor corporate performance relative to peers, excessive executive compensation, noncompliance with SEC rules or SRO listing standards, a lack of responsiveness to legitimate shareholder concerns, or various other factors we presume that the board is properly discharging its oversight role and that it is adequately policing itself in terms of board organization, composition and functioning.

Performance: According to PROXY *Governance* s performance analysis, the company has performed **in line** with peers over the past five years; the company ranks at the 53rd percentile relative to the S&P 1500.

Compensation: The average three-year compensation paid to the CEO is 48% above the median paid to CEOs at peer companies and the average three-year compensation paid to the other named executives is 72% above the median paid to executives at peer companies.

The company s executive compensation appears **somewhat high** compared to peers and given its financial performance relative to peers, which we attribute to the high value of stock options and restricted stock awarded to the company s other named executives.

The company s long-term incentive compensation for its executive officers included both stock options and restricted stock awards. The restricted stock awarded to an individual executive was based on a target stock incentive dollar value, which was established by the Compensation Committee at the market median of comparable stock compensation for the company s Compensation Comparison Group, a group of primarily Fortune 300 industrial manufacturing companies. Individual payments were determined by comparing the company s revenue growth, earnings per share, and return on invested capital to a group of approximately 20 peers. For example, President/COO Vande Steeg was awarded $2.7 million in restricted stock, and EVP J. Myslenski was awarded $2.5 million in restricted stock.

The stock option grants were also based on a target value established at the Compensation Comparison Group s market median of comparable stock incentive compensation. For example, Vande Steeg was granted stock options valued at $1.9 million using a binomial formula, and Myslenski was granted stock options valued at $2.3 million using a binomial formula. The options vest ratably over three years following the grant date.

While the company s compensation to its other named executives is somewhat high compared to peers, we note that company performance is generally in line, and that the long-term incentive awards are based on comparable stock-based awards within the industry. We will continue to monitor executive compensation.

Rationale/Conclusion:

PROXY *Governance* believes that the board is properly discharging its oversight role and adequately policing itself. However, we will continue to monitor executive compensation going forward.

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Management

2 Ratify Appointment of Auditors PricewaterhouseCoopers LLP

PROXY *Governance* Vote Recommendation: FOR

Proposal:

The Audit Committee has selected PricewaterhouseCoopers LLP as the company s independent auditors for the next fiscal year.

Analysis:

Barring circumstances where there is an audit failure due to the auditor not following its own procedures or where the auditor is otherwise complicit in an accounting treatment that misrepresents the financial condition of the company, PROXY *Governance* recommends the company s choice of auditor. PROXY *Governance* believes that concerns about a corporation s choice of auditor and the services performed (e.g., high non-audit fees) should be directed through withhold votes from the members of the audit committee, which is responsible for retaining and compensating the auditor.

We note that PricewaterhouseCoopers LLP has served as the company s outside auditor since 1938. Given this lengthy tenure, the Audit Committee report or charter should disclose the committee s policies and process for periodically evaluating the audit firm.

Rationale/Conclusion:

We believe that, in this circumstance, the board/audit committee should be accorded discretion in its selection of the auditor.

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Shareholder

3 Eliminate Classified Board

PROXY *Governance* Vote Recommendation: AGAINST

Proposal:

The proponent requests that the board take the necessary steps to declassify the board so that all directors are elected annually. Approval of this proposal will not automatically eliminate the classified board structure since to do so would require an amendment of the company s governing documents.

Proponent:

UNITE HERE

Shareholder View:

The proponent believes that shareholders should have the opportunity to vote on the performance of the entire board each year and notes that institutional investors are calling for the end of classified boards and many large companies are following this practice. The proponent also notes last year s vote result on the same issue.

Management View:

The company believes that it is in the best interests of shareholders to maintain the classified board structure because it ensures the stability of continuous, experienced directors who have specific knowledge of the company and the industry in which it operates, which helps to support long-term corporate strategies. In addition, a classified board enhances its ability to negotiate the best results for shareholders in a takeover situation since at least two annual meetings would be required to effect a change in control of the board.

Analysis:

PROXY *Governance* generally believes that, in many situations, classified boards serve a very useful purpose and that they should not always be disparaged as simply another antitakeover device. In some cases, a classified board can enhance director independence, and, at companies with majority voting in director elections, a classified board safeguards against the possibility of all directors failing an election at once.

We note that the arguments against classified boards relating to their antitakeover effect are solely dependent on the classification being coupled with a removal of directors only for cause provision. Absent such a provision there would be no antitakeover effect. However, the ability to decouple board classification and removal for cause only provisions varies from state to state. We believe, therefore, that much of the motivation for these declassification proposals and rationale for them is misdirected at the classified board concept, when it should be directed if the proponent is opposed to antitakeover measures at the removal for cause concept.

Under the Ohio General Corporation Law, if a corporation s board is divided into classes, then directors may be removed by the shareholders only for cause.

We note that the company has performed **in line** with peers over the past five years; the company ranks at the 53rd percentile relative to the S&P 1500.

We also note that the board is 80% independent and that the average tenure on the board is 5 years.

We note that a shareholder proposal on this issue received support from 78.3% of the votes cast at last year s annual meeting.

Rationale/Conclusion:

We do not believe the classified board has been detrimental to shareholders and, in fact, can provide benefits such as promoting independence and stability.

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