

GENERAC HOLDINGS INC.  
Form DEF 14A  
April 29, 2013

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

**SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of  
the Securities Exchange Act of 1934 (Amendment No. )

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material under §240.14a-12

**GENERAC HOLDINGS INC.**

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(Name of Registrant as Specified In Its Charter)

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

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.
  - (1) Title of each class of securities to which transaction applies:
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- (4) Proposed maximum aggregate value of transaction:
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      - (1) Amount Previously Paid:
      - (2) Form, Schedule or Registration Statement No.:
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      - (4) Date Filed:
-

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**GENERAC HOLDINGS INC.**

**S45 W29290 Hwy. 59  
Waukesha, Wisconsin 53189**

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**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS  
To Be Held June 12, 2013**

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To our stockholders,

Notice is hereby given that the 2013 annual meeting of stockholders of Generac Holdings Inc. will be held on Wednesday, June 12, 2013, at 9:00 a.m. local time, at Generac corporate headquarters at S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189, for the following purposes:

1. To elect the three nominees named herein as Class I directors;
2. To ratify the selection of Ernst & Young LLP as our independent registered public accounting firm for the year ending December 31, 2013;
3. To vote on an advisory, non-binding "say-on-pay" resolution to approve the compensation of our executive officers;
4. To consider any other matters that may properly come before the meeting or any adjournments or postponements of the meeting.

Holders of record of our common stock at the close of business on April 23, 2013 are entitled to notice of, and to vote at, the annual meeting. Stockholders of record may vote their shares via telephone or over the Internet or, if a paper proxy card is requested, by signing, dating and mailing the proxy card in the envelope provided or by delivering any completed proxy card at the annual meeting. Stockholders of record may also vote in person at the annual meeting. Instructions regarding all methods of voting are contained on any Notice of Internet Availability of Proxy Materials or proxy card provided. If your shares are held in the name of a bank, broker, fiduciary or custodian, follow the voting instructions you receive from your record holder.

By Order of the Board of Directors,

Aaron Jagdfeld  
*President and Chief Executive Officer*

April 29, 2013

**YOUR VOTE IS IMPORTANT. WHETHER OR NOT YOU INTEND TO BE PRESENT AT THE MEETING, TO ASSURE THAT YOUR SHARES ARE REPRESENTED AT THE MEETING PLEASE VOTE PROMPTLY BY TELEPHONE OR THE INTERNET, OR REQUEST A PROXY CARD TO COMPLETE, SIGN AND RETURN. IF YOU ATTEND THE MEETING, YOU MAY VOTE IN PERSON IF YOU WISH TO DO SO, EVEN IF YOU HAVE PREVIOUSLY SUBMITTED YOUR PROXY.**

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**GENERAC HOLDINGS INC.**

S45 W29290 Hwy. 59  
Waukesha, Wisconsin 53189

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**PROXY STATEMENT**

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**ANNUAL MEETING OF STOCKHOLDERS**

June 12, 2013

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**INFORMATION CONCERNING SOLICITATION AND VOTING**

The Board of Directors (the "*Board of Directors*" or "*Board*") of Generac Holdings Inc. ("*Generac*," "*we*," "*us*," "*our*," or the "*Company*,") is soliciting your proxy to be voted at the Annual Meeting of Stockholders to be held on Wednesday, June 12, 2013, at 9:00 a.m. local time, at Generac corporate headquarters at S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189, and any postponement or adjournment thereof.

In accordance with rules and regulations of the Securities and Exchange Commission (the "*SEC*"), instead of mailing a printed copy of our proxy materials to each stockholder of record or beneficial owner, we furnish proxy materials, which include this proxy statement and the accompanying proxy card, notice of meeting, and annual report to stockholders, to our stockholders over the Internet unless otherwise instructed by the stockholder. If you received a Notice of Internet Availability of Proxy Materials ("*Notice of Internet Availability*") by mail and would like to receive a printed copy of our proxy materials, you should follow the instructions for requesting such materials included in the Notice of Internet Availability. The Notice of Internet Availability was first mailed on or about May 2, 2013 to all stockholders of record as the record date for the annual meeting, which was the close of business on April 23, 2013.

**Matters to be Considered**

At the meeting, stockholders will be asked to vote to elect the three nominees named herein as Class I directors, to ratify the selection of the independent registered public accounting firm and to vote on an advisory, non-binding "say-on-pay" resolution to approve the compensation of our executive officers. See "PROPOSAL 1 ELECTION OF CLASS I DIRECTORS", "PROPOSAL 2 RATIFICATION OF SELECTION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM." and "PROPOSAL 3 ADVISORY VOTE ON EXECUTIVE COMPENSATION". The Board of Directors does not know of any matters to be brought before the meeting other than as set forth in the notice of meeting. If any other matters properly come before the meeting, the persons named in the enclosed form of proxy or their substitutes will vote in accordance with their best judgment on such matters.

**Record Date; Stock Outstanding and Entitled to Vote**

Holders of common stock as of the record date are entitled to notice of, and to vote at, the annual meeting. As of the record date, there were 68,398,269 shares of common stock outstanding and entitled to vote at the annual meeting, with each share entitled to one vote.

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If you are a stockholder of record, you will need to present the Notice of Internet Availability or proxy card that you received, together with a form of personal photo identification, in order to be admitted into the meeting. If you are the beneficial owner of shares held in "street name," you will need to provide proof of ownership, such as a recent account statement or letter from your bank, broker or other nominee as of the close of business on April 23, 2013, along with a form of personal photo identification. Alternatively, you may contact the broker, bank or other nominee in whose name your shares of common stock are registered and obtain a legal proxy to bring to the meeting. No cameras, recording equipment, electronic devices, large bags, briefcases or packages will be permitted into the meeting or adjacent areas. All other items may be subject to search.

**Information About This Proxy Statement**

*Why you received this proxy statement.* These materials have been made available to you on the internet or, upon your request, have been delivered to you in printed form, because our Board of Directors is soliciting your proxy to vote your shares at the annual meeting and any postponement or adjournment thereof. This proxy statement includes information that we are required to provide to you under the rules of the SEC and that is designed to assist you in voting your shares. If you own our common stock in more than one account, such as individually and also jointly with your spouse, you may receive more than one Notice of Internet Availability relating to these proxy materials or copy of these materials themselves. To assist us in saving money and to serve you more efficiently, we encourage you to have all your accounts registered in the same name and address by contacting our transfer agent:

Computershare Trust Company, N.A.  
250 Royall Street  
Canton, MA 02021  
Telephone: (800) 962-4284  
Fax: (312) 601 2312

*Householding.* The SEC's rules permit us to deliver a single Notice of Internet Availability or set of annual meeting materials to one address shared by two or more of our stockholders. This delivery method is referred to as "householding" and can result in significant cost savings. To take advantage of this opportunity, we have delivered only one Notice of Internet Availability or proxy statement and annual report to multiple stockholders who share an address, unless we received contrary instructions from the impacted stockholders prior to the mailing date. We agree to deliver promptly, upon written or oral request, a separate Notice of Internet Availability or copy of the other proxy materials to any stockholder at the shared address to which a single copy of those documents was delivered. If you are a record holder and if you prefer to receive separate copies of the proxy materials, please contact York Ragen, Chief Financial Officer, Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189.

If you are currently a stockholder sharing an address with another stockholder and wish to receive only one copy of future proxy statements and other communications for your household, please contact York Ragen, CFO, at the above address.

**Voting by and Revocation of Proxies**

Stockholders of record are requested to vote by proxy in one of three ways:

By telephone Use the toll-free telephone number shown on the Notice of Internet Availability or any proxy card you receive;

By internet Visit the Internet website indicated on the Notice of Internet Availability or any proxy card you receive and follow the on-screen instructions;

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**By mail** If you request a paper proxy card by telephone or internet, you may elect to vote by mail. If you elect to do so, you should date, sign and promptly return your proxy card by mail in the postage prepaid envelope which accompanied that proxy card; or

**In person** You can deliver a completed proxy card at the meeting or vote in person.

Voting instructions (including instructions for both telephonic and Internet proxies) are provided on the Notice of Internet Availability and on any proxy card you receive. The Internet and telephone proxy procedures are designed to authenticate stockholder identities, to allow stockholders to give voting instructions and to confirm that stockholders' instructions have been recorded properly. A control number, located on the Notice of Internet Availability or proxy card, will identify stockholders and allow them to submit their proxies and confirm that their voting instructions have been properly recorded. Costs associated with electronic access, such as usage charges from Internet access providers and telephone companies, must be borne by the stockholder. If you submit your proxy by Internet or telephone, it will not be necessary to return a proxy card for your vote to be counted.

If a stockholder does not submit a proxy by the Internet or by telephone or return a signed proxy card, and does not attend the meeting and vote in person, his or her shares will not be voted. Shares of our common stock represented by properly executed proxies received by us or proxies submitted by telephone or via the Internet, which are not revoked, will be voted at the meeting in accordance with the instructions contained therein.

**If instructions are not given and you do not indicate how your shares should be voted on a proposal, the shares represented by a properly completed proxy will be voted as the Board recommends.** In addition, we reserve the right to exercise discretionary authority to vote proxies, in the manner determined by the Company in its sole discretion, on any matters brought before the 2013 annual meeting for which we did not receive adequate notice under the proxy rules promulgated by the SEC.

Any proxy signed and returned by a stockholder or submitted by telephone or via the Internet may be revoked at any time before it is exercised by giving written notice of revocation to the Company's Secretary at our address set forth herein, by executing and delivering a later-dated proxy (either in writing, by telephone or via the Internet) or by voting in person at the meeting. Attendance at the meeting will not, in and of itself, constitute revocation of a proxy.

If your shares are held in the name of a bank, broker, fiduciary or custodian, follow the voting instructions on the form you receive from your record holder. The availability of Internet and telephone proxies for these stockholders will depend on their voting procedures.

### **Quorum**

The presence at the annual meeting, in person or by proxy, of the holders of at least 34,199,135 shares, constituting a majority of the number of shares of common stock issued and outstanding and entitled to vote as of the record date, is required to constitute a quorum to transact business at the annual meeting. Abstentions and broker non-votes will be counted toward the establishment of a quorum.

### **Required Votes**

*Election of Nominees named herein as Directors.* Proposal 1. Under our Amended and Restated Bylaws (the "Bylaws"), the affirmative vote of the holders of a plurality of shares of common stock voting on this matter at the annual meeting (i.e., the largest number of votes cast) is required to elect each nominee named herein as a director. Consequently, only shares that are voted in favor of a particular nominee will be counted toward such nominee's achievement of a plurality.



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*Ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm.* Proposal 2, relating to the ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm for 2013, will be approved if it receives the affirmative vote of the holders of a majority of the shares of common stock voting on the matter at the annual meeting. Shares not voted (because of abstention, broker non-vote, or otherwise) will have no effect on the approval of the resolution.

*Approval of Non-Binding "Say-on-Pay" Resolution Regarding Executive Compensation.* Proposal 3, relating to the non-binding resolution to approve our executive compensation, will be approved if it receives the affirmative vote of the holders of a majority of the shares of common stock voting on the matter at the annual meeting. Shares not voted (because of abstention, broker non-vote, or otherwise) will have no effect on the approval of the resolution.

*Other Matters.* If any other matters are properly presented at the annual meeting for action, including a question of adjourning or postponing the meeting from time to time, the persons named in the proxies and acting thereunder will have discretion to vote on such matters in accordance with their best judgment.

### **Shares Held by Brokers**

If you are the beneficial owner of shares held for you by a broker, your broker must vote those shares in accordance with your instructions. If you do not give voting instructions to your broker, your broker may vote your shares for you on any discretionary items of business to be voted upon at the annual meeting. If you do not provide voting instructions on a non-discretionary item, including the election of the nominees named herein as directors, the shares will be treated as "broker non-votes." We believe that the ratification of the appointment of Ernst & Young LLP (Proposal 2) is a routine matter on which brokers will be permitted to vote any unvoted shares in their discretion. We also believe that election of the three nominees named herein as Class I directors (Proposal 1) and the advisory, non-binding "say on pay" resolution (Proposal 3) are non-routine matters on which brokers will not be permitted to vote any unvoted shares. "Broker non-votes" will be included in determining the presence of a quorum at the annual meeting but will have no effect on the outcome of the vote on any of the matters described in this proxy statement.

### **Proxy Solicitation**

We will bear the costs of solicitation of proxies for the annual meeting, including preparation, assembly, printing and mailing of the Notice of Internet Availability, this proxy statement, the annual report, any proxy card and any additional information furnished to stockholders. Copies of our proxy statement will be furnished, upon request, to banks, brokerage houses, fiduciaries and custodians holding shares of common stock beneficially owned by others to forward to such beneficial owners. We may reimburse persons representing beneficial owners of common stock for their costs of forwarding solicitation material to such beneficial owners. In addition, under the terms of our engagement with Computershare Trust Company, N.A. ("*Computershare*") as transfer agent for the Company, Computershare provides services in connection with our annual meeting. The anticipated total cost of such engagement is \$12,000, of which a small portion of such cost relates to services provided in connection with our annual meeting. Solicitation of proxies by mail may be supplemented by telephone, email or personal solicitation by Computershare or by directors, officers, or other regular employees of the Company. No additional compensation will be paid to directors, officers or other regular employees for such services.

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**Independent Registered Public Accounting Firm**

We have been advised that a representative of Ernst & Young LLP, our independent registered public accounting firm for the year ended December 31, 2012, will attend the annual meeting, will have an opportunity to make a statement if such representative desires to do so, and will be available to respond to appropriate questions.

**Annual Report and Company Information**

**Our Annual Report to Stockholders, which contains consolidated financial statements for the year ended December 31, 2012, is being furnished to stockholders concurrently herewith. You also may obtain a copy of our Annual Report on Form 10-K for the year ended December 31, 2012 that was filed with the SEC, without charge, by writing to Generac Holdings Inc., Attn: Investor Relations, S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189. These materials will also be available without charge at "Investor Relations" on our website at [www.generac.com](http://www.generac.com).**

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**PROPOSAL 1 ELECTION OF CLASS I DIRECTORS**

Our Third Amended and Restated Certificate of Incorporation provides that our Board of Directors is divided into three classes, as nearly equal in number as possible, with each class serving a consecutive three-year term. The term of the current Class I Directors will expire on the date of the 2013 annual meeting, subject to the election and qualification of their respective successors.

In selecting director candidates, the Nominating and Corporate Governance Committee considers whether the candidates possess the required skill sets and fulfill the qualification requirements of directors approved by the Board of Directors, including integrity, objectivity, sound judgment, leadership and diversity of experience (for example, in relation to finance and accounting, strategy, risk, technical expertise, policy-making, etc.). The following biographies describe the business experience of each director. Following the biographical information for each director below, we have listed qualifications that, in addition to those discussed above, the Board of Directors considered in determining whether to recommend the director be nominated for reelection.

The nominees for election as Class I Directors at the 2013 annual meeting are described below. The Board, upon the recommendation of the Nominating and Corporate Governance Committee of the Board of Directors has nominated each of the candidates for election. If elected, each of the nominees is expected to serve for a three-year term expiring at the annual meeting of stockholders of the Company in 2016 and until their respective successors have been elected and qualified. The Board of Directors expects that each of the nominees will be available for election as a director. However, if by reason of an unexpected occurrence, one or more of the nominees is not available for election, the persons named in the form of proxy have advised that they will vote for such substitute nominees as the Board of Directors may nominate.

**The Board of Directors recommends a vote *FOR* the Company's nominees for Class I Directors.**

**Nominees for Election**

**Name and present position,  
if any, with the Company**

**Age, period served as a director, other business experience**

**Class I Directors**

Aaron Jagdfeld  
*President and Chief Executive  
Officer*

41, has served as our Chief Executive Officer since September 30, 2008 and as a director since November 2006. Prior to becoming Chief Executive Officer, Mr. Jagdfeld worked for Generac for 15 years. He began his career in the finance department in 1994 and became our Chief Financial Officer in 2002. In 2007, he was appointed president and was responsible for sales, marketing, engineering and product development. Prior to joining Generac, Mr. Jagdfeld worked in the audit practice of the Milwaukee, Wisconsin office of Deloitte & Touche. Mr. Jagdfeld holds a Bachelor of Business Administration in Accounting from the University of Wisconsin-Whitewater.

Mr. Jagdfeld is our Chief Executive Officer and a director on our Board of Directors. As the Chief Executive Officer and the only management representative on the Board, Mr. Jagdfeld provides valuable insight to the Board into the day-to-day business issues facing the Company. Since joining the Company, he has navigated a number of challenges, including our initial public offering and the recent significant increase in sales volumes. Mr. Jagdfeld has extensive finance experience and has high-level leadership experience in several prior positions.

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**Name and present position, if any, with the Company**

**Age, period served as a director, other business experience**

John D. Bowlin

62, has served as a director of Generac since December 2006. Mr. Bowlin served as a consultant to CCMP Capital Advisors, LLC ("CCMP") from January 2008 through December 2011. Mr. Bowlin previously served as President and Chief Executive Officer of Miller Brewing Company from 1999 until 2003. From 1985 until 2002, Mr. Bowlin was employed by Philip Morris Companies, Inc., in various leadership capacities, including President, Kraft International, Inc. (1996-1999), President and Chief Operating Officer, Kraft Foods North America (1994-1996), President and Chief Operating Officer, Miller Brewing Company (1993-1994), and President, Oscar Mayer Food Corporation (1991-1993). He currently serves as a director of Schwan Food Company, and he previously served as a director and Non-Executive Chairman of Spectrum Brands and as a director of Pliant Corporation.

Mr. Bowlin has extensive leadership skills and operations experience in senior positions, including as Chairman, Chief Executive Officer and Chief Operating Officer for a number of private companies and divisions of public companies.

Timothy Walsh

50, has served as a director of Generac since November 2006 and served as our Lead Director from the time of the Company's initial public offering to April 2013, when Timothy W. Sullivan was elected independent non-executive Chairman of the Board. Mr. Walsh currently serves as a Managing Director in the New York office of CCMP. Prior to joining CCMP when it was founded in August 2006, Mr. Walsh was a Partner at J.P. Morgan Partners, LLC. Prior to joining J.P. Morgan Partners in 1993, Mr. Walsh worked on various industry-focused client teams within The Chase Manhattan Corporation. Mr. Walsh holds a B.S. from Trinity College and an M.B.A. from the University of Chicago Graduate School of Business. During the past five years, he previously served on the board of directors of Kraton Performance Polymers, Inc., Klöckner Pentaplast GmbH & Co. KG, Pliant Corporation and PQ Corporation.

Mr. Walsh represents stockholder interests in that he was originally appointed as a director of the Company by our then-majority stockholder. He has excellent skills and experience in corporate finance, having over two decades of experience in banking, investment banking and private equity finance. He also has experience as a director of a diverse group of private and public companies, including early stage public companies. Mr. Walsh also has a longstanding tenure on the Board, which provides a breadth of experience with the Company that is beneficial to the Board as a whole.

**Other Members of the Board of Directors**

Including the nominees, the Board of Directors currently consists of eight (8) directors, each of whom, other than the nominees, is described below. The terms of the Class II Directors expire at the 2014 Annual Meeting of Stockholders, subject to the election and qualification of their respective successors. The terms of the Class III Directors expire at the 2015 Annual Meeting of Stockholders, subject to the election and qualification of their respective successors.

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**Name and present position,  
if any, with the Company**  
**Class II Directors**

**Age, period served as a director, other business experience**

Stephen Murray

50, has served as a director of Generac since November 2006. Mr. Murray currently serves as President and Chief Executive Officer of CCMP. Prior to joining CCMP when it was founded in August 2006, Mr. Murray was a Partner at J.P. Morgan Partners, LLC. Prior to joining J.P. Morgan Partners in 1989, Mr. Murray was a Vice President with the Middle-Market Lending Division of Manufacturers Hanover. Mr. Murray holds a B.A. from Boston College and an M.B.A. from Columbia Business School. He currently serves on the board of directors of ARAMARK Corporation and Warner Chilcott. In addition, during the past five years, he has served as a director of Cabelas Incorporated.

Mr. Murray represents stockholder interests in that he was originally appointed as a director of the Company by our then-majority stockholder. He has extensive experience in the financial and investment industry, a wealth of management experience and leadership skills he developed at CCMP and J.P. Morgan Partners. He also has experience as a director of a diverse group of private and public companies, including early stage public companies. Mr. Murray also has a longstanding tenure on the Board, which provides a breadth of experience with the Company that is beneficial to the Board as a whole.

Timothy W. Sullivan

59, has served as a director of Generac since September 2012 and as non-executive Chairman of the Board since April 9, 2013. In 2012 Mr. Sullivan served as a special consultant to Wisconsin Governor Scott Walker and as an Executive Advisor to CCMP. He chaired the Wisconsin Governor's Council on Workforce Investment, the Wisconsin Governor's College and Workforce Readiness Council and the Wisconsin Mining Association. Mr. Sullivan served as President and CEO of Bucyrus International, Inc. from 2004 to 2011 and also as President and COO from 2000 to 2004. He was President and CEO of United Container Machinery Company from 1999 to 2000. From 1976 to 1998 Mr. Sullivan worked for Bucyrus in a series of operating and management roles. He currently serves as a Trustee and Non-Executive Director of Northwestern Mutual Life Insurance Company and he sits on the Board of Directors of Aurora Health Care, Inc., the Bucyrus Foundation, Carroll University, Cliffs Natural Resources Inc., Metropolitan Milwaukee Association of Commerce, Milacron Inc. and St. Ann Center for Intergenerational Care. Mr. Sullivan earned a B.S. in Business Administration from Carroll University as well as a master's degree in business administration from the American Graduate School of International Management.

Mr. Sullivan brings to Generac extensive leadership skills and expertise in international industrial markets gained in such senior roles as Chief Executive Officer and Chief Operating Officer for both private and public companies.

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**Name and present position,  
if any, with the Company  
Class III Directors**

**Age, period served as a director, other business experience**

Barry J. Goldstein

70, has served as a director of Generac since September 2009. In October 2000, Mr. Goldstein retired as Executive Vice President and Chief Financial Officer of Office Depot, Inc., which he joined as Chief Financial Officer in May 1987. Mr. Goldstein was with Grant Thornton from 1969 through May 1987, where he was named a Partner in 1976. Mr. Goldstein currently serves on the board of directors of Kraton Performance Polymers, Inc.

Mr. Goldstein has over 30 years of finance experience and has experience as a director for a number of private and public companies.

David A. Ramon

57, has served as a director of Generac since April 15, 2010. Mr. Ramon has more than 30 years of broad management, operations and investment experience with both established and emerging companies. He co-founded Vaduz Partners in 1998, a private investment firm for which he continues to serve as a Managing Partner. From 2000 through 2007, Mr. Ramon was also President, Chief Executive Officer, and director of USA.NET, Inc. From 1997 to 1998, he was President of the Coleman Outdoor Recreation Group. From 1993 to 1997, Mr. Ramon held various senior management positions including President and Chief Operating Officer of New World Television, Inc. and director of New World Communications Group, Inc. From 1982 to 1994, Mr. Ramon served as the Executive Vice President and Chief Financial Officer of Gillett Holdings, Inc. Prior to 1982, Mr. Ramon was employed by Arthur Young & Company and earned a Bachelor of Business Administration degree in accounting from the University of Wisconsin. He serves on the management board of TTBG, LLC and Diversified Maintenance Systems Holdings, LLC.

Mr. Ramon has extensive finance, high-level leadership and financial experience, including as CEO, COO, President and CFO of a number of private and public companies. He also has excellent skills and experience in corporate finance, having over 30 years of experience in finance and accounting.

Robert D. Dixon

53, has served as a director of Generac since March 14, 2012. Since October 2012 Mr. Dixon has served as Chief Executive Officer of Seven Seas Water Corporation. Previously, Mr. Dixon was Senior Vice President & General Manager at Air Products and Chemicals, Inc. ("Air Products") from 2007 to 2011. From 2003 to 2006, while based in Singapore, he was President of Air Products Asia Inc. Mr. Dixon served as the Vice President for the Structured Business Division from 2001 to 2003. From 1989 to 2000, Mr. Dixon held various senior management positions within Air Products, including vice president, finance, for a joint venture with Mitsubishi Heavy Industries, Group Controller and General Manager. Prior to joining Air Products in 1983, he earned a Masters Degree in Business Administration from the Pennsylvania State University.

Mr. Dixon has 30 years of global management, operations and finance experience.

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**CORPORATE GOVERNANCE**

**Board of Directors Independence Standards for Directors and Controlled Company Exemption**

Pursuant to our Corporate Governance Policy, a copy of which is available on our website at [www.generac.com](http://www.generac.com), the Board of Directors is required to affirmatively determine whether our directors are independent under the listing standards of the New York Stock Exchange ("NYSE"), the principal exchange on which our common stock is traded.

During its annual review of director independence, the Board of Directors considers all information it deems relevant, including without limitation, any transactions and relationships between each director or any member of his immediate family and the Company and its subsidiaries and affiliates. The Board of Directors also considers the recommendations of the Nominating and Corporate Governance Committee, which conducts a separate independence assessment of all directors as part of its nomination process for the Board of Directors and its respective committees. The purpose of this review is to determine whether any such relationship or transaction is considered a "material relationship" that would be inconsistent with a determination that a director is independent. The Board of Directors has not adopted any "categorical standards" for assessing independence, preferring instead to consider all relevant facts and circumstances in making an independence determination including, without limitation, applicable independence standards promulgated by the NYSE.

As a result of this review, the Board of Directors affirmatively determined that John D. Bowlin, Robert D. Dixon, Barry J. Goldstein, David A. Ramon, Stephen Murray, Timothy Walsh and Timothy W. Sullivan are independent directors under the applicable rules of the NYSE.

Because affiliates of CCMP no longer control a majority of our outstanding common stock, we ceased to be a "controlled company" in December 2012 within the meaning of the NYSE corporate governance standards. As a result, we no longer rely upon the exemption whereby a "controlled company" may elect not to comply with certain NYSE corporate governance standards.

**Committees of the Board of Directors**

Our Board of Directors has three standing committees: an Audit Committee, a Compensation Committee and a Nominating and Corporate Governance Committee. Our Board of Directors has adopted charters for each of its standing committees. Copies of our committee charters are posted on our website at [www.generac.com](http://www.generac.com).

**Audit Committee**

The current members of the Audit Committee are Mr. Barry J. Goldstein (Chair), Mr. David A. Ramon and Mr. John D. Bowlin. The Board has determined that Mr. Goldstein and Mr. Ramon are "audit committee financial experts" as defined in Item 407(d)(5) of Regulation S-K, and the Board is satisfied that all members of our audit committee have sufficient expertise and business and financial experience necessary to effectively perform their duties as members of the audit committee. Each of the members of the Audit Committee meet the definition of "independent director" for purposes of serving on an audit committee under applicable SEC and New York Stock Exchange rules.

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The Audit Committee, among other things, assists the Board of Directors in fulfilling its responsibility relating to (a) the integrity of our financial statements, (b) our systems of internal controls and disclosure controls and procedures, (c) our compliance with applicable law and ethics programs, (d) the annual independent audit of our financial statements and (e) the evaluation of financial and enterprise risks. In connection with its review of the Company's financial statements, the Audit Committee receives reports from the Company's Chief Financial Officer and the Company's independent registered public accounting firm regarding significant risks and exposures and assesses management's steps to minimize them. The Audit Committee also reviews material legal and regulatory matters and compliance with significant applicable legal, ethical and regulatory requirements, and receives reports from the Company's management relating to these matters.

In discharging its duties, the Audit Committee has the sole authority to select, retain, oversee and terminate, if necessary, the independent registered public accounting firm, review and approve the scope of the annual audit, review and pre-approve the engagement of our independent registered public accounting firm to perform audit and non-audit services, meet independently with our independent registered public accounting firm and senior management, review the integrity of our financial reporting process and review our financial statements and disclosures and certain SEC filings and financial press releases.

The Audit Committee formally met nine times in 2012, and members of the Audit Committee also met informally amongst themselves, with management and with and other members of the Board from time to time. Decisions regarding audit-related matters were approved by our Board after taking into account the recommendations of the Audit Committee and its members. The Audit Committee maintains a committee charter and meets with our independent registered public accounting firm without management present on a regular basis.

**Compensation Committee**

The members of the Compensation Committee are Mr. Timothy Walsh (Chair), Mr. John D. Bowlin and Mr. Timothy W. Sullivan. The Board of Directors has determined that each member of the Compensation Committee qualifies as an "outside director" pursuant to Section 162(m) of the Internal Revenue Code of 1986, as amended. All members of the Compensation Committee consist of all independent directors as required by the NYSE corporate governance standards and applicable SEC rules.

The Compensation Committee plays an integral role in the Company's processes and procedures for the consideration and determination of executive and director compensation. The Compensation Committee determines the compensation policies and individual compensation decisions for our executive officers, and ensures that these policies and decisions are consistent with overall corporate performance. The Compensation Committee, in conjunction with the Nominating and Corporate Governance Committee, reviews the form and amount of director compensation and makes recommendations to the Board related thereto. The Compensation Committee has the authority to approve all stock option grants and other equity awards to our employees, directors and executive officers. The Compensation Committee also reviews and recommends to the Board of Directors the target annual incentive pool, the annual performance objectives for participants, and actual payouts to participants, including the executive officers. In setting compensation, the Compensation Committee works with its independent compensation consultant and management to create incentives that encourage an appropriate level of risk-taking that is consistent with the Company's business strategy and maximization of stockholder value.



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The Compensation Committee has sole decision-making authority with respect to all compensation decisions for our executive officers, including annual incentive plan awards and grants of equity awards subject to further action of the Board as the Board shall determine. The Compensation Committee is responsible for finalizing and approving the performance objectives relevant to the compensation of our CEO and other executive officers. The Nominating and Corporate Governance Committee is responsible for leading the Board of Directors in evaluating the performance of our CEO in light of those objectives.

The Compensation Committee's recommendations are developed with input from our CEO and, where appropriate, other senior executives. The Compensation Committee reviews management recommendations and input from compensation consultants, along with other sources of data when formulating its independent recommendations to the Board of Directors. A discussion and analysis of the Company's compensation decisions regarding the executive officers named in the Summary Compensation Table appears in this proxy statement under the heading "EXECUTIVE COMPENSATION Compensation Discussion and Analysis."

To assist it in performing its duties, the Compensation Committee has the authority to engage outside consulting firms. Pearl Meyer & Partners, LLC was engaged by the independent Compensation Committee in November 2011 to obtain independent information, analysis and recommendations respecting compensation matters. In its capacity as outside and independent compensation consultant, Pearl Meyer reports directly to the Compensation Committee.

The Compensation Committee has sole authority to replace compensation consultants retained from time to time, and to hire additional Compensation Committee consultants at any time. Representatives from outside consulting firms engaged by the Compensation Committee attend meetings of the Compensation Committee, as requested, and communicate with the Chairman of the Compensation Committee between meetings; however, the Compensation Committee is responsible for making recommendations to the Board of Directors regarding the compensation of our executive officers, and the Board of Directors has sole and ultimate decision-making authority in this regard.

The Compensation Committee determined that during the course of Pearl Meyer's engagement by the Committee that Pearl Meyer was independent.

The Compensation Committee reviews and discusses with management proposed Compensation Discussion and Analysis disclosures and determines whether to recommend the Compensation Discussion and Analysis to the Board of Directors for inclusion in the Company's proxy statement and annual report. The recommendation is described in the Compensation Committee Report included in this proxy statement.

The Compensation Committee formally met four times in 2012, and members of the Compensation Committee also met informally amongst themselves, with management and with other members of the Board from time to time. Decisions regarding executive compensation were approved by our Board after taking into account the recommendations of the Compensation Committee and its members.

**Nominating and Corporate Governance Committee**

The members of the Nominating and Corporate Governance Committee are Mr. Stephen Murray (Chair), Mr. Robert D. Dixon and Mr. Timothy W. Sullivan. The Nominating and Corporate Governance Committee consist of all independent directors within the meaning of the NYSE corporate governance standards and applicable SEC rules.

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The Nominating and Corporate Governance Committee (a) identifies candidates to serve as directors and on committees of the Board of Directors, (b) develops, recommends and reviews our corporate governance guidelines on a regular basis, and (c) assists the Board of Directors in its annual review of the Board of Directors performance. The Nominating and Corporate Governance Committee also undertakes such other tasks delegated to the committee by the Board of Directors, including matters relating to risk oversight. Specifically, going forward the Nominating and Corporate Governance Committee conducts an annual assessment of the Company's Code of Ethics and Business Conduct, and assesses compliance matters, ethics and training programs and certain other relevant legal and regulatory requirements as part of periodic updates from the Company's management.

The Nominating and Corporate Governance Committee formally met four times in 2012, but members of the Nominating and Corporate Governance Committee met informally amongst themselves, with management and other members of the Board from time to time. Decisions regarding board nominations and corporate governance-related matters were approved by our Board after taking into account the recommendations of the Nominating and Corporate Governance members.

**Criteria for Director Nominees**

In selecting director candidates, the Nominating and Corporate Governance Committee considers whether the candidates possess the required skill sets and fulfill the qualification requirements of directors approved by the Board of Directors, including integrity, objectivity, sound judgment, leadership and diversity of experience (for example, in relation to finance and accounting, international operations, strategy, risk, technical expertise, policy-making, etc.). Annually, the Nominating and Corporate Governance Committee assesses the composition of the Board of Directors, including the Committee's effectiveness in balancing the above considerations.

Other than the foregoing, there are no minimum criteria for director nominees, although the Nominating and Corporate Governance Committee may consider such other factors as it may deem are in the best interests of the Company and its stockholders. The Nominating and Corporate Governance Committee does not assign specific weights to, and a potential or incumbent director will not necessarily satisfy all of, the foregoing criteria and in evaluating a candidate does not distinguish on the basis of whether the candidate was recommended by a stockholder. Accordingly, the Nominating and Corporate Governance Committee does not have a formal diversity policy but considers diversity of experience, as noted above, as a component of evaluating the composition of the Board of Directors in connection with the annual nomination process.

**Process for Identifying and Evaluating Director Nominees**

The Nominating and Corporate Governance Committee identifies nominees by first evaluating the current members of the Board of Directors willing to continue in service. Current members of the Board of Directors with skills and experience that are relevant to the Company's business and who are willing to continue in service are considered for re-nomination, balancing the value of continuity of service by existing members of the Board of Directors with that of obtaining a new perspective. If any member of the Board of Directors does not wish to continue in service or if the Nominating and Corporate Governance Committee decides not to re-nominate a member for re-election, the Nominating and Corporate Governance Committee identifies the desired skills and experience of a new nominee based on the criteria listed above. Current members of the Nominating and Corporate Governance Committee and Board of Directors are polled for suggestions as to individuals meeting the criteria of the Nominating and Corporate Governance Committee. Executive search firms may also be retained to identify qualified individuals.

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**Stockholder Nominations**

Our Bylaws contain provisions which address the process by which a stockholder may nominate an individual to stand for election to the Board of Directors at the Company's annual meeting of stockholders. To make a nomination for election to the Board of Directors, a stockholder must submit his or her nomination by providing the person's name and appropriate background and biographical information by writing to the Nominating and Corporate Governance Committee at Generac Holdings Inc., Attn: Nominating and Corporate Governance Committee, S45 W29290 Hwy 59, Waukesha, Wisconsin 53189. A stockholder's nomination must be received by the Company's Secretary (i) no later than the close of business on the 90th day, nor earlier than the close of business on the 120th day, prior to the first anniversary of the previous year's annual meeting of stockholders, (ii) in the event the date of the annual meeting is more than 30 days before or more than 60 days after such anniversary date, notice by the stockholder to be timely must be so delivered not earlier than the close of business on the 120th day prior to the date of such annual meeting and not later than the close of business on the later of the 90th day prior to the date of such annual meeting or, if the first public announcement of the date of such annual meeting is less than 100 days prior to the date of such annual meeting, the 10th day following the day on which public announcement of the date of such meeting is first made by the Company, or (iii) in the case of a special meeting of stockholders called for the purpose of electing directors, not earlier than the close of business on the 120th day prior to such special meeting and not later than the close of business on the later of the 90th day prior to such special meeting or the 10th day following the date on which notice of the date of the special meeting was mailed or public disclosure of the date of the special meeting was made, whichever first occurs. A stockholder nomination must be accompanied by the information required by the Bylaws with respect to a stockholder director nominee.

We may require any proposed nominee to furnish other information as we may reasonably require to determine the eligibility of the proposed nominee to serve as a director of the Company. See "PROPOSALS BY STOCKHOLDERS" for the deadline for nominating persons for election as directors at our 2013 annual meeting of stockholders.

**Board of Directors Role in Risk Oversight**

Our Board and management continually monitor the material risks facing our Company, including financial risk, strategic risk, operational risk, and legal and compliance risk. Management regularly reports to the Board on its activities in monitoring and mitigating such risks. Overall responsibility for risk oversight rests with our Board. In addition, the Board may delegate risk oversight responsibility to a particular committee in situations in which the risk falls within the committee's area of focus or expertise. Our Board believes that for certain areas of risk, our Company is better served by having the initial risk evaluation and risk monitoring undertaken by a subset of the entire Board that is more focused on the issues pertaining to the particular risk. For instance, our Compensation Committee assists the Board in evaluating risks relating to our compensation policies and procedures. Also, our Audit Committee assists the Board in fulfilling the Board's oversight responsibility relating to the evaluation of financial and enterprise risks. As it deems necessary, the respective committee to which oversight and monitoring of a particular risk has been assigned reports on risk exposures and mitigation strategies with respect to such risk to the entire Board. In February 2013 an incentive plan risk assessment was performed. The Company has reviewed its compensation policies and practices and concluded that they are not reasonably likely to have a material adverse effect on the registrant.

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**Board of Directors Leadership Structure**

The Board elected Timothy W. Sullivan as non-executive Chairman of the Board on April 9, 2013. This position is independent from management. Prior to Mr. Sullivan's election, the Company's Board had not elected any of its members as Chairman of the Board (executive or non-executive). Mr. Sullivan has served as a Class II director of the Company since 2012. The non-executive Chairman of the Board sets the agendas for and presides over the Board meetings as well as meetings of the independent directors. In connection with Mr. Sullivan's appointment, the Board eliminated the position of Lead Director, which had been held by Timothy Walsh from the time of the Company's initial public offering until Mr. Sullivan's election as independent non-executive Chairman of the Board. The Company's President and Chief Executive Officer, Aaron Jagdfeld, also serves as a member of the Board. The Board believes that this leadership structure is appropriate because it helps to promote greater communication between management and the directors. It also increases the directors' understanding of management decisions and Company operations and provides an additional layer of independent oversight of the Company.

Stockholders and other parties interested in communicating directly with Mr. Sullivan as non-executive Chairman of the Board may do so by writing to Mr. Sullivan, c/o Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189. Additionally, stockholders and other parties interested in communicating directly with any other independent members of the Board, whether individually or as a group, may do so by writing to that director(s) or the Board of Directors, respectively, c/o Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189.

**Attendance at Meetings**

It is our policy that each director is expected to dedicate sufficient time to the performance of his or her duties as a director, including by attending meetings of the stockholders, Board of Directors and committees of which he or she is a member. All of the then members of the Board of Directors attended our 2012 Annual Meeting of Stockholders.

In 2012, the Board of Directors held seven (7) meetings (including regularly scheduled and special meetings) and took action by unanimous written consent from time to time. All incumbent directors attended at least 75% of (i) the total number of meetings of the Board of Directors (held during the period for which he has been a director); and (ii) the total number of meetings held by all committees on which he served (during the periods that he served).

**Stockholder Communications with the Board of Directors**

Stockholders and other parties interested in communicating directly with the Board of Directors as a group may do so by writing to the Board of Directors, c/o Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189. The Secretary will review all correspondence and regularly forward to the Board of Directors all such correspondence that, in the opinion of the Secretary, deals with the functions of the Board of Directors or committees thereof or that the Secretary otherwise determines requires attention. Concerns relating to accounting, internal controls or auditing matters will immediately be brought to the attention of the Chairman of the Audit Committee. We have adopted a Whistleblower Policy, which establishes procedures for submitting these types of concerns, either personally or anonymously through a toll free telephone "hotline" or web transmission operated by an independent party. Our Whistleblower Policy can be found on the Company's website at [www.generac.com](http://www.generac.com).

Stockholders and other parties interested in communicating directly with Mr. Barry J. Goldstein, as Chairman of the Audit Committee, may do so by writing to Mr. Goldstein, c/o Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189.

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**Code of Ethics and Business Conduct**

We have adopted a Code of Ethics and Business Conduct (the "*Code*"), that applies to all of our directors, officers and employees, including our principal executive officer and principal financial accounting officer. The Code is posted on our website at [www.generac.com](http://www.generac.com). Any amendments to, or waivers under, our Code which are required to be disclosed by the rules promulgated by the SEC will be disclosed on the Company's website at [www.generac.com](http://www.generac.com).

**Corporate Governance Guidelines and Principles**

We have adopted Corporate Governance Guidelines and Principles. These guidelines outline the role of our Board of Directors, the composition and operating principles of our Board of Directors and its committees and our Board of Directors' working process. Our Corporate Governance Guidelines and Principles are posted on our website at [www.generac.com](http://www.generac.com).

**Section 16(a) Beneficial Ownership Reporting Compliance**

Based upon a review of our records, all reports required to be filed pursuant to Section 16(a) of the Securities Exchange Act of 1934 were filed on a timely basis with the one exception of one Form 4 which was inadvertently filed late by each of Terrence Dolan, Aaron Jagdfeld, Roger Pascavis and York Ragen on February 19, 2013 and, in the case of Allen Gillette, two Forms 4 filed on December 7, 2012 and February 19, 2013, respectively.

**Compensation Committee Interlocks and Insider Participation**

The members of our Compensation Committee are Messrs. Timothy Walsh, John D. Bowlin and Timothy W. Sullivan. No member of the Compensation Committee was, during 2012 or previously, an officer or employee of Generac or its subsidiaries. In addition, during 2012, there were no compensation committee interlocks required to be disclosed.

Table of Contents**BENEFICIAL OWNERSHIP OF OUR COMMON STOCK**

The following table shows information regarding the beneficial ownership of our common stock by:

each person or group who is known by us to own beneficially more than 5% of our common stock;

each member of our Board of Directors and each of our named executive officers; and

all members of our Board of Directors and our executive officers as a group.

Beneficial ownership of shares is determined under rules of the SEC and generally includes any shares over which a person exercises sole or shared voting or investment power. Except as noted by footnote, and subject to community property laws where applicable, we believe based on the information provided to us that the persons and entities named in the table below have sole voting and investment power with respect to all shares of our common stock shown as beneficially owned by them.

Except as noted by footnote, all stockholdings are as of April 23, 2013 and the percentage of beneficial ownership is based on 68,398,269 shares of common stock outstanding as of April 23, 2013. Unless otherwise indicated, the address for each holder listed below is c/o Generac Holdings Inc., S45 W29290 Hwy. 59, Waukesha, Wisconsin 53189.

<b>Name and address of beneficial owner</b>	<b>Number of shares</b>	<b>Percentage of shares</b>
<b>Principal stockholders</b>		
CCMP Capital, LLC(1)	23,512,998	34.4%
Baron Capital Group, Inc.(2)	4,681,331	6.8%
<b>Directors and Named Executive Officers(3)</b>		
Aaron Jagdfeld	1,219,872	1.8%
York A. Ragen	134,480	0.2%
Dawn Tabat	585,581	0.9%
Terry Dolan	45,778	0.1%
Russ Minick	51,083	0.1%
John D. Bowlin	69,823	0.1%
Robert Dixon	3,960	*
Barry J. Goldstein	25,404	*
Stephen Murray(1)	23,512,998	34.4%
Timothy Walsh(1)	23,512,998	34.4%
David Ramon	19,287	*

(B) The total number of stock options granted in fiscal 2003 by the Company was 8,467,558, to approximately 1,195 employees.

(C) These assumed rates of appreciation are provided in order to comply with requirements of the Securities and Exchange Commission and do not represent the Company's expectation as to the actual rate of appreciation of the Common Stock. The actual value of the options will depend on the performance of the Common Stock and may be greater or less than the amounts shown.

**Exercise of Stock Options**

The following table sets forth information concerning the exercise of stock options during fiscal 2003 by each of the Named Executive Officers and the fiscal year-end value of unexercised options.

**Aggregated Option/SAR Exercises in Last Fiscal Year and**

**Fiscal Year-End Option/SAR Values**

Name	Shares		Number of Securities Underlying Unexercised Options/SARs at	Value of Unexercised In-the-Money Options/SARs at FY-End(\$)
	Acquired on Exercise (#)	Value Realized (\$ (A))	FY-End (#)	
			Exercisable/ Unexercisable	Exercisable/ Unexercisable
James D. Sinegal	90,000	1,503,900	1,140,000/460,000	13,815,620/276,000
Jeffrey H. Brotman	90,000	2,031,300	1,140,000/460,000	13,815,620/276,000
Richard D. DiCerchio	0	0	312,000/276,000	2,257,500/165,600
Richard A. Galanti	0	0	530,000/230,000	6,608,750/138,000
Franz E. Lazarus	20,000	266,500	110,000/230,000	0/138,000
Dennis R. Zook	40,000	721,700	210,000/230,000	937,500/138,000

(A) Market value of underlying securities at the exercise date, minus the exercise price of such options.

### **Compensation of Directors**

Each non-employee director of the Company earns \$30,000 per year for serving on the Board, \$1,000 for each Board meeting and \$500 for each committee meeting attended. In addition, non-employee directors receive an annual grant of options to purchase 12,000 shares of common stock and are reimbursed for travel expenses incurred in connection with the performance of their duties as directors.

Richard M. Libenson has been engaged as a consultant to the Company. For such services, a corporation owned by Mr. Libenson was paid \$300,000 during fiscal 2003. In addition, the Company paid premiums in the amount of \$2,813 during fiscal 2003 for term life insurance for the benefit of Mr. Libenson under a split-dollar endorsement plan and premiums on long-term disability insurance in the amount of \$6,527. These transactions were reviewed and approved by the Audit Committee.

### **Compensation Committee Interlocks and Insider Participation**

No member of the Compensation Committee is an executive officer or former officer of the Company. In addition, no executive officer of the Company served on the board of directors of any entity whose executive officers included a director of the Company.

### **Report of Compensation Committee**

The Compensation Committee of the Board of Directors of the Company (the Committee) determined and administered the compensation of the Company's executive officers during fiscal 2003.

*Compensation Philosophy.* The Committee endeavored to ensure that the compensation programs for executive officers of the Company during fiscal 2003 were effective in attracting and retaining key executives responsible for the success of the Company and in promoting its long-term interests and those of its shareholders. The Committee sought to align total compensation for senior management with corporate performance and the interests of the shareholders. The Committee placed emphasis on variable, performance-based components, such as stock option awards and bonuses, the value of which could increase or decrease to reflect changes in corporate and individual performances. These short-term and long-term incentive compensation programs were intended to reinforce management's commitment to enhancement of profitability and shareholder value.

The Committee took into account various qualitative and quantitative indicators of corporate and individual performance in determining the level and composition of compensation for the Company's executive officers during fiscal 2003. While the Committee considered such corporate performance measures as net income, earnings per common share, stock price performance, comparable warehouse sales, margins and rate of revenue increase, the Committee did not apply any specific quantitative formula in making compensation decisions. The Committee also recognized qualitative factors, such as the ability to meet annual corporate growth and profits goals, demonstrated leadership ability and enhancement of customer franchise.

Base salaries for the executive officers were established at levels considered appropriate in light of the duties and scope of responsibilities of each officer's position and the salaries paid to comparable officers by companies which are competitors of the Company. Salaries are reviewed periodically and adjusted as warranted to reflect sustained individual officer performance. The



Committee focused primarily on total annual compensation, including incentive awards, rather than base salary alone, as the appropriate measure of executive officer

performance and contribution. The Committee believes that it has established relatively low cash compensation levels in favor of equity-linked incentive programs.

From time to time, executive officers have been eligible to receive incentive compensation awards under the Company's annual bonus plan and stock option plan, based upon corporate and individual performance. In approving grants and awards under the bonus plan and the option plan, the Committee considered the quantitative and qualitative factors and industry comparisons outlined above. The factors taken into account in determining awards under the bonus plan were the corporate performance measures described above.

In general, awards under the option plan are approved at various times throughout the year. The number of options previously awarded to and held by executive officers was reviewed but was not a determinative factor in the size of 2003 option grants.

In general, compensation payments in excess of \$1 million to any of the Named Executive Officers are subject to a limitation on deductibility for the Company under Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code). However, certain performance-based compensation is not subject to such limitation. The Company's stock option plan currently qualifies for such performance-based exception.

*Chief Executive Officer Compensation.* In evaluating the compensation of James D. Sinegal, President and Chief Executive Officer of the Company for fiscal 2003, the Committee placed emphasis on Mr. Sinegal's superior leadership in managing the business, as well as the Company's financial and operating performance.

The Committee noted that Mr. Sinegal voluntarily requested to forego his bonus for this year (as he did last year and the year before) and that the salary for Mr. Sinegal has not increased in three years. In light of these facts, the contributions he has made this year, the compensation of his peers, and the performance of the Company, the Committee believes that he is underpaid. Accordingly, his compensation levels for fiscal 2003 are fair to the Company.

Hamilton E. James

Jill S. Ruckelshaus

Charles T. Munger

Benjamin S. Carson, Sr., M.D.

**Performance Graph**

The following graph compares the cumulative total shareholder return (stock price appreciation plus dividends) on the Common Stock with the cumulative total return of the S&P 500 Index and the following group of peer companies (based on weighted market capitalization) selected by the Company: BJ's Wholesale Club Inc.; The Home Depot, Inc.; Lowe's Companies; Albertson's, Inc.; Nordstrom Inc.; Office Depot, Inc.; Staples Inc.; Target Corporation; Toys R Us Inc.; and Wal-Mart Stores, Inc. The information provided is from September 1, 1998 through August 31, 2003, the end of fiscal 2003.

**COMPARED CUMULATIVE TOTAL RETURN**

**AMONG COSTCO WHOLESALE CORPORATION,**

**S&P 500 INDEX AND PEER GROUP INDEX**

**ASSUMES \$100 INVESTED ON SEPT. 1, 1998**

**FISCAL YEAR ENDING AUG. 31, 2003**

**Certain Relationships and Transactions**

John W. Meisenbach is a principal shareholder of MCM, A Meisenbach Company. MCM provided consulting and brokerage services in managing the Company's employee benefit and member insurance programs. Employee medical, life and disability benefits, together with member health, auto and homeowner insurance premiums, totaled nearly \$552 million. For these services, MCM received total compensation from third-party insurers of \$1,633,857 in fiscal 2003.

Richard D. DiCerchio's son and brothers-in-law were employed by the Company during fiscal year 2003 at annual salaries of \$75,102, \$170,823 and \$84,115, respectively. Richard M. Libenson's daughter was employed by the Company during fiscal year 2003 at an annual salary of \$78,444. James D. Sinegal's son and brother-in-law were employed by the Company during fiscal year 2003 at annual salaries of \$215,120, and \$190,001, respectively. No family members of executive officers or directors are executive officers of the Company.

The foregoing relationships and transactions were reviewed and approved by the Audit Committee.

**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Under SEC rules, the Company's directors, executive officers and beneficial owners of more than 10% of the Company's equity security are required to file periodic reports of their ownership, and changes in that ownership, with the SEC. Based solely on its review of copies of these reports and representations of such reporting persons, the Company believes during fiscal 2003, such SEC filing requirements were satisfied, except that Mr. DiCerchio filed late Forms 4 reporting two transactions and each remaining director and executive officer filed a late Form 4 reporting a single transaction.

**Report of the Audit Committee**

November 15, 2003

To the Board of Directors of Costco Wholesale Corporation:

We have reviewed and discussed with management the Company's audited consolidated financial statements as of and for the fiscal year ended August 31, 2003.

We have discussed with the independent auditors the matters required to be discussed by Statement on Auditing Standards No. 61, *Communication with Audit Committees*, as amended, by the Auditing Standards Board of the American Institute of Certified Public Accountants.

We have received and reviewed the written disclosures and the letter from the independent auditors required by Independence Standard No. 1, *Independence Discussions with Audit Committees*, as amended, by the Independence Standards Board, and have discussed with the auditors the auditors' independence.

Based on the reviews and discussions referred to above, we recommend to the Board of Directors that the consolidated financial statements referred to above be included in the Company's Annual Report on Form 10-K for the fiscal year ended August 31, 2003.

Hamilton E. James

Charles T. Munger

Jill S. Ruckelshaus

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**Code of Ethics for Senior Financial Officers**

The Board of Directors has adopted a Code of Ethics for Senior Financial Officers. A copy of the Code of Ethics may be obtained at no charge by written request to the Company's secretary.

**INDEPENDENT PUBLIC ACCOUNTANTS**

**Information Regarding our Independent Auditors**

KPMG LLP ( KPMG ) has served as our independent auditors since May 13, 2002. Upon recommendation of its Audit Committee, our Board of Directors has appointed KPMG as our independent auditors for the fiscal year ending August 29, 2004.

**Services and Fees of KPMG**

The following table presents fees for services rendered by KPMG for fiscal 2003.

Audit fees	\$ 791,281
Audit-related fees	128,444
Tax	552,712
All other fees	22,861
Total	<u>\$ 1,495,298</u>

KPMG has been approved by the Audit Committee to perform the following non-audit services during fiscal 2004:

Ongoing expatriate tax advisory and compliance work.

Periodic tax consultations and compliance services in various local, regional and national tax jurisdictions.

Security reviews concerning web sites.

Transfer pricing studies.

**Audit Committee Preapproval Policy**

All services to be performed for the Company by KPMG must be preapproved by the Audit Committee or a designated member of the Audit Committee. The Audit Committee Preapproval Policy is attached as Appendix B.

### **Annual Independence Determination**

The Audit Committee has determined that the provision by KPMG of non-audit services to the Company in fiscal 2003 is compatible with KPMG's maintaining its independence.

### **PROPOSAL 2: SHAREHOLDER PROPOSAL RELATING TO ANNUAL ELECTIONS OF DIRECTORS**

Walden Asset Management, 40 Court Street, Boston, Massachusetts 02108, owner of 230,000 shares of Common Stock, has given notice that it intends to present the following proposal for action at the Annual Meeting:

The stockholders request that the Board of Directors take the steps necessary to declassify the election of Directors by insuring that in future Board elections directors are elected annually and not by classes as is now provided. The declassification shall be phased in so that it does not effect the unexpired terms of Directors previously elected.

### **Supporting Statement**

This proposal requests the Board end the present staggered board system and instead insure that all Directors are elected annually. Presently our company has 3 classes of Directors, 1/3 elected each year and each Director serves a 3-year term.

However, we believe shareholders should have the opportunity to vote on the performance of the entire Board each year.

Increasingly, institutional investors are calling for the end of this system, believing it makes a Board less accountable to shareholders when directors do not stand for annual election.

Significant institutional investors such as California's Public Employees Retirement System, New York City pension funds, New York State pension funds and many others support this position. Shareholder proposals to end this staggered system of voting have received increasingly large votes, averaging over 60% in 2002. In 2003, a majority of the proposals asking for this reform received votes over 50%. Numerous companies have also demonstrated leadership by changing this practice.

We do not believe this reform would destabilize our Company or affect the continuity of Director service, in any way. Our Directors, like the Directors of the overwhelming majority of other public companies, are routinely elected with strong overall shareholder approval.

We strongly believe that our company's financial performance is linked to its corporate governance policies and procedures and the level of management accountability they impose.

Therefore, as shareholders concerned about the value of our investment, we're concerned about our Company's current system of electing only one-third of the board of directors each year. We believe this staggering of Director terms prevents shareholders from annually registering their views on the performance of the board collectively and each director individually.

A recent study found that firms with the strongest shareholder rights significantly outperform companies with weaker shareholder rights. A 2001 study of 1,500 firms conducted by researchers at Harvard University and the University of Pennsylvania's Wharton School found a significant positive relationship between greater shareholder rights, including annual election of Directors as measured by a governance index, and both firm valuation and performance from 1990 to 1999.

In addition we believe the Board should be accountable for our company's record on social and environmental issues at each shareholder's meeting which also necessitates an annual election of Directors.

Most alarming, a staggered board can help insulate directors and senior executives from the consequences of poor financial performance by denying shareholders the opportunity to challenge an entire Board which is pursuing failed policies, or not allowing for members of an Audit Committee to be held annually accountable for their performance.

Please vote for this important governance reform or your vote will be automatically cast against it by Management.

#### **Board of Directors Response**

Your Board of Directors has given this proposal careful consideration and believes that it should not be implemented. The Board therefore recommends a vote AGAINST Proposal 2 for the following reasons:

Under the classified board structure, board members are elected to three-year terms, such that generally every year only one-third of the directors are considered for election or re-election. The Company has had this structure continuously since it went public in 1985. The Company believes that roughly half of the 100 largest corporations in the United States have classified boards and that the percentage of the Standard & Poor's 500 that have classified boards is even higher.



Your Board believes that a classified board can promote enhanced continuity and stability in the Board's business strategies and policies. With a classified board, two-thirds of the directors will have had prior experience and familiarity with the Company's business, which is beneficial for long-term strategic planning. At the same time, our shareholders have an opportunity each year to vote on several directors and to shape the decision-making of the Board accordingly.

The Board further believes that annual elections for each director are not necessary to promote accountability. The Board has not seen any evidence that three-year terms have led to less accountability in the past. Directors' fiduciary duties to shareholders do not vary with the length of the directors' terms. In addition, the Company's bylaws provide the shareholders with the power to call meetings to remove directors for cause.

Your Board of Directors also believes that a classified board is potentially an important tool for resisting a takeover of the Company not supported by the Board, since a majority of the Board cannot be replaced at a single annual meeting. The Board believes that this will encourage those interested in business combinations to negotiate with the Board, enhancing the ability of the Board to achieve more beneficial terms for shareholders.

Approval by the shareholders of Proposal 2 will not itself declassify the Board of Directors. Declassification can be accomplished only through an amendment of the Company's articles of incorporation, which would require a two-thirds vote of all shares outstanding that are entitled to vote. In addition, under Washington law, the Board could propose such an amendment to the shareholders only if the Board recommends the proposed amendment, unless special circumstances exist. At present, the Board would not recommend such an amendment, and the Board has been advised that no special circumstances exist now that would permit proposing an amendment that the Board does not recommend. The Board will carefully consider the results of the vote of the shareholders on this proposal. Under Washington law an affirmative vote of even a majority of the shares present and voting would not necessarily permit the Board to propose an amendment to the articles of incorporation unless the Board were to change its view as to the advisability of such an amendment.

For the foregoing reasons, your Board of Directors unanimously believes that this proposal is not in the best interests of the Company and its shareholders and recommends that you vote AGAINST Proposal 2. Proxies solicited by the Board of Directors will be voted AGAINST this proposal unless a shareholder has indicated otherwise in voting the proxy.

### **PROPOSAL 3: SHAREHOLDER PROPOSAL RELATING TO A LAND PROCUREMENT POLICY**

Christian Brothers Investment Services, Inc., 90 Park Avenue, New York, New York 10016, owner of 35,900 shares of Common Stock, and Allan and Jane Paulson, owners of 1,000 shares of Common Stock, have given notice that they intend to present the following proposal for action at the Annual Meeting:

In 2001, Costco and a Mexican partner, Comercial Mexicana, purchased public land in Cuernavaca, Mexico. The plan to build two megastores there provoked strong community opposition because the site contained what we believe to be an architecturally significant hotel, the Casino de la Selva, that had long been an artistic center and contained what we believe to be renowned murals. Residents were also concerned about the loss of the hotel's wooded grounds, the presence of pre-Columbian artifacts at the site, and the project's impact on traffic.

Thousands of Cuernavacans demonstrated against the project in 2001.

At one demonstration, peaceful protestors were beaten and arrested. A Mexican Human Rights Commission stated: It was demonstrated that members of the private security police employed by the Costco company, which was undertaking construction on the indicated establishment, also participated in the events suffered by Ignacio Rodriguez Oliveros. Amnesty International stated in its 2003 International Report: In August and October plans to develop an environmentally sensitive site, Casino de la Selva, in Cuernavaca, Morelos State, led to protesters being detained, allegedly with excessive use of force.

As Costco proceeded to demolish the hotel, a number of elected officials, academics, environmentalists, clergy and other public figures expressed opposition to the project.

A study by the International Ombudsman Centre for the Environment and Development, a respected, independent non-governmental organization, concluded that the destruction of the hotel was a cultural (and to a lesser extent, environmental) crime of great proportions .

One muralists who decorated the hotel filed a \$15 million suit against Costco for copyright infringement. Costco claims the murals are undergoing restoration, but has refused some of the artists access to them.

A federal lawsuit is pending in Mexico against the authorities who approved Costco s project.

Costco has also been involved in domestic land use controversies. In Cypress, California, city plans to use eminent domain powers to transfer church-owned land to Costco were criticized by observers. The Wall Street Journal called the use of eminent domain on behalf of a private business the worst form of political collusion. In Lancaster, California, residents contested for years a plan to transfer parkland to Costco.

We believe negative publicity surrounding these ventures has damaged Costco s reputation, endangering shareholder value.

We believe these controversies could have been avoided with proper due diligence.

Costco s Code of Ethics does not appear to provide guidance as to how to avoid future controversies like these.

The shareholders request the Board of Directors of Costco to develop a policy for land procurement and use that incorporates social and environmental factors. A report on this policy and its implementation shall be prepared at reasonable expense, omitting proprietary information, and made available to shareholders by July 1, 2004.

### **Supporting Statement**

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Our company asserts that it complies with all relevant laws and has made significant alterations to its original plans in Cuernavaca. The conflicts surrounding its California stores were eventually resolved. However, we believe significant damage to our company's reputation has been done. The policy requested should include guidelines to

ensure preservation of communities' cultural heritage and natural environment and respect for human rights;

consult with affected communities and maintain high ethical standards when working with governments and partners.

### **Board of Directors' Response**

The Board of Directors unanimously recommends voting against this proposal and believes that adopting a land procurement policy for the Company is not in the best interests of the Company or its shareholders. The Company's future expansion depends on its ability to secure and develop new sites in a timely and cost-effective manner. The competition for sites is keen, and the legal, regulatory, political, and environmental factors that impact site selection and development have become more complex.

The Board believes that the policy sought by the proposal would be harmful to the interests of shareholders. The Company's practices with respect to real estate already take into account social and environmental factors, among other things. The Company does so not only because of legal requirements but because it seeks to be a valuable addition to and partner with the communities in which it locates. As a membership club, the Company strives to develop the goodwill of present and future members, and that includes being sensitive to the impacts of the warehouses. In addition, public interests are represented in these processes through a variety of means, including the participation of elected representatives, publicly employed development professionals, and concerned citizens. The Company's successful track record over decades of successful site development shows that it has capably balanced the competing interests involved in real estate development. It has always operated and will continue to operate under high ethical standards. To the extent that the proposal is proffered to avoid future controversies in land procurement, the Company believes it will not be effective. In the Company's experience, nearly every site involves some degree of controversy among competing interests, and the development of a one size fits all policy will not eliminate controversies. Finally, the Board believes that adoption of the policy sought could be counterproductive. Such a policy could be used by those opposed to the interests of the Company, including competitors, to stifle or delay the Company's efforts to acquire and develop sites.

*Background Concerning Cuernavaca.* The Supporting Statement focuses mainly on a development in Cuernavaca, Mexico. The site was formerly home to the Casino de la Selva, a hotel built in the 1930's. The hotel catered to an exclusive clientele and at no time in its history was it ever a park or a public space. It is doubtful that the average Cuernavacan ever had access to the property for any social or cultural reasons. The hotel went out of business and was closed in the early 1990's. From the time of its closure, the entire property, which was surrounded by a large wall, was closed to the public save for one occasion when the grounds were used to host a floral festival. The buildings and facilities were abandoned and left exposed to the weather. As a result, the grounds became overgrown and unkempt, and virtually every building on the property fell into a state of extreme disrepair. Following the hotel's closure, the owners defaulted on their tax obligations to the Mexican government and the property (along with several other of the owner's properties) was given to the Mexican government in lieu of foreclosure. As required by Mexican law, following its acquisition by the Mexican tax authorities, the property was sold by the Fidecomiso Liquidador de Instituciones y Organizaciones Auxiliares de Credito (FIDELIQ), an agency of the Mexican federal government charged with liquidation of seized and foreclosed assets. Having acquired the property through a tax default, FIDELIQ was required to sell the property through public auction and had no discretion to convert the property to a park or other public use. Costco Mexico purchased the property in 2001 at a public auction in which it was the successful bidder. The Company has no knowledge that any improper payments were made in connection with the acquisition or development of the property, and no party has presented any evidence of such payments.

*Architectural and Artistic Issues.* Although most significant works of art in Mexico have been registered as national patrimony or treasures and thus are subject to government restrictions to ensure preservation, none of the buildings or artwork abandoned at the Casino de La Selva, including the murals, were ever so registered with the Mexican government. The only building on the site that might be said to be of architectural significance was the theater building designed by Felix Candela, in his parabolic style. The techniques used to construct the vaulted concrete ceilings of this building have proven to be less than durable, and many of the buildings Candela designed throughout Mexico have been demolished due to construction and design deficiencies. At the time that Costco Mexico acquired the Cuernavaca property, it discussed with the government the possibility of preserving the Candela building and other

structures located on the site. It was determined, however, that the building, which had been left open and exposed to the elements for many years, was unsafe and beyond repair (as was the case with virtually all of the structures left on the property). Instead, it was agreed that a reproduction of the building in the exact form of Candela's design would be constructed using appropriate materials and construction techniques. This building has now been completed and is operating as a restaurant on the site.

With respect to the murals, at no time during the period following closure of the hotel in the early 1990's did the mural artists, private citizens or any government agency register the murals as artistically significant, even though such a procedure exists under Mexican law, or otherwise make any effort to preserve or salvage the murals. At the time construction began, the murals were crumbling and in poor condition as a result of the neglect of the hotel buildings. Costco Mexico decided to preserve these murals and offered them to the local government, which declined due to the cost of restoration. Not wanting to see the murals destroyed, Costco Mexico agreed to fund the removal and restoration of the murals by the Mexican National Institute of Fine Arts and Literature (INBA). All of the murals are now at INBA's facilities in Mexico City, where they are undergoing restoration. Costco Mexico is now being sued by one of the mural artists not for destroying the murals, but for restoring and saving them, claiming that such restoration work violates the artist's copyright. This lawsuit is currently pending; Costco Mexico believes it to be without merit. Access to the murals has been offered to at least one artist involved in the creation of the murals. Once restoration is completed, the murals will be displayed at a museum and cultural facility currently being constructed by Costco Mexico on the property once occupied by the hotel. Named Centro Cultural Parque Morelos, the facility will cost over \$3.5 million. That facility will also display the internationally renowned Jacques and Natasha Gelman Collection of Mexican Art, which includes works by Frida Kahlo, Diego Rivera and Rufino Tamayo.

*Human Rights Issues.* When construction began at the site, a small group of protestors initiated a series of demonstrations outside the property protesting the development of the commercial center on the property. In August 2002, a group of these demonstrators blocked the public roads in front of the property causing disruption of traffic and approximately eighteen protestors were arrested by the Mexican police. At no time did Costco Mexico's security personnel, employees or other agents abuse or in any way interfere with these protestors. The cited Amnesty International report did nothing more than note allegations of excessive force by unspecified persons. The entire statement concerning Cuernavaca in the cited Amnesty International report is as follows: In August and October plans to develop an environmentally sensitive site, Casino de la Selva, in Cuernavaca, Morelos State, led to protestors being detained, allegedly with excessive use of force.

*Environmental Issues.* As a condition to its development of the property, Costco Mexico was required to fund an extensive archeological survey of the property that was conducted by the National Institute of Anthropology and History (INAH), an agency of the Mexican federal government. The archeological survey took approximately three months and the final report issued by the INAH concluded that there were no items of archeological significance on the property.

In gaining approval of the proposed development plans, the project went through an exhaustive environmental review conducted by various agencies of the Mexican government. Once the review was complete, the results were presented to a twenty-four-member panel that represented pertinent federal, state and local government agencies, as well as Cuernavaca neighborhood groups and associations and local citizen interest groups. Twenty-three panel members voted in favor of the development. Before beginning construction, the company worked closely with the Mexican Department of Ecology to conduct a comprehensive survey of

every tree on the property. Thereafter, in accordance with the requirements dictated by the Department of Ecology, of the total of 353 trees located on the property, the majority were incorporated into the site design and preserved in place or relocated on site. With additional trees planted during construction, the total on site tree count is now approximately 650. In addition, in accordance with governmental regulations, Costco Mexico donated an additional 30,000 trees to the city of Cuernavaca, for the city to plant at locations of its own choosing.

The Board of Directors unanimously recommends a vote AGAINST Proposal 3 for the reasons described above. Proxies solicited by the Board of Directors will be voted AGAINST this proposal unless a shareholder has indicated otherwise in voting the proxy.

**PROPOSAL 4:**

**INDEPENDENT PUBLIC ACCOUNTANTS AND ANNUAL REPORT**

Subject to ratification by the shareholders at the Annual Meeting, the Audit Committee has selected KPMG to audit the consolidated financial statements of the Company and its subsidiaries for the fiscal year ending August 29, 2004. KPMG has issued its report, included in the Company's Form 10-K, on the audited consolidated financial statements of the Company for the fiscal year ending August 31, 2003. KPMG has served the Company in this capacity since May 13, 2002. Representatives of KPMG are expected to be present at the Annual Meeting, will have the opportunity to make a statement, if they desire to do so, and will be available to respond to appropriate questions.

The affirmative vote of a majority of the votes cast on this proposal shall constitute ratification of the appointment of KPMG.

The Board of Directors unanimously recommends a vote FOR the ratification of the selection of the independent auditors.

## OTHER MATTERS

Neither the Board of Directors nor management intends to bring before the meeting any business other than the matters referred to in the Notice of Meeting and this Proxy Statement. If any other business should properly come before the meeting, or any adjournment thereof, the persons named in the proxy will vote on such matters according to their best judgment.

## SHAREHOLDER PROPOSALS FOR 2005 ANNUAL MEETING

In order for a shareholder proposal to be included in the proxy statement for the 2005 annual meeting of shareholders, it must be received by the Company no later than August 18, 2004. Proposals may be mailed to the Company, to the attention of the Secretary, 999 Lake Drive, Issaquah, Washington 98027.

A shareholder who intends to present a proposal at the Company's annual meeting in 2005, other than pursuant to Rule 14a-8 under the Securities Exchange Act of 1934, must provide the Company notice of such intention by at least November 2, 2004, or management of the Company will have discretionary voting authority at the 2005 annual meeting with respect to any such proposal without discussion of the matter in the Company's proxy statement.

**A copy of the Company's annual report on Form 10-K filed with the Securities and Exchange Commission will be provided to shareholders without charge upon written request directed to Investor Relations. The Company makes available free of charge its Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to such reports filed pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after filing on or through our website at [http://media.corporate-ir.net/media\\_files/nsd/cost/irhome1.htm](http://media.corporate-ir.net/media_files/nsd/cost/irhome1.htm).**

By order of the Board of Directors,

Joel Benoliel

*Secretary*



**APPENDIX A**

**COSTCO WHOLESALE CORPORATION**

**AUDIT COMMITTEE CHARTER**

**REVISED AS OF SEPTEMBER 30, 2003**

The Costco Wholesale Corporation Audit Committee ( Committee ) shall be nominated and elected by the Board of Directors each year at the meeting of the Board of Directors held in conjunction with the Company s Annual Meeting of Shareholders.

The Audit Committee will be composed of from three to five directors, each of whom must in the judgment of the Board be independent as defined by the rules of the Securities and Exchange Commission ( SEC ). At least one member of the Committee shall in the judgment of the Board be an audit committee financial expert as defined by the SEC. Each member of the Committee shall meet the financial literacy and other applicable requirements of the NASDAQ Stock Market listing standards. Other personnel may attend meetings of the Committee at the invitation of the Committee or its Chairman.

The Committee is charged by the Board of Directors with the responsibility to:

1. Appoint and provide for the compensation of the Company s independent auditor, oversee the work of the independent auditor (including resolution of any disagreements between management and the independent auditor regarding financial reporting), evaluate the performance of the independent auditor and, if so determined by the Committee, replace the independent auditor; it being acknowledged that the independent auditor is ultimately accountable to the Board and the Committee, as representatives of the stockholders.
2. Ensure the receipt of, and evaluate the written disclosures and the letter that the independent auditor submits to the Committee regarding the auditor s independence in accordance with Independence Standards Board Standard No. 1, discuss such reports with the auditor, oversee the independence of the independent auditor and, if so determined by the Committee in response to such reports, take appropriate action to address issues raised by such evaluation.
3. Approve as required by law all professional services to be provided to the Company by its independent auditor, provided that the Committee shall not approve any non-audit services proscribed by section 10A(g) of the Exchange Act in the absence of an applicable exemption. The Committee may adopt policies and procedures for the approval of such services that may include delegation of authority to a designated member or members of the Committee to approve such services so long as any such approvals are disclosed to the full Committee at its next scheduled meeting.
4. Review and approve all related-party transactions that are required to be disclosed under SEC Regulation SK 404(a).

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5. Discuss with the independent auditor the matters required to be discussed by SAS 61, as it may be modified or supplemented.
  
6. Instruct the independent auditor and the internal auditor to advise the Committee if there are any subjects that require special attention.
  
7. Instruct the independent auditor to report to the Committee on all critical accounting policies of the Company, all alternative treatments of financial information within generally accepted accounting principles that have been discussed with management and involve

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material items or critical accounting policies, ramifications of the use of such alternative disclosures and treatments and the treatment preferred by the auditors, and other material written communication between the auditors and management.

8. Meet with management and the independent auditor to discuss the annual financial statements and the report of the independent auditor, and to discuss significant issues encountered in the course of the audit work, including: restrictions on the scope of activities; access to required information; the adequacy of internal financial controls; the adequacy of the disclosure of off-balance sheet transactions, arrangements, obligations and relationships in reports filed with the SEC; and the appropriateness of the presentation of any non-GAAP financial measures included in any report filed with the SEC or in any public disclosure or release.
9. Review the management letter delivered by the independent auditor in connection with the audit.
10. Following such review and discussions, if so determined by the Committee, recommend to the Board that the annual financial statements be included in the Company's annual report.
11. Meet quarterly with management and the independent auditor to discuss the quarterly earnings release and quarterly financial statements prior to the filing of the Form 10-Q; provided that this responsibility may be delegated to the chairman of the Committee or a member of the Committee who is an audit committee financial expert.
12. Meet as deemed appropriate by the Committee in executive sessions with management, the internal auditor or the independent auditor to discuss matters that any of them or the Committee believes could significantly affect the financial statements and should be discussed in executive session.
13. Review significant changes to the Company's accounting principles and practices proposed by the independent auditor, the internal auditor or management.
14. Review the scope and results of internal audits.
15. Evaluate the performance of the internal auditor and, if so determined by the Committee, recommend replacement of the internal auditor.
16. Review and decide whether to grant any requests for waiver of the Company's Code of Ethics for Senior Financial Officers.
17. Maintain a procedure for receipt, retention and treatment of any complaints received by the Company about its accounting, internal accounting controls or auditing matters and for the confidential and anonymous submission by employees of concerns regarding questionable accounting or auditing matters.

18. Provide minutes of Committee meetings to the Board, and report to the Board on any significant matters arising from the Committee's work.
19. Evaluate the performance of the Committee, review and reassess this Charter and, if appropriate, recommend changes to the Board.
20. Prepare the Committee report required by the SEC to be included in the Company's annual proxy statement.
21. Conduct or authorize such inquiries into matters within the Committee's scope of responsibility as the Committee deems appropriate.

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Authority

By adopting this Charter, the Board delegates to the Committee full authority to:

1. Perform the responsibilities of the Committee described above.
2. Appoint a chair of the Committee, unless a chair is designated by the Board.
3. Engage independent counsel and other advisers as the Committee determines necessary to carry out its responsibilities.
4. Cause the officers of the corporation to provide such funding as the Committee shall determine to be appropriate for payment of compensation to the Company's independent auditor and any legal counsel or other advisers engaged by the Committee.
5. Obtain advice and assistance from internal legal or other advisors.

Such authority shall be exclusive to the Committee to the extent required by law, the SEC or the NASDAQ listing standards.

## APPENDIX B

### Audit Committee Preapproval Policy

#### I. STATEMENT OF PRINCIPLES

The Audit Committee is required to preapprove the audit and non-audit services performed by the independent auditor in order to assure that the provision of such services do not impair the auditor's independence. Unless a type of service to be provided by the independent auditor has received general preapproval, it will require specific preapproval by the Committee. Any proposed services exceeding preapproved cost levels will require specific preapproval by the Committee.

The appendices to this Policy describe the Audit, Audit-related, Tax and All Other services that have the preapproval of the Committee. The term of any preapproval is twelve months from the date of preapproval, unless the Committee specifically provides for a different period. The Committee will annually review and preapprove the services that may be provided by the independent auditor without obtaining specific preapproval from the Committee. The Committee will revise the list of general preapproved services from time to time, based on subsequent determinations. The Committee does not delegate its responsibilities to preapprove services performed by the independent auditor to management.

#### II. DELEGATION

The Committee has delegated interim preapproval authority to Jill Ruckelshaus. Interim preapprovals shall be reported to the Committee at its next scheduled meeting.

#### III. AUDIT SERVICES

The annual Audit services engagement terms and fees will be subject to the specific preapproval of the Committee. The Committee will approve, if necessary, any changes in terms, conditions and fees resulting from changes in audit scope, Company structure or other matters.

In addition to the annual Audit services engagement specifically approved by the Committee, the Committee may grant general preapproval for other Audit services, which are those services that only the independent auditor reasonably can provide. The Committee has preapproved the Audit services listed in Appendix A. All other Audit services not listed in Appendix A must be specifically preapproved by the Committee.

#### IV. AUDIT-RELATED SERVICES

Audit-related services are assurance and related services that are reasonably related to the performance of the audit or review of the Company's financial statements or that are traditionally performed by the independent auditor. The Committee believes that the provision of Audit-related services does not impair the independence of the auditor, and has preapproved the Audit-related services listed in Appendix B. All other Audit-related services not listed in Appendix B must be specifically preapproved by the Committee.

#### V. TAX SERVICES

The Committee believes that the independent auditor can provide certain Tax services to the Company, such as tax compliance, tax planning and tax advice, without impairing the auditor's independence. However, the Committee will not permit the retention of the independent auditor in connection with a transaction initially recommended by the independent

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(1) The Committee is also required to preapprove the provision of all audit services that may be provided, including provision by multiple auditors.

B-1

auditor, the purpose of which may be tax avoidance and the tax treatment of which may not be supported in the Internal Revenue Code and related regulations. The Committee has preapproved the Tax services listed in Appendix C. All Tax services involving large and complex transactions not listed in Appendix C must be specifically preapproved by the Committee.

#### VI. ALL OTHER SERVICES

The Committee may grant general preapproval to those permissible non-audit services classified as All Other services that it believes are routine and recurring services and would not impair the independence of the auditor. The Committee has preapproved the All Other services listed in Appendix D. Permissible All Other services not listed in Appendix D must be specifically preapproved by the Committee.

A list of the SEC's prohibited non-audit services is attached to this policy as Exhibit 1. The independent auditor shall not be engaged to perform any of these services. Questions about whether a proposed service is prohibited shall be referred to the Legal Department at Corporate.

#### VII. PREAPPROVAL FEE LEVELS

Preapproval fee levels for all services to be provided by the independent auditor will be established annually by the Committee. Any proposed services exceeding these levels will require specific preapproval by the Committee.

#### VIII. PROCEDURES

Requests or applications to provide services that require specific approval by the Committee will be submitted to the Committee by both the independent auditor and the Chief Financial Officer and must include a joint statement as to whether, in their view, the request or application is consistent with the SEC's rules on auditor independence.

#### **Exhibit 1**

#### **Prohibited Non-Audit Services**

Bookkeeping or other services related to the accounting records or financial statements of the audit client\*

Financial information systems design and implementation\*



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Appraisal or valuation services, fairness opinions or contribution-in-kind reports\*

Actuarial services\*

Internal audit outsourcing services\*

Management functions

Human resources

Broker-dealer, investment adviser or investment banking services

Legal services

Expert services unrelated to the audit

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\* Unless it is reasonable to conclude that the results of these services will not be subject to audit procedures during an audit of the Company's financial statements.

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**VOTE BY INTERNET [www.proxyvote.com](http://www.proxyvote.com)**

Use the Internet to transmit your voting instructions and for electronic delivery of information up until 11:59 P.M. Eastern Time on January 28, 2004. Have your proxy card in hand when you access the web site and follow the instructions to obtain your records and to create an electronic voting instruction form.

**VOTE BY PHONE 1-800-690-6903**

Use any touch-tone telephone to transmit your voting instructions up until 11:59 P.M. Eastern Time on January 28, 2004. Have your proxy card in hand when you call and then follow the instructions.

**VOTE BY MAIL**

Mark, sign and date your proxy card and return it in the postage-paid envelope we've provided or return to Costco Wholesale Corporation, c/o ADP, 51 Mercedes Way, Edgewood, NY 11717.

**COSTCO WHOLESALE CORPORATION**  
**999 LAKE DRIVE**  
**ISSAQUAH, WA 98027**

TO VOTE, MARK BLOCKS BELOW IN BLUE OR BLACK INK AS FOLLOWS:

COSTCO

KEEP THIS PORTION FOR YOUR RECORDS.

DETACH AND RETURN THIS PORTION ONLY

**THIS PROXY CARD IS VALID ONLY WHEN SIGNED AND DATED.**

**COSTCO WHOLESALE CORPORATION**

**THE BOARD RECOMMENDS A VOTE FOR ITEMS**

**1 AND 4 AND A VOTE AGAINST ITEMS 2 AND 3.**

	For	Withhold	For All	To withhold authority to vote, mark For All Except and write the nominee's number on the line below.
1. Election of Class II Directors:	All	All	Except	
01) Benjamin S. Carson				_____
02) Hamilton E. James	..	..	..	
03) Jill S. Ruckelshaus				
04) William H. Gates, II				
Election of Class I Director:				For      Against      Abstain
05) Daniel J. Evans				

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- |    |   |    |    |    |
|----|---|----|----|----|
| 2. | Shareholder proposal to elect directors annually and not by classes | .. | .. | .. |
| 3. | Shareholder proposal to develop a policy for land procurement       | .. | .. | .. |
| 4. | Ratification of selection of independent auditors.                  | .. | .. | .. |

For address changes and/or comments, please check this box and write them on the back where indicated.

..

Please sign as name(s) appear on this proxy, and date this proxy. If a joint account, each joint owner must sign. If signing for a corporation or partnership or as agent, attorney or fiduciary, indicate the capacity in which you are signing.

Signature [PLEASE SIGN WITHIN BOX]	Date	Signature (Joint Owners)	Date

**COSTCO WHOLESALE CORPORATION**

**Annual Meeting of Shareholders**

Thursday, January 29, 2004

10:00 a.m.

Meydenbauer Center

Center Hall B

11100 NE 6<sup>th</sup>

Bellevue, Washington 98004

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**PROXY**

**COSTCO WHOLESALE CORPORATION**

**999 Lake Drive, Issaquah, Washington 98027**

**PROXY FOR THE JANUARY 29, 2004 ANNUAL MEETING OF SHAREHOLDERS**

**This Proxy is Solicited By The Board of Directors of COSTCO WHOLESALE CORPORATION**

The undersigned shareholder of **COSTCO WHOLESALE CORPORATION** (the Company ) hereby appoints Jeffrey H. Brotman and James D. Sinegal, and each of them, the lawful attorneys and proxies of the undersigned, each with several powers of substitution, to vote all of the shares of Common Stock of the Company held of record by the undersigned on December 5, 2003 at the Annual Meeting of Shareholders to be held at the Meydenbauer Center, Center Hall B, 11100 NE 6<sup>th</sup>, Bellevue, Washington 98004, on Thursday, January 29, 2004 at 10:00 a.m., local time, and at any and all adjournments thereof, with all the powers the undersigned would possess if personally present, upon all matters set forth in the Notice of Annual Meeting of Shareholders and Proxy Statement dated December 17, 2003.

Shares represented by all properly executed proxies will be voted in accordance with instructions appearing on the proxy and, in the discretion of the proxy holders, as to any other matter that may properly come before the Annual Meeting of Shareholders. **IN THE ABSENCE OF SPECIFIC INSTRUCTIONS, PROXIES WILL BE VOTED FOR ITEMS 1 AND 4, AGAINST ITEMS 2 AND 3, AND IN THE DISCRETION OF THE PROXY HOLDERS AS TO ANY OTHER MATTER THAT MAY PROPERLY COME BEFORE THE ANNUAL MEETING OF SHAREHOLDERS.**

Address/Comments: \_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

(If you noted any address changes/comments above, please mark corresponding box on other side.)

*(Continued and to be signed and dated on the reverse side and returned promptly in the enclosed envelope)*

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