Securities Alert
SEC Proposes Rules for Say-on-Pay

October 25, 2010

On October 18, 2010, the Securities and Exchange Commission (SEC) published proposed rules to implement the shareholder advisory votes and related disclosures required pursuant to Section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). Specifically, the proposed rules would require public companies subject to the proxy rules to—

• provide shareholders with an advisory vote to approve executive compensation (“say-on-pay”) at least once every three years

• provide shareholders with an advisory vote to determine whether the say-on-pay vote occurs every one, two or three years (“say-on-frequency”)

• provide shareholders with an advisory vote to approve golden parachute compensation arrangements (“say-on-golden parachutes”) in connection with mergers and other similar corporate transactions.

In addition to the rules implementing these shareholder advisory votes, the SEC has proposed related amendments to certain proxy rules and disclosure requirements. And, in a separate release, the SEC proposed rules that would require institutional investment managers to report annually to the SEC their votes on say-on-pay, say-on-frequency and say-on-golden parachutes. The proposed rules are discussed in more detail below.

Comments on the proposed rules are due by November 18, 2010, and the SEC is expected to adopt final rules in early 2011. Issuers are required to provide the separate say-on-pay vote and say-on-frequency vote for the first annual or other such meeting of shareholders occurring on or after January 21, 2011, without regard to whether the proposed rules discussed in this alert have been adopted and become effective by that time. The proposed disclosures and shareholder vote relating to golden parachute compensation, however, will not be required until the final rules become effective.

SAY-ON-PAY

Say-on-Pay Resolution. The SEC has proposed a new Rule 14a-21(a) to address the say-on-pay vote, which requires public companies subject to the proxy rules to, at least once every three years, provide for a shareholder advisory vote to approve the compensation of the company’s named executive officers (NEOs), as such compensation is disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis (CD&A), the compensation tables and other narrative executive compensation disclosures required by Item 402. The proposed rule makes clear that the say-on-pay vote does not extend to disclosures under Item 402 relating to director compensation or risks relating to a company’s compensation policies and practices for employees generally. If, however, the company’s CD&A includes disclosure on risks relating to a company’s compensation policies and procedures for its NEOs, such disclosure would be captured by the say-on-pay vote.

This shareholder vote (as well as the say-on-frequency vote) is required only when proxies are solicited for an annual or other meeting of shareholders where SEC rules require executive compensation disclosure (such as shareholder meetings that involve the election of directors). Although the proposed rule does not provide specific language or the form of resolution to be voted on by shareholders, the SEC is seeking comment on whether it should include in the final rules the exact form of resolution.

1 The Dodd-Frank Act amended the Securities Exchange Act of 1934 (the “Exchange Act”) by adding a new Section 14A that requires the shareholder advisory votes.
Proxy Statement Disclosure. The SEC has proposed a new Item 24 to Schedule 14A that would require companies to disclose in their proxy statements that they are providing a separate say-on-pay vote and to briefly explain the general effect of the vote, such as whether the vote is nonbinding. This is similar to the approach the SEC took in connection with disclosure requirements about the shareholder vote on executive compensation for companies subject to the Emergency Economic Stabilization Act.

CD&A Disclosure. The SEC has proposed an amendment to Item 402(b) of Regulation S-K that would require companies to address in CD&A whether they have considered the results of previous shareholder say-on-pay votes in determining compensation policies and decisions and, if so, how that consideration has affected their compensation policies and decisions. This disclosure is designed to facilitate better investor understanding of the company’s compensation decisions.

Smaller Reporting Companies. Smaller reporting companies are not exempt from the shareholder advisory votes in the proposed rules. But because smaller reporting companies are subject to scaled executive compensation disclosure requirements and are not required to include a CD&A, the proposed rules make clear that such companies would not be required to include a CD&A to comply with the rules and that shareholders of such companies would, instead, vote to approve the compensation of the NEOs as disclosed under Items 402(m) through (q) of Regulation S-K.

SAY-ON-FREQUENCY

Say-on-Frequency Resolution. The SEC has proposed a new Rule 14a-21(b) to address the say-on-frequency vote, which requires public companies subject to the proxy rules to, at least once every six years, provide for a shareholder advisory vote as to whether the say-on-pay vote (discussed above) should occur every one, two or three years.

Proxy Statement Disclosure. Similar to the disclosure required for the say-on-pay vote, proposed Item 24 of Schedule 14A would require companies to disclose in their proxy statement that they are providing a separate say-on-frequency vote and to briefly explain the general effect of the vote, such as whether the vote is nonbinding.

Amendment to Form of Proxy. Rule 14a-4 currently requires the form of proxy to give shareholders a choice between approval or disapproval of, or abstention with respect to, matters to be acted upon at a shareholder meeting (other than the election of directors). The SEC has proposed to amend this rule to give shareholders four choices on the say-on-frequency vote: whether the say-on-pay vote will occur every one, two or three years, or to abstain from voting on the matter. The board of directors would be allowed to include its recommendation on how shareholders should vote on this matter, but the company must make clear that shareholders are not voting to approve or disapprove the board’s recommendation.

Form 10-K and Form 10-Q Disclosures. The SEC’s proposal would amend Item 9B of Form 10-K and add a new Item 5(c) of Form 10-Q that would require a company to disclose its decision on how frequently it will conduct say-on-pay votes in light of the results of the say-on-frequency vote. Such disclosure would need to be included in the Form 10-Q covering the period during which the say-on-frequency vote occurs or in the Form 10-K if the vote occurred during the fourth quarter. The SEC is not proposing to change Item 5.07 of Form 8-K, which requires companies to disclose the results of shareholder votes within four business days following the day of the shareholder meeting. A company may, however, provide additional disclosure in Item 5.07 regarding how the results of these shareholder votes affect the company’s plans for the future.

PROPOSED RULES THAT RELATE TO BOTH SAY-ON-PAY AND SAY-ON-FREQUENCY VOTES

Amendment to Rule 14a-8 Shareholder Proposals. The SEC has proposed to amend Rule 14a-8 to clarify the status of shareholder proposals that seek a shareholder advisory vote on executive compensation or that relate to the frequency of such votes. The proposed amendment would allow companies to exclude such shareholder proposals on the basis of having been substantially implemented, provided the company (1) has adopted a policy on the frequency of say-on-pay votes that is consistent with the plurality of votes cast in the most recent say-on-frequency vote and (2) provides a say-on-frequency vote at least once every six years as required under the proposed rules.

2 The SEC indicated that, even though the final rules have not yet been adopted, it would not object if a company’s form of proxy for the say-on-frequency vote provided shareholders an opportunity to specify a choice among one, two or three years, or abstention. Further, if proxy service providers are unable to accommodate these four choices, the SEC will not object if the form of proxy gives shareholders an opportunity to choose among one, two or three years, and proxies are not voted on the matter if the shareholder does not select one of the three choices.
Preliminary Proxy Statement Not Required. Rule 14a-6 would be amended to provide that inclusion of say-on-pay and say-on-frequency votes in a proxy statement would not trigger the requirement to file the proxy statement in preliminary form.\(^3\)

Broker Discretionary Voting. The proposing release makes clear that, as required by Section 957 of the Dodd-Frank Act, national securities exchanges have begun to amend their rules to prohibit broker discretionary voting of uninstructed shares in shareholder votes on executive compensation, and, as such, broker discretionary voting is not permitted for say-on-pay and say-on-frequency votes.\(^4\)

TARP Companies. Issuers that received financial assistance under the Troubled Asset Relief Program (TARP) are already required to conduct a separate shareholder vote to approve executive compensation during the period in which any indebtedness under TARP remains outstanding. Because such vote is effectively the same vote required under the proposed rules, and because such vote is required on an annual basis, these issuers are not required to hold an additional say-on-pay vote or a say-on-frequency vote as required under the proposed rules until the first annual meeting of shareholders after the issuer has repaid all outstanding indebtedness under TARP.

SAY-ON-GOLDEN PARACHUTES

Disclosure of Golden Parachute Arrangements. The SEC has proposed a new Item 402(t) of Regulation S-K, which would require disclosure with respect to golden parachute compensation arrangements in proxy or consent solicitations in connection with an acquisition, merger, consolidation or proposed sale or other disposition of all or substantially all of a company’s assets. The proposed rules would also require this disclosure in filings relating to other similar types of transactions, including going private transactions and tender offers. As proposed, disclosure would be required of all golden parachute compensation relating to the NEOs of both the target company and the acquiring company.

The proposed rules broadly define golden parachutes to include any agreements or understandings between each NEO and the acquiring company or the target company concerning any type of compensation that is based on, or otherwise relates to, the transaction. Compensation disclosed in a company’s Pension Benefits Table and Nonqualified Deferred Compensation Table, previously vested equity awards and bona fide post-transaction employment agreements would not be included because they are not viewed by the SEC as compensation that is based on, or otherwise relates to, the transaction.

The golden parachute compensation disclosure would be required in both tabular and narrative formats. The tabular disclosure would be set forth in the following table:

<table>
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<th>Name</th>
<th>Cash ($)</th>
<th>Equity ($)</th>
<th>Pension/ NQDC ($)</th>
<th>Perquisites/ Benefits ($)</th>
<th>Tax Reimbursement ($)</th>
<th>Other ($)</th>
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The table would require companies to separately quantify the individual elements of compensation that an executive would receive, including—

- any cash severance payment (e.g., base salary, bonus and pro rata non-equity incentive plan compensation payments)
- the dollar value of any accelerated equity award or payments in cancellation thereof

\(^3\) The SEC indicated that, even though the final rules have not yet been adopted, it would not object if a company did not file a preliminary proxy statement if the only matters that would require such filing are the say-on-pay and say-on-frequency votes.

\(^4\) Broker discretionary voting is also not permitted for say-on-golden parachute votes because current rules of the national securities exchanges already prohibit broker discretionary voting in connection with merger or acquisition transactions.
• pension and nonqualified deferred compensation benefit enhancements
• perquisites and other personal benefits and health and welfare benefits (including those available generally to all salaried employees)
• tax reimbursements (e.g., tax gross-ups)
• other elements of compensation.

Further, the table would require separate footnote identification of amounts attributable to “single-trigger” and “double-trigger” arrangements, so that shareholders can readily discern these amounts.

In addition to the tabular disclosure discussed above, the proposed rules would also require companies to provide narrative disclosure. Proposed Item 402(t) would require companies to describe any material conditions or obligations applicable to the receipt of payment, including non-compete, non-solicitation, non-disparagement or confidentiality agreements, their duration and provisions regarding waiver or breach. Companies would also have to describe the specific circumstances that would trigger payment; whether the payments would or could be lump sum, or annual, and their duration; and who would provide the payments, as well as any material factors regarding each agreement.

**Say-on-Golden Parachute Resolution.** The SEC has proposed a new Rule 14a-12(c) to address the say-on-golden parachute vote, which requires companies subject to the proxy rules to provide for a shareholder advisory vote on the golden parachute arrangements (discussed above) in proxy statements for meetings at which shareholders are asked to approve an acquisition, merger, consolidation or proposed sale or other disposition of all or substantially all assets. The shareholder vote, however, would only apply to agreements and arrangements between the soliciting person and any NEO of the issuer. So, if the target company is the soliciting person, any agreements or understandings between its NEOs and the acquiring company would not be subject to the vote.

**Exception if Subject to Prior Say-on-Pay Vote.** A separate say-on-golden parachute vote would not be required if such compensation arrangements were subject to a prior say-on-pay vote under Rule 14a-21(a). To take advantage of this exception, issuers would need to include the new Item 402(t) disclosure (discussed above) in the proxy statement that includes the say-on-pay vote. The exception would only be available to the extent the same golden parachute arrangements subject to the say-on-pay vote remain in effect and the terms have not been modified. If any changes have been made or any new arrangements entered into after the say-on-pay vote, only such changes and arrangements would be subject to a separate say-on-golden parachute vote.

**REPORTING OF PROXY VOTES BY INSTITUTIONAL INVESTMENT MANAGERS**

The proposed rules would require institutional investment managers subject to Section 13(f) of the Exchange Act to report to the SEC on an annual basis on Form N-PX how they voted on say-on-pay, say-on-frequency and say-on-golden parachute proposals. Such institutional investment managers would be required to report how they voted with respect to those securities that they have or for which they share voting power. The Form N-PX would be due no later than August 31 of each year with respect to votes during the most recent 12-month period ended June 30. This proposed reporting requirement would apply to votes relating to shareholder meetings held on or after January 21, 2011.

**CONTACT INFORMATION**

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