SPEAKING OF YOUR PROXY: SEC PROPOSES "SAY-ON-PAY" RULES

October 27, 2010

To Our Clients and Friends:

The SEC proposed rules last week to implement the so-called "say-on-pay," "say-on-frequency," and "say-on-golden parachute" advisory votes required under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank")[1]. In addition, the proposed rules include new disclosure requirements for change in control transaction disclosure that go beyond the scope of Dodd-Frank.

EFFECTIVE DATES

Under Dodd-Frank, the say-on-pay and frequency votes are required for an issuer's first annual or other shareholder meeting for the election of directors occurring on or after January 21, 2011, regardless of whether the SEC adopts final rules by that time. As a result, the proposed rules will provide guidance for companies that mail their proxy statements prior to the adoption of final rules by the SEC. The SEC has indicated that the say-on-pay and frequency votes will not trigger a preliminary proxy filing. It should also be noted that issuers subject to say-on-pay under the Troubled Asset Relief Program ("TARP") need not comply with the Dodd-Frank requirements until the first annual meeting of shareholders after the issuer has repaid all TARP obligations. The say-on-golden parachute rules will not be effective until the SEC implements final rules. Comments on the proposed rules are due on November 18, 2010.

SAY-ON-PAY AND FREQUENCY RULES

Say-on-Pay. The proposed say-on-pay rules would require issuers to solicit a non-binding say-on-pay advisory vote from shareholders at least once every *three* years covering the compensation of named executive officers as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion & Analysis ("CD&A"), compensation tables and other narrative executive compensation disclosures required by Item 402 (subject to limited exceptions). The SEC clarified that the say-on-pay vote would be required only in a proxy statement with respect to an annual or other meeting of shareholders for the election

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[1] *The SEC's proposing release (SEC Release No. 33-9153) is available at: http://www.sec.gov/rules/proposed/2010/33-9153.pdf.*

of directors. The proposed rules do not prescribe any specific language or form of resolution to be voted on by shareholders. We anticipate that most issuers will prefer to have a single say-on-pay vote relating to the named executives' compensation in the aggregate. Issuers may, in addition to the required say-on-pay vote, also seek more specific shareholder views through separate votes on specific aspects of compensation.

Frequency Vote. The proposed rules would require issuers to solicit, not less frequently than once every *six* years, a non-binding advisory vote from shareholders to determine whether the say-on-pay advisory vote should occur every one, two, or three years. As with the say-on-pay advisory vote, the SEC clarified that the frequency vote would be required only in a proxy statement with respect to an annual or other meeting of shareholders for the election of directors. The SEC stated that it believes that Dodd-Frank requires shareholders be given four choices in a say-on-frequency vote: every one, two, or three years or to abstain from voting. However, recognizing that there may be various transition issues associated with this voting requirement, the SEC indicated that it will not object if, prior to adoption of final rules, issuers omit the "abstain" choice if proxy firms are unable to reprogram voting systems in time. The SEC also makes clear that the frequency vote is *non-binding*, and it is therefore not necessary to impose a "standard for determining which frequency has been 'adopted' by the shareholders."

New Disclosure Rules. Under the proposed rules, issuers must briefly explain to shareholders the nature and effects (for example, that the votes are non-binding, and that the shareholders are provided with four choices under the frequency vote) of the say-on-pay and frequency votes. If the issuer includes the Board's recommendation as to the appropriate frequency in the proxy disclosure, the disclosure must clarify that the vote is not to approve this recommendation. In addition, the SEC proposes to require issuers to discuss in their Form 10-Q for the period during which the say-on-frequency vote was held (or 10-K if the vote was held during the issuer's fourth quarter), how frequently it will conduct say-on-pay votes in light of the results of the frequency vote. This is in addition to the current Form 8-K requirement to report shareholder voting results within four business days of the meeting. In addition, an issuer would be required to discuss in its CD&A, whether and, if so, how its compensation policies and decisions have taken into account the results of shareholder advisory votes on executive compensation.

Together, these disclosure requirements put the onus on issuers to demonstrate that they have been responsive to the advisory votes or to explain why their existing policies are appropriate if they are not in line with those results.

Limitation on Shareholder Proposals. One concern that issuers have expressed with respect to the SEC's proposed proxy access and say-on-pay rules is that thoughtfully adopted policies might be challenged via shareholder proposals on an annual basis. The SEC proposes to permit issuers to exclude shareholder proposals regarding say-on-pay or frequency votes if the issuer 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 frequency vote.

GOLDEN PARACHUTES

Under Dodd-Frank, a person making a proxy or consent solicitation seeking shareholder approval of "an acquisition, merger, consolidation, or proposed sale or disposition of all or substantially all of an issuer's assets" must disclose agreements or understandings that the soliciting person has with the named executive officers of the issuer (or any named executive officers of the acquiring issuer, if the person conducting the solicitation is not the acquiring issuer), involving compensation based on or relating to the transaction in accordance with rules to be adopted by the SEC.

The SEC's proposed rules extend beyond Dodd-Frank to require broader golden parachute disclosure (as discussed below). The proposed rules also require the golden parachute disclosure to be included in connection with other similar solicitations, exchange offers, tender offers and going-private transactions because these types of transactions effectively seek the consent of shareholders with respect to their investment decision. Third-party bidders are required to provide disclosure as well, but only to the extent the bidder has made a reasonable inquiry and has knowledge of the arrangements. Arrangements with executive officers of foreign private issuers are exempted from the disclosure requirements.

Form of Disclosure. The new golden parachute disclosure, which will broadly cover any type of present, deferred or contingent compensation arrangements, whether written or unwritten, will be required in both tabular and narrative formats. The tabular disclosure would require quantification of all compensation *relating to the transaction*, including the following: (i) all cash severance payments; (ii) the dollar value of accelerated equity awards and payments in cancellation of equity awards; (iii) pension and nonqualified deferred compensation benefit enhancements; (iv) perquisites and other personal benefits and health and welfare benefits (even if available to all employees); and (v) tax reimbursements, including 280G tax gross ups. The compensation required to be disclosed is different than the current annual disclosure regarding change in control under Item 402 and includes disclosure about non-discriminatory arrangements that may currently be excluded under Item 402. Under the proposed rules, amounts attributable to "single-trigger" and "double-trigger" arrangements must be identified in a separate footnote. The narrative disclosure requires a description of the specific circumstances that would trigger payment, how the payment would be made, and any material conditions or obligations associated with the

arrangements, such as non-competes, non-solicitation covenants, non-disparagement or confidentiality arrangements.

Advisory Vote. Dodd-Frank requires issuers to provide a separate non-binding shareholder advisory vote on the golden parachute arrangements between the target company and its named executive officers. Note that the requirement for the advisory vote covers a narrower category of compensation than the new golden parachute disclosure requirements described above. The advisory vote is not required for golden parachute arrangements between the acquiring issuer and the named executive officers of the target. In addition, no advisory vote is required if the golden parachute arrangement was previously included in a say-on-pay vote. To rely on this exception, however, the disclosure accompanying the say-on-pay vote must have been made in accordance with the format and substance described above for golden parachute arrangements and the arrangements must not have been subsequently amended, making this exception of somewhat limited utility unless issuers choose to change their annual disclosure to satisfy the new golden parachute requirements.

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Please do not hesitate to call us if you have any questions or to discuss the proposed rules generally.

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