

SHAREHOLDERS GET THEIR SAY: A DIVIDED SEC ADOPTS FINAL “SAY-ON-PAY” RULES

January 31, 2011

To Our Clients and Friends:

By a 3 to 2 vote, the Securities and Exchange Commission last week adopted final rules on shareholder approval of executive compensation and golden parachute arrangements (colloquially referred to as “say-on-pay”).¹ The rules implement §951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”), and include several modifications to the proposed rules issued by the SEC in October 2010 in light of public comments.²

Among other things, the final rules:

- require that public companies provide shareholders with an advisory vote on executive compensation, at least once every **three** calendar years;
- require that public companies allow shareholders to vote on how often the vote on executive compensation will be presented, at least once every **six** calendar years;
- revise Form 8-K to require disclosure of the company’s decision regarding the timing of executive compensation approval votes following a frequency vote; and
- mandate (1) additional disclosure of golden parachute arrangements and (2) an advisory vote with respect to these arrangements in connection with corporate transactions.

Newly public companies are not exempt from these requirements and will be required to hold votes on executive compensation and frequency at their first annual meeting following the initial public offering. For the next two years, however, smaller reporting companies will be temporarily exempted from the executive compensation and frequency votes (but not the golden parachute requirements). The treatment of these companies under the final rules was

¹ The SEC’s release on the final rules (SEC Release No. 33-9178) is available at:

<http://www.sec.gov/rules/final/2011/33-9178.pdf>

² For more information on the proposed rules, please see our Client Update of October 27, 2010, “Speaking of Your Proxy: SEC Proposes ‘Say-on-Pay’ Rules,” available at:

<http://www.debevoise.com/news/press/publications/detail.aspx?id=c2500999-90cd-466b-85cc-16179a2cef2>

the subject of much controversy, and ultimately was the principal reason the two Commissioners who wanted a permanent exemption for smaller companies and a one-year delay for newly public companies voted against adoption.

The statutory provisions related to the executive compensation and frequency votes became effective as of **January 21, 2011**, and any proxy statement relating to a meeting on or after that date that is required to include executive compensation disclosure must also include separate resolutions for executive compensation and frequency votes, regardless of when the final rules go into effect. As a technical matter, however, the SEC's final rules are not effective until **April 25, 2011** and need not be complied with for proxy statements filed before that date; because of this unusual gap, from now until April 25, 2011, companies may rely for compliance purposes on the proposed rules, the final rules or the statute. The rules on golden parachutes will be effective for merger proxy statements filed on or after April 25, 2011.

SAY-ON-PAY AND FREQUENCY VOTES

Final Rules on Votes. The SEC adopted the rules on shareholder approval of executive compensation and the frequency of approval substantially as proposed. Under these rules, companies must provide a separate shareholder advisory vote in proxy statements to approve the compensation of their named executive officers, and must give shareholders the opportunity to weigh in on how often they are presented with a vote. Shareholders must be given the right to choose an annual, biennial or triennial vote, or to abstain.

The final rules also clarify that these votes are only required with respect to an annual or special meeting at which proxies will be solicited for the election of directors, and that the votes are required only once during every three or six *calendar* years for executive compensation and frequency, respectively. While no specific language is required for either of the vote resolutions under the final rules, the SEC noted that the resolution should expressly indicate that the advisory vote is to approve the compensation of named executive officers "as disclosed pursuant to Item 402 of Regulation S-K" and provided a nonexclusive example of a resolution that would comply with the applicable requirements.

Related Disclosure and Filings. The SEC also adopted disclosure rules with respect to the executive compensation and frequency votes. Under the final rules, companies will be required to discuss in their CD&A whether and how their compensation policies and decisions took into account the most recent advisory vote on executive compensation, and if material, prior votes. The rules also add a Form 8-K filing requirement to disclose the company's decision with respect to the scheduling of the say-on-pay vote in light of the shareholders' vote on frequency. To give companies the opportunity to fully consider the shareholder vote, the Form 8-K must be filed no later than 150 calendar days following the

meeting at which the frequency vote occurred, and in any event not later than 60 days prior to deadline for submission of shareholder proposals for the next annual meeting. The final rules also make clear that the inclusion of any advisory vote on executive compensation, including a say-on-pay vote or a vote on the frequency of say-on-pay votes, will not trigger a requirement that the proxy statement be filed in preliminary form with the SEC.

GOLDEN PARACHUTES

Disclosure. The SEC's final rules maintain the broad disclosure of golden parachute arrangements originally proposed last October. Under the final rules, companies will be required to disclose in merger proxies (and related disclosure documents), as well as other similar solicitations such as exchange offers, tender offers, and going private transactions, in both narrative and tabular formats the golden parachute arrangements between (i) the target or acquirer and (ii) the target's named executive officers. This disclosure is only necessary for compensation that is based on or otherwise relates to the transaction and excludes compensation related to any post-transaction employment agreements as well as arrangements with officers of foreign private issuers from the disclosure requirements. Unlike disclosure of change in control payments under the proxy rules for annual meetings, however, there is no exception for broad-based benefits *de minimis* perquisites or other personal benefits. Third-party bidders (other than ingoing private transactions) are not required to include the disclosure in their documents. The SEC also made clear that the golden parachute disclosure provision does not change the disclosure obligations in regular annual meeting proxies.

Shareholder Vote. The rule on shareholder advisory votes of golden parachute arrangements was adopted substantially as proposed. Unlike the disclosure provisions described above, the advisory vote will not be required at meetings in which shareholders are asked to approve other proposals (*e.g.*, stock issuances) in connection with a transaction, nor is the vote required to cover arrangements between the acquirer and the soliciting target's named executive officers. Golden parachute arrangements that were already subject to a shareholder say-on-pay vote are exempt from a separate vote in the merger proxy, but only if the shareholders received at the time of the say-on-pay vote information in the format required under the new golden parachute disclosure rules for merger proxies and the terms of those arrangements have not been modified. These conditions are therefore likely to limit the utility of this exception.

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Please do not hesitate to call us if you have any questions or wish to discuss the final rules in greater detail.

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