

ALERTS AND UPDATES

SEC Finalizes Rules for Shareholders' Say-on-Pay, Say-on-Frequency and Say-on-Golden Parachute Votes

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The U.S. Securities and Exchange Commission (the "SEC") has adopted [new rules](#) that require every public company¹ to conduct separate shareholder advisory votes on executive compensation and golden parachute arrangements. The new rules implement Section 14A of the Securities Exchange Act of 1934 (the "Exchange Act"), which was created under Section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), signed into law on July 21, 2010. The votes cast by a company's shareholders pursuant to Section 14A will be nonbinding on the company and its board of directors, will not overrule a decision by the company or its board of directors and will not create or change the fiduciary duties of the company or its board of directors.

Say-on-Pay Votes

Section 14A(a)(1) and Rule 14a-21(a) thereunder require that, at least once every three years, at an annual meeting of shareholders or other meeting of shareholders for which the SEC's proxy solicitation rules require Item 402 disclosure concerning executive compensation, a public company afford its shareholders the right to a separate, nonbinding vote to approve the compensation of the company's named executive officers² required to be disclosed in the proxy statement relating to such meeting under Item 402 of Regulation S-K³ (a "Say-on-Pay Vote").

Say-on-Frequency Votes

Under Section 14A(a)(2) and Rule 14a-21(b) thereunder, at least once every six years, a public company must afford its shareholders the right to a separate, nonbinding vote on whether the Say-on-Pay Vote will occur every one, two or three years (a "Say-on-Frequency Vote").⁴

Say-on-Golden Parachute Votes

Section 14A(b)(1) requires that, in connection with a meeting at which the shareholders of a public company are asked to approve a proposed acquisition, merger, consolidation, or proposed sale or other disposition of all or substantially all the company's assets (a "change of control transaction"), the company must disclose in its proxy statement certain so-called "golden parachute" arrangements that are based on or related to the change of control transaction, including any compensation agreements and understandings between the soliciting company and any of its named executive officers. Section 14A(b)(2) and Rule 14a-21(c) thereunder require the company at such meeting to afford its shareholders the right to a separate, nonbinding vote to approve the golden parachute arrangements (a "Say-on-Golden Parachute Vote").

However, a company does not have to submit its golden parachute arrangements to a Say-on-Golden Parachute Vote at a meeting at which its shareholders are asked to approve a change of control transaction if:

- the golden parachute arrangements were previously subject to a Say-on-Pay Vote under Section 14A(a);⁵
- the disclosure requirements under Item 402(t) of Regulation S-K (as outlined below) were satisfied in the proxy statement relating to a meeting at which shareholders were afforded a Say-on-Pay Vote;⁶ and
- the terms of the golden parachute agreements or arrangements that were previously subject to the Say-on-Pay Vote have not been modified.⁷

Additional Disclosure Requirements Related to Golden Parachutes

The SEC's new rules will require more detailed disclosure of golden parachute arrangements in the context of a change of control transaction than the SEC's rules previously required.⁸ Under Section 14A(b), the disclosure in the proxy statement must include a "clear and simple" presentation of the aggregate total of all compensation payable to any named executive officer based on or related to the change of control

transaction and the conditions upon which the compensation may be paid or become payable. Item 402(t) of Regulation S-K requires disclosure of golden parachute arrangements (i) between the target company and any of its named executive officers, and (ii) between the acquiring company and the target company's named executive officers⁹ in both tabular and narrative formats that include separated items for the elements of the officers' compensation.¹⁰

Under Item 402(t) of Regulation S-K, a company must describe all material conditions and obligations applicable to the executive's receipt of any executive compensation payments (such as noncompete, nonsolicitation, nondisparagement and confidentiality agreements; their duration; and provisions regarding waiver or breach), a description of the specific circumstances that would trigger such payments, whether the payments would or could be paid in a lump sum or annually, the duration of the payments, who would provide the payments and material factors regarding each golden parachute arrangement.

Timing Requirements Under Section 14A

A company, other than a smaller reporting company, is required to include both the Say-on-Pay Vote and the Say-on-Frequency Vote in its proxy statement for the first annual meeting, or other meeting of shareholders at which directors will be elected and for which the SEC rules require Item 402 disclosure concerning executive compensation, occurring after January 21, 2011. Smaller reporting companies are not required to conduct a Say-on-Pay Vote or a Say-on-Frequency Vote until their first annual meeting of shareholders, or other meeting of shareholders at which directors will be elected and for which the SEC rules require Item 402 disclosure concerning executive compensation, occurring after January 21, 2013.¹¹

Nevertheless, upon the effectiveness of Rule 14a-21(c), a public company, including a smaller reporting company, will be required to submit Say-on-Golden Parachute Votes to shareholders in connection with a meeting at which shareholders are asked to approve a change of control transaction.

Section 14A Vote Language

The SEC's new rules do not require specific language or a form of resolution that must be presented for the shareholder advisory votes required by Section 14A.¹² However, the respective Section 14A shareholder advisory votes have to generally relate to all executive compensation required to be disclosed under Item 402 of Regulation S-K.¹³

Disclosure of the Effects of Section 14A Advisory Votes

Disclosure of General Effect of Shareholder Advisory Votes. Under the new rules,¹⁴ a company is required to disclose, in the proxy statement relating to the meeting at which shareholders are entitled to a shareholder advisory vote, that the company is providing such vote as required by Section 14A, and briefly explain the general effect of the shareholder advisory vote, such as the nonbinding nature of the vote and, when applicable, disclose the current frequency of such company's Say-on-Pay Votes.

Disclosure in Compensation Discussion and Analysis. A company that is required to include a Compensation Discussion and Analysis in its proxy statement pursuant to Item 402 of Regulation S-K will have to include in that analysis disclosure relating to whether and how the company has considered the results of the most recent Say-on-Pay Vote in determining its executive compensation policies and decisions and, if so, how that consideration has affected the company's executive compensation policies and decisions. Although a smaller reporting company does not have to include a Compensation Discussion and Analysis in its proxy statement, it may have to include disclosure relating to the effects that prior Say-on-Pay Votes have had on its executive compensation policies and decisions as a result of Item 402(o) of Regulation S-K, which requires a smaller reporting company to provide a narrative description of any material factors necessary to an understanding of the information disclosed in its Summary Compensation Table.

Disclosure in Form 8-K. A company is required to make standard disclosures, based on Item 5.07 of Form 8-K, regarding each of the shareholder advisory votes required by Section 14A of the Exchange Act. In addition, a company will now be required to disclose on Form 8-K its decision regarding the frequency of its Say-on-Pay Votes in light of the results of the Say-on-Frequency Vote.¹⁵

No Preliminary Proxy Statement Required

The SEC has amended Rule 14a-6(a) of the Exchange Act such that Say-on-Pay Votes and Say-on-Frequency Votes will not trigger the requirement that a company file a preliminary proxy statement, as long as none of the other matters in the proxy statement trigger such a filing under Rule 14a-6(a).

No Broker Discretionary Voting

Section 6(b) of the Exchange Act, as amended by Section 957 of the Dodd-Frank Act, directs national securities exchanges to change their rules to prohibit brokers from voting uninstructed shares in certain matters, including Say-on-Pay Votes and Say-on-Frequency Votes.¹⁶

For Further Information

If you have any questions regarding the proposed say-on-pay, say-on-frequency and say-on-golden parachute rules discussed above, including how they may affect your company, please contact any [member](#) of the [Securities Law Practice Group](#) or the lawyer in the firm with whom you are regularly in contact.

Notes

1. The SEC's new rules apply to issuers that have a class of equity securities registered under Section 12 of the Exchange Act and are subject to the SEC's proxy rules.
2. As defined in Item 402(a)(3) of Regulation S-K.
3. Smaller reporting companies remain subject to scaled executive compensation disclosure requirements, and thus will not need to disclose Compensation Discussion and Analysis narratives in their annual proxy statements in order to comply with Section 14A; but smaller reporting companies will not be subject to Section 14A(a) and Rules 14a-21(a) and (b) until their first annual meeting of shareholders or other meeting of shareholders (at which directors will be elected) after January 21, 2013.
4. The SEC has not prescribed a standard for companies to determine which frequency has been "adopted" by the shareholders in a Say-on-Frequency Vote because the vote is merely advisory. However, a shareholder proposal that would provide a Say-on-Pay Vote, seeks future Say-on-Pay Votes or that relates to the frequency of Say-on-Pay Votes may be excluded from the proxy materials of a company if it has adopted a policy on the frequency of Say-on-Pay Votes that is consistent with the majority of votes cast by shareholders in the most recent Say-on-Frequency Vote.
5. Whether or not the vote was actually approved by shareholders is not considered by Rule 14a-21.
6. Companies may wish to voluntarily include Item 402(t) disclosure with their other executive compensation disclosure in annual meeting proxy statements soliciting Say-on-Pay Votes so that they need not present a Say-on-Golden Parachute Vote and associated required disclosures to shareholders in a potential subsequent change of control transaction.
7. New golden parachute arrangements and revised terms of such arrangements that were previously subject to a Say-on-Pay Vote would be subject to a Say-on-Golden Parachute Vote under Section 14A(b); provided, however, (i) if the disclosure under Item 402(t) has been updated to change only the value of the items on the Golden Parachute Compensation Table to reflect price movements in the company's securities, or (ii) if the changes result only in a reduction in value of the total compensation payable, such changes will not require a new shareholder vote.
8. In the context of a merger, Item 5 of Schedule 14A requires the disclosure of the substantial interest of any person who has been a director or executive officer since the beginning of the last fiscal year in any matter to be acted upon. Item 402(j) of Regulation S-K and Item 8 of Schedule 14A require companies to disclose in their annual reports and annual meeting proxy statements payments (and circumstances regarding such payments) that may be made to named executive officers in connection with a change of control.

9. Rule 14a-21(c) requires a Say-on-Golden Parachute Vote solely with respect to golden parachute arrangements between the target company and any of its named executive officers. Although Item 402(t) requires disclosure of the golden parachute arrangements between the target company and its named executive officers and between the acquiring company and the target company's named executive officers, neither Section 14A(b) nor Rule 14a-21(c) requires the target company to propose that its shareholders consider and vote upon the golden parachute arrangements between the acquiring company and the target company's named executive officers.
10. This table must include cash severance payments; the dollar value of accelerated stock awards, in-the-money option awards for which vesting would be accelerated, and payments in cancellation of stock and option awards; pension and nonqualified deferred compensation benefit enhancements; perquisites and other personal benefits and health and welfare benefits; tax reimbursements such as tax gross-ups; any additional compensation related to the transaction; and the aggregate total of all compensation related to the transaction.
11. The SEC has also granted a limited exemption to companies with outstanding indebtedness under the Troubled Asset Relief Program (the "TARP"). A company with outstanding indebtedness under the TARP is not required to conduct a Say-on-Frequency Vote until after it has repaid all outstanding indebtedness under the TARP because each such company is currently required to conduct an annual Say-on-Pay Vote under Section 111(e) of the Emergency Economic Stabilization Act.
12. While the SEC does not require specific resolution language, the instruction to Rule 14a-21(a) provides the following nonexclusive example resolution that would satisfy the Say-on-Pay Vote requirements: "RESOLVED, that the compensation paid to the company's named executive officers, as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis, compensation tables and narrative discussion, is hereby APPROVED." The SEC did not provide a similar example with respect to the Say-on-Frequency Vote or the Say-on-Golden Parachute Vote.
13. The compensation of directors, as disclosed under Item 402(k) or Item 402(r) of Regulation S-K, as well as the risk management and risk-taking incentive policies and practices of companies disclosed under Item 402(s) of Regulation S-K, as they relate to compensation for employees generally, will not be subject to a shareholder advisory vote under Section 14A.
14. See Item 24 of Schedule 14A.
15. The company's disclosure regarding its decision on the frequency of Say-on-Pay Votes must be made within 150 days after the meeting at which the Say-on-Frequency Vote was conducted, but in no event later than 60 days prior to the deadline for submission of shareholder proposals under Rule 14a-8 for the subsequent annual meeting. Such disclosure will be made by amendment to the company's most recent Form 8-K filed pursuant to Item 5.07(b).
16. Brokers are not permitted to vote uninstructed shares in connection with a merger or acquisition or acquisition transaction under the current rules of the national securities exchanges and, thus, have no discretion to vote uninstructed shares in a Say-on-Golden Parachute Vote.

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