

# Client Alert

Corporate Department

February 2011

## SEC Adopts Final “Say-On-Pay” Rules

On January 25, 2011, the Securities and Exchange Commission (“SEC”) adopted final rules under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), implementing provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act requiring:

- 1) A shareholder advisory vote on executive compensation (the “Say-on-Pay” vote);
- 2) A shareholder advisory vote on frequency of the Say-on-Pay vote (the “Say-on-Frequency” vote);
- 3) A shareholder advisory vote on golden parachute compensation arrangements in connection with a merger or similar transaction presented for shareholder approval (the “Say-on-Golden Parachutes” vote); and
- 4) Specified disclosure concerning golden parachute compensation arrangements in connection with a merger or similar transaction presented for shareholder approval.

Companies other than smaller reporting companies must conduct a Say-on-Pay vote and a Say-on-Frequency vote at their first annual or other meeting of shareholders occurring on or after January 21, 2011. All companies must conduct a Say-on-Golden Parachutes vote and comply with golden parachute disclosure rules in connection with merger proxy or consent statements filed on or after April 25, 2011.

Smaller reporting companies are not required to conduct the Say-on-Pay vote or the Say-on-Frequency vote until the first annual or other meeting of shareholders occurring on or after January 21, 2013. This two year temporary exemption does not apply to the Say-on-Golden Parachutes vote or to disclosure regarding golden parachute compensation arrangements. A smaller reporting company is a company with a public equity float of \$75 million or less, as measured at the end of its most recently completed second fiscal quarter.

There is no grace period for newly public companies; the Say-on-Pay vote and the Say-on-Frequency vote must be included in the proxy statement for such companies’ first annual meeting after their initial public offering.

## Say-on-Pay Vote

New Section 14A(a)(1) of the Exchange Act requires companies, at least once every three calendar years, to include a resolution subject to shareholder vote to approve executive compensation disclosed pursuant to Item 402 of Regulation S-K.

### Key points:

- The Say-on-Pay vote is only required with respect to an annual meeting, or a special meeting held in lieu thereof, at which proxies are being solicited to elect directors.
- The Say-on-Pay vote is *non-binding* and the advisory nature of the vote must be disclosed in the proxy statement.
- Rule 14a-6 has been amended to include the Say-on-Pay vote among the items that do not trigger the requirement to file a preliminary proxy statement with the SEC.
- Broker discretionary voting is not permitted on the Say-on-Pay vote.

The Say-on-Pay vote relates to the executive compensation disclosure required by Item 402 of Regulation S-K to be included in a company's proxy statements, *i.e.*, the compensation tables, narrative disclosure on executive compensation and the Compensation Discussion & Analyses (the "CD&A")<sup>1</sup>. The vote does not cover director compensation or disclosure concerning the company's compensation policies and practices as they relate to risk management and risk-taking incentives.

The rule does not require the use of a specified form of resolution, but provides the following example:

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 adopting release states that companies "should retain the flexibility to craft the resolution language."

Although the Say-on-Pay vote is non-binding, Item 402 of Regulation S-K has been amended to require disclosure in a company's CD&A, whether and, if so, to what extent, the company's compensation policies and decisions have taken into consideration the results of the most recent Say-on-Pay vote.

Disclosure of the effect of the Say-on-Pay vote on compensation policies and decisions is not required for smaller reporting companies that are subject to scaled disclosure requirements and are not required to include CD&A. However, smaller reporting companies are required to include a narrative description of any material factors necessary to understand the information

---

<sup>1</sup> The new rules do not change the scaled disclosure requirements for smaller reporting companies and such companies will not be required to provide a CD&A in order to comply with the rules.

disclosed in the Summary Compensation Table and, to the extent consideration of prior Say-on-Pay votes is relevant, such disclosure will be required.

### Say-on-Frequency Vote

New Section 14A(a)(2) of the Exchange Act requires companies, at least once every six calendar years, to include a resolution subject to shareholder vote to determine whether the Say-on-Pay vote should occur every 1, 2 or 3 years.

#### Key points:

- The Say-on-Frequency vote is only required with respect to an annual meeting, or a special meeting held in lieu thereof, in which proxies are being solicited to elect directors.
- The Say-on-Frequency vote is *non-binding* and the advisory nature of the vote must be disclosed in the proxy statement.
- Rule 14a-6 has been amended to include the Say-on-Frequency vote among the items that do not trigger the requirement to file a preliminary proxy statement with the SEC.
- Broker discretionary voting is not permitted on the Say-on-Frequency vote.
- The proxy card must contain four choices: whether the Say-on-Pay vote will occur every 1, 2 or 3 years or to abstain from voting<sup>2</sup>.
- The rule does not require a company to make a recommendation with respect to the Say-on-Frequency vote.
- Companies may vote uninstructed proxies in favor of management's recommended Say-on-Frequency vote if: (1) the company includes a recommendation for the Say-on-Frequency vote in the proxy statement, (2) the proxy card includes an option to abstain from voting, and (3) the proxy card includes language in bold regarding how uninstructed shares will be voted.
- No later than 150 days after the annual meeting, or such other meeting, at which the Say-on-Frequency vote was held (but not less than 60 days before the deadline for submission of shareholder proposals under Rule 14a-8 for the next annual meeting), companies must disclose in a Form 8-K their decision on how frequently they will hold the Say-on-Pay vote taking into account the Say-on-Frequency vote.
- A company that adopts a policy on the frequency of Say-on-Pay votes that is consistent with the frequency alternative that received a majority in the Say-on-Frequency vote may, within certain restrictions, exclude under Rule 14a-8 any shareholder proposal to hold a Say-on-Pay vote or that seeks future Say-on-Pay or Say-on-Frequency votes.

New Item 24 has been added to Schedule 14A, which includes the requirement that companies provide in their proxy materials disclosure of the current frequency of the Say-on-Pay vote and when the next scheduled Say-on-Pay vote will occur.

---

<sup>2</sup> In order to give tabulators additional time to implement the four option system, the SEC, until December 31, 2011, will not object if a company has only three options, 1, 2 or 3 years.

### Say-on-Golden Parachutes Vote

New Section 14A(b)(1) of the Exchange Act requires, in a proxy or consent solicitation to approve a merger or similar transaction, inclusion of a resolution subject to shareholder vote to approve the disclosed Golden Parachute Compensation (as defined and discussed below). While Item 402(t) of Regulation S-K requires disclosure of all Golden Parachute Compensation payable to the named executive officers of a company, the Say-on-Golden Parachutes vote is required only to approve the Golden Parachute Compensation payable by the company soliciting the proxies or consents to approve the transaction to its named executive officers. If the target company is the soliciting person, then agreements between the acquirer and the named executive officers of the target, though included in the required Golden Parachute Compensation disclosure, are not subject to the Say-on-Golden Parachutes vote.

#### Key points:

- The Say-on-Golden Parachutes vote is *non-binding*.
- The disclosure must include the aggregate total of all Golden Parachute Compensation that may be paid or become payable to each named executive officer and the conditions upon which it may be paid or become payable.
- A Say-on-Golden Parachutes vote is not required for Golden Parachute Compensation that was previously subjected to a Say-on-Pay vote (regardless of the outcome of such Say-on-Pay vote).

Companies may, though they are not required to, include Golden Parachute Compensation in the executive compensation disclosure subject to a Say-on-Pay vote. The exception identified in the third “key point” above applies only to the extent the Golden Parachute Compensation previously subject to a Say-on-Pay vote has not been subsequently modified. Any new or modified elements of the Golden Parachute Compensation (except a change that results only in a reduction in the value of the total compensation) would be subject to a separate Say-on-Golden Parachutes vote. In such event, the company must include two separate Golden Parachute Compensation tables in the proxy or consent statement, one table showing all of the Golden Parachute Compensation and one table showing only the new and/or modified elements of the Golden Parachute Compensation subject to the Say-on-Golden Parachutes vote.

### Golden Parachute Compensation Disclosure

Item 5 of Schedule 14A has been amended to require, in a company’s proxy or consent solicitation to approve a merger or similar transaction, additional disclosure of any agreements or understandings with named executive officers concerning compensation that is based on or otherwise relates to the merger or other similar transaction (the “Golden Parachute Compensation”). Item 402(t) of Regulation S-K requires disclosure of all Golden Parachute Compensation payable to the named executive officers of a company, whether payable by the company or an acquiring company. Disclosure of the Golden Parachute Compensation must be in both tabular and narrative form.

The tabular disclosure must include quantitative disclosure of the individual elements of compensation that would be received and the total for each named executive officer. The required table is set forth below:

Golden Parachute Compensation

| Name<br>(a) | Cash<br>(\$)<br>(b) | Equity<br>(\$)<br>(c) | Pension/<br>NQDC<br>(\$)<br>(d) | Perquisites/<br>Benefits<br>(\$)<br>(e) | Tax<br>Reim<br>burse<br>ment<br>(\$)<br>(f) | Other<br>(\$)<br>(g) | Total<br>(\$)<br>(h) |
|-------------|---------------------|-----------------------|---------------------------------|---|---|----------------------|----------------------|
| PEO         |                     |                       |                                 |   |   |                      |                      |
| PFO         |                     |                       |                                 |   |   |                      |                      |
| A           |                     |                       |                                 |   |   |                      |                      |
| B           |                     |                       |                                 |   |   |                      |                      |
| C           |                     |                       |                                 |   |   |                      |                      |

Column (b) represents any cash severance payment, *i.e.*, base salary, bonus and pro-rata non-equity incentive plan compensation payments). Column (c) represents 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. Column (d) represents pension and nonqualified deferred compensation benefit enhancements. Column (e) represents perquisites and other personal benefits and health and welfare benefits. Column (f) represents tax reimbursements. Additionally, there is an “Other” column, Column (g), for any additional elements of compensation not included in the other columns of the table. Column (h) requires the aggregate total of Golden Parachute Compensation for each named executive officer. Separate footnote identification of amounts attributable to “single trigger” and “double trigger” arrangements is also required.

The narrative disclosure must include descriptions of any material conditions or obligations applicable to the receipt of payment, including but not limited to non-compete, non-solicitation, non-disparagement or confidentiality agreements, their duration and provisions regarding waiver or breach. Disclosure must also include any specific circumstances that would trigger payment, whether the payments would or could be lump sum or annual, their duration, by whom the payments would be provided and any other material factors regarding each agreement.

A bidder in a third-party tender offer is not required to provide Golden Parachute Compensation disclosure on Schedule TO, unless it is also a Rule 13e-3 going private transaction. However, companies filing solicitation/recommendation statements on Schedule 14D-9 in connection with a third-party tender offer must include such disclosure.

## Company Considerations

We recommend that companies consider the following in complying with the new rules:

- Voting policies of institutional holders and their reliance on the recommendations of proxy advisory firms.
- The policies of proxy advisory firms (e.g., RiskMetrics and Glass Lewis have recommended an annual Say-on-Frequency vote).
- Voting results at other public companies as the proxy season progresses.
- Enhanced disclosure that justifies executive compensation, particularly with respect to any compensation practices that have been flagged by proxy advisory firms as problematic.
- Whether to supplement the CD&A with a summary that demonstrates pay for performance.
- When to include a supporting statement for the recommended vote. For example, if a company makes a recommendation on the Say-on-Frequency vote for biennial or triennial frequency, inclusion of a supporting statement for such recommendation may be needed.
- Recommendations of peer companies on the Say-on-Frequency vote.

Please feel free to contact any of the partners listed below or any corporate partner with whom you work if you would like to discuss the new rules and their potential ramifications.

---

David J. Adler  
[dadler@olshanlaw.com](mailto:dadler@olshanlaw.com)  
212.451.2244

Kenneth M. Silverman  
[ksilverman@olshanlaw.com](mailto:ksilverman@olshanlaw.com)  
212.451.2327

Ron S. Berenblat  
[rberenblat@olshanlaw.com](mailto:rberenblat@olshanlaw.com)  
212.451.2296

This publication is issued by Olshan Grundman Frome Rosenzweig & Wolosky LLP for informational purposes only and does not constitute legal advice or establish an attorney-client relationship. To ensure compliance with requirements imposed by the IRS, we inform you that unless specifically indicated otherwise, any tax advice contained in this publication was not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any tax-related matter addressed herein. In some jurisdictions, this publication may be considered attorney advertising.

Copyright © 2011 Olshan Grundman Frome Rosenzweig & Wolosky LLP. All Rights Reserved.