WHITE & CASE

Client**Alert**

Financial Markets Developments

Capital Markets/Securities
Executive Compensation and Employee Benefits
November 2010

SEC Proposes Rules on Say-on-Pay and Related Matters

On October 18, 2010, the Securities and Exchange Commission (the "SEC") proposed rules implementing Section 951 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") that would enable shareholders at all public companies subject to the federal proxy rules to cast a non-binding vote on executive compensation packages, including "golden parachute" arrangements relating to merger transactions (i.e., arrangements for executives concerning any type of compensation (deferred or contingent) that is based on or otherwise relates to the acquisition, merger, consolidation, sale or other disposition of all or substantially all of the assets of the issuer).

The proposed rules cover three broad areas: (1) shareholder advisory vote on executive compensation ("say-on-pay") and on the desired frequency of the say-on-pay votes ("say-on-frequency"); (2) shareholder advisory vote and disclosure of golden parachute arrangements; and (3) institutional investment manager annual reporting of say-on-pay and golden parachute votes (unless the votes are otherwise required to be reported publicly by SEC rules).

The SEC's 30-day public comment period on the proposals closes on November 18, 2010, with final rules expected to be adopted shortly thereafter. As a result, the say-on-pay regime will be in effect for the 2011 proxy season.

Shareholder Approval of Executive Compensation and of the Frequency of Shareholder Votes on Executive Compensation

Say-on-Pay

Section 951 of the Dodd-Frank Act provides that not less frequently than once every three years, at any annual or other meeting of shareholders for which the SEC's proxy rules require compensation disclosure, beginning with the first annual shareholders' meeting taking place on or after January 21, 2011, companies must seek a non-binding shareholder vote to approve the compensation of their named executive officers, as disclosed under Item 402 of Regulation S-K.

If you have questions or comments regarding this Alert, please contact one of the lawyers listed below:

Colin Diamond
Partner, New York
+ 1 212 819 8754
cdiamond@whitecase.com

Mark Hamilton
Partner, New York
+ 1 212 819 8262
mhamilton@whitecase.com

David Johansen
Partner, New York
+ 1 212 819 8509
djohansen@whitecase.com

White & Case LLP
1155 Avenue of the Americas
New York, NY 10036
United States
+ 1 212 819 8200

Under proposed new Rule 14a-21(a), the vote would be based on a company's executive compensation disclosure, including the Compensation Discussion & Analysis (the "CD&A"), compensation tables and related narrative disclosure. As expected, no change will be made to the compensation disclosure regime applicable to smaller reporting companies that will not be required to provide a CD&A to satisfy their disclosure obligations in connection with the general say-on-pay vote. In fact, the SEC has solicited comment on whether smaller reporting companies should be entirely exempt from say-on-pay. The compensation of directors is not subject to the shareholder advisory vote. In addition, if a company includes disclosure about its compensation policies and practices as they relate to risk management and risk-taking incentives, these policies and practices would not be subject to the shareholder advisory vote as they relate to the company's compensation for employees generally. However, when risk considerations represent a material aspect of the company's compensation policies or decisions for named executive officers and are therefore discussed in a CD&A, such disclosure would be considered by shareholders when voting on executive compensation.

While the proposed rules do not prescribe a specific form of a say-on-pay resolution, the SEC notes that such resolution is required to cover all compensation required to be disclosed in the proxy statement pursuant to Item 402 of Regulation S-K. The proposed rules specifically require disclosure about the say-on-pay vote in the annual meeting proxy statement, including whether the vote is non-binding. The proposals also require companies to address in the CD&A whether and how their compensation policies and decisions have taken into account the results of past say-on-pay votes. While the proposed new disclosure is not mandated by Section 951 of the Dodd-Frank Act, the SEC believes that such requirement will facilitate better investor understanding of companies' compensation decisions.

Say-on-Frequency

Section 951 of the Dodd-Frank Act provides that, not less frequently than once every six years, beginning with the first annual shareholders' meeting taking place on or after January 21, 2011, companies must seek a non-binding shareholder vote to determine whether the say-on-pay vote will occur every one, two or three years. Proposed new Rule 14a-21(b) affirms that the say-on-frequency vote is non-binding on a company and its board of directors (an issue left unresolved by the language in the Dodd-Frank Act), a position that, if adopted, may ultimately raise issues where a company is faced with a shareholder vote that is inconsistent with the views of its management and board of directors on the frequency of this vote. Companies would be required to offer four choices to shareholders on a say-on-frequency proxy card: (1) one year, (2) two years, (3) three years or (4) abstain, subject to certain transition rules if the transfer agent is unable to tabulate four choices. This will require all parties involved in the proxy process to adjust their procedures and may necessitate a bylaws amendment for certain companies. Furthermore, it could result in an option not preferred by a majority of shareholders being selected (e.g., if a majority of shareholders vote for one and two years, but three years still receives the largest number of votes of any of the choices).

The proposed rules would impose additional disclosure obligations on companies with respect to the effects of the frequency vote, including whether the vote is non-binding and whether the issuer intends to follow the results of the advisory vote. For example, an amended Item 9B of Form 10-K and a new Item 5(c) of Part II of Form 10-Q would require an issuer to disclose its decision regarding how frequently it will conduct advisory votes on executive compensation in light of the results of the shareholder vote on frequency.

The SEC is seeking public input, among others, on the manner in which issuers should present the shareholder say-on-pay or say-on-frequency vote and, with respect to smaller reporting companies, whether an exemption would be appropriate. The SEC is also seeking public input on whether the four choices available to shareholders for the frequency of shareholder votes on executive compensation will be sufficiently clear and whether issuers, brokers, transfer agents and data processing firms will be able to accommodate four choices for a single line item on a proxy card. The SEC specifically asks for comment on whether an IPO company should be able to disclose the planned frequency of its say-on-pay votes in its Form S-1 and then be exempt from conducting say-on-pay and say-on-frequency votes until the year disclosed (e.g, whether an issuer which discloses in its IPO prospectus that it will conduct a say-on-pay vote every two years would be exempt from the say-on-pay and say-on-frequency votes requirements for its first annual meeting as a reporting company).

Related Proposals

The SEC will amend the proxy rules to provide that companies are not required to file a preliminary proxy statement for say-on-pay or say-on-frequency resolutions (i.e., consistent with the approach applied to TARP recipients' shareholder say-on-pay votes implemented in 2008).

An amendment to Rule 14a-8 would allow companies to exclude a shareholder proposal providing for a say-on-pay or a say-on-frequency vote, provided that the company has adopted a policy on say-on-pay or say-on-frequency that is consistent with the plurality of votes cast in the most recent relevant vote.

Finally, the SEC confirmed that each of the say-on-pay and say-on-frequency votes is an "executive compensation matter" on which brokers are not permitted to vote uninstructed shares as stipulated in Section 957 of the Dodd-Frank Act.

Shareholder Approval and Disclosure of Golden Parachute Arrangements

Section 951 of the Dodd-Frank Act requires a non-binding shareholder vote on golden parachute payments to named executive officers in connection with a change of control transaction of the company (unless previously approved by a say-on-pay vote). The proposed rules would require companies to give shareholders advisory votes on golden parachutes and to provide information on those arrangements in merger proxy statements. The proposed rules are drafted broadly to encompass the full range of golden parachute agreements and understandings that acquiring and target companies have with named executive officers of both companies.

Section 14A(b)(1) of the Exchange Act requires "clear and simple" disclosure of the golden parachute compensation. The SEC believes that the current information required by Item 402(j) of Regulation S-K, which is applicable to annual reports and proxy statement and requires disclosure of potential payments in connection with any termination of a named executive officer or upon a change in control, does not conform to the dictates of the Dodd-Frank Act. For example, Item 402(j) does not require disclosure in tabular form (although most companies use a tabular approach) and certain items such as perquisites in amounts less than $10,000 in the aggregate for an individual named executive officer may be omitted from disclosure under Item 402(j). In the SEC's view, the Dodd-Frank Act does not allow for such exceptions. The SEC believes that amending Item 402(j) would impose unnecessary annual burdens on companies.

Accordingly, to satisfy Section 14A(b)(1)'s disclosure requirements, proposed new Item 402(t) of Regulation S-K would require both tabular and narrative disclosure of change in control payments in merger proxies with respect to the golden parachute vote in connection with a merger or other extraordinary corporate transaction. The tabular disclosure made in a new "Golden Parachute Compensation" table would include columns for the following categories of compensation that are based on or otherwise relate to a merger, acquisition or a similar transaction: cash; equity; pension and nonqualified deferred compensation; perquisites and other personal benefits; tax reimbursements; and other items (with footnote identification of each separate form of compensation reported, including amounts attributable to "single-trigger" arrangements and amounts attributable to "double-trigger" arrangements). Disclosure or quantification of previously vested equity awards would not be required under the proposed rues because the SEC believes that these amounts are vested without regard to the transaction (i.e., and therefore do not constitute compensation "that is based on or otherwise related to" the transaction). The total for each named executive officer would be required to be disclosed in a separate column.

Issuers would not be required to include in the merger proxy a separate shareholder vote on the golden parachute compensation disclosed under new Item 402(t) if such disclosure had been included in the executive compensation disclosure that was subject to a prior vote of shareholders (i.e., Section 14A(b)(2) requires only that the golden parachute arrangements have been subject to a prior shareholder vote, not that such arrangements have been actually approved by shareholders), provided that the previously included disclosure related to the same golden parachute arrangements. Therefore, a company seeking to take advantage of the exception to the shareholder advisory vote on golden parachutes requirement would have to provide disclosure in its annual meeting proxy statement about its change in control arrangements using the disclosure requirements of new Item 402(t) rather than the more general requirements of Item 402(j) (which would continue to apply to other severance arrangements).

Section 14A(b)(1) requires disclosure of any agreements or understandings between the soliciting person and any named executive officer of the issuer or any named executive officer of the acquiring company, if the soliciting person is not the acquiring issuer. When a target issuer conducts a proxy or consent solicitation to approve a merger or similar transaction, golden parachute compensation agreements or understandings between the acquiring issuer and the named executive officers of the target issuer are not within the scope of disclosure required by Section 14A(b)(1), and thus a shareholder vote to approve the arrangements is not required under Section 14A(b)(2). Therefore, the SEC has proposed Rule 14a-21(c) to require a shareholder advisory vote only on the golden parachute compensation agreements for which Section 14A(b)(1) requires disclosure and Section 14A(b)(2) requires a shareholder vote.

Proposed Item 402(t) of Regulation S-K would require disclosure of compensation agreements or understandings between the acquiring issuer and the named executive officers of the target issuer, as well as the arrangements for which Section 14A(b)(1) requires disclosure, in order to require disclosure of the full scope of golden parachute compensation applicable to the transaction, but a separate advisory vote would only be required concerning agreements and understandings described pursuant to Section 14A(b)(1). The SEC believes that, even though agreements and understandings between the acquiring issuer and the named executive officers of the target issuer would not be subject to the shareholder vote, this disclosure would be informative to shareholder voting decisions.

Under the proposed rules, companies providing for a shareholder vote on new arrangements or revised terms would provide two separate tables under new Item 402(t) in merger proxy statements. One table would disclose all golden parachute compensation, including both arrangements and amounts previously disclosed and subject to a say-on-pay vote and the new arrangements or revised terms. The second table would disclose only the new arrangements or revised terms subject to the vote, so that shareholders can clearly see what is subject to the shareholder vote.

Even though a shareholder vote may not be implicated in all change in control transactions, the SEC is requiring that Item 402(t) disclosure be included in the applicable document used in connection with, among other things, mergers, going-private transactions and third-party tender offers. In the case of a third-party tender offer, the information is only required to be included to the extent the bidder has made a reasonable inquiry and has knowledge of such arrangements. The SEC is also proposing that disclosure will not be required where the target or subject company is a foreign private issuer. The new CD&A disclosure required under Item 402, as proposed, would only relate to issuers who are already public companies and have conducted a prior shareholder vote on executive compensation and would not apply to issuers making an initial filing on Form S-1. Specifically, the new disclosure relating to golden parachute arrangements will be required in:

- Proxy or consent solicitation materials seeking shareholder approval for any acquisition, merger, consolidation or sale of substantially all of a company's assets.
- Information statements filed pursuant to Regulation 14C.
- Proxy or consent solicitation statements not containing merger proposals but requiring disclosure of information under Item 14 of Schedule 14A pursuant to Note A, such as approval for issuance of shares to conduct a merger transaction.
- Registration statements on Forms S-4 and F-4 containing disclosure relating to mergers and similar transactions.
- Going private transaction on Schedule 13E-3 (except where the target or subject company is a foreign private issuer).
- Third-party tender offers on Schedule TO and Schedule 14D-9.

The SEC is seeking public input on whether the Item 402(t) disclosure requirements should apply only in the context of an extraordinary transaction, as proposed. The SEC is also seeking input on whether Item 402(j) of Regulation S-K should be amended to cover the matters required by Section 14A(b)(1) that are not otherwise required by that Item, instead of adopting proposed Item 402(t).

Institutional Investment Manager Reporting of Votes

The SEC also proposed rules that would require institutional investment managers to annually (not later than August 31 of each year, for the twelve months ended June 30) file with the SEC their votes on say-on-pay, say-on-frequency, and "golden parachute" arrangements. The proposed rule applies to managers that currently have 13F reporting obligations because they have investment discretion with respect to at least $100 million in reportable securities. Specifically, any person who is an institutional investment manager (defined in the Exchange Act Section 13(f)(6)(A)) and required to file reports under Section 13(f) of the Exchange Act would be required on Form N-PX (which is currently used only by investment companies) "(1) for each shareholder vote pursuant to Sections 14A(a) and (b) of the Exchange Act (2) with respect to which the manager … had or shared the power to vote, or to direct the voting of, (3) any security", to identify securities voted, describe the executive compensation matters voted on, disclose the number of shares over which the manager held voting power and the number of shares voted, and indicate how the manager voted. Although the proposed rule encompasses all 13F filers, reports would be required only by the investment manager with "voting power" and not necessarily investment discretion.

Considerations for the 2011 Proxy Season

Because both the initial say-on-pay vote and the initial say-on-frequency vote must be included in proxy statements relating to an issuer's first annual or other shareholder meeting occurring on or after January 21, 2011, any preliminary or definitive proxy statements for meetings taking place on or after January 21, 2011 must include separate resolutions for shareholders to approve executive compensation and the

frequency of say-on-pay votes regardless of whether the SEC has adopted rules to implement say-on-pay by that time. Therefore, the say-on-pay regime will be effective for the upcoming proxy season. To prepare for the this, companies should begin an internal review of their executive compensation programs to identify any arrangements that may be considered poor pay practices and to determine whether any proactive steps are warranted. In some cases, engaging in a dialogue with major shareholders with respect to their views on the company's executive compensation practices may be appropriate and helpful. With respect to executive compensation disclosure, executive summary sections will become effective investor communication tools for many companies wishing to highlight the principle aspects of their executive compensation programs to their shareholders. The best CD&A disclosures will focus on links between pay and performance, outline any risk mitigating features of executive compensation programs, and explain any aspects of compensation policies that may be unique to the company. Boards should consider the preferred frequency of say-on-pay votes taking into account the general structure of the company's executive compensation programs cycle (i.e., long-term vs. short-term) in order to be prepared to make a recommendation on say-on-frequency to shareholders.

In its proposal, the SEC did not exercise its statutory authority to exempt smaller reporting companies from the rules. Because smaller reporting companies are subject to scaled disclosure requirements and are not required to include a CD&A, their shareholders would vote to approve the compensation of the named executive officers as disclosed under Items 402(m) through 402(q) of Regulation S-K.

Finally, to facilitate compliance, the SEC outlines some transitional rules with respect to companies holding meetings on or after January 21, 2011, but which will have to file their proxy materials before the SEC has finalized its rules. Until the SEC takes final action, it will not object if (1) issuers do not file preliminary proxy statements if the only matters that would require the filing are the votes under new Section 14A(a) and (2) if the form of proxy for a say-on-frequency vote provides means whereby the person solicited is afforded an opportunity to specify by boxes a choice among the proposed four choices (i.e., every year, every two years, every three years or abstain).

This Client Alert is provided for your convenience and does not constitute legal advice. It is prepared for the general information of our clients and other interested persons. This Client Alert should not be acted upon in any specific situation without appropriate legal advice and it may include links to websites other than the White & Case website.

White & Case has no responsibility for any websites other than its own and does not endorse the information, content, presentation or accuracy, or make any warranty, express or implied, regarding any other website.

This Client Alert is protected by copyright. Material appearing herein may be reproduced or translated with appropriate credit.

In this alert, White & Case means the international legal practice comprising White & Case LLP, a New York State registered limited liability partnership, White & Case LLP, a limited liability partnership incorporated under English law and all other affiliated partnerships, companies and entities.

NYC/1110_CM_A_05880_v2