

**CHEAT SHEET: THE LATEST DEVELOPMENTS IN GOVERNANCE AND COMPENSATION**

- **Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act” or the “Act”).** The Act, enacted on 7/21/2010, includes the following *corporate governance and compensation reforms*:
    - Say-on-Pay, Frequency Vote and Say on Parachutes.\* These advisory votes are required for virtually all public companies starting with their 2011 annual meeting, as discussed below. (§951)
    - Broker Discretionary Voting. For shareholder votes of *all public companies*, brokers must be prohibited from voting shares without instructions from the beneficial owner on compensation-related matters (including Say-on-Pay). (§957) The NYSE intends to amend its rules accordingly, for any shareholders meeting after 7/21/2010. *Proposed SEC rules expected at a future date.*
    - Disclosure of Pay vs. Performance. For *all public companies*, the SEC must adopt rules requiring in the proxy statement a clear description of any compensation required to be disclosed under Item 402 of Regulation S-K, including information on the relationship of executive compensation to the financial performance of the issuer, possibly a chart. (§953) *Proposed SEC rules expected Jan.-June 2012; final rules expected July-Dec. 2012.*
    - Pay Equity-Related Disclosure. For *all public companies*, the SEC must adopt rules requiring in the proxy statement a comparison (including the ratio) of (1) the median annual total compensation of all employees, excluding the CEO, with (2) the annual total compensation of the CEO. (§953) *Proposed SEC rules expected Jan.-June 2012; final rules expected July-Dec. 2012.*
    - Hedging Disclosure. For *all public companies*, the SEC must adopt rules requiring in the proxy statement disclosure of whether the company permits hedging in the issuer’s equity securities by employees or directors. (§955) *Proposed SEC rules expected Jan.-June 2012; final rules expected July-Dec. 2012.*
    - Disclosure about Chairman/CEO Structure. For *all public companies*, the SEC must adopt rules by 1/17/2011 requiring in the proxy statement disclosure of why the company did or did not separate the positions of chair and CEO. (§972)
    - Independence Standards for Compensation Committee.\* For *listed companies*, the Act requires the SEC by 7/16/2011 to adopt rules directing the national securities exchanges and associations to establish stricter independence standards for compensation committee members based on specified factors. (§952) *Proposed SEC rules (Release No. 33-9199) issued 3/30/11; final rules expected Jan.-June 2012.*
    - Standards for Compensation Committee Advisors.\* For *listed companies*, the Act requires the SEC by 7/16/2011 to adopt rules directing exchanges to authorize comp. committees to hire consultants and counsel and setting independence standards for advisors. Listed companies must also disclose in proxy statement for annual meeting on or after 7/21/2011 whether the comp. committee retained a consultant, whether the work of the consultant raised any conflict of interest and how it is being addressed. (§952) *Proposed SEC rules (Release No. 33-9199) issued 3/30/11; final rules expected Jan.-June 2012.*
    - Clawback Policy. For *listed companies*, the Act requires the SEC to adopt rules directing the national securities exchanges and associations to require listed companies to develop and implement a policy requiring the recovery of incentive compensation (including stock options) from current and former officers during the three years before an accounting restatement, to the extent the compensation was based on erroneous financial data. (§954) *Proposed SEC rules expected Jan.-June 2012; final rules expected July-Dec. 2012.*
    - Compensation Structures of Financial Institutions. For *covered financial institutions*, U.S. regulatory agencies must jointly adopt rules requiring compensation disclosures to regulators and prohibiting of risky compensation structures or excessive compensation. Rules have been approved by SEC and FDIC; awaiting approval by other agencies. (§956)
    - Proxy Access. See discussion below of Rule 14a-8, permitting shareholder proposals regarding proxy access; Rule 14a-11, facilitated by the Dodd-Frank Act, was struck down by D.C. Circuit Court. (§972)
- \* For these provisions, the SEC or national securities exchange or association is authorized under the Dodd-Frank Act to exempt a class of issuers based on size of the issuer or other factors.
- **SEC Final Rules on Say-on-Pay, Frequency Vote and Say-on-Parachutes – (Release No. 33-9178), issued 1/25/11 (effective 4/4/2011; Say-on-Parachute, parachute disclosure rules effective 4/25/2011)**
    - Section 951 of the Act requires a shareholder advisory vote on compensation (Say-on-Pay) every one, two or three years, effective with the first annual meeting on or after 1/21/2011.
    - The rules exempt smaller reporting companies (public float less than \$75 million) from the Say-on-Pay and frequency vote requirements until the first annual meeting on or after 1/21/2013.

- **Say-on-Pay, Frequency Vote and Say-on-Parachutes, cont.**
  - The Say-on-Pay vote is non-binding – it does not overrule any board decision or affect fiduciary duties.
  - Under Rule 14a-21(a), no specific language is required for the Say-on-Pay resolution (example language is included). Vote must be for approval of the compensation of named executive officers disclosed under Item 402 of Reg. S-K (includes CD&A, compensation tables and related disclosures).
  - The rules require proxy disclosure in CD&A to address how the board's compensation policies and decisions have taken into account the results of the most recent Say-on-Pay vote.
  - The frequency vote must be held at the first annual meeting on or after 1/21/2011, and at least once every six years thereafter.
  - Under Rule 14a-21(b), the frequency vote must offer shareholders four choices: annual, biennial or triennial Say-on-Pay votes, or "abstain". The frequency vote is non-binding.
  - The company must report on whether the board will follow the shareholders' recommendation in a subsequent Form 8-K, due 150 days after the annual meeting (but at least 60 days before the deadline for shareholder proposals for the next annual meeting). If the board does not follow the shareholders' recommendation on frequency that received a **majority** vote, then shareholders will be allowed to introduce shareholder resolutions at future annual meetings under Rule 14a-8 to change the frequency, and these resolutions may not be excluded from management's proxy statement.
  - The Say-on-Pay and frequency votes do not trigger a preliminary proxy statement filing requirement under amended Rule 14a-6.
  - New Item 402(t) of Reg. S-K requires disclosure of golden parachute compensation, which must be included in proxy statements to approve mergers, sales of assets and similar transactions (optional for annual meeting proxy statements) starting April 25, 2011. The table is also required in similar documents, such as tender offer information statements. Item 402(t) requires a table disclosing elements of compensation relating to the transaction for named executive officers, and a narrative description.
  - In connection with any shareholders meeting at which shareholder approval of a merger, sale of assets or similar transaction is sought, Rule 14a-21(c) requires Say-on-Parachutes – a shareholder advisory vote on the parachute compensation disclosed in the proxy statement under Item 402(t).
- **Amendments to Rule 14a-8 to Permit Shareholder Proposals on Proxy Access (Release No. 33-9136), effective September 14, 2011 (confirmed in Release No. 33-9259)**
  - The release amends Rule 14a-8(i)(8) to permit shareholder proposals to allow proxy access. The amendment was stayed by the SEC, along with Rule 14a-11, which would have required proxy access for all public companies. After a successful court challenge in July 2011 that struck down Rule 14a-11, the SEC confirmed that the stay on the Rule 14a-8 amendments expired.
  - Under prior Rule 14a-8(i)(8), the issuer had the general ability to exclude shareholder proposals relating to board nominations or elections or related procedures. As amended, this provision has been narrowed, allowing exclusion of a proposal to disqualify or include a specific nominee; remove a director; question the competence, etc. of an individual; or otherwise affect the election outcome.
  - Due to the narrowed exclusion, Rule 14a-8 now permits shareholder proposals to amend the bylaws, or request that the board consider amending the bylaws, to facilitate director nominations by shareholders. Under the principle of "private ordering," the proposal need not follow uniform proxy access requirements, such as the requirement under Rule 14a-11 that the nominating shareholders have held 3% of the company's voting securities for 3 years.
  - Under Rule 14a-8, a proposing shareholder must have continuously held at least \$2,000 in market value, or 1% of the company's outstanding voting securities, for at least one year by the date the proposal is submitted, and must continue to hold those securities through the date of the shareholders meeting.
  - The shareholder must submit the proposal by the deadline (generally stated in the proxy statement); and the company may exclude the proposal if there are procedural deficiencies, or may apply to the SEC to exclude the proposal if it fits within the exclusionary categories in Rule 14a-8(i).

*The descriptions above offer only a general overview of complex legal topics. These materials are not intended as a substitute for legal, financial or tax advice and should not be relied upon as such.*

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