

SEC Adopts Final Say-on-Pay and Golden Parachute Rules

On January 25, 2011, in a 3-2 vote, the SEC adopted [final rules](#) implementing the provisions of the Dodd-Frank Act that require U.S. public companies to conduct separate shareholder advisory votes on:

- executive pay (“**say-on-pay**”);
- frequency of the say-on-pay vote (the “**frequency vote**”); and
- executive compensation in connection with M&A transactions that is presented for shareholder approval (“**say-on-golden parachutes**”).

The final rules substantially reflect the proposed rules issued on October 18, 2010. For a summary of the proposed rules, [click here](#). The principal clarifications and modifications are noted below. The final rules become effective 60 days following publication in the *Federal Register*, except as otherwise discussed below.

Say-on-Pay and Frequency Votes

Annual Meetings Only. Say-on-pay and frequency votes are required only with respect to annual meetings of shareholders in which proxies are being solicited in order to elect directors, or a special meeting in lieu thereof.

Say-on-Pay and Frequency Vote Resolutions. While the final rules do not require specific language or form for the say-on-pay resolution, a company must indicate that the say-on-pay vote is a vote to approve all executive compensation disclosed pursuant to Item 402 of Regulation S-K. The final rules provide 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.” No specific language or form is required for the frequency vote, and no example was provided.

Disclosure of Impact of Most Recent Say-on-Pay Vote in the CD&A. Companies are required to discuss in their CD&A whether and, if so, to what extent they have taken into account the results of only their most recent say-on-pay vote required by the Dodd-Frank Act or the Emergency Economic Stabilization Act of 2008 (“EESA”) in determining compensation policies and decisions. Consideration of any other previous say-on-pay votes should be discussed to the extent material in making compensation decisions. The SEC staff has advised that companies that conducted a say-on-pay vote in 2010 because of EESA will be required to disclose the impact of this vote in their 2011 proxy statement if it is filed after the effective date of the rules.

Response to Frequency Vote. Companies must disclose their decisions as to how often they will hold say-on-pay votes going forward either in the Form 8-K disclosing their annual meeting voting results or in an amendment to that Form 8-K. If companies choose the latter, the amendment to the Form 8-K must be filed no later than 150 calendar days following their annual meetings and at least 60 calendar days before their deadlines for submission of shareholder proposals. The original proposal would have required that disclosure be made in the periodic filing for the same calendar quarter as the annual meeting. This extra bit of breathing room will generally mean that calendar year companies can defer their decision on this point until the fall of 2011.

Disclosure of Effect of Vote and Frequency. As proposed, companies must disclose in their proxy statements that they are providing separate say-on-pay and frequency votes, and must disclose the general nature and effect of the votes, such as indicating that the votes are non-binding. The final rules added a new requirement that companies disclose in their annual proxy statements the frequency with

which they will conduct say-on-pay votes and when their next say-on-pay vote will be held. However, this disclosure will not be required until after this year's initial votes.

Some Shareholder Proposals May Be Excluded Under Substantial Implementation. If a company adopts the frequency that received a majority (not a plurality) of votes cast in the most recent frequency vote, the company may exclude any shareholder proposals that provide for a say-on-pay vote, seek future say-on-pay votes or relate to the frequency of say-on-pay votes in certain circumstances. For this purpose, a say-on-pay shareholder proposal is an advisory vote on all elements of Item 402 executive compensation, and not on different aspects of executive compensation, limiting the utility of this rule. A company will not be able to take advantage of this exclusion basis if none of its frequency intervals receives a majority of the votes cast.

Uninstructed Proxies May Be Voted for Recommended Frequency. Companies may vote any uninstructed proxies in favor of management's recommended frequency if three requirements are met: (1) the company has made a recommendation regarding frequency, (2) the proxy card includes an option to abstain from voting, and (3) the proxy card includes a statement, in bold, indicating how uninstructed proxies would be voted. An uninstructed proxy is one that is signed and returned by a shareholder without any indication as to the shareholder's vote.

Preliminary Proxy Not Required. The final rules confirm that say-on-pay and frequency votes will not trigger a requirement to file a preliminary proxy statement. In addition, the final rules provide that other management proposals for advisory votes on executive compensation will not require a preliminary proxy statement.

No Transitional Relief for Newly Public Companies. Under the final rules, a newly public company is required to provide say-on-pay and frequency votes in the proxy statement for its first annual meeting after its initial public offering. The proposed rules had invited comment on whether a new issuer should be exempt from both votes until the annual meeting for the year as disclosed in its registration statement. The absence of relief for newly public companies was one of the cited reasons for the dissenting votes of Commissioners Casey and Paredes.

Exemption for Foreign Private Issuers. The final rules confirm that foreign private issuers are not required to conduct say-on-pay and frequency votes.

Two-Year Exemption for Smaller Reporting Companies. Smaller reporting companies are not required to comply with the say-on-pay and frequency vote rules until January 21, 2013. However, they are required to comply with the golden parachute rules upon effectiveness of those rules.

Say-on-Pay and Frequency Vote Results

Monsanto, Inc. held its annual meeting on January 25, 2011, the first S&P 500 company to have Dodd-Frank mandated say-on-pay and frequency votes. While Monsanto recommended a triennial frequency, a majority (approximately 62%) of its shareholders voted in favor of an annual vote, and Monsanto has already announced that it will adopt an annual frequency. In addition, Monsanto's shareholders approved the compensation of its named executive officers with a vote of approximately 66% "For" the say-on-pay resolution.

Upcoming annual meetings include Costco (January 27), Air Products & Chemicals (January 27), Emerson Electric (February 1), Accenture (February 3) and Tyson Foods (February 4).

Say-on-Golden Parachutes

Golden Parachute Rules Effective April 25, 2011. Issuers, including smaller reporting companies, must comply with the golden parachute disclosure and voting requirements for initial filings on or after April 25, 2011.

Scope of Golden Parachute Disclosure. “Golden parachutes” are broadly defined and include all agreements and understandings between the target or the acquirer and each named executive officer of the target or the acquirer that relate to an M&A transaction. Golden parachute disclosure is required only for executive compensation that is based on or otherwise relates to the applicable transaction. The final rules confirm that golden parachute disclosure is required to be provided in both tabular (Item 402(t) table) and narrative formats, and must include all arrangements whether or not they discriminate in scope, terms or operation in favor of executive officers, and without a *de minimis* exception of any kind. Golden parachutes do not include certain types of compensation that are deemed not related to the transaction, such as previously vested equity awards, deferred compensation and compensation from *bona fide* post-transaction employment agreements.

Golden Parachute Calculation. The company stock price used to calculate compensation disclosed in the Item 402(t) table in a transactional filing will be the deal price, if known. If not, it will be the average closing price of the company’s stock over the first five business days following the public announcement of the transaction. If the Item 402(t) table is provided in a proxy statement for an annual meeting, the company stock price used to calculate the compensation disclosed is the closing price of the company’s stock on the last business day of the company’s last completed fiscal year.

Golden Parachute Disclosure Not Required by Bidders in Third-Party Tender Offers. Bidders in third-party tender offers are not required to provide golden parachute disclosure on Schedule TO, if the third-party tender offer is not also a Rule 13e-3 going-private transaction.

Scope of Say-on-Golden Parachute Vote. The final rules confirm that if, as is often the case, the target company is the soliciting person, then agreements or understandings between the acquirer and the named executive officers of the target, while required to be disclosed, are not subject to the say-on-golden parachute vote.

Say-on-Golden Parachute Vote May Be Incorporated in Annual Meeting Say-on-Pay Vote. As proposed, companies are not required to conduct say-on-golden parachute votes if the golden parachute arrangements were already voted upon in an annual say-on-pay vote and have not been modified. Changes to golden parachute arrangements that decrease the total compensation do not require a subsequent shareholder vote. In our view, there continues to be little advantage to including the necessary enhanced golden parachute disclosure in an annual proxy statement.

Say-on-Golden Parachute Vote Required Only Where Seeking Transactional Approval. Golden parachute votes are only required in transactional filings where shareholders are being asked to approve the transaction, and not where the shareholders vote on a related issue, such as a vote to increase the number of authorized shares or issue more than 20% of the shares outstanding to facilitate a merger.

Additional Dodd-Frank Compensation-Related Rulemaking

The SEC’s online rulemaking schedule for additional Dodd-Frank compensation-related rules, such as clawbacks and its disclosure of pay-versus-performance, the pay ratio of CEO compensation to employee compensation and any hedging policy for employees and directors, has been delayed from between April and July 2011 to between August and December 2011. It is possible that these rules may not be in effect for the 2012 proxy season.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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