

“Say on Pay” Now a Reality for TARP Participants

DAVIS POLK & WARDWELL

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Media and public attention surrounding the American Recovery and Reinvestment Act of 2009, enacted on February 17, 2009 and commonly referred to as the stimulus bill, has typically focused on the law’s restrictions on the amounts and forms of compensation payable to executives of TARP participants.¹ An important provision of the stimulus bill that has not as yet received much notice, but is now a reality for all institutions that receive or have received government assistance under TARP, is the requirement that such institutions permit their shareholders to vote on executive compensation – a so-called “say on pay” vote.

Shareholder proposals advocating for say on pay have been a recent priority item on shareholders’ governance agenda, with reports indicating that as many as 100 proposals have been submitted to public companies for the 2009 season. Support for the approximately 70 proposals submitted to shareholders in the 2008 season averaged approximately 42%, with ten proposals reported as receiving majority support from shareholders. Although say on pay has not been widely adopted by companies, 18 companies to date have agreed to institute company proposals seeking a say on pay vote in their proxy statements. Six of these companies have already included such a company proposal in their proxy statements, with shareholder support for the companies’ executive compensation ranging from 62.5% to 98.7%.

The new SEC leadership has publicly expressed its support of adopting say on pay for all companies outside the context of the stimulus bill. Mary Schapiro, Chairman of the SEC, stated in a recent speech that “giving shareholders a greater say on . . . how company executives are paid” is on the SEC’s agenda. Further, SEC Commissioner Elisse B. Walter in recent remarks stated that she believes say on pay can help restore investor trust, and she encouraged more companies to voluntarily adopt say on pay.

Stimulus Bill Requires Say on Pay, But Timing of Implementation Originally Unclear

The stimulus bill requires that the shareholders of any institution that has received or will receive financial assistance under TARP be provided with an annual non-binding say on pay vote on executive compensation each year during the period in which any obligation arising from such financial assistance remains outstanding. In its annual meeting proxy statement, each institution must provide a separate shareholder vote to approve the compensation of the institution’s executives as disclosed pursuant to the SEC’s compensation disclosure rules, which include the compensation discussion and analysis, the compensation tables and related narrative.

The stimulus bill called for the SEC to issue final regulations regarding this say on pay provision within one year after the date of the bill’s enactment. The legislation did not indicate whether the say on pay provision was effective immediately upon its enactment, or would only become effective after the SEC issued these regulations.

The stimulus bill also makes clear that this shareholder vote is not intended to be binding upon an institution’s board of directors and may not be construed as overruling any board decision, nor does it create or imply any additional fiduciary duty of the board.

¹ Davis Polk has separately prepared a client memorandum entitled [Compensation Provisions in the American Recovery and Reinvestment Act of 2009](#), dated February 17, 2009, regarding these compensation restrictions.

Senator Dodd’s Letter to the SEC – Intent to Make Say on Pay Immediately Effective

On February 20, 2009, Senator Christopher Dodd, the author of the executive compensation restrictions in the stimulus bill, issued a letter to Chairman Schapiro. He stated that he intended for the say on pay provision under the stimulus bill to be effective immediately upon its enactment. His intent was for the provision to apply to all proxy statements filed after February 17, 2009 (the date of enactment of the stimulus bill), except for definitive proxy statements filed after such date for which preliminary proxy statements had been filed before such date. Senator Dodd requested that the SEC provide clarifying guidance as soon as practicable.

SEC Guidance – Preliminary Proxy Required for Company Proposals

Yesterday evening, the SEC issued guidance with regard to the say on pay provision as requested by Senator Dodd. While this guidance is limited in its scope to those institutions subject to the stimulus bill, it may foreshadow future SEC rulemaking:

- » ***Effective Now:*** Unless a company has filed a preliminary or definitive proxy statement on or before February 17, 2009, it seems clear that if a company is required to comply with the stimulus bill provision by including a say on pay proposal, it must do so in this year’s annual meeting proxy statement.
- » ***Preliminary Proxy Statement Required:*** Consistent with existing rules, when a company say on pay proposal is included in a proxy statement, the company is required to file a preliminary proxy statement before filing its definitive statement. If the company faces special circumstances, it may request acceleration of the ten-day review period by contacting the Assistant Director of the Office of the Division of Corporation Finance at the SEC who reviews the company’s filings to discuss possible acceleration of the review period. The Assistant Director for companies in the Financial Services industry is Todd Schiffman, 202-551-3770. For a list of all Assistant Directors, click [here](#).
- » ***Required in Proxy Statements for Certain Meetings:*** A separate shareholder vote on executive compensation is only required for the annual meeting of shareholders for which proxies will be solicited for the election of directors or a special meeting in lieu of such annual meeting.
- » ***No Specific Guidance on Proposal Language:*** The SEC did not provide any guidance on the particular language a company should use for its say on pay proposal.
- » ***Company Proposals are Traditionally a “Routine” Matter Under NYSE Broker Discretionary Vote Rules:*** Generally, the NYSE views a company proposal supported by the company’s board as a routine matter that NYSE member brokers can vote on at their discretion without specific instruction. The NYSE rules regarding broker voting govern the actions of NYSE member brokers without regard to whether a company is listed on the NYSE or elsewhere.

The guidance described above was provided in the form of Compliance and Disclosure Interpretations and not regulations. Under the stimulus bill, the SEC is still required to issue final regulations regarding say on pay within one year after the date of the stimulus bill’s enactment. We expect that such regulations will be subject to public notice and comment.

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For the text of the SEC guidance described above, click [here](#).

This memorandum is a summary for general information only. It is not a full analysis of the matters presented and should not be relied upon as legal advice. To ensure compliance with requirements imposed by the Internal Revenue Service, we inform you that the discussion of U.S. federal tax issues contained in this memorandum is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

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

Beverly Fanger Chase, Partner
212-450-4383 | beverly.chase@dpw.com

Ning Chiu, Counsel
212-450-4908 | ning.chiu@dpw.com

Edmond T. FitzGerald, Partner
212-450-4644 | edmond.fitzgerald@dpw.com

Kyoko Takahashi Lin, Partner
212-450-4706 | kyoko.lin@dpw.com

Jean M. McLoughlin, Partner
212-450-4416 | jean.mcloughlin@dpw.com

Barbara Nims, Partner
212-450-4591 | barbara.nims@dpw.com