

**CRAVATH, SWAINE & MOORE LLP**

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**Corporate Governance  
Developments: Getting Ready for New  
Disclosure Requirements, Proxy Access &  
'Say-on-Pay'**

October 2, 2009

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# Warning

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- **The material discussed in these slides is for illustrative purposes only and does not purport to reflect appropriate or inappropriate disclosure or procedures that should be followed or inquiries that should be made, if any, in any particular situation.**

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# **A Brief Look at the SEC Landscape**

# 2009 Commission

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- **Chairman Mary Schapiro**
  - Joined in January 2009
  - Career regulator
  - Former CEO of FINRA
  - Former Chairman of CFTC
  - Former SEC commissioner
- **Democrats:** Elisse Walter and Luis Aguilar
- **Republicans:** Kathy Casey and Troy Paredes

# SEC in 2009

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- **Schapiro themes**
  - Enhanced enforcement
  - **Corporate accountability**
  - Improving market regulation
- **Commitment, direction and resolve**
  - 3-2 votes
- **Responses to Madoff scandal**
  - Inspector General's Report issued in September 2009
  - Series of SEC reforms

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# Corporate Accountability in 2009

# U.S. Legislative Focus on Corporate Accountability

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- Senate
  - Schumer: *Shareholders Bill of Rights Act of 2009*
- House
  - Peters: *Shareholder Empowerment Act of 2009*
  - Frank: *Corporate and Financial Institutions Fairness Act of 2009*
- Obama Administration
  - *Financial Regulatory Reform* white paper
  - *Investor Protection Act of 2009*
- Expand SEC authority to cover all companies

# Accountability

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## Step 1: Disclosure

- Corporate governance and risk
- Executive compensation

“ . . . . but even disclosure only takes us so far”

*Mary Schapiro, June 10, 2009*

## Step 2: Proxy Access

- Shareholder nominees in company proxy

# Accountability

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**“Proxy access is about making boards more accountable for the risks undertaken by the companies they manage.”**

*Mary Schapiro, April 6, 2009*

**“I believe the meaningful ability of shareholders to nominate directors is intricately linked to the ability of shareholders to hold directors accountable for their compensation decisions”**

*Mary Schapiro, June 10, 2009*

# 1. Corporate Governance

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- **SEC disclosure proposals** (July 1, 2009)
  - Director experience and qualifications
    - Specific to your company
    - Including committees
  - Board leadership structure
    - Separate chair?
    - Why your structure is best for your company
  - Board's role in risk oversight process

# 1. Corporate Governance

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- **Legislative proposals** (via listing standards)
  - Independent chair (Schumer and Peters)
    - Independence includes not a former officer
  - Annual election of directors (Schumer)
  - Majority voting (Schumer and Peters)
  - Risk committee (Schumer)

## 2. Compensation

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- **SEC disclosure proposals** (July 1, 2009)
  - Incentives and risk
    - For employees generally
    - Executive officers already covered by CD&A
  - Compensation consultants
    - Disclosure if services provided to management
  - Stock option and restricted stock expense
    - Move to grant date fair value from FAS 123R

## 2. Compensation

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- **Legislative proposals**
  - Frank: Compensation committee provisions
    - Independent consultants and lawyers
    - Independence (similar to audit committees)
  - Frank: “To reduce perverse incentives”
    - Prohibit arrangements if encourage “inappropriate risks”
    - Applies to all financial institutions
  - Durbin: limit deductions to 100x average comp

## 2. Compensation

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- **Say-on-Pay**

- Non-binding shareholder vote on executive compensation disclosed in CD&A and the Summary Compensation Table
- Shareholder proposals permitted today
  - Vote usually follows if proposal passes
- Required of TARP companies
- Schumer, Peters and Obama Administration bills would require vote at all public companies

## 3. Director Elections

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- **NYSE Rule 452 amendments**
  - Ending broker discretionary voting of uninstructed shares in director elections
  - Approved 3-2 by SEC
  - Effective January 1, 2010
- **Proxy access**
  - Allow shareholders to nominate directors using company proxy
  - Legislative mandate (Frank, Schumer)

# History of Proxy Access

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- **Long history at SEC**
- **Increasingly intense over past decade**
  - SEC proposals in 2003 and 2007
  - Congressional interest and new Commissioners in 2008
  - Focus for Chairman Schapiro's first year
  - June 2009 proposal
    - Issued by 3-2 vote
    - Comment period closed August 17, 2009

# June 2009 Proxy Access Proposal

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- **First prong: New rule 14a-11**
  - Federal right of access
    - Cannot be superseded by company bylaw
  - Available to 1% shareholders (or group) for larger companies
  - Nominate 25% of directors
- **Second prong: Revise rule 14a-8(i)(8)**
  - Permit shareholders to submit proxy access bylaw proposals

# June 2009 Proxy Access Proposal

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- **Divisiveness reflected in comment letters**
  - In favor:
    - Would enhance board accountability
    - Would restore balance between executive suite and shareholders as owners of the company
    - Would increase investor confidence
  - Opposed:
    - Would wrongly preempt state law and private ordering
    - Would greatly drain resources from corporation and its board without corresponding benefits
    - Would promote special interests at expense of long-term value of the company

# June 2009 Proxy Access Proposal

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## SEC plans to move forward this fall

- Likelihood of 3-2 vote
  - But which 3?

## ● Timing and effectiveness

- Both rules, or just 14a-8(i)(8)?
- Impact on 2010 proxy season?

# Looking Ahead

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- **Which investors will use proxy access?**
- **When will there be no votes on “say on pay”?**
- **When will there be “no vote” campaigns?**
- **Impact of access on shareholder relations**
- **Impact of access on boards and directors**

# Managing Your Corporate Governance Profile

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- **Advising companies this fall**
  - Know yourself
  - Avoid being “low hanging fruit”
    - Corporate governance practices
    - Executive compensation practices
    - Communications with shareholders
    - Activist “hot buttons”

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# Thank You