

# Meridian Client Update

September 27, 2010

## Effective Date for Many Executive Compensation Provisions Under Dodd-Frank Act Will Be Late 2011 or Early 2012

**The Securities and Exchange Commission (SEC) has given companies an early holiday gift by signaling that most of the executive compensation/corporate governance provisions under the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) will not be in effect for the majority of the 2011 proxy season.**

On September 19, 2010, the SEC announced a proposed rulemaking schedule under the Dodd-Frank Act. The quick take away is that, **except for say-on-pay**, none of the executive compensation/corporate governance provisions will be in effect until after most companies with December 31 year-ends have filed their 2011 proxy. Certain provisions may take effect mid to late next year; however, it is certainly conceivable that some provisions will not take effect until 2012.

*It is important to note that the SEC is not obligated to follow its planned rulemaking schedule. The SEC's rulemaking priorities may change over time resulting in delays (or, in the less likely event, acceleration) in its rulemaking schedule.*

### Say on Pay Provisions

**Summary of Provisions.** The Dodd-Frank Act grants shareholders of a public company the right to a non-binding vote on the company's executive pay disclosures and, in certain circumstances, the right to a non-binding vote on the company's golden parachute agreements. In addition, shareholders are granted the right to determine the frequency of shareholder voting on executive pay.

**Proposed Rulemaking Calendar.** The SEC expects to issue proposed rules on say on pay provisions sometime during the fourth quarter of 2010 and expects to issue final rules sometime during the first quarter of 2011. Presumably these rules will also cover the disclosure requirement relating to golden parachute agreements subject to a shareholder vote. **However, say on pay provisions require no SEC rulemaking to become effective.** The Dodd-Frank Act specifies the effective date of these provisions (see below).

**Effective Date under Dodd Frank Act.** The initial say on pay vote (and the initial say on frequency vote) must occur at the first shareholder meeting occurring after January 20, 2011. In addition, the say on golden parachute arrangements is effective for shareholder meetings occurring after January 20, 2011 where shareholders are asked to approve certain major corporate transactions.

**Projected Effective Date of Final Rules.** If final rules are issued during the first quarter of 2011, we expect the rules would become effective some time during the second or third quarter of 2011. However, before that time, rules are needed to explain the method by which companies are to implement the say on pay frequency vote requirement and to provide guidance as to the level of detail required for golden parachute disclosures. For companies mailing proxy materials prior to the adoption of any applicable rules, these companies will still need to comply with each of the say on pay requirements, despite the absence of regulatory guidance.

The SEC's planned rulemaking schedule will not impact say on pay's **mandated effective date** of mid-January 2011. Therefore, companies should **not** be waiting for the SEC's adoption of say-on-pay rules and should start to develop strategies to address the implementation of say on pay for the 2011 proxy season.

## Compensation Committee Standards

**Summary of Provisions.** The SEC is directed to issue rules no later than July 16, 2011 to require national securities exchanges and national securities associations to **prohibit** the listing of any company (subject to certain limited exceptions) that does not comply with compensation committee independence standards to be promulgated by the SEC. These standards relate to independence requirements for compensation committee members, the selection of compensation committee advisers, the committee's authority to retain advisers and the disclosure of conflicts involving compensation consultants.

**Proposed Rulemaking Calendar.** The SEC expects to issue proposed rules on compensation committee standards sometime during the fourth quarter of 2010 and expects to issue final rules sometime during the second quarter of 2011.

**Projected Effective Date of Final Rules.** If final rules are issued during the second quarter of 2011, we would expect the rules would become effective some time during the third or fourth quarter of 2011.

*Given the heightened concerns regarding the independence of compensation consultants, we believe some compensation committees, in advance of SEC rulemaking, may begin to implement the compensation committee standards relating to the selection of compensation consultants and other advisers.*

## Proxy Disclosures

**Summary of Provisions.** The Dodd-Frank Act directs the SEC to write rules to require companies to disclose the following matters in their proxy materials:

- **Pay versus performance.** The relationship between executive compensation actually paid and the financial performance of the company, taking into account any change in the value of shares of stock and dividends of the company and any distributions.
- **CEO pay ratio.** The ratio of the median annual total compensation of all employees to the total compensation of the chief executive officer.
- **Hedging by employees and directors.** Whether *any employee or director* is permitted to purchase financial instruments that are designed to hedge or offset any decrease in the market value of the company's equity securities granted to or otherwise held by the employee or director.

**Proposed Rulemaking Calendar.** The SEC expects to issue proposed rules on the foregoing disclosure items sometime during the second quarter of 2011.

**Projected Effective Date of Final Rules.** The SEC neither disclosed a time frame by which it expects to adopt final rules nor provided any indication as to when it may disclose a time frame. However, if the SEC sticks to its schedule and issues proposed rules during the second quarter of 2011, we would expect final rules to be adopted no earlier than the fourth quarter of 2011 with a likely effective date sometime in the first quarter of 2012.

Companies now have upwards of a year or more to determine an appropriate manner in which to develop pay data necessary to make the CEO pay ratio disclosure or to persuade Congress to repeal or significantly modify the disclosure requirement. Many companies, particularly large global firms, are very concerned that the necessary accumulation of pay data is both impractical and expensive. Until the SEC issues rules on this disclosure, we recommend that companies keep to a minimum their expenditure of time and money to determine methods to comply with the CEO pay ratio disclosure requirement.

## Mandatory Recoupment (Clawback) Provision

**Summary of Provisions.** The SEC is directed to issue rules to require national securities exchanges and national securities associations to list only those companies that implement a policy requiring the mandatory recoupment of erroneously paid incentive awards to current and former executive officers and that properly disclose such policy in proxy materials.

**Proposed Rulemaking Calendar.** The SEC expects to issue proposed rules on the foregoing disclosure items sometime during the second quarter of 2011.

**Projected Effective Date of Final Rules.** The SEC neither disclosed a time frame by which it expects to adopt final rules nor provided any indication as to when it may disclose a time frame. However, if the SEC sticks to its schedule and issues proposed rules during the second quarter of 2011, we would expect final rules to be adopted no earlier than the fourth quarter of 2011 with a likely effective date sometime in the first quarter of 2012.

*We understand that some companies have started to evaluate and even revise their clawback policies in light of the Dodd-Frank Act mandatory recoupment provisions. At the time Dodd-Frank Act was enacted, we believed it was premature to undertake any revisions to clawback policies **solely** on account of the Dodd-Frank Act and we continue to believe that is the case. We recommend that any significant revisions to clawback policies wait until the SEC issues rules on the matter.*

## Ban on Non-Directed Broker Votes

**Summary of Provisions.** Brokers are prohibited from voting shares with respect to the election of board members, executive compensation or **any other significant matters** as determined by the SEC, unless a broker receives specific voting instructions from the beneficial owner of shares held by the broker.

**Proposed Rulemaking Calendar.** The SEC expects to issue proposed rules defining “other significant matters” sometime during the second quarter of 2011.

**Projected Effective Date of Final Rules.** The SEC neither disclosed a time frame by which it expects to adopt final rules nor provided any indication as to when it may disclose a time frame. However, if the SEC sticks to its schedule and issues proposed rules during the second quarter of 2011, we would expect final rules to be adopted no earlier than the fourth quarter of 2011 with a likely effective date sometime in the first quarter of 2012.

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The **Client Update** is prepared by Meridian Compensation Partners' Technical Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-235-3605 or [dkalfen@meridiancp.com](mailto:dkalfen@meridiancp.com).

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