

# Financial Reform Act Triggers Significant New Executive Compensation Requirements

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On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act into law. The Act imposes many significant corporate governance and executive compensation requirements that are applicable to public companies.

While many of the Act's corporate governance and executive compensation provisions require further rulemaking by the SEC and the national securities exchanges, this advisory primarily identifies those provisions that will become effective upon enactment. As it is likely that some rules promulgated under the Act could take effect in time for the 2011 proxy season, we expect to provide updates on final SEC and national securities exchange rules in future advisories.

## **Mandatory Say-on-Pay**

Companies must include a separate, non-binding resolution for shareholders to vote on their named executive officers' compensation (also known as say-on-pay). This provision applies to the company's first annual or special meeting that occurs more than six months after enactment of the Act. Companies must also include in the proxy materials for this meeting an additional resolution to determine the frequency of future say-on-pay votes (either every one, two or three years) and must hold future votes on frequency at least every six years.

## **Mandatory Vote on Golden Parachute Payments**

Companies must include a separate, non-binding resolution for shareholders to vote on any compensation arrangements providing for payments to their named executive officers in connection with an acquisition, merger, consolidation or disposition of all or substantially all of the company's assets (also known as golden parachutes) unless these arrangements have already been the subject of a shareholder say-on-pay vote.

The resolution must be included in the proxy materials for any annual or special meeting that occurs more than six months after enactment of the Act at which shareholders are being asked to approve such a transaction and must be accompanied by clear proxy statement disclosure of all such compensation arrangements, including the total value of and any conditions for payment of, all golden parachute payments to each named executive officer.

## **Clawbacks**

The Act directs the SEC to issue rules requiring companies to adopt and disclose a clawback policy requiring that the company recover any incentive compensation paid to current or former executive officers during the three-year period preceding an accounting restatement that is the result of material noncompliance with financial reporting requirements. In such event, the policy must require that the company recover from current and former executive officers any incentive compensation (including options) received during the three-year period preceding restatement in excess of what otherwise would have been paid to the officer.

This is stricter than the clawback provision contained in Section 304 of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), which requires that the restatement be the result of misconduct and only applies to incentive compensation paid to the chief executive officer and chief financial officer during the preceding 12-month period.

## Financial Reform Act Triggers Significant New Executive Compensation Requirements (Continued)

### **Compensation Consultant Disclosure**

Companies must disclose in their proxy materials for any annual or special meetings that occur more than one year after enactment of the Act whether the compensation committee retained or obtained the advice of a compensation consultant, whether the work of the compensation consultant's engagement has resulted in any conflict of interest and, if so, the nature of the conflict and how it is being addressed.

In practice, this provision adds little to SEC rules adopted in 2009, which require companies to disclose compensation consultant engagements and certain conflicts of interest.

### **Small Business Exemption from Sarbanes-Oxley Section 404(b)**

The Act permanently exempts all companies that are neither "large accelerated filers" nor "accelerated filers" from the Section 404(b) requirement that a company's independent auditor attest to its internal control over financial reporting.

If you would like additional information about the issues addressed in this Advisory, please contact:

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