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Corporate & Securities Law BLOG
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House Quickly Passes Legislation to Control Executive Compensation Practices

Acting in rapid fashion, on July 31, 2009, the House of Representatives passed legislation that, if enacted, would further advance the federal government's efforts to realign executive compensation practices. As we reported in our July 22, 2009 blog, the Treasury Department released draft legislation just two weeks earlier to require (i) an annual shareholder vote to approve named executive officer compensation, (ii) a shareholder vote to approve golden parachute arrangements and (iii) enhanced compensation committee independence and authority. The House-approved legislation, which now has been referred to the Senate's Committee on Banking, Housing, and Urban Affairs, in some respects goes even further than what was originally contemplated by Treasury.

The new legislation, referred to as the Corporate and Financial Institution Compensation Fairness Act of 2009 (the "Act"), generally provides for the following:

- Advisory Shareholder Vote ("Say-On-Pay")
  - An annual shareholder vote to approve the compensation of public company named executive officers commencing with shareholder meetings occurring on or after six months after the Securities and Exchange Commission ("SEC") adopts final rules for the Act.
  - A shareholder vote to approve any golden parachute arrangements with the public company's named executive officers when there is a solicitation of shareholders to approve a corporate transaction. This will be effective for any such shareholder meetings occurring on or after six months after the SEC adopts final rules for the Act.
  - The SEC must issue final rules to implement the shareholder "Say-On-Pay" provisions within six months of the Act's enactment. The SEC may exempt certain companies, such as smaller reporting issuers, from the Say-On-Pay requirements.
- Compensation Committee Standards
  - Within nine months of the Act's enactment, the SEC must adopt rules mandating that the national stock exchanges prohibit the listing of companies that do not comply with

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enumerated compensation committee standards. The SEC may exempt certain companies, such as smaller reporting issuers, from these requirements.

- Each compensation committee member must be independent meaning, in part, that the members cannot receive compensation from the company other than pursuant to their services as a director.

- Compensation consultants or other advisors to the compensation committee must satisfy independence standards established by the SEC. Companies will have to disclose in their proxy statements whether they retained such consultants and the SEC likely will require fuller disclosures regarding a committee's use of compensation consultants.

- The Compensation Committee will expressly have the authority to retain and direct the services of compensation consultants and/or other advisors including independent legal counsel. The Committee will also receive sufficient funding from the company to compensate such advisors.

- Stricter Compensation Regulations for Financial Institutions

  - Financial institutions with assets of at least $1 billion would be prohibited from having incentive-based compensation that encourage inappropriate risks which could threaten the institution's soundness or which could seriously impact economic conditions or financial stability.

  - Covered financial institutions would be requested to disclose to their specific federal regulators the structures of their incentive-based compensation in order to facilitate a determination that such arrangements are aligned with sound risk management and do not promote undue risk taking by employees.

  - Within nine months of the Act's enactment, the applicable federal regulators would jointly prescribe regulations implementing these requirements.

Upon House passage of the Act, Treasury Secretary Geithner stated:

> "*This is a positive step forward to increase accountability and transparency in executive compensation, and to help ensure that pay encourages long-term performance, not excessive risk-taking. Improving executive compensation practices is an essential part of our broader efforts towards comprehensive regulatory reform.*"

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Given the House's expedited passage of the Act, along with the Obama Administration's endorsement of the House's actions, some form of the legislation may very well soon be enacted into law. Accordingly, as we have previously commented (see our prior blogs on July 22, 2009, July 17, 2009 and June 18, 2009), public companies and financial institutions should examine their compensation arrangements, relationships with their compensation advisors and counsel, and compensation-related disclosures in order to be properly prepared for these stricter requirements. Moreover, compensation committees should consult corporate counsel, or retain separate and independent legal counsel, to ensure that they are appropriately advised under the current environment in which compensation decisions and processes are heavily scrutinized.

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