

GOVERNANCE

2012 Proxy Season Preview

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As we near the end of 2011, public companies are beginning to look toward next year’s proxy season. Here are some observations on what to expect:

Proxy access. Just a year ago, proxy access had been formally endorsed in the Dodd-Frank Act and mandated by the SEC for all U.S. public companies. In July of this year, however, proxy access ran into a roadblock in the D.C. Circuit Court of Appeals. The court invalidated the SEC’s one-size-fits-all rule to allow shareholder access to a company’s proxy for the purpose of nominating directors on the grounds that the rule was “arbitrary and capricious.” The SEC has decided not to appeal that decision and, instead, settled for allowing the “private ordering” of proxy access procedures via shareholder proposals submitted under Rule 14a-8.

The SEC’s amendments narrowing the Rule 14a-8 director election exclusion to allow proxy access proposals recently went into effect. Reports vary, but we believe that the number of these proposals will be limited as shareholders and corporations alike test the waters. Shareholders will likely target a few troubled companies where the chances of success are higher instead of submitting such proposals at a broad swath of companies as they have in other contexts. There is also little indication of the form that these proposals will take—whether they will be binding or nonbinding, for example—although we note that binding proposals are more susceptible to challenge under Rule 14a-8 and may be difficult to construct within the confines of the rule’s 500-word limit on the resolution and supporting statement.

Say on pay. Say on pay will continue to receive top billing in 2012. The vast majority of companies have chosen to allow annual say-on-pay votes, so we will continue to see these advisory votes on the 2012 ballot. Approximately 98% of companies subject to say on pay last year received approval of their compensation packages, and we do not anticipate that trend changing significantly in 2012.

Say-on-pay votes will likely continue to serve as a proxy for shareholders’ overall satisfaction, and we expect that negative say-on-pay votes will continue to substitute for withhold campaigns against directors as a means of expressing dissatisfaction with a company. Pay/performance disconnects, poor pay practices, and poor compensation disclosure will continue to drive failed say-on-pay votes. The general political and economic climate, which has given rise to movements

such as the Occupy Wall Street protests, could also influence say-on-pay votes.

Several lawsuits have been filed against companies after failed say-on-pay votes alleging various claims, such as breach of fiduciary duties or corporate waste. We believe that these suits would be unlikely to prevail in a jurisdiction like Delaware, but until there is a broader trend of loss on such claims, these suits will continue to be filed.

Compensation committee rules. Companies should be on the lookout for the SEC’s pending rules on compensation committee independence and responsibilities and disclosures regarding compensation consultants. While the substantive rules relating to independence and responsibilities may not be in place by the 2012 proxy season, there is still a chance that the SEC will adopt its disclosure rules related to compensation consultants in time for the bulk of company proxy filings later in 2011 and early 2012. The SEC’s other rules regarding executive compensation, such as disclosure related to pay ratios, pay for performance, hedging policies, and clawbacks, will not be proposed until 2012.

Shareholder proposals. 2011 saw a lower volume of shareholder proposals, in part because say-on-pay proposals became moot. The most popular proposals were related to majority voting, corporate reports on political spending/lobbying, and board declassification. While majority voting and declassification proposals received average levels of support (approximately 60% and 73%, respectively), proposals related to political spending/lobbying reports garnered average levels of support in the 30% range. The average levels of support for all three categories increased in 2011 (although the increases were small for majority voting and political spending/lobbying reports).

Environmental, social, and governance proposals also continued to increase in number and support. Although the average level of support for such proposals (around 20%) was still below majority approval, it was nevertheless a historical high for these type of proposals. We anticipate that such shareholder proposals will continue to appear and win levels of support at or higher than in past years.