



**Asia-Pacific  
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## **Corporate Governance and Executive Compensation Issues Under the Dodd-Frank Act**

Submitted by: United States



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# Corporate Governance and Executive Compensation Issues under the Dodd-Frank Act

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## Corporate Governance and Financial Crisis

- “[The Dodd-Frank Act ] creates a new, more effective regulatory structure, fills a host of regulatory gaps, brings greater public transparency and market accountability to the financial system and gives investors important protections and greater input into corporate governance.” — SEC Chairman Mary L. Schapiro

## **Dodd-Frank Wall Street Reform and Consumer Protection Act**

- Sweeping changes to the financial regulatory landscape in response to the recent financial crisis
- Increased capital requirements
- Expansive new regulations for derivatives
- Regulators must engage in extensive rulemaking
- “Volcker Rule” – generally prohibits banking entity from engaging in proprietary trading or sponsoring or investing in a hedge fund or private equity fund
- Regulation of systemically important nonbank financial companies
- Created new agencies and offices within existing agencies

## **Dodd-Frank Act Corporate Governance and Executive Compensation**

- Enhanced Compensation Disclosure
- Disclosure of Employee and Director Hedging
- Disclosure of Chairman and CEO Structure
- Say on Pay
- Compensation Committee and Adviser Independence
- Incentive-Based Compensation for Covered Financial Institutions
- Clawback
- Broker Voting
- Proxy Access

## Enhanced Compensation Disclosure

- Pay versus Performance – The SEC is required to amend its executive compensation disclosure requirements to require a company to disclose in its annual meeting proxy materials the relationship between executive compensation actually paid and the company's financial performance.

## Enhanced Compensation Disclosure

- Internal Pay Equity Disclosure – The SEC is required to adopt rules requiring disclosure of the CEO's annual total compensation, the median annual total compensation of all other employees, and the ratio between these two amounts.

## Enhanced Compensation Disclosure

- Disclosure of Employee and Director Hedging – The SEC is required to adopt rules requiring companies to disclose in their annual meeting proxy statements whether directors or employees are permitted to purchase financial instruments designed to hedge any decrease in market value of equity securities granted as part of their compensation.

## Chairman and CEO Structure

- The SEC must adopt rules requiring a company to disclose in its proxy statement why it has chosen either to have the same person serve as Chairman and CEO or to have different individuals serve in each position

## Say on Pay

- Say on Pay Vote
- Say on Frequency of Say on Pay Vote
- Say on Golden Parachute Vote
- Disclosure of Institutional Investors' Vote on these Compensation-Related Matters

## Say on Pay

- Say on Pay – Shareholder advisory vote on executive compensation at least once every three years
- Say on Frequency of Say on Pay Vote – Shareholder advisory vote at least once every six years to determine whether the say on pay vote will occur every one, two, or three years
- These two DFA provisions go into effect for shareholder meetings that take place on or after January 21, 2011.

## Say on Pay

- Say on Golden Parachute Vote – For companies soliciting votes in a proxy to approve merger or acquisition transactions generally requires disclosure about, and, in certain circumstances, a separate shareholder advisory vote to approve golden parachute compensation arrangements
- Final rules adopted on January 25, 2011; the rule amendments are effective on April 25, 2011

## Say on Pay

- Institutional investment managers must disclose at least annually how they voted on the executive-compensation related shareholder votes required by the preceding provisions
- The SEC proposed rules on October 18, 2010.

## Compensation Committee Independence

- The SEC must adopt rules prohibiting securities exchanges from listing a security unless all members of an issuer's compensation committee are independent

## Independence of Compensation Committee Advisers

- The SEC must adopt rules directing securities exchanges to require a listed company's compensation committee to consider the independence of compensation consultants when selecting an adviser
- A company will be required to disclose in its proxy statement whether it has hired a compensation consultant and whether the work of the consultant raised any conflict of interest, and if so, how the conflict of interest is being addressed



## Incentive-Based Compensation for Covered Financial Institutions

- Requires covered financial institutions to disclose to the appropriate regulator the structure of incentive-based compensation, and prohibits incentive-based payment arrangements that encourage inappropriate risks by providing excessive compensation or that could lead to material financial loss to the covered financial institution

## Clawback

- The SEC must issue rules directing securities exchanges to prohibit listing a company's securities unless the company has developed and implemented a policy providing for disclosure of its policy on incentive-based compensation that is based on publicly reported financial information and mandating recovery of such incentive-based compensation from current or former executive officers following a restatement due to material noncompliance with financial reporting requirements

## Broker Voting

- Prohibits brokers from voting uninstructed shares on the election of directors, executive compensation, or any other significant matter
- Commission previously approved changes to the exchange rules to prohibit broker voting of uninstructed shares in director elections

## Proxy Access

- The Dodd-Frank Act gave the SEC express authority to issue rules permitting shareholders to use the company's proxy materials to include a nominee to the company's board of directors
- Proposal – June 10, 2009
- Adopted – Aug. 25, 2010
- Lawsuit – Business Roundtable and the Chamber of Commerce filed on Sept. 29, 2010
- SEC Stay/Postponement – Oct. 4, 2010

## Proxy Mechanics

- The SEC issued a concept release seeking input in connection with a broad review of the U.S. proxy system so it may update its rules to promote greater efficiency and transparency in the system and to enhance the accuracy and adequacy of the shareholder vote
- This review is not related to the Dodd-Frank Act

## Dodd-Frank Act Statutory References

- Enhanced Compensation Disclosure – Section 953
- Disclosure of Employee and Director Hedging – Section 955
- Disclosure of Chairman and CEO Structure – Section 972
- Say on Pay – Section 951
- Compensation Committee and Adviser Independence – Section 952
- Incentive-Based Compensation for Covered Financial Institutions – Section 956
- Clawback – Section 954
- Broker Voting – Section 957
- Proxy Access – Section 971