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Grahall Regulatory Client Advisory

July 24, 2010

DODD-FRANK FINANCIAL REFORM LAW CONTAINS SIGNIFICANT COMPENSATION CHANGES POTENTIALLY AFFECTING ALL PUBLIC FILERS

On July 21, 2010, President Barack Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act into law ("*Dodd-Frank*"). Aimed dead center at the heart of the financial services industry, Dodd-Frank represents the culmination of over 12 months of intense debate, lobbying and reconciliation as Congress attempts to clamp down on many of the practices that have led to a crisis in both the U.S. economy, and in the public's perception of the fairness of our public markets.

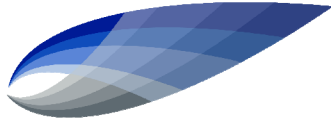
Accordingly, Dodd-Frank not only contains substantial changes regarding the financial services industry, but in the public markets regarding the determination and reporting of executive pay and corporate governance.

Both an Executive Summary and fuller discussion of Dodd-Frank's new rules with respect to pay and governance is as follows:

EXECUTIVE SUMMARY

I. EXECUTIVE COMPENSATION DISCLOSURES

- Say on Pay
 - Shareholders to provide advisory vote on Executive Compensation and IRC §280G "Golden Parachute" arrangements
- Pay For Performance
 - Companies to provide clear disclosure regarding compensation/performance relationship for amounts paid to the Named Executive Officers ("*NEOs*"). This may include graphical representation



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- CEO Pay Ratio
 - Companies must report CEO “Total Compensation” as a ratio relative to median Total Compensation of the companies’ employees
- Clawbacks
 - Companies must implement and disclose recapture policies
 - Movement away from “fraud-based” scheme under Section 304 of Sarbanes-Oxley (“SOX”) to close to a “strict liability” standard
 - Covered parties expanded beyond CEO/CFO to include all NEOs
 - Clawback period lengthened from 12 to 36 months

II. COMMITTEE COMPENSATION GOVERNANCE

- Compensation Committee Member Independence
 - National securities exchanges must consider relevant factors in determining Director independence
- Compensation Consultant Advisor Independence
 - The SEC to identify factors affecting independence of Composition Consultants , Legal Counsel, and other Committee advisers, including:
 - Provision of other services to the issuer
 - Fees: Consulting fees expressed as a percentage of the total revenue of the person/entity providing the consulting services
 - Policies of the entity providing consulting services designed to prevent conflicts of interest
 - Any business or personal relationship of the Competition Consultant (or other advisor) with the Compensation Committee
- CEO/Chairman structure
 - Company to provide proxy disclosure explaining rationale behind determination to have CEO and chairman staff by one or two individuals

III. OTHER

- Hedging
 - Companies to disclose whether executives and directors are allowed to hedge positions in company stock
- Broker Voting
 - Brokers no longer able to vote shares on specific topics such as “Say on Pay” and “Say on Parachute”



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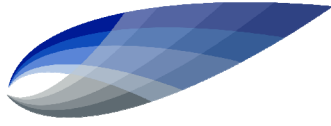
DISCUSSION

I. EXECUTIVE COMPENSATION DISCLOSURES

Say on Pay

The intense debate regarding shareholder advisory votes is over. Despite recent high-profile negative votes at Motorola and Occidental Petroleum, and significant growing resistance in the compensation community at large, "Say-on-Pay" is now mandatory for all public filers. Changes are effective on January 21, 2011 (6 months from the date the Act was signed) as follows:

- *Executive Compensation*
 - Non-binding advisory vote must occur no less than every three years regarding general compensation arrangements for Named Executive Officers
- *Frequency*
 - Shareholders at most public companies in 2011 will determine whether the advisory vote is to occur annually, biennially, or triennially
 - After the initial determination in 2011, shareholders must be given the opportunity to reaffirm their decision regarding the frequency of the compensation approval process no less than every six years
- *"Golden Parachute" Compensation*
 - Companies must now disclose to shareholders all agreements or understandings that the company has with any Named Executive Officer concerning any type of compensation (whether present, deferred, or contingent) that is based on or otherwise relates to any corporate transaction that would constitute a Change In Control as defined in §280G of the Internal Revenue Code
 - Companies must also disclose the total of all such compensation that may be paid or become payable to such executive officer (as well as any conditions that may apply such payments)
 - Shareholders to be given the opportunity to provide advisory vote on any such arrangements to the extent such advisory vote has not already occurred prior to 2011



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Grahall Comment: *An interesting new provision of Dodd-Frank will require that institutional investment managers be required to report no less than annually how they voted on the Say On Pay proposal.*

Grahall Comment: *Dodd-Frank grants the SEC explicit authority to exempt any company or class of companies from the Say on Pay requirements, particularly with respect to any disproportionate burden which may fall on smaller companies. Currently, the SEC defines a small company as one with \$75 million of annual revenues or less, but is not bound to this definition*

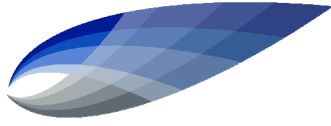
Executive Compensation Disclosures

- *Pay For Performance*
 - Each public company must clearly explain the relationship between executive compensation actually paid and the financial performance of the issuer. This may include a graphic representation

Grahall Comment: *CD&A disclosure presumably just got more challenging. The SEC explicitly provided that the CD&A be the sole province of management, albeit with disclosure regarding the Composition Committee's role in the process. Will this change under the new regulations? It would appear that some mechanism may need to develop for the Compensation Committee to have impact in the proxy statement. In addition, we believe pay-for-performance may translate into a link between annual incentive payments and short-term share price fluctuation.*

Grahall Comment: *We anticipate that the SEC will in fact require that companies provide some graphical representation, similar to the old "performance graph" against peers/market index that was previously required in all proxy filings. In fact, we never understood why this filing requirement was eliminated*

- *CEO Pay Ratio*
 - Public companies must calculate "total compensation" for each employee in its entire employee base and express the result as a ratio to the CEO's total compensation level (b)(1). Total Compensation will be determined consistent with the methods used to determine compensation for current reporting purposes in the Summary Compensation Table, including
 - Base
 - Bonus
 - LTI (equity or cash)
 - Pension/Other benefits



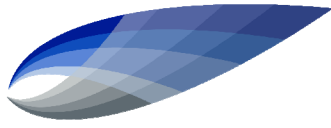
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Grahall Comment: A Powerful Rules Change. Though often disparaged and dismissed by industry participants as overly simplistic, unrelated to performance, and potentially distortive (i.e., not comparable across industries), there is little question in our minds that the simplicity and magnitude of the CEO Total Compensation Ratio will have an enormous impact on how compensation is considered and reported. For better or for worse, we anticipate this ratio will become a standard measuring stick both within and across industry segments, become a normal metric in market pricing CEOs against peers, and that significant outliers will be highly scrutinized

Grahall Comment: Administrative Headache? Some commentators have observed that calculating total compensation for a company's entire employee population could represent an administrative nightmare, particularly in large organizations with a multinational employee base with differing currencies. While guidance from the SEC remains pending, companies would be wise to commence preparation for the necessity of determining individual pay levels for each employee in accordance with the Summary Compensation Table Rules, rather than rely on a "Hail Mary" from the SEC which may not materialize. It is also worth noting that many companies already provide employees with a "Total Awards" statement, which enumerates each element of compensation and any other value creation realized by an employee during the applicable compensation year



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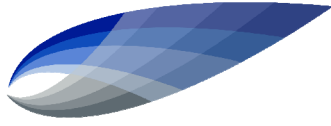
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Mandatory “Clawback” Policies

- Public companies must implement and disclose corporate policies that enable the company to recover *excess* compensatory payments to current and former NEOs in the event of a financial restatement that occurs as a result of the company’s material noncompliance with financial reporting requirements
 - “Scienter” (an extremely difficult element of proof required under Section 304 of the Sarbanes Oxley Act (“SOX”)) thus is no longer required for implementation of a public companies recapture rights
 - Accordingly, the new SEC rule essentially migrates acceptable “clawback” policy from a “fraud prevention” model to more of a “strict liability/disgorgement” model, assuming material noncompliance with financial reporting requirements has occurred
 - In addition, the concept of “Covered Executives” for purposes of implementing callback is broadened from the SOX standard – the CEO and CFO to all Named Executive Officers
 - Finally, the “clawback period” is expanded from 12 months under SOX to 36 months under Dodd-Frank

Grahall Comment: *Dodd-Frank significantly broadens and deepens the potential impact of the clawback remedy. Once reserved as primarily a threat against potential competitive or bad behavior by departing executives, clawback/recapture policies have now become an integral part of a public company’s compensation, governance and risk management programs, and Competition Committees need to ensure that their clawback policies are aligned with the Company’s overall compensation philosophy*

Grahall Comment: *Calculation of actual “excess” amounts to be “clawed back” is likely to be a thorny and complicated issue – we won’t speculate on eventual calculation methods. Accordingly, SEC guidance regarding this issue needs to be precise*



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II. COMPENSATION COMMITTEE AND GOVERNANCE

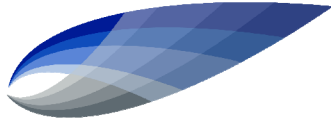
Compensation Committee Member Independence

- The SEC will now require that all members of the Compensation Committee be independent Board members
- “Independence” shall be determined under relevant factors established by the SEC within 12 months of the enactment of Dodd-Frank
 - Factors towards determining independent shall include:
 - Sources of Compensation Committee members’ additional compensation
 - Consulting, advisory or other fees
 - Affiliations
 - Whether any Committee members are affiliated with the company, its subsidiaries or affiliates
 - Some listed companies may be exempt from these requirements if the stock exchange determines such exemption is necessary due to size (small) or other concerns
 - It is currently unclear whether the SEC will adhere to its current practice of limiting compensation in non-Director related fees received from the company to \$120,000 or less

Grahall Comment: both national exchanges already require review of executive compensation by a Compensation Committee comprised of independent directors. While the new rules differ somewhat, their practical impact may be minimal to nonexistent

Compensation Consultants, Other Advisors, Legal Counsel

- Advisors may be selected by a Compensation Committee only after considering factors established by the SEC, to include:
 - Other services provided by the advisor to the company
 - Fees paid to the advisor by the company, expressed as a percent of the advisor’s total revenue
 - Policies of the advisor designed to prevent conflict of interest
 - Business or personal relationship between advisor and Compensation Committee members
 - Any equity interest held by the advisor in the company
 - Any additional factors established by the SEC



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Grahall Comment: SEC regulations need to clarify and finalize this criteria, which may be expanded by the SEC

CEO/Chairman Construction

- The SEC will require companies to discuss in its annual proxy statement the rationale regarding the company's leadership structure - specifically, why one person serves as CEO/Chairman, or alternatively why separate individuals serve in these roles

III. OTHER

Hedging Policies

- The SEC must require each company to disclose in its annual proxy its policies regarding permissible "hedging" strategies by which any employee or director could profit (or decrease realized loss) in the event of share price decline of company stock

Grahall Comment: To the extent that any significant hedging activity is actually occurring among employees or directors at public companies, we expect this rule change (combined with the anticipated reaction of shareholder advisory services) will eliminate all such practices

Elimination of Discretionary Broker Voting

- Securities Brokers holding shares for customers in "street name" no longer vote those shares without customer approval regarding certain issues, including the Say on Pay and Severance Pay advisory votes

Grahall Comment: changes in the voting rules with respect to brokers (who typically favor the status quo) is a potentially negative development for companies and significantly enhances the chances of negative "Say on Pay" or "Say on Parachute" votes

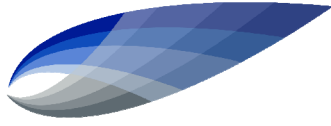


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CLIENT ACTION ITEMS

- **Say on Pay** – if your annual meeting occurs after January 21, 2011, your proxy will require the following additions:
 - A shareholder non-binding advisory vote approving or disapproving the executive compensation program
 - Shareholder advisory vote to determine how often the “Say on Pay” vote will occur from the following choices:
 - annually
 - every two years
 - every three years
- **CEO Total Compensation Ratio** – though the SEC has not yet issued final regulations regarding the calculation of the CEO total compensation ratio, company should commence determining how it will undertake a task of computing the total annual compensation amount for each employee
- **Pay for Performance** – companies should reconsider the philosophy behind its short and long-term pay programs and be prepared to explain to its shareholders satisfaction any potential divergence between short-term pay and stock price fluctuations which often move in uncorrelated or opposite directions
- **Clawbacks** – to the extent companies do not have a policy regarding clawbacks, the policy should be discussed and implemented consistent with the guidelines established under Dodd-Frank. Great care should be taken to integrate the policy with the company’s other compensation governance and risk management programs, all of which should be consistent with the company’s compensation philosophy
- **Hedging Policy** – companies should discuss and implement policies regarding executive and Director hedging against positions in company stock. To the extent such activity is permitted, Compensation Committees should be prepared with a strong rationale for disclosure to shareholders
- **Independence** – both independent of Compensation Committee members and of outside advisors should be reviewed in anticipation of the SEC issuing final regulations



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