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SEC Eliminates Broker Discretionary Votes for Directors and Seeks Enhanced Proxy Disclosures

The SEC has approved the NYSE's proposal on Rule 452 and proposed several new rules marking the latest volley in the rapidly shifting corporate governance and compensation environment, and accelerating the empowerment of activists, proxy advisory firms and institutional shareholders while further expanding the disclosure obligations imposed on public companies.

Rule 452: Eliminating Discretionary Voting by Brokers on Directors. By a vote of three to two, the SEC approved the NYSE's proposal to eliminate broker discretionary voting in uncontested director elections, effective for shareholder meetings in 2010. The SEC justified its approval (and what it acknowledges will be increased costs to companies) in part on the familiar but questionable premise that board failures were a principal cause of the recent market turmoil. As discussed in our [March 26, 2009 memorandum](#), the elimination of discretionary voting by brokers will have the effect of disenfranchising some retail shareholders and will correspondingly increase the power of activist shareholders who have pressured companies for short term results and others with special interests. We agree with the two dissenting Commissioners and the vast majority of those who commented on the proposed rule that this change should rather be considered in light of all recent developments, including the widespread adoption of majority voting and the opportunity for shareholder access to corporate proxy materials created by recent amendments to state laws.

New Corporate Governance Disclosures. In a continued expansion of disclosure obligations, the SEC proposed a package of new proxy disclosures concerning the qualifications of directors, executives and board nominees, the company's leadership structure (including as to separated or combined CEO/Chairman positions), and the board's role in risk management and oversight.

Codification of TARP Say-on-Pay Provisions. The SEC unanimously approved a new proposed Rule 14a-20 requiring TARP recipients to include a separate, non-binding shareholder advisory vote on the compensation of executives as disclosed pursuant to Item 402 of Regulation S-K. The requirement would apply at any annual meeting where directors are up for election as long as any obligation arising from the TARP recipient's receipt of financial assistance remains outstanding. Notably, the rule does not specify any particular formulation for the advisory vote, nor does it require a vote in the context of a change in control transaction, as has been proposed in other contexts.

New Compensation-Related Disclosures. The SEC also approved several compensation disclosure proposals that, if adopted, would apply to all registrants (not just TARP recipients) for the 2010 proxy season. The proposals would require disclosure concerning the relationship of a company's overall compensation policies to risk (as opposed to only the risk implications of executive compensation policies) and potential conflicts of interests of compensation consultants.

One can hope that these new disclosure requirements signal a reassessment by the SEC of the wisdom of federally mandated one-size-fits-all approaches and a return to traditional disclosure-oriented reforms, but whether they will improve the total mix of information available to shareholders – or merely increase issuers' disclosure burdens – remains to be seen. The SEC also indicated its intention to focus on the “plumbing” of proxy solicitation to enhance shareholder communication and voting, and any proposed changes in this area will need to be closely monitored so that they do not tip the balance even further in the direction of activist shareholders.

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