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Market Trends: Say on Pay, Frequency, and Golden Parachute Payments

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Overview

The 2017 proxy season marked the first recurrence of the Say on Frequency Vote and the sixth year in which companies were required to conduct Golden Parachute Votes (each as defined below). Regardless of whether companies hold their Say on Pay Votes annually, biennially, or triennially, shareholders for most companies cast Say on Pay Votes this year. This article outlines trends across Russell 3000 companies for proxies filed between January 1 and September 30 for years 2015, 2016, and 2017, respectively, for Say on Pay and Say on Golden Parachute Votes. This article also outlines comparisons for Say on Frequency Votes cast during the same period for years 2011 and 2017. For additional information on these and other proxy season trends, see Market Trends: Proxy Statements and Annual Meetings. For additional information on the proxy and annual meeting process in general, see Proxy Statement and Annual Meeting Resource Kit.

Say on Pay

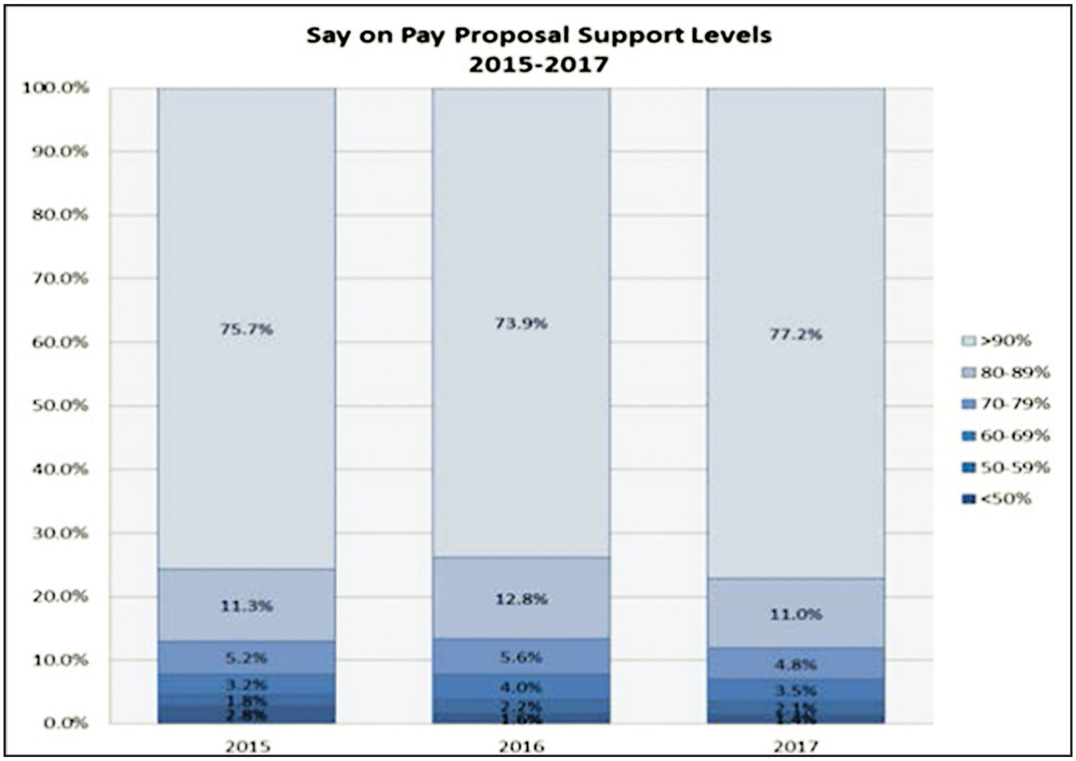
Since 2011, companies have been required to conduct nonbinding shareholder advisory votes to approve the compensation of their named executive officers (the Say on Pay Vote) pursuant to final rules promulgated by the Securities and Exchange Commission (the SEC) implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (111 P.L. 203, 124 Stat. 1376) (the final rules). For additional information on Say on Pay, see Complying with Dodd-Frank's Say-on-Pay Provisions and Dodd-Frank Act – Executive Compensation Provisions.

Trends in Say on Pay Votes

In general, the trend since 2011 has been for the level of shareholder support for Say on Pay Vote proposals, and therefore support for companies' named executive officer compensation practices, to increase. Rates of failure of Say on Pay Votes have decreased slightly over each of 2015, 2016, and 2017. In 2017 specifically, of 2,319 Russell 3000 companies reporting the results of Say on Pay Votes during January 1 through September 30, 2017, approximately:

- 77.2% have passed with at least 90% support
- 11.0% have passed with 80 to 89% support
- 4.8% have passed with 70 to 79% support
- 3.5% have passed with 60 to 69% support
- 2.1% have passed with 50 to 59% support
- 1.4% (29 companies) obtained less than 50% support

These 2017 Say on Pay Vote results are not substantially different when compared to results for the previous two years. Companies appear to be receiving slightly higher levels of support year after year. So far in 2017, the percentage of companies with shareholder approval of Say on Pay Vote proposals of at least 90% is slightly higher than in the previous two years.



At the same time, proxy advisory service recommendations regarding Say on Pay Vote proposals appear to have remained relatively constant across the same time period. For example, influential proxy advisory firm Institutional Shareholder Services (ISS) recommended that shareholders vote against about 12% of the Say on Pay Vote proposals it assessed thus far in 2017. This is consistent with the level of negative ISS recommendations on Say on Pay Vote proposals for the previous two years. For additional information on proxy advisory firms and their role, see Understanding the Role of Proxy Advisory Firms, Preparing for ISS Proxy Voting Recommendations Checklist, and Market Trends: Additional Proxy Soliciting Materials Responding to Negative Voting Recommendations.

Increased Shareholder Engagement and Company Responsiveness

Two factors appear to be contributing most significantly to the trend of incrementally more favorable Say on Pay Vote results over the last several years: increased shareholder engagement and increased company responsiveness to ISS and shareholder concerns raised with respect to named executive officer compensation practices. Companies taking affirmative steps in enhancing substantive engagement with shareholders over named executive compensation practices have seen the benefit of such engagement. Shareholder understanding of compensation approaches and decisions, coupled with clear disclosure of companies' compensation philosophy and rationale, has contributed to favorable Say on Pay Vote results.

For example, many companies have expanded their disclosures to include concise executive summaries, including summaries of companies' financial performance and its relationship to compensation, often with highlights at the beginning of the Compensation Discussion & Analysis section of the proxy statement. Increased use of clear and easy to understand graphical disclosure of company and individual performance, their relationship to earned and delivered named executive officer compensation, and the allocation of different elements of compensation have contributed to better shareholder understanding of companies' named executive officer compensation practices, and in turn to more favorable Say on Pay Vote results. At the same time, companies demonstrated responsiveness to specific shareholder concerns raised during the engagement process or concerns raised by ISS in connection with its review of named executive officer compensation. This has helped such companies achieve higher levels of shareholder support for Say on Pay Vote proposals year over year. The trends indicate that companies have had greater Say on Pay Vote success in recent years because they have been able to successfully foster a relationship with shareholders through engagement and demonstrate responsiveness to such engagement via clear disclosure. For additional information on engagement with shareholders, see Board Engagement with Shareholders Policy Checklist.

Say on Frequency

The final rules also require that shareholders cast advisory votes on the frequency (annually, biennially, or triennially) of Say on Pay Votes (the Say on Frequency Vote). Further, the final rules require that companies repeat the Say on Frequency Vote no later than the annual meeting held in the sixth calendar year immediately preceding the prior vote. Many public companies held their second Say on Frequency Vote during the 2017 proxy season. For additional information on Say on Frequency, see Q&A: Key Provisions of Executive Compensation under Dodd-Frank.

Trends in Say on Frequency Votes

Similar to the 2011 results for the Say on Frequency Vote, in 2017, the vast majority of shareholders of Russell 3000 companies elected to hold Say on Pay Votes on an annual basis. Of 1,790 Russell 3000 companies that held Say on Pay Votes between January 1 and September 30, 2017, 90.8% had shareholders elect annual Say on Pay Votes. While ISS uniformly recommended annual Say on Frequency votes, 8.9% of Russell 3000 companies had a majority of their shareholders cast votes in favor of a triennial vote, and a handful of companies (0.2%) had a majority of shareholders cast votes in favor of a biennial Say on Frequency Vote. For the most part, 2017 trends are similar to 2011 trends. It appears that if Russell 3000 companies altered their approach from 2011, they changed their practice from holding votes triennially to annually. The percentage of companies whose shareholders favor annual Say on Pay Votes increased by 8.6% between 2011 and 2017 whereas the number of Russell 3000 companies whose shareholders elected to have triennial Say on Pay Votes decreased by 8.3 over the same period. For example, 82.1% of Dollar General Corporation's shareholders cast votes in favor of an annual Say on Pay Vote in 2017, while 81.1% of the company's shareholders had voted in favor of a triennial Say on Pay Vote in 2011. In both instances, Dollar General Corporation's management recommended a triennial Say on Pay Vote. Amazon.com Inc.'s shareholders also favored an annual Say on Pay Vote in 2017, while the majority had voted for a triennial Say on Pay Vote in 2011. In both years, however, only a slight majority (56.9% in 2011 and 53.6% in 2017) of shareholders cast votes in favor of a triennial and annual Say on Pay Vote, respectively. Similar to the trends in 2011, based on the 2017 trends, it is clear that an annual Say on Frequency Vote is the predominant practice.

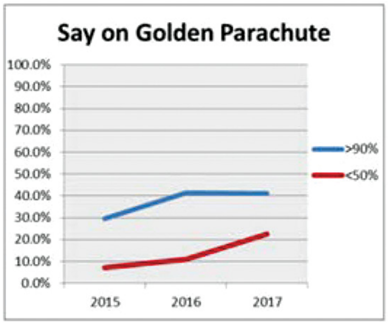
Say on Golden Parachutes

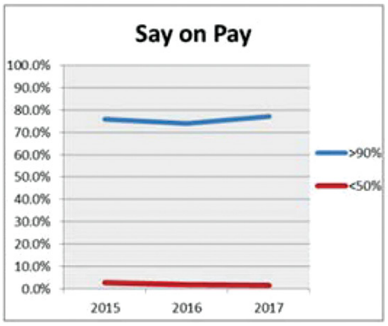
With respect to corporate transactions, the final rules also require companies to disclose any agreements or undertakings that the target company has with its named executive officers or those of the acquiring company. In addition, when companies seek shareholder approval of a merger or acquisition, they are required to conduct a separate advisory shareholder vote to approve the disclosed golden parachute compensation arrangements between the target company and its named executive officers (the Say on Golden Parachute Vote). However, companies are not required to conduct such a vote if the golden parachute disclosures were included in prior executive compensation disclosures that were previously subject to a Say on Pay Vote. For information on golden parachutes, see Guide to Disclosure and Shareholder Vote for Golden Parachute Compensation.

Trends in Say on Golden Parachute Votes

Recent trends indicate that shareholder support for Say on Golden Parachute Votes is less strong than for Say on Pay Votes. As shown in the table above, the percentage of Russell 3000 companies whose shareholders approved the compensation for named executive officers in Say on Pay Vote proposals by at least 90% was 75.7%, 73.9%, and 77.2%, in 2015, 2016, and 2017, respectively. With respect to Say on Golden Parachute Votes over the same period, the percent of companies whose shareholders approved golden parachute payments by at least 90% was 29.6% in 2015, 41.5% in 2016 and 41.3% in 2017.

Further, while the failure rate for Say on Pay Votes has decreased every year for the past three years, the failure rate for Say on Golden Parachute Votes has increased each year for the same period, with 22.5% of Russell 3000 companies failing to win approval of a majority of their shareholders for such golden parachute proposals in the first nine months of 2017 (compared to 7% of companies in 2015 and 11% of companies in 2016). For the 18 Russell 3000 companies that ultimately failed to secure majority approval for Say on Golden Parachute Votes during this nine-month period in 2017, the shareholder approval rate ranged from 28 to 49.5%. As described above, with respect to Say on Pay Votes, 1.4% of Russell 3000 companies failed to secure approval of a majority of shareholders during the same nine-month period in 2017.





Support for Underlying Transaction Undiminished

Lack of shareholder support for golden parachute payments does not appear to impede the consummation of the transaction. For example, in spite of failure to obtain approval of a majority of shareholders with respect to its Golden Parachute Vote and four shareholder lawsuits filed prior to closing alleging insufficient disclosures, JAB Holding Company's $7.5 billion acquisition of Panera Bread Company closed on July 18, 2017. In fact, in all instances thus far in 2017 in which shareholders rejected golden parachute payments, they simultaneously voted in favor of the proposed transaction. In particular, for the 18 companies that failed to win majority support for golden parachute payments in 2017, at least 70% of shareholders voted to approve the transaction (often with more than 90% of shareholders casting votes in favor of the transaction). For additional information on various merger and acquisition trends, see Market Trends: M&A Financing, Market Trends: Reverse Mergers, Market Trends: Leveraged Finance, and Market Trends: Special Purpose Acquisition Companies (SPACs).

As compared to shareholder engagement in connection with Say on Pay Votes, it is less clear how companies may successfully modify shareholder engagement efforts with respect to Say on Golden Parachute Votes to secure stronger support on behalf of shareholders. The misalignment of outcomes with respect to Say on Pay and Say on Golden Parachute Votes suggests that shareholders have a materially different view with respect to annual named executive officer compensation that is the subject of Say on Pay Vote proposals, as compared to compensation payable to named executive officers in connection with acquisition transactions. For example, the companies that failed to secure majority approval of shareholders for golden parachute payments thus far in 2017 obtained majority approval with respect to their Say on Pay Votes in 2016 (for those companies that reported the outcome of their 2016 Say on Pay Votes). Companies may wish to reflect on their best practices of shareholder engagement with respect to Say on Pay Votes and determine whether any lessons learned may be applied in the event that they need to conduct Say on Golden Parachute Votes.

Market Outlook

With respect to the 2018 proxy season, most public companies are currently focusing their efforts on preparing for the rollout of the pay ratio disclosure. The impact that the pay ratio disclosure will have on shareholder activism and ultimate approval of executive compensation is yet to be determined. Further, any adoption of certain changes proposed in the newly proposed Tax Cuts and Jobs Act may cause companies to restructure their current executive compensation practices, which would in turn require significant explanatory disclosures in the 2019 proxy season. In preparing for these changes, companies may wish to review their best practices with respect to shareholder engagement and responsiveness to try to proactively overcome some of the challenges involved in complying with the new disclosure requirements and any other disclosures related to compliance with the forthcoming changes to applicable law.