Course: Corporations and Corporate Governance

Contents: Reading Materials, Sessions Four: Recent Events in Executive Pay: The Financial Crisis and Beyond

Instructor: Professor Robert J. Jackson, Jr.

Meeting Details: Tuesday, July 26, 12:45 PM to 2:45 PM Jerome Greene Hall

Readings:
Having begun our consideration of the law and economics of executive compensation at large American public companies, we will turn to several recent events that have influenced both law and policy in this area—and, in particular, the financial crisis of 2008. In preparation for Tuesday afternoon’s session, then, please review the following:

- Section 111 of the Emergency Economic Stabilization Act of 2008, as amended by the American Recovery and Reinvestment Act of 2009 (only skim these restrictions on pay at recipients of assistance under the federal Troubled Asset Relief Program, or “TARP”).

- United States Department of the Treasury, Fact Sheet: The Special Master for TARP Executive Compensation Issues First Rulings (October 22, 2009).

- Sections 951 to 955 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (please only skim these statutory provisions, enacted in July 2010, which apply to executive compensation at all U.S. public companies).

I very much look forward to discussing these materials, and concluding our work together on executive compensation, on Tuesday afternoon.
(2) The national broadband plan required by this section shall seek to ensure that all people of the United States have access to broadband capability and shall establish benchmarks for meeting that goal. The plan shall also include—
(A) an analysis of the most effective and efficient mechanisms for ensuring broadband access by all people of the United States;
(B) a detailed strategy for achieving affordability of such service and maximum utilization of broadband infrastructure and service by the public;
(C) an evaluation of the status of deployment of broadband service, including progress of projects supported by the grants made pursuant to this section; and
(D) a plan for use of broadband infrastructure and services in advancing consumer welfare, civic participation, public safety and homeland security, community development, health care delivery, energy independence and efficiency, education, worker training, private sector investment, entrepreneurial activity, job creation and economic growth, and other national purposes.

(3) In developing the plan, the Commission shall have access to data provided to other Government agencies under the Broadband Data Improvement Act (47 U.S.C. 1301 note).

(i) The Assistant Secretary shall develop and maintain a comprehensive nationwide inventory map of existing broadband service capability and availability in the United States that depicts the geographic extent to which broadband service capability is deployed and available from a commercial provider or public provider throughout each State. Not later than 2 years after the date of the enactment of this Act, the Assistant Secretary shall make the broadband inventory map developed and maintained pursuant to this section accessible by the public on a World Wide Web site of the National Telecommunications and Information Administration in a form that is interactive and searchable.

(m) The Assistant Secretary shall have the authority to prescribe such rules as are necessary to carry out the purposes of this section.

TITLE VII—LIMITS ON EXECUTIVE COMPENSATION

SEC. 7000. TABLE OF CONTENTS.

The table of contents of this title is as follows:

TITLE VII—LIMITS ON EXECUTIVE COMPENSATION

Sec. 7000. Table of contents.
Sec. 7001. Executive compensation and corporate governance.
Sec. 7002. Applicability with respect to loan modifications.

SEC. 7001. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

Section 111 of the Emergency Economic Stabilization Act of 2008 (12 U.S.C. 5221) is amended to read as follows:
"SEC. 111. EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.

"(a) Definitions.—For purposes of this section, the following definitions shall apply:

(1) SENIOR EXECUTIVE OFFICER.—The term ‘senior executive officer’ means an individual who is 1 of the top 5 most highly paid executives of a public company, whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934, and any regulations issued thereunder, and non-public company counterparts.

(2) GOLDEN PARACHUTE PAYMENT.—The term ‘golden parachute payment’ means any payment to a senior executive officer for departure from a company for any reason, except for payments for services performed or benefits accrued.

(3) TARP RECIPIENT.—The term ‘TARP recipient’ means any entity that has received or will receive financial assistance under the financial assistance provided under the TARP.

(4) COMMISSION.—The term ‘Commission’ means the Securities and Exchange Commission.

(5) PERIOD IN WHICH OBLIGATION IS OUTSTANDING; RULE OF CONSTRUCTION.—For purposes of this section, the period in which any obligation arising from financial assistance provided under the TARP remains outstanding does not include any period during which the Federal Government only holds warrants to purchase common stock of the TARP recipient.

(b) EXECUTIVE COMPENSATION AND CORPORATE GOVERNANCE.—

(1) ESTABLISHMENT OF STANDARDS.—During the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, each TARP recipient shall be subject to—

(A) the standards established by the Secretary under this section; and

(B) the provisions of section 162(m)(5) of the Internal Revenue Code of 1986, as applicable.

(2) STANDARDS REQUIRED.—The Secretary shall require each TARP recipient to meet appropriate standards for executive compensation and corporate governance.

(3) SPECIFIC REQUIREMENTS.—The standards established under paragraph (2) shall include the following:

(A) Limits on compensation that exclude incentives for senior executive officers of the TARP recipient to take unnecessary and excessive risks that threaten the value of such recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding.

(B) A provision for the recovery by such TARP recipient of any bonus, retention award, or incentive compensation paid to a senior executive officer and any of the next 20 most highly-compensated employees of the TARP recipient based on statements of earnings, revenues, gains, or other criteria that are later found to be materially inaccurate.

(C) A prohibition on such TARP recipient making any golden parachute payment to a senior executive officer or any of the next 5 most highly-compensated employees of the TARP recipient during the period in which any
obligation arising from financial assistance provided under the TARP remains outstanding.

“(D)(i) A prohibition on such TARP recipient paying or accruing any bonus, retention award, or incentive compensation during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding, except that any prohibition developed under this paragraph shall not apply to the payment of long-term restricted stock by such TARP recipient, provided that such long-term restricted stock—

"(I) does not fully vest during the period in which any obligation arising from financial assistance provided to that TARP recipient remains outstanding;

"(II) has a value in an amount that is not greater than 1/5 of the total amount of annual compensation of the employee receiving the stock; and

"(III) is subject to such other terms and conditions as the Secretary may determine is in the public interest.

“(ii) The prohibition required under clause (i) shall apply as follows.

“(I) For any financial institution that received financial assistance provided under the TARP equal to less than $25,000,000, the prohibition shall apply only to the most highly compensated employee of the financial institution.

“(II) For any financial institution that received financial assistance provided under the TARP equal to at least $25,000,000, but less than $250,000,000, the prohibition shall apply to at least the 5 most highly-compensated employees of the financial institution, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

“(III) For any financial institution that received financial assistance provided under the TARP equal to at least $250,000,000, but less than $500,000,000, the prohibition shall apply to the senior executive officers and at least the 10 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

“(IV) For any financial institution that received financial assistance provided under the TARP equal to $500,000,000 or more, the prohibition shall apply to the senior executive officers and at least the 20 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest with respect to any TARP recipient.

“(iii) The prohibition required under clause (i) shall not be construed to prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009, as such valid employment contracts are determined by the Secretary or the designee of the Secretary.

“(E) A prohibition on any compensation plan that would encourage manipulation of the reported earnings of such
TARP recipient to enhance the compensation of any of its employees.

“(F) A requirement for the establishment of a Board Compensation Committee that meets the requirements of subsection (c).

“(4) CERTIFICATION OF COMPLIANCE.—The chief executive officer and chief financial officer (or the equivalents thereof) of each TARP recipient shall provide a written certification of compliance by the TARP recipient with the requirements of this section—

“(A) in the case of a TARP recipient, the securities of which are publicly traded, to the Securities and Exchange Commission, together with annual filings required under the securities laws; and

“(B) in the case of a TARP recipient that is not a publicly traded company, to the Secretary.

“(c) BOARD COMPENSATION COMMITTEE.—

“(1) ESTABLISHMENT OF BOARD REQUIRED.—Each TARP recipient shall establish a Board Compensation Committee, comprised entirely of independent directors, for the purpose of reviewing employee compensation plans.

“(2) MEETINGS.—The Board Compensation Committee of each TARP recipient shall meet at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to the TARP recipient from such plans.

“(3) COMPLIANCE BY NON-SEC REGISTRANTS.—In the case of any TARP recipient, the common or preferred stock of which is not registered pursuant to the Securities Exchange Act of 1934, and that has received $25,000,000 or less of TARP assistance, the duties of the Board Compensation Committee under this subsection shall be carried out by the board of directors of such TARP recipient.

“(d) LIMITATION ON LUXURY EXPENDITURES.—The board of directors of any TARP recipient shall have in place a company-wide policy regarding excessive or luxury expenditures, as identified by the Secretary, which may include excessive expenditures on—

“(1) entertainment or events;

“(2) office and facility renovations;

“(3) aviation or other transportation services; or

“(4) other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives, or other similar measures conducted in the normal course of the business operations of the TARP recipient.

“(e) SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—

“(1) ANNUAL SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.—Any proxy or consent or authorization for an annual or other meeting of the shareholders of any TARP recipient during the period in which any obligation arising from financial assistance provided under the TARP remains outstanding shall permit a separate shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the compensation discussion and analysis, the compensation tables, and any related material).

“(2) NONBINDING VOTE.—A shareholder vote described in paragraph (1) shall not be binding on the board of directors of a TARP recipient, and may not be construed as overruling
a decision by such board, nor to create or imply any additional fiduciary duty by such board, nor shall such vote be construed
to restrict or limit the ability of shareholders to make proposals
for inclusion in proxy materials related to executive compensa-
"(3) DEADLINE FOR RULEMAKING.—Not later than 1 year
after the date of enactment of the American Recovery and
Reinvestment Act of 2009, the Commission shall issue any
final rules and regulations required by this subsection.
"(f) REVIEW OF PRIOR PAYMENTS TO EXECUTIVES.—
"(1) IN GENERAL.—The Secretary shall review bonuses, 
retention awards, and other compensation paid to the senior
executive officers and the next 20 most highly-compensated 
employees of each entity receiving TARP assistance before the
date of enactment of the American Recovery and Reinvestment
Act of 2009, to determine whether any such payments were
inconsistent with the purposes of this section or the TARP
or were otherwise contrary to the public interest.
"(2) NEGOTIATIONS FOR REIMBURSEMENT.—If the Secretary
makes a determination described in paragraph (1), the Sec-
tary shall seek to negotiate with the TARP recipient and
the subject employee for appropriate reimbursements to the
Federal Government with respect to compensation or bonuses.
"(g) NO IMPEDIMENT TO WITHDRAWAL BY TARP RECIPIENTS.—
Subject to consultation with the appropriate Federal banking 
agency (as that term is defined in section 3 of the Federal Deposit Insurance
Act), if any, the Secretary shall permit a TARP recipient to repay
any assistance previously provided under the TARP to such finan-
cial institution, without regard to whether the financial institution
has replaced such funds from any other source or to any waiting
period, and when such assistance is repaid, the Secretary shall
liquidate warrants associated with such assistance at the current
market price.
"(h) REGULATIONS.—The Secretary shall promulgate regulations
to implement this section."
Today, the Special Master for TARP Executive Compensation Kenneth R. Feinberg released determinations on the compensation packages for the top executives at firms that received exceptional TARP assistance. Under the Emergency Economic Stabilization Act (EESA) as amended in 2009, the Special Master has a mandate to review all forms of compensation for five most senior executive officers and the next 20 most highly compensated employees at the seven firms that received exceptional TARP assistance (AIG, Citigroup, Bank of America, Chrysler, GM, GMAC and Chrysler Financial).

1. **Reforms Pay Practices for Top Executives to Align Compensation Practices With Long-Term Value Creation and Financial Stability:** The Special Master's rulings represent a fundamental transformation from the pay practices of the past. These decisions will significantly alter the way that executives covered by the Special Master's decisions—including the senior executive officers and next 20 most highly compensated employees of each of the seven recipients of “exceptional” assistance under the TARP (AIG, Citigroup, Bank of America, Chrysler, GM, GMAC and Chrysler Financial)—are paid.

   ◦ **Rejects Cash Payments Based on Short-Term Performance, as required by statute:** Traditionally, compensation for these employees has included large cash amounts, including significant cash bonuses. These payments gave executives incentives to take short-term risks and little reason to protect the long-term the health of the company or financial stability. After today's rulings, as required by statute and Treasury regulations, these executives will receive the overwhelming majority of their pay in company stock that may only be sold over the long term, aligning their interests with those of taxpayers and shareholders.

   ◦ **Restructures Existing “Guaranteed” Cash Payments into Stock Held For the Long Term:** Under the pay practices of the past, several executives in this group were awarded cash “guarantees” in 2009. A Guaranteed minimum amounts give employees little downside risk in the event of poor performance—but upside when times are good. The Special Master required these agreements to be restructured. Under today's rulings, these amounts will be paid in company stock that must be held over the long term.

   ◦ **Citigroup and Phibro:** At Phibro, Citigroup's commodities trading unit, the Chief Executive Officer was to receive a significant cash bonus based on the short-term results of significant risk-taking. The Special Master rejected this approach, and Citigroup agreed to sell Phibro to a company that has not received taxpayer funds. Under today's ruling, nothing may be paid to the Phibro CEO until the sale is complete.

2. **Significantly Reduces Compensation Across the Board:** To break from the pay practices of the past, the Special Master has reduced compensation across the board—both in terms of cash and the total compensation executives will receive.

   ◦ **On Average, Cash Compensation Decreased by More Than 90 percent:** The Special Master rejected cash payments based on short-term results that may prove illusory, and cash guarantees that separate pay from performance. A Overall, the Special Master reduced cash pay by more than 90 percent from 2008 levels—and, as required by Treasury regulations, cash bonuses may no longer be paid to any of these employees.

   ◦ **Approved cash salary generally limited to $500,000:** Consistent with the Administration’s February 4 guidance on executive compensation at TARP recipients, the Special Master approved base salaries of $500,000 or less for more than 90 percent of the employees in this group. Base salaries greater than $1 million were approved in just three cases: for the new CEO of AIG, as previously announced, and for two employees of Chrysler Financial, which will wind down its operations in the near term and cannot grant employees long-term incentives.

   ◦ **On Average, Total Compensation Decreased by More Than 50 percent:** Even including the value of stock that must be held for the long term, the Special Master reduced the total compensation packages for executives in this group to less than half of 2008 levels.

   ◦ **Exceptions Where Necessary to Retain Talent and Protect Taxpayer Interests:** Although the Special Master's rulings generally emphasize decreases in both cash and total compensation across the seven companies, increases in compensation were permitted where shown to be necessary to retaining key talent critical to a company's long-term success—and, ultimately, ability to repay.
3. **Requires Salaries to be Paid in Company Stock Held Over the Long Term:** The Special Master's rulings fundamentally change the structure of compensation at these firms. Rather than cash, today's rulings require that the majority of salaries be paid in stock that must be held for the long term—giving executives incentives to pursue long-term value creation and financial stability.

- **Stock is Immediately Vested, Requiring Executives to Put Their Own Funds at Stake:** Rather than just cash, executives will earn base salaries in the form of vested stock in their companies. In effect, the Special Master is requiring each executive to invest their base salary in the long-term future of the firm, alongside taxpayers. These structures ensure that executives do not have incentives to take the excessive risks that contributed to the financial crisis.

- **Stock May Only Be Sold in One-Third Installments, Beginning In Two Years:** Unlike the pay practices of the past, which allowed executives to sell stock in their companies immediately, the Special Master's rulings require stock to be held for the long term. Stock received as salary may only be sold in one-third installments that will not begin until 2011, unless the taxpayer is repaid earlier.

4. **Require Incentive Compensation to be Paid in the Form of Long Term Restricted Stock & to be Contingent on Performance and on TARP Repayment:** As the Secretary noted in his June 10 statement, incentive pay can be undermined by compensation practices that set the performance bar too low or simply reward rising tides. The Special Master's rulings require that incentives be paid only if executives reach objective goals agreed upon in consultation with the Special Master—and only if TARP is repaid.

- **Requires Achievement of Goals Set in Consultation with the Special Master:** The Special Master's rulings permit these executives to receive incentive pay only if the executives attain objective, predetermined performance goals set in consultation with the Special Master. Achievement of these goals must be certified by each company's compensation committee—which, under Treasury regulations, must be composed solely of directors fully independent from management.

- **Requires Three Years of Service, and TARP Repaid, Before Payment:** To ensure that taxpayers continue to receive the benefits of the executives' talents, the Special Master's ruling requires that any incentive awards be paid only if the employee provides at least three years of service to the company after the award is made. And, under Treasury regulations, the awards must be paid in the form of restricted stock that may not be paid unless the company repays its TARP obligations.

5. **Requires Immediate Reform of Practices Not Aligned With Shareholder Interests:** As the Secretary noted in his June 10 statement, in some cases golden parachutes and supplemental executive retirement plans have expanded beyond their original purpose, and may not enhance the long-term value of the firm or allow shareholders to easily ascertain the full value of the "walkaway" pay an executive will receive when departing the firm. The Special Master's rulings place tough new restrictions on these payments—as well as perquisites and other personal benefits—for executives at companies that have received exceptional taxpayer assistance.

- **Caps perquisites and "other" compensation:** Several experts, including the Conference Board Task Force on Executive Compensation, have concluded that executives—and not companies—should generally cover the costs of personal expenses. The Special Master's rulings generally cap these types of payments at $25,000, with limited exceptions for unusual circumstances that can be justified to the Special Master.

- **Additional limitations on "golden parachute" payments:** Large "golden parachute" or severance payments often serve to enrich executives rather than provide reasonable compensation during unemployment, and often do not enhance the long-term value of a company. Tough new Treasury regulations prohibit these payments to the senior executive officers and five most highly compensated employees at all companies that have received taxpayer assistance. The Special Master's rulings go further, however, and prohibit companies from increasing the amount of any "golden parachute" payable to any of the top 20 most highly compensated executives during 2009.

- **Freezing supplemental executive retirement plans:** Supplemental executive retirement benefits can provide substantial cash guarantees to departing executives, regardless of performance. And, as the Secretary noted on June 10, these complex benefits can make it difficult for shareholders—and, in the case of exceptional assistance companies, taxpayers—to ascertain the full amount of pay an executive will receive upon retirement. The Special Master's rulings conclude that these executives should provide for their retirements with wealth based on performance while they are employed, rather than being guaranteed substantial retirement benefits beyond those provided to everyday workers. As a result, the Special Master's decisions prohibit additional accruals under supplemental executive pension programs and company credits to other non-qualified deferred compensation plans following the release of today's rulings.
Subtitle E—Accountability and Executive Compensation

SEC. 951. SHAREHOLDER VOTE ON EXECUTIVE COMPENSATION DISCLOSURES.


"SEC. 14A. SHAREHOLDER APPROVAL OF EXECUTIVE COMPENSATION.

(a) SEPARATE RESOLUTION REQUIRED.—

(1) IN GENERAL.—Not less frequently than once every 3 years, a proxy or consent or authorization for an annual or other meeting of the shareholders for which the proxy solicitation rules of the Commission require compensation disclosure shall include a separate resolution subject to shareholder vote to approve the compensation of executives, as disclosed pursuant to section 229.402 of title 17, Code of Federal Regulations, or any successor thereto.

(2) FREQUENCY OF VOTE.—Not less frequently than once every 6 years, a proxy or consent or authorization for an annual or other meeting of the shareholders for which the proxy solicitation rules of the Commission require compensation disclosure shall include a separate resolution subject to shareholder vote to determine whether votes on the resolutions required under paragraph (1) will occur every 1, 2, or 3 years.

(3) EFFECTIVE DATE.—The proxy or consent or authorization for the first annual or other meeting of the shareholders occurring after the end of the 6-month period beginning on the date of enactment of this section shall include—

(A) the resolution described in paragraph (1); and

(B) a separate resolution subject to shareholder vote to determine whether votes on the resolutions required under paragraph (1) will occur every 1, 2, or 3 years.

(b) SHAREHOLDER APPROVAL OF GOLDEN PARACHUTE COMPENSATION.—

(1) DISCLOSURE.—In any proxy or consent solicitation material (the solicitation of which is subject to the rules of the Commission pursuant to subsection (a)) for a meeting of the shareholders occurring after the end of the 6-month period beginning on the date of enactment of this section, at which shareholders are asked to approve an acquisition, merger, consolidation, or proposed sale or other disposition of all or substantially all the assets of an issuer, the person making such solicitation shall disclose in the proxy or consent solicitation material, in a clear and simple form in accordance with regulations to be promulgated by the Commission, any agreements or understandings that such person has with any named executive officers of such issuer (or of the acquiring issuer, if such issuer is not the acquiring issuer) concerning any type of compensation (whether present, deferred, or contingent) that is based on or otherwise relates to the acquisition, merger, consolidation, sale, or other disposition of all or substantially all of the assets of the issuer and the aggregate total of all such compensation that may (and the conditions upon which

15 USC 78n–1.

Deadlines.
it may) be paid or become payable to or on behalf of such executive officer.

“(2) SHAREHOLDER APPROVAL.—Any proxy or consent or authorization relating to the proxy or consent solicitation material containing the disclosure required by paragraph (1) shall include a separate resolution subject to shareholder vote to approve such agreements or understandings and compensation as disclosed, unless such agreements or understandings have been subject to a shareholder vote under subsection (a).

“(c) RULE OF CONSTRUCTION.—The shareholder vote referred to in subsections (a) and (b) shall not be binding on the issuer or the board of directors of an issuer, and may not be construed—

“(1) as overruling a decision by such issuer or board of directors;

“(2) to create or imply any change to the fiduciary duties of such issuer or board of directors;

“(3) to create or imply any additional fiduciary duties for such issuer or board of directors; or

“(4) to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation.

“(d) DISCLOSURE OF VOTES.—Every institutional investment manager subject to section 13(f) shall report at least annually how it voted on any shareholder vote pursuant to subsections (a) and (b), unless such vote is otherwise required to be reported publicly by rule or regulation of the Commission.

“(e) EXEMPTION.—The Commission may, by rule or order, exempt an issuer or class of issuers from the requirement under subsection (a) or (b). In determining whether to make an exemption under this subsection, the Commission shall take into account, among other considerations, whether the requirements under subsections (a) and (b) disproportionately burdens small issuers.”.

SEC. 952. COMPENSATION COMMITTEE INDEPENDENCE.

(a) IN GENERAL.—The Securities Exchange Act of 1934 (15 U.S.C. 78 et seq.) is amended by inserting after section 10B, as added by section 753, the following:

“SEC. 10C. COMPENSATION COMMITTEES.

“(a) INDEPENDENCE OF COMPENSATION COMMITTEES.—

“(1) LISTING STANDARDS.—The Commission shall, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any equity security of an issuer, other than an issuer that is a controlled company, limited partnership, company in bankruptcy proceedings, open-ended management investment company that is registered under the Investment Company Act of 1940, or a foreign private issuer that provides annual disclosures to shareholders of the reasons that the foreign private issuer does not have an independent compensation committee, that does not comply with the requirements of this subsection.

“(2) INDEPENDENCE OF COMPENSATION COMMITTEES.—The rules of the Commission under paragraph (1) shall require that each member of the compensation committee of the board of directors of an issuer be—

“(A) a member of the board of directors of the issuer; and

“(B) independent.
“(3) INDEPENDENCE.—The rules of the Commission under paragraph (1) shall require that, in determining the definition of the term ‘independence’ for purposes of paragraph (2), the national securities exchanges and the national securities associations shall consider relevant factors, including—

“(A) the source of compensation of a member of the board of directors of an issuer, including any consulting, advisory, or other compensatory fee paid by the issuer to such member of the board of directors; and

“(B) whether a member of the board of directors of an issuer is affiliated with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer.

“(4) EXEMPTION AUTHORITY.—The rules of the Commission under paragraph (1) shall permit a national securities exchange or a national securities association to exempt a particular relationship from the requirements of paragraph (2), with respect to the members of a compensation committee, as the national securities exchange or national securities association determines is appropriate, taking into consideration the size of an issuer and any other relevant factors.

“(b) INDEPENDENCE OF COMPENSATION CONSULTANTS AND OTHER COMPENSATION COMMITTEE ADVISERS.—

“(1) IN GENERAL.—The compensation committee of an issuer may only select a compensation consultant, legal counsel, or other adviser to the compensation committee after taking into consideration the factors identified by the Commission under paragraph (2).

“(2) RULES.—The Commission shall identify factors that affect the independence of a compensation consultant, legal counsel, or other adviser to a compensation committee of an issuer. Such factors shall be competitively neutral among categories of consultants, legal counsel, or other advisers and preserve the ability of compensation committees to retain the services of members of any such category, and shall include—

“(A) the provision of other services to the issuer by the person that employs the compensation consultant, legal counsel, or other adviser;

“(B) the amount of fees received from the issuer by the person that employs the compensation consultant, legal counsel, or other adviser, as a percentage of the total revenue of the person that employs the compensation consultant, legal counsel, or other adviser;

“(C) the policies and procedures of the person that employs the compensation consultant, legal counsel, or other adviser that are designed to prevent conflicts of interest;

“(D) any business or personal relationship of the compensation consultant, legal counsel, or other adviser with a member of the compensation committee; and

“(E) any stock of the issuer owned by the compensation consultant, legal counsel, or other adviser.

“(c) COMPENSATION COMMITTEE AUTHORITY RELATING TO COMPENSATION CONSULTANTS.—

“(1) AUTHORITY TO RETAIN COMPENSATION CONSULTANT.—
“(A) IN GENERAL.—The compensation committee of an issuer, in its capacity as a committee of the board of directors, may, in its sole discretion, retain or obtain the advice of a compensation consultant.

“(B) DIRECT RESPONSIBILITY OF COMPENSATION COMMITTEE.—The compensation committee of an issuer shall be directly responsible for the appointment, compensation, and oversight of the work of a compensation consultant.

“(C) RULE OF CONSTRUCTION.—This paragraph may not be construed—

“(i) to require the compensation committee to implement or act consistently with the advice or recommendations of the compensation consultant; or

“(ii) to affect the ability or obligation of a compensation committee to exercise its own judgment in fulfillment of the duties of the compensation committee.

“(2) DISCLOSURE.—In any proxy or consent solicitation material for an annual meeting of the shareholders (or a special meeting in lieu of the annual meeting) occurring on or after the date that is 1 year after the date of enactment of this section, each issuer shall disclose in the proxy or consent material, in accordance with regulations of the Commission, whether—

“(A) the compensation committee of the issuer retained or obtained the advice of a compensation consultant; and

“(B) the work of the compensation consultant has raised any conflict of interest and, if so, the nature of the conflict and how the conflict is being addressed.

“(d) AUTHORITY TO ENGAGE INDEPENDENT LEGAL COUNSEL AND OTHER ADVISERS.—

“(1) IN GENERAL.—The compensation committee of an issuer, in its capacity as a committee of the board of directors, may, in its sole discretion, retain and obtain the advice of independent legal counsel and other advisers.

“(2) DIRECT RESPONSIBILITY OF COMPENSATION COMMITTEE.—The compensation committee of an issuer shall be directly responsible for the appointment, compensation, and oversight of the work of independent legal counsel and other advisers.

“(3) RULE OF CONSTRUCTION.—This subsection may not be construed—

“(A) to require a compensation committee to implement or act consistently with the advice or recommendations of independent legal counsel or other advisers under this subsection; or

“(B) to affect the ability or obligation of a compensation committee to exercise its own judgment in fulfillment of the duties of the compensation committee.

“(e) COMPENSATION OF COMPENSATION CONSULTANTS, INDEPENDENT LEGAL COUNSEL, AND OTHER ADVISERS.—Each issuer shall provide for appropriate funding, as determined by the compensation committee in its capacity as a committee of the board of directors, for payment of reasonable compensation—

“(1) to a compensation consultant; and

“(2) to independent legal counsel or any other adviser to the compensation committee.
“(f) Commission Rules.—

“(1) In General.—Not later than 360 days after the date of enactment of this section, the Commission shall, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that is not in compliance with the requirements of this section.

“(2) Opportunity to Cure Defects.—The rules of the Commission under paragraph (1) shall provide for appropriate procedures for an issuer to have a reasonable opportunity to cure any defects that would be the basis for the prohibition under paragraph (1), before the imposition of such prohibition.

“(g) Exemption Authority.—

“(A) In General.—The rules of the Commission under paragraph (1) shall permit a national securities exchange or a national securities association to exempt a category of issuers from the requirements under this section, as the national securities exchange or the national securities association determines is appropriate.

“(B) Considerations.—In determining appropriate exemptions under subparagraph (A), the national securities exchange or the national securities association shall take into account the potential impact of the requirements of this section on smaller reporting issuers.

“(h) Controlled Company Exemption.—

“(1) In General.—This section shall not apply to any controlled company.

“(2) Definition.—For purposes of this section, the term ‘controlled company’ means an issuer—

“(A) that is listed on a national securities exchange or by a national securities association; and

“(B) that holds an election for the board of directors of the issuer in which more than 50 percent of the voting power is held by an individual, a group, or another issuer.”.

(b) Study and Report.—

(1) Study.—The Securities and Exchange Commission shall conduct a study and review of the use of compensation consultants and the effects of such use.

(2) Report.—Not later than 2 years after the date of the enactment of this Act, the Commission shall submit a report to Congress on the results of the study and review required by this subsection.

SEC. 953. EXECUTIVE COMPENSATION DISCLOSURES.

(a) Disclosure of Pay Versus Performance.—Section 14 of the Securities Exchange Act of 1934 (15 U.S.C. 78n), as amended by this title, is amended by adding at the end the following:

“(i) Disclosure of Pay Versus Performance.—The Commission shall, by rule, require each issuer to disclose in any proxy or consent solicitation material for an annual meeting of the shareholders of the issuer a clear description of any compensation required to be disclosed by the issuer under section 229.402 of title 17, Code of Federal Regulations (or any successor thereto), including information that shows the relationship between executive compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends of the issuer and any distributions. The
disclosure under this subsection may include a graphic representation of the information required to be disclosed.”.

(b) ADDITIONAL DISCLOSURE REQUIREMENTS.—

(1) IN GENERAL.—The Commission shall amend section 229.402 of title 17, Code of Federal Regulations, to require each issuer to disclose in any filing of the issuer described in section 229.10(a) of title 17, Code of Federal Regulations (or any successor thereto)—

(A) the median of the annual total compensation of all employees of the issuer, except the chief executive officer (or any equivalent position) of the issuer;

(B) the annual total compensation of the chief executive officer (or any equivalent position) of the issuer; and

(C) the ratio of the amount described in subparagraph (A) to the amount described in subparagraph (B).

(2) TOTAL COMPENSATION.—For purposes of this subsection, the total compensation of an employee of an issuer shall be determined in accordance with section 229.402(c)(2)(x) of title 17, Code of Federal Regulations, as in effect on the day before the date of enactment of this Act.

SEC. 954. RECOVERY OF ERRONEOUSLY AWARDED COMPENSATION.

The Securities Exchange Act of 1934 is amended by inserting after section 10C, as added by section 952, the following:

SEC. 10D. RECOVERY OF ERRONEOUSLY AWARDED COMPENSATION POLICY.

“(a) LISTING STANDARDS.—The Commission shall, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that does not comply with the requirements of this section.

“(b) RECOVERY OF FUNDS.—The rules of the Commission under subsection (a) shall require each issuer to develop and implement a policy providing—

“(1) for disclosure of the policy of the issuer on incentive-based compensation that is based on financial information required to be reported under the securities laws; and

“(2) that, in the event that the issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer with any financial reporting requirement under the securities laws, the issuer will recover from any current or former executive officer of the issuer who received incentive-based compensation (including stock options awarded as compensation) during the 3-year period preceding the date on which the issuer is required to prepare an accounting restatement, based on the erroneous data, in excess of what would have been paid to the executive officer under the accounting restatement.”.

SEC. 955. DISCLOSURE REGARDING EMPLOYEE AND DIRECTOR HEDGING.

Section 14 of the Securities Exchange Act of 1934 (15 U.S.C. 78n), as amended by this title, is amended by adding at the end the following:

“(j) DISCLOSURE OF HEDGING BY EMPLOYEES AND DIRECTORS.—

The Commission shall, by rule, require each issuer to disclose in any proxy or consent solicitation material for an annual meeting of the shareholders of the issuer whether any employee or member
of the board of directors of the issuer, or any designee of such employee or member, is permitted to purchase financial instruments (including prepaid variable forward contracts, equity swaps, collars, and exchange funds) that are designed to hedge or offset any decrease in the market value of equity securities—

“(1) granted to the employee or member of the board of directors by the issuer as part of the compensation of the employee or member of the board of directors; or

“(2) held, directly or indirectly, by the employee or member of the board of directors.”.

SEC. 956. ENHANCED COMPENSATION STRUCTURE REPORTING.

(a) Enhanced Disclosure and Reporting of Compensation Arrangements.—

(1) In General.—Not later than 9 months after the date of enactment of this title, the appropriate Federal regulators jointly shall prescribe regulations or guidelines to require each covered financial institution to disclose to the appropriate Federal regulator the structures of all incentive-based compensation arrangements offered by such covered financial institutions sufficient to determine whether the compensation structure—

(A) provides an executive officer, employee, director, or principal shareholder of the covered financial institution with excessive compensation, fees, or benefits; or

(B) could lead to material financial loss to the covered financial institution.

(2) Rules of Construction.—Nothing in this section shall be construed as requiring the reporting of the actual compensation of particular individuals. Nothing in this section shall be construed to require a covered financial institution that does not have an incentive-based payment arrangement to make the disclosures required under this subsection.

(b) Prohibition on Certain Compensation Arrangements.—Not later than 9 months after the date of enactment of this title, the appropriate Federal regulators shall jointly prescribe regulations or guidelines that prohibit any types of incentive-based payment arrangement, or any feature of any such arrangement, that the regulators determine encourages inappropriate risks by covered financial institutions—

(1) by providing an executive officer, employee, director, or principal shareholder of the covered financial institution with excessive compensation, fees, or benefits; or

(2) that could lead to material financial loss to the covered financial institution.

(c) Standards.—The appropriate Federal regulators shall—

(1) ensure that any standards for compensation established under subsections (a) or (b) are comparable to the standards established under section of the Federal Deposit Insurance Act (12 U.S.C. 21831p–1) for insured depository institutions; and

(2) in establishing such standards under such subsections, take into consideration the compensation standards described in section 39(c) of the Federal Deposit Insurance Act (12 U.S.C. 1831p–9 1(c));

(d) Enforcement.—The provisions of this section and the regulations issued under this section shall be enforced under section
505 of the Gramm-Leach-Bliley Act and, for purposes of such section, a violation of this section or such regulations shall be treated as a violation of subtitle A of title V of such Act.

(e) DEFINITIONS.—As used in this section—

(1) the term “appropriate Federal regulator” means the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Board of Directors of the Federal Deposit Insurance Corporation, the Director of the Office of Thrift Supervision, the National Credit Union Administration Board, the Securities and Exchange Commission, the Federal Housing Finance Agency; and

(2) the term “covered financial institution” means—

(A) a depository institution or depository institution holding company, as such terms are defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813);

(B) a broker-dealer registered under section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o);

(C) a credit union, as described in section 19(b)(1)(A)(iv) of the Federal Reserve Act;

(D) an investment advisor, as such term is defined in section 202(a)(11) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(11));

(E) the Federal National Mortgage Association;

(F) the Federal Home Loan Mortgage Corporation; and

(G) any other financial institution that the appropriate Federal regulators, jointly, by rule, determine should be treated as a covered financial institution for purposes of this section.

(f) EXEMPTION FOR CERTAIN FINANCIAL INSTITUTIONS.—The requirements of this section shall not apply to covered financial institutions with assets of less than $1,000,000,000.

SEC. 957. VOTING BY BROKERS.

Section 6(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78f(b)) is amended—

(1) in paragraph (9)—

(A) in subparagraph (A), by redesignating clauses (i) through (v) as subclauses (I) through (V), respectively, and adjusting the margins accordingly;

(B) by redesignating subparagraphs (A) through (D) as clauses (i) through (iv), respectively, and adjusting the margins accordingly;

(C) by inserting “(A)” after “(9)”;

(D) in the matter immediately following clause (iv), as so redesignated, by striking “As used” and inserting the following:

“(B) As used”.

(2) by adding at the end the following:

“(10)(A) The rules of the exchange prohibit any member that is not the beneficial owner of a security registered under section 12 from granting a proxy to vote the security in connection with a shareholder vote described in subparagraph (B), unless the beneficial owner of the security has instructed the member to vote the proxy in accordance with the voting instructions of the beneficial owner.

(B) A shareholder vote described in this subparagraph is a shareholder vote with respect to the election of a member