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'Say on pay' may be here to stay

Tresa Baldas / Staff reporter
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A movement to give shareholders some say regarding executive pay is gaining momentum, leaving Corporate America uneasy and triggering debate within the legal profession concerning the role of shareholders.

During the past year, attorneys say, so-called "say on pay" policies — which give shareholders a nonbinding vote on how much executives are paid — have taken off in the business world, fueled largely by public outrage over exorbitant executive salaries.

The reaction among corporate attorneys who are advising their clients on formulating such policies ranges widely, with some calling them a nuisance that grants too much power to shareholders and others calling them a valuable safety valve that could help prevent litigation.

" 'Shareholder democracy' is a popular rage right now," said John Gamble, a management-side labor and employment lawyer at Atlanta's Fisher & Phillips. "But one wonders how much of the fervor is really about shareholder 'rights,' and how much is political populism, or just an emotional reaction" to large salaries and bonuses.

Whatever the reason, "say on pay" is the topic du jour.

Presidential candidates from both major political parties are supporting it.
Congress has a bill pending that would mandate the shareholder advisory vote.

On the business front, many companies are currently contemplating the idea of adopting say-on-pay policies, while several others have recently embraced the concept, including Blockbuster Inc., Verizon Communications Inc. and bond insurer MBIA Inc.

In May, insurance giant Aflac Inc. became the first U.S. company in which shareholders cast nonbinding votes on top management's compensation.

Investors at more than 90 other firms are also expected to vote on say-on-pay proposals this year, according to data from RiskMetrics Group, a provider of risk management and corporate governance products and services to financial market participants.

"It's a nuisance," said J. Mark Poerio, who co-chairs the executive compensation and employee benefits practice group at the Washington office of Paul, Hastings, Janofsky & Walker.

"We're seen as being hyperregulated. This is just one more added burden on public companies," he added.

Poerio noted that "[g]overnmental regulators and the courts have long drawn a line between the appropriate role of shareholders, which is to elect those who will govern a company as its directors, and the board of directors, which is to make business decisions considered to be in the best interests of shareholders."

"The say-on-pay initiative seems to me to step over this line, encroaching on board functions in a manner that, although minor, places us on a slippery slope that opens the door for mandating future nonbinding votes on any issue that becomes front-page news," he said.

'A PR nightmare'

Paul Ritter, a partner at New York's Kramer Levin Naftalis & Frankel, who specializes in executive-compensation issues, echoed similar concerns. He believes that shareholders having a say on pay doesn't solve the problem of excessive compensation because a yes or no vote doesn't really say much.

But that doesn't mean a nonbinding vote won't have an impact.

"A board just can't simply ignore shareholdings voting against something because that will create all kinds of media attention, and attention from proxy advisory firms," he said. "It's a PR nightmare."

Ritter also argued that shareholders are ill-equipped to make informed judgments on executive compensation. He said they lack knowledge about the design of compensation packages and current information about competitive practices.

But they should still have a voice, particularly if they're upset about something, countered Rogge Dunn, a partner at Dallas' Clouse Dunn Khoshbin.

"Obviously, people who feel that their opinions are heard are less likely to file suit or cause problems," Dunn said. "How can it hurt to survey your shareholders and see what they think? . . . If you're inclusive of the shareholders and they're satisfied, you're less likely to have disgruntled shareholders causing problems and potentially filing suit."

Dunn believes that say on pay could help eliminate litigation over excessive salaries, noting that a growing number of companies are being sued over the terms and conditions of senior-level compensation.

In 2006, he settled a lawsuit for $2.8 million on behalf of former Pizza Inn Inc. CEO Ronnie Parker, who was fired and sued by his company after shareholders argued that his contract was too rich. Pizza Inn v. Akin Gump, No. 04-10265 (Dallas Co., Texas, Dist. Ct.).

"The good old days of a County Club board rubber-stamping proposed executive compensation are over because of abuses that have led to lawsuits," Dunn said.

"I'm getting more calls from my clients on this issue than I have in past years," Dunn said. "They are wanting to make sure that they set executive compensation at a level that is appropriate."

Officials at Blockbuster said they had similar goals, which is why they gave shareholders the right to vote on employee compensation. Their first vote will take place next spring.

"It's a clear sign that Blockbuster and its board of directors are committed to implementing strong corporate governance practices with the goal of complete transparency, and we will certainly take into account feedback from shareholders in carrying out compensation," said Blockbuster spokeswoman Karen Raskopf.

Officials at Verizon, whose shareholders will also vote on compensation next spring, said: "We believe that it is important to engage in an ongoing dialogue with shareholders and others."

Meanwhile, Johanna O'Loughlin in the Pittsburgh office of Reed Smith called say-on-pay policies "questionable" because they don't address specific concerns or perceived flaws with compensation plans.

"It isn't clear what a 'no' vote means or what steps a company should take in response," O'Loughlin said.

To avoid problems with shareholders over compensation, O'Loughlin advised companies to focus on what key shareholders want to see in the compensation plan — usually strong links to performance.

Also, make sure that disclosure is transparent in describing the plan, including the operation of the performance metrics, O'Loughlin said.

Talking to shareholders in the off-season about these issues also is a good practice, she added.

Larry Mandala of Dallas-based Munck Butrus Carter, who advises companies on executive compensation, said his clients are staying away from say on pay for now.

"None of my clients are ready to jump in right now," Mandala said.

"This is really only the second year that you've seen the mad dash by large companies to take a look at the issue."

Mandala said his clients, which are smaller public companies, "want to see what the larger companies do as a whole before they jump in."