Client Advisory

KELLEY DRYE

SECURITIES PRACTICE GROUP

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House Passes Controversial Executive Compensation Bill

On Friday, November 11, 2005, the House of Representatives (led by Rep. Barney Frank) passed "The Protection Against Executive Compensation Abuse Act," which aims to address perceived runaway executive compensation by requiring greater disclosure of executive compensation to shareholders.The bill, which can be found at http://www.house.gov/banking_democrats/HR4291BillLanguage.pdf and would amend Exchange Act Section 16, emphasizes executive compensation disclosure rather than placing substantive limits on executive compensation.Following are some of the bill's provisions:

Executive Compensation Plan

The bill would require that public companies include in their proxy solicitations for shareholder approval a comprehensive "Executive Compensation Plan," including disclosure as to: (a) all types of compensation to be paid and as to compensation policies for top executives (including performance targets used to determine compensation (and whether the targets were met in the prior year)); and (b) clawback policies as to executive compensation (such as recapture of performance-based bonuses for negatively restated periods).

Shareholder Approval of Golden Parachutes

The bill would require that shareholders separately approve any additional compensation for top executives that coincides with the sale or purchase of substantial company assets.

Compensation Disclosure on Website

The bill would require that companies include on their websites clear and simple disclosures explaining their SEC filings regarding compensation.

Definition of "Top Executives"

Top executives would be defined as:

- in the case of companies with under $250 million in total assets, the CEO;
- in the case of companies with $250 million to $500 million in assets, the CEO and the next two highest paid executives; and
- in the case of companies with more than $500 million in total assets, the CEO and next four highest paid executives.

Background

A white paper issued relating to the bill indicated that, according to the Corporate Library's recent CEO Pay Survey, the median total compensation received by CEOs increased 30% in fiscal 2004, with the average increasing 91% (driven by 27 CEOs receiving compensation over 1,000% greater than their previous year's pay). A *USA Today* report found that the median 2004 CEO compensation was $14 million. The *USA Today* study found that the average rank-and-file worker's pay increased 2.5%. The white paper indicated that the disparity between CEO and rank-and-file workers' compensation has grown significantly over the last few years, so that in 2003 the average large-company CEO received approximately 500 times the pay of an average worker (in 1991 the ratio was about 140:1). The paper indicated that compensation schemes may give executives a perverse incentive to shirk their fiduciary duty to shareholders in a number of ways, such as by manipulating earnings by using aggressive accounting methods or by entering into unprofitable mergers and acquisitions so as to receive additional compensation for the transaction or to procure a plum job post-acquisition.

For more information please contact:

M. Ridgway Barker
Stamford
(203) 351-8032
mrbarker@kelleydrye.com

Randi-Jean G. Hedin
Stamford
(203) 351-8107
rhedin@kelleydrye.com

Jeanne R. Solomon
New York
(212) 808-7513
jsolomon@kelleydrye.com