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GOVERNANCE
PERSPECTIVES

DEBATE ABOUT "GOLDEN LEASH" PAYMENTS TO DIRECTOR NOMINEES CONTINUES

In the past few years, much attention has been paid to the issue of special compensation arrangements sometimes paid by so-called activist shareholders to their director nominees in proxy fights. Activists claim that these arrangements provide appropriate compensation for insurgent director nominees and are necessary to recruit qualified candidates for board service, particularly in the case of a contested election. Companies argue, however, that the payment of incentive compensation by a sponsoring shareholder establishes a two-tiered compensation structure for the board, creates dissension in the boardroom, and fosters continuing allegiances between the director and the activist shareholder following the election. Further, if the sponsoring shareholder has a short-term investment horizon, these arrangements may incentivize the director nominees to focus on the activists' interests or short-term goals at the expense of long-term value creation for all shareholders. As counsel to Corporate America, we firmly believe that these special compensation arrangements improperly incentivize activist-sponsored candidates and undermine boardroom stability.

Some companies have attempted to address the issues relating to special director compensation payments by adopting corporate bylaws that expressly prohibit third-party payments to directors for board service other than the typical retainer, expense reimbursement, and indemnification offered to director candidates. Proxy advisory firms such as ISS, however, have resisted bars on these types of special compensation arrangements, claiming that they restrict shareholders' ability to nominate and elect directors in a proxy contest, and thus infringe on the shareholder franchise. ISS has said it would not object to mandated disclosures of these types of arrangements.

Most recently, Nasdaq has joined the debate. Nasdaq is expected to propose new rules requiring disclosure of any compensation arrangements with individuals who serve as dissident director candidates. We applaud Nasdaq's efforts to put sunlight on this so that shareholders can make an informed decision as to whether these compensation arrangements will harm boardroom dynamics and whether an activist's director candidates will be financially incentivized to the preferences of a single constituency through separate compensation. We hope sunlight becomes the disinfectant that will rid Corporate America of these two-tiered director compensation structures, encouraging all board members to align in their focus on the long-term prospects of the company and the interests of shareholders as a whole.

LAWYER CONTACTS

For further information, please contact your principal Firm representative or one of the lawyers listed below. General email messages may be sent using our "Contact Us" form, which can be found at www.jonesday.com/contactus/.

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