



# New Wave of Proxy Statement Injunctive Lawsuits: How to Win & Prevent Them

## ALERT

As many public companies are painfully aware, the plaintiffs' class action bar has historically filed shareholder class and derivative suits challenging the sufficiency and legality of disclosures relating to shareholder approval of M&A transactions and Internal Revenue Code Section 162(m) performance-based incentive compensation programs.

Recently, a new litigation tactic has emerged in which plaintiffs seek to enjoin public companies from proceeding with annual meetings and shareholder approval on proposals to increase the share reserve for stock plans and "Say-on-Pay" ("SOP") votes until the company publicly files supplemental disclosures. Over 20 of these cases have been filed to date. The obvious goal of the plaintiffs' bar is to use the threat of delaying the shareholder vote as a means to obtain attorney fees. We are aware of at least one preliminary injunction motion targeting a stock plan proposal as well as two settlements also involving stock plan proposals.

The recently filed *Symantec*<sup>1</sup> case presents an interesting example of the new litigation tactic in action. The plaintiff in that case filed a motion seeking to enjoin Symantec's annual shareholder meeting claiming that the company was asking shareholders to vote on an SOP proposal without providing adequate information. Plaintiff argued that shareholders were entitled to more detailed public disclosures regarding the work of the company's compensation consultants, certain compensation metrics underlying the SOP proposal, and other details regarding the company's compensation-related processes. Lacking any precedent for such an injunction, the court denied the motion.

### Lessons Learned in Preparing Proposals

Based on a review of several recent challenges, we would recommend the following best practices for future proxy proposals to dissuade the plaintiff's bar from filing a complaint or to increase the odds of a swift victory in the event litigation does occur.

#### 1. Stock Plan Share Reserve Increase Proposals

- Disclose the number of shares currently available for issuance under the stock plan. As many claims are based on a failure to discuss the need for new shares, include an explanation as to why the existing share reserve is insufficient to meet the future needs of the company. For example, a disclosure might explain that based on the current burn rate and anticipated hiring of new executive officers, the company expects to exhaust the existing share reserve in the next 12 months and without the additional shares the company would be unable to attract and retain the most qualified employees.
- Explain the planned use of the existing share reserve and the additional shares, including how long the company expects the new share reserve to last.
- Describe the methodology used to determine the requested number of additional shares. As part of the methodology, the company should consider, and discuss in the proposal, the historical and post amendment annual burn rate, shareholder value transfer and overhang with respect to the stock plan.

## 2. Say on Pay Votes

- Remove any quantitative data or items that need further explanation from the SOP proposal. Sometimes “less is more.”
- In the Compensation Discussion and Analysis (“CD&A”):
  1. Discuss the process used to hire the company's compensation consultant and summarize the consultant's role and any advice/recommendations.
  2. Clearly disclose how management is involved in the compensation process.
  3. Minimize references to specific peer group benchmarking on compensation targets and payouts and, in the event such references are necessary, provide a summary of the 25th, median and 75th percentiles of pay in the peer group.
  4. Carefully assess any proposed statements correlating executive pay and peer group ranking to company performance and, where possible, link compensation changes to internal company year-over-year performance rather than relative to the peer group.
  5. Discuss the underlying analysis or criteria and any applicable weighting used to make specific decisions.
  6. Clearly describe the basis for any executive pay changes disclosed in the CD&A; for example, a peer group change or target compensation percentage increase.

### **Litigation Considerations**

If your company is in the unfortunate position of facing litigation seeking to enjoin a shareholder vote, the following are some of the many action items that should be considered in dealing with the litigation:

- Act quickly to establish that the necessary legal protections will apply; for example, process-oriented defenses available under Delaware and most other state law.
- Work with expert executive compensation counsel to evaluate existing proxy disclosures to assess and reduce ongoing risks posed by the litigation.
- Structure the litigation so that any threatened motion seeking injunctive relief will not disturb a planned proxy vote.
- Analyze whether supplemental disclosures are appropriate and, if so, whether they will trigger fee liability to the suing plaintiffs' lawyers.
- Reduce or eliminate the burden on senior executives/outside directors by anticipating and addressing discovery obligations.
- Evaluate preliminary pleading challenges that may terminate the litigation at the outset and without further legal expenditure.
- To the extent any further disclosures occur, implement such disclosures in a manner that reduces as much as possible the company's risk of liability.
- Confirm that all appropriate document retention practices are in place.
- Evaluate whether insurance policies will apply to such suits and begin a dialogue with carriers.
- Consider the impact and applicability of existing indemnity provisions.
- Consider whether any proposed settlement will actually benefit the company and its shareholders and, if a settlement occurs, structure the settlement in a manner that minimizes any negative financial impact on the company.

Deft handling of court complaints over executive compensation can result in an early end to the litigation, minimize legal costs, and reduce distractions to senior management. While the *Symantec* decision may slow down the plaintiffs' bar, we expect that challenges to proxy disclosures, particularly stock plan proxy proposals, will continue at a rapid pace through this proxy season.

The new reality is that your executive compensation counsel must have up-to-date knowledge of the most recent court developments and, if necessary, must work seamlessly with litigators experienced in winning early dismissals of suits over executive pay. Although we cannot guarantee that a company will avoid being sued, following the suggestions above will reduce the likelihood of a suit and increase the odds of an early, favorable conclusion.

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For more information contact [Brett Cooper](#), Partner, [Capital Markets](#), [Jon Ocker](#), Chair, [Compensation & Benefits](#) or [Michael Torpey](#), Chair, [Securities Litigation & Regulatory Enforcement Group](#).

<sup>1</sup>*Gordon v Symantec Corporation, et al.*, Case No. 1-12-CV-231541 (Cal. Santa Clara County Superior Court)

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