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Inside This Issue

Say-on-Pay Derivative Litigation Update

By Michele D. Johnson and Colleen C. Smith

The Dodd-Frank Act requires most publicly traded companies to seek a non-binding shareholder vote to approve the company's executive compensation plans. In 2011, the first year of the so-called "say-on-pay" vote, approximately 40 companies failed to receive support from a majority of their shareholders for their executive compensation proposals. Almost half of these companies were promptly sued. In each case, shareholders filed derivative actions claiming that the directors breached their fiduciary duties by approving pay raises and bonuses to executives in a year when, according to the plaintiffs, the companies performed poorly.

Only a few courts have addressed these claims. Of the rulings to date, a consensus is emerging that an adverse shareholder say-on-pay vote does not give rise to a valid breach of fiduciary duty claim and is not a sufficient basis to overcome the business judgment rule. The following provides a brief update regarding the decisions reached, and a preview of the 2012 proxy season.

Teamsters Local 237 Additional Security Benefit Fund v. McCarthy (Beazer Homes)

Beazer Homes was one of the first companies to report a negative say-on-pay vote. A shareholder filed a derivative action, alleging that the Beazer Homes board breached its fiduciary duties by approving excessive executive pay, by recommending that shareholders approve the executives' compensation and by not rescinding the compensation program.

The defendants and the company moved to dismiss, arguing that, under Delaware law, the plaintiff failed to plead that a demand on the board to file suit on behalf of the company would have been futile, and that the complaint did not allege particularized facts sufficient to rebut the business judgment presumption. The Georgia Superior Court agreed and dismissed the suit.[1]

The court concluded that demand was not excused because the complaint failed to raise a reasonable doubt either that a majority of the board was disinterested, or that the challenged decision was the result of a valid exercise of business judgment. Where only one member of the seven-member board received the challenged pay, the fact that the directors had approved the challenged compensation was not sufficient to establish that the board could not faithfully evaluate a litigation demand. Moreover, the mere fact of the adverse say-on-pay vote did not raise a reasonable doubt that the compensation decisions were the product of a valid exercise of business judgment. And because Dodd-Frank expressly provides that a say-on-pay vote is not binding and does not change directors' fiduciary duties, the directors were not obligated to rescind the executives' compensation following the vote.

In addition, the court concluded that the complaint also failed to state a claim because no alleged facts justified departure from the business judgment rule or established that the directors misled shareholders regarding the company's pay-for-performance compensation policy.

NECA-IBEW Pension Fund v. Cox (Cincinnati Bell)

Within days of the *Beazer Homes* decision, the United States District Court for the Southern District of Ohio reached the opposite result under Ohio law, refusing to dismiss a similar say-on-pay derivative action filed by shareholders of Cincinnati Bell, Inc.[2] (Cincinnati Bell).

The *Cincinnati Bell* defendants made arguments similar to those advanced in *Beazer Homes*: both that pre-suit demand on the board was not futile, and that the complaint failed to state a claim in light of the business judgment rule. Applying Ohio law, according to the state of incorporation of Cincinnati Bell, Inc., the district court held that the plaintiff had stated a plausible claim that "the multi-million dollar bonuses approved by the directors in a time of the company's declining financial performance violated Cincinnati Bell's pay-for-performance compensation policy" and constituted an abuse of discretion or bad faith. The court found the negative shareholder advisory vote on executive compensation to be "direct and probative evidence that the 2010 executive compensation was not in the best interests of the Cincinnati Bell shareholders."[3] In contrast to Delaware law, under Ohio law, the plaintiff was not required to plead with particularity facts sufficient to rebut the business judgment presumption, leaving the court to conclude that although the defendants may offer the business judgment rule as an affirmative defense at trial or summary judgment, dismissal on this ground was not warranted.

The district court also rejected the defendants' contention that the plaintiff failed to plead demand futility. In another departure from Delaware law, demand under Ohio law is presumptively futile when the directors are involved in the challenged transaction. The court reasoned that demand was futile because the directors devised, approved, and recommended the challenged compensation, and then suffered a negative shareholder vote on the plan.

Plumbers Local No. 137 Pension Fund v. Davis (Umpqua Holdings)

In *Plumbers Local No. 137 Pension Fund v. Davis*,[4] the court concluded that the plaintiffs did not plead demand futility, as only one member of the 10-member board received the challenged compensation, and the fact that the other directors were involved in determining or approving the challenged compensation did not raise a reasonable doubt regarding their independence and disinterestedness under Oregon and Delaware law. The court rejected the plaintiffs' reliance upon *Cincinnati Bell*.

The court also concluded that because compensation determinations are typically within the business judgment of the board, neither the allegation that executive compensation was not aligned with corporate performance, nor the negative say-on-pay vote, raised a reasonable doubt that the directors exercised their good faith business judgment.

The Rest

In the four other say-on-pay cases decided to date, courts have sided with the *Beazer Homes* decision and have dismissed the cases at the pleading stage. In *Jacobs Engineering Group, Inc. Consolidated Shareholder Derivative Litigation*,[5] the California state court twice sustained the defendants' demurrer for failure to plead demand futility under California (and identical Delaware) law, noting that executive compensation is generally a matter of business judgment that the courts will not second-guess.

In the *PICO Holdings* cases, the federal court dismissed the claim under the Dodd-Frank Act, which "did not create a private right of action or create new fiduciary duties," but remanded the state law claims to state court.[6]

In *Laborers' Local #231 Pension Fund v. Intersil*,[7] the Northern District of California (applying Delaware law) granted a motion to dismiss based on the plaintiff's failure to plead facts sufficient to excuse a pre-suit demand on the board, while leaving open the possibility that a negative shareholder vote "may be used as evidence" — albeit insufficient by itself — to raise a reasonable doubt that a company's directors exercised their good faith business judgment in setting executive compensation.

Finally, in *Weinberg v. Gold*,[8] the District of Maryland (applying Maryland law) held that the BioMed directors' participation in issuing the proxy statement and approving the challenged compensation, and their refusal to modify the executive compensation in response to a negative say-on-pay vote, did not excuse a pre-suit demand.

Predictions

While many say-on-pay lawsuits filed in the wake of the 2011 proxy season remain undecided, the consensus so far suggests that other courts will reject such claims. Less clear is how courts will address these issues following the 2012 proxy season. A few principles drawn from the cases that have been decided provide some clues to the future of say-on-pay litigation.

First, the *Cincinnati Bell* court's denial of a motion to dismiss has encouraged a proliferation of say-on-pay claims against directors of other companies with failed say-on-pay votes. Almost half of the companies with failed say-on-pay votes during 2011 were named in shareholder suits. This wave of litigation is probably not over.

Second, the outcome of these cases may depend substantially upon the applicable law. In *McCarthy* (*Beazer Homes*) and *Davis* (*Umpqua Holdings*), the dismissals were based on Delaware law. Courts applying Delaware law seem unlikely to depart from these courts' reasoning, although the *Intersil* court's reasoning leaves open the possibility that a plaintiff might satisfy Delaware's pleading standards by alleging something more than just a failed say-on-pay vote. In contrast, the less stringent requirements of Ohio law enabled the plaintiff in *Cox* to survive the pleading stage. Future decisions will inform whether *Cincinnati Bell* is an outlier, or whether say-on-pay claims can survive motions to dismiss under any other state's laws.

Third, the published decisions address claims premised upon only a single failed say-on-pay vote. No company has yet failed two votes. While the existing decisions will be instructive, the new issues presented by two consecutive failed (or narrowly successful) say-on-pay votes are yet to be tested and may be more challenging for those companies and their directors to overcome at the pleading stages. ■

Endnotes

1 *Teamsters Local 237 Additional Sec. Benefit Fund v. McCarthy*, No. 2011-CV-197841 (Ga. Super. Fulton County Sept. 16, 2011).

2 *NECA-IBEW Pension Fund v. Cox*, No. 11-CV-451, 2011 WL 4383368 (S.D. Ohio Sept. 20, 2011).

3 *Id.* at *3 n.4.

4 No. 11-CV-633-AC, 2012 WL 104776, at *2 (D. Ore. Feb. 23, 2012).

5 No. BC457808 (Los Angeles Super. Ct. Mar. 6, 2012 & Nov. 11, 2011).

6 *Assad v. Hart*, No. 11-CV-2269 WQH (BGS), at *5; *Dennis v. Hart*, No. 11-CV-2271 WQH (WVG), at *5 (S.D. Cal. Jan. 6, 2012).

7 No. 11-CV-04093 EJD, 2012 WL 762319, at *1-2 (N.D. Cal. Mar. 7, 2012).

8 __ F. Supp. 2d __, 2012 WL 812348, at *5 (D. Md. Mar. 12, 2012). Latham & Watkins LLP represents BioMed in this case.

US Proxy Season 2012 Early Trends

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Proxy season 2012 is now underway and many larger US public companies are expected to hold their second mandatory non-binding say-on-pay votes this year. As of the last week of April 2012, approximately 260 of the 3,000-plus companies that will hold say-on-pay votes this year have already done so. Based on these meetings and proxy materials filed with the US Securities and Exchange Commission by many more companies, we are already seeing some important trends.

First, with respect to vote results, this season is starting out pretty much the same as the 2011 season ended. With respect to the 8 percent of companies that have already held say-on-pay votes for the current year, five companies have failed to obtain 50 percent support, 71 percent have passed with over 90 percent support, and 91 percent have passed with more than 70 percent support.

Second, proxy advisers continue to be very influential, with Institutional Shareholder Services (ISS), the largest and the most influential US proxy adviser, recommending negative say-on-pay votes at approximately 16 percent of the companies that have met in 2012 (up from 12 percent in 2011). On average, shareholder support has been 27 percent lower at companies that received negative ISS recommendations.

Third, continuing last year's trend, companies are publicly challenging negative proxy adviser recommendations, some anticipatorily in their initial proxies, often without naming the proxy advisers though clearly targeting their voting policies, and others in response in supplemental proxy materials. As of the end of the last week of April 2012, 35 companies had already filed supplemental materials calling out proxy advisers and challenging their negative recommendations.

Fourth, it is already clear that the major battleground this year will be on the issue of how well company executive pay aligns with company performance, so-called "pay for performance." While this was also the single most frequently disputed issue in 2011, pay for performance will be an even bigger issue this year.

ISS fired the first salvo on the 2012 pay for performance front by substantially revamping its blunt 2011 voting policy. While ISS' 2012 pay for performance policy is a substantial improvement over its 2011 policy, it still leaves much to be desired. In response to the problems with ISS' 2011 and 2012 pay for performance voting policies, compensation consultants and other proxy advisers have raced to gather data and build better analytical models to compete with ISS, and to provide investors with more meaningful data and analytics on company pay and performance. These analytics attack the ways in which ISS determines peer groups for applying its tests, its exclusive focus on total shareholder returns (stock appreciation plus reinvested dividends) as the only measure of a company's performance and its use of pay opportunities rather than realizable or realized pay to determine executive pay. This competition in the market should elevate the quality of the debate on pay for performance, result in more thoughtful and holistic analyses than in the past, and hopefully begin to define the boundary between legitimate shareholder involvement and micromanagement of executive pay plans.

The next issue of *The Working World* will provide a further update on the US proxy season and a closer look at the battle over pay for performance. ■

BCE Group Highlights

Latham's Benefits, Compensation and Employment (BCE) Group frequently produces thought leadership and webcasts that may be of interest. A selection of recent offerings appear on the BCE Practice page at http://www.lw.com/practices/BenefitsCompensationAndEmployment.

Thought Leadership

State Wage Theft Prevention Laws
New York and California have enacted laws requiring all private-sector employers, regardless of size, to make certain written disclosures to employees.

Proxy Season 2012: The Year of Pay for Performance
A review of how proxy advisors, compensation consultants, companies and others are analyzing the alignment between executive pay and company financial and total shareholder return performance.

California Supreme Court Clarifies Meal and Rest Break Rules
Employers must relieve employees of all duties, but need not prevent employees from working during breaks.

April 2012 Key Changes to UK Employment Law and Employment Related Tax
A summary of the key changes to UK tax rules and employment law announced or due to be implemented in Spring 2012.

Webcasts

The recent 3-part 2012 Proxy Season webcast series is now available for on-demand viewing. Click on the links below to register for the applicable program.

- Addressing ISS and Glass Lewis Institutional Investor Voting Policies
- Dealing With Say on Pay and Shareholder Proposals
- Preparing for the 2012 Season

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Be a Good Sport!: Managing Employee and Staff Disruptions During the 2012 Olympic Games

By Gretchen Lennon

The 2012 Olympic and Paralympic Games (the Games) will be hosted in London this summer and it is not only the athletes who need to ensure they are well prepared. If they have not already done so, employers should consider implementing adequate policies and procedures, and, if necessary, temporarily amending working practices, to ensure they maintain a high level of employee productivity while preserving a healthy relationship with staff during the Olympics. Set out below is a number of the potential challenges that employers in the UK are likely to face this summer, and the practical steps that can be taken to alleviate their impact.

Requests for Leave

The Challenges

Employers should expect a greater than usual number of requests for annual leave during this period. Those hoping to take vacation will include not only the usual holiday-makers wishing to take time off during the peak vacation season, but will extend to employees who have been able to get hold of tickets for an Olympic or Paralympic event, those who have volunteered to assist with the organization and coordination of the events as 'Games Makers,' and finally those who simply want to take vacation to watch the events from the comfort of their own homes. The challenge is to deal with these requests fairly and reasonably in light of conflicting business requirements and employee expectations.

The Solutions

Employers must begin by considering the needs of their businesses and whether they will be able to grant the requests of all employees wishing to take time off for the Games. Consideration should be given to the adequacy of an existing annual leave policy, particularly whether a specific policy should be implemented to deal with vacation requests during this period. Generally, employers in the UK have the right to decline employees' vacation requests (as long as employees are permitted to take their annual vacation entitlement at some other time in the applicable year). However, employers should take care to ensure that their approach to granting or denying vacation requests is fair and consistent, in order to avoid potential conflict or claims of unfair discrimination.

Balloting system. One solution may be to adopt a balloting or other objective system to ensure fair and impartial selection where an employer is unable to grant all received requests. This would be preferable to a 'first come, first served' system which, while it may at first glance seem like a reasonable method of selection, may risk disadvantaging part-time employees or those currently on leave.

Flexible working. Employers could also consider implementing a more flexible approach to working hours whereby employees could arrive earlier in the morning, in order to leave earlier in the evening, or vice versa. Further, employees could reduce the work week to four days, while still working the equivalent number of hours of a full working week. The viability of this approach will depend on a number of considerations, including the nature of the employees' work and the readiness of other employees to accommodate these changes by working longer hours, if necessary.

Working from home. Permitting employees to work from home may also be feasible for certain organizations and will alleviate any commuting problems that may be encountered. However, there are a number of important considerations that employers should bear in mind before implementing a blanket policy that allows all employees to work from home. Firstly, organizations will need to have appropriate information technology (IT) infrastructure in place, such as ensuring employees (a) have the necessary equipment, such as a computer (although equipment does not have to be provided at the employer's expense, employers are responsible for any equipment they provide) and (b) can remotely access the relevant networks and systems. In addition, it will necessarily be more difficult to supervise employees or monitor their performance or hours of work if they are not required to attend the workplace. Confidentiality may also be a concern if employees will be permitted to take confidential documents home. Finally, because employers are still responsible for employees' health and safety when they are working from home, it may be advisable to carry out workplace risk assessments in order to identify any hazards, such as loose wires or badly lit computer screens, and minimize any risks these pose. Ensuring employees are adequately set up to work from home may be a costly and time-consuming exercise and, if such systems are not already in place or are unlikely to be used beyond this summer, this may not be a practical solution.

The most important consideration for handling requests for leave during the Games will be to ensure that the policy is clearly communicated to employees in good time, and applied consistently throughout an employer's organization .

Short Term Absenteeism

The Challenges

It is likely that, during the Olympics and Paralympics, employers will notice a spike in short-term absenteeism: employees might call in sick in order to avoid using any of their annual leave entitlement, disappear during working hours (perhaps for an extended lunch break) or arrive late or leave early without authorization. This may be a deliberate decision on the part of ticket-holders who have been denied annual vacation for example, or could simply be because employees have been caught in the heavy traffic generated by the Games. Therefore, employers will need to consider how to fairly, but effectively, stem a trend that could prove detrimental to both overall productivity and staff morale.

The Solutions

The issue of employees suspected of 'pulling a sickie' conveniently timed to coincide with a particular Olympic or Paralympic event may be difficult for employers to navigate. If an employer suspects that an employee may not genuinely be sick, formal disciplinary proceedings may be appropriate. While it can be difficult to disprove an employee's claim that he or she was sick, an incriminating update on a public forum, such as a social networking website, may be very useful in these circumstances. However, absent any proof that the employee was not actually sick, the employer may have little remedy, as implementing a disciplinary hearing arguably means the employee is being accused of lying, which could possibly lead to a claim for constructive unfair dismissal as a result of a breakdown in mutual trust and confidence.

As an alternative, preventative measures should be taken as soon as possible to dissuade employees from trying this ruse during the Games. Where an organization 's sickness absence policy is not contractual, one solution may be to amend the current policy to require employees to submit medical certificates for any absence taken as sick leave during the course of the Olympics and Paralympics, even if such absence is only for one day. However, if a sickness absence policy forms part of an employee's terms and conditions of employment, any proposed amendments will require the employee's consent before they can be implemented.

Employers should ensure that employees are aware of the terms of the sickness absence policy and should be warned that breaches of the policy may lead to disciplinary action, regardless of whether any amendments to an existing sickness absence policy are proposed.

In circumstances where employees take unauthorized absences without authorization (*i.e.*, by leaving work prematurely to catch an early evening event), employers can take disciplinary action and, following an investigation, may perhaps issue employees with a warning that repeat offences may lead to more serious sanctions. Offenders may be required to make up time for such unauthorized absences, or may be required to take the time spent off work as annual leave. However, employers should be mindful of the need to deal fairly with employees who have a reasonable justification for lateness, such as difficulties with commuting in light of increased traffic (which is expected to have a severe impact on journey times in London this summer). As mentioned above, employers should consider whether more flexibility in relation to working hours or permitting employees to work from home are viable solutions in light of their business needs.

Following the Games in the Workplace

The Challenges

Permitting employees to watch the Games in the workplace, or to follow live updates via Internet feeds, might be taken as a license to work less productively, or to take too frequent breaks. Meanwhile, IT system speeds might be negatively impacted if events are to be streamed through the organization 's network.

The Solutions

Employers should consider whether to permit employees to follow the Games using office IT facilities. Generally, employers will have the right to either restrict or monitor the use of the Internet, and it is important that employees are made aware of this. If permitting employees to watch the Games using their office computers is not practical, or for those employees who do not have access to computers at work, employers may consider screening particular events, perhaps in a communal area such as the workplace canteen. This may have the combined benefit of reducing IT traffic while also regulating staff access to the Games and boosting workforce morale.

Let the Games Begin!

In adopting concessionary solutions in order to deal with any of these problems, employers should be aware of other potential pitfalls. Employees with no interest in the Games, and whose journey times are not affected by them might be estranged by any alterations to working hours or arrangements, while working from home raises important issues of IT access, health and safety concerns and the need to ensure data confidentiality. Employers should give careful consideration to implementing a practical solution for their business which treats employees fairly and reasonably, whilst minimizing disruption to the day-to-day running of the business.

A recent poll in the UK found that 88 percent of employees questioned are largely unaware of the policies their employer has in place for dealing with potential worker absences and business disruptions during the Games. Clear communication is therefore essential if employers are to avoid confusion and minimize any reduction in productivity. Through careful consideration of the specific needs of their own organization, by instituting the appropriate procedures and policies as soon as possible, and by ensuring that employees are aware of these procedures and policies, employers should be in a position to manage employee expectations and minimize disruption to deliver a winning performance for their businesses during the 2012 Olympic and Paralympic Games. ■

STATUS UPDATE: #YOU'RE FIRED! @yourjob NLRB Guidelines on Employer Social Media Policy

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As previously detailed in *The Working World*, Issue 10,[1] the US National Labor Relations Board (the NLRB) has challenged some employers' decisions to discipline employees for their use of social media sites. The NLRB recently issued a report presenting various case developments and emerging issues in the social media context, including 14 examples of employer disciplinary action and the agency's determination in each case.[2] This update provides additional guidance to employers in a rapidly evolving and often unpredictable area of the law.

The NLRA

Section 7 of the National Labor Relations Act of 1935, as amended (the NLRA) guarantees an employee the right to engage in "concerted activities for the purpose of collective bargaining or other mutual aid or protection."[3] Section 8(a)(3) of the NLRA prohibits employers from discouraging "labor organization," defined as "any organization of any kind… in which employees participate and which exists for the purpose, in whole or in part, of dealing with employers concerning grievances, labor disputes, wages, rates of pay, hours of employment, or conditions of work."[4]

An employer's social media policy will be in violation of Section 8(a)(1) of the NLRA, and deemed unlawful, if it is found "to interfere with, [or] restrain … employees in the exercise of the rights guaranteed in section 7 [of the NLRA]."[5] If the policy does not explicitly restrict Section 7-protected activities, it may still be found unlawful if employees would *reasonably construe* the policy's language to prohibit Section 7 activity.[6]

A Savings Clause is No Salvation

While every instance of discipline for employee misuse of social media will require examination of the specific content and context of the employee's comments, the NLRA has shown that it will focus on, and ultimately will dissect, the language of the employer's social media policy. The cases outlined below illustrate the need for careful drafting and caution against ambiguous descriptions and reliance on general limiting language.

In its second report, the NLRB explicitly advises that an employer's inclusion of language stating that its policy will not be interpreted or enforced in a manner inconsistent with employee Section 7 rights is not sufficient. We therefore no longer believe it advisable for an employer to simply add savings language to its social media policy. Instead, we believe the preferred approach is to include specific examples of policy violations, as suggested by the cases below, in order to ensure that an employee understands exactly which uses of social media are protected and which are not. Any social media policy that fails to provide specific examples of potential violations and activities that are allowed will be at risk of being deemed overbroad.

The recent NLRB guidelines highlight various reasons for which an employer's social media policy could be found unlawful. Policies that generally prohibit employees from "making disparaging comments" or that prohibit "insubordination or other disrespectful conduct" about the employer in social media are classified as overbroad. The NLRB explained that a reasonable employee could construe such policies to restrict protected Section 7 activity, because comments regarding an employee's wages, rates of pay, or terms and conditions of employment, even if disparaging, could be classified as protected.

Policies that prohibit "inappropriate conversation" or "unprofessional communication" have been found unlawful for similar reasons. In these cases, the NLRB focused on each policy's failure to specify the exact type of communication that qualifies as 'appropriate' or 'professional.' As a result of this ambiguity, employees would be required to infer that certain protected rights, such as the right to converse about wages or terms and conditions of employment, would not be restricted under the policy.

As noted above, the NLRB cases caution against employer reliance on savings language in social media policies. For instance, an employer's policy was deemed unlawful when it excepted the "discussion of terms and conditions of employment in an appropriate manner" from its prohibition on an employee's comments about the employer in social media. Although it had attempted to identify and permit specific Section 7 communications, the employer ultimately restricted its employees' ability to discuss other protected Section 7 matters, such as wages and terms and conditions of employment, that might be considered "inappropriate."

It is therefore imperative for an employer to assure that its social media policy narrows the scope of potential violations to cover only those specific communications that are not protected, and to ensure that such examples could not be interpreted to infringe protected Section 7 rights.

Concerted Communication?

Even if the employer's social media policy is found to be unlawful, the NLRB will not automatically presume the imposed disciplinary action was also improper. Such a determination requires a review of the content and context of the employee's offending activity. In order to determine whether the employee's social media communications qualify as protected "concerted activity," the NLRB will consider whether the employee acted with other employees and not solely by, and on behalf of, himself or herself, in an effort to initiate, induce or to prepare for group action rather than merely expressing an individual gripe.

As noted in our earlier discussion of this topic, the NLRB tends to disallow employer discipline of employees for using strong language or engaging in offensive actions in the context of protesting working conditions. The NLRB's second report, which analyzes 14 separate employer disciplinary actions, highlights just how nuanced the agency's factual determination can be in practice.

In several instances in which the NLRB invalidated the employer's social media policy, the employee's discharge under that policy was still upheld because the communications at issue did not warrant protection (*i.e.*, they were not "concerted activity"). The agency upheld the employee's dismissal because the activities were found to be mere expressions of personal anger or individual gripes which bore only a tangential relationship to the terms and conditions of employment, and which were not intended to induce group action (examples include, a bartender complaining on a social network about dishonest employees who gave away alcohol; and a phlebotomist's profane outburst on a social network against her employer and the coworkers she hates).

Where there is no clear audience for the individual rant, the NLRB will generally find that the communication is not intended to induce group action. If the commentary is directed to a social media space that could reach coworkers, however, such as when the employee and co-workers are social network friends, the NLRB will examine the audience's reception of the statement. If a complaint is made to an audience of other workers and it does not elicit a response, the guidelines suggest that the NLRB would find the communication unprotected (for example, a truck driver's social network complaints about his supervisor's unresponsiveness, which went unacknowledged by his co-worker social network friends, were found to be an individual gripe not initiated to induce group activity). If other workers pick up or develop the discussion, the NLRB is more likely to find that the comment induced group action. This, in turn, can convert what would otherwise have been an "individual rant" into concerted labor activity (for example, the agency found a veterinarian hospital employee's social network complaint about a co-worker's promotion to be protected concerted activity when it induced a social network conversation with three other coworkers regarding the hospital's promotion policy). Employers should note that communications *will* constitute concerted activity whenever there is group interaction regarding Section 7 rights; the employees need not act (or even have a current plan to initiate action) in order to meet this standard.

Keeping Your Company's Social Media Practices Up-to-Date

In light of the speed at which technology and social media usage have expanded in the workplace in recent years (with no slow-down in sight), and given the NLRB decisions and guidelines discussed above, now is the time for employers to review their social media policies. Please contact any member of the Latham & Watkins BCE team for assistance in drafting or modifying your company's policy and for advice on handling employee issues related to social media usage.

In the Next Issue: A Look at Employer Social Media Rules in the UK. ■

Endnotes

1 *The Working World*, Issue 10, December 2010 can be found at http://www.lw.com/thoughtLeadership/working-world-december-2010.

2 *Report of the Acting Gen. Counsel Concerning Social Media Cases*, N.L.R.B. OFFICE OF THE GEN. COUNSEL, Jan. 24, 2012, *available at* http://nlrb.gov/news/acting-general-counsel-issues-second-social-media-report.

3 29 U.S.C. § 157 (2012).

4 *Id*. §§ 152, 158.

5 *Id*. § 158.

6 Employers should note, however, that even if the rule is deemed overbroad, an employer will not be liable for discipline imposed pursuant to the rule if it can establish that the employee's conduct actually interfered with the employee's own work, that of other employees, or with the employer's operations, and that the interference itself was the reason for the discipline.

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JOBS Act Establishes IPO On-Ramp

By Joel Trotter[1] and John Kim

On April 5, 2012, President Obama signed the Jumpstart Our Business Startups Act (the JOBS Act) into law after the US Congress approved the bill with broad bipartisan support. This article dicusses the significant changes the JOBS Act make to US securities laws, such as easing the intial public offering (IPO) process for most US and non-US companies and altering the regulatory regime for all issuers that conduct private offerings.

As discussed in our recent *Client Alerts*,[2] the IPO-related provisions of the JOBS Act implement the recommendations of the IPO Task Force, a national group of industry experts that presented a report to the US Department of the Treasury.

The JOBS Act makes significant changes to US securities laws to ease the IPO process for most US and non-US companies. The JOBS Act creates a new category of issuer, called an emerging growth company (each, an EGC), that benefits from a transition period, or "on-ramp," from private to public company. During this period — which can last for up to five years — EGCs are exempt from certain costly requirements of being a public company.

The JOBS Act separately introduced other changes to US securities laws, including altering the regulatory regime for all issuers that conduct private offerings and increasing the number of shareholders that private companies may have.

Emerging Growth Company

To qualify as an EGC, a company must have annual revenue for its most recently completed fiscal year of less than $1.0 billion (and must not have priced an IPO before December 9, 2011). After the initial determination of EGC status, a company will remain an EGC until the earliest of:

- the last day of any fiscal year in which the company earns $1.0 billion in revenue;
- the date when the company qualifies as a "large accelerated filer," with at least $700 million in public float;
- the issuance, in any three-year period, of more than $1.0 billion in non-convertible debt securities; or
- the last day of the fiscal year ending after the fifth anniversary of the IPO pricing date.

Streamlined IPO Process

The JOBS Act significantly streamlines the IPO process for EGCs, which benefit from the following changes to the IPO process:

- they may make pre-filing offers to institutional investors;
- they may initiate the registration process confidentially with the US Securities and Exchange Commission (SEC);
- they need only two, rather than three, years of audited financial statements to go public; and
- existing communications safe harbors are expanded to permit research analysts to cover EGCs sooner than was permitted under prior law and to permit additional interactions with research analysts during the IPO process.

IPO On-Ramp

Once public, an EGC has a limited transition period of one to five years, depending upon the size of the company, during which the regulatory requirements are scaled in order to ease the cost of compliance. During this on-ramp period, an EGC is:

- exempt from Section 404(b) of the Sarbanes-Oxley Act of 2002, which requires auditor attestation of internal control over financial reporting;

- exempt from the detailed narrative disclosure requirements of compensation, discussion and analysis;
- exempt from the shareholder advisory voting requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as amended (Dodd-Frank) for say-on-pay, say-on-frequency and say-on-golden-parachute votes;
- exempt from SEC rules that will implement the Dodd-Frank executive compensation disclosure provisions for the pay-for-performance graph and CEO pay ratio disclosure;
- subject to the longer phase-in periods that apply to private companies for any new or revised financial accounting standards; and
- exempt from any rules that the US Public Company Accounting Oversight Board may adopt to mandate audit firm rotation or to require the audit report to include an auditor discussion and analysis narrative.

These changes became effective immediately upon enactment on April 5, 2012 and do not require any SEC rulemaking. The SEC staff is now in the process of providing interpretive guidance on specific implementation issues.

For the latest information regarding the JOBS Act, visit Latham's web page dedicated to the topic at http://www.lw.com/news/jobsact. ■

Endnotes

1 Joel Trotter, a partner in our Washington, D.C. office, served as one of two securities lawyers on the IPO Task Force.

2 The *Client Alert* addressing Title I of the JOBS Act is available at http://www.lw.com/thoughtLeadership/JOBS-Act-Establishes-IPO-On-Ramp. The *Client Alert* addressing the 50 most frequently asked questions since the JOBS Act has been signed is available at http://www.lw.com/thoughtLeadership/JOBS-Act-FAQs. For the latest information regarding the JOBS Act, regularly check Latham's web page dedicated to the topic at http://www.lw.com/news/jobsact.

UK Financial Institution Applies Bonus "Claw-Back" Mechanism

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By Sarah Gadd

Supplementing previous publications relating to the rise of "claw-back" and "hold-back" provisions in executive remuneration terms,[1] the new Financial Services Authority (FSA) Remuneration Code regulating the pay of certain employees in the financial services sector[2] and executive pay in the current, challenging economic environment,[3] this article considers a recent decision by one major UK financial institution to apply a form of claw-back in relation to certain executive bonus awards.

The UK financial institution in question incurred a large liability in 2011 arising from claims that it was "mis-selling" loan payment protection insurance; "mis-selling" refers generally to the practice of providing misrepresentations or misleading information to potential consumers and/or investors. The financial institution decided to claw-back over £1.5 million in bonuses, which were due to be paid to 13 of its senior executives. The bonuses were originally awarded in 2010 (before the mis-selling- related losses emerged) but were subject to a three-year deferral before payment. In February 2012, the financial institution announced that the bonuses would be reduced to encourage "accountability" among its senior executives.

This decision is notable as it is the first known example of a major UK financial institution applying a claw-back in relation to deferred bonuses. The revised FSA Remuneration Code, introduced in January 2011, requires banks and other employers who are authorized by the FSA to carry out regulated activities to comply with certain rules relating to how their staff are remunerated. In particular, institutions of a particular size are required to defer between 40 and 60 percent of any bonus entitlements over a period of at least three years.

The announcement was made at a time when the UK media were particularly focused on executive pay packages as the 2011 bonus season was launched against a backdrop of public sector spending cuts and recession warnings. It remains to be seen whether other employers will apply such claw-backs to their bonuses in the coming months, or whether this will be an isolated incident, connected to a particularly high profile mis-selling scandal. ■

Endnotes

1. *See, The Working World*, Issue 8, June 2010 at http://www.lw.com/thoughtLeadership/working-world-june-2010.
2. *See*, Latham & Watkins *Client Alert* "A Guide to the New FSA Remuneration Rules," March 3, 2011 at http://www.lw.com/thoughtLeadership/guide-to-new-fsa-remuneration-rules-in-uk.
3. *See page 15, The Working World*, Issue 14, March 2012.

New US Retirement Plan Fee Disclosure Rules

By Robin Struve and Sandhya Chandrasekhar

New rules require disclosures about fees under US tax-qualified retirement plans by both service providers to plans and plan sponsors.

US tax-qualified plans may only pay "reasonable compensation" for services. If the plan pays more than reasonable compensation, there may be a "prohibited transaction" creating fiduciary liability and resulting in excise taxes. Accordingly, plans must be able to determine what services they are purchasing and the fees being paid for those services. However, many plans receive service under "bundled" arrangements, in which services and fees are not specified. For example, a mutual fund company and its affiliates may provide investment services, recordkeeping and trustee services for one fee.

Effective July 1, 2012, most service providers will be required to report to plan sponsors the details of the services provided, how they are compensated and whether there are any potential conflicts of interest. Both direct and indirect compensation (where a party other than the plan or the plan sponsor pays the service provider) must be disclosed. In the case of indirect compensation, the ultimate payer for the services must be listed. Plan sponsors must, then, consider all of this information in their selection and subsequent retention of service providers.

Plan sponsors are similarly required to disclose to plan participants the types and amounts of fees that are charged, as well as information about making investment elections. This includes certain information required to be disclosed annually (no later than August 30, 2012 for calendar year plans). Other information must be disclosed quarterly, starting with the third quarter of 2012. Plan sponsors should coordinate with their service providers to ensure that these disclosure rules and deadlines are met. ■

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