



Carrot and the Stick: Delving Into Various Stick-Related Retention Ideas

Presentation for:
Hunton's Executive Compensation Webinar Series
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HUNTON

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- Questions during this presentation
 - We encourage questions (even though your audio lines are muted)
 - To submit a question, use the Q&A icon on your Zoom tool bar to submit a question
 - If time permits, your questions will be answered at the end of this presentation. And if there is insufficient time, the speaker will respond to you via e-mail after this presentation

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About Anthony “Tony” Eppert



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- Tony practices in the areas of executive compensation and employee benefits
- Before entering private practice, Tony:
 - Served as a judicial clerk to the Hon. Richard F. Suhrheinrich of the United States Court of Appeals for the Sixth Circuit
 - Obtained his LL.M. (Taxation) from New York University
 - Obtained his J.D. (Tax Concentration) from Michigan State University College of Law
 - Editor-in-Chief, Journal of Medicine and Law
 - President, Tax and Estate Planning Society

Upcoming 2026 Webinars

- 2026 webinars:
 - Form 4 Training Course (11/12/26)
 - Compensation: Year-End Review of 2026 Items (12/10/26)

Sign up here: <https://www.hunton.com/en/insights/executive-compensation-webinar-schedule.html>

Our Compensation Practice – What Sets Us Apart

- Compensation issues are complex, especially for publicly-traded companies, and involve substantive areas of:
 - Tax,
 - Securities,
 - Accounting,
 - Governance,
 - Surveys, and
 - Human resources

- Historically, compensation issues were addressed using multiple service providers, including:
 - Tax lawyers,
 - Securities/corporate lawyers,
 - Labor & employment lawyers,
 - Accountants, and
 - Survey consultants

Our Compensation Practice – What Sets Us Apart (cont.)

- The members of our Compensation Practice Group are multi-disciplinary within the various substantive areas of compensation. As multi-disciplinary practitioners, we take a holistic and full-service approach to compensation matters that considers all substantive areas of compensation



Our Compensation Practice – What Sets Us Apart (cont.)

- Our Compensation Practice Group provides a variety of multi-disciplinary services within the field of compensation, including:

Traditional Consulting Services

- Surveys
- Peer group analyses/benchmarking
- Assess competitive markets
- Pay-for-performance analyses
- Advise on say-on-pay issues
- Pay ratio
- 280G golden parachute mitigation

Corporate Governance

- Implement “best practices”
- Advise Compensation Committee
- Risk assessments
- Grant practices & delegations
- Clawback policies
- Stock ownership guidelines
- Dodd-Frank

Securities/Disclosure

- Section 16 issues & compliance
- 10b5-1 trading plans
- Compliance with listing rules
- CD&A disclosure and related optics
- Sarbanes Oxley compliance
- Perquisite design/related disclosure
- Shareholder advisory services
- Activist shareholders
- Form 4s, S-8s & Form 8-Ks
- Proxy disclosures

Design/Draft Plan

- Equity incentive plans
- Synthetic equity plans
- Long-term incentive plans
- Partnership profits interests
- Partnership blocker entities
- Executive contracts
- Severance arrangements
- Deferred compensation plans
- Change-in-control plans/bonuses
- Employee stock purchase plans
- Employee stock ownership plans

Traditional Compensation Planning

- Section 83
- Section 409A
- Section 280G golden parachutes
- Deductibility under Section 162(m)
- ERISA, 401(k), pension plans
- Fringe benefit plans/arrangements
- Deferred compensation & SERPs
- Employment taxes
- Health & welfare plans, 125 plans

International Tax Planning

- Internationally mobile employees
- Expatriate packages
- Secondment agreements
- Global equity plans
- Analysis of applicable treaties
- Recharge agreements
- Data privacy

Vesting Schedules and Forfeiture Provisions

- Vesting schedules create incentive to remain employed through vesting dates
- However, vested awards could also be forfeited upon certain circumstances, such as termination for Cause, failure to satisfy withholding, failure to comply with restrictive covenants provisions, etc.
- Additionally, repurchase rights in favor of the employer can be implemented as a stick whereby the repurchase price fluctuates depending upon how the individual terminated his or her employment. Examples include:
 - Repurchase at fair market value as of the date of termination of employment, but only if the employee quits for Good Reason or is terminated without Cause,
 - Repurchase at the lower of fair market value or what the individual paid for it, but only if the employee is terminated for Cause, and
 - Repurchase at a discount of fair market value, determined at the time of termination of employment, but only if the individual quits without Good Reason
- A similar stick-like award can be implemented when the employee purchases equity of the employer at fair market value using a loan structure that is at least 51% recourse
 - The above fair market value fluctuations could be implemented
 - The debt repayment provisions could be structured to accelerate if the employee terminates employment in certain manners or is terminated by the employer for Cause
 - Additionally, any debt cancellation would trigger cancellation of indebtedness income, which is taxable at ordinary rates (subject to Section 108(e)(5))

Non-Competition, Non-Solicitation and Economic Forfeitures

- A purpose of non-competition provisions is to restrict an employee from working for competitors or starting a competing business during employment AND during a certain period of time following cessation of employment
 - It is intended to protect legitimate business interests such as trade secrets, customer relationships, and employer goodwill
 - Consideration is required. Such can take the form of access (or continued access) to confidential information, special compensation, equity awards . . .
- A purpose of non-solicitation provisions is to prohibit an employee from soliciting employees and/or customers/clients
- Economic forfeiture provisions could also be incorporated whereby the individual would be permitted to perform the offending behavior (e.g., compete), but the cost of such is that he or she would have to lose his or her equity award or pay money to the employer

Non-Competition Clauses/Agreements

- Some states prohibit non-competes, such as (though even in these states, non-competes are generally permissible in the context of change in control where the obligor under the non-compete is selling the goodwill of the business to which the non-compete relates, and too, some of these states have exemptions for certain executives):
 - California,
 - Minnesota,
 - North Dakota,
 - Oklahoma,
 - Washington (most banned effective June 30, 2027), and
 - Wyoming

Non-Competition Clauses/Agreements (cont.)

- A number of states have legislation pending that, if enacted, would prohibit or severely restrict non-competes, such as:
 - Illinois,
 - Indiana,
 - Maryland,
 - New York,
 - Ohio,
 - Rhode Island, and
 - Utah
- Employers should continually monitor the geographic footprint of its workers relative to states that ban or are highly dis-favorable to non-competes
- Additionally, employers should continue to refine:
 - Confidentiality agreements,
 - Non-solicitation agreements,
 - Invention assignment agreements,
 - Use of economic forfeiture agreements, and
 - Choice of law and venue selection provisions

Non-Disparagement Provisions

- Means that one party will not disparage the other party
 - The provision is typically enforced by the Company against Executive by the former holding the “purse strings” of severance pay (*i.e.*, breach of the provision by Executive would stop the flow of severance pay from the Company to Executive)
- Executives typically seek a mutual non-disparagement clause
 - However, such can be problematic for the company because the Company cannot affirmatively control its employees
- A solution is to:
 - Limit the non-disparagement clause to bind Executive’s actions
 - Then the Company could provide Executive with a limited non-disparagement clause that would essentially require the Company to instruct its Board members, executive team and senior management, to not say anything disparaging about Executive

Clawbacks

- Clawback rules under Dodd-Frank and Section 304 of SOX include:
 - Under Dodd-Frank, compensation clawback policy must apply at least to current and former executive officers
 - In contrast, Section 304 of SOX applies only to the CEO and CFO
 - Under Dodd-Frank, the clawback policy must be triggered any time the issuer is required to prepare an accounting restatement due to the issuer's material noncompliance with any financial reporting requirement under the securities laws
 - In contrast, Section 304 of SOX applies only when a restatement of financial statements is "required" and is the result of "misconduct". Thus, Section 304 of SOX contains a fault requirement and Dodd-Frank does not
 - Dodd-Frank clawback applies to "Little r" restatements (*i.e.*, financial restatements that are not deemed material errors and do not require a full restatement of previously issued financial statements)
 - Dodd-Frank clawback applies to "Big R" restatements (*i.e.*, financial restatements that are deemed material errors and do require a full restatement of previously issued financial statements)
 - Under Dodd-Frank, once the clawback is triggered, it would apply to all "incentive-based" compensation that is "received" based on financial information required to be reported under the securities laws
 - For this purpose, compensation is "received" in the fiscal year during which the relevant goal in question is satisfied (even if payment or grant occurs after the end of such period)

Clawbacks (cont.)

- [Continued List from Prior Slide]:
 - Under Dodd-Frank, the look back period for which incentive-based compensation is subject to clawback is the 3-year period preceding the date on which the restatement is required
 - In contrast, the look back period under Section 304 of SOX is 12 months
 - Under Dodd-Frank, the amount subject to the clawback is the difference between the amount paid and the amount that should have been paid under the accounting restatement
 - To the extent the financial metrics involve stock price and TSR, reasonable estimates may be used to determine the impact of the restatement
 - Such amount to be recovered must be calculated without respect to taxes paid by the executive officer
 - Under Dodd-Frank, the employer must pursue recovery except in 3 situations:
 - If enforcement costs of recovery would exceed the amount to be recovered,
 - If recovery would violate the home country laws, or
 - If recovery would violate rules governing tax-qualified retirement plans

Clawbacks (cont.)

- Dodd-Frank only applies to incentive-based compensation
- However, clawback policies could cover several forms of compensation paid to an individual, including:
 - Annual cash bonuses
 - Long-term cash incentive awards
 - Equity awards (both full-value awards, such as restricted stock or restricted stock units, and appreciation-only awards, such as stock options and stock appreciation rights)
 - Gains from the sale or exercise of equity-based compensation
 - Nonqualified deferred compensation
- Fixed pay is typically not included (*e.g.*, salary, retention bonuses, etc.)

Attorneys' Fees

- A purpose of this provision within a contract is to expressly define which party will pay legal fees and costs arising from any dispute under the contract
 - Typically, the provision obligates the losing party to pay the prevailing party's attorneys' fees, if any
- Example
 - “In any proceeding by which one party either seeks to enforce its rights under this Agreement or seeks a declaration of any rights or obligations under this Agreement, the prevailing party shall be awarded its reasonable attorneys' fees, and costs and expenses incurred.”
 - Another example is contained on the next Slide that also contains guiding principles
- Thoughts
 - Who is more likely to sue?
 - Who has deeper financial pockets?

Attorneys' Fees (cont.)

- Another example is the following (a more robust provision):

“The Company and each Participant hereby agrees and stipulates as follows:

(i) **Recovery of Attorneys' Fees, Costs and Expenses.** If there is any suit, action, or proceeding pursuant to Section 8(j) of this Plan alleging a breach of this Plan, then the prevailing party in any such suit, action, or proceeding, on trial or appeal, shall be entitled to recover from the non-prevailing party, in addition to any other relief awarded, its reasonable and necessary attorneys' fees, costs, and expenses incurred in such suit, action, or proceeding. If there is no prevailing party, each party will pay its own attorneys' fees, costs, and expenses. Whether a prevailing party exists shall be determined solely by the court on a claim-by-claim basis and the court, in its sole discretion, shall determine the amount of reasonable and necessary attorneys' fees, costs, and/or expenses, if any, for which a party is entitled.

(ii) **Guiding Principles.** The following guiding principles shall be applied by a court in any determination of a prevailing party: (i) the intent of the parties is to avoid any suit, action, or proceeding arising from a breach of this Plan, and therefore, the parties will work together to resolve any such dispute; (ii) none of the parties will proceed with a suit, action, or proceeding arising from a breach of this Plan until after exhausting all reasonable efforts to resolve such dispute using best efforts, and an impasse has resulted and a satisfactory result cannot be reached without moving forward with such suit, action, or proceeding; and (iii) none of the parties will bring any suit, action, or proceeding or claim (including cross-claims) arising from a breach of this Plan until after such party has fully evaluated the merits of such purported claim or cause of action and made a determination that such party has a good-faith basis to move forward with such suit, action, proceeding or claim (including cross-claims).

(iii) **Appeals.** In any appeal from the award or denial of attorneys' fees, the court reviewing the award may not modify the decision of the court making or denying an award, or the decision of the court as to the amount of the award, except upon a finding of an abuse of discretion.”

Stock Ownership Requirements

- A stock ownership provision requires certain key employees to acquire and maintain a specified minimum level of employer stock
 - Purpose is to align executive financial interests with long-term shareholder value and retention of capital risk
 - Enforced through mandatory retention of equity award shares, open-market purchases, or some combination of the foregoing
- Common ownership levels include:
 - Chief Executive Officer: 5–6x annual base salary
 - Other Named Executive Officers: 2–3x annual base salary
 - Non-Employee Directors: 3–5x annual cash retainer
 - Counting methodology: shares owned outright, vested/unvested RSUs; typically excludes unexercised options
- Compliance Timeline and Cure Mechanism
 - Initial compliance period is typically 5 years from hire date or promotion to covered role
 - Consequence of non-compliance typically include mandatory retention of 100% of net after-tax shares until threshold achieved
 - If there is a market-downturn, typically the executive is not required to purchase additional shares solely because stock price declined

Hold Period Requirements

- Very similar to stock ownership policies, but hold policies are different because the required hold is for a certain period of time following vesting or exercise
- Common Hold Periods
 - Post-vesting mandatory hold: retain 50–100% of net after-tax shares for 1–3 years following each vesting date
 - Post-exercise hold for stock options: retain specified percentage of net shares for 12–24 months after exercise
 - Until-ownership-threshold-met hold: retain shares until stock ownership guideline is achieved and sustained
 - Post-separation hold: retain specified shares for 6–12 months following termination of employment
- Typically, exceptions are permitted for tax withholding, sales to fund option exercise price, documented financial hardship, etc.
- Enforcement and Violation Consequences
 - Unauthorized sale constitutes breach of the award agreement and are subject to forfeiture of proceeds
 - Potential clawback of related incentive compensation under company's recovery policy
 - Typically, the Board or Compensation Committee retains discretion to waive hold requirement in extraordinary circumstances

Waiver and Release

- It is common practice to require the executive to timely execute, as a condition precedent to any accelerated vesting or separation pay, a waiver and release of all known and unknown claims
- And too, consider requiring certain compensatory forfeitures to occur if such waiver and release is not timely executed
- Finally, consider attaching the form waiver and release, “substantially in the form attached hereto,” so as to avoid future issues at the time of an employment termination event (*i.e.*, who breached first, presentation of an alleged non-market waiver and release, or the Executive who failed to timely sign it?)

Stay-or-Pay Provisions

- California and New York have enacted statutory rules that prohibit “stay-or-pay” arrangements, such as:
 - Training repayment agreements where the employee must repay the cost of training or education if he/she leaves the employer within a certain period;
 - Sign-on or retention bonus clawbacks; and
 - Recovery of relocation costs the employer incurred in moving the employee to the location
- The following two slides focus only on the impact of such provisions on clawback of sign-on bonus provisions

Stay-or-Pay Provisions: Bonus Clawbacks

- Effective January 1, 2026, a new California law invalidates payments to employees and consultants that are subject to repayment, unless such payments fit within a limited exception
 - Thus, a large cash sign-on bonus that is paid to an executive, and which has to be repaid if the executive leaves within a certain period of time, is invalid
- With respect to the California law, a limited exception applies such that the repayment obligation would remain valid, if:
 - Payment must be provided to the employee at the outset of employment;
 - The repayment obligation is contained in a document that is separate from the employment agreement/offer letter;
 - The employee is provided the right to consult an attorney and such employee is provided at least 5 days to obtain legal counsel;
 - Any obligation to repay is subject to interest and must be pro rated based upon the remaining term of such retention period (which is capped at 2 years);
 - The employee must be provided the opportunity to defer receipt of the payment to the end of the retention period (thus, avoiding any repayment obligation); and
 - Clawback allowed only if the employee voluntarily resigns or is fired for “misconduct”
- Applies to all agreements entered into on or after January 1, 2026, including any pre-existing contracts that are subsequently amended
- Workers can file civil lawsuit (including class action) and minimum penalty is \$5,000 per work plus attorneys’ fees and costs

Sign-On Bonuses Subject to Clawback – New York

- Effective February 13, 2027, a new New York law has a similar approach as California but different, as follows:
 - Per a later amendment to the statute, this rule only covers employees (not independent contractors)
 - Clawback of the sign-on bonus is NOT allowed if:
 - The employee is terminated for any reason other than misconduct, or
 - The employee's duties or the requirements of the job function were materially misrepresented to the employee
- Different from California, under New York law there is no private right of action to enforce the rule (*i.e.*, only the New York Department of Labor can bring enforcement actions)
- Civil penalties range from \$1,000 to \$5,000 per violation
- Watch out for other states who have, or are in the process of developing, legislation that constrains certain bonuses (*e.g.*, Connecticut, Colorado, Indiana, Pennsylvania, Washington, Wyoming)
 - These are different from New York and California in that they do not directly ban sign-on bonuses, however, these laws will also have to be navigated

Sign-On Bonuses Subject to Clawback – What To Do

- Employers, especially multi-state employers, should consider:
 - Review employment agreements and offer letters for offending language and requirements;
 - Ensure any requirements to repay a sign-on bonus are contained in a separate agreement; and
 - Review any provisions relating to training programs and related repayment provisions for costs of the same

Survival Provisions

- A purpose of this provision is to specify which provisions of the contract will remain in effect after the contract expires or is terminated
- Example:
 - “This Agreement shall terminate upon the termination of employment of the Executive; however, the following shall survive the termination of the Executive's employment and/or the expiration or termination of this Agreement, regardless of the reasons for such expiration or termination: Section 3 (Compensation and Benefits”) and the corresponding Exhibit A (”Restricted Stock Award Agreement”), Section 4 (”Termination of Employment”) and the corresponding Exhibit B (”Waiver and Release”), Section 5 (”Change in Control”), Section 7(a) (”Defense of Claims”), Section 7(b) (”Non-Disparagement”), Section 7(e) (”Entire Agreement”), Section 7(f) (”Governing Law/Venue”), Section 7(k) (”Successors; Binding Agreement”), Section 7(l) (”Notices”).”
- Thoughts
 - The most common and important provisions that must survive a termination of the contract relate to restrictive covenants (e.g., non-competition, non-solicitation, confidentiality, duty to defend, etc.)

Don't Forget Next Month's Webinar

- Title:
 - Form 4 Training Course
- When:
 - 10:00 am to 11:00 am Central
 - November 12, 2026