

# Compensation and Corporate Governance Disclosure Update

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## SEC PUBLISHES PROPOSED RULES TO ENHANCE COMPENSATION AND CORPORATE GOVERNANCE DISCLOSURE; MAY ALSO FACILITATE STOCKHOLDER ACTIVISM

In a July 10 release, the SEC published proposed rules to expand the level of disclosure in proxy statements, primarily in the areas of executive compensation and corporate governance. Also tucked into the release are additional proposed amendments to the proxy rules that should further facilitate stockholder activism.

While these changes are still in the proposal stage, it is clear that the SEC is focusing on risk management and how compensation policies affect a registrant's risk profile. In order to get ahead of this trend, companies may want to begin considering risk management as another key component of its compensation review and corporate governance review.

It is the SEC's desire to have the new amended rules in effect for the 2010 proxy season.

## CHANGES TO COMPENSATION DISCLOSURES

### Risk Management Disclosures for Some Registrants

The SEC is proposing to expand the required CD&A disclosures to include a discussion of its broader compensation policies across all employees as it relates to risk management, if risks arising from those policies may have a material effect on the registrant. The purpose of this additional disclosure requirement is to help investors identify whether the registrant's compensation policies can lead to excessive or inappropriate risk taking.

This disclosure follows the principles-based approach of the CD&A and the specific disclosures would vary depending upon the size of the company, its industry and its particular compensation program. Some situations that the SEC believes might trigger such a discussion include compensation policies and practices:

- At business units that carry a significant portion of a company's risk profile;
- At business units with compensation structured significantly differently than other units within the company;

- At business units that are significantly more profitable than others within the company;
- At business units where compensation expense is a significant percentage of the units revenues; and
- That vary significantly with the overall risk and reward structure of the company, such as when a bonus is paid in a current year, but the risk and liability to the company extend over a significantly longer period of time.

While these types of situations seem specifically geared to situations that arose within the financial services industry, the proposed disclosure would apply to all registrants if risks arising from the compensation policies may have a material effect on the registrant.

### Compensation Consultants

The SEC is proposing changes to Item 407 of Regulation S-K to require disclosure of the amount of fees paid to compensation consultants when they play a role in determining or recommending the amount or form of executive officer and director compensation.

A description of other services provided by compensation consultants as well as the fees paid for those services must also be disclosed. These disclosure requirements would not apply in situations where the compensation consultant was consulting with respect to broad-based plans that do not discriminate in favor of executives, such as health insurance or 401(k) plans.

### Changes to Summary Compensation Table

Registrants are currently required to disclose in the Summary Compensation Table and the Director Compensation Table, the dollar amount recognized for stock and option awards for the fiscal year under FAS 123R. Despite the fact that this information is provided in the Grant of Plan-Based Awards Table, as well as in the footnotes to the Director Compensation Table, the SEC is proposing to require the disclosure of the aggregate grant date fair value of these awards in the Summary Compensation Table and the Director Compensation Table.

Because the aggregate grant date fair value is typically significantly larger than the annual 123R expense, companies should keep in mind that any officer receiving a

significant “refresh” grant of equity awards or any newly-hired officer would be much more likely to be a “named executive officer” than in the past few years.

## CORPORATE GOVERNANCE DISCLOSURES

### Leadership Structure and Risk Management

With the additional proposed corporate governance disclosures under Item 407 of Regulation S-K, registrants will be required to briefly describe their leadership structure, such as whether the same person serves as the Chief Executive Officer and the Chairman of the Board. If a registrant has a Lead Independent Director, it will need to describe the role of the Lead Independent Director.

Registrants will also need to discuss the Board’s role in the company’s risk management process.

### Additional Disclosure Regarding Director and Nominees

The proposed rules are intended to provide investors with additional disclosure beyond the brief biographical information currently required in order for them to determine a director’s or nominee’s qualifications to serve on the Board.

Item 401 would add a requirement to discuss each director’s or nominee’s specific experience, qualifications, attributes or skills that qualify the person to serve as a director. In addition, disclosure of a director’s or nominee’s other public company directorships for the past five years must also be disclosed, as compared to only current directorships. The current requirement to disclose involvement in specified types of legal proceedings during the past five years would be expanded to ten years.

## DISCLOSURE OF VOTING RESULTS OF FORM 8-K

Currently, voting results from annual or special meetings are required to be disclosed on the next upcoming annual or quarterly report. The SEC is proposing to instead have voting results disclosed within four business days under a new Item 5.07 of Form 8-K.

## CHANGES TO PROXY RULES

The SEC has also proposed changes to the proxy rules that may facilitate communication by activist stockholders and aid non-incumbents in certain contested elections.

## “Just Say No”

Ordinarily, a communication soliciting the granting of a proxy to vote for a stockholder or soliciting a revocation of a proxy would be subject to the various requirements, including the filing of a proxy statement, of the proxy rules. The proposed changes to Rule 14a-2 would specifically exclude from the definition of “form of revocation” an unmarked duplicate copy of management’s proxy card with a request that it be returned directly to the registrant. This would help stockholders or others conduct “just say no” types of proxy campaigns. This exemption would not be available to persons with a substantial interest in the subject matter of the solicitation or that would be likely to receive a substantial benefit from a successful solicitation.

## Filling out Short Slates

Under current Rule 14a-4(d), a person soliciting proxies for the election of directors constituting a minority of the Board (or “short slate”) could also seek authority to fill out the short slate with members of management’s slate. The SEC is proposing changes to Rule 14a-4 that would permit a person to round out a short slate with nominees from a slate proposed by either management or one or more third parties. So long as that person represents in its proxy statement that it has not agreed and will not agree to act as a “group” with the other third parties. This proposed rule change essentially codifies the SEC’s no-action letter given to Carl Icahn earlier this year and could become quite important in elections where there are nominees proposed by more than one other third party. If the SEC’s earlier proposed stockholder nomination rules are enacted as proposed, we would expect to see this proposed rule taken on much greater significance in future contested elections.

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*The full text of the release is located at*  
<http://sec.gov/rules/proposed/2009/33-9052.pdf>.

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