The Proxy Season Field Guide

Sixth Edition

Morrison & Foerster LLP
Corporate Finance Practice

RR DONNELLEY
Financial Services

THE PROXY SEASON FIELD GUIDE

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Acknowledgements: The Proxy Season Field Guide was prepared by the Corporate Finance Practice of Morrison & Foerster LLP.

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EXECUTIVE SUMMARY

The 2016 proxy season occurs in an environment of heightened shareholder activism and an ever-increasing focus on compensation and corporate governance disclosures. This Proxy Season Field Guide provides you with an overview of recent legislative, regulatory and shareholder developments, and provides guidance on how these developments will impact you in the 2016 proxy season.

The Legislative and Regulatory Developments Shaping the Proxy Season

On July 21, 2010, President Obama signed into law what was called the most sweeping set of financial reforms since the Great Depression, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”). While this legislation focused principally on changes to the financial regulatory system, several corporate governance and compensation provisions of the Dodd-Frank Act target public companies. The corporate governance and compensation provisions include:

- A requirement that public companies solicit an advisory vote on executive compensation (“Say-on-Pay”), an advisory vote on the frequency of Say-on-Pay votes (“Say-on-Frequency”) and, in the event of a merger or other extraordinary transaction, an advisory vote on certain “golden parachute” payments (“Say-on-Golden Parachutes”);
- Requirements that the Securities and Exchange Commission (“SEC”) adopt rules directing the securities exchanges to adopt listing standards with respect to compensation committee independence and the use of consultants;
- Provisions calling for the SEC to adopt expanded disclosure in the annual proxy statement and other filings, particularly in the area of executive compensation, such as disclosure of pay versus performance, the ratio of CEO pay to the pay of a median employee, and policies with regard to hedging transactions conducted by employees and directors; and
- Provisions that require the adoption or revision of certain other policies, such as compensation recovery policies providing for the recovery of executive compensation in the event of a financial restatement.

The SEC and the stock exchanges are working to adopt a number of new rules and standards in order to implement the requirements of the Dodd-Frank Act discussed above. Several of the key provisions of the Dodd-Frank Act will be in place for the 2016 proxy season, with many issuers facing their sixth year of Say-on-Pay votes.

SAY-ON-PAY

The implementation of Say-on-Pay votes was one of the most widely anticipated corporate governance developments in the United States over the past five years. Advocates for Say-on-Pay in the United States hoped that the advisory votes on executive compensation would serve to encourage greater accountability for executive compensation decisions, as well as more focused compensation disclosure in proxy statements and expanded shareholder engagement. In many ways, these objectives have been realized as Say-on-Pay has matured.

The SEC rules for Say-on-Pay provide:

- Issuers must provide a separate shareholder advisory vote in proxy statements to approve the compensation of executives not less than every three years. Shareholders must vote, on an advisory basis, to approve the compensation of the issuer's named executive officers, as such compensation is disclosed under Item 402 of Regulation S-K, including the Compensation Discussion and Analysis ("CD&A"), the compensation tables, and other narrative executive compensation disclosures required by Item 402. The rule does not require issuers to use any specific language or a specific form of resolution; however an Instruction to the Rule provides a non-exclusive example of a form of resolution;
- Issuers must provide a separate shareholder advisory vote in proxy statements for annual meetings to determine whether the vote on the compensation of executives will occur every 1, 2, or 3 years. This Say-on-Frequency vote is required not less frequently than once every six years;
- Issuers must explain in the proxy statement the general effect of the Say-on-Pay votes (i.e., the vote is non-binding), and also must disclose, when applicable, the current frequency of Say-on-Pay votes and when the next Say-on-Pay vote will occur;
- Say-on-Pay and Say-on-Frequency votes do not trigger the filing of a preliminary proxy statement with the SEC;
- Issuers are able to exclude shareholder proposals that would provide a Say-on-Pay vote, seek future Say-on-Pay votes, or relate to the frequency of Say-on-Pay votes in certain circumstances when, in the most recent Say-on-Frequency vote, a single frequency received a majority of votes cast and the issuer adopted a policy for the frequency of Say-on-Pay votes that is consistent with that choice;

- The CD&A must disclose whether and, if so, how the issuer has considered the results of the most recent shareholder advisory vote on executive compensation in determining compensation policies and decisions and, if so, how that consideration has affected the issuer's compensation decisions and policies; and
- Issuers must report, pursuant to Item 5.07 of Form 8-K, the decision as to how frequently the issuer will conduct its Say-on-Pay votes following each Say-on-Frequency vote. If the information is provided by amendment to the Form 8-K, the amendment is due no later than 150 calendar days after the date of the end of the annual meeting in which the Say-on-Frequency vote occurred, but in no event later than 60 calendar days prior to the deadline for the submission of shareholder proposals for the next annual meeting as disclosed in the proxy materials for the meeting at which the Say-on-Frequency vote occurred.

During the 2015 proxy season, only 64 issuers failed to achieve majority shareholder support for mandatory Say-on-Pay resolutions. The high level of shareholder support for Say-on-Pay resolutions during the 2015 proxy season was very similar to the experience for issuers that conducted Say-on-Pay votes over the past five years. In the vast majority of those situations, shareholders have provided strong support for Say-on-Pay proposals, absent some significant concerns with the company's executive compensation programs. Even with the likelihood of shareholder support relatively high for Say-on-Pay resolutions, companies have paid very close attention to the message communicated through their CD&A and other disclosures, while at the same time seeking to engage with key shareholder constituencies.

A key agenda item for the compensation committee remains the consideration of the outcome of the most recent Say-on-Pay vote. This is because a "mandatory" CD&A item requires that an issuer must address whether and, if so, how the issuer has considered the results of the most recent Say-on-Pay vote in determining compensation policies and decisions and, if so, how that consideration has affected the company's executive compensation decisions and policies. An issuer that failed to achieve majority support or that received majority support but less than 70%-75% in support for the Say-on-Pay proposal likely needs to make substantial disclosures regarding the engagement efforts that the issuer undertook to understand the reasons for the lack of support, the consideration by the compensation committee of the vote and the results of the engagement efforts, and the specific steps undertaken with the executive compensation program that responded to shareholders' concerns. While the early shareholder engagement efforts were often reactive, recent proxy seasons have been

characterized by much more proactive engagement efforts, utilizing "road show" meetings, conference calls, and perhaps even electronic communications to more effectively engage with shareholders.

When drafting the proxy statement for 2016, the same focus on transparency and communicating an effective message that characterized the last few proxy seasons should carry through. It remains critically important for the CD&A to reflect the notable aspects of the compensation policies and decisions, while highlighting the pay-for-performance aspects of compensation plans.

Key Disclosure Considerations for Proxy Statements and Annual Reports

The SEC Staff (the "Staff") has come to expect that issuers are aware of the interpretive positions taken by the Staff in comment letters on filings, which often reflect nuanced readings of the rules or require more detailed disclosure than might otherwise be expected. It has become increasingly important that issuers make themselves familiar with Staff comment letters that have been issued to other issuers, so that they can respond to the issues raised in those letters when preparing their own filings.

Over the past several years, the SEC has provided significant guidance with respect to its interpretation of executive compensation disclosure rules, including numerous Staff speeches, interpretations and comments on individual filings. There are a number of significant areas of focus in Staff comments and other interpretive guidance on executive compensation disclosure. For example, the Staff has repeatedly stated that an issuer's CD&A should focus on *how* and *why* the issuer arrived at specific executive compensation decisions and policies and should address why specific compensation decisions were made. Other principal areas of Staff comment in the CD&A have related to the disclosure of incentive plan performance targets, individual performance goals and benchmarking practices or processes.

Areas of frequent Staff comment in annual reports have addressed disclosure of goodwill impairment charges, loss contingency disclosures, liquidity, debt covenants, disclosure controls and procedures, cybersecurity risks, risk factors, restatements and exhibits. Over the past several years, the SEC has also provided interpretive guidance outside of the comment process in several key areas relevant to preparing Form 10-Ks and proxy statements, including guidance on non-GAAP measures, the discussion of liquidity and funding risks in the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A), cybersecurity risks, European sovereign debt exposures, disclosures under Section 13(r) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and audit committee disclosures.

Shareholder Activism and Corporate Governance

Continued shareholder concerns over corporate governance and executive compensation issues will shape the outcome of votes in the 2016 proxy season. Issuers will need to continue to focus on voting policies of institutional shareholders and proxy advisory services when making corporate governance and executive compensation decisions. Shareholder proposals in 2015 focused on:

- Proxy access shareholder proposals;
- Compensation-related proposals (i.e., pay-for-performance, clawbacks, compensation consultants, and conflicts of interest);
- Majority voting for directors (particularly at Russell 3000 companies);
- Shareholder ability to call special meetings and take action by written consent;
- Declassified board of directors;
- Disclosure, limits, board oversight, and shareholder approval or ratification of political contributions and lobbying; and
- Split chairman/CEO proposals.

Up until the 2015 proxy season, many issuers had been taking a "wait-and-see" approach with respect to amending their bylaws to permit proxy access in order to allow greater flexibility in responding to future shareholder proposals. In November 2014, the Comptroller of the City of New York, on behalf of the New York City pension funds, launched a large-scale campaign for the 2015 proxy season targeting 75 issuers with a proxy access shareholder proposal. The campaign is called the "Boardroom Accountability Project," and targeted the 75 issuers based on the Comptroller's three "priority" issues. The Comptroller's office has indicated this initiative is part of a wider effort to implement universal proxy access through private ordering. Proxy access remains as one of the key corporate governance issues for the 2016 proxy season.

Institutional Shareholder Services ("ISS"), the leading proxy advisory firm, released 2016 updates to its U.S. proxy voting guidelines, addressing, among other issues, director overboarding, unilateral board actions, compensation of externally managed issuers and proxy access .

The proxy advisory service Glass Lewis also recently updated its voting policies to address policies regarding, among other issues, conflicting management and share-

holder proposals, exclusive forum provisions, environmental and social risk oversight, nominating committee performance and director overboarding.

Conclusion

The 2016 proxy season will continue to present challenges for issuers as they seek to obtain strong support for their Say-on-Pay votes, while at the same time remaining attentive to ongoing shareholder concerns regarding corporate governance and executive compensation. This Proxy Season Field Guide will provide you with the resources necessary to successfully navigate the proxy season.

CHAPTER 1

THE LEGISLATIVE AND REGULATORY DEVELOPMENTS SHAPING THE PROXY SEASON

THE LEGISLATIVE AND REGULATORY DEVELOPMENTS SHAPING THE PROXY SEASON

On July 21, 2010, President Obama signed into law what was called the most sweeping set of financial reforms since the Great Depression, the Dodd-Frank Act. The Dodd-Frank Act focuses principally on changes to the financial regulatory system; however, several corporate governance and compensation provisions of the Dodd-Frank Act target public companies. The corporate governance and compensation provisions include:

- A requirement that public companies solicit a Say-on-Pay vote, a Say-on-Frequency Vote and, in the event of a merger or other extraordinary transaction, a Say-on-Golden Parachute vote;
- Requirements that the SEC adopt rules directing the securities exchanges to adopt listing standards with respect to compensation committee independence and the use of consultants;
- Provisions calling for the SEC to adopt expanded disclosure requirements for the annual proxy statement and other filings, particularly in the area of executive compensation; and
- Provisions that will require the adoption or revision of certain other policies, such as compensation recovery policies providing for the recovery of executive compensation in the event of a financial restatement.

The SEC and the stock exchanges are working to adopt a number of new rules and standards in order to implement the requirements of the Dodd-Frank Act discussed above.

ADVISORY VOTES ON EXECUTIVE COMPENSATION

Say-on-Pay and Say-on-Frequency

For larger public issuers, beginning with shareholder meetings occurring on or after January 21, 2011, Section 951 of the Dodd-Frank Act required that issuers include a resolution in their proxy statements asking shareholders to approve, in a non-binding vote, the compensation of their executive officers, as disclosed under Item 402 of Regulation S-K. A separate resolution is also required to determine whether this Say-on-Pay vote takes place every one, two, or three years.

On January 25, 2011, the SEC adopted rules implementing Say-on-Pay and the related advisory vote on executive compensation provisions. The new rules and amendments to existing rules became effective on April 4, 2011, except that the Say-on-Golden Parachute requirements became effective for filings made on or after April 25, 2011, for all issuers.

A complete description of these rules, rule amendments and applicable SEC and Staff interpretations is provided in Chapter 2.

The applicable rules and rule amendments are as follows:

- Rule 14a-21(a) requires that issuers must provide a separate shareholder advisory vote in proxy statements to approve the compensation of executives not less than every three years. In accordance with Section 14A(a)(1) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), shareholders must vote, on an advisory basis, to approve the compensation of the issuer's named executive officers, as such compensation is disclosed under Item 402 of Regulation S-K, including the CD&A, the compensation tables and other narrative executive compensation disclosures required by Item 402. The rule does not require issuers to use any specific language or a specific form of resolution; however, an Instruction to Rule 14a-21 provides a non-exclusive example of a form of resolution. The shareholder vote must relate to all executive compensation disclosure set forth pursuant to Item 402 of Regulation S-K, with the exception of disclosure provided pursuant to paragraph (s) of Item 402 of Regulation S-K and director compensation required by paragraph (k) or (r) of Item 402 of Regulation S-K;

- Rule 14a-21(b) requires that issuers provide a separate shareholder advisory vote in proxy statements for annual meetings to determine whether the vote on the compensation of executives required by Section 14A(a)(1) of the Exchange Act "will occur every 1, 2, or 3 years." This Say-on-Frequency vote is required not less frequently than once every six years;

- Item 24 of Schedule 14A requires disclosure that the issuer is providing the vote pursuant to Section 14A of the Exchange Act, as well as an explanation of the general effect of the Say-on-Pay votes (i.e., the vote is non-binding). Issuers also must disclose, when applicable, the current frequency of Say-on-Pay votes and when the next Say-on-Pay vote will occur;

- Rule 14a-6(a) includes Say-on-Pay and Say-on-Frequency votes in the list of items that do not trigger the filing of a preliminary proxy;

- A Note to Rule 14a-8(i)(10) permits the exclusion of a shareholder proposal that would provide a Say-on-Pay vote, seek future Say-on-Pay votes, or relate to the frequency of Say-on-Pay votes in certain circumstances. Such shareholder proposals could be excluded under the Note if, in the most recent Say-on-Frequency vote, a single frequency received a majority of votes cast and the issuer adopted a policy for the frequency of Say-on-Pay votes that is consistent with that choice. For the purposes of this Note, the SEC states that an abstention would not count as a vote cast;

- An amendment to Item 402(b) of Regulation S-K requires an issuer to address, in the CD&A, whether and, if so, how the issuer has considered the results of the most recent shareholder advisory vote on executive compensation (as required by Exchange Act Section 14A or Exchange Act Rule 14a-20, which is the rule governing Say-on-Pay votes required for recipients of financial assistance under the Troubled Asset Relief Program, or "TARP") in determining compensation policies and decisions and, if so, how that consideration has affected the issuer's compensation decisions and policies. This requirement is included among the "mandatory" CD&A disclosure items specified by Item 402(b)(1) of Regulation S-K; and

- An amendment to Item 5.07 of Form 8-K requires that an issuer must disclose its decision as to how frequently the issuer will conduct Say-on-Pay votes following each Say-on-Frequency vote. In order to comply with this requirement, an issuer must disclose the determination in the original Form 8-K or file an amendment to its original Form 8-K filing (or filings) that disclosed the preliminary and final results of the Say-on-Frequency vote. The Form 8-K amendment is due no later than 150 calendar days after the date of the end of the annual meeting in which the Say-on-Frequency vote occurred, but in no event later than 60 calendar days prior to the deadline for the submission of shareholder proposals as disclosed in the proxy materials for the meeting at which the Say-on-Frequency vote occurred. Specifically with respect to Say-on-Frequency votes, an issuer must disclose the number of votes cast for each of the choices, as well as the number of abstentions in Item 5.07 of Form 8-K.

Say-on-Golden Parachutes

Rule 14a-21(c) provides that if a solicitation is made by an issuer for a meeting of shareholders at which the shareholders are asked to approve an acquisition, merger,

consolidation, or proposed sale or other disposition of all or substantially all of the assets of the issuer, the issuer must provide a separate shareholder vote to approve any agreements or understandings and compensation disclosed pursuant to Item 402(t) of Regulation S-K. Consistent with Exchange Act Section 14A(b), any agreements or understandings between an acquiring company and the named executive officers of the issuer, where the issuer is not the acquiring company, are not required to be subject to the separate shareholder advisory vote.

If any of the agreements or understandings contemplated in Rule 14a-21(c) previously have been subject to a shareholder advisory vote or the Say-on-Pay vote, then a separate shareholder vote is not required at the time of the vote on the merger or other similar extraordinary transaction. If there are changes to the arrangements after the date of the annual meeting or if new arrangements are adopted that were not subject to a prior Say-on-Pay vote, then a Say-on-Golden Parachutes vote is still required. In that case, the vote is required only with respect to the amended golden parachute payment arrangements.

The SEC adopted Item 402(t) of Regulation S-K, which requires disclosure of named executive officers' golden parachute arrangements in a proxy statement for shareholder approval of a merger, sale of a company's assets, or similar transactions. This disclosure is only required in annual meeting proxy statements when an issuer is seeking to rely on the exception from a separate merger proxy shareholder vote by including the proposed Item 402(t) disclosure in the annual meeting proxy statement soliciting a Say-on-Pay vote. The disclosure includes a table labeled "Golden Parachute Compensation," as well as detailed narrative disclosure about the arrangements pursuant to which the compensation is to be paid. The disclosure is also required under a variety of rules and forms; however, the SEC made clear that Item 402(t) disclosure is not required in third-party bidders' tender offer statements, so long as the subject transactions are not also Exchange Act Rule 13e-3 going-private transactions.

Compensation Committees and Compensation Consultants

The Dodd-Frank Act requires that stock exchange listing standards prescribe that compensation committee members be independent in light of the Dodd-Frank Act standards and that a compensation committee may only select compensation consultants, legal counsel, or other advisers after taking into consideration independence standards established by the SEC. The Dodd-Frank Act requires that these independence factors include:

- The provision of other services by the person that employs the adviser;
- The amount of fees received as a percentage of an entity's total revenue;
- Policies and procedures designed to prevent conflicts of interest;
- Any business or personal relationship of the adviser with a member of the compensation committee; and
- Any stock of the company owned by an adviser.

Further, the compensation committee must be vested with direct authority for the appointment, compensation, and oversight of the work of the consultant.

Enhanced disclosure is also required by the SEC, addressing whether the compensation committee retained or obtained the advice of a compensation consultant and whether the consultant's work raised any conflicts of interest, the nature of any such conflict, and how it was addressed. In December 2009, the SEC adopted rules requiring disclosure of fees paid to compensation consultants when they provide executive compensation consulting and additional services.

SEC Rulemaking

On June 20, 2012, the SEC adopted Rule 10C-1, which directs the national securities exchanges to adopt listing standards requiring that each member of a compensation committee must be an independent member of the board of directors. Neither the Dodd-Frank Act nor the SEC's final rule specifically define independence for this purpose, however consistent with Section 10C of the Exchange Act, the national securities exchanges must consider: (1) the sources of compensation of the director, including any consulting, advisory or other compensatory fee paid by the company to the director and (2) whether the director is affiliated with the company or any of its subsidiaries or their affiliates.

The SEC provided the national securities exchanges with more discretion in setting the definition of independence than is currently available with respect to the independence of audit committee members as required pursuant to the Section 10A(m) of the Exchange Act. The SEC did not adopt any additional factors to be considered by the national securities exchanges in establishing their listing standards. The SEC did not adopt any "look back" period to be applied with respect to the independence determination, leaving it to the national securities exchanges to determine whether to adopt a look back period.

Rule 10C-1 also directs the national securities exchanges to prohibit the listing of an equity security of an issuer that is not in compliance with the following standards:

- The compensation committee, in its sole discretion, must have authority to obtain or retain the advice of compensation advisers;
- The compensation committee must be directly responsible for the appointment, retention, compensation and oversight of the work of any compensation advisers; and
- The issuer must provide the appropriate funding for the payment of reasonable compensation, as determined by the compensation committee, to the compensation advisers, if any.

Under the rule as adopted, a compensation committee is expressly permitted to receive advice from a non-independent adviser, such as in-house counsel or a compensation consultant engaged by management. The SEC made clear that the final rule would not require that the compensation committee act in accordance with the advice of compensation advisers or otherwise affect the ability or obligation of the compensation committee to exercise its own judgment. Further, the final rule and the resulting listing standards are not intended to preclude the engagement of non-independent legal counsel or obtaining advice from in-house or outside counsel retained by the company or the company's management.

Rule 10C-1 also directs the national securities exchanges to adopt listing standards requiring that the compensation committee consider the independence factors specified in Rule 10C-1, as well as any other relevant factors identified by the national securities exchanges, prior to engaging any compensation advisers. The SEC did not define or provide further clarification regarding any of the factors specified in Section 10C, however it did adopt one additional factor, which is any business or personal

relationships between the company's executive officers and the compensation adviser or the firm employing the compensation adviser.

Further, in accordance with Section 10C, the SEC adopted an amendment to expand its current disclosure requirements regarding compensation consultants. The SEC amended Item 407 of Regulation S-K to specifically require that a company disclose the nature of any conflict of interest and how it is being addressed if the work of the compensation consultant raised a conflict of interest. While the SEC has not defined what constitutes a conflict of interest, Item 407 provides that the same six factors specified in Rule 10C-1 should be considered in determining if a conflict of interest exists.

Exchange Listing Standards

Pursuant to Rule 10C-1, the national securities exchanges were directed to provide the SEC with proposed changes to their listing standards related to compensation committee and adviser independence. The New York Stock Exchange ("NYSE") and Nasdaq submitted their proposed changes to the SEC on September 25, 2012. Both exchanges later submitted amendments to their proposals and the SEC approved the exchanges' proposals, as amended, on January 11, 2013. Further amendments to Nasdaq's standards were approved in December 2013.

Independence of Compensation Committee Members

Under Rule 10C-1, the exchanges were directed to adopt listing standards related to the independence of compensation committee members. Although neither the Dodd-Frank Act nor Rule 10C-1 specifically defines independence for this purpose, the listing standards adopted by national securities exchanges must consider:

- The sources of compensation of the director, including any consulting, advisory, or other compensatory fee paid by the company to the director; and
- Whether the director is affiliated with the company or any of its subsidiaries or their affiliates.

Rule 10C-1 provided the exchanges with more discretion in setting the definition of independence than is permitted in determining the independence of audit committee members. In its rulemaking, the SEC did not adopt any additional factors to be considered by the exchanges in establishing their listing standards beyond what was required under the Dodd-Frank Act, which left open the possibility that the exchanges would

consider and adopt additional relevant factors to be considered when determining whether a compensation committee member is independent.

The NYSE and Nasdaq listing standards do not, however, include any additional criteria to be considered in determining whether a member of the compensation committee is independent. The commentary to both the NYSE's and Nasdaq's proposals made clear that in order to be considered independent, members of the compensation committee must meet both the general independence criteria already included in the exchanges' listing standards and the compensation committee-specific criteria required by Rule 10C-1.

The new NYSE listing standards provide some guidance as to how issuers should apply the two factors listed above in making an independence determination. With respect to sources of compensation, the commentary to the NYSE standards instructs the listed company's board to consider whether the director receives compensation from any person or entity that would impair the director's ability to make independent judgments about the listed company's executive compensation. Similarly, when considering any affiliate relationship, the commentary to the new listing standards instructs the board to consider whether there is an affiliate relationship that places the director "under the direct or indirect control of the listed company or its senior management, or creates a direct relationship between the director and members of senior management, in each case of a nature that would impair his ability to make independent judgments about the listed company's executive compensation." The NYSE specifically declined to include a bar on independence based solely on affiliate status due to stock ownership.

Nasdaq amended its listing standards in December 2013 to harmonize the compensation committee-specific independence standards with these standards adopted by the NYSE. As amended, Nasdaq Rule 5605(d)(2)(A) provides that "in affirmatively determining the independence of any director who will serve on the compensation committee of a board of directors, the board of directors must consider all factors specifically relevant to determining whether a director has a relationship to the Company which is material to that director's ability to be independent from management in connection with the duties of a compensation committee member, including, but not limited to: (i) the source of compensation of such director, including any consulting, advisory or other compensatory fee paid by the Company to such director; and (ii) whether such director is affiliated with the Company, a subsidiary of the Company or an affiliate of a subsidiary of the Company." The focus of this analysis is on

independence from management, and the revised interpretive material (IM-5605-6) makes clear that compensation must be evaluated in the context of whether it could affect judgments regarding executive compensation, noting "[w]hen considering the sources of a director's compensation for this purpose, the board should consider whether the director receives compensation from any person or entity that would impair the director's ability to make independent judgments about the Company's executive compensation." The revised interpretation also states that when considering affiliate relationships, the board should consider whether the affiliate relationship places the director under the "direct or indirect control of the Company or its senior management, or creates a direct relationship between the director and members of senior management, in each case of a nature that would impair the director's ability to make independent judgments about the Company's executive compensation."

Compensation Committee Authority and Funding

Rule 10C-1 also directed the exchanges to prohibit the listing of a security of an issuer that is not in compliance with the following standards:

- The compensation committee, which for this purpose includes those members of a the board of directors who oversee executive compensation matters on behalf of the board of directors in the absence of a board committee, must be directly responsible for the appointment, compensation, and oversight of the work of any compensation advisers;

- The compensation committee, in its sole discretion, must have authority to retain or obtain the advice of compensation advisers;

- The issuer must provide the appropriate funding for the payment of reasonable compensation, as determined by the compensation committee, to the compensation advisers, if any; and

- Before selecting any compensation adviser, the compensation committee must take into consideration the six independence criteria specified in Rule 10C-1 (described below), as well as any additional factors specified in the listing criteria adopted by the exchanges.

The SEC made clear that Rule 10C-1 does not require that the compensation committee act in accordance with the advice of compensation advisers or otherwise affect the ability or obligation of the compensation committee to exercise its own

judgment. Further, Rule 10C-1 and the resulting listing standards are not intended to preclude obtaining advice from in-house counsel. Rule 10C-1 and both exchanges' listing standards also make clear that while the compensation committee must conduct an independence assessment in selecting a compensation adviser, companies may still retain and seek advice from advisers who are not independent (subject to the new compensation adviser disclosure requirements in Item 407 of Regulation S-K).

The NYSE and Nasdaq listing standards both require companies to impose the requirements listed above on their compensation committees. The NYSE noted in its commentary that the required powers of the compensation committee set forth above had in significant part already been required by existing NYSE listing standards, which require these powers to be included in the compensation committee charter. In any case, the NYSE adopted the requirements noted above exactly as they appear in Rule 10C-1, and removed the comparable requirements included in existing NYSE listing standards. Nasdaq's listing standards also require that, subject to certain exceptions described below, listed companies adopt a formal compensation committee charter that states that the compensation committee will review and reassess the adequacy of the charter on an annual basis.

Compensation Adviser Independence

Rule 10C-1 also directed the exchanges to adopt listing standards requiring that the compensation committee consider the independence factors specified in Rule 10C-1, as well as any other relevant factors identified by the exchange, prior to engaging any compensation advisers. The independence criteria specified in Rule 10C-1 are:

- The provision of other services to the company by the firm employing the compensation adviser;
- The amount of fees received from the company by the firm employing the compensation adviser, as a percentage of that firm's total revenue;
- The policies and procedures adopted by the firm employing the compensation adviser that are designed to prevent conflicts of interest;
- Any business or personal relationship of the compensation adviser with a member of the compensation committee;
- The compensation adviser's ownership of the company's stock; and
- Any business or personal relationships between the company's executive officers and the compensation adviser or the firm employing the adviser.

As with the criteria relating to compensation committee member independence, the new NYSE and Nasdaq listing standards do not include any additional factors to be considered in determining the independence of compensation advisers beyond those in Rule 10C-1.

Consistent with the compensation adviser disclosure requirements in Item 407 of Regulation S-K, the NYSE and Nasdaq listing standards provide that a compensation committee is not required to conduct the independence assessment with respect to a compensation adviser that acts in a role limited to (1) consulting on any broad-based plan that does not discriminate in scope, terms, or operation, in favor of executive officers or directors of the registrant, and that is available generally to all salaried employees or (2) providing information that either is not customized for a particular registrant or that is customized based on parameters that are not developed by the compensation consultant, and about which the compensation consultant does not provide advice.

Exemptions and Applicability of Listing Standards

The listing standards for compensation committee member independence and compensation committee adviser independence do not apply to controlled companies, issuers of securities futures products cleared by a registered clearing agency or a clearing agency exempt from registration, or registered clearing agencies that issue standardized options. The following categories of companies are also exempt from the compensation committee member independence requirements:

- Limited partnerships;
- Companies in bankruptcy proceedings;
- Open-end management investment companies registered under the Investment Company Act of 1940;
- Foreign private issuers that disclose annually why they do not have an independent compensation committee; and
- Smaller reporting companies.

The NYSE and Nasdaq listing standards both include general exemptions for other categories of issuers that are currently exempt from their existing compensation committee requirements. These include passive business organizations and issuers whose only listed equity security is a preferred stock.

The listing standards of both the NYSE and Nasdaq already provide that a foreign private issuer may follow its home country's practice rather than U.S. compensation-related listing standards so long as the issuer discloses in its annual reports filed with the SEC each requirement that it does not follow and describes the home country practice the issuer follows in lieu of such requirements. Under both the NYSE and Nasdaq listing standards, a foreign private issuer that follows its home country's practice in lieu of the requirement to maintain an independent compensation committee must now also disclose in its annual reports filed with the SEC the reasons why it does not have such a committee.

Under both the NYSE and Nasdaq listing standards, smaller reporting companies are not required to adhere to the enhanced independence standards for compensation committee members or the compensation adviser independence considerations. Nasdaq's listing standards also permit smaller reporting companies to adopt a board resolution that specifies the compensation committee's responsibilities and authority in lieu of adopting a formal written compensation committee charter. Further, under Nasdaq's listing standards, smaller reporting companies are not required to include language regarding the committee's authority to retrain compensation advisers in the compensation committee charter or board resolutions. Under Nasdaq's listing standards, smaller reporting companies are also exempt from the requirement to review the compensation committee charter or board resolutions on an annual basis.

Implementation Timeline

Under the NYSE and Nasdaq listing standards, companies had until the earlier of (1) their first annual meeting after January 15, 2014, or (2) October 31, 2014, to comply with the compensation committee independence requirements. Issuers were required to comply with the other new standards, including those related to the funding and authority of the compensation committee and the independence of compensation committee advisers, by July 1, 2013.

Both the NYSE and Nasdaq listing standards provided listed companies with opportunities to cure compensation committee member independence issues after the standards went into effect. Under the NYSE listing standards, if a member of a compensation committee ceases to be independent for reasons outside the member's reasonable control, that member may remain on the compensation committee until the earlier of the next annual meeting or one year from the occurrence of the event that caused the member to be no longer independent. Notably, however, the cure period provided under the NYSE standards is limited to circumstances where the compensa-

tion committee continues to have a majority of directors who are independent under the new listing standards. Under the Nasdaq listing standards, the listed company is required to cure any noncompliance by the earlier of the next annual shareholders meeting or one year from the occurrence of the event that caused the noncompliance. Both exchanges' listing standards require companies to notify the relevant exchange upon learning of noncompliance.

The NYSE and Nasdaq listing standards both generally provide a phased-in compliance period for newly listed companies. These issuers are required to have one independent compensation committee member at the time of listing, a majority of independent compensation committee members within 90 days of listing, and all independent compensation committee members within one year of listing.

Expanded Compensation Disclosure

Several provisions of the Dodd-Frank Act require that the SEC further expand the disclosure requirements applicable for proxy statements and other filings to address several areas of compensation with respect to employees, executive officers, and directors; including:

- Disclosure of Pay versus Performance – Section 953(a) of the Dodd-Frank Act requires that the SEC adopt rules mandating that issuers disclose the relationship of the compensation actually paid to their executive officers versus the issuer's financial performance, taking into account changes in the value of stock and dividends or distributions. This disclosure may be presented graphically or in narrative form.

- Disclosure of CEO Pay versus Median Employee Pay – Section 953(b) of the Dodd-Frank Act requires that the SEC adopt rules mandating disclosure of the median annual total compensation of all employees (except the CEO), the annual total compensation of the CEO, and the ratio of the median employee total compensation to the CEO total compensation. Total compensation is determined by reference to the "total compensation" column of the Summary Compensation Table.

- Disclosure of Employee or Director Hedging Policies – Section 955 of the Dodd-Frank Act directs the SEC to adopt rules mandating disclosure of whether any employee or director (or designee of such persons) is permitted to purchase financial instruments, such as prepaid variable forwards, equity

swaps, collars, and exchange funds, that are designed to hedge or offset any decrease in the market value of equity securities granted as compensation or held directly or indirectly by the employee or director.

The SEC has proposed implementing rules regarding pay versus performance and disclosure of employee or director hedging policies, and has adopted final rules regarding CEO pay ratio disclosure.

Pay Versus Performance Disclosure

On April 29, 2015, the SEC proposed rules to implement Section 953(a) of the Act, which were subject to a 60-day comment period that ended on July 6, 2015. The proposed rules would add new Item 402(v) of Regulation S-K, which would require an issuer to provide a clear description of (1) the relationship between executive compensation actually paid to the issuer's named executive officers and the cumulative total shareholder return ("TSR") of the issuer, and (2) the relationship between the issuer's TSR and the TSR of a peer group chosen by the issuer, over each of the issuer's five most recently completed fiscal years. The proposed disclosure would be required in proxy or information statements for annual meetings of shareholders in which executive compensation disclosure is required. The proposed disclosure would require issuers to add a new table to their proxy materials with the following information:

- Executive compensation actually paid for the principal executive officer and the average compensation actually paid to the remaining named executive officers;
- The total executive compensation reported in the Summary Compensation Table included under Item 402(c) of Regulation S-K for the principal executive officer and the average of the reported amounts for the remaining executive officers;
- The issuer's TSR on an annual basis, using the definition of TSR in Item 201(e) of Regulation S-K, which sets forth an existing requirement for a stock performance graph; and
- The TSR on an annual basis of the issuers in a peer group.

The new table prescribed by the proposed rules would include executive compensation "actually paid" to named executive officers, as defined in Item 402(a)(3) of Regulation S-K.

- While the proposed rules would require issuers to disclose the executive compensation actually paid to the principal executive officer, the compensation amounts disclosed for the remaining named executive officers would be the average compensation actually paid to those executives. Under the proposed rules, executive compensation "actually paid" would be calculated using compensation that issuers already report in the proxy statement as a starting point. Specifically, compensation "actually paid" pursuant to the proposed rules would equal total compensation, as reported in the Summary Compensation Table, with certain adjustments relating to pension amounts and equity awards.

- The proposed rules would require that companies use TSR (as defined in Item 201(e) of Regulation S-K) as the measure of financial performance of the company for purposes of pay-versus-performance disclosure. To supplement the required disclosure, the proposed rules would permit issuers to provide supplemental measures of financial performance, as long as any such additional disclosure is clearly identified, not misleading and not presented with greater prominence than the required disclosure.

- Pursuant to the proposed rules, issuers would be required to disclose the relationship between issuer TSR and peer group TSR, in each case over the company's five most recently completed fiscal years, using the peer group identified by the issuer in its stock performance graph or in its CD&A included in Item 402(b) of Regulation S-K.

- Issuers would be required to provide the disclosure contemplated by proposed rules for the last five fiscal years, except that smaller reporting companies would be required to provide disclosure for only the last three fiscal years.

- In addition to providing the tabular and narrative disclosure contemplated by the proposed rules, issuers would also be required to tag the disclosure in an interactive data format using eXtensible Business Reporting Language, or XBRL.

CEO Pay Ratio Disclosure

On August 5, 2015, the SEC adopted the rules implementing Section 953(b) of the Act. The final rule adds new paragraph (u) to Item 402 of Regulation S-K, which requires disclosure of the following:

A. The median of the annual total compensation of all employees of the company, except the CEO of the issuer;

B. The annual total compensation of the CEO of the issuer; and

C. The ratio of the amount in (B) to the amount in (A), presented as a ratio in which the amount in (A) equals one, or, alternatively, expressed narratively in terms of the multiple that the amount in (B) bears to the amount in (A).

The final rule also requires disclosure of the ratio such that the CEO's annual total compensation is always compared to the median employee's annual total compensation—the ratio must always show how much larger or smaller the CEO's annual total compensation is as compared to the median employee's annual total compensation. Issuers that are subject to the rule will be required to provide the disclosure starting with the first fiscal year beginning on or after January 1, 2017. The final rules also include the following provisions:

- Filings Requiring Pay Ratio Disclosure. The pay ratio disclosure as set forth in the final rule is required in any filing that calls for executive compensation disclosure pursuant to Item 402 of Regulation S-K, including annual reports on Form 10-K and registration statements under the Securities Act of 1933, as amended (the "Securities Act"), as well as proxy materials to the same extent that these forms require compliance with Item 402 of Regulation S-K. The pay ratio disclosure, as with other Item 402 information, will be treated as "filed" for purposes of the Securities Act and Exchange Act and, as such, will be subject to potential liabilities under those statutes, including Section 18 liability under the Exchange Act.

- Definition of "Employee." The final rule defines "employee" to include an issuer's U.S. and non-U.S. employees, as well as its part-time, seasonal, and temporary employees employed by the issuer or any of its consolidated subsidiaries. Also included in this definition are all of a issuer's officers, other than the CEO. The definition of "employee" does not include independent contractors or "leased" workers employed by a third party and whose com-

pensation is determined by the third party. An issuer can supplement its pay ratio disclosure or provide additional pay ratios for its shareholders to consider if it wants to explain the effect of including part-time, seasonal, and temporary employees on its CEO pay ratio disclosure. The final rule includes only employees of consolidated subsidiaries, as determined by reference to applicable accounting standards, rather than employees of all subsidiaries, as was originally proposed.

- Median Employee Determination Date. The final rule provides flexibility in choosing the median employee determination date, as opposed to the proposed rule, which proposed to define "employee" as an individual employed as of the last date of the company's last completed fiscal year. The final rule defines "employee" as an individual employed on any date of the issuer's choosing within the last three months of the issuer's last completed fiscal year. Issuers must disclose the date used to identify the median employee.

- Exemptions. In response to particular issues and concerns raised during the comment process, the final rule provides two tailored exemptions from the general requirement to include all employees located outside of the United States.

    - Data Privacy Exemption. The first exemption to the general requirement that non-U.S. employees be included in the pay ratio disclosure is when a jurisdiction's data privacy laws or regulations are such that, despite an issuer's reasonable efforts to obtain or process information necessary to comply with the rule, it is unable to do so without violating those laws or regulations. For example, the European Union prohibits the transfer of personal data to a third country that does not ensure an adequate level of privacy protection; China, Japan, Mexico, Canada, Peru, Australia, Russia, Switzerland, Argentina, and Singapore have adopted or are considering similar rules. To prevent any potential manipulation, issuers are required to exercise reasonable efforts to obtain or process the information necessary for compliance with the final rule. As part of its reasonable efforts, the issuer must seek an exemption or other relief under the applicable jurisdiction's governing data privacy laws or regulations and use the exemption if granted. If an issuer excludes any non-U.S. employees in a particular jurisdiction under the data privacy exemption, it must exclude all non-U.S. employees in that jurisdiction. Additionally, the issuer must list the excluded jurisdictions, identify the

specific data privacy law or regulation, explain how complying with the final rule violates the law or regulation (including the efforts made by the issuer to use or seek an exemption or other relief under such law or regulation), and provide the approximate number of employees exempted from each jurisdiction based on this exemption. The issuer must obtain a legal opinion that opines on the inability of the issuer to obtain or process the information necessary for compliance with the final rule without violating that jurisdiction's laws or regulations governing data privacy, including the issuer's inability to obtain an exemption or other relief under any governing laws or regulations. The legal opinion must be filed as an exhibit to any filing in which the pay ratio disclosure is included.

- De Minimis Exemption. The second exemption from the general requirement to include non-U.S. employees in identifying the median employee is when a *de minimis* number of an issuer's employees work outside the United States. Under the final rule, if an issuer's non-U.S. employees account for five percent or less of its total employees, it may exclude all of those employees when making its pay ratio calculations. If the issuer chooses to exclude any non-U.S. employees, it must exclude all of them. If an issuer's non-U.S. employees exceed five percent of the issuer's total U.S. and non-U.S. employees, it may exclude up to five percent of its total employees who are non-U.S. employees. If an issuer excludes any non-U.S. employees in a particular jurisdiction, it must exclude all non-U.S. employees in that jurisdiction. The issuer must also disclose the jurisdictions from which its non-U.S. employees are being excluded, the approximate number of employees excluded from each jurisdiction under the *de minimis* exemption, the total number of its U.S. and non-U.S. employees irrespective of any exemption *(de minimis* or data privacy), and the total number of its U.S. and non-U.S. employees used for its *de minimis* calculation.

- Cost-of-Living Adjustments. The SEC recognized that differences between the underlying economic conditions of the countries in which companies operate likely have an effect on the compensation paid to employees in those jurisdictions, and therefore the final rule provides issuers with the option of making cost-of-living adjustments to the compensation of their employees in jurisdictions other than the jurisdiction in which the CEO resides when iden-

tifying the median employee (whether using annual total compensation or any other consistently applied compensation measure). The issuer is required to disclose the country in which the median employee is located, briefly describe the cost-of-living adjustments it used to identify the median employee, and briefly describe the cost-of-living adjustments it used to calculate the median employee's annual total compensation, including the measure used as the basis for the cost-of-living adjustment. To provide context for the Item 402(u)(1)(iii) disclosure, an issuer electing to present the pay ratio in this manner must also disclose the median employee's annual total compensation and pay ratio without the cost-of-living adjustments. To calculate this pay ratio, the issuer must identify the median employee without using any cost-of-living adjustments.

- Replacement of CEO. When an issuer replaces its CEO with another CEO during its fiscal year, the final rule allows a choice of two options in calculating the annual total compensation for its CEO: (a) an issuer may take the total compensation calculated pursuant to Item 402(c)(2)(x), and reflected in the Summary Compensation Table, provided to each person who served as CEO during the year and combine those figures, which would constitute the company's annual total CEO compensation; or (b) an issuer may look to the CEO serving in that position on the date it selects to identify the median employee and annualize that CEO's compensation. An issuer must disclose which option it chooses, and how it calculates its CEO's annual total compensation.

- Additional Information. The final rule includes an instruction stating that issuers may present additional ratios or other information to supplement the required ratio, but are not required to do so. Additional pay ratios are not limited to any particular information, such as pay ratios covering U.S. and non-U.S. employees. If an issuer includes any additional ratios, the ratios must be clearly identified, not misleading, and not presented with greater prominence than the required ratio.

- Identification of the Median Employee. In order to comply with the final rule, an issuer must identify the "median employee"—whose compensation will be used for the annual total compensation calculation—once every three years, unless there has been a change in its employee population or employee compensation arrangements such that the issuer reasonably

believes the change would result in a significant change in the pay ratio. If there has been such a change, the issuer must disclose this change, re-identify the median employee, and provide a brief explanation about the reason or reasons for the change. Alternatively, if there has been no such change, the issuer must disclose that it is using the same median employee in its pay ratio calculation and describe briefly the basis for its reasonable belief. For example, the issuer could disclose that there has been no change in its employee population or employee compensation arrangements that it believes would significantly affect the pay ratio. If the median employee identified in year one is no longer in the same position or no longer employed by the issuer on the median employee determination date in year two or year three, the final rule permits the issuer to replace its median employee with an employee in a similar compensation position.

- Methodology for Identifying the Median Employee. To provide additional transparency about how the pay ratio disclosure has been calculated, the final rule requires that issuers disclose the date used to identify the median employee. Although Section 953(b) of the Act requires that issuers choose the "median" employee as the point of comparison, rather than the average or some other measure, the provision did not prescribe a methodology that must be used to identify the median. Consistent with the proposal, the final rule provides issuers with the flexibility to choose a method to identify the median employee based on their own facts and circumstances. Issuers may use a methodology that uses reasonable estimates. The median employee may be identified using annual total compensation, or any other compensation measure that is consistently applied to all employees included in the calculation, such as information derived from tax and/or payroll records. In addition, in determining the employees from which the median is derived, an issuer is permitted to use its employee population or statistical sampling, and/or other reasonable methods. If statistical sampling is used, the SEC believes that a relatively small sample size may be appropriate in certain situations, and that reasonable estimates of the median may be determined using more than one statistical sampling approach by issuers with multiple business lines or geographical units. Regardless of the calculation method chosen, the final rule requires that the company briefly describe the methodology it used to identify the median employee and any material assumptions, adjustments (including any cost- of-living adjustments), or estimates it used

to identify the median employee or to determine total compensation or any elements of total compensation, which shall be consistently applied. The final rule requires issuers to briefly describe and consistently apply any methodology used to identify the median and any material assumptions, adjustments (including cost-of-living adjustments), or estimates used to identify the median or to determine total compensation or any elements of total compensation. The final rule also requires an issuer to clearly identify any estimates used. For example, when statistical sampling is used, an issuer must describe the size of both the sample and the estimated whole population, any material assumptions used in determining the sample size, and the sampling method (or methods) used. However, issuers are not required to include any technical analyses, formulas, confidence levels, or the steps used in data analysis.

- Annual Total Compensation. The final rule requires that "annual total compensation" for both the median employee and CEO be calculated using the requirements of Item 402(c)(2)(x) of Regulation S-K. This is the case even if the issuer has identified the median employee using reasonable estimates of compensation based on payroll or tax records. Accordingly, an issuer must go through the process of replicating the Summary Compensation Table compensation for the median employee, including, for example, the grant date fair value of equity awards, the incremental change in pension value, and "all other compensation" items such as 401(k) contributions and other benefits. The SEC notes in the final rule that any compensation that is permitted to be excluded from annual total compensation under Item 402 of Regulation S-K, such as benefits under plans available to all employees, may be added back into the calculation if necessary to reflect benefits that are significant for non-management employees of the issuer. Issuers are permitted to use reasonable estimates in calculating the annual total compensation of their median employee, including any elements of the total compensation, but must clearly identify any estimates used and have a reasonable basis to conclude that their estimates approximate the actual amounts of Item 402(c)(2)(x) compensation, or a particular element of compensation that is awarded to, earned by, or paid to the median employee. Although the final rule allows issuers to identify the median employee every three years, it requires total compensation for that employee to be calculated each year. Accordingly, following the issuer's calculation of the median employee's

annual total compensation in year one, it must recalculate the annual total compensation for that employee in year two and again in year three.

Employee or Director Hedging Policies Disclosure

On February 9, 2015, the SEC proposed amendments to implement Section 955 of the Act. The proposed amendments were subject to a 60-day comment period which ended on April 20, 2015.

The proposal would add new paragraph (i) to Item 407 of Regulation S-K. Proposed Item 407(i) would specify the types of transactions that are subject to the disclosure requirement. The scope of the proposed disclosure requirement would not be limited to any particular types of hedging transactions or instruments, but would require disclosure of all transactions with economic consequences comparable to the financial instruments specified in Section 14(j). Specifically, proposed Item 407(i) would require disclosure of whether an employee, officer, or director, or any of their designees, is permitted to purchase financial instruments (including prepaid variable forward contracts, equity swaps, collars, and exchange funds) or otherwise engage in transactions that are designed to or have the effect of hedging or offsetting any decrease in the market value of equity securities (1) granted to the employee or director by the issuer as part of the compensation of the employee or director; or (2) held, directly or indirectly, by the employee or director.

ADDITIONAL GOVERNANCE REQUIREMENTS

Compensation Recovery

Section 954 of the Dodd-Frank Act requires that stock exchange listing standards be amended to require that issuers adopt a policy providing that, if an issuer is required to prepare an accounting restatement due to material noncompliance with any financial reporting requirement under the securities laws, it will recover from any current or former executive officer who received incentive-based compensation (including stock options awarded as compensation) during the three-year period preceding the date on which the issuer is required to prepare an accounting restatement, amounts based on the erroneous data, in excess of what would have been paid under the restatement. Additional disclosure will also be required of an issuer's policy on incentive-based compensation that is based on financial information required to be reported under the securities laws.

On July 1, 2015, the SEC proposed rules to implement Section 954 of the Act. The proposed rules were subject to a 60-day comment period that ended on September 14, 2015.

The proposed rules would require national securities exchanges and associations to establish listing standards that would require listed companies to adopt and comply with a compensation recovery policy in which:

- Recovery would be required from current and former executive officers who received incentive-based compensation during the three fiscal years preceding the date on which the issuer is required to prepare an accounting restatement to correct a material error. The recovery would be required on a "no fault" basis, without regard to whether any misconduct occurred or an executive officer's responsibility for the erroneous financial statements.

- Issuers would be required to recover the amount of incentive-based compensation received by an executive officer that exceeds the amount the executive officer would have received had the incentive-based compensation been determined based on the accounting restatement. For incentive-based compensation based on stock price or total shareholder return, issuers could use a reasonable estimate of the effect of the restatement on the applicable measure to determine the amount to be recovered.

- Issuers would have discretion not to recover the excess incentive-based compensation received by executive officers if the direct expense of enforcing recovery would exceed the amount to be recovered.

Under the proposed rules, an issuer would be subject to delisting if it does not adopt a compensation recovery policy that complies with the applicable listing standard, disclose the policy in accordance with SEC rules or comply with the policy's recovery provisions. The proposed rules also include the following provisions:

- The proposed rules would include a definition of an "executive officer" that is based on the definition of "officer" under Section 16 under the Exchange Act. The definition includes the issuer's president, principal financial officer, principal accounting officer, any vice-president in charge of a principal business unit, division or function, and any other person who performs policy-making functions for the company.

- Under the proposed rules, incentive-based compensation that is granted, earned or vested based wholly or in part on the attainment of any financial reporting measure would be subject to recovery. Financial reporting measures are those based on the accounting principles used in preparing the company's financial statements, any measures derived wholly or in part from such financial information, and stock price and total shareholder return.
- Each listed issuer would be required to file its compensation recovery policy as an exhibit to its Exchange Act annual report.
- In addition, if during its last completed fiscal year the issuer either prepared a restatement that required recovery of excess incentive-based compensation, or there was an outstanding balance of excess incentive-based compensation relating to a prior restatement, the listed issuer would be required to disclose:
    - The date on which it was required to prepare each accounting restatement, the aggregate dollar amount of excess incentive-based compensation attributable to the restatement and the aggregate dollar amount that remained outstanding at the end of its last completed fiscal year.
    - The name of each person subject to recovery from whom the issuer decided not to pursue recovery, the amounts due from each such person, and a brief description of the reason the issuer decided not to pursue recovery.
    - If amounts of excess incentive-based compensation are outstanding for more than 180 days, the name of, and amount due from, each person at the end of the issuer's last completed fiscal year.
- The proposed disclosure would be included along with the listed issuer's other executive compensation disclosure in annual reports, and in any proxy or information statements in which executive compensation disclosure is required.
- Listed issuer's would also be required to block tag the disclosure in an interactive data format using XBRL.
- Each listed issuer would be required to adopt its recovery policy no later than 60 days following the date on which the listing exchange's listing standard becomes effective. Each listed issuer would be required to recover

all excess incentive-based compensation received by current and former executive officers on or after the effective date of Rule 10D-1 that results from attaining a financial reporting measure based on financial information for any fiscal period ending on or after the effective date of Rule 10D-1.

- Listed issuers would be required to comply with the new disclosures in proxy or information statements and Exchange Act annual reports filed on or after the effective date of the listing exchange's rule.

Other Governance Provisions

The Dodd-Frank Act includes a number of additional corporate governance provisions, including:

- Authorizing the SEC to promulgate "proxy access" rules, allowing specified shareholders to include director nominees in the issuer's proxy materials, but not prescribing specific standards for those rules (Section 971). The SEC issued final rules facilitating shareholder director nominations on August 25, 2010, which were scheduled to become effective on November 15, 2010. However, Rule 14a-11 was vacated by U.S. Court of Appeals for the District of Columbia Circuit in July 2011;

- Directing the SEC to promulgate rules mandating proxy statement disclosure of the reasons why the issuer has chosen to have one person serve as Chairman and CEO, or to have different individuals serve in those roles (Section 972). The SEC amended its disclosure rules in December 2009 to require a discussion of this topic and it appears that no further SEC rulemaking will be completed on this topic; and

- Barring brokers from using discretionary authority to vote proxies in connection with election of directors, executive compensation, or other significant matters, as determined by the SEC (Section 957). Under changes already adopted by Rule 452 of the rules of the New York Stock Exchange, no broker discretionary voting is permitted for the election of directors and executive compensation matters.

SEC Staff Guidance for Proxy Advisors

The SEC's Division of Investment Management and Division of Corporation Finance published Staff Legal Bulletin No. 20 on June 30, 2014 regarding investment advisers' responsibilities in voting client proxies, and two exemptions from the federal

proxy rules that are often relied upon by proxy advisory firms. The Staff noted that the guidance may require investment advisers and proxy advisory firms to make changes to their systems and processes. In this regard, the Staff stated its expectation that these changes should be made in advance of the 2015 proxy season.

Investment Advisers

Staff Legal Bulletin No. 20 provides the following guidance for investment advisers:

- Compliance with fiduciary duty. An investment adviser's fiduciary duties require that adviser to cast proxy votes in a manner that is in accordance with the clients' best interests and the adviser's proxy voting procedures. The Staff provided examples of how to demonstrate compliance with this obligation, including: (1) sampling proxy votes to ensure they comply with proxy voting policies; (2) reviewing sample proxy votes to determine if the issues require more analysis; and (3) confirming at least annually, as part of an ongoing compliance program, that the investment adviser's proxy voting policies are being implemented effectively and continue to be designed to provide that proxies are voted in the best interests of clients

- Voting every proxy not required. Advisers and their clients may agree by contract on the manner in which they will delegate proxy voting authority. Some arrangements may provide for the adviser not to assume all proxy voting authority. Examples of these arrangements include, among other things: (1) a client may agree that the benefits may not justify the time and cost of evaluating certain proposals or issuers; (2) a client may agree that the adviser may vote all proposals consistent with management's recommendations or in favor of all proposals made by a particular shareholder proponent, absent a contrary instruction for the client or a determination by the adviser that voting a different way would further the clients' investment strategies (3) a client may agree that the adviser will abstain from voting any proxies, whether or not the client chooses to vote them; and (4) a client may agree that the adviser will focus resources only on particular types of proposals based on the client's preference.

- Selecting a proxy advisory firm. Investment advisers should establish and implement measures reasonably designed to identify and address the proxy

advisory firm's conflicts that can arise on an ongoing basis. For example, the adviser could require the proxy advisory firm to update the investment adviser of business changes the investment adviser considers relevant (i.e., with respect to the proxy advisory firm's capacity and competency to provide proxy voting advice) or conflict policies and procedures.

- Ongoing oversight of proxy advisory firms. Advisers should implement policies and procedures that are reasonably designed to provide sufficient ongoing oversight of the proxy advisory firm to ensure that the investment adviser, acting through the proxy advisory firm, continues to vote proxies in the best interests of its clients. Advisers should determine that the proxy advisory firm has the capacity and competency to adequately analyze proxy issues, including the ability to make voting recommendations based on materially accurate information that it receives and analyzes.

Proxy Advisory Firms

Staff Legal Bulletin No. 20 provides the following guidance for proxy advisory firms:

- Application of proxy rules to proxy advisory firms. Generally, proxy advisory firms are subject to federal proxy rules, because their advice constitutes a "solicitation" of proxies; however, proxy advisory firms are exempt from the information and filing requirements if they comply with the requirements of exemptions contained in Rule 14a-2(b).
- Applicability of Rule 14a-2(b)(1). Rule 14a-2(b)(1) generally exempts persons who do not seek the power to act as a proxy for a security holder. Proxy advisory firms would not be able to rely on this exemption if they allow the client to establish, in advance of receiving proxy materials for particular shareholder meetings, general guidelines or policies that the proxy advisory firm will apply to vote on behalf of the client (even where the authority was revocable by the client).
- Applicability of Rule 14a-2(b)(3). Rule 14a-2(b)(3) generally exempts persons that furnish proxy voting advice to another person with whom a business relationship exists, subject to conditions. A business relationship includes, for example, providing financial advice in the ordinary course of business, provided that the proxy advice is incidental to this relationship and does not involve special compensation. A proxy advisory firm must first

determine whether it has a significant relationship with an issuer or a security holder proponent or whether it has a material interest in the proxy proposal, and what constitutes "significant" or a "material interest" will depend on the facts and circumstances. A proxy adviser must clearly disclose to the client whether it has a "significant relationship or material interest" that could present a conflict of interest, and in this regard boilerplate disclosures will not be sufficient. Disclosure of a significant relationship or material interest is an affirmative duty; it is not sufficient to provide disclosures only upon request. Further, disclosure should be made publicly or in such a way as to allow the client to assess the nature of the significant relationship or interest.

SEC Staff Guidance on Shareholder Proposals

On October 22, 2015, the Staff of the SEC's Division of Corporation Finance issued Staff Legal Bulletin No. 14H ("SLB 14H"), which provided the Staff's views regarding the application of Rule 14a-8(i)(9) (proposals that "directly conflict" with management proposals) and Rule 14a-8(i)(7) (proposals relating to "ordinary business operations"), which are two important substantive bases for the omission of a proposal from an issuer's proxy materials.

Rule 14a-8(i)(9) Guidance

Rule 14a-8(i)(9) permits an issuer to omit a proposal submitted by an eligible shareholder from the issuer's proxy statement if the shareholder proposal "directly conflicts" with a management proposal set forth in the same proxy statement. Rule 14a-8(i)(9) has been used in recent years to exclude shareholder proposals addressing topics such as compensation plan provisions, proxy access, shareholders' ability to call a special meeting, and shareholders' ability to take action by written consent. The SEC has stated that the subject proposals need not be "identical in scope or focus" in order for this basis for exclusion to be available. See SEC Release No. 34-40018 (May 21, 1998). Consistent with the SEC's position, the Staff has historically concurred that where a shareholder proposal and a management proposal present alternative and conflicting decisions for shareholders, and where submitting both proposals could provide inconsistent and ambiguous results, the shareholder proposal could be excluded under Rule 14a-8(i)(9).

On January 16, 2015, Chair Mary Jo White directed the Division of Corporation Finance to review the proper scope and application of Rule 14a-8(i)(9), and the Staff

thereafter announced that it would express no view on no-action requests relating to the exclusion of shareholder proposals in reliance on Rule 14a-8(i)(9). Without having the ability to seek the Staff's concurrence to exclude a shareholder proposal based on Rule 14a-8(i)(9), issuers pursued a number of alternative methods for addressing shareholder proposals that conflicted with management proposals. The most common alternative methods were (i) including both the shareholder proposal and the management proposal in the proxy statement, with an explanation to shareholders regarding any differences in scope of applicability and recommending that shareholders vote in favor of the management proposal; and (ii) including only the shareholder proposal, and recommending that shareholders vote against that proposal.

In SLB 14H, the Staff expressed the view that there is a "direct conflict" between a shareholder proposal and management proposal only where "a reasonable shareholder could not logically vote in favor of both proposals, i.e., a vote for one proposal is tantamount to a vote against the other proposal." The Staff noted that this analysis "more appropriately focuses on whether a reasonable shareholder could vote favorably on both proposals, or whether they are, in essence, mutually exclusive proposals." In communicating this interpretation, the Staff focused on the principle that Rule 14a-8(i)(9) is designed to ensure that the shareholder proposal process is not used as a means to circumvent the SEC's proxy rules governing solicitations.

In SLB 14H, the Staff provided the following examples to provide a better understanding of the Staff's focus on "whether a reasonable shareholder could logically vote for both proposals."

- Direct Conflict Exists. The Staff stated that (i) "where a company seeks shareholder approval of a merger, and a shareholder proposal asks shareholders to vote against the merger;" or (ii) "a shareholder proposal that asks for the separation of the company's chairman and CEO would directly conflict with a management proposal seeking approval of a bylaw provision requiring the CEO to be the chair at all times," the Staff "would agree that the proposals directly conflict."

- Direct Conflict Does Not Exist. In illustrating those circumstances in which a direct conflict would not exist for purposes of Rule 14a-8(i)(9), the Staff provided the following examples: (i) "if a company does not allow shareholder nominees to be included in the company's proxy statement, a shareholder proposal that would permit a shareholder or group of shareholders

holding at least 3% of the company's outstanding stock for at least 3 years to nominate up to 20% of the directors would not be excludable if a management proposal would allow shareholders holding at least 5% of the company's stock for at least 5 years to nominate for inclusion in the company's proxy statement 10% of the directors;" and (ii) "a shareholder proposal asking the compensation committee to implement a policy that equity awards would have no less than four-year annual vesting would not directly conflict with a management proposal to approve an incentive plan that gives the compensation committee discretion to set the vesting provisions for equity awards." The Staff noted that these situations would not present a "direct conflict" because "a reasonable shareholder, although possibly preferring one proposal over the other, could logically vote for both."

With respect to the proxy access example described above, the Staff stated that there would be no direct conflict because "both proposals generally seek a similar objective, to give shareholders the ability to include their nominees for director alongside management's nominees in the proxy statement, and the proposals do not present shareholders with conflicting decisions such that a reasonable shareholder could not logically vote in favor of both proposals." The Staff analyzed the compensation example similarly, stating that "a reasonable shareholder could logically vote for a compensation plan that gives the compensation committee the discretion to determine the vesting of awards, as well as a proposal seeking implementation of a specific vesting policy that would apply to future awards granted under the plan."

The Staff noted that SLB 14H could impose "a higher burden for some companies seeking to exclude a proposal to meet than had been the case under our previous formulation." As a result, issuers may turn to Rule 14a-8(i)(10) in seeking to exclude a shareholder proposal that is very similar to a management proposal or action. Rule 14a-8(i)(10) provides an exclusion from an issuer's obligation to include shareholder proposals from eligible shareholders in the issuer's proxy statement if the issuer's existing policies and practices "substantially implement" the shareholder proposal.

Rule 14a-8(i)(7) Guidance

Rule 14a-8(i)(7) provides that a proposal is excludable when the proposal deals with a matter relating to the company's ordinary business operations. A recent Third Circuit Court of Appeals decision in *Trinity Wall Street v. Wal-Mart Stores, Inc.* held that an issuer could exclude a shareholder proposal from its proxy materials based on

Rule 14a-8(i)(7), but raised some questions as to the proper framework for analysis under Rule 14a-8(i)(7). Notwithstanding the fact that the outcome of the Third Circuit decision was in line with the Staff's earlier conclusions in the same matter, the Staff expressed a concern in SLB 14H that the decision could lead to the unwarranted exclusion of a shareholder proposal. In this regard, SLB 14H specifically addressed the Third Circuit's majority ruling regarding the "significant policy issue" exception to the ordinary business exclusion, which described a two-part test under which "a shareholder must do more than focus its proposal on a significant policy issue; the subject matter of its proposal must 'transcend' the company's ordinary business." The Staff noted that the court "found that to transcend a company's ordinary business, the significant policy issue must be 'divorced from how a company approaches the nitty-gritty of its core business.'" The Staff concluded that it would continue to follow the one-part "ordinary business" analysis that it has historically applied, based on the SEC's view (which was articulated by the concurring judge in the Third Circuit decision) that proposals focusing on a significant policy issue are not excludable under the ordinary business exception "because the proposals would transcend the day-to-day business matters and raise policy issues so significant that it would be appropriate for a shareholder vote." As a result, the Staff indicates in SLB 14H that "a proposal may transcend a company's ordinary business operations even if the significant policy issue relates to the 'nitty-gritty of its core business.'"

CHAPTER 2

SAY-ON-PAY

SAY-ON-PAY

Advisory Votes on Executive Compensation – Rules and Guidance

Introduction

Say-on-Pay was one of the most highly anticipated corporate governance developments in the United States. Say-on-Pay has been utilized in other jurisdictions, such as in the United Kingdom, where Say-on-Pay encouraged greater engagement between issuers and institutional investors over compensation and governance issues. Advocates of Say-on-Pay in the United States hoped that the advisory votes will encourage greater accountability for executive compensation decisions through a direct shareholder referendum, more focused disclosure in proxy statements and significantly expanded shareholder engagement.

The Say-on-Pay and Say-on-Frequency requirements were effective for larger public companies for annual meetings on or after January 21, 2011. The SEC's implementing rules, adopted on January 25, 2011, became effective on April 4, 2011 (with the exception of golden parachute requirements, which became effective for filings made on or after April 25, 2011). Smaller reporting companies were exempt from the Say-on-Pay and Say-on-Frequency vote requirements until the first annual meeting or other meeting of shareholders occurring on or after January 21, 2013.

The Dodd-Frank Act Requirements

Section 951 of the Dodd-Frank Act, which added Section 14A to the Exchange Act, requires that issuers include a resolution in their proxy statements (at least once every three years) asking that shareholders approve, in a nonbinding vote, the compensation of the executive officers, as disclosed under Item 402 of Regulation S-K, the Say-on-Pay vote.

A separate resolution is required (at least once every six years) to determine whether the Say-on-Pay vote takes place every one, two, or three years—the Say-on-Frequency vote. Those issuers that conducted their first Say-on-Frequency vote immediately after the enactment of the Dodd-Frank Act will be required to conduct a Say-on-Frequency vote again in the 2017 proxy season.

If golden parachute compensation has not been approved as part of a Say-on-Pay vote, then issuers must solicit shareholder approval of golden parachute compensation

through a separate nonbinding vote at the meeting where the shareholders are asked to approve a merger or similar extraordinary transaction that would trigger payments under the "golden parachute" provisions, the Say-on-Golden Parachute vote.

Section 14A also requires that any proxy statement used for soliciting the Say-on-Golden Parachute vote must include "clear and simple" disclosure of the golden parachute arrangements or understandings and the amounts payable.

In order to implement these requirements, the SEC adopted, in SEC Release No. 33-9178 (January 25, 2011) (the "Adopting Release"), new Exchange Act Rule 14a-21, which governs advisory votes on executive compensation going forward (with the exception of those issuers that have indebtedness outstanding under the TARP program, who must solicit annual Say-on-Pay votes under the Emergency Economic Stabilization Act, as amended ("EESA"), and Exchange Act Rule 14a-20). The SEC also adopted a number of additional rule, form and schedule changes to accommodate the new Say-on-Pay, Say-on-Frequency and Say-on-Golden Parachute votes.

Say-on-Pay Votes

Rule 14a-21(a) provides that if a solicitation is made by an issuer relating to an annual or other meeting of shareholders at which directors will be elected and for which the SEC's rules require executive compensation disclosure pursuant to Item 402 of Regulation S-K, then the issuer must conduct a Say-on-Pay vote, and a Say-on-Pay vote must occur thereafter no later than the annual or other meeting of shareholders held in the third calendar year after the immediately preceding Say-on-Pay vote. The Say-on-Pay vote relates to the executive compensation disclosure required to be included in the proxy statement, which generally includes the CD&A, the compensation tables, and the narrative disclosure on executive compensation.

The SEC states in footnote 18 of the Adopting Release that it views Section 951 of the Dodd-Frank Act as requiring a separate shareholder vote on executive compensation only with respect to "an annual meeting of shareholders for which proxies will be solicited for the election of directors, or a special meeting in lieu of such annual meeting." Accordingly, Rules 14a-21(a) and 14a-21(b) (governing the Say-on-Frequency vote, as discussed below) are intended to apply in connection with the election of directors when the related proxy materials must include executive compensation disclosure.

The key Say-on-Pay rules and interpretations are as follows:

- Director Compensation and Risk Disclosure Not Covered. Instruction 1 to Rule 14a-21 provides that the Say-on-Pay vote does not cover director compensation disclosed pursuant to paragraphs (k) and (r) of Item 402 of Regulation S-K, as well as any disclosure pursuant to Item 402(s) of Regulation S-K about the issuer's compensation policies and practices as they relate to risk management and risk-taking incentives. However, if risk considerations are a material aspect of the issuer's compensation policies or decisions for named executive officers, then the Instruction indicates that the company must discuss these considerations as part of the CD&A, and such disclosure will then be subject to the Say-on-Pay vote.

- Wording of the Say-on-Pay Resolution. Rule 14a-21(a) does not require that issuers use a specific form of resolution. However, the Instruction to Rule 14a-21(a) provides the following nonexclusive example that would satisfy the requirements of the rule: "RESOLVED, that the compensation paid to the company's named executive officers, as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis, compensation tables and narrative discussion, is hereby APPROVED."

  While the SEC has provided this nonexclusive example of a form of resolution, the SEC states in the Adopting Release that issuers "should retain the flexibility to craft the resolution language." Issuers have adopted differing language in order to present their Say-on-Pay vote, including language that is not presented as a resolution to be adopted by shareholders.

  In Exchange Act Rules Compliance and Disclosure Interpretations Question 169.05, the Staff has indicated that it is permissible for the Say-on-Pay vote to omit the words, "pursuant to Item 402 of Regulation S-K," and to replace those words with a plain English equivalent, such as "pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the compensation discussion and analysis, the compensation tables and any related material disclosed in this proxy statement."

- Wording of the Description of the Say-on-Pay Proposal on the Proxy Card. In Exchange Act Rules Compliance and Disclosure Interpretations Ques-

tion 169.07, the Staff notes that an issuer's proxy card and voting instruction form should not describe the advisory vote to approve executive compensation with the language "to hold an advisory vote on executive compensation," and should rather use formulations such as: "to approve the company's executive compensation;" "advisory approval of the company's executive compensation;" "advisory resolution to approve executive compensation;" or "advisory vote to approve named executive officer compensation." The Staff states that impermissible example referenced above would not be consistent with Rule 14a-21 because it is not clear from the description as to what shareholders are being asked to vote on.

Say-on-Frequency Votes

Rule 14a-21(b) provides that if a solicitation is made by an issuer relating to an annual or other meeting of shareholders at which directors will be elected, and for which the SEC's rules require executive compensation disclosure pursuant to Item 402 of Regulation S-K, then that issuer must conduct a Say-on-Frequency vote for its first annual or other meeting of shareholders occurring on or after January 21, 2011, and that such Say-on-Frequency vote must occur thereafter no later than the annual or other meeting of shareholders held in the sixth calendar year after the immediately preceding Say-on-Frequency vote. An issuer could hold a Say-on-Frequency vote more frequently than every six years if it elects to do so.

The key Say-on-Frequency rules and interpretations are as follows:

- Say-on-Frequency Choices. Under Rule 14a-21(b), the required Say-on-Frequency resolution must ask shareholders to indicate whether future Say-on-Pay votes should occur every one, two or three years. As a result, shareholders are given four choices on the proxy card: whether the Say-on-Pay vote will take place every one, two, or three years, or to abstain from voting on the resolution. In order to implement the voting choices for the Say-on-Frequency vote, the SEC amended Exchange Act Rule 14a-4 to specifically allow proxy cards to reflect the choices of one, two, or three years, or abstain.
- Wording of the Say-on-Frequency Resolution. Rule 14a-21(b) does not require that issuers use a specific form of resolution. Unlike the Say-on-Pay vote requirement in Rule 14a-21(a), the SEC does not provide a non-exclusive example of a Say-on-Frequency resolution. Exchange Act Rules

Compliance and Disclosure Interpretations Question 169.04 indicates that the Say-on-Frequency vote need not be set forth as a resolution. Separately, the Staff has informally cautioned that the Say-on-Frequency vote must be clearly stated, and that in this regard it must be clear that shareholders can vote on the options of every one, two or three years (or abstain from voting), rather than solely following management's recommendation (if any is provided). Issuers relied on this Staff guidance to provide more Say-on-Frequency votes in a "proposal" format, such as by simply referencing the four choices that are available on the proxy card. The Staff also indicates in Exchange Act Rules Compliance and Disclosure Interpretations Question 169.06 that it is permissible for the Say-on-Frequency vote to include the words "every year, every other year, or every three years, or abstain" in lieu of "every 1, 2, or 3 years, or abstain."

- Recommendations. Neither Rule 14a-21(b) nor the SEC's other proxy rules require that an issuer make a recommendation with respect to the Say-on-Frequency vote; however, the SEC notes that proxy holders may vote uninstructed proxy cards in accordance with management's recommendation only if the company follows the existing requirements of Rule 14a-4, which include specifying how proxies will be voted (i.e., in accordance with management's recommendations) in the absence of instruction from the shareholder. Most proxy statements filed in the 2011 proxy season with mandatory Say-on-Frequency votes included a recommendation as to the preferred frequency of future Say-on-Pay votes, with the majority of those recommendations favoring Say-on-Pay votes annually.

Additional Requirements

The SEC adopted other changes to rules and forms relating to Say-on-Pay and Say-on-Frequency, including:

- No Preliminary Proxy Statement. The SEC amended Exchange Act Rule 14a-6(a) to add any shareholder advisory votes on executive compensation, including the Say-on-Pay or Say-on-Frequency votes, to the list of items that will not trigger the requirement to file a preliminary proxy statement with the SEC. This amendment contemplates an advisory vote on executive compensation that is not required by Section 14A of the Exchange Act.

- Proxy Statement Disclosures. Item 24 to Schedule 14A requires disclosure, in the proxy statement in which the issuer is providing a Say-on-Pay, Say-on-Frequency or Say-on-Golden Parachute vote, that the issuer is providing such vote as required pursuant to Section 14A of the Exchange Act. Further, the issuer must explain the general effect of such vote, such as that the vote is non-binding. Issuers also must disclose, when applicable, the current frequency of Say-on-Pay votes and when the next Say-on-Pay vote will occur.

- CD&A Disclosure. Amended Item 402(b)(1) of Regulation S-K requires an issuer to address in its CD&A whether and, if so, how the issuer has considered the results of the most recent shareholder advisory vote on executive compensation (as required by Section 14A of the Exchange Act or Exchange Act Rule 14a-20, which is the rule governing Say-on-Pay votes required for recipients of financial assistance under TARP) in determining compensation policies and decisions and, if so, how that consideration has affected the issuer's compensation decisions and policies. This requirement is included among the "mandatory" CD&A disclosure items specified by Item 402(b)(1) of Regulation S-K.

- Item 5.07 Form 8-K. Item 5.07 of Form 8-K, as amended, requires that an issuer must disclose its decision as to how frequently the issuer will conduct Say-on-Pay votes following each Say-on-Frequency vote. If an issuer does not disclose the issuer's frequency determination in its initial Item 5.07 Form 8-K, then the issuer must file an amendment to its prior Form 8-K filing (or filings) that disclose the preliminary and final results of the Say-on-Frequency vote. The Form 8-K amendment is due no later than 150 calendar days after the date of the end of the annual meeting in which the Say-on-Frequency vote occurred, but in no event later than 60 calendar days prior to the deadline for the submission of shareholder proposals as disclosed in the proxy materials for the meeting at which the Say-on-Frequency vote occurred. An issuer must disclose in Item 5.07 of Form 8-K the number of votes cast for each of the choices of every one, two or three years, as well as the number of abstentions.

- Substantially Implemented Shareholder Proposals. The SEC added a Note to Exchange Act Rule 14a-8(i)(10) to permit the exclusion of a shareholder proposal as "substantially implemented" if the proposal would provide for a Say-on-Pay vote, seek future Say-on-Pay votes, or relate to the frequency of

Say-on-Pay votes. Such shareholder proposals may be excluded under the new Note if, in the most recent Say-on-Frequency vote, a single frequency received a majority of the votes cast and the issuer adopted a policy for the frequency of Say-on-Pay votes that is consistent with that choice. The Staff has noted that this Note will also apply to shareholder proposals seeking votes on matters that are already "subsumed" within the Say-on-Pay or Say-on-Frequency vote, not just a Section 14A-compliant Say-on-Pay/Say-on-Frequency proposal.

Say-on-Golden Parachute Vote

Rule 14a-21(c) provides that if a solicitation is made by the issuer for a meeting of shareholders at which the shareholders are asked to approve an acquisition, merger, consolidation, or proposed sale or other disposition of all or substantially all of the assets of the issuer, then the issuer must provide a separate shareholder vote to approve any agreements or understandings and compensation disclosed pursuant to Item 402(t) of Regulation S-K. However, if such agreements or understandings have been subject to a shareholder advisory vote under Rule 14a-21(a) (the Say-on-Pay vote), then a separate shareholder vote is not required. Consistent with Exchange Act Section 14A(b), any agreements or understandings between an acquiring company and the named executive officers of the issuer, where the issuer is not the acquiring company, are not required to be subject to the separate shareholder advisory vote. The SEC did not adopt any specific form of the Say-on-Golden Parachute resolution and has clarified the advisory nature of the Say-on-Golden Parachute vote.

The rule provides as follows:

- Item 402(t) of Regulation S-K requires disclosure of named executive officers' golden parachute arrangements in a proxy statement for shareholder approval of a merger, sale of a company's assets or similar transactions. This Item 402(t) disclosure is only required in annual meeting proxy statements when an issuer is seeking to rely on the exception from a separate merger proxy shareholder vote by including the proposed Item 402(t) disclosure in the annual meeting proxy statement soliciting a Say-on-Pay vote.

- Golden parachute compensation must be disclosed in a table along with accompanying footnotes and narrative disclosure. This table is set forth below:

Golden Parachute Compensation

Name (a)	Cash ($) (b)	Equity ($) (c)	Pension/ NQDC ($) (d)	Perquisites/ Benefits ($) (e)	Tax Reimbursement ($) (f)	Other ($) (g)	Total ($) (h)
PEO							
PFO							
A							
B							
C							

- The table requires quantification of:
  - cash severance payments;
  - the value of equity awards that are accelerated or cashed out;
  - pension and nonqualified deferred compensation enhancements;
  - perquisites and other personal benefits;
  - tax reimbursements; and
  - in the “Other” column, any additional compensation that is not included in any other column.
- Separate footnote identification is required for amounts attributable to “single-trigger” and “double-trigger” arrangements.
- The table requires quantification with respect to any type of compensation, whether present, deferred or contingent, that is based on or relates to an acquisition, merger, consolidation, sale or other disposition of all or substantially all of the assets.
- Item 402(t) of Regulation S-K also requires issuers to describe any material conditions or obligations applicable to the receipt of payment, including but not limited to non-compete, non-solicitation, non-disparagement or confidentiality agreements, their duration, and provisions regarding waiver or breach.

- Disclosure of the specific circumstances that would trigger payment, whether the payments would be lump sum, or annual, and their duration, and by whom the payments would be provided, and other material factors regarding each agreement is also required.
- Separate disclosure or quantification with respect to compensation disclosed in the Pension Benefits Table and Nonqualified Deferred Compensation Table (unless such benefits are enhanced in connection with the transaction), previously vested equity awards and compensation from bona fide post-transaction employment agreements entered into in connection with the merger or acquisition is not required.

In Regulation S-K Compliance and Disclosure Interpretations Question 128B.01, the Staff provides the following guidance regarding the application of Item 402(t):

> **Question:** Instruction 1 to Item 402(t)(2) provides that Item 402(t) disclosure will be required for those executive officers who were included in the most recently filed Summary Compensation Table. If a company files its annual meeting proxy statement in March 2011 (including the 2010 Summary Compensation Table), hires a new principal executive officer in May 2011 and prepares a merger proxy in September 2011, may the company rely on this instruction to exclude the new principal executive officer from the merger proxy's say-on-golden parachute vote and Item 402(t) disclosure?
>
> **Answer:** No. Instruction 1 to Item 402(t) specifies that Item 402(t) information must be provided for the individuals covered by Items 402(a)(3)(i), (ii) and (iii) of Regulation S-K. Instruction 1 to Item 402(t)(2) applies only to those executive officers who are included in the Summary Compensation Table under Item 402(a)(3)(iii), because they are the three most highly compensated executive officers other than the principal executive officer and the principal financial officer. Under Items 402(a)(3)(i) and (ii), the principal executive officer and the principal financial officer are, per se, named executive officers, regardless of compensation level. Consequently, Instruction 1 to Item 402(t)(2) is not instructive as to whether the principal executive officer or principal financial officer is a named executive officer. This position also applies to Instruction 2 to Item 1011(b), which is the corresponding instruction in Regulation M-A.

Additional forms, schedules and disclosure requirements address golden parachute compensation, such as Schedule 14A, Schedule 14C, Forms S-4 and F-4, Schedule 14D-9, Schedule 13E-3 and Item 1011 of Regulation M-A. Schedule TO provides that Item 402(t) disclosure is not required in a third-party bidders' tender offer statement, so long as the subject transaction is not also Rule 13e-3 going private transaction. Issuers filing solicitation/recommendation statements on Schedule 14D-9 in connection with third-party tender offers will be obligated to provide the disclosure required by Item 402(t) of Regulation S-K.

Smaller Reporting Companies

"Smaller reporting companies," as defined in SEC rules, were not subject to the Say-on-Pay or Say-on-Frequency requirements and the SEC's related rules until their first annual meeting or other meeting of shareholders at which directors will be elected, and for which executive compensation disclosure is required, occurring on or after January 21, 2013.

Background Regarding Smaller Reporting Company Rules

A "smaller reporting company" is generally defined for the purposes of its initial testing as an issuer that has a public float of less than $75 million or, in the case of an issuer that has no public float, has annual revenues of less than $50 million. A reporting issuer with a public float determines eligibility as a smaller reporting company as of the last business day of its most recently completed second fiscal quarter, calculating its float by multiplying (i) the aggregate worldwide number of shares of its (voting and non-voting) common equity held by non-affiliates by (ii) the price at which the common equity was last sold, or the average of the bid and asked prices, in the principal market. With respect to any issuer that is above the smaller reporting company threshold at the time of its initial testing, when that issuer subsequently tests annually for smaller reporting company status, the applicable thresholds are: (i) less than $50 million public float or, in the case of an issuer that has no public float; and (ii) annual consolidated revenues of less than $40 million during its previous fiscal year. The rules contemplate an annual testing of smaller reporting company status, consistent with the annual testing for non-accelerated filer, accelerated filer and large accelerated filer status.

In general, smaller reporting companies are not required to provide as much executive compensation disclosure as is required for companies that do not qualify for the smaller reporting company reporting regime. The following differences exist between the smaller reporting company requirements and the requirements applicable to larger issuers in Items 402 and 407 of Regulation S-K:

- The number of named executive officers that is required to be disclosed is reduced, in that smaller reporting companies only have to report in the Summary Compensation Table the compensation for the principal executive officer and the two most highly compensated executive officers other than the principal executive officer who are serving at the end of the last completed fiscal year and whose total compensation exceeds $100,000, as well as two additional individuals for whom disclosure would have been provided, except for the fact that they were not serving as executive officers at the end of the fiscal year;
- The smaller reporting company requirements require information in the Summary Compensation Table for the last two completed fiscal years, rather than the last three completed fiscal years as required for larger issuers; in addition, the Summary Compensation Table under the smaller reporting company requirements does not require the inclusion of the change in actuarial pension plan value;
- The smaller reporting company requirement mandates additional narrative requirements with regard to the Summary Compensation Table to explain some of the items of compensation;
- The Outstanding Equity Awards at Fiscal Year-End Table is required under the smaller reporting company rules, and some additional narrative disclosure is required about items such as retirement benefits and the material terms of contracts that would provide for benefits upon termination and change of control;
- The CD&A, the Grants of Plan-Based Awards Table, the Option Exercises and Stock Vested Table, the Non-Qualified Deferred Compensation Table, the Pension Benefits Table and the Compensation Committee Report are not required under the smaller reporting company rules;
- The disclosure required by Item 402(s) regarding the relationship of compensation and risk is not required for smaller reporting companies; and

- The Director Compensation Table is required under both the rules applicable to smaller reporting companies and the rules applicable to larger issuers.

No changes were made to the scaled disclosure requirements as a result of the Say-on-Pay and Say-on-Frequency votes, and thus smaller reporting companies are not required to include a CD&A in order to comply with Rule 14a-21. Pursuant to Item 402(o) of Regulation S-K, however, smaller reporting companies are required to provide a narrative description of any material factors necessary to an understanding of the information in the Summary Compensation Table; therefore, if consideration of prior Say-on-Pay votes is such a factor, disclosure would be required.

Transition Issues for Smaller Reporting Companies

When a non-smaller reporting company first drops below the applicable threshold, the issuer may immediately transition to smaller reporting company scaled disclosure discussed above beginning with the Form 10-Q covering that second fiscal quarter-end measurement date establishing the issuer's status as a smaller reporting company, although the smaller reporting company status does not begin until the beginning of the next fiscal year. If the issuer decides to immediately transition to smaller reporting company status, then the issuer would begin checking the smaller reporting company box on the cover page of the second quarter Form 10-Q. The rules provide that, when a smaller reporting company's annual testing determines that it is no longer a smaller reporting company, the issuer must transition to the regular reporting system, beginning with the Form 10-Q for the first fiscal quarter of the next fiscal year after the determination date.

In Question 104.13 of the Exchange Act Forms Compliance and Disclosure Interpretations, the Staff presents a scenario where an issuer files its 2008 Form 10-K using the disclosure permitted for smaller reporting companies under Regulation S-K, and the cover page of the Form 10-K indicates that the issuer will no longer qualify to use the smaller reporting company disclosure for 2009, because its public float exceeded $75 million at the end of its second fiscal quarter in 2008. The issuer proposes to rely on General Instruction G(3) to incorporate by reference executive compensation and other disclosure required by Part III of Form 10-K into the 2008 Form 10-K from its definitive proxy statement to be filed not later than 120 days after its 2008 fiscal year end. The Staff indicates that, in these circumstances, the issuer may use smaller reporting company disclosure in this proxy statement, even though it does not qualify to use smaller reporting company disclosure for 2009. In the Staff's view, this is because the

issuer could have used the smaller reporting company disclosure for Part III of its 2008 Form 10-K if it had not used General Instruction G(3) to incorporate that information by reference from the definitive proxy statement.

On February 11, 2011, the Staff of the SEC's Division of Corporation Finance issued a number of Compliance and Disclosure Interpretations to explain how the Say-on-Pay/Say-on-Frequency exemption for smaller reporting companies will apply. The interpretations are as follows:

- **Exchange Act Rules Compliance and Disclosure Interpretations Question 169.01:**
  Question: Based on its $30 million public float as of the last business day of the second quarter in 2010, an issuer with a December 31 fiscal year end is permitted to begin filing reports as a smaller reporting company with its Form 10-Q for the second quarter in 2010. The issuer has opted to continue complying with the reporting requirements for larger companies until its Form 10-Q for the first quarter in 2011 and therefore will not check the "Smaller Reporting Company" box on the cover of any periodic report until that Form 10-Q. Is the issuer entitled to rely on the delayed phase-in period for smaller reporting companies for compliance with Rule 14a-21, even though it has not indicated its status as a smaller reporting company by checking the "Smaller Reporting Company" box on a periodic report before January 21, 2011 (the date provided in the Commission release for eligibility for the smaller reporting company delayed phase-in period)?

  Answer: Yes. An issuer that is a smaller reporting company as of January 21, 2011 is entitled to rely on the delayed phase-in period for smaller reporting companies. Each issuer determines its eligibility for smaller reporting company status for 2011 on the basis of its public float or annual revenue as of the last business day of the second fiscal quarter of 2010. Although an issuer is permitted to early adopt its status as a smaller reporting company, it takes that status on the first day of 2011. Accordingly, in this example, on January 1, 2011, the issuer is a smaller reporting company, even though it is not required to indicate as such until its Form 10-Q for the first quarter of 2011.

- **Exchange Act Rules Compliance and Disclosure Interpretations Question 169.02:**
  Question: Based on its $100 million public float as of the last business day of the second quarter in 2010, an issuer with a December 31 fiscal year end will be required to report under non-smaller reporting company disclosure provisions beginning with the Form 10-Q for the first quarter in 2011. Does this issuer qualify as a smaller reporting company as of January 21, 2011, thus entitling it to rely on the delayed phase-in period for smaller reporting companies for compliance with Rule 14a-21?

  Answer: No. Each issuer determines its eligibility for smaller reporting company status for 2011 on the basis of its public float or annual revenue as of the last business day of the second fiscal quarter of 2010. If an issuer with a December 31 fiscal year end is no longer eligible to be a smaller reporting company, it loses that status on the first day of 2011, even though it is permitted to file its Form 10-K for 2010 in 2011 as a smaller reporting company. Accordingly, in this example, on January 1, 2011, the issuer is no longer a smaller reporting company, even though it can check the "Smaller Reporting Company" box on the cover of its Form 10-K for fiscal year 2010. The issuer will not be permitted to check the "Smaller Reporting Company" box on the cover of its Form 10-Q for the first quarter of 2011.

- **Exchange Act Rules Compliance and Disclosure Interpretations Question 169.03:**
  Question: Based on its $100 million public float as of September 30, 2010, which is the last business day of its second fiscal quarter in 2010, an issuer with a March 31 fiscal year end that has been reporting as a smaller reporting company will be required to report under non-smaller reporting company disclosure provisions beginning with the Form 10-Q for its first fiscal quarter in 2011, which begins on April 1, 2011. Does this issuer qualify as a smaller reporting company as of January 21, 2011, thus entitling it to rely on the delayed phase-in period for smaller reporting companies for compliance with Rule 14a-21?

  Answer: Yes. This issuer would continue to qualify as a smaller reporting company until April 1, 2011 (the first day of its next fiscal year). As of January 21, 2011, this issuer would be a smaller reporting company eligible for the delayed phase-in period.

Interaction With The Tarp Say-on-Pay Requirements

For those issuers that have received financial assistance under the TARP and who have indebtedness outstanding under TARP, the vote to approve executive compensation under Rule 14a-20 would satisfy the Say-on-Pay vote requirement. Once these issuers have repaid all outstanding indebtedness under TARP, they would have to include a Say-on-Pay vote under Exchange Act Section 14A and Rule 14a-21(a) for the first annual meeting after the issuer has repaid all outstanding indebtedness. These issuers would not have to provide for a Say-on-Frequency vote as long as they still have indebtedness outstanding under TARP, given that the EESA already requires an annual Say-on-Pay vote for TARP recipients.

The Jumpstart Our Business Startups Act

The Jumpstart Our Business Startups Act (the "JOBS Act") was enacted on April 5, 2012. The JOBS Act was the culmination of a year-long bipartisan effort in both the House and Senate to address concerns about capital formation and unduly burdensome SEC regulations. The JOBS Act affects both exempt and registered offerings, as well as the reporting requirements for certain public issuers.

A centerpiece of the JOBS Act is an "IPO on-ramp" approach for a class of "emerging growth companies" (Title I), with confidential SEC Staff review of draft IPO registration statements, scaled disclosure requirements, no restrictions on "test-the-waters" communications with qualified institutional buyers (QIBs) and institutional accredited investors before and after filing a registration statement, and fewer restrictions on research (including research by participating underwriters) around the time of an offering.

Emerging Growth Company Status

Title I of the JOBS Act established process and disclosures for IPOs by issuers referred to as "emerging growth companies." Title I was retroactively effective to December 9, 2011 for qualifying issuers.

An "emerging growth company" (an "EGC") is defined as an issuer (including a foreign private issuer) with total annual gross revenues of less than $1 billion (subject to inflationary adjustment by the SEC every five years) during its most recently completed fiscal year. In its Frequently Asked Questions of General Applicability on Title I of the JOBS Act issued on April 16, 2012, the Staff of the SEC's Division of Corporation Finance specified that the phrase "total annual gross revenues" means total

revenues of the issuer (or a predecessor of the issuer, if the predecessor's financial statements are presented in the registration statement for the most recent fiscal year), as presented on the income statement in accordance with U.S. generally accepted accounting principles ("GAAP"). For financial institutions, the SEC Staff has indicated that total annual gross revenues should be determined in the manner consistent with the approach used for determining status as a "smaller reporting company," which looks to all gross revenues from traditional banking activities. If a foreign private issuer is using International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") as its basis for presentation, then the IFRS revenue number is used for this test. Because an issuer must determine its EGC status based on revenues as expressed in U.S. dollars, the SEC Staff indicates that a foreign private issuer's conversion of revenues should be based on the exchange rate as of the last day of the fiscal year. In Question 51 of the Frequently Asked Questions of General Applicability on Title I of the JOBS Act issued on September 28, 2012, the Staff provides that, in applying the revenue test for determining EGC status, a calendar year-end issuer that would like to file a registration statement for an initial public offering of common equity securities in January 2013 (which would present financial statements for 2011 and 2010 and the nine months ended September 30, 2012 and 2011) should look to its most recently completed fiscal year, which would be the most recent annual period completed, regardless of whether financial statements for the period are presented in the registration statement. In this example, the most recent annual period completed would be 2012.

An issuer can qualify as an EGC if it first sold its common stock in a registered offering on or after December 9, 2011. The Staff notes in its April 16 Frequently Asked Questions that this eligibility determination is not limited to initial public offerings that took place on or prior to December 8, 2011, in that it could also include an offering of common equity securities under an employee benefit plan on Form S-8, as well as a selling shareholder's registered secondary offering. The Staff does note that just having a registration statement go effective on or before December 8, 2011 is not a bar to EGC status, as long as no common equity securities were actually sold off of the registration statement on or before December 8, 2011.

The Staff notes in its May 3 Frequently Asked Questions that an issuer that succeeds to a predecessor's Exchange Act registration or reporting obligations under Rule 12g-3 and 15d-5 will not qualify for EGC status if the predecessor's first sale of common equity securities occurred on or before December 8, 2011, as the predecessor

was not eligible for that EGC status. This FAQ left unanswered the more common circumstance where an issuer may have gone private in the past and is going public again, either as the same entity or through a parent or subsidiary of that entity, where there is no Exchange Act succession. This is particularly an issue for those companies that were taken private through private equity or management buyouts with the expectation of a liquidity event or exit through an IPO in the future, which have made up a relatively significant portion of the IPO market in recent years.

In Question 54 of the September 28 Frequently Asked Questions, the Staff addresses the EGC status of an issuer that was once an Exchange Act reporting company but is not currently required to file Exchange Act reports. The Staff notes that such an issuer can take advantage of the benefits of EGC status, even though its initial public offering of common equity securities occurred on or before December 8, 2011. In this regard, the Staff notes that if an issuer would otherwise qualify as an EGC but for the fact that its initial public offering of common equity securities occurred on or before December 8, 2011, and such issuer was once an Exchange Act reporting company but is not currently required to file Exchange Act reports, then the Staff would not object if such issuer takes advantage of all of the benefits of EGC status for its next registered offering and thereafter, until it triggers one of the disqualification provisions in Sections 2(a)(19)(A)-(D) of the Securities Act. This position is not available to an issuer that has had the registration of a class of its securities revoked pursuant to Exchange Act Section 12(j). The Staff goes on to note that, based on the particular facts and circumstances, the EGC status of an issuer may be questioned if it appears that the issuer ceased to be a reporting company for the purpose of conducting a registered offering as an EGC. The Staff recommends that issuers with questions relating to these issues should contact the Division of Corporation Finance's Office of the Chief Counsel.

In Question 53 of the September 28 Frequently Asked Questions, the Staff addresses EGC status in the context of spin-offs. The Staff addresses the situation where a parent decides either to spin-off a wholly owned subsidiary, register an offer and sale of the wholly-owned subsidiary's common stock for an initial public offering, or transfer a business into a newly-formed subsidiary for purposes of undertaking an initial public offering of that subsidiary's common stock. In each such case, the subsidiary's total annual gross revenues for its most recently completed fiscal year are less than $1 billion, the subsidiary would not trigger any of the disqualification provisions in Sections 2(a)(19)(A)-(D) of the Securities Act, and the parent does not qualify as an

EGC because its first sale of common equity securities occurred on or before December 8, 2011. The Staff notes that the subsidiary would qualify as an EGC, based on an analysis which focuses on whether the issuer, and not its parent, meets the EGC requirements. The Staff notes that, based on the particular facts and circumstances, the EGC status of an issuer may be questioned if it appears that the issuer or its parent is engaging in a transaction for the purpose of converting a non-EGC into an EGC, or for the purpose of obtaining the benefits of EGC status indirectly when it is not entitled to do so directly. The Staff recommends that issuers with questions relating to these issues should contact the Division of Corporation Finance's Office of the Chief Counsel.

Status as an EGC is maintained until the earliest of: (i) the last day of the fiscal year in which the issuer's total annual gross revenues are $1 billion or more; (ii) the last day of the issuer's fiscal year following the fifth anniversary of the date of the first sale of common equity securities of the issuer pursuant to an effective registration statement under the Securities Act (for an debt-only issuer that never sold its common equity pursuant to an Exchange Act registration statement, this five-year period will not run); (iii) any date on which the issuer has, during the prior three-year period, issued more than $1 billion in non-convertible debt; or (iv) the date on which the issuer becomes a "Large Accelerated Filer," as defined in the SEC's rules. If an EGC loses its status, it cannot be regained by the issuer.

With regard to the $1 billion debt issuance test, the Staff indicated in its Frequently Asked Questions that the three-year period covers any rolling three-year period, which is not in any way limited to completed calendar or fiscal years. The Staff also noted that it reads "non-convertible debt" to mean any non-convertible security that constitutes indebtedness (whether issued in a registered offering or not), thereby excluding bank debt or credit facilities. The debt test references debt "issued," as opposed to "issued and outstanding," so that any debt issued to refinance existing indebtedness over the course of the three-year period could be counted multiple times. However, the Staff indicated in its May 3 Frequently Asked Questions that they will not object if an issuer does not double count the principal amount from a private placement and the principal amount from the related Exxon Capital exchange offer.

Scaled Disclosures for EGCs

Among other areas of scaled disclosure available to EGCs (including reduced financial statement requirements), an EGC may comply with the executive compensation disclosures applicable to a "smaller reporting company" as defined in the SEC's

rules, which means that an EGC need provide only a Summary Compensation Table (with three rather than five named executive officers and limited to two fiscal years of information), an Outstanding Equity Awards Table, and a Director Compensation Table, along with some narrative disclosures to augment those tables. EGCs are not required to provide a Compensation Discussion and Analysis, or disclosures about payments upon termination of employment or change in control.

Say-on-Pay and Other Relief for EGCs

Title I of the JOBS Act provides relief from a number of requirements for EGCs following an initial public offering. An EGC will not be subject to the Say-on-Pay, Say-on-Frequency or Say-on-Golden Parachute vote required by the Dodd-Frank Act, for as long as the issuer qualifies as an EGC. An issuer that was an EGC, but lost that status, will be required to comply with the Say-on-Pay vote requirement as follows: (i) in the case of an issuer that was an EGC for less than two years, by the end of the three-year period following its IPO, and (ii) for any other issuer, within one year of having lost its EGC status. An EGC also is not subject to any requirement to disclose the relationship between executive compensation and the financial performance of the company (should such requirement be adopted), or the requirement to disclose the CEO's pay relative to the median employee's pay. In a 2015 meeting between the Staff of the Division of Corporation Finance and the American Bar Association's Joint Committee on Employee Benefits, the Staff made clear its position that a former EGC's first Say-on-Frequency vote cannot be delayed to coincide with its first required Say-on-Pay vote. The disconnect between the timing of the two votes results from the fact that Section 102(a)(2) of Title I of the JOBS Act (codified as Section 14A(a)(2) of the Exchange Act), which exempts EGCs from the Say-on-Pay and Say-on-Frequency voting requirements, allows an issuer that loses its EGC status a transition period before having to comply with the Say-on-Pay requirement, but does not extend the same transition period for the Say-on-Frequency vote.

Other than the provisions for extended transition to new or revised accounting standards, an EGC may decide to follow only some of the scaled disclosure provisions and corporate governance relief available for EGCs.

THE SAY-ON-PAY EXPERIENCE

The implementation of Say-on-Pay votes was one of the most widely-anticipated corporate governance developments in the United States over the past five years.

Advocates for Say-on-Pay in the United States hoped that the advisory votes on executive compensation would serve to encourage greater accountability for executive compensation decisions, as well as more focused compensation disclosure in proxy statements and expanded shareholder engagement.

During the 2011 proxy season, approximately forty issuers failed to achieve majority shareholder support for mandatory Say-on-Pay resolutions. During the 2012 proxy season, approximately sixty issuers failed to achieve majority shareholder support for mandatory Say-on-Pay resolutions. During the 2013 proxy season, approximately seventy-three issuers failed to achieve majority stockholder support for mandatory Say-on-Pay resolutions. During the 2014 proxy season, approximately sixty-six issuers failed to achieve majority stockholder support for mandatory Say-on-Pay resolutions. During the 2015 proxy season, approximately sixty-four issuers failed to achieve majority stockholder support for mandatory Say-on-Pay resolutions. The high level of shareholder support for Say-on-Pay resolutions over the history of the mandatory Say-on-Pay vote is similar to the experience in the past with respect to those companies who held Say-on-Pay votes on a voluntary basis, or because the company was required to hold a Say-on-Pay vote because it had outstanding indebtedness under TARP. In the vast majority of those situations, shareholders have provided strong support for Say-on-Pay proposals, absent some significant concerns with the company's executive compensation programs. Even with the likelihood of shareholder support relatively high for Say-on-Pay resolutions, companies have paid very close attention to the message communicated through their CD&A and other disclosures, while at the same time seeking to engage with key shareholder constituencies.

Disclosure For Say-on-Pay

In many ways, the disclosure that is provided in the proxy statement remains the key point of engagement with shareholders on executive compensation issues. The Say-on-Pay vote caused many companies to streamline and clarify their CD&A disclosure to facilitate utilizing the CD&A to explain why shareholders should support the Say-on-Pay vote. In addition, issuers have sought to emphasize the overall "pay for performance" message in the CD&A and throughout the executive compensation disclosure in the proxy statement. To this end, many issuers began the CD&A with an "Executive Summary" or "Overview" section. The Executive Summary has proven to be an effective way of communicating the key executive compensation information

that shareholders need to make an informed decision on the Say-on-Pay votes. An effective Executive Summary should include:

- A brief description of the company's financial and business results for the last completed fiscal year, focusing in particular on measures of performance that are relevant to determining the compensation for the named executive officers, while complying with any applicable requirements with respect to the use of non-GAAP measures (see Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 108.01);
- A discussion of how the issuer's results have impacted executive compensation decisions in the last fiscal year;
- A list of important compensation actions during the last completed fiscal year, including the actions with respect to the CEO and the other named executive officers; and
- A discussion of significant compensation policies and practices implemented or revised, as well as any pre-existing governance and compensation-setting procedures, which demonstrate the issuer's "pay for performance" philosophy and commitment to compensation and corporate governance best practices.

Issuers have also been utilizing graphic presentations in the Executive Summary and in the rest of the CD&A as a means of effectively highlighting the issuer's business results and relating those results to the compensation decisions.

An overriding theme has been the relationship between pay and performance. As a result, the Executive Summary and the remainder of the CD&A often focused on how the compensation programs have aligned pay and performance, which necessitated fulsome disclosure about the performance target measures used to determine the level of performance, as well as more detailed disclosure concerning the individual achievements of the named executive officers when such performance is an element pursuant to which compensation is determined.

Disclosures also include more discussion of how the compensation committee considered the relationship between compensation programs and risks arising for the company in the course of making decisions and taking actions with respect to compensation. This area of focus will likely continue to drive more detailed disclosure in proxy statements about the relationship between compensation and risk.

Many companies addressed the adoption or revision of some key compensation policies, including stock ownership and equity holding policies, compensation recovery policies, policies limiting perquisites and other personal benefits and policies with respect to limiting severance and post-retirement benefits.

Recently, a number of companies have utilized alternative pay measures, such as "realized pay" and "realizable pay," as part of their overall disclosure approach to Say-on-Pay, either as part of the pay-for-performance discussion in the CD&A or in supplemental soliciting material responding to a negative Say-on-Pay recommendation from ISS or Glass Lewis. These alternative measures are used to compare pay to the company's performance, and to compare an executive officer's reported and/or target pay to the realized or realizable pay. While there is no uniform approach to these measures, formulations of "realized pay" typically include: (i) actual earned cash compensation (including salary and bonuses); (ii) actual payouts under performance share or performance cash awards; and (iii) the value of exercised or taxable equity awards, essentially including any equity awards that vested, were exercised or were otherwise earned during the relevant measurement period, and excluding those awards that remain outstanding and have not yet vested or have not been exercised, while "realizable pay" usually differs from "realized pay" by including the intrinsic value of all (or a portion of) equity awards that are outstanding at the end of the relevant period, regardless of whether the awards have been exercised (with respect to options or SARs) or paid or vested (with respect to restricted stock, RSUs and other full-value equity awards). For this purpose, the equity awards are valued using the company's stock price at the end of the fiscal year-end. Realizable pay is often compared directly to the total compensation reported in the Summary Company Table, and changes in realizable pay are compared to changes in total shareholder return and other issuer performance metrics over a specified long-term performance period, such as three years.

Say-on-Pay Engagement

Active engagement with shareholders on executive compensation and corporate governance issues is one of the expected results of a Say-on-Pay vote. Companies have explored a variety of approaches to accomplish effective engagement with shareholders.

Direct Interaction with Shareholders

Some issuers elected to conduct a "road show" focused on (or including as a component) executive compensation and corporate governance matters. These road shows typically took place in advance of the filing of the proxy statement (*e.g.*, 30-60 days before the proxy statement filing) and were conducted in person or via teleconference, typically involving both portfolio managers and voting analysts at institutional investors and senior level management, and in some cases, a director from the company. The road shows are largely designed to be informational, rather than serving to actively solicit any vote on expected proposals for the annual meeting, which could present solicitation issues under the SEC's proxy rules. Participants in these engagement activities usually address publicly-disclosed corporate governance and executive compensation initiatives demonstrating the company's responsiveness to shareholders, pay-for-performance considerations and the issuer's continuing attention to shareholder concerns (if any) on corporate governance and executive compensation issues. Participants typically avoid discussing material non-public information about the issuer's performance or plans for corporate governance and executive compensation program changes.

In the 2011 proxy season, a group of large institutional investors requested that some large companies hold a "fifth analyst call" to focus on executive compensation and corporate governance issues. The fifth analyst call would take place after a company mailed its proxy statement, but before the annual meeting. The institutional investor proposal for a fifth analyst call sought board member involvement in the call, such as the chairman of the board or the lead independent director. This fifth analyst call has not become a common practice.

The Use of Additional Soliciting Material

In a number of situations during the past three proxy seasons, Say-on-Pay voting led to the filing of additional soliciting material (filed as under the submission type "DEFA14A" on the SEC's EDGAR filing system) by issuers during the period of time between the mailing of the proxy statement and the annual meeting. In many of these situations, the additional soliciting material responded to an adverse Say-on-Pay recommendation made by a proxy adviser, either ISS or Glass, Lewis & Co. Issuers used the additional soliciting material to identify errors or flaws in the analysis underlying the proxy adviser's recommendation, while at the same time providing arguments as to why the Say-on-Pay proposal should be supported. The use of the

additional soliciting material, along with active engagement efforts, most often led to a successful Say-on-Pay vote.

Say-on-Frequency Recommendations and Voting

Most proxy statements filed in the 2011 proxy season with mandatory Say-on-Frequency votes included a recommendation as to the preferred frequency of future Say-on-Pay votes, with the majority of those recommendations favoring Say-on-Pay votes every year. In approximately half of those cases where issuers recommended a once every three years frequency, shareholders supported an annual Say-on-Pay vote, notwithstanding the once every three years recommendation. In the relatively few situations where the board recommended a Say-on-Pay vote once every two years, an annual frequency for Say-on-Pay voting was favored in approximately 65 percent of those cases. In the few circumstances where no recommendation from the board was provided, shareholders mostly supported an annual Say-on-Pay vote.

Proxy advisory firms ISS and Glass Lewis will only recommend voting for an annual Say-on-Pay vote frequency. Some institutional investors that do not follow ISS or Glass Lewis recommendations also adopted policies supporting annual Say-on-Pay votes. However, a few institutional investors adopted policies providing support for Say-on-Pay votes that occur once every three years. Given these circumstances, obtaining the plurality or majority support of shareholders for an “every three years” or an “every two years” Say-on-Pay voting interval became increasingly difficult as the 2011 proxy season unfolded.

Smaller reporting companies conducted Say-on-Frequency votes for the first time in 2013.

Considerations for the Frequency of the Say-on-Pay Vote

The following summarizes some of the key considerations for determining what Say-on-Pay voting frequency to recommend to shareholders.

A Vote of Once Every Year – Positive Considerations:

- A vote that occurs every year could make the Say-on-Pay vote less of a significant event from a shareholder’s perspective, which could make it more routine, similar to the ratification of auditors.
- With a Say-on-Pay vote occurring once every year, shareholders are able to express their views on an annual basis, which may mean that they will be

less concerned with the issuer's compensation policies, practices and decisions than if they were only able to vote once every two or three years.

- In 2010, ISS implemented a policy (commonly referred to as the "yellow card/red card approach") which provides that, for those issuers submitting a Say-on-Pay vote to shareholders, ISS will first recommend against the Say-on-Pay resolution if there is an issue with executive compensation, and then if the issue is not addressed by the next meeting, ISS will then recommend against the election of compensation committee members.
- ISS and Glass Lewis will only recommend for an annual Say-on-Pay vote frequency.
- Proxy advisers such as ISS, certain investors, and commentators view an annual vote on executive compensation as a good corporate governance practice and may therefore be less likely to target issuers that provide for an annual Say-on-Pay vote.

A Vote of Once Every Year – Negative Considerations:

- Certain institutional investors have sought a Say-on-Pay vote once every two or three years, in recognition of the fact that it is difficult for investors to deal with the volume of work necessary to make an informed decision on a Say-on-Pay vote.
- Engagement with institutional investors on compensation issues can be difficult to do on an annual basis, given that so many issuers seek to engage with institutional investors in advance of a Say-on-Pay vote.
- In the event that an issuer gets a negative vote, it typically must very quickly adjust its compensation policies and practices in order to have the changes take effect and be considered in advance of the next Say-on-Pay vote.

A Vote of Once Every Two or Three Years – Positive Considerations:

- A Say-on-Pay vote occurring once every two or three years allows proxy advisers and institutional investors more time to review and analyze the executive compensation program and practices between votes, so that those parties can better formulate their views on an issuer's executive compensation.
- The frequency of once every two or three years could potentially provide the issuer with more time to address compensation concerns through the

engagement process with shareholders and through changes to compensation policies and practices.

- A Say-on-Pay vote occurring once every two or three years allows institutional investors to better evaluate the effectiveness of long-term incentive components of compensation, given that the interval between votes more closely aligns with performance cycles and allows a more meaningful comparison between compensation and performance.
- A Say-on-Pay vote occurring once every two or three years allows an issuer the option to bring a Say-on-Pay vote on a more frequent basis if it wants to do so, because the vote on the frequency of voting is non-binding.

A Vote of Once Every Two or Three Years – Negative Considerations:

- A vote of once every two or three years may be portrayed negatively in the press, because it does not provide investors with an annual voice with respect to compensation issues and thereby may be seen as implying that an issuer is attempting to hide something from shareholders.
- A Say-on-Pay vote occurring once every two or three years is less likely to receive institutional investor support.
- ISS and Glass Lewis will only recommend for an annual Say-on-Pay vote frequency.
- A Say-on-Pay vote occurring once every two or three years could expose members of the compensation committee to recommendations against them in a year when no Say-on-Pay vote is on the ballot.
- A vote occurring every two or three years may be viewed by some proxy advisers, investors and commentators as a poor corporate governance practice because it does not provide investors with an annual voice on compensation issues.
- Voting on Say-on-Pay once every two or three years potentially makes the resolution appear to have more significance, because the resolution is not presented on a more frequent basis to shareholders, and there is more time for shareholders and proxy advisers to organize opposition to the issuer's Say-on-Pay vote.

Say-on-Golden Parachute Compensation Disclosure and Voting

A company seeking to avoid an advisory vote on golden parachute compensation in connection with a future vote on a merger or similar extraordinary transaction may voluntarily include the Item 402(t) tabular and narrative disclosures in the proxy statement for an annual meeting at which a Say-on-Pay vote will be held under the Dodd-Frank Act and the SEC's rules. However, if there are changes to the arrangements after the date of the vote or if new arrangements are entered into that were not subject to a prior Say-on-Pay vote, then a separate shareholder advisory vote on the golden parachute compensation is still required. In that case, the Say-on-Golden Parachute vote is required only with respect to the amended golden parachute payment arrangements. Other than changes that result only in a reduction in the amount of golden parachute compensation or that arise because of a change in the stock price, any other change to the golden parachute arrangements after the Say-on-Pay vote will trigger the requirement for a new vote.

A relatively small number of issuers have included the golden parachute compensation disclosure in annual meeting proxy statements where no vote was taking place with respect to a merger or similar transaction. It appears likely that issuers will avoid such "advance" votes on golden parachute compensation, given concerns about how the required disclosures concerning golden parachute compensation arrangements could impact the Say-on-Pay vote. In addition, issuers may be concerned that providing such disclosures may voluntarily signal to the market that the issuer could be engaged in a significant transaction in the near future.

Issuers have generally adhered closely to the requirements of the Golden Parachute Compensation Table in merger proxies, registration statements and other transactional forms filed since the rules became effective. In some cases, the new disclosure results in an additional page of disclosure in the applicable form or schedule, while in other cases the table and footnotes extend over several pages because of the complexity of various scenarios and triggering events. In addition, many issuers that have filed merger proxies or registration statements that require a shareholder advisory vote on golden parachutes have described the relationship of the golden parachute advisory vote to other votes on the transaction, including approval of the merger or other transaction itself. While issuers are required to disclose that the golden parachute vote is nonbinding, many have gone further to disclose whether or not the golden parachute vote is a condition of the transaction and whether the results of the advisory vote on golden parachutes would affect the consummation of the merger. Approval of the golden parachute arrangements is typi-

cally not a condition of the transaction, and a lack of approval of the golden parachutes will not affect consummation of the transaction.

Many issuers have included disclosure regarding the effect of the golden parachute advisory vote on the status of the golden parachute payments. This type of disclosure typically notes that the golden parachute arrangements are contractual obligations of the issuer, and that even though the issuer values the input of shareholders as to whether such arrangements are appropriate, the issuer would nonetheless be required contractually to make, and would make, such payments even if the arrangements are not approved by the shareholders in the advisory vote.

Say-on-Pay Lawsuits

The Say-on-Pay vote is nonbinding, and the Dodd-Frank Act expressly provides that such advisory vote may not be construed as (1) overruling a decision by an issuer or its board of directors; (2) creating or implying any change to the fiduciary duties of a company or its board of directors; (3) creating or implying any additional fiduciary duties for an issuer or its board of directors; or (4) restricting or limiting the ability of shareholders to make proposals for inclusion in proxy materials related to executive compensation. Nonetheless, a few years ago plaintiffs filed derivative actions in state courts against directors of companies (and in some cases their executive officers and compensation consultants) based on the outcome of a Say-on-Pay vote. These lawsuits typically alleged that directors breached their fiduciary duties of care and loyalty in one or more of the following ways: (i) directors diverted corporate assets to executive officers, putting the interests of the executive officers ahead of the interests of stockholders; (ii) issuers that disclosed "pay-for-performance" compensation policies did not adequately disclose or misrepresented that compensation was nonetheless paid to executive officers in contravention of such policies (*i.e.*, compensation was paid even if performance goals were not met or financial performance was otherwise poor); and (iii) directors are subject to corporate waste claims based on the overall size of executive compensation awards. Further, the lawsuits alleged that executive officers were unjustly enriched by pay increases, and that in some cases compensation consultants aided and abetted the directors in their breaches of fiduciary duty and/or breached the consulting agreement with the issuer. In the lawsuits, plaintiffs have alleged that the failed Say-on-Pay vote is probative evidence that the compensation programs are not in the best interests of stockholders and that directors should not be entitled to the protections of the "business judgment rule." In these cases, the plaintiffs sought, among other things, unspecified damages resulting from the executive compensation

plans, costs and attorneys' fees, as well as the implementation of internal controls to prevent excessive compensation in the future.

Proxy Statement Litigation

Issuers have historically been able to solicit proxies for their annual meetings without the threat of the type of shareholder litigation that usually accompanies the solicitation of votes for special meeting to approve a merger or acquisition. In past proxy seasons, plantiffs have filed lawsuits seeking to enjoin annual meetings based on alleged deficiencies in the proxy statement disclosures for proposals to approve increases in equity plan reserves or authorized shares, as well as advisory votes on executive compensation.

These types of lawsuits often alleged breaches of fiduciary duties by management and directors of issuers, as well as aiding and abetting by the issuer itself, based on purported disclosure deficiencies in the proxy statements seeking shareholder votes on an increase in the amount of shares reserved for an equity compensation plan, an increase in the authorized shares and/or advisory votes on executive compensation. These claims are not based on a failure to include disclosure required in the proxy statement by the SEC's rules, but are rather based on state law fiduciary duty concepts. Typically, the lawsuits alleged that, with respect to proposals to increase the size of an equity plan or to increase the number of authorized shares, the company has failed to adequately describe the reason for an increase in the amount of shares, as well as the projections considered and the potential dilution that may result. With regard to advisory votes on executive compensation, the plaintiffs alleged a failure to adequately describe the role and advice of compensation consultants, to provide additional disclosure regarding peer group compensation practices, and disclose the rationale for the mix of short-term and long-term compensation. The plaintiffs sought a tactical advantage by filing these lawsuits after the issuer mailed the definitive proxy statement and before the annual meeting, thus providing typically only about one month for a court to decide on the motion to enjoin the annual meeting. An issuer often first learn of these lawsuits when the plaintiffs' law firm issues a press release to announce a "pending investigation."

These lawsuits have typically been shareholder class actions that are filed in state courts where the subject issuer has sufficient contacts. These lawsuits were usually not filed in federal court or in Delaware (where many of the subject companies are incorporated), presumably because there is a higher likelihood that the disclosure-based claims would be dismissed in federal court or in the Delaware Chancery Court. The lawsuits usually did not allege that the subject issuers have failed to meet dis-

closure requirements established by the SEC with regard to the proposals included in the proxy statement; rather, the lawsuits alleged that the defendants (which typically include the members of the board of directors, senior management and the company) breached their fiduciary duties to shareholders by failing to adequately disclose information when seeking a vote on the proposals.

The complaints often alleged that the individual defendants, i.e., the members of the board of directors and senior management, have breached fiduciary duties of care, loyalty, candor and good faith owed to public shareholders, and have acted to put their own personal interests ahead of the interests of shareholders. These individual defendants were alleged to have failed to disclose all material information necessary to make an informed decision regarding the advisory vote on executive compensation or an increase in shares proposal. As a result of these actions, it was alleged that the individual defendants have failed to exercise ordinary care and diligence in the exercise of their fiduciary duties. The issuer was alleged to have knowingly aided and abetted the disclosure deficiencies and therefore the breaches of fiduciary duty.

In the complaints, plaintiffs sought: (i) a declaration that the proxy statement was issued in breach of the fiduciary duties of the individual defendants and is therefore unlawful, and that the company aided and abetted the issuance of the materially misleading and incomplete proxy statement; (ii) an injunction from consummating the vote on the subject proposals until the company provides adequate disclosure regarding the proposals; (iii) an award of damages, attorneys' and experts fees and other costs, and (iv) any other further relief that the court deems appropriate.

The claims of inadequate disclosure in these lawsuits focused on information that the plaintiffs' deemed to be important details relevant to the advisory vote on executive compensation, the vote to increase the share reserve for the equity compensation plan or the vote to increase the number of authorized shares. These claims were not based on a failure to meet SEC-established requirements or applicable case law-established standards for disclosure.

The allegations in the lawsuits focused on a number of areas where the disclosure that is related to the advisory vote on executive compensation was alleged to be deficient, including:

- The disclosure does not include a fair summary of the advice, counsel and analysis performed and provided to the board of directors and/or management by a compensation consultant;

- The disclosure does not address how the board of directors or the compensation committee selected outside advisors and how much was paid to the outside advisors in connection with their engagement;
- The discussion of the peer group utilized in analyzing executive compensation does not include detailed disclosure of the data with respect to salary, short-term and long-term incentives and total direct compensation for each of the companies in the peer group;
- The disclosure does not adequately address the rationale for the mix of long-term and short-term compensation;
- The role of management in the compensation-setting process is not adequately addressed; and
- Changes in various things in the current year are not adequately addressed in terms of the rationale for the change, such as changes to the peer group or an increase in compensation.

It is possible that plaintiffs would raise any number of additional disclosure deficiencies in future lawsuits, based on the success of other claims and the individual circumstances of the proxy statements that are the subject of the claims.

Further, the allegations in the lawsuits focused on a number of areas where the disclosure related to an increase in the shares reserved for an equity compensation plan or an increase the amount of common stock authorized was alleged to be deficient, including:

- A failure to disclose the number of shares currently expected to be paid out in the year under the company's equity compensation plan, or any other projections considered by the board of directors;
- The disclosure does not describe the criteria considered by the board of directors to implement the proposal, and why the proposal would be in the best interests of the shareholders;
- The disclosure does not describe why the current share reserve is inadequate;
- The disclosure does not describe how the board of directors determined the number of additional shares requested to be authorized;

- The disclosure does not identify the potential equity value and/or the cost of issuance of the additional authorized shares;
- A failure to disclose the dilutive impact of issuing additional shares under the equity plan on existing shareholders, and any share repurchases that might be planned;
- The disclosure does not identify the expected use for the shares and how long the company expects the increased share reserve to last;
- The proxy statement does not include a fair summary of any expert's analysis or opinion obtained in connection with the proposal; and
- A lack of specificity in describing the performance goals.

It is possible that plaintiffs will raise any number of additional disclosure deficiencies in future lawsuits, based on the success of other claims and the individual circumstances of the proxy statements that are the subject of the claims.

It is difficult to determine the likelihood of the commencement of this type of litigation when an issuer files its proxy statement, however it appears that the frequency of these types of lawsuits has recently declined.

One approach to anticipating these types of lawsuits would be to include enhanced disclosure in the proxy statement as filed which fully addresses the information identified above. The addition of this disclosure would not in any way ensure that a lawsuit would not be filed, however, because the plaintiffs could identify any number of areas in which to allege that the disclosure is deficient, even if the disclosure is indeed not deficient under the standards of the SEC requirements and general principles of materiality.

Some issuers, upon learning of the pending investigation by a plaintiffs' law firm, have appeared to file supplemental proxy soliciting materials which provide the information sought in the similar lawsuits. It is possible that this disclosure would thereby prevent the plaintiffs from filing a complaint, because their claims have been rendered moot by the supplemental disclosure.

A third option would be to anticipate the possibility of the lawsuit and to be prepared to enter into settlement discussions quickly, which would likely result in the release of additional proxy soliciting material, the payment of costs and the potential for a delay in the vote on the subject proposal or proposals.

The fourth option would be to defend the lawsuit, seeking to have the court dismiss the claims prior to the issuer's annual meeting. Depending on the court system in which the issuer would be sued, this strategy could potentially lead to a delay in the annual meeting or at least a delay in the vote on the proposals as the litigation proceeds, and there is no certainty as to whether the outcome of the litigation would ultimately be favorable to the issuer.

Annotated Model Say-on-Pay and Say-on-Frequency Proposals

Annotated Model Say-on-Pay Proposal

PROPOSAL [ ] – ADVISORY VOTE ON EXECUTIVE COMPENSATION

The Dodd-Frank Wall Street Reform and Consumer Protection Act added Section 14A to the Securities Exchange Act of 1934, which requires that we provide our shareholders with the opportunity to vote to approve, on a nonbinding, advisory basis, the compensation of our named executives officers as disclosed in this proxy statement in accordance with the compensation disclosure rules of the Securities and Exchange Commission.

As described in greater detail under the heading "*Compensation Discussion and Analysis,*" we seek to closely align the interests of our named executive officers with the interests of our shareholders. [Our compensation programs are designed to reward our named executive officers for the achievement of short-term and long-term strategic and operational goals and the achievement of increased total shareholder return, while at the same time avoiding the encouragement of unnecessary or excessive risk-taking.] [*This statement should be adapted as appropriate for the issuer. In this regard, a brief statement of the issuer's philosophy with respect to executive compensation is useful in this context. Moreover, smaller reporting companies may not have a "Compensation Discussion and Analysis" section to refer to, so they may want to reference where other relevant disclosures are provided.*]

[The proposal may include a brief discussion of important compensation actions and decisions in the last completed fiscal year. In this regard, the disclosure in the proposal can provide a high-level overview of the reasons why shareholders should vote for the issuer's executive compensation. The summary included in the proposal itself can work in conjunction with the "Executive Summary" or "Overview." In some instances, issuers choose to only cross-reference the CD&A disclosure without including a statement in support of the Say-on-Pay resolution in the proposal.]

This vote is advisory, which means that the vote on executive compensation is not binding on the Company, our Board of Directors or the Compensation Committee of the Board of Directors. The vote on this resolution is not intended to address any specific element of compensation, but rather relates to the overall compensation of our named executive officers, as described in this proxy statement in accordance with the compensation disclosure rules of the Securities and Exchange Commission. [To the extent there is a significant vote against our named executive officer compensation as disclosed in this proxy statement, the Compensation Committee will evaluate whether any actions are necessary to address our shareholders' concerns.] [*The SEC's rules do not require that an issuer address what actions it will undertake in response to the Say-on-Pay vote (by contrast to the disclosure required with respect to ratification of auditors), rather requiring a discussion in subsequent CD&A disclosure of whether and, if so, how the issuer has considered the results of the most recent shareholder advisory vote on executive compensation in determining compensation policies and decisions and, if so, how that consideration has affected the issuer's compensation decisions and policies. It may, nevertheless, be useful at the time of presenting the proposal to explain how the vote will be considered as a means of clarifying the advisory nature of the vote.]*

[The affirmative vote of a majority of the shares present or represented and entitled to vote either in person or by proxy is required to approve this Proposal [ ]]. [*Issuers will have to evaluate what is the most appropriate voting standard for a Say-on-Pay proposal. Issuers should also consider describing, in this section or in the front portion of the proxy statement, the effect of abstentions and broker non-votes on the vote.*]

Accordingly, we ask our shareholders to vote on the following resolution at the Annual Meeting:

[The following is the form of resolution that the SEC includes in the Instruction to Exchange Act Rule 14a-21(a). Smaller reporting companies will need to revise the form of resolution if they elect to not provide CD&A disclosure under the scaled disclosure requirements.]

> "RESOLVED, that the compensation paid to the company's named executive officers, as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis, compensation tables and narrative discussion, is hereby APPROVED."

[The following is an alternative form of the resolution. In Exchange Act Rules Compliance and Disclosure Interpretations Question 169.05, the SEC Staff has indicated that it is permissible for the Say-on-Pay vote to omit the words, "pursuant to Item 402 of Regulation S-K," and to replace those words with a plain English equivalent, such as, "pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the compensation discussion and analysis, the compensation tables and any related material disclosed in this proxy statement." This alternative formulation also makes clear in the language of the resolution itself that the vote is advisory. Smaller reporting companies will need to revise the form of resolution if they elect to not provide CD&A disclosure under the scaled disclosure requirements.]

> "RESOLVED, that the Company's shareholders approve, on an advisory basis, the compensation of the named executive officers, as disclosed in the Company's Proxy Statement for the 2011 Annual Meeting of Shareholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the Compensation Discussion and Analysis, the Summary Compensation Table and the other related tables and disclosure."

We have determined that our shareholders should cast an advisory vote on the compensation of our named executive officers on an [annual] basis. Unless this policy changes, the next advisory vote on the compensation of our named executive officers will be at the [ ] annual meeting of shareholders.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS A VOTE *FOR* THE APPROVAL OF THE COMPENSATION OF OUR NAMED EXECUTIVE OFFICERS, AS DISCLOSED IN THIS PROXY STATEMENT.

Annotated Model Say-on-Frequency Proposal

PROPOSAL [ ] – ADVISORY VOTE ON THE FREQUENCY OF AN ADVISORY VOTE ON EXECUTIVE COMPENSATION

The Dodd-Frank Wall Street Reform and Consumer Protection Act added Section 14A to the Securities Exchange Act of 1934, which requires that we provide shareholders with the opportunity to vote, on a non-binding, advisory basis, for their preference as to how frequently to vote on future advisory votes on the compensation of our named executive officers as disclosed in accordance with the compensation disclosure rules of the Securities and Exchange Commission.

Shareholders may indicate whether they would prefer that we conduct future advisory votes on executive compensation once every one, two, or three years. Shareholders also may abstain from casting a vote on this proposal.

[The following language should be adjusted to reflect the board of directors' determination as to the recommended frequency of every year, every two years or every three years. Neither Rule 14a-21(b) nor the SEC's other proxy rules require that an issuer make a recommendation with respect to the Say-on-Frequency vote; however, the SEC notes that proxy holders may vote uninstructed proxy cards in accordance with management's recommendation only if the issuer follows the existing requirements of Rule 14a-4, which include specifying how proxies will be voted (*i.e.*, in accordance with management's recommendations) in the absence of instruction from the shareholder. Most proxy statements filed in the 2011 proxy season with mandatory Say-on-Frequency votes have included a recommendation as to the preferred frequency of future Say-on-Pay votes, with the majority of those recommendations favoring Say-on-Pay votes once every three years.]

[The Board of Directors has determined that an advisory vote on executive compensation that occurs once [every three years][every two years] is the most appropriate alternative for the Company and therefore the Board recommends that you vote for a [three-year interval][two-year interval] for the advisory vote on executive compensation. In determining to recommend that shareholders vote for a frequency of once [every three years][every two years], the Board considered how an advisory vote at this frequency will provide our shareholders with sufficient time to evaluate the effectiveness of our overall compensation philosophy, policies and practices in the context of our long-term business results for the corresponding period, while avoiding overemphasis on short-term variations in compensation and business results. An advisory vote occurring once [every three years][every two years] will also permit our shareholders to observe and evaluate the impact of any changes to our executive compensation policies and practices which have occurred since the last advisory vote on executive compensation, including changes made in response to the outcome of a prior advisory vote on executive compensation.]

[The Board of Directors has determined that an annual advisory vote on executive compensation will permit our shareholders to provide direct input on the Company's executive compensation philosophy, policies and practices as disclosed in the proxy statement each year, which is consistent with our efforts to engage in an ongoing dia-

logue with our shareholders on executive compensation and corporate governance matters.]

This vote is advisory, which means that the vote on executive compensation is not binding on the Company, our Board of Directors or the Compensation Committee of the Board of Directors. The Company recognizes that the shareholders may have different views as to the best approach for the Company, and therefore we look forward to hearing from our shareholders as to their preferences on the frequency of an advisory vote on executive compensation. [*This statement is not required by the SEC's rules; however, it may be advisable to include this statement in order to clarify that the board of directors is open to considering the preferences expressed by shareholders through the vote, without necessarily committing to adopt the frequency most favored by the shareholders.*] [The Board of Directors and the Compensation Committee will take into account the outcome of the vote; however, when considering the frequency of future advisory votes on executive compensation, the Board of Directors may decide that it is in the best interests of our shareholders and the Company to hold an advisory vote on executive compensation more or less frequently than the frequency receiving the most votes cast by our shareholders.] [*The SEC's rules do not require an issuer to address in the proxy statement what actions it will undertake in response to the Say-on-Frequency vote, however, it may be useful to include this information as a means for describing the advisory nature of the vote. Moreover, issuers will have to evaluate what is the most appropriate voting standard for interpreting the Say-on-Frequency vote. In this regard, it should be noted that the SEC has added a new Note to Exchange Act Rule 14a-8(i)(10) to permit the exclusion of a shareholder proposal as "substantially implemented" if the proposal would provide for a Say-on-Pay vote, seek future Say-on-Pay votes, or relate to the frequency of Say-on-Pay votes. Such shareholder proposals may be excluded under the new Note if, in the most recent Say-on-Frequency vote, a single frequency received a majority of the votes cast and the issuer adopted a policy for the frequency of Say-on-Pay votes that is consistent with that choice. This does not mean that an issuer could not utilize a different voting standard for determining the preference of the shareholders, such as plurality (i.e., the frequency receiving the most votes cast by the shareholders)*.]

[The following is an example of a resolution for the Say-on-Frequency vote. The Staff indicates in Compliance and Disclosure Interpretations Question 169.06 that it is permissible for the Say-on-Frequency vote to include the words "every year, every other year, or every three years, or abstain" in lieu of "every 1, 2, or 3 years, or abstain."]

Shareholders may cast a vote on the preferred voting frequency by selecting the option of one year, two years, or three years (or abstain) when voting in response to the resolution set forth below.

"RESOLVED, that the shareholders determine, on an advisory basis, whether the preferred frequency of an advisory vote on the executive compensation of the Company's named executive officers as set forth in the Company's proxy statement should be every year, every two years, or every three years."

[The following is an example of proposal language that does not include a resolution for the Say-on-Frequency vote. Exchange Act Rules Compliance and Disclosure Interpretations Question 169.04 indicates that the Say-on-Frequency vote need not be set forth as a resolution. Separately, the Staff has informally cautioned that the Say-on-Frequency vote must be clearly stated, and that in this regard it must be clear that shareholders can vote on the options of every one, two or three years (or abstain from voting), rather than solely following management's recommendation (if any is provided). It is likely that issuers will rely on this guidance to provide more Say-on-Frequency votes in a "proposal" format, such as by simply referencing the four choices that are available on the proxy card.]

The proxy card provides shareholders with the opportunity to choose among four options (holding the vote every one, two or three years, or abstain from voting) and, therefore, shareholders will not be voting to approve or disapprove the recommendation of the Board of Directors.

THE BOARD OF DIRECTORS RECOMMENDS THAT YOU VOTE *FOR* THE OPTION OF [ONCE EVERY THREE YEARS][ONCE EVERY TWO YEARS][ONCE EVERY YEAR] AS THE PREFERRED FREQUENCY FOR ADVISORY VOTES ON EXECUTIVE COMPENSATION.

Model Say-On-Pay and Say-On-Frequency Board Resolutions

Resolutions for the Annual Meeting

The following model resolutions can be utilized in preparing resolutions for the annual meeting:

Advisory Vote on Executive Compensation

WHEREAS, the Securities and Exchange Act of 1934, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"),

requires that the Corporation submit a resolution for its stockholders to approve, on an advisory basis, the compensation of the Corporation's "named executive officers" (as such term is defined in the applicable SEC rules), as disclosed in the Corporation's proxy statement under the SEC's rules, at least once every three years;

WHEREAS, in accordance with the Dodd-Frank Act, the vote to approve the compensation of the Corporation's named executive officers as disclosed in the proxy statement under the SEC's rules shall not be construed: (i) as overruling any decision by the Corporation or the Board; (ii) to create or imply any change in the fiduciary duties of the Corporation or the Board; (iii) to create or imply any additional fiduciary duties for the Corporation or the Board; and (iv) to restrict or limit the ability of the Corporation's stockholders to make proposals for inclusion in the Corporation's proxy statement relating to executive compensation except as may be provided under applicable SEC rules;

WHEREAS, the Board has determined that it is in the best interests of the stockholders of the Corporation to submit a resolution for its stockholders to approve, on an advisory basis, the compensation of the Corporation's named executive officers as disclosed in the proxy statement under the SEC's rules at least once every three years; and

WHEREAS, the Board has determined that it is in the best interests of the stockholders of the Corporation for the Board to recommend that the stockholders of the Corporation vote, on an advisory basis, "For" the compensation of the Corporation's named executive officers as disclosed in the proxy statement under the SEC's rules at least once every three years;

NOW, THEREFORE, BE IT RESOLVED, that the Corporation's stockholders shall vote on a resolution to approve, on an advisory basis, the compensation of the Corporation's named executive officers as disclosed in accordance with the SEC's rules in the proxy statement for the Annual Meeting of Stockholders; and

RESOLVED FURTHER, that the Board unanimously recommends that the Corporation's stockholders approve, on an advisory basis, the compensation of the Corporation's named executive officers as disclosed in accordance with the SEC's rules in the proxy statement for the Annual Meeting of Stockholders.

Frequency of the Advisory Vote on Executive Compensation

WHEREAS, the Dodd-Frank Act requires that the Corporation submit a resolution at least once every six years for its stockholders to determine, on an advisory

basis, the frequency with which the Corporation's stockholders approve, on an advisory basis, the compensation of the Corporation's named executive officers as disclosed in the Corporation's proxy statement under the SEC's rules;

WHEREAS, in accordance with the Dodd-Frank Act, the vote on the frequency of the advisory vote on the compensation of the Corporation's named executive officers as disclosed in the proxy statement under the SEC's rules shall not be construed: (i) as overruling any decision by the Corporation or the Board; (ii) to create or imply any change in the fiduciary duties of the Corporation or the Board; (iii) to create or imply any additional fiduciary duties for the Corporation or the Board; and (iv) to restrict or limit the ability of the Corporation's stockholders to make proposals for inclusion in the Corporation's proxy statement relating to executive compensation except as may be provided under applicable SEC rules; and

[WHEREAS, the Board believes that an annual advisory vote on executive compensation will allow the Corporation's stockholders to provide the Corporation with their direct input on the Corporation's compensation philosophy, policies and practices as disclosed in the Corporation's proxy statement every year and that an annual advisory vote on executive compensation is consistent with the Corporation's general policy of seeking input from, and engaging in discussions with, the Corporation's stockholders on corporate governance matters and the Corporation's executive compensation philosophy, policies and practices;]

[WHEREAS, the Board believes that an advisory vote on executive compensation that occurs once [every three years][every two years] will provide stockholders with sufficient time to evaluate the effectiveness of the Corporation's overall compensation philosophy, policies and practices in the context of long-term business results for the corresponding period, while avoiding over-emphasis on short-term variations in compensation and business results; and that an advisory vote occurring once [every three years][every two years] will also permit the Corporation's stockholders to observe and evaluate the impact of any changes to the Corporation's executive compensation policies and practices which have occurred since the last advisory vote on executive compensation, including changes made in response to the outcome of a prior advisory vote on executive compensation;]

NOW, THEREFORE, BE IT RESOLVED, that a proposal as to whether to hold an advisory vote on executive compensation once every year, once every two years, or once every three years shall be included in the proxy statement and submitted to the

stockholders of the Corporation for a vote at the Corporation's Annual Meeting of Stockholders; and

RESOLVED FURTHER, that the Board unanimously recommends that the stockholders of the Corporation vote to approve, on an advisory basis, a frequency for holding an advisory vote on executive compensation of [once every year] [once every two years] [once every three years] until the next advisory vote on the frequency of holding an advisory vote on executive compensation.

General Authority

RESOLVED, that any and all actions heretofore taken by the officers and directors of the Corporation, or any one or more of them, within the terms of the foregoing resolutions are hereby approved, adopted, ratified and confirmed in all respects and declared to be the valid and binding acts and deeds of the Corporation; and

RESOLVED FURTHER, that the officers of the Corporation are, and each of them is, hereby authorized, directed and empowered in the name and on behalf of the Corporation to take such further action, and to execute, acknowledge, certify, file, deliver and record such documents, instruments, agreements, consents and certificates, as they or any of them in their discretion deem necessary or appropriate, to carry out the purposes and intent of the foregoing resolutions, and that the execution by such officers of any such documents, instruments, agreements, consents and certificates or the doing by them of any act in connection with the foregoing matters shall conclusively establish their authority therefor from this Corporation and the approval and ratification by this Corporation of the documents, instruments, agreements, consents and certificates so executed and the actions so taken.

Resolutions for after the Annual Meeting

The following model resolutions can be utilized in preparing resolutions for the determination of the frequency of the Say-on-Pay vote following the annual meeting:

Approval of Frequency of Say-on-Pay Votes

WHEREAS, at the recently completed Annual Meeting of Stockholders of the Corporation, it was determined that, with respect to the resolution on the frequency of holding an advisory vote on executive compensation, the option of once every [one year][two years][three years] [received the highest number of votes cast by the stockholders] and, accordingly, such frequency is the preferred frequency with which

the Corporation is to hold a stockholder vote, on an advisory basis, to approve the compensation of the named executive officers, as disclosed pursuant to the Securities and Exchange Commission's compensation disclosure rules (which disclosure shall include the Summary Compensation Table and the other related tables and disclosure); and

[WHEREAS, the Board believes that an annual advisory vote on executive compensation will allow the Corporation's stockholders to provide the Corporation with their direct input on the Corporation's compensation philosophy, policies and practices as disclosed in the Corporation's proxy statement every year and that an annual advisory vote on executive compensation is consistent with the Corporation's general policy of seeking input from, and engaging in discussions with, the Corporation's stockholders on corporate governance matters and the Corporation's executive compensation philosophy, policies and practices;]

[WHEREAS, the Board believes that an advisory vote on executive compensation that occurs once [every three years][every two years] will provide stockholders with sufficient time to evaluate the effectiveness of the Corporation's overall compensation philosophy, policies and practices in the context of long-term business results for the corresponding period, while avoiding over-emphasis on short-term variations in compensation and business results; and that an advisory vote occurring once [every three years][every two years] will also permit the Corporation's stockholders to observe and evaluate the impact of any changes to the Corporation's executive compensation policies and practices which have occurred since the last advisory vote on executive compensation, including changes made in response to the outcome of a prior advisory vote on executive compensation;]

NOW, THEREFORE, BE IT RESOLVED, that the Board hereby determines that, in light of the preferred frequency determined by the Corporation's stockholders at the Annual Meeting of Stockholders, the Corporation shall include an advisory vote of the stockholders on executive compensation in the Corporation's proxy materials once every [year][two years][three years] until the next required vote on the frequency of stockholder votes on the compensation of executives of the Corporation; and

RESOLVED FURTHER, that the officers of the Corporation are, and each of them is, hereby authorized, directed and empowered in the name and on behalf of the Corporation to implement the foregoing policy of the Corporation.

General Authority

RESOLVED, that any and all actions heretofore taken by the officers and directors of the Corporation, or any one or more of them, within the terms of the foregoing resolutions are hereby approved, adopted, ratified and confirmed in all respects and declared to be the valid and binding acts and deeds of the Corporation; and

RESOLVED FURTHER, that the officers of the Corporation are, and each of them is, hereby authorized, directed and empowered in the name and on behalf of the Corporation to take such further action, and to execute, acknowledge, certify, file, deliver and record such documents, instruments, agreements, consents and certificates, as they or any of them in their discretion deem necessary or appropriate, to carry out the purposes and intent of the foregoing resolutions, and that the execution by such officers of any such documents, instruments, agreements, consents and certificates or the doing by them of any act in connection with the foregoing matters shall conclusively establish their authority therefor from this Corporation and the approval and ratification by this Corporation of the documents, instruments, agreements, consents and certificates so executed and the actions so taken.

CHAPTER 3

KEY DISCLOSURE CONSIDERATIONS FOR PROXY STATEMENTS AND ANNUAL REPORTS

KEY DISCLOSURE CONSIDERATIONS FOR PROXY STATEMENTS AND ANNUAL REPORTS

SEC REVIEW PROCESS

The Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") requires the SEC to review the Form 10-K of every public issuer at least once every three years. Beginning January 1, 2012, the SEC has released filing review correspondence no earlier than 20 business days following the completion of a filing review. As a result of the public availability of these letters, the Staff has come to expect that issuers are aware of the interpretive positions taken by the SEC in their comment letters, which often reflect nuanced readings of the rules or require more detailed disclosure than might otherwise be expected. It has become increasingly important that issuers make themselves familiar with Staff comment letters that have been issued to other issuers, so that they can respond to the issues raised in those letters when preparing their own filings. The SEC Staff has also noted that issuers should be cognizant of the information provided in response to comments from the Staff, given that the public release of those responses makes the responses a part of the issuer's public disclosures.

In the past, the Staff of the Division of Corporation Finance has often limited its review to financial statements and related disclosure. However, recently the Staff has been conducting more complete legal reviews of periodic reports. In addition, review of executive compensation disclosures has been integrated into the Form 10-K and proxy statement review process, and comment letters often include at least one to two comments on executive compensation. Below is an analysis of recent frequent areas of Staff comment in Form 10-Ks and proxy statements. Attention to these areas during the drafting process can save time and effort later, when the filings become subject to Staff review.

SEC COMMENTS ON EXECUTIVE COMPENSATION DISCLOSURE

Over the past several years, the SEC has provided significant guidance with respect to its interpretation of executive compensation disclosure rules, including numerous Staff speeches, new and revised Compliance and Disclosure Interpretations, its "Staff Observations in the Review of Executive Compensation" (which was released in October 2007 following a review of the disclosure of 350 issuers), and Staff comments on individual filings. Historically, the Staff has addressed executive compensation disclosure deficiencies identified in the review process by issuing "futures" comments, which require an issuer to address any identified deficiencies in

future filings. However, that approach has begun to change. In a November 2009 speech, Shelley Parratt, Deputy Director of the Division of Corporation Finance, stated:

> "[A]fter three years of futures comments, we expect companies and their advisors to understand our rules and apply them thoroughly. So, any company that waits until it receives Staff comments to comply with the disclosure requirements should be prepared to amend its filings if it does not materially comply with the rules."

Under the Staff's new approach, it has become increasingly likely that the SEC will require that issuers amend disclosure if it believes that the issuer has not appropriately followed outstanding Staff guidance. Issuers should attempt to address in their disclosure the issues that are most often raised by the Staff during the review process.

In her November 2009 speech, Ms. Parratt urged issuers to focus on several key areas of executive compensation disclosure, as well as consider the comments, reports and speeches on CD&A provided by the Staff over the years. In particular, Ms. Parratt provided the following recommendations for preparing 2010 proxy statement disclosures:

- Explain *why* compensation decisions were made in the context of addressing the decision-making processes;
- Disclose any material performance targets used in determining executive compensation for the named executive officers for the periods covered by the disclosure, as well as the actual achievement level against the targets;
- In the event of Staff review, be prepared to explain how disclosure of material performance targets would cause competitive harm when that is the basis for omitting the performance target disclosure;
- Provide meaningful disclosure regarding the degree of difficulty in achieving performance targets when those targets are omitted;
- Disclose the names of any peer group companies used for benchmarking purposes, how those companies were selected, and how the actual awards compared to the benchmarks; and
- In addition to addressing the examples provided in Item 402(b) of Regulation S-K, provide additional disclosure in the CD&A that would be material to an understanding of an issuer's compensation policies or decisions.

Trends in Executive Compensation Comments

There are a number of significant areas of focus in Staff comments and other interpretive guidance on executive compensation disclosure. For example, the Staff has repeatedly stated that an issuer's CD&A should focus on *how* and *why* the issuer arrived at specific executive compensation decisions and policies and should address why specific compensation decisions were made. Issuers frequently receive comments on this issue during the review process. Other principal areas of SEC comment in the CD&A have related to the disclosure of incentive plan performance targets, individual performance goals and benchmarking practices or processes.

Meaningful Analysis in the Compensation Discussion & Analysis

The Staff has repeatedly requested that issuers provide more detailed, meaningful analysis in the CD&A. Issuers should discuss both *how* and *why* they arrived at specific compensation decisions. In addition to identifying what the goals of the compensation program are, issuers should also identify the reasons for individual awards to named executive officers, as well as how those awards fit into the issuer's overall compensation objectives. The Staff expects issuers to provide detailed, specific analysis.

The Staff generally views as insufficient any discussion of award decisions that addresses all named executive officers as a group and does not address each named executive officer's individual circumstances. In addition, as part of the analysis of the reasons for each element of compensation (e.g., base salary, cash incentive award or equity award) for each named executive officer, the Staff expects a discussion of why the compensation committee decided to award specific amounts or make changes in an element of compensation from period to period. For example, this discussion should include the reasons the compensation for a named executive officer increased or decreased as compared to prior periods, as well as how the compensation committee arrived at its decision.

Disclosure of Performance Targets

Another focus of Staff comments on CD&A is on the disclosure of performance targets as they relate to executive compensation. Issuers are required to disclose any specific items of corporate performance that are taken into account in setting compensation policies and making compensation decisions. In addition to disclosing any material performance targets, issuers are expected to disclose the extent to which those performance targets were achieved. However, they are not required to disclose any

performance targets that are not material or that would cause competitive harm to the issuer (applying the same competitive harm standard that is applied to confidential treatment requests).

Some issuers have chosen not to disclose performance targets in reliance on the argument that this disclosure would cause competitive harm to the issuer. However, the Staff has focused significant attention on the competitive harm argument in its comments and has limited the extent to which issuers may rely on it. The Staff has repeatedly required issuers to justify their use of the standard, sometimes going beyond the standards generally applied to confidential treatment requests. Issuers have been asked to specifically identify the nature of the competitive harm that they would suffer if the performance targets were to be disclosed, including how the issuer's competitors would actually use the information. If the Staff accepts the competitive harm argument, performance targets are not disclosed based on the competitive harm exception, then the issuer must disclose the level of difficulty associated with achieving the undisclosed goal.

The Staff is more likely to accept that disclosure of a performance target would cause competitive harm in the context of non-financial operational performance targets or performance goals related to specific business units. The Staff will generally not accept the argument that the disclosure of financial information or financial targets for a completed fiscal year will cause competitive harm. If the performance target relates to a completed fiscal year, the Staff position is that, because the issuer's financial results have already been publicly disclosed, no competitive harm should arise from the disclosure in the CD&A of the financial performance target and the extent to which it was met. However, the Staff generally does not require disclosure of financial performance targets for the current or a future period, if the issuer is able to argue that those current or future period targets are not material to an understanding of compensation policies and decisions with respect to the fiscal year being discussed in the CD&A.

If issuers use non-GAAP performance targets, the Staff requires that the non-GAAP performance targets be disclosed in the CD&A, together with an explanation of how it is calculated. However, a full-scale reconciliation to GAAP is not required.

Individual Performance Goals

Staff comments on CD&A have also focused on disclosure of individual performance goals for named executive officers. Issuers often provide general disclosure that

states that some percentage or component of executive compensation is based on achievement of individual performance goals. However, the Staff raises a concern if sufficient disclosure of how the level of individual achievement affects the actual compensation received by the executive, or why the compensation committee adopted the performance goal and how achievement is measured.

The Staff has repeatedly requested that issuers provide more specific disclosure in this area. Issuers must identify the extent to which achievement of individual performance goals impacts compensation for each named executive officer. If individual performance goals were a material factor in determining compensation, issuers must disclose the specific performance goals and achievements, even if the performance targets are subjective and not quantifiable. Disclosure of specific performance targets may not be required if the performance target was not a material factor in determining compensation, for example if it was just one factor among many taken into account by the compensation committee. However, formulaic, objective or quantifiable performance targets should generally be disclosed in the Staff's view.

The Staff has also requested that issuers provide additional disclosure when the compensation committee has approved compensation in excess of or less than what is provided for in the issuer's compensation plans, or when the overall amount to which the executive is entitled under the program has been increased or decreased as a result of the executive's individual performance. In those situations, issuers have been asked to disclose the activities or individual performance standards that were applied in making that decision, as well as how the compensation committee considered those standards when making its decision.

Benchmarking

The use of benchmarking in the CD&A is another area of Staff focus throughout the comment process. It is important to note that many issuers use the term "benchmarking" in their CD&As when they are not in fact benchmarking as that term is understood by the SEC. For purposes of the CD&A, benchmarking refers to the tying of specific elements of compensation to a benchmark, as opposed to, for example, simply using comparable company data as a market check after arriving at compensation decisions based on some other method. As another example, a company is benchmarking when it ties base salaries to a certain targeted range (for example, the median level) within a set of peer companies. Issuers that do not engage in benchmarking should modify their disclosure in the CD&A to clarify how they use comparative issuer information.

For issuers that do engage in benchmarking, the Staff has consistently requested that all of the companies comprising the peer group or survey be listed and that the issuer describe the methodology it uses for assessing and utilizing the information. The issuer must also identify where its compensation plan falls within the targeted parameters. If its compensation falls outside of the targeted range, the issuer is asked to provide an explanation of the change.

Comments and Interpretations on Corporate Governance Disclosure

Background

On December 16, 2009, the SEC adopted, in SEC Release No. 33-9089 (December 16, 2009), rule changes that mandate more disclosure in proxy and information statements regarding risk, compensation and corporate governance matters. Specifically, the changes require disclosure concerning:

- The relationship of an issuer's compensation policies and practices to risk management, when those compensation policies and practices create risks that are reasonably likely to have a material adverse effect on the issuer;
- The grant date fair value of equity awards in the Summary Compensation Table, replacing the prior approach of requiring disclosure of the amounts of compensation expense recognized for financial reporting purposes;
- The potential conflicts of interest that compensation consultants may have when performing services for the issuer, focusing on disclosure of fees paid (subject to a $120,000 threshold) for executive compensation services and for additional services;
- The background and qualifications of directors and nominees for director, describing the experience and skills that led the issuer to choose the director or nominee for the board;
- Other public company directorships held by each director or nominee over the past five years;
- Legal proceedings involving an issuer's executive officers, directors, and nominees for director, including disclosure covering the past ten years and covering a significantly expanded list of relevant proceedings;

- The board of directors' consideration of diversity in the process by which directors are considered for nomination to the board;
- The leadership structure of the board, including whether the issuer has combined or separated the roles of chairman and principal executive officer, and why the issuer believes that its leadership structure is appropriate for the issuer, as well as a discussion, in some circumstances, of whether and why an issuer has a lead independent director;
- The extent of the board's role in the oversight of risk; and
- Voting results, which are to be provided on a significantly accelerated basis under cover of Form 8-K.

These rule changes were effective on February 28, 2010, and were first included in proxy statements for annual meetings occurring in 2010.

The Relationship between Compensation and Risk

The SEC adopted Item 402(s) of Regulation S-K, which elicits disclosure about the relationship of risk to the compensation policies and practices for *all* employees, not just the executive officers of the issuer. This disclosure is limited to compensation policies and practices, however, such that no further disclosure regarding the specific amounts of compensation paid to employees would be required under the rule. In response to commenters' concerns that this disclosure may be confusing if included as part of the CD&A, the SEC decided to require the disclosure outside of the CD&A, under a discrete disclosure requirement. Nonetheless, disclosure concerning the relationship between compensation and risk may be required in the CD&A specifically with regard to the named executive officers, consistent with the guidance that the SEC provided in both the proposing and adopting releases for this rule change, which both stated that "[t]o the extent … such risk considerations are a material aspect of the company's compensation policies or decisions for named executive officers, the company is required to discuss them as part of its CD&A under the current rules."

Requirements of Item 402(s) of Regulation S-K

As adopted, the disclosure is triggered if compensation policies and practices create risks that are "reasonably likely to have a material adverse effect" on the issuer. The standard of "reasonably likely to have a material adverse effect" tracks the requirements in Item 303 of Regulation S-K. In response to concerns expressed by

commenters, the SEC decided to adopt this higher standard relative to the proposed standard, which looked to whether the compensation policies or practices "may have a material effect" on the issuer. In discussing these changes between the proposed rule and the final rule, the SEC noted that this standard would be more familiar to issuers, given that it is applied in determining whether known material trends, demands, events, and uncertainties must be disclosed. Focusing the standard on whether the risk may have a material adverse effect on the issuer also permits issuers to consider compensation policies and practices that mitigate or balance incentives. Further, the addition of the term "adverse" to the test clarifies that issuers do not have to discuss ways in which compensation policies and practices may encourage risk taking that is beneficial to the issuer.

The final rule includes a non-exclusive list of situations where compensation programs may have the potential to cause material adverse risks for issuers. These include compensation policies and practices:

- At a business unit of the issuer that carries a significant portion of the issuer's risk profile;
- At a business unit with compensation structured significantly differently than other units within the issuer;
- At a business unit that is significantly more profitable than others within the issuer;
- At a business unit where the compensation expense is a significant percentage of the unit's revenues; and
- That vary significantly from the overall risk and reward structure of the issuer, such as when bonuses are awarded upon accomplishment of a task, while the income and risk to the issuer from the task extend over a significantly longer period of time.

Further, the final rule includes a non-exclusive list of illustrative examples of the type of issues that an issuer may need to address if it has determined that compensation policies and practices create risks that are reasonably likely to have a material adverse effect on the issuer. These issues include:

- The general design philosophy of the issuer's compensation policies and practices for employees whose behavior would be most affected by the

incentives established by the policies and practices, as such policies and practices relate to or that affect risk taking by those employees on behalf of the issuer, and the manner of their implementation;

- The issuer's risk assessment or incentive considerations, if any, in structuring its compensation policies and practices or in awarding and paying compensation;
- How the issuer's compensation policies and practices relate to the realization of risks resulting from the actions of employees in both the short term and the long term, such as through policies requiring clawbacks or imposing holding periods;
- The issuer's policies regarding adjustments to its compensation policies and practices to address changes in its risk profile;
- Material adjustments the issuer has made to its compensation policies and practices as a result of changes in its risk profile; and
- The extent to which the issuer monitors its compensation policies and practices to determine whether its risk management objectives are being met with respect to incentivizing its employees.

This disclosure regarding the relationship between compensation and risk is not required for those issuers that qualify for scaled disclosure as a smaller reporting company.

The rule does not require an issuer to make an affirmative statement that it has determined that risks arising from compensation policies and practices are not reasonably likely to have a material adverse effect on the issuer, although issuers may need to consider whether to add such a statement, as well as an explanation of the issuer's process for evaluating risks arising from compensation policies and practices, in order to address the inevitable concerns of shareholders and proxy advisors.

SEC Staff Interpretations and Comments

During 2010, the Staff asked issuers what was done and what conclusion was reached in response to this disclosure item, most likely as a first-year check on compliance with the new rule. The Staff asked for a supplemental explanation if the issuer included no disclosure in the proxy statement regarding the evaluation of the relationship between employee compensation and risk; or if the issuer included only a state-

ment of a conclusion without a description of the process; or where an issuer did include some discussion of the process undertaken, but did not include a fulsome discussion of the process.

In each of these situations, the Staff asked for a supplemental explanation of the process undertaken to reach the conclusion that compensation policies are not reasonably likely to have a material adverse effect on the issuer. In many of the responses, issuers describe a process whereby compensation programs were reviewed, particularly focusing on incentive compensation programs and program features which could potentially encourage risk taking. These processes involved identifying the specific business risks that related to these compensation features, as well as "mitigating" factors that offset the risks. Issuers consistently undertook an analysis to determine the potential effects of the risks and the impact of the other factors considered, and whether any of the particular situations described in Item 402(s) applied to the issuer. In most cases, issuers indicated that the compensation committee was involved in some capacity with the analysis; responses often noted that the analysis was conducted by management with the concurrence of or consultation with the compensation committee.

The findings that companies often reached were similar, focusing on:

- The mix of compensation, which tended to be balanced with an emphasis toward rewarding long-term performance;
- The use of multiple performance metrics that are closely aligned with strategic business goals;
- The use of discretion as a means to adjust compensation downward to reflect performance or other factors;
- Caps on incentive compensation arrangements;
- The lack of highly leveraged payout curves;
- Multi-year time vesting on equity awards which requires long-term commitment on the part of employees;
- The governance, code of conduct, internal control and other measures implemented by the company;
- The role of the compensation committee in its oversight of pay programs;

- Frequent business reviews;
- The existence of compensation recovery policies;
- The implementation of stock ownership or stock holding requirements;
- The use of benchmarking to ensure the compensation programs are consistent with industry practice;
- The uniformity of compensation programs across business units and geographic regions, or alternatively, the differences employed to reflect specific business unit or geographic considerations; and
- The immaterial nature of some plans.

Changes to the Summary Compensation Table and the Director Compensation Table

In the 2006 changes to the executive compensation disclosure rules, the SEC required disclosure in the Summary Compensation Table of the compensation expense associated with equity awards (which included expensed amounts related to awards granted in prior fiscal years), rather than the grant date fair value of the awards made in the subject fiscal year covered in the Summary Compensation Table.

This approach created difficulties for issuers when presenting their executive compensation disclosure, because the presentation in the Summary Compensation Table of equity award values did not necessarily correspond with decisions that the compensation committee made in the fiscal year covered by the CD&A. In order to address this disconnect, some issuers began including "alternative summary compensation tables" and taking other approaches to try to clarify how the decisions addressed in the CD&A related to the amounts presented for the named executive officers.

Accordingly, as part of the December 2009 amendments, the SEC adopted changes that now require the disclosure of the grant date fair value of the equity awards made during the fiscal year in the "Option Awards" and "Stock Awards" columns of the Summary Compensation Table and the Director Compensation Table. These numbers reflect the grant date fair values calculated in accordance with the Financial Accounting Standards Board's Accounting Standards Codification Topic 718 (formerly known as FAS 123R and referred to here as "ASC Topic 718"). For performance-based awards, the SEC requires reporting of the fair value at the grant

date based on the probable outcome of the performance conditions (rather than the maximum potential value of the award), which should be consistent with the estimate of aggregate compensation cost to be recognized over the service period determined as of the grant date under ASC Topic 718. The maximum potential value of the awards is disclosed in a footnote to the Summary Compensation Table and the Director Compensation Table.

Issuers are required to report the full grant date fair value of each equity award in the Grants of Plan-Based Awards Table. Performance-based equity awards reported in the Grants of Plan-Based Awards Table are reported based on the probable outcome of meeting the performance condition, as with the Summary Compensation Table.

The SEC decided not to adopt a proposed change to its rules that would have permitted issuers to report salary and bonus foregone at the named executive officer's election in the appropriate column for the award elected. As a result, salary and bonus is reported in the "Salary" and "Bonus" columns even when foregone at the named executive officer's election, with footnote disclosure indicating receipt of the non-cash compensation and referring to the Grants of Plan-Based Awards Table where the stock, option, or non-equity incentive plan compensation is reported.

Compensation Consultant Conflicts

The rules require disclosure about fees paid to compensation consultants and their affiliates in specified circumstances.

In particular, if the board, compensation committee, or other persons performing an equivalent function (referred to in this section as the "board") has engaged its own compensation consultant to provide advice or recommendations regarding the amount or form of executive and director compensation, and this same consultant or the consultant's affiliates provide other consulting services to the issuer (which consulting services do not involve executive compensation) in an amount that exceeds $120,000 during the last fiscal year, then the issuer must disclose:

- The aggregate fees paid for services provided either to the board or the issuer with regard to determining or recommending the amount or form of executive and director compensation;
- The aggregate fees paid for any additional services provided by the consultant or its affiliates; and

- Whether the decision to engage the compensation consultant or its affiliates for the non-executive compensation consulting services was made, or recommended by, management and whether the board approved such other services.

In situations where the board has not engaged its own consultant, then disclosures are required if a consultant is engaged to provide both executive compensation consulting services and non-executive compensation consulting services to the issuer, provided that the fees for the non-executive compensation consulting services exceed $120,000 during the issuer's fiscal year. In this situation, disclosure is required of:

- The aggregate fees paid to the consultant or its affiliates for determining or recommending the amount or form of executive and director compensation; and
- The aggregate fees paid for any additional services provided by the consultant or its affiliates.

If the board and management have different compensation consultants, then no fee disclosure is required even if management's compensation consultant provides additional services to the issuer, recognizing that when the board engages its own compensation consultant, it mitigates the risks for the conflicts of interest that the SEC is seeking to address with the additional fee disclosure. Moreover, disclosure is not required when the compensation consultant's only role in recommending the amount or form of executive or director compensation is limited to consulting on broad-based plans that do not discriminate in favor of executive officers or directors of the issuer. Disclosure is also not required when the compensation consultant's services are limited to providing information, such as surveys, that is not customized for a particular issuer, or that is customized based on parameters that were not developed by the compensation consultant.

The SEC did not adopt a proposed requirement to disclose the nature and extent of additional services provided by the compensation consultant or its affiliates, given the potentially competitive nature of this information. Issuers still may provide some explanation of the types of services provided, if the additional information is necessary to an understanding of a potential conflict of interest.

Director and Nominee Qualifications

Requirements

The SEC adopted revisions to Item 401 of Regulation S-K, which sets forth disclosure requirements for the backgrounds of executive officers, directors, and nomi-

nees for director, to require pursuant to Item 401(e)(1) of Regulation S-K, for each director and any nominee for director, disclosure of the particular experience, qualifications, attributes, or skills that led the board to conclude that the person should serve as a director of the issuer, as of the time that the filing is made with the SEC. The disclosure is required for all nominees for director (including nominees put forward by a proponent other than the issuer), as well as for all existing directors, even if not subject to re-election at the meeting to which the proxy statement relates. This director and nominee disclosure requirement augments, but does not replace, specific disclosure required regarding the consideration by the nominating committee of minimum director qualifications, or specific qualities or skills.

The disclosure requirement does not mandate the particular information that must be disclosed. Rather, the SEC indicated that it wanted to provide issuers with flexibility to determine what information concerning a director's or nominee's skills, qualifications, or particular area of expertise should be disclosed to shareholders.

The SEC did not adopt a proposal to require disclosure of the specific experience, qualifications or skills that qualify a director to serve as a member of a particular committee. However, the SEC has noted in the adopting release that if the director or a nominee has been chosen to join the board because of particular expertise that is relevant to a specific committee, then that fact should be disclosed in response to the disclosure item.

SEC Staff Interpretations and Comments

In Regulation S-K Compliance and Disclosure Interpretations Question 116.05, the Staff made clear that it intended for issuers to disclose why the person's *particular* and *specific* experience, qualifications, attributes or skills led the board to conclude that such person should serve as a director of the issuer, so that disclosures made on a group basis would be unacceptable, even if the directors or nominees share similar characteristics.

Further, in Regulation S-K Compliance and Disclosure Interpretations Question 116.06, the Staff noted that an issuer with a classified board needs to provide the Item 401(e)(1) disclosure for the entire board, focusing on the evaluation of the director's particular and specific experience, qualifications, attributes or skills, and the conclusion on why the director should continue serving on the board, as of the time that a filing containing the disclosure is made. The Staff noted that this interpretation may necessitate adding in additional disclosure controls and procedures to ensure that

such information about directors who are not up for re-election at the upcoming shareholders' meeting is recorded, processed, summarized and reported in a timely manner.

The Staff raised a number of comments on the director qualifications disclosure provided in the 2010 proxy season, including the following:

- Omission of Required Disclosure. One consistent Staff comment on the governance disclosures, including the director qualification disclosures, was a comment asking the issuer to include the disclosure when it was not included. Perhaps because the rules became effective immediately before the proxy season, a surprising number of issuers did not comply with some or all of the new governance disclosure requirements in 2010. Given that it was the first year the disclosure was required, the Staff generally did not request that the issuers file an amendment to the Form 10-K to include the required disclosure, but rather allowed issuers to remedy the situation in future filings.
- Specificity of the Disclosure. In June 2010, SEC Chairman Mary Schapiro made a speech at the Stanford Directors' College where she discussed the adequacy of compliance with the new director qualifications disclosure item. She gave examples of actual good and bad disclosures (without identifying the issuers) to demonstrate the point that the disclosure should be individualized for each director and should avoid over-generalizations such as "our directors each have integrity, sound business judgment and honesty, which are important characteristics of a good board member." Chairman Schapiro's viewpoint was borne out through the Staff comment process, where the Staff frequently asked for an explicit description of the qualifications and experience over and above the basic biographical description that has been required by Item 401 of Regulation S-K, emphasizing that the disclosure needed to communicate how the specific qualifications, attributes or skills *led to the conclusion* that the director should serve on the particular issuer's board.
- Location of the Disclosure. The Staff did not typically raise comments concerning where issuers actually placed the director qualification disclosure. In many instances, the director qualification disclosure was included as a separate paragraph following each director's biographical information; in other cases, the disclosure was incorporated directly into the biography paragraph or included in a separate section entirely.

- Directors Serving Under a Shareholder Agreement. Many issuers have directors who serve because a shareholder has appointed the director to serve pursuant to some contractual or other arrangement, or particular shareholders nominate and elect certain directors under the terms of the issuer's charter, bylaws or other governing documents. In cases where issuers sought to reference only the shareholder agreement or arrangement as the basis for the conclusion as to why the director serves on the board, the Staff asked for the more complete description of the director's qualifications, even if that information had to be obtained from the shareholder.

Outside Directorships

The SEC also adopted a requirement for disclosure regarding other public company directorships held by directors or nominees over the past five years (even if a director is no longer serving as a director of the other public company). This requirement expands upon previously required disclosure regarding current director positions at other public companies.

Legal Proceedings

Item 401(f) of Regulation S-K previously required disclosure regarding a director's, nominee's, or executive officer's involvement in specific legal proceedings that are material to an evaluation of the integrity of such person. The SEC has extended the "look back" provision in Item 401(f) from five years to ten years, and now requires disclosure regarding the following additional legal proceedings:

- Any judicial or administrative proceedings resulting from involvement in mail or wire fraud or fraud in connection with any business entity;
- Any judicial or administrative proceedings based on violations of federal or state securities, commodities, banking, or insurance laws and regulations, or any settlement of such actions; and
- Any disciplinary sanctions or orders imposed by stock, commodities, or derivatives exchanges or other self-regulatory organizations.

The rules do not require disclosure of a settlement of a civil proceeding among private parties. As is the case before these amendments, the disclosure of specific legal proceedings (including the newly added proceedings specified above) are not required to be disclosed if the proceeding is not material to an evaluation of the ability or integrity of the director or director nominee.

Director Diversity

Requirements

The rules require disclosure of whether and, if so, how the nominating committee considers diversity in identifying director nominees. Further, if the nominating committee or the board has a policy with regard to the consideration of diversity in identifying director nominees, then disclosure is required of how the policy is implemented and monitored for effectiveness. In adopting this new requirement, the SEC has not defined the term "diversity," leaving it to each issuer to define diversity in the way that the issuer deems appropriate. The SEC noted that some issuers may define diversity to include "differences of viewpoint, professional experience, education, skill and other qualities or attributes that contribute to board heterogeneity," while other issuers may define diversity to include race, gender and national origin.

SEC Staff Interpretations and Comments

In some cases, issuers expressly disclaimed any policy on diversity, but the Staff consistently raised a comment requesting the "policy" disclosure whenever diversity is mentioned in a filing. In many cases, issuers have addressed diversity in the context of the director qualifications considered in the nomination process, and even if the word "diversity" is not used directly, but the disclosure implies the consideration of a broad range of skills and qualifications, the Staff will raise a comment asking for the complete diversity disclosure. As a result, the Staff's interpretation contemplates the policy disclosure whenever diversity (however defined) is considered, even if no such policy is actually articulated in writing. The additional disclosure required once it is determined that a diversity "policy" exists involves discussing how the policy has been implemented (i.e., through the nominating committee process) and how it is monitored (i.e., typically through the annual committee and/or board self-evaluation process).

Board Leadership Structure

Requirements

Under Item 407(h) of Regulation S-K, an issuer must disclose whether and why it has chosen to combine or separate the principal executive officer and board chairman positions, as well as the reasons why the issuer believes that this board leadership structure is the most appropriate structure for the issuer at the time of the applicable filing. In those situations where there is a combined principal executive officer and board chairman, but also a lead independent director, then the issuer must disclose

whether and why the issuer has a lead independent director and the specific role that the lead independent director plays in the leadership of the issuer. Further, the issuer must explain the effect that the board's role in the oversight of risk has on the leadership structure.

SEC Staff Interpretations and Comments

The Staff's main focus in the comment process has been on eliciting a specific discussion of why the leadership structure is appropriate given the specific characteristics or circumstances of the issuer. In some cases, issuers did not explain why either the combined or separate Chairman/CEO made particular sense in light of an issuer's particular circumstances. This problem was particularly evident for issuers with a separate Chairman/CEO leadership structure, because that structure has historically been seen as a "good" governance practice. Nonetheless, the Staff has raised the comment asking for a more detailed explanation, even in those situations where the separate Chairman/CEO structure was in place. Issuers tended to not always include disclosures responsive to the requirement to explain the effect that the board's role in the oversight of risk has on the leadership structure, so the Staff frequently raised a comment seeking full compliance with Item 407(h). Some issuers chose to say that the board's role in the oversight of risk had no effect on the board leadership structure, while others focused on the interaction of the interested committees with the Chairman and/or CEO in the course of overseeing the issuer's risk management.

The Board's Oversight of Risk

The SEC mandates disclosure about the board's involvement in the oversight of the issuer's risk management process. Issuers have flexibility under this disclosure requirement to describe how the oversight role is exercised, i.e*.,* whether it is through the activities of the entire board, a risk committee of the board, or another committee of the board, such as the audit committee. The SEC also indicates that, where relevant, issuers may want to address whether the individuals who supervise risk management report to the board or a board committee, or otherwise how the board or the appropriate committee receives information from risk managers.

Accelerated Disclosure of Voting Results

Prior to the SEC's action in 2009, voting results from annual or special meetings were required to be disclosed in periodic reports on Form 10-Q or 10-K, which resulted in a significant delay in the time between when the meeting occurred and when shareholders learned of the results from their voting decisions. The SEC moved

the requirement for disclosure of voting results from Forms 10-Q and 10-K to Form 8-K. Now, voting results are filed under Item 5.07 of Form 8-K within four business days after the end of the meeting at which the vote was held.

In order to accommodate situations where it may be difficult to determine final voting results within the four-day filing window, the SEC provided an Instruction to Item 5.07 which indicates that an issuer is required to file preliminary voting results within four days after the end of the shareholders' meeting, and then file an amended Form 8-K within four business days after the final voting results are known. If definitive voting results are obtained within the initial four day filing window, then those definitive results may be filed and no preliminary results need be filed.

Areas of Focus in SEC Comments on Annual Reports

Recent Staff comments reflect the trend of Staff review of both legal and accounting or financial disclosures in the Form 10-K. Recent areas of frequent Staff comment have addressed disclosure of goodwill impairment charges, liquidity, debt covenants, disclosure controls and procedures, risk factors and exhibits. Each of these areas is further discussed below.

Management 'S Discussion and Analysis

Impairments

One of the most frequent areas of Staff comment on Form 10-Ks relates to disclosure of goodwill impairment. The Staff may request additional supplemental information or disclosure if an issuer has taken an impairment charge, but it has also raised comments if no impairment charge has been taken but goodwill accounts for a significant portion of total assets and there are downward trends in revenue, income or stock price. In situations where the issuer has already taken a goodwill impairment charge, the Staff may request that issuers discuss the primary drivers in assumptions that resulted in the charge. For example, the issuer may be asked whether it significantly reduced projected future revenues or net cash flows or increased the discount rates, or whether it considered an economic recovery in its cash flow projections. In addition, issuers are frequently asked to disclose expectations regarding future operating results and liquidity as a result of the impairment charge, including a discussion of whether they expect historical operating results to be indicative of future operating results.

If an issuer has not taken an impairment charge but goodwill accounts for a significant portion of total assets and there are downward trends in revenue, income or

stock price, the Staff may issue comments related to the issuer's goodwill impairment analysis. For example, the issuer may be asked to provide a more detailed description of the steps it performs to review goodwill for recoverability, describe the nature of the valuation techniques and significant estimates and assumptions employed to determine the fair value in the impairment analysis and discuss whether there have been any changes to the assumptions and methodologies used since the last impairment test. In addition, the issuer may be asked to discuss its estimates of future cash flows, including disclosures related to the cash flow growth rate used to determine the future cash flow projections.

The Staff may also ask issuers to break down goodwill by reporting unit. Issuers may be requested to disclose any changes to reporting units or allocations of goodwill by reporting unit, as well as the reasons for these changes. The Staff may perform a detailed review of documentation related to the reporting structure in order to determine whether there is a basis for the allocation decisions.

Liquidity

Another area of increased Staff comments in Form 10-Ks has been in the liquidity disclosure of MD&A. The primary focus of Staff comments has been on how the economy has impacted the availability of cash and credit. Comments have reflected a concern that an issuer's risk factors and MD&A disclosure be consistent, and that the MD&A disclosure provide a sufficient level of detail about known trends, demands, events and uncertainties. The SEC has also released interpretive guidance related to liquidity disclosure in MD&A, which is described below in "Additional SEC Interpretive Guidance – Liquidity and Capital Resource Disclosure."

Staff comments related to liquidity also address the disclosure of financial covenants related to debt instruments. Issuers have been asked to disclose the specific terms of material financial covenants in both the footnotes to financial statements and MD&A. Typically, this disclosure must include any required ratios, as well as actual ratios as of the end of the period. As described below, the SEC has also issued interpretive guidance that provides that when management believes a financial covenant is material to the issuer's financial condition and/or liquidity, the financial covenant should be disclosed even if it relies on a non-GAAP measure. The disclosure around the non-GAAP measure should address the material terms of the credit agreement, the amount or limit required for compliance with the covenant, and the actual or reasonably likely effects of compliance or non-compliance with the covenant on the issuer's financial condition and liquidity. Issuers must also provide a reconciliation to GAAP.

The Staff has recently focused on the impact of offshore cash holding on the issuer's liquidity position. The Staff's comments have focused on the extent to which U.S. taxation of funds repatriated into the country would limit the availability of that offshore cash to satisfy the issuer's liquidity obligations.

Loss Contingency Disclosures

The standard for loss contingency accounting and disclosure is Accounting Standards Codification 450-20 (referred to as "ASC 450-20," formerly known as Statement of Financial Accounting Standards No. 5). At the end of 2010, the Staff of the Division of Corporation Finance announced an increased focus on disclosures made in financial statements, financial statement footnotes and in related disclosures when the Staff reviews Form 10-Ks in its regular review process.

Under ASC 450-20, each loss contingency must be classified as either a "probable" loss contingency, a "reasonably possible" loss contingency, or a "remote" loss contingency. Then, each loss contingency must be classified as either "reasonably estimable" or "not reasonably estimable." For probable loss contingencies, if the loss can be reasonably estimated, an issuer must record an accrual in the financial statements, disclose the nature of the accrued loss contingency in a footnote to the financial statements, and, if necessary for the financial statements to not be misleading, disclose the amount of the accrued loss contingency in a footnote to the financial statements. For reasonably possible loss contingencies (where it is determined that the contingency is less than probable but more than remote), no accrual is recorded in the financial statements, however, the issuer must disclose the nature of the loss contingency in a footnote to the financial statements. In addition, an issuer must disclose the reasonable estimate of the possible loss in a footnote to the financial statements or, if that amount is not reasonably estimable, the issuer must include a statement in a footnote to the financial statements that such an estimate cannot be made. Although not required by ASC 450-20, through the comment process the Staff has sought further disclosure with regard to why a contingency is not reasonably estimable. With regard to remote loss contingencies (where there is only a slight chance that the contingency will occur), no accrual is recorded in the financial statements, and no disclosure regarding the loss contingency is required in a footnote to the financial statements. No accrual or disclosure is required for loss contingencies that are immaterial to the issuer's financial statements, and when disclosure is required, reasonable aggregation has been permitted.

The Staff has focused on often generic risk factor disclosure regarding the potential material adverse effects of pending or future litigation, as well as legal proceedings disclosure which states that the issuer has no pending material litigation and no disclosure regarding contingencies in their financial statements or the footnotes to those financial statements. In these circumstances, the Staff has requested an explanation as to how these disclosures are consistent. Moreover, the Staff has raised comments where issuers do not use the specific language of ASC 450-20, and as a result, issuers should specifically include disclosures regarding "contingencies," rather than "liabilities" or "results," and issuers should indicate that management believes that any contingencies would not have a material effect on "the issuer's financial statements," rather than "the issuer's results of operations" or "the issuer's financial condition."

The Staff's comments have also focused on announcements of significant settlements of litigation or regulatory actions and the Staff will review loss contingency disclosures in the periods prior to those settlements. The Staff will under these circumstances review the disclosures of the issuer, as well as any disclosures made by the co-parties or counter-parties to the litigation. The Staff also regularly seeks background information regarding the basis for "not reasonably estimable" determinations.

Disclosure Controls and Procedures

The Staff has continued to issue comments requiring issuers to include the entire definition of disclosure controls and procedures in their filings, as the definition is set forth in Exchange Act Rule 13a-15(e). Rule 13a-15(e) defines the term disclosure controls and procedures, then goes on to add "disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure." Issuers including part, but not all, of the above language will be asked to expand their disclosure to include it in its entirety. However, issuers may also limit their disclosure to state simply that their disclosure controls and procedures are effective (or not effective). Issuers using the shortened term "disclosure controls" are asked to refer to "disclosure controls and procedures." In addition, the Staff continues to focus on whether references to "reasonable assurance" are included in the disclosure controls and procedures section, and, if so, whether the issuer has indicated that the principal executive officer and principal financial officer have concluded that disclosure controls and procedures were effective at that reasonable assurance level.

Risk Factors

Recent Staff comments on risk factor disclosure in periodic reports have focused on the following areas: reliance on customers, suppliers, governments and key employees; the market for an issuer's products and services; the impact of regulatory changes; cybersecurity risks; ineffective disclosure and internal controls; legal exposures and reliance on legal positions; conflicts of interest and related party transactions; a history of operating losses; and going concern issues. Issuers should review their risk factors to ensure that they provide adequate disclosure of these issues, to the extent they are applicable. In addition, issuers should ensure that they updated their forward-looking statements disclaimer in conjunction with changes to their risk factors.

Exhibits

Staff comments have recently addressed the practice of omitting schedules and exhibits to material agreements other than merger agreements. Staff comments have highlighted that the exception permitting issuers to exclude schedules to a merger agreement does not apply to other material agreements filed under Item 601(b)(10) of Regulation S-K. Issuers have been asked to either provide a materiality analysis indicating that the omitted schedules and exhibits are not material, or to file the schedules and exhibits to the agreement as part of the agreement.

RESTATEMENTS

The Staff has noted that recent filing reviews have focused on issues arising in connection with little "r" restatements, which generally occur in situations where an immaterial error that is not corrected over multiple periods eventually grows large enough to become material and thus must be corrected. The Staff appears to be concerned in some cases with whether a little "r" restatement should in fact have been a big "R" restatement, based on the issuer's assessment of materiality. Further, the Staff is concerned that issuers should address the extent to which the prior errors impact the conclusions that the issuer has made with regard to internal control over financial reporting and disclosure controls and procedures, and whether any material changes in internal control over financial reporting must be disclosed.

The Staff's typical comment regarding a little "r" restatement will point out the guidance in both SAB 108 and SAB 99. Among other guidance, SAB 99 points issuers to both the quantitative and qualitative considerations that must go into evaluating materiality. Among the qualitative factors that issuers will consider in connection with

little "r" restatements are: (1) the errors were capable of precise measurement and resulted from the misapplication of accounting policy; (2) the misstatements did not result from an attempt to mask a change in earnings or other trends, nor to hide a failure to meet analysts' consensus expectations; (3) there was no change in loss to income in any period (or vice-a-versa); (4) the errors do not relate to a particular segment or other important aspect of the business; (5) there is no impact on compliance with any regulatory requirements as a result of the errors; (6) there is no impact to debt covenants or any other contractual requirements as a result of the errors; (7) there is no impact on management's compensation; and (8) the errors do not result from an attempt to conceal an unlawful transaction.

The Staff appears to be concerned that, while the errors prompting a little "r" restatement do not lead to non-reliance on previously issued financial statements, the fact of a little "r" restatement nonetheless means that errors did occur in the prior periods, and the existence of such errors may have an impact on the conclusions as to the effectiveness of the issuer's disclosure controls and procedures and internal control over financial reporting. This concern arises because, from an evaluation of internal controls perspective, an issuer must demonstrate that the internal control deficiencies related to the errors did not result in a reasonable possibility that a material misstatement would not be prevented, or detected and corrected on a timely basis. In the event that the Staff cannot be convinced that the errors did not affect the conclusions as to effectiveness of disclosure controls and procedures and internal control over financial reporting, the issuer may find itself in the situation of having to go back and revisit those conclusions in amended filings.

In evaluating whether the past deficiencies should be considered a significant deficiency or a material weakness, the issuer must consider the following indicators: (1) there were no indications of fraud on the part of senior management; (2) the deficiencies did not result in a restatement of previously issued financial statements to reflect the correction of a material misstatement due to error or fraud; (3) the deficiencies were not identified by the auditor under circumstances that indicate the misstatement would not otherwise have been detected by the entity's internal control; and (4) the deficiencies were not the result of ineffective oversight of the issuer's financial reporting and internal control by those charged with governance.

Issuers who receive a comment from the Staff will point to compensating controls which prevented the deficiency causing the error from becoming a material weakness (*e.g.*, monthly reconciliations and income statement and balance sheet reviews). Fur-

ther, issuers sometimes point out the extent to which control issues that may have led to the errors were later corrected before the controls were evaluated for effectiveness, in which case the Staff may ask whether such changes to internal control over financial reporting were material and were required to be disclosed. In this regard, issuers often note that while changes to internal controls have occurred as a result of identifying the errors, no disclosure of such changes is required because the changes in internal control over financial reporting did not materially affect, and are not reasonably likely to materially affect, the issuer's internal control over financial reporting.

Segment Disclosure

The Staff has indicated that it is not using the chief operating decision maker ("CODM") reports as a litmus test for segment reporting. The Staff will now look at the issue of segment reporting more holistically in accordance with the accounting standards. Without as much emphasis on the CODM reports, the Staff typically seeks a more detailed analysis from the issuer as to how all of the factors in ASC 280 have been considered in determining the issuer's operating segments, and whether the issuer's operating segments are appropriately aggregated (focusing on the standard of having similar economic characteristics and how the issuer has analyzed the five areas specified in ASC 280). In many instances, the Staff's comments have been focused on how the issuer is considering its segment presentation in light of changes to the business over time. All in all, the Staff appears to be likely to employ the same level of skepticism to segment disclosures, with or without asking for the CODM reports.

Additional SEC Interpretive Guidance

The SEC has also provided interpretive guidance outside of the comment process in several areas relevant to preparing Form 10-Ks and proxy statements.

Use of Non-GAAP Measures

On January 15, 2010, the Staff issued new Compliance and Disclosure Interpretations regarding the use of non-GAAP financial measures under Item 10(e) of Regulation S-K. These revised interpretations related to the use of non-GAAP measures arise out of the Staff's concern that periodic reports have become "compliance documents" that do not sufficiently communicate issuers' operating performance and financial condition in a manner that is consistent with the disclosure made by issuers outside of their SEC filings. According to the Staff, the new interpretations are not intended to encourage an increased use of non-GAAP measures, but rather to improve disclosure in SEC filings. By providing more flexibility to use non-GAAP measures in

periodic reports, the SEC is expecting issuers to provide a consistent message across their SEC filings and other public communications. The Staff has also made clear that it reviews an issuer's statements outside of SEC filings to determine whether an issuer's public statements, including those using non-GAAP financial measures, are consistent with disclosure in its SEC filings.

While the Staff has indicated that it is not seeking to require that issuers put non-GAAP measures in filings, some of the key Non-GAAP Financial Measures Compliance and Disclosure Interpretations provide additional flexibility that will facilitate inclusion of some non-GAAP measures in filings in compliance with Item 10(e) of Regulation S-K. The key interpretations are as follows:

- Permitting Adjustments for Recurring Items. A frequent area of Staff comment has been with respect to Item 10(e)'s prohibition on adjustments that "eliminate or smooth items identified as non-recurring, infrequent or unusual" if the item occurred in the past two years or is reasonably likely to occur in the next two years. The Staff's comments have discouraged non-GAAP adjustments for what it views as recurring items even if there were sufficient additional disclosure to explain the nature of the item. Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 102.03 now permits the presentation of a non-GAAP measure that excludes a gain or charge that is recurring, as long as the issuer does not attempt to represent that particular item as non-recurring, infrequent or unusual.

- Business Purpose Not Required for Use of Non-GAAP Measures. Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 102.04 clarifies that a non-GAAP measure may be included in an SEC filing even when management does not use the measure for the purpose of managing its business or for other purposes. The Staff focuses now on the fact that Item 10(e)(1)(i)(D) of Regulation S-K provides that a statement of additional purposes is required "if material" and that an issuer is to disclose additional purposes, "if any," for using the measure. This reverses a prior trend in the comment process, using this provision in Item 10(e) as one of the bases for objecting as to whether there is a legitimate purpose for presenting the non-GAAP measure. However, the interpretation does not alter the requirement in Item 10(e)(1)(i)(C) to describe the reasons why management believes that presentation of the non-GAAP measure provides useful information to investors regarding the issuer's financial condition and results of operations.

- Per Share Performance Measures Permitted. Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 102.05 clarifies that, while the SEC continues to prohibit per share non-GAAP liquidity measures in any documents filed with or furnished to the SEC, the Staff will not object to a per share non-GAAP measure used to present financial performance.
- Free Cash Flow Permitted. Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 102.07 indicates that Item 10(e) of Regulation S-K does not prohibit the presentation in SEC filings of a "free cash flow" measure, which is usually defined as cash flow from operating activities less capital expenditures. The Staff's guidance cautions that the free cash flow measure must be accompanied by a clear description of the way in which it is calculated as well as the necessary GAAP reconciliation, and that issuers should avoid "inappropriate or potentially misleading inferences about its usefulness," such as implying that the amounts represent "residual cash flow."
- Adjusted EBITDA under Financial Covenants. Non-GAAP Financial Measures Compliance and Disclosure Interpretations Question 102.09 indicates that the prohibitions in Item 10(e) on the presentation of adjusted EBIT and EBITDA has prevented issuers from fully addressing in MD&A the financial covenants of their credit agreements. The Staff states that, "the prohibition in Item 10(e) notwithstanding," when management believes that the credit agreement is material and that an adjusted EBIT/EBITDA financial covenant is material to understanding the agreement and the issuer's financial condition and/or liquidity, then the issuer may be required to disclose the measure in the MD&A. The interpretation also provides that the disclosure around the measure should probably also address: (1) the material terms of the credit agreement, including the covenant; (2) the amount or limit required for compliance with the covenant; and (3) the actual or reasonably likely effects of compliance or non-compliance with the covenant on the issuer's financial condition and liquidity.

Liquidity and Capital Resources Disclosures

Effective September 28, 2010, the Staff provided interpretive guidance intended to improve the discussion of liquidity and funding risks in MD&A. This guidance focuses on disclosures related to liquidity, leverage ratios and the contractual obligations table. The Staff has also proposed amendments to disclosure requirements related

to short-term borrowings, but these amendments have not yet been adopted. The SEC's interpretive release, SEC Release No. 33-9144 (September 17, 2010), emphasizes that issuers are required to disclose known trends or demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in, a material change in the issuer's liquidity. The release highlights a number of trends and uncertainties relating to liquidity that issuers should consider including in their MD&A, including: difficulties in accessing the debt markets; reliance on commercial paper or other short-term financing arrangements; maturity mismatches between borrowing sources and the assets funded by those sources; changes in terms requested by counterparties; changes in the valuation of collateral; and counterparty risk. Issuers should provide disclosure of any intra-period variations if their disclosure does not otherwise adequately convey their financing arrangements. In addition, if a repurchase transaction is reasonably likely to result in the use of a material amount of cash or other liquid assets, it may be required to be disclosed in MD&A. The SEC also suggests that issuers consider describing cash management and risk management policies that are relevant to an assessment of their financial condition.

The interpretive release also addresses the inclusion of capital and leverage ratios in MD&A. If a capital or leverage ratio financial measure is presented, the issuer should clearly state why the measure is useful to understanding its financial condition and the measure should be accompanied by a clear explanation of the calculation methodology. This explanation should include a discussion of any unusual, infrequent or non-recurring inputs, or any inputs that are adjusted so that the ratio is calculated differently from directly comparable measures. Issuers should also consider whether the measure differs from other measures used in their industry; if so, additional discussion may be required to ensure that the disclosure is not misleading. Any non-GAAP financial measure, including any non-GAAP capital or leverage ratio, that is disclosed in an issuer's filing should comply with SEC rules and guidance related to the inclusion of non-GAAP financial measures.

In its interpretive release, the SEC recognizes that different approaches to the contractual obligations table have developed. The SEC declines to provide specific presentation requirements or guidance on the treatment of certain items; instead, it states that issuers should provide a presentation that is clear, understandable and not misleading, and that appropriately reflects the obligations that are meaningful to the issuer. The format and content of the disclosure should support the purpose of the disclosure in this section, which is to provide aggregated information about contractual obligations in a single location in order to improve transparency of an issuer's liquidity

and capital resource needs, and to provide context for assessing the role of off-balance sheet arrangements. Issuers should use footnotes, in the SEC's view, to provide information necessary for an understanding of the timing and amount of specified contractual obligations. Additional narrative disclosure should be provided if necessary to explain what the table does and does not include and to promote understanding of the information provided in the table.

Cybersecurity Disclosure

On October 13, 2011, the SEC's Division of Corporation Finance issued disclosure guidance to assist publicly-traded companies "in assessing what, if any, disclosures should be provided about cybersecurity matters in light of each registrant's specific facts and circumstances." CF Disclosure Guidance Topic No. 2 reviews the applicability of existing SEC disclosure requirements to today's cybersecurity concerns, noting that: (i) businesses increasingly focus or rely on internet communications and remote data storage; (ii) risks and potential costs associated with cyber attacks and inadequate cyber security are increasing; and (iii) as with other operational and financial risks and events, companies should on an ongoing basis review the adequacy of disclosure relating to cybersecurity risks and other cyber incidents. The Staff further notes that the guidance is meant to be consistent with disclosure considerations for any business risk, and that any disclosure should not compromise cybersecurity efforts. The Staff highlights a number of critical considerations, including: (i) potential costs and other negative consequences, such as increased protection costs (e.g., additional personnel, training, third party consultants), remediation costs, liability for stolen assets or information, the repair of damaged systems and incentives for customers to maintain business relationship after cyber attack; (ii) lost revenues arising from the unauthorized use of proprietary information, and the failure to retain or attract customers; (iii) litigation; and (iv) reputational damage.

Specifically with respect to risk factors disclosures, the Staff notes that issuers should consider the probability that cyber incidents will occur in the future, and the potential costs and other consequences that could result. In this regard, issuers must evaluate prior cyber incidents, including the severity and frequency of such incidents, as well as the probability of cyber attacks occurring. To the extent material, risk factor disclosure of potential cyber incidents may be necessary and may include aspects of a company's operations that give rise to or mitigate these cyber risks. The Staff indicates that issuers should not disclose "boilerplate" risks that generally apply to all public companies, and should not disclose any information in a risk factor that would increase a company's cybersecurity risks.

With regard to disclosures in MD&A, the Staff indicates that issuers should address cybersecurity risks or incidents if the costs or other impact of a known cyber risk or incident represents a material event, trend or uncertainty that is reasonably likely to have a material effect on the company's results of operations, financial condition or liquidity. MD&A disclosure may be required even if a past cyber incident did not have a material effect on the company's financial condition if the incident caused the company to materially increase its cybersecurity expenditures.

As for business disclosures, the Staff indicates that issuers should evaluate the impact of cyber incidents or cybersecurity risks on each reportable business segment, and if a cyber incident or cybersecurity risk materially impacts a company's (or business segment's) relationships with customers or suppliers, or materially impacts the competitive landscape, a company should summarize the cyber risk or incident and its impact in the description of that company's business. In the context of legal proceedings disclosure, issuers should discuss any material pending legal proceeding related to a cyber incident to which a company is a party.

The Staff notes that with regard to disclosure controls and procedures, issuers should evaluate the extent to which cyber incidents pose a risk to the company's ability to record, process, summarize and report information that is required to be disclosed in SEC filings. If it is reasonably possible that information would not be properly recorded, processed, summarized or reported due to a cyber incident, issuers must evaluate how cybersecurity risks impact the company's disclosure controls and procedures, whether these controls and procedures are effective and whether any remedial measures are required.

With respect to an issuer's financial statement disclosures, issuers should consider accounting principles that may be important when summarizing the impact of a cyber incident on the company's financial statements, including: (i) costs incurred to prevent cyber incidents; (ii) costs incurred to mitigate damages from a cyber incident; (iii) loss contingencies related to cyber incidents; (iv) impairment of certain assets; and (v) subsequent event disclosures.

Cybersecurity continues to be an area of interest for members of Congress, and they continue to look for opportunities to mandate disclosure or escalate the SEC Staff guidance to Commission guidance. In May 2013, Senator Rockefeller (Chairman of the Committee on Commerce, Science and Transportation) and SEC Chair White exchanged letters on the topic of cybersecurity disclosure, and Chair White indicated that this issue continues to be a disclosure priority for the Division of Corporation

Finance. She further indicated that, at that time, the Staff had issued about fifty comment letters to issuers asking about their cybersecurity disclosure.

In October 2014, the U.S. Chamber of Commerce sent a letter to SEC Chair White requesting that the SEC not adopt regulations that would mandate specific disclosures about cybersecurity. The Chamber was reacting to calls by those in Congress who have encouraged the SEC to beef up its rules about cybersecurity disclosure.

The Staff's comments on cybersecurity risk factor disclosure address a number of areas:

- Disclosure of Cybersecurity Risks. When the Staff has found no disclosure about cybersecurity risks, the Staff has issued a comment asking whether the issuer has considered the guidance in CF Disclosure Guidance Topic No. 2. In drafting this risk factor disclosure, issuers should address the risk that cyber incidents may go undetected for a long period of time. Issuers also typically address any preventative measures that have been established for the purpose of addressing cyber risks, and the risk that such measures may not be effective to avoid an incident. Moreover, risk factor disclosure should address the particular risks that may arise as a result of third-party access to an issuer's information technology systems. Risk factor disclosure about cybersecurity also addresses when an issuer has insurance coverage for cyber incidents, and the extent to which costs of a cyber attack could exceed that insurance coverage. The risk factor disclosure will also typically highlight the potential consequences of a cyber attack, which could include things like reputational harm, costs to remediate the impact of the attack, and costs for implementing protective measures.

- Unbundling the Cybersecurity Risk. The Staff has often asked that an issuer break out cybersecurity risks into a separate risk factor, rather than including the risk in one risk factor that addresses a variety of other concerns that the issuer faces.

- Context for the Risk Factor. A frequent Staff comment has been to ask that an issuer address in the risk factor any security breaches, cyber attacks or other cyber incidents that have been experienced in the past, even if those were not major breaches or did not have a material adverse impact on the issuer's business. In the Staff's view, this disclosure is important to an understanding of the extent to which an issuer faces threats.

- Post-Breach Disclosure. In general, as outlined in CF Disclosure Guidance Topic No. 2, the Staff is looking for disclosures about the costs and consequences of the incident, including: (i) the scope and magnitude of the breach; (ii) whether the incident was material; (iii) any known or potential remediation or other costs; and (iv) preventative measures to address the risk of future incidents.

Issuers should also consider the extent to which investors will be looking for the cybersecurity topic to be addressed in the proxy statement. Proxy advisor recommendations against directors of issuers who experienced cyber attacks have focused attention on cybersecurity as a governance issue, as investors consider what role the board should play in overseeing an issuer's cybersecurity program. Issuers are increasingly disclosing in their proxy statements the extent to which the board and its committees oversee cybersecurity risks, particularly in the context of those issuers who have experienced a significant cyber incident.

Guidance on European Debt Exposures

On January 6, 2012, the SEC's Division of Corporation Finance issued guidance regarding disclosures about exposure to the debt of sovereign and non-sovereign issuers in Europe. Topic No. 4 of the SEC Staff's new "CF Disclosure Guidance" series addresses specific concerns about the adequacy of public disclosures made principally by financial institutions regarding their European debt exposures, and the potential consequences of such exposures on those issuers. The Staff encourages affected issuers to consider this guidance in preparing their SEC reports, including in the upcoming annual reports for calendar year-end issuers.

The Staff has focused its attention on disclosure about European debt exposure included (or required to be included) in risk factors, MD&A, qualitative and quantitative disclosure about market risks ("Market Risk Disclosure"), as well as Industry Guide 3 disclosures required of bank holding companies and similar lending and deposit-taking financial institutions ("Guide 3"). The Staff's guidance in Topic No. 4 is directed at both U.S. and non-U.S. financial institutions, and the Staff notes that, to date, disclosures about the nature and extent of direct or indirect exposure to European sovereign debt "have been inconsistent in both substance and presentation." For this reason, the Staff lays out a very specific structure for evaluating what disclosures may be necessary regarding the exposures, based on the Staff's own experience in commenting on those disclosures that it has, to date, found to be lacking.

In providing its guidance, the Staff has not specifically identified the countries in Europe that are of principal concern, noting the specific countries may change over time. However, the Staff does indicate that issuers should focus on those countries experiencing "significant economic, fiscal and/or political strains such that the likelihood of default would be higher than would be anticipated when such factors do not exist." The Staff encourages issuers to identify the basis for determining which countries are included in the disclosure.

In comments issued by the Staff in its review of periodic reports filed in 2011, enhanced disclosure was requested, separately by country, as to: (i) gross sovereign, financial institutions, and non-financial corporations' exposure; (ii) quantified disclosure explaining how gross exposures are hedged; and (iii) a discussion of the circumstances under which losses may not be covered by purchased credit protection.

In addition to providing the disclosure separately by country as indicated above, the Staff has requested that issuers segregate between sovereign debt and non-sovereign debt exposures, and by financial statement category, in order to arrive at the gross funded exposure. In addition, the Staff has asked that issuers consider separately providing disclosure of gross unfunded commitments made. Further, the Staff suggests that information regarding hedges be provided in order to present an amount of net funded exposure. As discussed below, the Staff has provided a wide-ranging outline for assessing what qualitative and quantitative disclosures may be necessary regarding direct or indirect exposures to the European debt crisis.

The Staff believes that the disclosures outlined in Topic No. 4 are called for under existing, principles-based disclosure requirements. In this regard, the Staff notes the following applicable disclosure requirements and how they should be interpreted when evaluating what disclosure is necessary regarding European debt exposures:

- MD&A. Issuers must identify know trends or known demands, commitments, events or uncertainties that will result, or that are reasonably likely to result, in a material increase or decrease in liquidity, and issuers must also discuss any known trends or uncertainties that have had, or that the issuer reasonably expects may have, a material favorable or unfavorable impact on income.
- Guide 3. Item III.C.3 of Guide 3 calls for issuers to identify cross-border outstandings to borrowers in each foreign country where the exposures exceed one percent of total assets, as well as disclosure where "current conditions in a foreign country give rise to liquidity problems which are

expected to have a material impact on the timely repayment of principal or interest on the country's private or public sector debt," including tabular disclosure of changes in outstandings, and in some situations tabular disclosure of restructured outstandings.

- Risk Factors and Market Risk Disclosure. Issuers must provide disclosure of material risks, including in risk factors disclosure and in specific Market Risk Disclosures, and the Staff indicates that such disclosures should not be generic "boilerplate" and should rather be tailored to the issuer's specific facts and circumstances.

In Topic No. 4, the Staff provides a highly detailed outline for preparing the types of disclosure called for by the guidance. This outline provides considerations to be used when determining, in light of an issuer's specific facts, what disclosure should be provided in a manner that is consistent with the guidance. The outline is as follows:

I. Gross Funded Exposure

a. Countries

i. The basis for the countries selected for disclosure.

ii. The basis for determining the domicile of the exposure.

b. Type of Counterparty

i. Separate categories of exposure to sovereign and non-sovereign counterparties.

1. Sovereign exposures consist of financial instruments entered into with sovereign and local governments.

2. Non-sovereign exposures comprise exposure to corporations and financial institutions. To the extent material, separate disclosure may be required between financial and non-financial institutions.

c. Categories of Financial Instruments

i. Categories to be considered for disclosure include loans and leases, held-to-maturity securities, available-for-sale securities, trading securities, derivatives, and other financial exposures to arrive at gross-funded exposure.

1. For loans and leases, the gross amount prior to the deduction of the impairment provision and the net amount after the impairment provision.

2. For held-to-maturity securities, the amortized cost basis and the fair value.

3. For available-for-sale securities, the fair value, and if material, the amortized cost basis.

4. For trading securities, the fair value.

5. For derivative assets, the fair value, except that amount could be offset by the amount of cash collateral applied if separate footnote disclosure quantifying the amount of the offset is provided.

6. For credit default contracts sold, the fair value and the notional value of protection sold, along with a description of the events that would trigger payout under the contracts.

7. For other financial exposures, to the extent carried at fair value, the fair value. To the extent carried at amortized cost, the gross amount prior to the deduction of impairment and the net amount after impairment.

II. Unfunded Exposure

a. The amount of unfunded commitments by type of counterparty and by country.

b. The key terms and any potential limitations of the counterparty being able to draw down on the facilities.

III. Total Gross Exposure (Funded and Unfunded)

a. The effect of gross funded exposure and total unfunded exposure should be subtotaled to arrive at total gross exposure as of the balance sheet date, separated between type of counterparty and by country.

b. Appropriate footnote disclosure may be provided highlighting additional key details, such as maturity information for the exposures.

IV. Effects of Credit Default Protection to Arrive at Net Exposures.

a. The effects of credit default protection purchased separately by counterparty or country.

b. The fair value and notional value of the purchased credit protection.

c. The nature of payout or trigger events under the purchased credit protection contracts.

d. The types of counterparties that the credit protection was purchased from and an indication of the counterparty's credit quality.

e. Whether credit protection purchased has a shorter maturity date than the bonds or other exposure against which the protection was purchased. If the credit protection has a shorter maturity date, clarifying disclosure should be provided about this fact, as well as the risks presented by the mismatch of the maturity.

V. Other Risk Management Disclosures

a. How management is monitoring and/or mitigating exposures to selected countries, including any stress testing that is being performed.

b. How management is monitoring and/or mitigating the effects of indirect exposure in the analysis of risk. Disclosure should explain how the issuer identifies their indirect exposures, provide examples of the identified exposures, along with the level of the indirect exposures.

c. Current developments (rating downgrades, financial relief plans for impacted countries, widening credit spreads, etc.) of the identified countries, how those developments, or changes to them, could impact the issuer's financial condition, results of operations, liquidity or capital resources.

VI. Post-Reporting Date Events

a. Significant developments since the reporting date and the effects of those events on the reported amounts.

As noted in the "Supplementary Information" section of Topic No. 4, the statements in the CF Disclosure Guidance represent views of the Staff, and do not constitute a new rule, regulation or statement of the SEC. Nonetheless, financial

institutions preparing disclosure for their SEC reports should carefully consider the disclosure that should be provided in response to the Staff's expectations, as the Staff's outline included in Topic No. 4 will likely serve as a roadmap for the type of comments that the Staff will issue when reviewing the annual reports of any issuers with European credit exposure in 2012. While the Staff has not sought to provide a "one-size-fits-all" approach for these disclosures, Topic No. 4 does seek to provide key principles that need to be considered when evaluating and describing European debt exposures in upcoming SEC reports.

Iran Threat Reduction and Syria Human Rights Act of 2012

The Iran Threat Reduction and Syria Human Rights Act of 2012 (the "ITR Act"), was enacted on August 10, 2012. This law added Exchange Act Section 13(r), requiring disclosure by issuers and the filing of a notice with the SEC. If an issuer or any of its affiliates have engaged in any of the activities referenced in Section 13(r), the issuer's periodic reports must include disclosure of: (i) the nature and extent of the activity; (ii) the gross revenues and net profits, if any, attributable to the activity; and (iii) whether the issuer or affiliate intends to continue to engage in the activity. If an issuer or an affiliate of the issuer has knowingly engaged in any of the subject activities, then, in addition to the required disclosure, the issuer must submit a publicly-available notice to the SEC under the new EDGAR form type "IRANNOTICE." The SEC must send the notice to the President and certain Congressional committees.

The activities referenced in Section 13(r) focus in particular on transactions and investments relating to the petrochemical, petroleum and marine transport industries, activities relating to weapons of mass destruction and other military capabilities, financial and other transactions with those whose assets are frozen and certain specified Iranian entities, activities relating to the transfer of goods, technologies or services likely to be used by the government of Iran (as defined in U.S. sanctions laws) to commit human rights abuses, and any transactions or dealings with the government of Iran without the specific authorization of a Federal department or agency.

Section 13(r) did not require any SEC rulemaking. On December 4, 2012, the Staff of the SEC's Division of Corporation Finance updated its Exchange Act Sections Compliance and Disclosure Interpretations to include seven interpretations that address the implementation of Section 13(r).

The Staff notes in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.01 that if a periodic report is due after February 6, 2013 but

the issuer chooses to file the report prior to that date, the issuer is still subject to the Section 13(r) disclosure requirements for that report, and, as noted in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.02, the disclosure must cover activities that took place over the entire fiscal year (*e.g.*, January 1 through December 31, 2012), even if those activities pre-dated the August 10, 2012 enactment date of Section 13(r).

In the event an issuer has not identified any reportable activities during the relevant period, the Staff indicates in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.04 that an issuer is not required to include disclosure in its periodic reports. Disclosure is only required if any of the covered activities occurred during the reporting period.

One of the requirements of Exchange Act Section 13(r) is that issuers must disclose any dealings by the issuer or its affiliates with the government of Iran, even if those activities are not sanctionable, *unless* the activity is conducted under a specific authorization from a U.S. federal government department or agency. The Staff stated in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.05 that this exception is only available when the activity was authorized by a *U.S.* government agency or department, not an equivalent *foreign* governmental authority. Both general and specific licenses from the Office of Foreign Assets Control (OFAC) for transactions can qualify, so long as all of the conditions of the license are strictly observed, as noted in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.06.

In Exchange Act Sections Compliance and Disclosure Interpretations Question 147.07, the Staff notes that the disclosure made under Section 13(r) is public when filed with the SEC, and the notice of the disclosure that is filed on EDGAR would also be publicly available upon filing (as noted in the SEC's notice regarding the new EDGAR form type). The SEC has not prescribed the form of the notice, other than to say that notice should be a separate document that includes the information required by Section 13(r).

The Staff stated in Exchange Act Sections Compliance and Disclosure Interpretations Question 147.03 that Section 13(r) applies to both the issuer and its affiliates, and for this purpose "affiliate" has the same meaning as in 1934 Act Rule 12b-2. Rule 12b-2's definition of affiliate is typically read to include directors and officers, therefore issuers must determine whether any such persons have engaged in the activities regarding Iran that are specified in Section 13(r). While no consensus has

emerged as to whether specific questions about Iran activities should be included in the D&O questionnaire, some issuers have included questions with varying degrees of detail regarding this disclosure item.

Unbundling

Litigation by shareholder activists alleging violations of the SEC's rules which concern the "unbundling" of separate matters that are submitted to a shareholder vote by an issuer or any other person soliciting proxy authority has focused attention on the presentation of matters in the proxy statement. Exchange Act Rule 14a-4(a)(3) requires that the form of proxy "identify clearly and impartially each separate matter intended to be acted upon, whether or not related to or conditioned on the approval of other matters." Rule 14a-4(b)(1) further requires that the form of proxy provide separate boxes for shareholders to choose between approval, disapproval or abstention "with respect to each separate matter referred to therein as intended to be acted upon." These rules are intended to provide a means for shareholders to communicate their views to the board of directors on each matter to be acted upon. In Exchange Act Rule 14a-4(a)(3) Compliance and Disclosure Interpretations published on January 24, 2014, the SEC Staff addressed a number of specific proposals and whether the matters contemplated by those proposals must be unbundled under Rule 14a-4(a)(3).

In Exchange Act Rule 14a-4(a)(3) Compliance and Disclosure Interpretations Question 101.01, the Staff addresses a situation where management of an issuer has negotiated concessions from holders of a series of its preferred stock to reduce the dividend rate on the preferred stock in exchange for an extension of the maturity date. The Staff indicates that a single proposal submitted by management to holders of the issuer's common stock to approve a charter amendment containing these modifications need not be unbundled into separate proposals under Rule 14a-4(a)(3) (i.e., one relating to the reduction of the dividend rate, and another relating to the extension of the maturity date). In this regard, the Staff notes that multiple matters that are so "inextricably intertwined" as to effectively constitute a single matter need not be unbundled. The Staff would view the matters relating to the terms of the preferred stock as being inextricably intertwined, "because each of the proposed provisions relates to a basic financial term of the same series of capital stock and was the sole consideration for the countervailing provision." The Staff notes, however, that it would not view two separate matters as being inextricably intertwined "merely because the matters were negotiated as part of a transaction with a third party, nor because the matters represent terms of a contract that one or the other of the parties considers essential to the overall bargain."

In Exchange Act Rule 14a-4(a)(3) Compliance and Disclosure Interpretations Question 101.02, the Staff addresses a situation where management of an issuer intends to present an amended and restated charter to shareholders for approval at an annual meeting, with proposed amendments that would change the par value of the common stock, eliminate provisions relating to a series of preferred stock that is no longer outstanding and is not subject to further issuance, and declassify the board of directors. The Staff indicated that under Rule 14a-4(a)(3), these individual amendments that are part of the restatement would not need to be unbundled into separate proposals. In this regard, the Staff notes that it would not ordinarily object to the bundling of any number of immaterial matters with a single material matter. The Staff indicates that while there is no bright-line test for determining materiality in the context of Rule 14a-4(a)(3), issuers should consider whether a given matter substantively affects shareholder rights. Therefore, in this particular example, while the declassification amendment would be material given its impact on shareholder rights, the amendments relating to par value and preferred stock do not substantively affect shareholder rights, and therefore both of these amendments ordinarily could be included in a single restatement proposal together with the declassification amendment. The Staff notes, however, that "if management knows or has reason to believe that a particular amendment that does not substantively affect shareholder rights nevertheless is one on which shareholders could reasonably be expected to wish to express a view separate from their views on the other amendments that are part of the restatement, the amendment should be unbundled." Further, the Staff notes that the analysis under Rule 14a-4(a)(3) is not governed by the fact that, for state law purposes, these amendments could be presented to shareholders as a single restatement proposal.

In Exchange Act Rule 14a-4(a)(3) Compliance and Disclosure Interpretations Question 101.03, the Staff addresses a single proposal covering an omnibus amendment to a registrant's equity incentive plan. The Staff indicated that the separate changes need not be unbundled into separate proposals, when those changes included: (i) an increase to the total number of shares reserved for issuance under the plan; (ii) an increase in the maximum amount of compensation payable to an employee during a specified period for purposes of meeting the requirements for qualified performance-based compensation under Section 162(m) of the Internal Revenue Code; (iii) the addition of restricted stock to the types of awards that can be granted under the plan; and (iv) an extension of the term of the plan. The Staff notes that while it generally will object to the bundling of multiple, material matters into a single proposal – provided that the individual matters would require shareholder approval under state

law, the rules of a national securities exchange, or the registrant's organizational documents if presented on a standalone basis – the Staff will not object to the presentation of multiple changes to an equity incentive plan in a single proposal. See Section III of SEC Release No. 34-33229 (November 22, 1993). The Staff notes that this is the case even if the changes can be characterized as material in the context of the plan and the rules of a national securities exchange would require shareholder approval of each of the changes if presented on a standalone basis.

The Staff of the Division of Corporation Finance recently published revised guidance regarding the "unbundling" of matters presented for shareholder votes in connection with mergers and acquisitions. The guidance is contained in new Exchange Act Rule 14a-4(a)(3) Compliance and Disclosure Interpretations Questions 201.01 and 201.02, which replace unbundling interpretations that the Staff issued in 2004.

Under the revised guidance, if the acquiring company is required to present a proposed amendment to its organizational documents separately on its form of proxy for shareholder approval, then a target company subject to the SEC's proxy rules also must present this proposed amendment separately on the form of its proxy for approval by its own shareholders. This vote is required even if a separate vote is not required under state law or if the proposed amendment is the only matter that the acquiring company is submitting for a shareholder vote. In the Staff's view, unbundling is required because the proposed amendment is a term of the transaction and would effect a material change to the equity securities that the target company's shareholders are receiving in the transaction. As a result, these shareholders should be allowed to express their separate views on changes that would establish their substantive shareholder rights. The Staff indicated that only material matters must be unbundled, including amendments to a classified or staggered board, limitations on the removal of directors and supermajority voting provisions. Matters that the Staff would view as immaterial (and thus would not require unbundling) include changes to the company's name, restatements of charters and technical changes. A target company also is not required to separately present a proposed amendment to increase the number of authorized shares of the acquiring company's equity securities as long as the increase is limited to the number of shares reasonably expected to be issued in the transaction. Companies are permitted to condition the completion of a transaction on shareholder approval of any separate proposals. In this case, the company must clearly disclose such conditions in the proxy materials submitted to shareholders.

The revised unbundling guidance also applies to transactions in which the parties form a new entity to act as an acquisition vehicle and issue equity securities in the transaction. Under these circumstances, the party whose shareholders are expected to own the largest percentage of equity securities of the acquisition entity following the completion of the transaction would be considered the acquiring company for purposes of the unbundling analysis. The acquiring company must separately submit for shareholder approval any material provision of the acquisition entity's organizational documents if: (1) those provisions are material changes from the acquiring company's organizational documents; and (2) the changes would require approval of the acquiring company's shareholders. This position does not apply in the context of provisions that are required by the law of the governing jurisdiction of the acquisition entity. If the acquiring company must present separately any provision of the acquisition entity's organizational documents for approval by its shareholders (or would be required to do so if it were conducting a solicitation subject to the proxy rules), then the target company must also present such provisions separately for its shareholders.

Changes to the SEC's Review Program

In 2010, the SEC announced a restructuring of the Division of Corporate Finance that created three new offices, including an office for large and significant financial services companies. Although most public companies were not subject to review by that office, it is important to note that the office employed a "continuous review" approach that the Division of Corporation Finance has been developing over the past few years. In 2015, this office was combined with the office responsible for reviewing the filings of financial institutions.

The shift towards continuous review by the Staff is also evident in another recent trend. Some issuers have received follow-up letters on their proxy statements, even though the Staff had already completed its review of the issuer's Form 10-K before the proxy statement was filed. If a continuous review model is adopted more broadly by the Staff, it could result in issuers spending more time responding to Staff comments.

In addition to the shift towards continuous review, the Staff has indicated that it will begin reviewing documents outside of an issuer's filings. This has been made clear in the updates to the Staff's statements in connection with the non-GAAP measures guidance discussed above. The Staff has expressed concern that issuers' SEC filings seem to have become "compliance" documents, rather than communicative tools that provide useful information to shareholders, and has suggested that it will look outside of an issuer's filings in its review of the issuer's risk factors and MD&A. The

Staff has stated that it will focus on ensuring that the story an issuer is telling in its SEC filings is consistent with the story being told elsewhere, including in earnings releases, presentations, statements, news coverage and analyst reports. As a result, issuers are now more likely to see comments that reference disclosure made in other forums that raise questions or issues about the disclosures in filings.

In 2012, the Division of Corporation Finance announced the establishment of an Office of Disclosure Standards. The stated responsibilities of this office include evaluating the outcomes of the Division's selective review of various materials filed under the federal securities laws, with a view towards enhancing the standards and policies for those reviews to enhance their effectiveness and efficiency, and conducting ongoing program assessments to evaluate the effectiveness of the internal supervisory controls, and to ensure the Division's filing reviews are consistently performed with professional competence and integrity.

Audit Committee Disclosure

There is an increasing focus on the role played by the audit committee of the board of directors and the audit committee-auditor relationship. In October 2014, SEC Chair White announced an ongoing SEC effort to address a variety of issues raised about, e.g., the role that audit committees play and the information that issuers provide about their audit committee's efforts. In addition, the Investor Advisory Group of the PCAOB issued a report requesting that the PCAOB and SEC consider requiring that the audit committee report on its role, as well as considering whether auditors or another third party should assess and report on the duties and operational effectiveness of the audit committee. In 2013 a consortium of audit and governance groups (*e.g.*, the Center for Audit Quality, Corporate Board Member, and the NACD), calling itself the "Audit Committee Collaboration," published a report entitled "Enhancing the Audit Committee Report: A Call to Action." In December 2014, the Center for Audit Quality and Audit Analytics launched the "Audit Committee Transparency Barometer," which presented the results of an analysis of 2014 proxy statement disclosures about audit committees and auditors.

The Call to Action report noted that increased transparency through enhanced audit committee reporting about the audit committee's role and responsibilities was a means for increasing investor confidence in the work of the audit committee. That report cited instances where issuers had included expanded disclosure about the audit committee function and the audit committee's oversight of the auditor in 2013 proxy

statement disclosures. The report indicated that issuers could follow those examples to provide voluntary disclosures that

- clarify the scope of the audit committee's duties;
- clearly define the audit committee's composition; and
- provide information about: (1) factors considered when selecting or reappointing an audit firm; (2) selection of the lead audit engagement partner; (3) factors considered when determining auditor compensation; (4) how the committee oversees the auditor; and (5) the evaluation of the auditor.

Issuers must carefully consider whether and how to present any voluntary additional disclosures called for by these initiatives, particularly given current investor expectations and concerns about effective governance.

On July 1, 2015, the SEC issued SEC Release No. 33-9862 (July 1, 2015), *Audit Committee Oversight*, which solicits comment regarding potential disclosures about a number of areas relating to the audit committee's relationship with the auditor. The SEC is considering whether a number of new disclosure requirements should address the level of oversight that the audit committee exercises over the auditor. The SEC states that this disclosure would provide insight into the quality of oversight, which could potentially allow investors to understand the potential differences in performance or quality of financial reporting among issuers. The areas for which the SEC seeks input include:

- <u>Communications with the Auditor.</u> The SEC seeks comment on whether disclosure might include some discussion of the audit committee's consideration of communications that are required of auditors under applicable auditing standards, such as: (1) communications regarding the auditors overall audit strategy, timing and significant risks identified; (2) the nature and extent of specialized skills used in the audit; (3) the use of other firms or other persons, including internal audit; (4) the basis for determining that the auditor is able to serve as the issuer's principal auditor; and (5) the results of the audit.
- <u>Auditor/Audit Committee Meetings.</u> The SEC seeks comment on whether it should expand currently required disclosure about the frequency of audit committee meetings to include additional disclosure about the frequency of

private meetings or topics discussed with the auditor which could serve to provide additional insight about the audit committee's oversight of the auditor.

- Audit Quality Considerations. Comments are solicited regarding additional required disclosure, which could include a description of the nature of any discussions held with the auditor regarding the results of the audit firm's internal quality review, as well as the PCAOB's most recent inspection. This disclosure could address whether the audit committee discussed with the auditor the inspection report matters that are set forth in PCAOB Rel. No. 2012-003, *Information for Audit Committees about the PCAOB Inspection Process* (2012).

- Assessing and Selecting the Auditor. The SEC seeks comment on whether disclosure should be provided regarding the steps that the audit committee took in its process for assessment of the auditor, and the specific elements of the criteria considered by the committee.

- Consideration of Proposals. If an issuer has gone through a request for proposal process, the SEC seeks comment on whether the disclosure should include a discussion of the number of auditors asked to make proposals, how they were selected and the information that was used by the audit committee in making its decision.

- Ratification of Auditor Selection. The SEC indicates that the disclosure provided regarding a ratification of auditor proposal should "provide useful information to shareholders as to how and why the board is seeking ratification of the auditor, as well as the implication of the shareholder vote being solicited."

- Disclosure about the Audit Engagement Team. The concept release seeks input on whether disclosure should be provided regarding the audit engagement team, including the name of the engagement partner, as well as potentially the names of the other key members of the engagement team. In addition, the disclosure might include information about how long the individuals have served in their respective roles, as well as their relevant experience (e.g., the number of prior audit engagements performed and whether they were in the same industry).

- Audit Partner Selection. The SEC indicates that disclosure could be provided regarding the involvement of the audit committee in the selection of the

audit engagement partner. It is believed that any input the audit committee has in this selection could provide "transparency and insight into the exercise of the audit committee's responsibilities in overseeing the auditor."

- Auditor Tenure. The concept release solicits comment on whether auditor tenure disclosure should be required. The SEC indicates that disclosure of this information "could provide insight into the audit committee's overall decision to engage or retain the auditor."
- Involvement of Other Firms. The SEC seeks comment on whether disclosure should address the names, locations and responsibilities of accounting firms affiliated with the auditor, as well as non-affiliated accounting firms and other third party participants involved in the audit (such as actuaries, tax advisors, consultants).

The concept release also seeks comment as to whether disclosure of this type should remain voluntary, where the disclosure should appear, and whether additional disclosures should be required of all issuers. The release also seeks comment on whether audit committees should be required to report on other areas of oversight, such as risk governance, whistleblower complaints, cyber risk, or information technology risk.

Director Election Voting Standard Disclosure

The Staff of the Division of Corporation Finance has recently observed that issuers should review the disclosure in their proxy statements about the voting standard for director elections. The Staff's focus on the issue was prompted by a rule-making petition filed by the Council of Institutional Investors ("CII"), which requested that the SEC require companies to clarify the voting standards for the election of directors because, in CII's view, issuers that use the state law default plurality rule, coupled with a policy that requires the director to submit a resignation if the director does not receive a majority of votes in favor, should not be permitted to state that their directors are elected by majority voting standards. The United Brotherhood of Carpenters previously submitted a supplement to a petition filed in 2011 which addressed a similar problem. The SEC Staff in the Division of Economic and Risk Analysis found numerous examples where companies which described their director election voting standards in a confusing manner, such as by referring to a "plurality-plus" voting standard as "majority voting" for director elections.

SEC Enforcement Actions

On September 10, 2014, the SEC announced settlements with officers, directors, and significant shareholders for violating federal securities laws requiring information about their transactions in issuer stock. In addition, issuers settled charges with the SEC for contributing to filing failures by insiders and failing to report their insiders' filing delinquencies. Notable for its departure from the SEC's previous practice of generally bringing such charges only in cases in which insiders were also being charged with other violations, these actions signal increased attention by the SEC on the compliance obligations of insiders and large shareholders of reporting issuers.

Settlements by Insiders

The SEC charged insiders with violations of the federal securities laws, specifically violations of Sections 16(a), 13(d) and 13(g) of the Exchange Act. The SEC's cases naming insiders included cease-and-desist proceedings against officers, directors, and major shareholders. Such officers included CEOs, CFOs, Presidents, General Counsels, and Vice Presidents. Major shareholders charged were individuals, registered investment advisors, and entities providing investment management services to investment vehicles. The charges against these insiders revealed significant delinquencies in terms of filing the required Forms 4, Forms 5, Schedules 13D, Schedules 13G, or applicable amendments.

The details of each case and the degree of non-compliance with the beneficial ownership reporting requirements varied significantly. For example, insiders were charged with the untimely filing of between nine and 70 Forms 4 and 5, with an average number of 30 untimely filings. Regarding the degree of untimeliness, Forms 4 were generally filed approximately six months late in the cases brought by the SEC, but some forms were filed up to four years late. Late-reported transactions had aggregate market values of between $1 million and $182 million. The SEC proceedings also addressed several instances in which beneficial owners failed to file required amendments to Schedules 13D and 13G disclosing changes in beneficial ownership.

For corporate insiders settling these violations with the SEC, monetary penalties ranged from $25,000 to $120,000, with the average penalty being just over $72,000 among the 28 insiders. Larger penalties—ranging from $60,000 and up—were associated with a greater number of missing reports (for example, 25 untimely beneficial ownership reports being filed) and/or extreme untimeliness in filing (for example, filing a required report three years late).

Officers and directors charged with violations of Sections 16(a), 13(d), and 13(g) of the Exchange Act by the SEC often claimed that the violations were the result of the failure of their publicly-traded issuer employer to file beneficial ownership reports and required amendments on their behalf. In turn, their publicly-traded issuer employer often blamed such violations on lack of internal staffing or the late receipt of necessary information from the corporate insider. The major shareholders charged by the SEC indicated that the violations were the result of the failure of outside counsel to correctly advise them on their reporting obligations.

When such defenses were brought by corporate insiders, the SEC noted in the cease-and-desist orders that reliance on an employer, outside personnel, or counsel to make the required beneficial ownership filings or provide correct advice does not excuse the charged violations, as an insider retains legal responsibility for compliance with the filing requirements.

Such defenses proved unpersuasive to the SEC and ultimately unsuccessful to the charged insiders because there is no state of mind requirement for violations of Sections 16(a) and 13(d) and the rules thereunder. The failure to timely file a required report, even if inadvertent, constitutes a violation.

Settlements by Issuers

In a series of settlements, the SEC issued cease-and-desist orders against, and collected fines from, issuers for misstatements in, and failures to include, the required Item 405 disclosures. The misstatements and omissions were violations of Section 13(a) of the Exchange Act and Rule 13a-1 thereunder. In each matter, the SEC noted that the issuer "was required to review the forms filed and identify by name each such insider who failed to file on a timely basis and set forth the number of late reports and the number of transactions that were not reported on a timely basis." Further, the SEC listed the annual disclosures by each issuer and then stated the facts which showed the inaccuracy of those disclosures. For example, the settlements noted the following improper disclosures in response to Item 405:

- "Based solely upon a review of such reports and amendments thereto furnished to us and upon written representations of certain of such persons regarding their ownership of Common Stock, we believe that no person failed to file any such report on a timely basis during 2010, except that within the required two business day reporting requirement imposed by the SEC, the Company did not timely file one Form 4 report for [Section 16

Officer] with respect to the sale of 55 shares for which he has indirect beneficial ownership." The SEC noted that, during the fiscal years described in the disclosure, all of the company's officers and directors filed untimely Forms 4.

- "Based solely on a review of Forms 3, 4, and 5 and amendments thereto furnished to us, we know of no failure in Section 16(a) beneficial ownership reporting compliance except that through inadvertence certain directors or executives filed late." The SEC noted that, during each of the fiscal years described in the disclosure, there were multiple failures by insiders to file reports on a timely basis.

- "During the fiscal year ended December 31, 201[X], our Directors, executive officers and holders of more than ten percent of our common stock complied with all applicable Section 16(a) filing requirements." The SEC noted that, during each of the fiscal years described in the disclosure, there were multiple failures by insiders to file reports on a timely basis.

- "All Section 16(a) filing requirements applicable to its Directors, executive officers and greater than 10 percent beneficial owners were complied with for the most recent fiscal year." The SEC noted that, during each of the fiscal years described in the disclosure, the issuer's principal accounting officer failed to file required Section 16(a) reports. The issuer later disclosed that the principal accounting officer had not filed those reports, stating that "because the Company failed to timely advise [the principal accounting officer] that he was subject to the reporting requirements of Section 16 in his position as chief accounting officer."

- "All officers, directors and 10% beneficial owners, known to the Company, had timely filed required forms reporting beneficial ownership of Company securities, based solely on review of Filed Forms 3 and 4 furnished to the Company." The SEC noted that, during each of the fiscal years described in the disclosure, there were multiple failures by insiders to file reports on a timely basis.

In bringing actions against issuers for causing violations of Section 16(a) by their insiders, the SEC noted that—while it encourages issuers to assist insiders in complying with Section 16(a) filing requirements—issuers that voluntarily accept certain responsibilities and then act negligently in the performance of those tasks may be

liable for causing Section 16(a) violations by insiders. In each matter, the SEC noted that the issuer had voluntarily agreed with its insiders to perform certain tasks in connection with the filing of Section 16(a) reports on their behalf, including the preparation and filing of all such reports. After noting that the issuers had received the required information in a timely manner, the SEC stated that issuer personnel responsible for tasks relating to the preparation and filing of Section 16(a) reports repeatedly failed to perform on a timely basis the tasks the company had agreed to perform. The number of untimely filings ranged from 35 untimely filings over three years to 75 untimely filings in a single year. The amount of the fines in these matters ranged from $75,000 to $150,000.

Fraud Settlements

The SEC's charging of a publicly-traded issuer and corporate insiders for violations of Section 16(a) of the Exchange Act in separately announced settlements demonstrates the SEC's focus on these activities and the potential for fraud charges if these violations continue. The SEC charged a biotech issuer and its former CEO with defrauding investors by failing to report his sales of company stock. Given the CEO's failure to file initial and annual beneficial ownership reports on Forms 3 and 5, respectively, the degree of untimeliness of the filing of several Forms 4 (up to 26 months late), and the significant value of the late-reported sales, the SEC order found that the CEO's "sales would have been viewed by a reasonable investor as significantly altering the total mix of available information given, among other things, his position as CEO, the frequency with which he was selling [company] stock, and the size of his sales." Due to his conduct, the CEO was charged with violating Section 16(a) of the Exchange Act, as well as various federal securities law provisions relating to committing fraud upon investors as a result of the CEO's certification of annual reports and signing of a proxy statement, which all included material misstatements regarding his compliance with Section 16(a) of the Exchange Act.

Related to the CEO's violations of Section 16(a), the issuer was charged with failing to provide the disclosures required by Item 405 of Regulation S-K in annual reports, in violation of Section 13(a) of the Exchange Act, and with various federal securities law provisions relating to committing fraud upon investors as a result of such action.

Both the publicly-traded issuer and its former CEO settled with the SEC, and agreed to the imposition of significant monetary penalties, in the amounts of $175,000 for the CEO and $375,000 for the issuer.

Key Observations

The actions undertaken by the SEC as discussed above give rise to a number of important observations, as well as considerations for insiders, investors, and public companies.

- Issuers almost universally assist their officers and directors with the filing of Section 16 reports. Although the filing obligation ultimately rests with the individuals, the SEC actions make clear that issuers who undertake to assist their insiders with Section 16 obligations will also be held responsible for significant failures in Section 16 compliance. Accordingly, issuers must maintain a robust compliance system reasonably designed to avoid late or missed Section 16 filings.

- Likewise, the SEC actions make clear that insiders cannot rely solely on their issuers or counsel for compliance with Section 16; they must understand their reporting obligations. Periodic reminders and training are important to keep these compliance obligations front of mind. (We also recommend that issuers provide a short summary of the SEC's actions to their directors and officers as enforcement actions often make good "teaching moments.")

- It is very common for issuers to include in their Item 405 disclosure language that the disclosures are "based solely on a review of Forms 3, 4, and 5, and amendments thereto furnished to us." It is clear from several of the actions that the issuers actually did not review the forms, or that the individual reviewing the forms was unfamiliar with the legal requirements underlying them. As with other disclosures in an issuer's periodic reports, there should be a procedure that covers this review and an appropriately trained individual should undertake such review.

- One of the actions included a settlement with an insider and the related public issuer that included violations of Section 17(a) of the Securities Act of 1933, as amended. The SEC took the position that the insider and the issuer violated the anti-fraud provisions of the securities laws by failing to file Section 16(a) reports of securities transactions and holdings in a timely and accurate manner, rendering the issuer's annual reports and proxy statements false and misleading. This settlement demonstrates the SEC's belief that the failure to file timely reports, and an issuer's related materially inaccurate Item 405 disclosures, can serve as the basis of a fraud charge.

- The SEC noted the Enforcement Staff's use of "quantitative data sources and ranking algorithms" to identify late filers. The Staff has mentioned on numerous occasions its increasing use of electronic methods to identify potential issues. Expect to see more charges and settlements derived from these methods.

CHAPTER 4

SHAREHOLDER ACTIVISM AND CORPORATE GOVERNANCE

SHAREHOLDER ACTIVISM AND CORPORATE GOVERNANCE

Introduction

Continued shareholder concerns over corporate governance and executive compensation issues will shape the outcome of votes in the 2016 proxy season. Issuers will need to continue to focus on voting policies of institutional shareholders and proxy advisory services when making corporate governance and executive compensation decisions.

Shareholder Proposals

Trends in Shareholder Proposals

Key trends in the 2015 proxy season for governance and executive compensation shareholder proposals were as follows:

- A continued focus on corporate governance issues, including: (i) independent chair proposals; (ii) declassification of the board of directors; and (iii) anti-takeover provisions, including the right to call a special meeting, super-majority voting provisions and the ability of shareholders to act by written consent;
- A reduced number of shareholder proposals on executive compensation proposals since the advent of Say-on-Pay; and
- A continuing focus on political contributions and lobbying disclosure and oversight.

Shareholder proposals in 2015 focused on:

- Proxy access shareholder proposals;
- Compensation-related proposals (i.e., pay-for-performance, clawbacks, compensation consultants, and conflicts of interest);
- Majority voting for directors (particularly at Russell 3000 companies);
- Shareholder ability to call special meetings and take action by written consent;
- Declassified board of directors;

- Disclosure, limits, board oversight, and shareholder approval or ratification of political contributions; and
- Split chairman/CEO proposals.

Proxy Access

Important developments with the SEC's proxy access rule have resulted in increased attention on proxy access shareholder proposals.

Section 971 of the Dodd-Frank Act provided the SEC with authority to promulgate "proxy access" rules, allowing specified shareholders to include director nominees in a company's proxy materials. The Dodd-Frank Act did not prescribe specific standards for these rules, and the SEC had in fact proposed proxy access rules prior to enactment of the Dodd-Frank Act. The SEC issued final rules facilitating shareholder director nominations on August 25, 2010, and such rules were scheduled to become effective on November 15, 2010. However, the effectiveness of those rules was stayed due to litigation challenging the rules.

Under Rule 14a-11 as adopted by the SEC, qualifying shareholders or groups holding at least three percent of the voting power of a company's securities, who had held their shares for at least three years, would have had the right to include director nominees in proxy materials upon meeting certain other requirements. An amendment to Rule 14a-8 provided that companies may not exclude from their proxy materials shareholder proposals for less restrictive proxy access procedures. However, on September 29, 2010, the Business Roundtable and Chamber of Commerce of the United States of America filed a petition with the United States Court of Appeals for the District of Columbia Circuit (the "Court") seeking judicial review of the changes to the SEC's proxy access rule, and on the same day filed with the SEC a request to stay the effective date of Rule 14a-11. On October 4, 2010, the SEC granted the request for a stay of the Rule 14a-11 and associated rules pending resolution of the petition for review by the Court.

On July 22, 2011, the Court vacated Rule 14a-11. The Court held that the SEC was "arbitrary and capricious" in promulgating Rule 14a-11, based principally on the SEC's failure to adequately address the economic effects of the rule. The Court expressed significant concerns about the conclusions that the SEC reached and the agency's consideration of comments during the course of the rulemaking. The Court did not address the First Amendment challenge to the rule that had been raised by the petitioners. On September 6, 2011, the SEC issued a statement indicating that it would

not seek rehearing of the Court's decision, nor would it seek Supreme Court review of the decision; however, the SEC's staff would continue to study the viability of a proxy access rule. The statement also indicated that the amendment to Rule 14a-8 referenced above would go into effect when the Court's mandate was finalized, which occurred on September 14, 2011. As a result, the amendments to Rule 14a-8 (along with other rules adopted in connection with Rule 14a-11) became effective on September 20, 2011, following the SEC's publication of a notice announcing the effective date of the rule changes.

The amendments to Rule 14a-8 have permitted the type of "private ordering" for proxy access through the shareholder proposal process that many commenters had supported in the course of the proxy access rulemaking. Under Rule 14a-8(i)(8), as amended, a company may not exclude under this basis for exclusion a shareholder proposal that would amend or request that the company consider amending governing documents to facilitate director nominations by shareholders or disclosures related to nominations made by shareholders, as long as such proposal does not conflict with Rule 14a-11 and is not otherwise excludable under some other procedural or substantive basis in Rule 14a-8. The SEC also codified some of the Staff's historical interpretations of 14a-8(i)(8) which permitted exclusion of a shareholder proposal that would: (i) seek to disqualify a nominee standing for election; (ii) remove a director from office before the expiration of his or her term; (iii) question the competence, business judgment or character of a nominee or director; (iv) nominate a specific individual for election to the board of directors, other than through the Rule 14a-11 process, an applicable state law provision, or an issuer's governing documents; or (v) otherwise affect the outcome of the upcoming election of directors.

While the SEC's amendments to Rule 14a-8(i)(8) eliminated one basis to exclude proxy access shareholder proposals, there may be other options for seeking to exclude proxy access shareholder proposals. An issuer could: (i) argue that the proposal is contrary to the proxy rules under Rule 14a-8(i)(3), i.e., the resolution contained in the proposal is inherently vague or indefinite; (ii) that by adopting its own proxy access bylaw amendment, the shareholder's proxy access proposal has been "substantially implemented" under Rule 14a-8(i)(10); (iii) the shareholder proposal conflicts with a similar company-sponsored proposal under Rule 14a-8(i)(9), however the Staff has recently issued SLB No. 14H which substantially reduced the ability to rely on this basis for exclusion; or (iv) other potential bases for exclusion that may be applicable based on the wording of the proposal and supporting statement. Many companies have

been taking a "wait-and-see" approach with respect to amending their bylaws to permit proxy access in order to allow greater flexibility in responding to a future shareholder proposal, however pressure has begun to mount in 2015.

In November 2014, the Comptroller of the City of New York, on behalf of the New York City pension funds, launched a large-scale campaign for the 2015 proxy season targeting 75 issuers with a proxy access shareholder proposal. The campaign is called the "Boardroom Accountability Project." The Comptroller's office indicated this initiative is part of a wider effort to implement universal proxy access through private ordering.

The New York City Comptroller indicated that the 75 Boardroom Accountability Project proposals were submitted to issuers that were selected based on three priority issues: "climate change, board diversity, and excessive CEO pay." Based on that analysis, the proposals were submitted to: (1) 33 carbon-intensive coal, oil and gas, and utility companies; (2) 24 companies with few or no women directors, and little or no apparent racial or ethnic diversity; and (3) 25 companies that received significant opposition to their 2014 say-on-pay votes. The 75 identical precatory proposals submitted by the Comptroller requested that the board of directors adopt, and present for shareholder approval, a bylaw to give shareholders who meet a threshold of owning 3 percent of an issuer's shares continuously for three or more years the right to list their director candidates, representing up to 25 percent of the board, in the issuer's proxy materials. The proposal contemplated that the nominating shareholder would provide notice to the issuer, within the time specified in the bylaws, and would provide at that time the information required by the bylaws and the SEC's rules about both the director nominee and the nominator. The proposal also contemplated that the nominating shareholder would certify that (1) it will assume liability stemming from any legal or regulatory violation arising out of the nominator's communications with the issuer's shareholders; (2) it will comply with all applicable laws and regulations if it uses soliciting material other than the issuer's proxy materials; and (3) to the best of its knowledge, the required shares were acquired in the ordinary course of business and not to change or influence control of the issuer.

The proposal further provided that the nominating shareholder may submit a 500-word statement in support of the director nominee. The proposal would leave to the board the ability to adopt procedures to deal with whether submissions are timely and adequate, as well as how to prioritize multiple nominees. The proposal's supporting statement was very limited, noting a 2014 CFA Institute study which concluded that proxy access would "benefit both the markets and corporate boardrooms, with little cost or disruption" and has the potential to raise overall US market-capitalization by

"up to $140.3 billion if adopted market-wide." The supporting statement also noted that votes for similar proposals averaged 55 percent through September 2014 and similar bylaws have been adopted by Chesapeake Energy, Hewlett Packard, Western Union and Verizon Communications.

During the 2015 proxy season, over 90 proxy access shareholder proposals appeared on ballots, and as of the end of 2015, approximately 100 issuers have adopted some form of proxy access, with much of this momentum prompted by the Boardroom Accountability Project. As the 2016 proxy season approaches, more and more larger issuers have been considering the topic and deciding whether to implement proxy access.

Most proxy access bylaw provisions adopted this year have included a 3% ownership threshold, a 3-year continuous holding period, a 20% nomination limit and a 20 member limit on groups of nominating shareholders. Issuers and shareholders continue to debate a number of other important provisions:

- Maximum number of nominees. The Boardroom Accountability Project shareholder proposal and Rule 14a-11 both contemplated that the maximum number of proxy access nominees would be 25%, but many bylaw provisions include 20% maximum on the percentage of the board that may be represented by proxy access nominees. CII's proxy access best practices disfavor any percentage maximum which results in less than 2 nominees.

- Nominating Shareholder Groups. Shareholder proposals submitted to issuers during the 2015 proxy season did not usually contemplate limitations on the number of shareholders who could aggregate their holdings to meet minimum ownership requirements. Recently adopted bylaw provisions have tended to include a limitation on the aggregation by up to 20 eligible shareholders to meet the 3%-for-3 years ownership threshold.

- Treatment of Loaned Shares. Consistent with the CII's best practices, many proxy access bylaws include provisions which treat loaned shares as continuously owned for the purposes of the 3-year ownership requirement, provided that the nominating shareholder has the right to recall the loaned shares and does so as of the date of the nomination notice, when the nominating shareholder is notified that the nominees will be included in the proxy materials, or in time to vote the securities at the meeting.

- Nominee Compensation. Also consistent with CII's best practices, many proxy access bylaws tend to allow proxy access nominees to have some form of compensation arrangement with a third party for serving as a director of the issuer, provided that such compensation arrangements are disclosed. Again, these provisions appear to be bringing adopted proxy access bylaw provisions more in line with the CII's best practices.
- Proxy Access Nominees. Issuers are taking varied approaches to incumbent proxy access nominees, as well as restrictions on the eligibility of repeat nominating shareholders. In many cases, incumbent proxy access nominees will continue to count against the maximum number of permitted proxy access nominees. Some proxy access bylaws include a restriction that would prevent a shareholder (or group) from nominating further proxy access nominees for at least two or three years if that shareholder (or group) already has a proxy access nominee serving on the board. In another example of evolving practice, a significant number of proxy access bylaw provisions would exclude nominees who received less than a certain level of support in a prior meeting during a period of up to two years. CII's best practices oppose any restriction on re-nomination due to the outcome of a prior vote.
- Other Terms. Some other relevant terms include director qualifications, a prohibition on nominating other nominees by the nominating shareholder, a prohibition on engaging in any sort of solicitation for any other shareholder nominee, a prohibition on entering into voting commitments or entering into voting commitments without disclosure, and a prohibition on using the issuer's proxy statement if the issuer receives notice that the shareholder intends to nominate a candidate at the issuer's annual meeting.

Key Proxy Adviser Voting Guidelines For 2016

The proxy advisory firms Glass Lewis and ISS released the 2016 updates to their U.S. proxy voting guidelines. These updates do not reflect major revisions to policies, but rather reflect changes to specific areas of concern for the proxy advisory services and their institutional investor clients.

Glass Lewis Updates

Glass Lewis updated its 2016 proxy voting guidelines with the following notable changes:

Conflicting Management and Shareholder Proposals. When analyzing and

determining whether to support conflicting management and shareholder proposals, Glass Lewis indicated that it will consider the following:

- The nature of the underlying issue;
- The benefit to shareholders for implementation of the proposal;
- The materiality of the differences between the terms of the shareholder proposal and management proposal;
- The appropriateness of the provisions in the context of a company's shareholder base, corporate structure and other relevant circumstances; and
- An issuer's overall governance profile and, specifically, its responsiveness to shareholders as evidenced by an issuer's response to previous shareholder proposals and its adoption of progressive shareholder rights provisions.

Exclusive Forum Provisions. In its revised policies, Glass Lewis refined its approach to issuers that include exclusive forum provisions in their governing documents in connection with an initial public offering. Specifically, Glass Lewis will no longer recommend that shareholders vote against the chairman of the nominating and governance committees in such situations, but instead, for new public issuers, will weigh the presence of an exclusive forum provision in the bylaws in conjunction with other provisions that it believes will unduly limit shareholder rights. Such provisions include supermajority vote requirements, a classified board or a fee-shifting bylaw provision. However, Glass Lewis's policy to recommend voting against the chairman of the nominating and governance committee when an issuer adopts an exclusive forum provision without shareholder approval outside of a spin-off, merger or IPO will not change.

Environmental and Social Risk Oversight. Glass Lewis codified its policy regarding the responsibilities of a board of directors for oversight of environmental and social issues. In cases where the board or management, in Glass Lewis's view, has failed to sufficiently identify and manage a material environmental or social risk that did or could negatively impact shareholder value, Glass Lewis will recommend shareholders vote against directors responsible for risk oversight in consideration of the nature of the risk and the potential effect on shareholder value.

Nominating Committee Performance. Glass Lewis revised its guidelines to clarify that it may consider recommending shareholders vote against the chair of the

nominating committee where the board's failure to ensure the board has directors with relevant experience, either through periodic director assessment or board refreshment, has contributed to a company's poor performance.

Director Overboarding. Glass Lewis noted that, in 2016, it will closely review director board commitments and may note as a concern instances of directors serving on more than five total boards, for directors who are not also executives, and more than two total boards for a director who serves as an executive of a public issuer.

Glass Lewis's voting recommendations in 2016, however, will continue to be based on the firm's existing thresholds of three total boards for a director who serves as an executive of a public issuer, and six total boards for directors who are not public issuer executives.

Glass Lewis indicated that, beginning in 2017, it generally will recommend voting against a director who serves as an executive officer of any public issuer while serving on a total of more than two public issuer boards, and any other director who serves on a total of more than five public issuer boards.

ISS Updates

ISS released its voting policy changes for 2016, which are effective for shareholder meetings taking place on or after February 1, 2016. Among the notable changes to the guidelines included:

Director Overboarding. Current ISS policy considers a director "overboarded" if he or she sits on more than six public issuer boards—or, if he or she is also a CEO, more than two public issuer boards (not counting subsidiaries of the CEO's "home board"). In its updated policy, ISS noted that, for most directors except for standing CEOs, the maximum number of public issuer boards that a director can sit on before being considered "overboarded" is being reduced from six to five. ISS will allow a one-year grace period until 2017, giving directors and issuers sufficient time to make any changes in advance of the 2017 proxy season, should they wish to do so. During 2016, ISS will highlight if a director is on more than five public issuer boards, but adverse voting recommendations will not be issued under this new overboarding policy unless the current policy's maximum of six boards is exceeded. For CEOs, the current overboarding limit will remain at two outside directorships. ISS revised its policy in light of the increasing demands on public issuer directors over the decade since its prior framework was first developed.

Unilateral Board Actions. When a unilateral board amendment of the articles or bylaws adversely affects shareholder rights, current ISS policy provides for adverse vote recommendations on individual directors or the full board at the next annual meeting. Unilateral board actions many include, among other things, “classifying the board” or “establishing supermajority vote requirements for bylaw/charter amendments.”

ISS has updated its policy to distinguish between (i) unilateral board adoptions of bylaw or charter provisions made prior to or in connection with an issuer’s initial public offering (IPO); and (ii) unilateral board amendments to those documents made after an issuer’s IPO. For newly public issuers that have taken action to diminish shareholder rights prior to or in connection with the IPO, the updated policy calls for a case-by-case approach to withhold votes in subsequent years, with significant weight given to shareholders’ ability to change the governance structure in the future through a simple majority vote, and their ability to hold directors accountable through annual director elections. A public commitment by the issuer to put the adverse provisions to a shareholder vote within three years of the IPO can be a mitigating factor.

For established public issuers, ISS’s updated policy generally calls for continuing to withhold votes from directors who have unilaterally adopted a classified board structure, implemented supermajority vote requirements to amend the bylaws or charter, or eliminated shareholders’ ability to amend the bylaws altogether.

Compensation of Externally Managed Issuers. ISS had not historically considered insufficient disclosure of compensation arrangements for executives at an externally managed issuer as a problematic pay practice under ISS policy.

ISS had revised its policy to provide that an externally managed issuer’s failure to provide sufficient disclosure for shareholders to reasonably assess compensation for the named executive officers will be deemed a problematic pay practice, and generally warrant a recommendation to vote against the say-on-pay proposal.

Proxy Access. ISS has not revised its fundamental approach to management and shareholder proposals to adopt proxy access and ISS will continue to vote case-by-case for each director on the ballot in the case of a proxy contest or proxy access, considering a variety of factors.

In updated Frequently Asked Questions published on December 18, 2015, ISS provided further guidance on its approach to proxy access proposals and proxy access nominees. Under ISS’s Board Responsiveness policy guidelines, ISS will evaluate a

board's response to a majority supported shareholder proposal for proxy access by examining whether the major points of the shareholder proposal are being implemented. Further, ISS will examine additional provisions that were not included in the shareholder proposal in order to assess whether such provisions unnecessarily restrict the use of a proxy access right. Any vote recommendations driven by a board's implementation of proxy access may pertain to individual directors, nominating/governance committee members, or the entire board, as appropriate.

ISS may issue an adverse recommendation if a proxy access policy implemented or proposed by management contains material restrictions more stringent than those included in a majority-supported proxy access shareholder proposal with respect to the following, at a minimum:

- Ownership thresholds above three percent;
- Ownership duration longer than three years;
- Aggregation limits below 20 shareholders;
- A cap on nominees below 20 percent of the board.

In instances where the cap or aggregation limit differs from what was specifically stated in the shareholder proposal, the lack of disclosure by the issuer regarding shareholder outreach efforts and engagement may also warrant negative vote recommendations.

If an implemented proxy access policy or management proxy access proposal contains restrictions or conditions on proxy access nominees, ISS will review the implementation and restrictions on a case-by-case basis. Restrictions that would be viewed as problematic include:

- Prohibitions on resubmission of failed nominees in subsequent years;
- Restrictions on third-party compensation of proxy access nominees;
- Restrictions on the use of proxy access and proxy contest procedures for the same meeting;
- How long and under what terms an elected shareholder nominee will count towards the maximum number of proxy access nominees; and

- When the right will be fully implemented and accessible to qualifying shareholders.

ISS considers two types of restrictions to be especially problematic, because they are so restrictive as to effectively nullify the proxy access right:

- Counting individual funds within a mutual fund family as separate shareholders for purposes of an aggregation limit; and
- The imposition of post-meeting shareholding requirements for nominating shareholders.

Recognizing the differences between evaluating a candidate in a proxy access situation as compared to a proxy contest situation, ISS has created additional analytical latitude for evaluating candidates nominated through proxy access. When evaluating proxy access candidates, ISS will consider, among other factors:

- Nominee/Nominator specific factors:
  - Nominators' rationale;
  - Nominators' critique of management/incumbent directors; and
  - Nominee's qualifications, independence, and overall fitness for directorship.
- Issuer specific factors:
  - Issuer performance relative to its peers;
  - Background to the contested situation (if applicable);
  - Board's track record and responsiveness;
  - Independence of directors/nominees;
  - Governance profile of the company;
  - Evidence of board entrenchment;
  - Current board composition (skill sets, tenure, diversity, etc.); and
  - Ongoing controversies, if any.

- Election specific factors:
  - Whether the number of nominees exceeds the number of board seats; and
  - Vote standard for the election of directors.

Hedging and Pledging Policies

Over the past few years, considerable attention has been focused on policies addressing the hedging and pledging of securities by an issuer's employees, executives and directors. In particular, significant market volatility has brought to light some key issues arising from the pledging of issuer securities by employees, executives and directors of issuers, including concerns as to whether an individual's interests remain aligned with shareholders through his or her pledging of equity awards or other shares owned to secure loans. Similar concerns have been raised with regard to hedging and monetization arrangements, where employees, executives or directors may seek to continue to own issuer securities obtained through the company's benefit plans or otherwise, but without the full risks and rewards of ownership.

Background

Hedging or monetization transactions can be accomplished through a number of possible mechanisms, including, but not limited to, through the use of financial instruments such as exchange funds, prepaid variable forwards, equity swaps, puts, calls, collars, forwards and other derivative instruments, or through the establishment of a short position in the issuer's securities. In addition, individuals may seek to secure loans by pledging the issuer's stock as collateral for the loan, including through the use of traditional margin accounts with a broker. Because securities held in a margin account as collateral for a margin loan may be sold by the broker without the customer's consent if the customer fails to meet a margin call, and securities pledged (or hypothecated) as collateral for a loan may be sold in foreclosure if the borrower defaults on the loan, significant concerns have been raised when the margin sale or foreclosure sale may occur at a time when the pledgor is aware of material nonpublic information or otherwise is not permitted to trade in the issuer's securities. The issuer may also face potentially adverse public perceptions when employees, executives and directors engage in these types of transactions.

Regulatory Developments

The Dodd-Frank Act directed the SEC to adopt rules requiring disclosure of whether any employee or director is permitted to purchase financial instruments that

are designed to hedge or offset any decrease in the market value of equity securities granted as compensation or held directly or indirectly by the employee or director. While the SEC has not yet adopted rules implementing this directive, public companies have felt pressure from institutional investors and proxy advisory firms to disclose the issuer's policies about hedging and monetization transactions. Meanwhile, the SEC first required disclosure of shares pledged by the highest paid executive officers and the company's directors beginning in 2006, focusing additional attention on these arrangements in the context of an issuer's overall corporate governance and compensation policies and practices.

ISS Policy

ISS adopted policy changes for the 2013 proxy season that focused additional attention on pledging and hedging activities when ISS is conducting its analysis for determining vote recommendations on the election of directors. This policy change reflected the results of ISS's 2012-13 policy survey, where 49% of institutional respondents and 45% of company respondents indicated that any pledging of issuer stock by executive officers or directors is significantly problematic. ISS takes a case-by-case approach in determining whether pledging of company stock rises to a serious concern for shareholders, and has included significant pledging of issuer stock as a failure of risk oversight for which directors should be held accountable (as opposed to as a consideration relevant to making a recommendation on a say-on-pay proposal). In determining vote recommendations for the election of directors at companies who currently have executives or directors with pledged common stock, ISS considers the following factors: (i) the presence in the issuer's proxy statement of an anti-pledging policy that prohibits future pledging activities; (ii) the magnitude of aggregate pledged shares in terms of the total common shares outstanding or the market value or trading volume of the common stock; (iii) disclosure of progress (or lack thereof) in reducing the magnitude of aggregate pledged shares over time; (iv) disclosure in the proxy statement that stock ownership or holding requirements do not include pledged company stock; and (v) any other relevant factors. With regard to hedging, the updated policy notes that hedging company stock "severs the ultimate alignment with shareholders' interests," therefore *any* amounts hedged will be considered a problematic practice potentially warranting a negative voting recommendation on the election of directors.

Adopting or Revisiting Policies

The increasing level of disclosure, the heightened investor scrutiny and the consideration accorded by proxy advisory firms has caused many issuers to adopt policies about hedging, monetization or pledging transactions, or revisit existing policies to

consider whether the scope or coverage of such policies should be changed. The options that issuers have pursued include:

- Prohibiting hedging, monetization and/or pledging transactions for executive officers and directors, or perhaps even for all employees and directors;
- Subjecting hedging, monetization and/or pledging transactions to a pre-approval process;
- Restricting the types of hedging, monetization and/or pledging transactions that may be undertaken; or
- Permitting hedging, monetization or pledging transactions without any specific policy on their use.

The variation in approaches reflects how situations differ substantially from company to company, and from individual to individual. In some cases, hedging, monetization or pledging transactions may serve legitimate tax planning or other purposes, thereby making a complete prohibition on such transactions unworkable. For this reason, some issuers have chosen to address the situation though a pre-clearance process, which provides compliance personnel within the organization the ability to carefully analyze a transaction before an individual proceeds with the transaction. Other issuers may choose to restrict only certain types of transactions, particularly where it is perceived that the risks to the company and the participating individuals may be high.

Another key area of consideration is the extent of coverage for these policies. The Dodd-Frank Act disclosure requirement will seek disclosure with respect policies concerning *all* employees and directors, while in many cases issuers have adopted policies that are specifically limited to the issuer's executive officers and directors. Issuers are often concerned that adopting policies broadly applicable to all employees and directors may be difficult to communicate and enforce.

Some issuers have also sought to extend prohibitions to other types of short-term or speculative transactions, such as trading in exchange traded puts and calls on the issuer's securities, or short-term trading transactions (i.e., buying and selling the issuer's securities within six months).

Location of Policies

Very often, policies with regard to hedging, monetization or pledging are included in an issuer's insider trading policy. Some issuers have adopted standalone policies addressing some or all of these topics, while others have incorporated these concepts into the issuer's code of conduct, stock ownership guidelines and corporate governance guidelines.

Conclusion

With the advent of advisory votes on executive compensation and increased disclosure regarding a wide variety of "hot button" issues for shareholders, we will continue to see issuers adopting or revisiting their policies concerning hedging, monetization and/or pledging transactions.

FORM OF HEDGING AND PLEDGING POLICY

[Note: This policy may be incorporated into other policies of the company, such as the insider trading policy]

Introduction

Hedging or monetization transactions can be accomplished through a number of possible mechanisms, including, but not limited to, through the use of financial instruments such as exchange funds, prepaid variable forwards, equity swaps, puts, calls, collars, forwards and other derivative instruments, or through the establishment of a short position in the Company's securities. Such hedging and monetization transactions may permit an [employee,] officer or director to continue to own the securities of [Company Name] (the "Company") obtained through Company's benefit plans or otherwise, but without the full risks and rewards of ownership. When that occurs, the director, officer or employee may no longer have the same objectives as the Company's other stockholders. Moreover, certain short-term or speculative transactions in the Company's securities by [employees,] officers and directors create the potential for heightened legal risk and/or the appearance of improper or inappropriate conduct involving the Company's securities.

Objectives

The objectives of this Policy are to: (1) prohibit the Company's [employees,] officers and directors from directly or indirectly engaging in hedging or monetization trans-

actions, through transactions in the Company's securities or through the use of financial instruments designed for such purpose; and (2) prohibit [employees,] officers and directors from engaging in short-term or speculative transactions in the Company's securities that could create heightened legal risk and/or the appearance of improper or inappropriate conduct by the Company's employees, officers or directors.

Applicability

This policy applies to all of the Company's [employees,] officers and directors. The Board of Directors may determine whether the policy should apply to other individuals, including consultants and contractors to the Company.

Policy

The Company's [employees,] officers and directors may not engage in any hedging or monetization transactions with respect to the Company's securities, including, but not limited to, through the use of financial instruments such as exchange funds, prepaid variable forwards, equity swaps, puts, calls, collars, forwards and other derivative instruments, or through the establishment of a short position in the Company's securities. Further, the Company's [employees,] officers and directors may not engage in the following in short-term or speculative transactions in the Company's securities that could create heightened legal risk and/or the appearance of improper or inappropriate conduct by the Company's employees, officers or directors:

- *Short-Term Trading.* Short-term trading of the Company's securities may be distracting to the person and may unduly focus the person on the Company's short-term stock market performance, instead of the Company's long-term business objectives. For these reasons, any [employee,] officer or director of the Company who purchases the Company's securities in the open market may not sell any Company securities of the same class during the six months following the purchase (or vice versa).
- *Short Sales.* Short sales of the Company's securities (*i.e.,* the sale of a security that the seller does not own) may evidence an expectation on the part of the seller that the securities will decline in value, and therefore have the potential to signal to the market that the seller lacks confidence in the Company's prospects. In addition, short sales may reduce a seller's incentive to seek to improve the Company's performance. For these reasons, short sales of the Company's securities by [employees,] officers or directors are

prohibited. Short sales arising in certain types of hedging transactions are governed by this Policy's prohibition on hedging transactions, as described above.

- *Publicly-Traded Options.* Given the relatively short term of publicly-traded options, transactions in options may cause an [employee,] officer or director to focus on short-term performance at the expense of the Company's long-term objectives. Accordingly, this Policy prohibits transactions by [employees,] officers or directors in put options, call options or other derivative securities related to the Company's securities, on an exchange or in any other organized market. Transactions in options arising in certain types of hedging transactions are governed by this Policy's prohibition on hedging transactions, as described above.

Margin Accounts and Pledged Securities. Securities held in a margin account as collateral for a margin loan may be sold by the broker without the customer's consent if the customer fails to meet a margin call. Similarly, securities pledged (or hypothecated) as collateral for a loan may be sold in foreclosure if the borrower defaults on the loan. Because a margin sale or foreclosure sale may occur at a time when the pledgor is aware of material nonpublic information or otherwise is not permitted to trade in the Company's securities, [employees,] officers and directors are prohibited from holding the Company's securities in a margin account or otherwise pledging the Company's securities as collateral for a loan. Pledges of Company Securities arising from certain types of hedging transactions are governed by this Policy's prohibition on hedging transactions, as described above. [An exception to this prohibition may be granted where a person covered by this Policy wishes to pledge the Company's securities as collateral for a loan (not including margin debt) and clearly demonstrates the financial capacity to repay the loan without resort to the pledged securities. Any person seeking an exception from this policy must submit a request for pre-approval to the [designated Compliance Officer] at least two weeks prior to the contemplated transaction and the person should be advised that any sale of stock by the pledgee will be deemed a sale by the pledgor for purposes of the short-swing profit recovery provisions of Section 16 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the prohibition on insider trading in Rule 10b-5 under the Exchange Act.]

CHAPTER 5

FREQUENTLY ASKED QUESTIONS ABOUT SHAREHOLDER PROPOSALS AND PROXY ACCESS

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Shareholder Proposals

Shareholder proposals are matters that shareholders of an issuer seek to have acted on at an annual or other meeting of the issuer. In accordance with the requirements specified in state corporation laws and in an issuer's organizational documents, a shareholder could seek to have a matter voted on by raising the matter at a meeting of shareholders. Alternatively, a qualifying shareholder could seek to include the proposal in the issuer's proxy statement under Rule 14a-8 adopted under Section 14(a) of the Exchange Act, and thereby have the issuer solicit proxies with respect to the proposal that would be presented at the meeting. The following Questions and Answers address many of the common issues that arise with regard to shareholder proposals and proxy access.

Shareholder Proposals Generally

Who submits shareholder proposals to companies?

Shareholder proposals come from a wide variety of shareholders, sometimes referred to as "proponents." Shareholder proponents may be individual investors who are seeking to raise a particular issue or implement a policy at an issuer, corporate "gadflies" who seek to bring about changes to corporate activity through the shareholder proposal process, activist investors who are seeking to bring about a change-in-control or a change in the strategy or policies of the company, and institutional investors who may be focused on particular corporate governance or social issues.

Who regulates the shareholder proposal process?

The SEC has adopted Rule 14a-8 as a means to control the process whereby proponents seek to have shareholder proposals included in the proxy statements of issuers, and the SEC Staff is involved in considering the arguments of companies that seek to exclude shareholder proposals based on the operation of Rule 14a-8 through a process whereby companies typically seek a "no-action letter" from the Staff with regard to whether the company may exclude the shareholder proposal. Under Rule 14a-8, an issuer must include a shareholder proposal in its proxy materials unless it violates one of the rule's eligibility and procedural requirements or falls within one of the rule's thirteen substantive bases for exclusion.

The Scope of Rule 14a-8

Does Rule 14a-8 require that all shareholder proposals be included in an issuer's proxy statement?

Under Rule 14a-8, an issuer must include a shareholder proposal in its proxy materials unless it violates one of the rule's eligibility and procedural requirements, or one of the thirteen substantive bases for exclusion specified in the rule.

What are the eligibility and procedural requirements for shareholder proposals under Rule 14a-8?

Rule 14a-8 imposes several eligibility and procedural requirements on shareholders who rely on the rule. A shareholder may only submit one proposal per meeting, must own at least $2,000 or 1% of securities entitled to vote on the proposal and must limit its proposal to 500 words. A shareholder must submit the proposal at least 120 days before the date of the issuer's proxy statement for the previous year's annual meeting (or a reasonable time before the issuer begins to print and mail its proxy materials if the issuer did not have an annual meeting during the previous year, or if the date of the annual meeting has been changed by more than 30 days from the date of the previous year's annual meeting). An issuer that intends to rely on the rule to exclude a proposal must submit its "no-action" request 80 days in advance of the date that it proposes to file its definitive proxy materials.

What are the substantive requirements under Rule 14a-8?

Under paragraph (i) of Rule 14a-8, an issuer may exclude a shareholder proposal from its proxy materials if the proposal falls into one of thirteen specific substantive bases for exclusion. These substantive bases represent areas that the SEC has determined over the years to not be appropriate matters for consideration by shareholders through the shareholder proposal process. To exclude a proposal, an issuer must first notify the SEC, which is typically done through a request for a "no-action" letter. In the no-action letter request, an issuer may argue that the subject shareholder proposal can be excluded under more than one basis for exclusion.

How does the no-action letter process work with respect to shareholder proposals?

The central component of the Rule 14a-8 process is the no-action letter. A no-action letter is a letter from the Staff that provides the Staff's informal view regarding whether it would recommend enforcement action to the SEC if the issuer takes the course of action described in the no-action request. No-action letters reflect the Staff's

views concerning the application of securities laws to a particular set of facts. In the context of Rule 14a-8, no-action letters often serve as a key hurdle for shareholders that hope to include a proposal in an issuer's proxy materials.

There is no rule that requires the submission of no-action requests, nor is there a rule that requires that the Staff respond to such requests. Issuers submit requests to comply with Rule 14a-8(j), which requires that issuers "file their reasons" with the SEC. The Staff responds to such requests as a convenience to both issuers and shareholders, and in order to assist both issuers and shareholders in complying with the proxy rules. While the Staff's no-action letters typically address whether the issuer has a basis to exclude the proposal, there also may be times when the Staff will say that there appears to be some basis for the issuer's objection, but the problem can be cured if the proponent changes the proposal in some specific way, for example, the proponent makes a mandatory proposal into a nonbinding proposal, or deletes certain words or sentences in the proposal to avoid vagueness.

Some issuers have elected to submit a notice to the SEC of the company's intention to exclude the proposal, and then file suit in federal court seeking a declaratory judgment as to whether the proposal may be excluded under Rule 14a-8(i)(8).

The Eligibility and Procedural Requirements of Rule 14a-8

What are the requirements as to ownership for submitting shareholder proposals?

A shareholder proposal may be submitted under Rule 14a-8 by a proponent who has held at least $2,000 worth of the issuer's stock (or 1% of the shares eligible to vote, whichever figure is smaller) continuously for at least one year before the date the proposal is submitted to the issuer. Further, the proponent must hold the securities through the date of the annual meeting.

How does a proponent demonstrate that the ownership requirements have been satisfied?

Under Rule 14a-8(b), at the time a shareholder submits a proposal, the shareholder must prove eligibility by being a record holder of the securities that the issuer could verify on its own, or by submitting either:

- A written statement from the record holder of the securities (usually a broker or bank that is a DTC participant) verifying that, at the time the shareholder submits the proposal, the shareholder continuously held at least $2,000 in market value or 1% of the company's securities entitled to vote on the pro-

posal at the meeting for at least one year by the date the shareholder submitted the proposal; or

- A copy of a Schedule 13D, Schedule 13G, Form 3, Form 4, Form 5, or amendments to those documents or updated forms, reflecting the shareholder's ownership of the shares as of or before the date on which the one-year eligibility period begins.

Rule 14a-8(b)(2)(i) provides that, in addition to the proof of ownership, "You [the shareholder proponent] must also include your own written statement that you intend to continue to hold the securities through the date of the meeting of shareholders."

What must a proponent submit if the proponent is not the record holder of the securities?

Usually, a proponent would submit a written statement from the "record" holder of the securities (usually a broker or bank that is a DTC participant) verifying that, at the time the shareholder submits the proposal, the shareholder continuously held at least $2,000 in market value or 1% of the company's securities entitled to vote on the proposal at the meeting for at least one year by the date the shareholder submitted the proposal. In Staff Legal Bulletin No. 14F ("SLB 14F"), the Staff clarified that only DTC participants should be viewed as "record" holders of securities that are deposited with DTC. In Staff Legal Bulletin No. 14G ("SLB 14G") the Staff states that "for purposes of Rule 14a-8(b)(2)(i), a proof of ownership letter from an affiliate of a DTC participant satisfies the requirement to provide a proof of ownership letter from a DTC participant."

In accordance with this guidance, a shareholder that owns shares through a broker or bank that is not a DTC participant or an affiliate of a DTC participant must obtain and submit two proof of ownership statements – one from the shareholder's broker or bank confirming the shareholder's ownership and one from the DTC participant or an affiliate of the DTC participant through which the securities are held confirming the ownership of the shareholder's broker or bank.

An issuer that seeks to exclude a shareholder proposal from its proxy materials on the basis of proof of ownership now must take at least the following steps: (i) determine whether the shareholder is a registered shareholder by checking its list of registered shareholders; (ii) review the proof of ownership to see if the bank or broker providing such proof is a DTC participant by comparing such bank or broker's name

against the list of DTC participants; and (iii) notify the shareholder that the person that provided proof of ownership is not a DTC participant and request that the shareholder obtain a second letter demonstrating proof of ownership from the bank or broker that is a DTC participant through which the other bank or broker holds shares.

Is there particular language that a proponent should have its broker or bank use when providing the proof of ownership information?

SLB 14F also suggests that a shareholder proponent use the following format to have its broker or bank provide the required proof of ownership as of the date the shareholder plans to submit the proposal: “As of [date the proposal is submitted], [name of shareholder] held, and has held continuously for at least one year, [number of securities] shares of [company name] [class of securities].” Noting situations where proof of ownership letters that do not verify a proponent’s beneficial ownership for the entire one-year period preceding and including the date the proposal was submitted, as required by Rule 14a-8(b)(1), the Staff made clear in SLB 14G that a notice of defect in these situations would not satisfy the notice requirement unless the notice actually mentions the discrepancy in the period of ownership covered by the proponent’s proof of ownership letter.

How does a proponent determine the market value of the securities held for the purposes of eligibility to submit a proposal under Rule 14a-8?

The Staff noted in Staff Legal Bulletin No. 14 (“SLB 14”) that, in order to determine whether the shareholder satisfies the $2,000 threshold, the Staff looks at whether, on any date within the 60 calendar days before the date the shareholder submits the proposal, the shareholder’s investment is valued at $2,000 or greater, based on the average of the bid and ask prices. If bid and ask prices are not available, then the market value is determined by multiplying the number of securities the shareholder held for the one-year period by the highest selling price during the 60 calendar days before the shareholder submitted the proposal. The Staff notes that a security’s highest selling price is not necessarily the same as its highest closing price.

How many proposals may a shareholder proponent submit?

Under Rule 14a-8(c), a proponent may submit no more than one proposal for a particular shareholders’ meeting.

How long can a shareholder proposal be?

Under Rule 14a-8(d), the proposal, including any accompanying supporting statement, may not exceed 500 words.

The Staff notes, in SLB 14, that any statements which are arguments "in support of the proposal" are considered to be part of the supporting statement, therefore, any title or heading in the proposal meeting that test may be counted toward the 500-word limitation. In general, the reference to a website address does not violate the 500 word limitation by virtue of indirectly including the content of the website in the proposal and supporting statement. In SLB 14, the Staff indicated that it counts a website address as one word for purposes of the 500-word limitation because the Staff does not believe that a website address raises the concern that Rule 14a-8(d) was intended to address.

What is the deadline for submitting a shareholder proposal?

Rule 14a-8(e)(2) requires that proposals for a regularly scheduled annual meeting be received at the issuer's principal executive offices by a date not less than 120 calendar days before the date of the company's proxy statement released to shareholders in connection with the previous year's annual meeting. The deadline for shareholder proposals is included in the issuer's proxy statement, and is determined by (i) starting with the release date disclosed in the previous year's proxy statement; (ii) increasing the year by one; and (iii) counting back 120 calendar days.

Must a proponent or a proponent's designee attend the meeting to present the proposal?

Rule 14a-8(h)(1) requires that the proponent or the proponent's qualified representative attend the shareholders' meeting to present the proposal. Rule 14a-8(h)(3) provides that an issuer may exclude a proponent's proposals for two calendar years if the issuer included one of the proponent's proposals in its proxy materials for a shareholders' meeting, neither the proponent nor the proponent's qualified representative appeared and presented the proposal, and the proponent did not demonstrate "good cause" for failing to attend the meeting or present the proposal.

If a proponent voluntarily provides a written statement evidencing an intention to act contrary to Rule 14a-8(h)(1) and not attend the meeting, Rule 14a-8(i)(3) (discussed below) may serve as a basis for the issuer to exclude the proposal because the proponent's actions are contrary to the proxy rules.

What must a company do if it seeks to exclude a proposal based on the failure of the proponent to meet one these eligibility and procedural requirements?

If a shareholder fails to follow the eligibility or procedural requirements of Rule 14a-8, Rule 14a-8(f) provides that an issuer may exclude a proposal from its proxy materials due to eligibility or procedural defects if (i) within 14 calendar days of receiving the proposal, the company provides the shareholder with written notice of the defect or defects with the proposal, including the time frame for responding; and (ii) the shareholder fails to respond to this notice within 14 calendar days of receiving the notice of the defect or defects, or the shareholder timely responds but does not cure the eligibility or procedural defect(s). If the shareholder does not timely respond or remedy the defect(s) and the issuer intends to exclude the proposal, the issuer must still submit, to the Staff and the shareholder, a copy of the proposal and the reasons for excluding the proposal.

The issuer does not need to provide the shareholder with a notice of defect if the defect cannot be remedied; however, the issuer must still submit its reasons regarding exclusion of the proposal to the Staff and the shareholder. The shareholder may, but is not required to, submit a reply to the Staff with a copy sent to the company.

Under what circumstances must a company accept a revised shareholder proposal?

Under guidance provided in SLB 14F, if a shareholder proponent submits a revised proposal before the issuer's deadline for shareholder proposals, the issuer must accept the revised proposal. If a shareholder submits a revised proposal after the issuer's deadline, the company does not have to accept the revised proposal.

Does the Staff provide responses to no-action requests by e-mail?

The Staff indicated in SLB 14F that it now transmits Rule 14a-8 no-action responses by e-mail to issuers and proponents, provided that they include e-mail addresses for recipients in their correspondence.

Can a no-action letter be withdrawn?

If an issuer determines that it does not want to obtain a Staff response to a pending no-action request, because, for example, the company has negotiated with the proponent to withdraw the proposal or the issuer has elected to include the proposal in its proxy statement, then the issuer should submit a letter to the Staff requesting withdrawal of the no-action request.

The Substantive Bases for Exclusion of Shareholder Proposals Under Rule 14a-8

Rule 14a-8(i)(1) provides that a proposal is excludable when it is not a proper subject for action by shareholders under the laws of the jurisdiction of the issuer's organization. Under what circumstances is this basis for exclusion applicable?

Rule 14-8(i)(1) focuses on proposals that would not be a proper subject for shareholder action. With respect to subjects and procedures for shareholder votes, most state corporation laws provide that a corporation's charter or bylaws can specify the types of proposals that are permitted to be brought before the shareholders for a vote at an annual or special meeting. The SEC indicates that, depending on the subject matter, a proposal that would bind the issuer if approved by shareholders may not be considered proper under state law. Proposals cast as recommendations or requests that the board of directors take specified action, however, are generally considered proper under state law. As a result, the Staff will assume that a proposal drafted as a recommendation or suggestion is proper unless the company demonstrates otherwise. The Staff will let a proponent amend a proposal to make it a "precatory" recommendation if the company objects to the mandatory nature of the proposal.

The Staff has consistently granted no-action relief to corporations under Rule 14a-8(i)(1) where a shareholder proposal mandates action that, under state law, falls within the powers of the board of directors. For example, the Staff has allowed issuers to exclude proposals that would require a board to declassify a staggered board, while the Staff has permitted proposals requesting company "take the steps necessary" to declassify staggered board.

Issuers must provide a supporting opinion of counsel when the reason for exclusion is based on matters of state or foreign law. Further, under a 2007 amendment to Delaware law, the SEC may request a legal interpretation from the Delaware Supreme Court. In June 2008, the SEC certified to the Supreme Court questions about the propriety under state law of a shareholder proposal submitted to CA by the AFSCME pension plan.

Rule 14a-8(i)(2) provides that a proposal is excludable when the proposal would, if implemented, cause the issuer to violate any state, federal or foreign law to which it is subject. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(2) focuses on situations where the implementation of the shareholder proposal would result in a violation of any state, federal or foreign law. Such a

violation could include a violation of applicable corporate law, or it could include the violation of other laws applicable to the company and its operations. For example, the Staff has allowed an issuer exclude a proposal that would require mandatory board retirement age, where doing so would violate a state age discrimination law. A note to Rule 14a-8(i)(2) provides that an issuer cannot exclude a proposal on the basis that it would violate foreign law if compliance with that law would result in violation of state or federal law. As with requests to exclude under Rule 14a-8(i)(1), the Staff will permit a proponent to amend a proposal to make it a "precatory" recommendation if the company objects to the mandatory nature of the proposal as a potential violation of state corporate law.

As with Rule 14a-8(i)(1), companies must provide a supporting opinion of counsel when the reason for exclusion is based on matters of state or foreign law. Further, under a 2007 amendment to Delaware law, the SEC may request a legal interpretation from the Delaware Supreme Court.

Rule 14a-8(i)(3) provides that a proposal is excludable when the proposal or supporting statement is contrary to any of the SEC's proxy rules, including Rule 14a-9, which prohibits materially false or misleading statements in proxy soliciting materials. Under what circumstances is this basis for exclusion applicable?

The Staff has indicated that reliance on Rule 14a-8(i)(3) to exclude or modify a statement may be appropriate where: (i) statements directly or indirectly impugn character, integrity, or personal reputation, or directly or indirectly make charges concerning improper, illegal, or immoral conduct or association, without factual foundation; (ii) the company demonstrates objectively that a factual statement is materially false or misleading; (iii) the resolution contained in the proposal is so inherently vague or indefinite that neither the shareholders voting on the proposal, nor the issuer implementing the proposal (if adopted), would be able to determine with any reasonable certainty exactly what actions or measures the proposal requires – this objection also may be appropriate where the proposal and the supporting statement, when read together, have the same result; and (iv) substantial portions of the supporting statement are irrelevant to a consideration of the subject matter of the proposal, such that there is a strong likelihood that a reasonable shareholder would be uncertain as to the matter on which it is being asked to vote.

By contrast, in Staff Legal Bulletin No. 14B ("SLB 14B"), the Staff indicated that it would not be appropriate for issuer to exclude supporting statement language and/or

an entire proposal in reliance on Rule 14a-8(i)(3) in the following circumstances: (1) the issuer objects to factual assertions because they are not supported; (2) the issuer objects to factual assertions that, while not materially false or misleading, may be disputed or countered; (3) the issuer objects to factual assertions because those assertions may be interpreted by shareholders in a manner that is unfavorable to the company, its directors, or its officers; and/or (4) the company objects to statements because they represent the opinion of the shareholder proponent or a referenced source, but the statements are not identified specifically as such.

Under these standards, a request to exclude a proposal *in its entirety* under Rule 14a-8(i)(3) is unlikely to be granted.

Rule 14a-8(i)(4) provides that a proposal is excludable when the proposal relates to the redress of a personal claim or grievance against the issuer or any other person, or is designed to result in a benefit to the shareholder, or to further a personal interest, which is not shared by the other shareholders at large. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(4) focuses on proposals involving matters that are deemed not to rise to the level that shareholders as a whole should vote on as a shareholder proposal. For example, if a proponent is involved in litigation with the issuer, and the proposal deals with a matter being litigated, that could serve as grounds to exclude the proposal on the theory that the proponent is pursuing its own agenda. The SEC has stated that Rule 14a-8(i)(4) is designed to "insure that the security holder proposal process [is] not abused by proponents attempting to achieve personal ends that are not necessarily in the common interest of the issuer's shareholders generally." *See* SEC Release No. 34-20091 (August 16, 1983).

In considering exclusion requests under Rule 14a-8(i)(4), the Staff often looks to the particular motives of proponent. However, a proponent's particular objectives need not be apparent from a proposal's plain language in order to be excludable under Rule 14a-8(i)(4). Rather, proposals phrased in broad terms that "might relate to matters which may be of general interest to all security holders" may be omitted from proxy materials "if it is clear from the facts…that the proponent is using the proposal as a tactic designed to…further a personal interest." *See* SEC Release No. 34-19135 (October 14, 1982). These types of exclusion requests often involve proposals by disgruntled former employees of a company relating to personal issues that the former employees have with the issuer.

Rule 14a-8(i)(5) provides that a proposal is excludable when the proposal relates to operations that account for less than 5% of the issuer's total assets at the end of its most recent fiscal year, and for less than 5% of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the company's business. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(5) is referred to as the "relevance rule." A significant focus of the Staff is on whether the proposal relates to operations that are "not otherwise significantly related to the company's business." As a practical matter, the Rule 14a-8(i)(5) exclusion has not been frequently raised successfully in recent years, because proponents have been able to frame issues in a way that adequately establishes the significance of an issue, even if the economic impact may be minimal. The SEC stated in SEC Release No. 34-19135 (October 14, 1982):

> Historically, the Commission staff has taken the position that certain proposals, while relating to only a small portion of the issuer's operations, raise policy issues of significance to the issuer's business…For example, the proponent could provide information that indicates that while a particular corporate policy which involves an arguably economically insignificant portion of an issuer's business, the policy may have a significant impact on other segments of the issuer's business or subject the issuer to significant contingent liabilities.

The Staff has typically been relatively permissive when the Rule 14a-8(i)(5) basis for exclusion has been raised by issuers, permitting proposals to be included in proxy statements when they are deemed to be of social or political "significance" and somehow related to the issuer's business, even in some instances where 5% asset and gross sales thresholds were not met.

Rule 14a-8(i)(6) provides that a proposal is excludable when the company would lack the power or authority to implement the proposal. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(6) focuses on proposals requesting that a board of directors do something that it lacks the power or authority to implement. For example, the Staff has allowed exclusion of a proposal that would require an issuer to breach existing contracts; however, the Staff has permitted revisions to such a proposal so that it applied only to future contracts. Further, the Staff has held that Rule 14a-8(i)(6) applies to a

shareholder proposal that, if adopted by the issuer's shareholders, would cause the issuer to violate applicable state law. With respect to shareholder proposals that, if adopted by the issuer's shareholders, would cause the company to violate applicable state law, s*ee Noble Corporation* (January 19, 2007); *SBC Communications Inc.* (January 11, 2004); *Xerox Corp.* (February 23, 2004). As with Rule 14a-8(i)(1) and Rule 14a-8(i)(2), issuers must provide a supporting opinion of counsel when the reason for exclusion is based on matters of state or foreign law. Further, under a 2007 amendment to Delaware law, the SEC may request a legal interpretation from the Delaware Supreme Court.

Rule 14a-8(i)(7) provides that a proposal is excludable when the proposal deals with a matter relating to the issuer's ordinary business operations. Under what circumstances is this basis for exclusion applicable?

The SEC has explained that the analysis under the "ordinary business" exclusion is based on two key considerations. First, certain tasks "are so fundamental to management's ability to run a company on a day-to-day basis that they could not, as a practical matter, be subject to direct shareholder oversight." Examples that the SEC has cited include employee hiring, promotion and termination decisions, decisions on production quality or quantity, or the retention of suppliers. Even so, some proposals "focusing on sufficiently significant social policy issues" (such as employment discrimination policies) transcend day-to-day operational matters and raise issues "so significant" that shareholders should be afforded the opportunity to express their views. The second key consideration relates to "the degree to which the proposal seeks to 'micro-manage' the company by probing too deeply into matters of a complex nature upon which, shareowners, as a group, would not be in a position to make an informed judgment." Examples cited were proposals involving "intricate detail" or seeking to impose "specific timeframes or methods for implementing complex policies."

Most of the no-action letters under Rule 14a-8(i)(7) arise because the fact that a proposal relates to ordinary business matters does not conclusively establish that an issuer may exclude the proposal from its proxy materials. As the SEC stated in SEC Release No. 34-40018 (May 21, 1988), proposals that relate to ordinary business matters but that focus on "sufficiently significant social policy issues would not be considered to be excludable because the proposals would transcend the day-to-day business matters." Among the areas considered to be significant social policy issues are: renewable energy generation; antibiotics in foods; health care reform;

collateralization of derivatives; loan foreclosures; risk oversight; CEO succession planning; executive compensation; auditor rotation; environmental matters; South Africa; Myanmar; human rights; net neutrality; and predatory lending.

Rule 14a-8(i)(8) provides that a proposal is excludable when the proposal relates to an election for membership on the issuer's board of directors or analogous governing body. Under what circumstances is this basis for exclusion applicable?

The SEC adopted amendments to Rule 14a-8 in 2010 in connection with its "proxy access" rulemaking. Rule 14a-11, the SEC's proxy access rule, was vacated, but the amendments to Rule 14a-8(i)(8) recently became effective. Rule 14a-8(i)(8) has permitted the type of "private ordering" for proxy access through the shareholder proposal process that many commenters had supported in the course of the proxy access rulemaking. Under Rule 14a-8(i)(8), as amended, an issuer may not exclude under this basis a shareholder proposal that would amend or request that the issuer consider amending governing documents to facilitate director nominations by shareholders or disclosures related to nominations made by shareholders, as long as such proposal does not conflict with Rule 14a-11 and is not otherwise excludable under some other procedural or substantive basis in Rule 14a-8. The SEC also codified some of the Staff's historical interpretations of Rule 14a-8(i)(8) which permitted exclusion of a shareholder proposal that would: (i) seek to disqualify a nominee standing for election; (ii) remove a director from office before the expiration of his or her term; (iii) question the competence, business judgment, or character of a nominee or director; (iv) nominate a specific individual for election to the board of directors, other than through the Rule 14a-11 process, an applicable state law provision, or an issuer's governing documents; or (v) otherwise affect the outcome of an upcoming election of directors.

Rule 14a-8(i)(9) provides that a proposal is excludable when the proposal directly conflicts with one of the issuer's own proposals to be submitted to shareholders at the same meeting. Under what circumstances is this basis for exclusion applicable?

An issuer may properly exclude a proposal from its proxy materials under Rule 14a-8(i)(9) "if the proposal directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting." Prior to the 2015 proxy season, Rule 14a-8(i)(9) has been used to exclude shareholder proposals addressing topics such as compensation plan provisions, proxy access, shareholders' ability to call a special meeting, and shareholders' ability to take action by written consent. On January 16, 2015, Chair Mary Jo White directed the SEC's Division of Corporation Finance to review the proper scope and application of Rule 14a-8(i)(9), and the Staff

thereafter announced that it would express no view on no-action requests relating to the exclusion of shareholder proposals in reliance on Rule 14a-8(i)(9). Without having the ability to seek the Staff's concurrence to exclude a shareholder proposal based on Rule 14a-8(i)(9), issuers pursued a number of alternative methods for addressing shareholder proposals that conflicted with management proposals. The most common alternative methods were (i) including both the shareholder proposal and the management proposal in the proxy statement, with an explanation to shareholders regarding any differences in scope of applicability and recommending that shareholders vote in favor of the management proposal; and (ii) including only the shareholder proposal, and recommending that shareholders vote against that proposal.

In SLB 14H, the Staff expressed the view that there is a "direct conflict" between a shareholder proposal and management proposal only where "a reasonable shareholder could not logically vote in favor of both proposals, i.e., a vote for one proposal is tantamount to a vote against the other proposal." The Staff noted that this analysis "more appropriately focuses on whether a reasonable shareholder could vote favorably on both proposals, or whether they are, in essence, mutually exclusive proposals." In communicating this interpretation, the Staff focused on the principle that Rule 14a-8(i)(9) is designed to ensure that the shareholder proposal process is not used as a means to circumvent the SEC's proxy rules governing solicitations.

In SLB 14H, the Staff provided the following examples to provide a better understanding of the Staff's focus on "whether a reasonable shareholder could logically vote for both proposals."

- Direct Conflict Exists. The Staff stated that (i) "where a company seeks shareholder approval of a merger, and a shareholder proposal asks shareholders to vote against the merger;" or (ii) "a shareholder proposal that asks for the separation of the company's chairman and CEO would directly conflict with a management proposal seeking approval of a bylaw provision requiring the CEO to be the chair at all times," the Staff "would agree that the proposals directly conflict."
- Direct Conflict Does Not Exist. In illustrating those circumstances in which a direct conflict would not exist for purposes of Rule 14a-8(i)(9), the Staff provided the following examples: (i) "if a company does not allow shareholder nominees to be included in the company's proxy statement, a shareholder proposal that would permit a shareholder or group of shareholders

> holding at least 3% of the company's outstanding stock for at least 3 years to nominate up to 20% of the directors would not be excludable if a management proposal would allow shareholders holding at least 5% of the company's stock for at least 5 years to nominate for inclusion in the company's proxy statement 10% of the directors;" and (ii) "a shareholder proposal asking the compensation committee to implement a policy that equity awards would have no less than four-year annual vesting would not directly conflict with a management proposal to approve an incentive plan that gives the compensation committee discretion to set the vesting provisions for equity awards." The Staff noted that these situations would not present a "direct conflict" because "a reasonable shareholder, although possibly preferring one proposal over the other, could logically vote for both."

With respect to the proxy access example described above, the Staff stated that there would be no direct conflict because "both proposals generally seek a similar objective, to give shareholders the ability to include their nominees for director alongside management's nominees in the proxy statement, and the proposals do not present shareholders with conflicting decisions such that a reasonable shareholder could not logically vote in favor of both proposals." The Staff analyzed the compensation example similarly, stating that "a reasonable shareholder could logically vote for a compensation plan that gives the compensation committee the discretion to determine the vesting of awards, as well as a proposal seeking implementation of a specific vesting policy that would apply to future awards granted under the plan."

The Staff noted that SLB 14H could impose "a higher burden for some companies seeking to exclude a proposal to meet than had been the case under our previous formulation." As a result, issuers may turn to Rule 14a-8(i)(10) in seeking to exclude a shareholder proposal that is very similar to a management proposal or action. Rule 14a-8(i)(10) provides an exclusion from an issuer's obligation to include shareholder proposals from eligible shareholders in the issuer's proxy statement if the issuer's existing policies and practices "substantially implement" the shareholder proposal.

Rule 14a-8(i)(10) provides that a proposal is excludable when the issuer has already substantially implemented the proposal. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(10) permits an issuer to exclude a shareholder proposal from its proxy materials if the issuer has "substantially implemented" the proposal.

Interpreting the predecessor to Rule 14a-8(i)(10), the SEC stated in Release No. 34-12598 (July 7, 1976) that the rule was "designed to avoid the possibility of shareholders having to consider matters which have already been favorably acted upon by the management." To be excluded, the proposal does not need to be implemented in full or exactly as presented by the proponent. Instead, the standard for exclusion is substantial implementation. *See* SEC Release No. 34-40018 (May 21, 1998, *note 30 and accompanying text*); *see also* SEC Release No.34-20091 (August 16, 1983).

The Staff has stated that, in determining whether a shareholder proposal has been substantially implemented, it will consider whether an issuer's particular policies, practices, and procedures "compare favorably with the guidelines of the proposal," and not where those policies, practices, and procedures are embodied. *Texaco, Inc.* (March 28, 1991). The Staff has provided no-action relief under Rule 14a-8(i)(10) where an issuer has satisfied the essential objective of the proposal, even if the issuer (i) did not take the exact action requested by the proponent, (ii) did not implement the proposal in every detail or (iii) exercised discretion in determining how to implement the proposal. *See, e.g.*, *Exelon Corp.* (February 26, 2010); and *Anheuser-Busch Companies, Inc.* (January 17, 2007). In these cases, the Staff concurred with the issuer's determination that the proposal was substantially implemented in accordance with Rule 14a-8(i)(10) when the issuer had taken actions that included modifications from what was directly contemplated by the proposal, including in circumstances when the issuer had policies and procedures in place relating to the subject matter of the proposal, or the company had otherwise implemented the essential objectives of the proposal.

Rule 14a-8(i)(11) provides that a proposal is excludable when the proposal substantially duplicates another proposal previously submitted to the issuer by another shareholder that will be included in the issuer's proxy materials for the same meeting. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(11) creates a means to ensure that only one shareholder proposal relating to substantially the same matter is included in the company's proxy statement. The shareholder proposal that is the first submitted is the one that is included (absent some other basis for exclusion). In this regard, management cannot choose among multiple proposals. Rule 14-8(i)(11) involves three elements: (i) substantially duplicative proposals; (ii) the order in which such proposals were received; and (iii) the inclusion of the first-received proposal in the proxy materials. The purpose of Rule 14a-8(i)(11) is to avoid shareholder confusion and to prevent various proponents from including in proxy materials several versions of essentially the same proposal.

Rule 14a-8(i)(12) provides that a proposal is excludable when the proposal deals with substantially the same subject matter as another proposal or proposals that previously has or have been included in the issuer's proxy materials within a specified time frame and did not receive a specified percentage of the vote. Under what circumstances is this basis for exclusion applicable?

Rule 14a-8(i)(12) operates as follows:

- The issuer should look back three calendar years to see if it previously included a proposal or proposals dealing with substantially the same subject matter. If it has not, Rule 14a-8(i)(12) is not available as a basis to exclude a proposal from this year's proxy materials.
- If it has, the issuer should then count the number of times that a proposal or proposals dealing with substantially the same subject matter was or were included over the preceding five calendar years.
- The issuer should look at the percentage of the shareholder vote that a proposal dealing with substantially the same subject matter received the last time it was included.

Only votes for and against a proposal are included in the calculation of the shareholder vote of that proposal. Abstentions and broker non-votes are not included in this calculation. This basis for exclusion is not frequently utilized because the minimum previous thresholds for support (3%, 6%, or 10%, depending on how frequently the proposal was proposed during previous five calendar years) are so low.

Rule 14a-8(i)(13) provides that a proposal is excludable when the proposal relates to specific amounts of cash or stock dividends. Under what circumstances is this basis for exclusion applicable?

The basis for exclusion in Rule 14a-8(i)(13) is viewed as a function of the board of directors, not shareholders. For example, the Staff has allowed exclusion of a shareholder proposal seeking declaration of a dividend of 75% of earnings per share. Proposals seeking that company's distribute specific amounts of cash or stock dividends have been relatively uncommon in recent years.

Proxy Access

What is "proxy access" or "shareholder access"?

Under the SEC's proxy solicitation rules, only the issuer's director nominees are included in the company's proxy statement and proxy card. If shareholders want to nominate their own candidates, then, in addition to complying with applicable state corporation law and the issuer's charter and bylaws, a nominating shareholder must prepare its own proxy statement and proxy card and conduct its own proxy solicitation for the director candidates. This is referred to as a "proxy contest." The terms "proxy access" or "shareholder access" refers to an alternative approach whereby director nominees from qualifying shareholders must be included in the company's proxy statement and on the issuer's proxy card.

Did the Dodd-Frank Wall Act require that the SEC adopt a proxy access rule?

Section 971 of the Dodd-Frank Act provided the SEC with the authority to promulgate "proxy access" rules, allowing specified shareholders to include director nominees in a company's proxy materials. The Dodd-Frank Act did not prescribe specific standards for these rules, and the SEC had in fact proposed proxy access rules prior to enactment of the Dodd-Frank Act.

Did the SEC adopt a proxy access rule and what is the status of that rule?

The SEC issued final rules facilitating shareholder director nominations on August 25, 2010, and such rules were scheduled to become effective on November 15, 2010. However, the effectiveness of those rules was stayed due to litigation challenging the rules.

Under Rule 14a-11 as adopted by the SEC, qualifying shareholders or groups holding at least 3% of the voting power of an issuer's securities, who had held their shares for at least three years, would have had the right to include director nominees in proxy materials upon meeting certain other requirements. An amendment to Rule 14a-8 provided that issuers may not exclude from their proxy materials shareholder proposals for less restrictive proxy access procedures.

On September 29, 2010, the Business Roundtable and Chamber of Commerce of the United States of America filed a petition with the United States Court of Appeals for the District of Columbia Circuit (the "Court") seeking judicial review of the changes to the SEC's proxy access rule, and on the same day filed with the SEC a request to stay the effective date of Rule 14a-11. On October 4, 2010, the SEC granted

the request for a stay of the Rule 14a-11 and associated rules pending resolution of the petition for review by the Court. On July 22, 2011, the Court vacated Rule 14a-11. The Court held that the SEC was “arbitrary and capricious” in promulgating Rule 14a-11, based principally on the SEC’s failure to adequately address the economic effects of the rule. The Court expressed significant concerns about the conclusions that the SEC reached and the agency’s consideration of comments during the course of the rule-making. The Court did not address the First Amendment challenge to the rule that had been raised by the petitioners.

On September 6, 2011, the SEC issued a statement indicating that it would not seek rehearing of the Court’s decision, nor would it seek Supreme Court review of the decision; however, the Staff would continue to study the viability of a proxy access rule. The statement also indicated that the amendment to Rule 14a-8 referenced above would go into effect when the Court’s mandate was finalized, which occurred on September 14, 2011. As a result, the amendments to Rule 14a-8 (along with other rules adopted in connection with Rule 14a-11) became effective on September 20, 2011, following the SEC’s publication of a notice announcing the effective date of the rule changes.

What changes did the SEC make to the shareholder proposal rule and what is the status of those changes?

The amendments to Rule 14a-8 that the SEC adopted in 2010, which became effective on September 20, 2011, have served to facilitate, the type of “private ordering” for proxy access through the shareholder proposal process that many commenters had supported in the course of the proxy access rulemaking.

Under Rule 14a-8(i)(8), as amended, an issuer may not exclude a shareholder proposal that would amend or request that the issuer consider amending governing documents to facilitate director nominations by shareholders or disclosures related to nominations made by shareholders, as long as such proposal does not conflict with Rule 14a-11 and is not otherwise excludable under some other procedural or substantive basis in Rule 14a-8. The SEC also codified some of the Staff’s historical interpretations of Rule 14a-8(i)(8) which permitted exclusion of a shareholder proposal that would: (i) seek to disqualify a nominee standing for election; (ii) remove a director from office before the expiration of his or her term; (iii) question the competence, business judgment or character of a nominee or director; (iv) nominate a specific individual for election to the board of directors, other than through the Rule 14a-11 process, an applicable state law provision, or an issuer’s governing documents; or (v) otherwise affect the outcome of an upcoming election of directors.

Are there other bases under which companies could exclude a shareholder proposal seeking to establish proxy access at a company?

While the SEC's amendments to Rule 14a-8(i)(8) eliminated one basis to exclude proxy access shareholder proposals, there may be other options for seeking to exclude proxy access shareholder proposals. An issuer could argue (i) that the proposal is contrary to the proxy rules under Rule 14a-8(i)(3), i.e., the resolution contained in the proposal is inherently vague or indefinite; (ii) that by adopting its own proxy access bylaw amendment, the shareholder's proxy access proposal has been "substantially implemented" under Rule 14a-8(i)(10); (iii) the shareholder proposal directly conflicts with a similar company-sponsored proposal under Rule 14a-8(i)(9), however the Staff has recently issued SLB No. 14H which substantially reduced the ability to rely on this basis for exclusion; or (iv) that another basis for exclusion specified in Rule 14a-8(i) applies, based on the specific language of the proposal and the supporting statement or the particular circumstances of the company or the proponent.

Are issuers adopting a proxy access bylaw as a result of the prospect of shareholder proposals seeking to establish proxy access?

Up until the 2015 proxy season, many issuers had been taking a "wait-and-see" approach with respect to amending their bylaws to permit proxy access in order to allow greater flexibility in responding to future shareholder proposals. In November 2014, the Comptroller of the City of New York, on behalf of the New York City pension funds, launched a large-scale campaign for the 2015 proxy season targeting 75 issuers with a proxy access shareholder proposal. The Comptroller's office has indicated this initiative is part of a wider effort to implement universal proxy access through private ordering.

The New York City Comptroller indicated that the 75 Boardroom Accountability Project proposals were submitted to issuers that were selected based on three priority issues: "climate change, board diversity, and excessive CEO pay." Based on that analysis, the proposals were submitted to: (1) 33 carbon-intensive coal, oil and gas, and utility companies; (2) 24 companies with few or no women directors, and little or no apparent racial or ethnic diversity; and (3) 25 companies that received significant opposition to their 2014 say-on-pay votes. The 75 identical precatory proposals submitted by the Comptroller requested that the board of directors adopt, and present for shareholder approval, a bylaw to give shareholders who meet a threshold of owning 3 percent of an issuer's shares continuously for three or more years the right to list their director candidates, representing up to 25 percent of the board, in the issuer's proxy

materials. The proposal contemplated that the nominating shareholder would provide notice to the issuer, within the time specified in the bylaws, and would provide at that time the information required by the bylaws and the SEC's rules about both the director nominee and the nominator. The proposal also contemplated that the nominating shareholder would certify that (1) it will assume liability stemming from any legal or regulatory violation arising out of the nominator's communications with the issuer's shareholders; (2) it will comply with all applicable laws and regulations if it uses soliciting material other than the issuer's proxy materials; and (3) to the best of its knowledge, the required shares were acquired in the ordinary course of business and not to change or influence control of the issuer.

The proposal further provided that the nominating shareholder may submit a 500-word statement in support of the director nominee. The proposal would leave to the board the ability to adopt procedures to deal with whether submissions are timely and adequate, as well as how to prioritize multiple nominees. The proposal's supporting statement was very limited, noting a 2014 CFA Institute study which concluded that proxy access would "benefit both the markets and corporate boardrooms, with little cost or disruption" and has the potential to raise overall US market-capitalization by "up to $140.3 billion if adopted market-wide." The supporting statement also noted that votes for similar proposals averaged 55 percent through September 2014 and similar bylaws have been adopted by Chesapeake Energy, Hewlett Packard, Western Union and Verizon Communications.

During the 2015 proxy season, over 90 proxy access shareholder proposals appeared on ballots, and as of the end of 2015, approximately 100 issuers have adopted some form of proxy access, with much of this momentum prompted by the Boardroom Accountability Project. As the 2016 proxy season approaches, more and more larger issuers have been considering the topic and deciding whether to implement proxy access.

Most proxy access bylaw provisions adopted this year have included a 3% ownership threshold, a 3-year continuous holding period, a 20% nomination limit and a 20 member limit on groups of nominating shareholders. Issuers and shareholders continue to debate a number of other important provisions:

- <u>Maximum number of nominees.</u> The Boardroom Accountability Project shareholder proposal and Rule 14a-11 both contemplated that the maximum number of proxy access nominees would be 25%, but many bylaw provisions include 20% maximum on the percentage of the board that may be

represented by proxy access nominees. CII's proxy access best practices disfavor any percentage maximum which results in less than 2 nominees.

- Nominating Shareholder Groups. Shareholder proposals submitted to issuers during the 2015 proxy season did not usually contemplate limitations on the number of shareholders who could aggregate their holdings to meet minimum ownership requirements. Recently adopted bylaw provisions have tended to include a limitation on the aggregation by up to 20 eligible shareholders to meet the 3%-for-3 years ownership threshold.
- Treatment of Loaned Shares. Consistent with the CII's best practices, many proxy access bylaws include provisions which treat loaned shares as continuously owned for the purposes of the 3-year ownership requirement, provided that the nominating shareholder has the right to recall the loaned shares and does so as of the date of the nomination notice, when the nominating shareholder is notified that the nominees will be included in the proxy materials, or in time to vote the securities at the meeting.
- Nominee Compensation. Also consistent with CII's best practices, many proxy access bylaws tend to allow proxy access nominees to have some form of compensation arrangement with a third party for serving as a director of the issuer, provided that such compensation arrangements are disclosed. Again, these provisions appear to be bringing adopted proxy access bylaw provisions more in line with the CII's best practices.
- Proxy Access Nominees. Issuers are taking varied approaches to incumbent proxy access nominees, as well as restrictions on the eligibility of repeat nominating shareholders. In many cases, incumbent proxy access nominees will continue to count against the maximum number of permitted proxy access nominees. Some proxy access bylaws include a restriction that would prevent a shareholder (or group) from nominating further proxy access nominees for at least two or three years if that shareholder (or group) already has a proxy access nominee serving on the board. In another example of evolving practice, a significant number of proxy access bylaw provisions would exclude nominees who received less than a certain level of support in a prior meeting during a period of up to two years. CII's best practices oppose any restriction on re-nomination due to the outcome of a prior vote.
- Other Terms. Some other relevant terms include director qualifications, a prohibition on nominating other nominees by the nominating shareholder, a

prohibition on engaging in any sort of solicitation for any other shareholder nominee, a prohibition on entering into voting commitments or entering into voting commitments without disclosure, and a prohibition on using the issuer's proxy statement if the issuer receives notice that the shareholder intends to nominate a candidate at the issuer's annual meeting.

APPENDIX A

COMPLIANCE CHECKLIST

SCHEDULE 14A

FOR AN ANNUAL MEETING OF STOCKHOLDERS

January 2016

This checklist is a summary of the proxy rules that are generally applicable to proxy statements for annual stockholder' meetings. This checklist should not replace a careful review of the proxy rules and requirements, including, without limitation, Schedule 14A and Rule 14a-1 through Rule 14b-2 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). References to Items herein are references to Items of Schedule 14A unless otherwise noted, and references to rules herein are references to rules under the Exchange Act unless otherwise noted.

Item 1. Date, Time and Place Information

- The date, time, and place of the annual meeting.
- The complete mailing address of the company's principal offices, including the zip code.
- The approximate date on which the proxy statement and form of proxy are being sent to stockholders must appear on the first page of the proxy statement as delivered to stockholders.
- The deadline for submitting shareholder proposals for inclusion in the company's proxy statement for the following year (calculated according to Rule 14a-8(e)).
- The date after which a notice of shareholder proposal submitted outside the process of Rule 14a-8 is considered untimely.

Item 2. Revocability of Proxy

State whether or not the proxies are revocable. If the right to revoke is limited in any way or subject to compliance with any formal procedures, briefly describe such limitation or procedure.

Item 3. Dissenters' Rights of Appraisal

- Briefly outline the appraisal rights or similar rights of the dissenters with respect to any proposal to be acted on, and indicate the procedures that must be followed by a stockholder, including a deadline, if any, to exercise or perfect such rights.

- Indicate whether a stockholder's failure to vote against a proposal will constitute a waiver of appraisal or similar rights and whether a vote against a proposal will be deemed to satisfy any notice requirements.

Item 4. Persons Making the Solicitation

- State that the company (or its board of directors, on behalf of the company) is soliciting the proxy.
- If any director has informed the company that he or she intends to oppose a proposal, state the name of the director and the proposal at issue.
- State who will pay the costs of solicitation.
- If proxy solicitors are to be used, disclose the material terms of their contract, the anticipated costs, and who is paying the costs.
- If the solicitation is to be made in a manner other than through the mail, describe the methods to be used.
- If the proxy is being filed in connection with a proxy contest by a person in opposition to management's slate, see Item 4(b) for additional disclosure requirements.

Item 5. Interest of Certain Persons in Matters to be Acted Upon

- Briefly describe any substantial interest, direct or indirect, by security holdings or otherwise, of each of the following persons in any matter to be acted upon, other than elections to office:
  - ➢ each person who has been a director or executive officer of the company at any time since the beginning of the last fiscal year;
  - ➢ each nominee for election as a director of the company; and
  - ➢ each associate of any of the foregoing persons.

Item 6. Voting Securities and Principal Holders Thereof

- For each class of voting stock entitled to vote at the meeting, state the number of shares outstanding and the number of votes to which each class is entitled.
- State the record date for the annual meeting.

- If action is to be taken with respect to the election of directors and the stockholders have the right to cumulative voting, state the existence of the rights, briefly describe the rights, and state the conditions to the exercise of the rights.

- If the company has undergone a change of control since the beginning of its last fiscal year, see Item 6(e) for required disclosure.

Security Ownership of Certain Beneficial Owners and Management (Item 403 of Reg. S-K)

The following people must be listed in this table:

- Beneficial owners of more than 5% of any class of voting securities;

- Directors and director nominees; and

- Named executive officers (as defined under Item 402(a)(3)).

The table must include columns listing the following:

- Class of security;

- Name of beneficial owner (and home or business address for 5% shareholders);

- Amount and nature of beneficial ownership;

- Percentage of class owned; and

Any arrangement known to the company, including any pledge of the company's securities, which might result in a change of control must be described. See Item 403(c) of Regulation S-K.

Item 7. Directors and Executive Officers

If action is to be taken with respect to the election of directors, the following information must be included for each director, executive officer, person chosen to become an executive officer and director nominee, using tables where possible (Item 401 of Reg. S-K):

- Name and age;

- All positions and offices held with the company;

- Term of service with the company;

- A brief description of the person's business experience during the past five years, including the name and principal business of employers and whether or not these employers are parents, subsidiaries or affiliates of the company;
- Other public company directorships held or held during the last 5 years;
- A brief description of any arrangement or understanding with any other person by which the director was selected and the identity of such other person;
- Any involvement in certain legal proceedings during the last 10 years, including, without limitation, bankruptcy petitions, criminal convictions, orders limiting business practices or securities law violations among others (see Item 401(f) of Reg. S-K);
- Any material proceedings where any directors, nominees, executive officers or any of their associates is an adverse party to the company or any of its subsidiaries (see Instruction 4 to Item 103 of Reg. S-K);
- If the company has gone public in the last year, additional disclosure may be required for promoters or "control persons" (see Item 401(g) of Reg. S-K*)*; and
- Briefly describe any family relationships between any director, executive officer, person chosen to become an executive officer or director nominee.

Related Person Transactions (see Item 404 of Reg. S-K)

Describe any transaction or series of related transactions, since the beginning of the company's last fiscal year, or any currently proposed transaction, in which the company was or is to be a participant and the amount involved exceeds $120,000 (for smaller reporting companies, the disclosure is required if the transaction amount exceeds the lesser of $120,000 or 1% of the company's total assets, and transactions must be reported for the prior two years), and in which any director, executive officer, person chosen to become an executive officer, director nominee or 5% stockholder (or family member of any of the foregoing) had or will have a direct or indirect material interest. Such description must include the following information regarding the transaction:

- The name of the related person and the basis on which the person is a related person.

- The related person's interest in the transaction, including the related person's position(s) or relationship(s) with, or ownership in, a firm, corporation, or other entity that is a party to, or has an interest in, the transaction.

- The approximate dollar value of the amount involved in the transaction.

- The approximate dollar value of the amount of the related person's interest in the transaction, which shall be computed without regard to the amount of profit or loss.

- In the case of indebtedness, the amount involved in the transaction shall include the largest aggregate amount of principal outstanding during the period for which disclosure is provided, the amount thereof outstanding as of the latest practicable date, the amount of principal paid during the periods for which disclosure is provided, the amount of interest paid during the period for which disclosure is provided, and the rate or amount of interest payable on the indebtedness.

- Any other material information regarding the transaction or the related person in the context of the transaction.

Review and Approval of Related Party Transactions (not required for smaller reporting companies)

- Describe the company's policies and procedures for the review, approval, or ratification of any transaction required to be reported as a related party transaction, such as, among other things:

    ➢ The types of transactions that are covered by such policies and procedures;

    ➢ The standards to be applied pursuant to such policies and procedures;

    ➢ The persons or groups of persons on the board of directors or otherwise who are responsible for applying such policies and procedures; and

- Identify any related party transaction that was required to be reported since the beginning of the company's last fiscal year where such policies and procedures did not require review, approval or ratification or where such policies and procedures were not followed.

Compliance with Section 16(a) of the Exchange Act

- Identify any person required to file reports under Section 16 of the Exchange Act that failed to timely file a report under Section 16 during the last fiscal year, including:
  - ➢ The number of late reports;
  - ➢ The number of transactions that were not timely reported; and
  - ➢ Any known failure to file a required report.

Corporate Governance

- Director Independence (see Item 407(a) of Regulation S-K)
  - ➢ Identify each director and nominee for director that is independent under applicable listing standards (if the company is not listed on an exchange, the definition of independence for any national securities exchange may be used, but the definition used should be noted);
  - ➢ State the total number of board meetings that took place during the last fiscal year;
  - ➢ Name each director who attended less than 75% of the aggregate of (i) the total number of board meetings and (ii) the total number of meetings of committees on which he or she served; and
  - ➢ Describe the company's policy, if any, with respect to board member attendance at annual stockholders' meetings.
- State whether or not the company has the following committees;
  - ➢ Audit committee;
  - ➢ Compensation committee; and
  - ➢ Nominating committee.
- For each of these committees:
  - ➢ Describe briefly the functions performed by the committee;
  - ➢ Identify each committee member, and whether each member is independent under applicable listing standards and heightened standards for audit committee members, if applicable;

- ➢ State whether the committee has a charter, and if so, whether it can be found on the company's website or is otherwise available;
- ➢ State the number of committee meetings held during the last fiscal year; and
- ➢ List the members of the audit committee that qualify as an "audit committee financial expert," (as defined in Item 407(d)(5) of Regulation S-K).

Nominating Committee (see Item 407(c) of Regulation S-K)

- If the company does not have a nominating committee, state the basis for the board's view that it does not need one, and identify each director who participates in the consideration of director nominees.
- If the company has a policy concerning shareholder nominees for director, discuss the material terms of such policy, and the procedures for shareholders who want to nominate a director; if the company has no such policy, state the basis for the board's view that it does not need one.
- Describe the nominating committee's procedures for identifying and evaluating director nominees, and any differences in procedures with respect to shareholder nominees, including any minimum qualifications for serving on the board and how the nominating committee considers diversity in evaluating nominees.
- With regard to each nominee for director (other than current directors or executive officers), disclose the source of the nomination: stockholder, director, CEO, other executive officer, third party search firm, or other source.
- Disclose any fees paid to a third-party search firm.
- If the nominating committee received a shareholder nomination from a stockholder or group of stockholders holding in the aggregate 5% of more of the company's outstanding stock, disclose that fact.

Audit Committee Requirements (see Item 407(d) of Regulation S-K)

Include an Audit Committee Report, stating:

- ➢ Whether the audit committee has reviewed and discussed the audited financials with management;

- Whether the audit committee has discussed with the auditors the matters required to be discussed by Auditing Standard No. 16 as adopted by the Public Company Accounting Oversight Board [which replaced SAS 61 (Codification of Statements of Auditing Standards, AU § 380), as adopted by the Public Company Accounting Oversight Board in Rule 3200T];
- Whether the audit committee has received the required independence-of-auditor letter from the accountants and has had discussions with the accountants regarding their independence;
- Whether the audit committee has recommended to the Board that the audited financials be included in the company's 10-K; and
- The name of each member of the audit committee must be set forth below the report.

Compensation Committee

- Describe the committee's processes and procedures for determining executive compensation, including:
  - The scope of authority of the compensation committee (or persons performing the equivalent functions);
  - The extent to which the compensation committee may delegate any authority, specifying what authority may be so delegated and to whom;
  - The role of executive officers in determining or recommending the amount or form of executive and director compensation; and
  - The role of compensation consultants in determining or recommending the amount or form of executive and director compensation.
- The fees paid to any compensation consultant used by the compensation committee, if the company paid such consultant fees in excess of $120,000 during the last fiscal year for services other than consulting on executive compensation.
- With regard to any compensation consultant identified in response to Item 407(e)(3)(iii) whose work has raised any conflict of interest, disclose the nature of the conflict and how the conflict is being addressed.

- Compensation Committee Interlocks and Insider Participation (see Item 407(e)(4) of Regulation S-K – must be separately captioned)
    - ➢ Identify each person who served on the compensation committee during the last fiscal year who was an employee of the company during the last fiscal year, was ever an officer of the company, or had a relationship during the last fiscal year requiring disclosure under Item 404(a) of Regulation S-K, describing such relationship.
    - ➢ If an executive officer of the company served as a director (or on the compensation committee) of another entity during the past year, and an executive officer of the other entity serves on the company's board or compensation committee, identify the directors and describe the relationships.
- Compensation Committee Report (see Item 407(e)(5) of Regulation S-K – must be separately captioned)
    - ➢ State that the compensation committee has reviewed the CD&A and recommended it for inclusion in the Form 10-K.
    - ➢ The name of each compensation committee member must be set forth below the report.

Shareholder Communications (see Item 407(b) and (f) of Regulation S-K)

- Describe the manner in which stockholders may send communications to members of the board.
- If company does not have a process for stockholders to communicate with the board, explain why.
- If all security holder communications are not sent directly to board members, describe the company's process for determining which communications will be relayed to board members.

Board Leadership and Role in Risk Oversight (*see Item 407(h) of Regulation S-K)*

- Disclose whether the same person serves as CEO and board chairman.
- Describe why the company has chosen to combine or separate the CEO and board chairman positions, as well as the reasons why the company

believes that this board leadership structure is the most appropriate structure for the company at the time of the applicable filing.

- Where there is a combined CEO and board chairman but also a lead independent director, disclose whether and why the company has a lead independent director and the specific role that the lead independent director plays in the leadership of the company.
- Disclose the extent of the board's role in risk oversight.
  - ➢ Disclose the effect that the board's role in the oversight of risk has on the leadership structure.

Item 8. Compensation of Directors and Executive Officers

Furnish the following information if action is to be taken with respect to (a) the election of directors; or (b) any compensation plans in which executive officers or directors participate.

The compensation disclosure required by Item 8 is extensive and detailed. A high level summary of the requirements is below, however we strongly advise you to consult Item 402 of Regulation S-K for the specific disclosure requirements (smaller reporting companies and emerging growth companies have scaled reporting requirements which are set forth in Items 402(l) – (r)).

- Compensation Discussion and Analysis
  - ➢ Objectives of the company's compensation program;
  - ➢ What the compensation program is designed to reward;
  - ➢ Each element of compensation;
  - ➢ Why the company chooses to pay each element;
  - ➢ How the company determines the amount (and, where applicable, the formula) for each element;
  - ➢ How each element and the company's decisions regarding that element fits into the overall compensation objectives and affects decisions regarding other elements; and
  - ➢ Whether, and if so, how, the company has considered the results of the most recent shareholder advisory vote on executive compensation (as required by Section 14A of the Exchange Act or

Exchange Act Rule 14a-20) in determining compensation policies and decisions and, if so, how that consideration has affected the company's compensation decisions and policies.

- Summary Compensation Table
- Grants of Plan-Based Awards Table
- Narrative Disclosure to the Summary Compensation Table and the Grants of Plan-Based Awards Table – Describe material factors necessary to understand tables, including:
    - ➢ Material terms of each named executive officer's employment arrangements, whether written or unwritten;
    - ➢ Material modifications to options or other equity-based awards, including repricings;
    - ➢ Material terms of any plan-based award disclosed in the tables, including formulas to be applied in determining amounts and vesting schedules; and
    - ➢ An explanation of the amount of salary and bonus in proportion to total compensation.
- Outstanding Equity Awards at Fiscal Year-End Table
- Option Exercises and Stock Vested Table
- Pension Benefits Table
- Nonqualified Deferred Compensation Table
- Potential Payments Upon Termination or Change in Control
    - ➢ Describe and explain the specific circumstances that would trigger payments or other benefits, including perquisites and healthcare benefits;
    - ➢ Describe and quantify estimated payments and benefits;
    - ➢ Describe how payment and benefit levels are determined under various circumstances;
    - ➢ Describe material obligations or conditions to receipt of payments or benefits, e.g., non-compete, non-solicitation or non-disparagement agreements; and
    - ➢ Any other material factors.

- Director Compensation Table
- Narrative to Director Compensation Table – Describe material factors necessary to understand the table, including:
  - ➢ A description of standard compensation arrangements (such as fees for retainer, committee service, service as chairman of the board or a committee, and meeting attendance); and
  - ➢ Whether any director has a different compensation arrangement, identifying that director and describing the terms of that arrangement.
- Narrative of the Company's Compensation Policies and Practices as they Relate to Risk Management
  - ➢ If risks arising from the company's compensation policies and practices for its employees are reasonably likely to have a material adverse effect on the company, disclose the company's policies and practices of compensating its employees, including non-executive officers, as they relate to risk management practices and risk-taking incentives.

Item 9. Independent Public Accountants.

- If the meeting involves (1) election of directors or (2) approval or ratification of the company's accountant, include the following:
  - ➢ The name of the accountant selected or being recommended for approval or ratification;
  - ➢ The name of the accountant for the last fiscal year if different from the accountant being recommended for approval or ratification, or if no accountant is being named for the current year;
  - ➢ Whether or not representatives of the accountant will be present at the annual meeting;
  - ➢ Whether or not the representatives of the accountant will have the opportunity to make a statement at the meeting if they desire to do so; and
  - ➢ Whether or not the representatives of the accountant will be available at the meeting to answer questions.
- If the accountant has changed during the last two years, additional disclosure may be required under Item 9(d).

Accountant Fee Disclosure (see Item 9(e))

- Under the caption "Audit Fees" list the aggregate fees billed by the accountant for the preparation of the annual financials for each of the last two fiscal years and the financials included in the company's 10-Qs for those fiscal years.
- Under the caption "Audit-Related Fees" list the aggregate fees billed for each of the last two fiscal years for assurance and related services by the accountant that are reasonably related to the audit or review of the company's financial statements and are not reported as "Audit Fees."
- Under the caption "Tax Fees" list the aggregate fees billed for each of the last two fiscal years for professional services rendered by the accountant for tax compliance, tax advice, and tax planning and describe the nature of the services provided.
- Under the caption "All Other Fees" list the aggregate fees billed for each of the last two fiscal years by the accountant for all other services not otherwise described and identify the nature of the services provided.
- Describe the audit committee's pre-approval policies and procedures.
- Describe the percentage of services other than Audit Fees that were approved by the audit committee pursuant to the "de minimis" exception in Regulation S-X Rule 2.01(c)(7)(1)(C).
- If more than 50% of the audit work was performed by persons other than the accountant's full-time employees, list the percentage of work done by these people.

Item 10. Compensation Plans.

If any action is to be taken with regard to any compensation plan (cash or noncash) provide the information listed below. If a plan is being amended, provide the information for the amended plan and note any material differences from the existing plan.

- Briefly describe the material features of the plan being acted on, including (i) each class of persons that will be entitled to participate, (ii) the approximate number of people in each class and (iii) the basis for participation.

- Using the form of table specified in Item 10(a)(2)(i), disclose the benefits or amounts under the plan that will be received by or allocated to, subject to shareholder approval, each of the following:
    - ➢ Each named executive officer;
    - ➢ All current executive officers as a group;
    - ➢ All current directors who are not executive officers as a group; and
    - ➢ All employees, including all current officers who are not executive officers, as a group.
- If the plan grants options or warrants disclose:
    - ➢ The title and amount of securities underlying the options or warrants;
    - ➢ The price, expiration date and other material conditions for exercising the options or warrants;
    - ➢ The consideration received or to be received by the company on grant of the options or warrants;
    - ➢ The market value of the securities underlying the options or warrants as of the latest practicable date; and
    - ➢ In the case of options, the federal income tax consequences of the issuance and exercise of the options for the recipient and the company.
- The options received or to be received by the following people must be listed separately:
    - ➢ Each named executive officer;
    - ➢ All current executive officers as a group;
    - ➢ All current directors who are not executive officers as a group;
    - ➢ Each nominee for director;
    - ➢ Each associate of any such director, executive officer or nominee;

  - ➢ Each other person who will receive 5% of the options under the plan; and
  - ➢ All employees, including all current officers who are not executive officers, as a group.

- If the plan is a written, it must be filed as an appendix to the proxy statement in the SEC filing. See Instruction 3 to Item 10. The plan does not need to be included in the printed version of the proxy statement sent to stockholders.
- Equity Compensation Plan Table (Item 10(c) of Schedule 14A and Item 201(d) of Regulation S-K)

Item 21. Voting Procedures.

As to each matter which is to be submitted to a vote of security holders, furnish the following information:

- The vote required for approval or election, other than for the approval of auditors.
- The method by which votes will be counted, including the treatment and effect of abstentions and broker non-votes under applicable state law as well as the company's organizational documents.
- Items 11 through 20 of Schedule 14A set forth disclosure requirements applicable when action is being taken with respect to specific matters such as issuance of securities, modification or exchange of securities, mergers, consolidations or similar matters, restatement of accounts and amendment of charter or bylaws among other matters. Please refer to Items 11 through Item 20 to determine whether those requirements are applicable to your particular circumstances.

Item 23. Delivery of Documents to Security Holders Sharing an Address.

If one annual report, proxy statement or notice of availability of proxy materials is being delivered to multiple stockholders at the same address:

- State that only one annual report, proxy statement or notice of internet availability of proxy materials, as applicable, is being delivered to multiple security holders sharing an address unless the company has received contrary instructions from one of the security holders.

- Promptly deliver a separate copy of the applicable materials, if requested.
- Provide a phone number and mailing address for stockholders to contact if they wish to receive a separate copy of such materials in the future.
- Provide instructions on how stockholders can request delivery of a single copy if they are receiving multiple copies.
- Provide instructions on how a stockholder can request separate copies in the future.

Item 24. Shareholder Approval of Executive Compensation (Item 24 does not apply to emerging growth companies).

Companies that are required to provide any of the separate shareholder votes pursuant to Exchange Act Rule 14a-21 shall disclose:

- That they are providing such vote as required pursuant to Section 14A of the Exchange Act;
- A brief explanation of the general effect of each vote, such as whether each such vote is non-binding;
- Where applicable, the current frequency of advisory votes on executive compensation as required by Exchange Act Rule 14a-21(a) and when the next such shareholder advisory vote will occur.

APPENDIX B

CONFIDENTIAL

[Insert Company Name]
Directors and Officers Questionnaire

Date: ______________________________

Name: ______________________________

This Questionnaire is being furnished to you to obtain information to prepare and file **[the Proxy[1] Statement and an Annual Report on Form 10-K (collectively, the "Annual Report") of [Insert Company Name] (the "Company") with the Securities and Exchange Commission (the "SEC") covering the fiscal year ended [Insert Date of Last Fiscal Year End] ("Fiscal Year [Insert Last Fiscal Year]")] for [Insert Company Name] (the "Company")]**. The Questionnaire will also assist the Company's board of directors in assessing each of its members' independence (as defined by the SEC and **[Nasdaq] [the New York Stock Exchange (the "NYSE")]**). As used in this Questionnaire, the term "Company" includes any *affiliate* of the Company, [including **[Insert Applicable Entities]**]. "You" also refers to any entity on whose behalf you are responding. Certain terms are *italicized,* and definitions of those terms are provided at the end of the Questionnaire.

Important Note**: Please note several of the questions contained in this Questionnaire have changed from prior years as a result of recent SEC rule changes, including changes requiring additional disclosure related to your professional background and compensation.**

Unless otherwise directed, please answer every question. If the Company has completed portions of the Questionnaire on your behalf, please confirm the accuracy of that information. If your answer to a question is "None" or "Not Applicable," please so state. If you do not provide an answer to a question, the Company will assume the answer is "None" or "No," as applicable. Unless otherwise stated, your answers should be given as of the date you sign the Questionnaire. Please note that certain questions are necessarily broad in scope, so if you have doubts regarding whether something should be included in your response please err on the side of over-inclusion. The Company may have additional follow-up questions for you in connection with preparing the Annual Report**.** It is important that you review the draft(s) of the Annual Report that are presented to you to confirm that the information about you is accurate.

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[1] If preparing for Schedule 14C, replace "Proxy" with "Information."

Once you have completed the Questionnaire, please sign it to indicate: (i) your consent for the Company to use the information provided in its Annual Report; (ii) your acknowledgment that material misstatements or omissions in the Annual Report may give rise to civil and criminal liabilities to the Company, each officer and director of the Company signing the Annual Report, the officers providing certifications pursuant to Sections 302 and 906 of the Sarbanes-Oxley Act, and other persons associated with the preparation and filing of the Annual Report; (iii) your agreement to notify the Company of any misstatement of a material fact in the Annual Report, and of the omission of any material fact necessary to make the statements contained in the Annual Report not misleading, promptly after you become aware of any such misstatement or omission; (iv) your agreement to promptly notify the Company of any changes in information provided in the Questionnaire occurring after the date you sign the Questionnaire; and (v) your confirmation that the information contained in the Questionnaire is true and correct, to the best of your knowledge and belief after a reasonable investigation, as of the date you sign the Questionnaire.

Please complete the Questionnaire and return it, along with a copy of your current resume, by **[Insert date—should allow at least two weeks]**. Please return the completed Questionnaire by overnight delivery to **[Insert Address]**, Attention: **[Insert Contact]**. If you have any questions with respect to these matters, please call **[Insert Contact Name]** at **[Insert Telephone Number]**.

THE EXISTENCE AND CONTENTS OF THE QUESTIONNAIRE, AS WELL AS YOUR ANSWERS AND ALL NOTES AND DRAFTS PREPARED BY YOU, ARE CONSIDERED EXTREMELY CONFIDENTIAL AND PROPRIETARY BY THE COMPANY AND SHOULD BE TREATED ACCORDINGLY.

BACKGROUND INFORMATION

QUESTION 1. Name, Birth Date, Address and Telephone Number[2]

(a) Your full name (as it should appear in the Company's Annual Report):

____

(b) Please provide all previous, assumed or fictitious names or aliases:

____

[2] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(a), (b) (c) and instruction thereto.

(c) Your birth date: ____

Business Address:	***Home Address:***
Business Telephone: ( )	***Home Telephone: ( )***
E-Mail Address:	

QUESTION 2. Arrangement for Selection

Is there any *arrangement* between you and any other person(s) pursuant to which you were or are to be selected as a director, nominee for directorship, or officer?[3]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "YES," please describe:

____

____

QUESTION 3. Family Relationships

(a) Is there any "family relationship" between you and any director, *executive officer*, or person nominated or chosen to become a director or *executive officer* of the Company?[4] The term "family relationship" means any relationship by blood, marriage or adoption not more remote than first cousin.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

____

____

[3] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(a), (b) and instruction thereto.

[4] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(d) and instruction thereto.

(b) Are any of your *family members* employed by the Company or any of its *affiliates*, or do any of your *family members* otherwise have business or other relationships with the Company or any of its *affiliates*? To your knowledge, does any group or entity with which any of your *family members* are affiliated have any business or other relationships with the Company or any of its *affiliates*?

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

____

____

QUESTION 4. Business Experience

(a) Please describe your business experience during the past five (5) years in the table below (please attach additional pages as necessary), and note whether your employer was an *affiliate* of the Company.[5] (You may refer to your attached resume if it provides the requested information.)

Time Period (Month/Year) From:	**To:**	**Principal Occupation**	**Position or Office**	**Name and Principal Business of Employer**	**Nature of Responsibilities**	***Affiliate* of the Company?**
						☐ YES ☐ NO
						☐ YES ☐ NO
						☐ YES ☐ NO
						☐ YES ☐ NO
						☐ YES ☐ NO

[5] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(e)(1) and instruction thereto.

(b) Please list in the table below all positions and offices (including board of directors memberships) that you have held with the Company and/or any *subsidiary* during the past five (5) years (including your present position(s)), and the time periods in which you have held those positions or offices.[6] (You may refer to your attached resume to the extent that it provides the requested information.)

Positions/Offices Held	**Time Period (Month and Year)**	
	From:	**To:**

QUESTION 5. Directorships

Have you served as a director of any entity besides the Company at any time in the past five years, or have you been selected to serve in the future as a director of any such entity?[7]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please list in the following table the name of each such entity, the positions (including committee memberships) you have held or have been selected to hold, your dates of service, and indicate if the applicable entity is a public company or a registered investment company.

Entity	**Positions and/or Board Committees**	**Dates of Service (Month and Year)**		**Public Company/ Registered Investment Company**
		From:	**To:**	
				☐ YES ☐ NO
				☐ YES ☐ NO
				☐ YES ☐ NO
				☐ YES ☐ NO

[6] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(e)(1) and instruction thereto.

[7] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(e)(2) and instruction thereto.

QUESTION 6. Educational [and Other] Background[8]

(a) Please complete the following table regarding your educational background. (You may refer to your attached resume if it provides the requested information.)

Name and Address of College, University or Professional School Attended	Dates of Attendance (Month and Year)		Area of Study (Major)	Degree Received
	From:	To:		

(b) **[**If you are a director, aside from any information provided in Questions 4 through 6(a), above, please describe any specific experiences, qualifications or skills that qualify you to serve as a director.[9] Such information may include information about your risk assessment skills or any particular area of expertise. (You may refer to your attached resume if it provides the requested information.)**]**[10]

____

____

____

QUESTION 7. Involvement in Legal and Regulatory Proceedings

Have any of the following events occurred during the past **[ten (10)]**[11] years? When computing the ten-year period, the date of an event should be the date on which the final order, judgment or decree was entered, or the date on which any rights of

[8] Consider attaching the prior year's disclosure for each recipient regarding background and including space for the recipient to update any changes.

[9] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(e)(1) and instruction thereto.

[10] Note, this information is required disclosure; however, consider whether or not this question should be included in the Questionnaire or left to the Company and/or the nominating committee to address through enhanced disclosure based on the background information otherwise obtained from directors in Questions 4, 5 and 6(a). If this question is not included in the Questionnaire, please ensure that the appropriate person at the Company is made aware of this disclosure requirement.

[11] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f) and instructions thereto. See also Cal. Corp. Code § 1502.1(a)(6), (7) and § 2117.1(a)(6), (7). The ten year time period is required disclosure; however, to the extent that this Questionnaire is being used for a registration statement, consider removing the time limitation in an effort to elicit more expansive disclosure.

appeal from preliminary orders, judgments, or decrees lapsed. Regarding bankruptcy petitions, the date should be the date of filing for uncontested petitions or the date upon which approval of a contested petition became final. If your answer is "*YES*" to any of these questions, or if you are in doubt as to whether a question applies to a particular proceeding, please provide details on a separate sheet and attach it to the Questionnaire.[12]

(a) Was a petition under the federal bankruptcy laws or any state insolvency law filed by or against, or a receiver, fiscal agent or similar officer appointed by a court for the business or property of: (i) you, (ii) any partnership in which you were a general partner within two (2) years before the time of the filing, or (iii) any corporation or business association of which you were an *executive officer* at or within two (2) years before the time of the filing?[13]

ANSWER: *YES* ☐ *NO* ☐

(b) Were you convicted in a criminal proceeding, or are you the named subject in a criminal proceeding that is presently pending (other than traffic violations and other minor offenses), including, but not limited to, any felony or misdemeanor (i) in connection with the purchase or sale of any security; (ii) involving the making of any false filing with the SEC, or (iii) arising out of the conduct of the business of an underwriter, broker, dealer, municipal securities dealer, investment advisor or paid solicitor of purchasers of securities?[14]

ANSWER: *YES* ☐ *NO* ☐

(c) Were you the subject of any court order, judgment or decree, not subsequently reversed, suspended or vacated, which permanently or temporarily enjoined you or otherwise limited you from any of the following activities:[15]

(i) Acting as a futures commission merchant, introducing broker, commodity trading adviser, commodity pool operator, floor broker, leverage transaction merchant, any other person regulated by the U.S. Commodity Futures Trading Commission, or an associated person of any of the foregoing; or as an investment adviser, *underwriter*,

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[12] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f) and instructions thereto.

[13] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(1) and instructions thereto.

[14] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(2) and instructions thereto. Additionally, see Rule 506(d)(1)(i) of Regulation D.

[15] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(3) and instructions thereto.

broker or dealer in securities, or as an affiliated person of any of the foregoing; or as a director or employee of any investment company, bank, savings and loan association or insurance company; or engaging in or continuing any conduct or practice in connection with such activity?[16]

(ii) Engaging in any type of business practice?[17]

(iii) Engaging in any activity in connection with the purchase or sale of any security or commodity or in connection with any violation of federal or state securities laws or federal commodities laws?[18]

ANSWER: *YES* ☐ *NO* ☐

(d) Were you the subject of any order, judgment or decree, not subsequently reversed, suspended or vacated, or any professional disciplinary proceeding, of any federal or state authority barring, suspending or otherwise limiting for more than sixty (60) days your right to engage in any of the activities described above or your right to be associated with persons engaged in any such activities?[19]

ANSWER: *YES* ☐ *NO* ☐

(e) Were you found by a court of competent jurisdiction in a civil action or by the SEC to have violated any federal or state securities law where the judgment or finding has not subsequently been reversed, suspended or vacated?[20]

ANSWER: *YES* ☐ *NO* ☐

(f) Were you found by a court of competent jurisdiction or by the U.S. Commodity Futures Trading Commission to have violated any federal commodities law where the judgment or finding has not been subsequently reversed, suspended or vacated?[21]

ANSWER: *YES* ☐ *NO* ☐

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[16] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(3)(i).

[17] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(3)(ii).

[18] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(3)(iii).

[19] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(4) and instructions thereto.

[20] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(5) and instructions thereto.

[21] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(6) and instructions thereto.

(g) Other than in connection with the settlement of a civil proceeding among private litigants, were you the subject of, or a party to, any federal or state judicial or administrative order, judgment, decree, or finding, not subsequently reversed, suspended or vacated, relating to any of the following?

(i) An alleged violation of any federal or state securities or commodities law or regulation?[22]

(ii) An alleged violation of any law or regulation respecting financial institutions or insurance companies including, but not limited to, a temporary or permanent injunction, order of disgorgement or restitution, civil money penalty or temporary or permanent cease-and-desist order, or removal or prohibition order?[23]

(iii) An alleged violation of any law or regulation prohibiting mail or wire fraud or fraud in connection with any business entity?[24]

ANSWER: *YES* ☐ *NO* ☐

(h) Were you the subject of, or a party to, any sanction or order, not subsequently reversed, suspended or vacated, of any self-regulatory organization, any registered entity, or any equivalent exchange, association, entity or organization that has disciplinary authority over its members or persons associated with a member?[25]

ANSWER: *YES* ☐ *NO* ☐

(i) Were you convicted of fraud?[26]

ANSWER: *YES* ☐ *NO* ☐

(j) Were you named as a defendant in any action, or have you been the subject of an action instituted by the SEC, in which it was alleged that you violated any securities law, engaged in any fraudulent conduct, or violated any fiduciary obligations such as that of an officer, director, trustee or partner of a corporation, trust or partnership?

ANSWER: *YES* ☐ *NO* ☐

[22] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(7)(i).
[23] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(7)(ii).
[24] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(7)(iii).
[25] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(f)(8). Self-regulatory organization is defined by 15 U.S.C. 78c(a)(26); registered entity is defined by 7 U.S.C. 1(a)(29).
[26] To the extent that the Company is required to file Form SI-PT in California, the Questionnaire should include this question regarding fraud convictions. Note reference change from to fn 11.

(k) Have you ever been: (i) suspended or barred from being associated with an issuer or public accounting firm; or (ii) suspended or barred from appearing or practicing before the SEC?[27]

ANSWER: *YES* ☐ *NO* ☐

(l) Are you subject to any order, judgment or decree entered into within the past five years that restrains or enjoins you from engaging or continuing to engage in any conduct or practice: (i) in connection with the purchase or sale of any security, (ii) involving the making of any false filing with the SEC; or (iii) arising out of the conduct of the business of an underwriter, broker, dealer or municipal securities dealer, investment advisor or paid solicitor of purchasers of securities?[28]

ANSWER: *YES* ☐ *NO* ☐

(m) Are you subject to a final order from any of the following entities that bar you from (i) associating with such entity; (ii) engaging in the business of securities, insurance or banking; or (iii) engaging in savings association or credit union activities? Was a final order entered against you within the past ten years by any of these entities that prohibit fraudulent, manipulative or deceptive conduct?[29]

(i) State securities commissions;

(ii) State authorities that supervise or examines banks, savings associations or credit unions;

(iii) State insurance commissions;

(iv) Federal banking agencies;

(v) The U.S. Commodity Futures Trading Commission; or

(vi) The National Credit Union Administration?

ANSWER: *YES* ☐ *NO* ☐

(n) Are you subject to an order of the SEC entered pursuant to Section 15(b) or 15B(c) of the Securities Exchange Act of 1934 (the "Exchange Act") or Section 203(e) or (f) of the Investment Advisers Act of 1940 that (i) suspends or revokes your

[27] 15 U.S.C. § 7215(c)(7)(B) (Sarbanes-Oxley Act § 105(c)(7)(B)).

[28] See Rule 506(d)(1)(ii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[29] See Rule 506(d)(1)(iii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

registration as a broker, dealer, municipal securities dealer or investment adviser; (ii) places limitations on your activities, functions or operations; or (iii) bars you from being associated with any entity or from participating in the offering of any penny stock?[30]

ANSWER: *YES* ☐ *NO* ☐

(o) Are you subject to any order of the SEC entered within five years that orders you to cease and desist from committing or causing a violation or future violation of (i) any scienter-based anti-fraud provision of the federal securities laws, including without limitation Section 17(a)(1) of the Securities Act of 1933 (the "Securities Act"), Section 10(b) of the Exchange Act and Rule10b-5, Section 15(c)(1) of the Exchange Act and Section 206(1) of the Investment Advisers Act of 1940, or any other rule or regulation thereunder; or (ii) Section 5 of the Securities Act?[31]

ANSWER: *YES* ☐ *NO* ☐

(p) Have you ever been suspended or expelled from membership in, or suspended or barred from association with a member of, a registered national securities exchange or a registered national or affiliated securities association for any act or omission to act constituting conduct inconsistent with just and equitable principles of trade?[32]

ANSWER: *YES* ☐ *NO* ☐

(q) Are you the subject of an investigation or proceeding to determine whether a stop order or suspension order should be issued in connection with any registration statement or Regulation A offering statement filed with the SEC[33]

ANSWER: *YES* ☐ *NO* ☐

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[30] See Rule 506(d)(1)(iv) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[31] See Rule 506(d)(1)(v) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[32] See Rule 506(d)(1)(vi) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[33] See Rule 506(d)(1)(vii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

(r) Have you filed (as a registrant or issuer), or were or were named as an underwriter in, any registration statement or Regulation A offering statement filed with the SEC that, within the past five years, was the subject of a refusal order, stop order, or order suspending the Regulation A exemption?[34]

ANSWER: *YES* ☐ *NO* ☐

(s) Have you been subject to a United States Postal Service false representation order during the past five years?[35]

ANSWER: *YES* ☐ *NO* ☐

(t) Are you subject to a temporary restraining order or preliminary injunction with respect to conduct alleged by the United States Postal Service to constitute a scheme or device for obtaining money or property through the mail by means of false representations?[36]

ANSWER: *YES* ☐ *NO* ☐

QUESTION 8. [Promoters and Control Persons][37]

To your knowledge, has one or more of the events listed in (a) through (f) in Question 8 occurred to any *promoter* or *control person* of the Company during the same period referred to in Question 8?[38]

ANSWER: *YES* ☐ *NO* ☐

[34] See Rule 506(d)(1)(vii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[35] See Rule 506(d)(1)(viii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[36] See Rule 506(d)(1)(viii) of Regulation D (to be included if the company anticipates relying on Rule 506 of Regulation D).

[37] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(g) and instructions thereto. This question only needs to be included if the Company has not been subject to the reporting requirements of Section 13(a) or 15(d) of the Exchange Act for the 12 months immediately prior to the filing of the document to which this item is applicable, and if the Company had a promoter at any time during the past five fiscal years per Item 401(g) of Regulation S-K.

[38] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 401(g).

OFFICER COMPENSATION AND RELATED MATTERS

Note: Questions 10 through 19 should be completed by (i) **all** executive officers of the Company, (ii) **anyone** who served as the Company's principal executive officer (or acted in a similar capacity) at any time during Fiscal Year **[Insert Last Fiscal Year]**, and (iii) **anyone** who served as the Company's principal financial officer (or acted in a similar capacity) at any time during Fiscal Year **[Insert Last Fiscal Year]**.[39]

QUESTION 9. Salary; Bonus; Earnings Under Non-Equity Incentive Plans *(Officers Only)*[40]

Please indicate in the table below the dollar value of the base salary (cash and non-cash) and any bonus (cash and non-cash) you earned from the Company or any of its *affiliates* during Fiscal Year **[Insert Last Fiscal Year]**, whether or not you elected to forego any portion of such base salary or bonus amounts. If any amount of your salary or bonus earned is not presently calculable please so indicate in the table.[41]

If you elected to forego any portion of your salary or bonus and instead receive stock, equity-based or other forms of non-cash compensation from the Company, please describe such election below the table.[42] Do not include the amount of salary or bonus taken instead as non-cash compensation in the "Salary" and "Bonus" columns below, but instead note those amounts in your description of the election.[43]

Please also indicate in the table below the dollar value of all earnings for services performed during Fiscal Year **[Insert Last Fiscal Year]** pursuant to awards under *Non-Equity Incentive Plans* and all earnings on any outstanding awards under those

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[39] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(a)(3). Please note that compensation disclosure under Item 402 of Regulation S-K is also required for up to two additional individuals for whom disclosure would have been required but for the fact that the individual was not serving as an executive officer of the registrant at the end of the last completed fiscal year – i.e., someone who was hired as or promoted to an executive officer position after the end of the last fiscal year or was terminated from an executive officer position prior to the end of the last fiscal year. See Regulation S-K, Item 402(a)(3)(iv). The Company will likely be required to rely on its own records for any such additional person who was terminated. Any new hires should be picked up by the "all executive officers" note in the introduction to the Compensation section of the Questionnaire.

[40] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(a) and (b)(2)(ii), (iii)(A) and (B) and instructions thereto.

[41] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 1 to Item 402(c)(2)(iii) and (iv).

[42] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(iii) and (iv).

[43] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(iii) and (iv).

plans.[44] (Please note that a "*Non-Equity Incentive Plan*" includes plans that are commonly thought of as "bonus" plans but that are designed to provide cash incentive for performance to occur over a specified period of time, e.g., a management incentive plan or bonus plan where cash payouts are dependent on the satisfaction of financial or other targets.)

If the relevant performance measure(s) under a *Non-Equity Incentive Plan* were satisfied during Fiscal Year **[Insert Last Fiscal Year]** (including for a single year in a plan with a multi-year performance measure), you should report the earnings in the table below (even if they are not payable until a later date) and note the payment terms below the table.[45] All earnings under *Non-Equity Incentive Plans* during Fiscal Year **[Insert Last Fiscal Year]** should be reported, whether the earnings were paid during the fiscal year, payable during the period but deferred at your election, or payable by their terms at a later date.[46]

Fiscal Year	Salary	Bonus	Non-Equity Incentive Plans
[Insert Last Fiscal Year]			

[44] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(vii).
[45] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 1 to Item 402(c)(2)(vii).
[46] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(vii).

QUESTION 10. Stock and Option/SAR Awards *(Officers Only)*

(a) Please indicate in the table below all awards of stock (including restricted stock) that were granted to you during Fiscal Year **[Insert Last Fiscal Year]**, including the date the particular grant was made, the number of shares subject to the award, the vesting period, forfeiture terms, and/or performance, market or other conditions (if applicable) of the award and any consideration you paid for the shares.[47] Please include and note any stock granted in lieu of cash compensation payments and indicate the amount of compensation foregone.[48] If any of the stock you were granted was not common stock, please so indicate.[49]

Stock Granted (#)	Grant Date	Vesting and/or Conditions (if applicable)	Consideration Paid

(b) Please indicate in the table below all awards of *stock options*, with or without tandem *SARs*, that were granted to you during Fiscal Year **[Insert Last Fiscal Year]**, including the date the particular grant was made, the number of shares or SARs subject to the award, the per share exercise or base price, any forfeiture terms, and/or performance, market or other conditions (if applicable) of the award and the expiration date of the *stock options* or *SARs*.[50] You should include in the table any *stock options* or *SARs* that were granted to you but that you subsequently transferred.[51]

[47] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(v).

[48] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(1) and (2)(iii)-(iv) and instructions thereto.

[49] Most grants will be of common stock, but it should be noted if that was not the case.

[50] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(vi).

[51] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(vi).

If the exercise or base price is adjustable, please so indicate and describe the adjustment feature. If the Company made more than one grant to you during Fiscal Year **[Insert Last Fiscal Year]**, please use a separate line to note each grant. *Stock options* granted in connection with an option repricing transaction reported in Question 12 should also be reported below. Please include and note any *stock option* granted in lieu of cash compensation payments and indicate the amount of compensation fore-gone.[52]

Options Granted (#)	SARs Granted (#)	Exercise or Base Price (Dollar Value/Share)	Expiration Date

QUESTION 11. Repricings

Was the exercise price of any of your outstanding *stock option*, *SAR* or other equity-based awards adjusted or amended, whether through amendment, cancellation, replacement grants or other means, during Fiscal Year **[Insert Last Fiscal Year]**?[53] Were the terms of any of your outstanding *stock option*, *SAR* or other equity-based awards otherwise modified during Fiscal Year **[Insert Last Fiscal Year]**?[54]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

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[52] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(1) and (2)(iii)-(iv) and instructions thereto.

[53] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(v)-(vi).

[54] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(v) and (vi). Only material modifications (and all repricings) must be disclosed, but the Questionnaire is designed to elicit information about any modifications so that the Company and the drafter can determine whether the modifications are material. See also Regulation S-K, Item 402(e)(1)(ii).

QUESTION 12. Pension and Non-Qualified Deferred Compensation Earnings *(Officers Only)*

(a) Did you participate in any defined benefit or other pension plans (including supplemental plans) of the Company during Fiscal Year **[Insert Last Fiscal Year]**?[55] This would include any plan that provides for the payment of retirement benefits, or benefits that will be paid primarily following retirement, including but not limited to tax-qualified defined benefit plans (e.g., a plan that pays a life annuity at retirement based on annual compensation at retirement and years of service) and supplemental executive retirement plans (e.g., a non-qualified deferred compensation plan that is related to a traditional pension plan), but would exclude any tax-qualified defined contribution plans (e.g., a 401(k) or profit sharing plan) and nonqualified defined contribution plans (e.g., a traditional deferred compensation plan).[56]

ANSWER: *YES* ☐ *NO* ☐

(b) Did you defer any compensation during Fiscal Year **[Insert Last Fiscal Year]** on a basis that was not tax qualified (i.e., generally other than through a 401(k) or profit sharing plan)?[57] If "YES," please note the aggregate dollar amount of deferrals/contributions and the dollar amount of aggregate interest or other earning accrued during the fiscal year[58] below.

ANSWER: *YES* ☐ *NO* ☐

(c) If you answered "YES" to question (b) above, did you receive above-market or preferential earnings (or dividends in the case of deferred stock) on the compensation you deferred?[59] For purposes of this question, interest on deferred compensation is above-market only if the rate of interest exceeds 120% of the applicable federal long-term rate, with compounding at the rate that corresponds most closely the rate under

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[55] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(viii)(A) and Item 402(h). This question is designed to elicit basic information to enable the drafter to, with assistance from the Company, draft disclosure responsive to both Items 402(c) and 402(h). With respect to Item 402(h), the Company will need to provide the majority of the data.

[56] See Instruction 1 to Regulation S-K, Item 402(c)(2)(viii) and Instruction 1 to Item 402(h)(2).

[57] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(viii)(B) and Item 402(i).

[58] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(i)(2)(iv).

[59] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(viii)(B) and the instructions thereto. Only the above-market portion of the interest or dividends must be reported. The Company will likely need to calculate this amount. The Company will also need to identify whether there has been a discretionary reset of the applicable interest rate. The calculation will also be different if the rates vary depending upon conditions such as a minimum period of continued service. See Instruction 2 to Item 402(c)(2)(viii).

the applicable plan at the time the interest rate or formula was set.[60] If you are not sure whether you received above-market or preferential earnings, please indicate below.

ANSWER: *YES* ☐ *NO* ☐

(d) If you answered "YES" to question (b) above, did the Company contribute any funds on your behalf to the plan(s) during Fiscal Year **[Insert Last Fiscal Year]**?[61] If "YES," please note the aggregate dollar amount of contributions below.

ANSWER: *YES* ☐ *NO* ☐

(e) If you answered "YES" to question (b) above, did you make any withdrawals or receive any distributions from the plan(s) during Fiscal Year **[Insert Last Fiscal Year]**?[62] If "YES," please note the aggregate dollar amount of withdrawals and distributions below.

ANSWER: *YES* ☐ *NO* ☐

(f) If you answered "YES" to question (b) above, please indicate below the total balance in your account(s) under each particular plan as of the end of Fiscal Year **[Insert Last Fiscal Year]**.[63]

If you answered "YES" to any of the questions above, please elaborate on your responses by noting the specific plans, the amount deferred (i.e., contributed by you), the amount the Company contributed or other information requested above:

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[60] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 2 to Item 402(c)(2)(viii).
[61] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(i)(2)(iii).
[62] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(i)(2)(v).
[63] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(i)(2)(vi).

QUESTION 13. Other Officer Compensation *(Officers Only)*

Please indicate in the table below all other compensation (regardless of amount) awarded to, earned by, or paid to you during Fiscal Year **[Insert Last Fiscal Year]** that is not already reported under Questions 10-13 above[64] (including compensation related to transactions between the Company or any of its *affiliates* and any third party where a purpose of the transaction was to furnish compensation to you or your *family members*). Such compensation would include, but is not limited to:

- Perquisites and other personal benefits, or property, **[unless the aggregate amount of such compensation (based on its incremental cost to the Company) was less than $10,000]**;[65]
- All "gross-ups" or other amounts reimbursed to you during the fiscal year for the payment of taxes;[66]
- Any security that you purchased from the Company or its subsidiaries (through deferral of salary or bonus, or otherwise) at a discount from the market price of the security on the date of purchase, unless the discount is generally available either to all security holders of the Company or to all of the Company's salaried employees;[67]
- Amounts you received or accrued in connection with a change of control of the Company;[68]
- Company contributions or other allocations to vested and unvested defined contribution plans (e.g. matching contributions to a 401(k) plan);[69]
- The dollar value of any insurance premiums paid by, or on behalf of, the Company during the fiscal year with respect to life insurance for your benefit;[70] and

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[64] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix).

[65] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(A) and Instruction 4 thereto. Note that the drafter may want to delete the exclusion of perquisites amounting to less than $10,000 to enable the Company to obtain information regarding all perquisites and then consider for itself the proper valuation for disclosure purposes.

[66] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(B).

[67] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(C).

[68] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(D)(2). Note that under Item 402(c)(2)(ix)(D)(1) payments or accruals in connection with a Named Executive Officer's termination of employment, including through retirement, resignation, severance or constructive termination (including a change in responsibilities), must be reported, but someone in that position will not likely be filling out a D&O questionnaire. The Company will need to provide the required information.

[69] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(E).

[70] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(F).

- The dollar value of any dividends or other earnings paid on stock or option awards.[71]

The SEC has stated that among the factors to be considered in determining whether an item is a perquisite or other personal benefit are the following:[72]

- An item is not a perquisite if it is integrally and directly related to the performance of your duties. This factor should be interpreted narrowly.
- Otherwise, an item is a perquisite or personal benefit if it confers a direct or indirect benefit that has a personal aspect, without regard to whether it may be provided for some business reason or for the convenience of the Company, unless it is generally available on a non-discriminatory basis to all employees. This factor should be interpreted broadly.

The following are some examples of items that would qualify as perquisites or other personal benefits: (i) club memberships not used exclusively for business entertainment purposes; (ii) personal financial or tax advice; (iii) personal travel using vehicles owned or leased by the Company; (iv) personal travel otherwise financed by the Company; (v) personal use of other property owned or leased by the Company; (vi) housing and other living expenses (including but not limited to relocation assistance and payments for you to stay at your personal residence); (vii) security provided at a personal residence or during personal travel; (viii) commuting expenses (whether or not for the Company's convenience or benefit); and (ix) discounts on the Company's products or services not generally available to employees on a nondiscriminatory basis.[73]

Description of Other Fiscal Year [Insert Last Fiscal Year] Compensation	**Dollar Value**

[71] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(ix)(G). Note that this only needs to be disclosed if the amounts were not factored into the grant date fair value required to be reported for the stock or option award itself. The drafter will need to confirm with the Company whether that was the case.

[72] SEC Release 33-8732, 34-54302, p. 74 (August 29, 2006).

[73] Note that any item for which an executive officer has actually fully reimbursed the Company for its total cost should not be considered a perquisite or other personal benefit. See Regulation S-K Compliance and Disclosure Interpretations, Question 119.07.

QUESTION 14. Grants of Plan-Based Awards *(Officers Only)*

Did you receive any grants or awards under any *Incentive Plan* during Fiscal Year **[Insert Last Fiscal Year]**?[74] This would include grants or awards under both *Non-Equity Incentive Plans* and *Equity Incentive Plans*, and would also include grants or awards that you subsequently transferred.[75]

ANSWER: *YES* ☐ *NO* ☐

If you answered "YES," please briefly describe each grant or award (including the grant date and any threshold, target and maximum amounts applicable to the awards) in the table below.[76] If you paid any consideration for the particular award, please note the amount you paid.[77] You may cross reference to grants of stock, *stock options* and *SARs* that you previously noted in response to Question 11 instead of repeating the information.

Date of Grant/Award	Description of Grant/Award

QUESTION 15. Outstanding Equity Awards *(Officers Only)*

Please describe in the table below all outstanding equity awards (e.g., *stock options*, *SARs*, restricted stock, restricted stock units and similar instruments) that you held as of the end of Fiscal Year **[Insert Last Fiscal Year]** (regardless of when the award was granted to you).[78] Please indicate the number of securities, vesting schedule, expiration date and exercise price, as applicable, for each award.[79] If any of the

[74] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(d).

[75] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(d)(1).

[76] This question is designed to elicit basic information to identify the particular grants and awards that the grantee received. The attorney preparing the SEC disclosure will need to do additional diligence with the Company to identify the remaining information that must be disclosed under Item 402(d), such as deviations between the grant date and the date on which the award was approved, deviations between the strike price of the award and the closing market price of the underlying security on the date of grant, etc.

[77] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 5 to Item 402(d).

[78] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(f).

[79] This data is required to be disclosed per Item 402(f) to the extent it is applicable to the particular award. This question is designed to elicit basic information to identify the particular grants and awards that the grantee held at the end of the subject fiscal year. The attorney preparing the disclosure will be required to take the data the respondent provides here and work with the Company to assemble the related data that must be disclosed under Item 402(f), e.g., the market value of stock and equity incentive plan awards of stock.

awards have been transferred other than for value, please so indicate and describe the nature of the transfer.[80] You may cross reference to grants of stock, *stock options* and *SARs* that you previously noted in response to Question 11 instead of repeating the information.

Date of Grant/Award	Description of Grant/Award

If you have been granted any equity awards (e.g., *stock options*, *SARs*, restricted stock, restricted stock units and similar instruments) since the end of Fiscal Year **[Insert Last Fiscal Year]**, please note the grants below:

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QUESTION 16. Option Exercises and Stock Vesting *(Officers Only)*

(a) Please describe in the table below each exercise of *stock options*, *SARs* and similar instruments that you had in during Fiscal Year **[Insert Last Fiscal Year]**.[81] If you transferred any such securities for value, please indicate which securities were transferred, when they were transferred and what you received as consideration for the transfer.[82]

Exercise Date	Security Exercised (Option, SAR, etc.)	Grant Date of Security Exercised	Number Exercised	Sale Price (if applicable)

(b) Please describe in the table below each grant of stock, including restricted stock, restricted stock units and similar instruments, that you held at any point during

[80] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 1 to Item 402(f)(2).
[81] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(g).
[82] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(g)(2)(iii).

Fiscal Year **[Insert Last Fiscal Year]**.[83] To the extent that any or all of the grants that would be responsive to this question were already reported in response to Question 16 above (because you held them at the end of the fiscal year), you may so indicate instead of repeating the information. If you transferred any such securities for value, please indicate which securities were transferred, when they were transferred and what you received as consideration for the transfer.[84]

Security	Grant Date	Vesting Schedule

QUESTION 17. Termination and Change of Control Arrangements *(Officers Only)*

Do you have any contract, agreement, plan or other *arrangement* with the Company, whether written or unwritten, that provides for payment(s) to you at, following, or in connection with any termination, including without limitation resignation, severance, retirement or a constructive termination, or a change of control of the Company or a change in your responsibilities?[85] This question does not apply to contracts, agreements, plans or other *arrangements* to the extent they do not discriminate in scope, terms or operation in favor of executive officers of the Company and that are available generally to all salaried employees.[86]

ANSWER: *YES* ☐ *NO* ☐

If you answered "YES," please identify each such contract, agreement, plan or other *arrangement*:

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[83] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(g). The Company will be required to disclose information regarding amounts realized upon vesting of outstanding stock options, restricted stock, etc., during the last fiscal year, which can be derived based on the data provided regarding the vesting schedules, etc. for the particular awards.

[84] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(g)(2)(v).

[85] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(j). This question is designed to elicit information regarding the existence of any such contract, agreement, plan or arrangement. If the respondent identifies any such agreement, the drafter will need to work with the respondent and the Company to identify the information regarding that agreement that Item 402(j) requires to be disclosed.

[86] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Instruction 5 to Item 402(j).

QUESTION 18. Employment Agreements *(Officers Only)*

Except for any change of control agreement identified in response to Question 18, do you have any other contract, agreement, plan or *arrangement* with the Company with respect to your employment (such as an employment agreement or offer letter)?

ANSWER: *YES* ☐ *NO* ☐

If you answered "YES," please identify each such contract, agreement, plan or *arrangement*:

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DIRECTOR COMPENSATION AND RELATED MATTERS

QUESTION 19. Director Compensation *(Directors only)*

(a) Please provide a description of any *arrangement* (including the Company's standard *arrangements* with directors), stating amounts, pursuant to which you are compensated for all services as a director, including any additional amounts payable for committee participation or special assignments.[87]

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(b) Please state the aggregate dollar amount of all fees you earned or were paid in cash for services as a director during Fiscal Year **[Insert Last Fiscal Year]**, including annual retainer fees, committee and or chairmanship fees, and meeting fees.[88]

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[87] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(3). The Company is required to disclose both its standard compensation arrangements with directors and whether any director has a non-standard arrangement. A copy of last year's proxy statement could be used as a reference.

[88] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(ii).

(c) Please identify in the table below any awards of stock (including restricted stock) and *stock options* (with or without tandem *SARs*) that you were granted during Fiscal Year **[Insert Last Fiscal Year],** the number of shares subject to the award, the vesting period, forfeiture terms, and/or performance, market or other conditions (if applicable) of the award and any consideration you paid for the shares.[89] Please note in the table any awards that you subsequently transferred.[90]

Security Granted	Grant Date	# Shares/ Units	Vesting and/ or Conditions (if applicable)	Consideration Paid (if applicable)

(d) Please describe in the table below all outstanding *stock option* (with or without tandem *SARs*) and stock (including restricted stock) awards that you held as of the end of Fiscal Year **[Insert Last Fiscal Year]** (regardless of when the award was granted to you).[91] You may cross reference to grants that you previously noted in response to Question 20(c) instead of repeating the information.

Security Granted	Grant Date	# Shares/ Units	Vesting and/ or Conditions (if applicable)	Consideration Paid (if applicable)

(e) Did you participate in any *Non-Equity Incentive Plan* during Fiscal Year **[Insert Last Fiscal Year]**?[92]

ANSWER: *YES* ☐ *NO* ☐

[89] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(iii) and (iv).

[90] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(iv).

[91] Form 10-K, Item 11; Schedule 14A, Item 8. See Instruction to Regulation S-K, Item 402(k)(2)(iii) and (iv). Unlike with respect to officers of the Company, only the aggregate number of stock awards and aggregate number of option awards outstanding at fiscal year end needs to be disclosed for directors.

[92] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(v).

If you answered "YES," please identify the plan(s) and note the dollar value of all earnings for services performed during Fiscal Year **[Insert Last Fiscal Year]** and all earnings on outstanding awards under the plan(s), as applicable:

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(f) Did you participate in any defined benefit or other pension plans (including supplemental plans) of the Company during Fiscal Year **[Insert Last Fiscal Year]**?[93] This would include any plan that provides for the payment of retirement benefits, or benefits that will be paid primarily following retirement, including but not limited to tax-qualified defined benefit plans (e.g., a plan that pays a life annuity at retirement based on annual compensation at retirement and years of service) and supplemental executive retirement plans (e.g., a non-qualified deferred compensation plan that is related to a traditional pension plan), but would exclude any tax-qualified defined contribution plans (e.g., a 401(k) or profit sharing plan) and nonqualified defined contribution plans (e.g., a traditional deferred compensation plan).[94]

ANSWER: *YES* ☐ *NO* ☐

(g) Did you defer any compensation during Fiscal Year **[Insert Last Fiscal Year]** on a basis that was not tax qualified (i.e., generally other than through a 401(k) or profit sharing plan)?[95]

ANSWER: *YES* ☐ *NO* ☐

(h) If you answered "YES" to question (g) above, did you receive above-market or preferential earnings (or dividends in the case of deferred stock) on the compensation you deferred?[96] For purposes of this question, interest on deferred compensation is

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[93] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vi)(A) and (B). This question is designed to elicit basic information to enable the drafter to, with assistance from the Company, draft responsive disclosure. With respect to Item 402(k)(2)(vi)(A), the Company will need to provide the data.

[94] See Instruction 1 to Regulation S-K, Item 402(c)(2)(viii). Certain instructions to Item 402(c) apply equally to Item 402(k) as well per Instruction to Item 402(k).

[95] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vi)(B).

[96] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(c)(2)(viii)(B) and the instructions thereto. Certain instructions to Item 402(c) apply equally to Item 402(k) as well per the instruction to Item 402(k). Only the above-market portion of the interest or dividends must be reported. The Company will likely need to calculate this amount. The Company will also need to identify whether there has been a discretionary reset of the applicable interest rate. The calculation will also be different if the rates vary depending upon conditions such as a minimum period of continued service. See Regulation S-K, Instruction 2 to Item 402(c)(2)(viii).

above-market only if the rate of interest exceeds 120% of the applicable federal long-term rate, with compounding at the rate that corresponds most closely the rate under the applicable plan at the time the interest rate or formula was set.[97] If you are not sure whether you received above-market or preferential earnings, please indicate below.

ANSWER: *YES* ☐ *NO* ☐

(i) Please indicate in the table below all other compensation (regardless of amount) awarded to, earned by, or paid to you during Fiscal Year **[Insert Last Fiscal Year]** that is not already reported in this Question 20[98] (including compensation related to transactions between the Company or any of its *affiliates* and any third party where a purpose of the transaction was to furnish compensation to you or your *family members*). Such compensation would include, but is not limited to:

- Perquisites and other personal benefits, or property, unless the aggregate amount of such compensation (based on its incremental cost to the Company) was less than $10,000;[99]
- All "gross-ups" or other amounts reimbursed to you during the fiscal year for the payment of taxes;[100]
- Any security that you purchased from the Company or its subsidiaries (through deferral of salary or bonus, or otherwise) at a discount from the market price of the security on the date of purchase, unless the discount is generally available either to all security holders of the Company or to all of the Company's salaried employees;[101]
- Amounts you received or accrued in connection with a change of control of the Company;[102]
- Company contributions or other allocations to vested and unvested defined contribution plans (e.g. matching contributions to a 401(k) plan);[103]

[97] See Regulation S-K, Instruction 2 to Item 402(c)(2)(viii).
[98] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii).
[99] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(A) and Instructions 2 and 3 thereto.
[100] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(B).
[101] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(C).
[102] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(D)(2). Note that under Item 402(k)(2)(vii)(D)(1) payments or accruals in connection with a director's resignation, retirement or other termination must be reported, but someone in that position will not likely be filling out a D&O questionnaire. The Company will need to provide the required information.
[103] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(E).

- Consulting fees earned from, or paid or payable by the Company and/or its *subsidiaries* (including joint ventures);[104]

- The annual costs of payments and promises of payments pursuant to director legacy programs and similar charitable award programs;[105]

- The dollar value of any insurance premiums paid by, or on behalf of, the Company during the fiscal year with respect to life insurance for your benefit;[106] and

- The dollar value of any dividends or other earnings paid on stock or option awards.[107]

The SEC has stated that among the factors to be considered in determining whether an item is a perquisite or other personal benefit are the following:[108]

- An item is not a perquisite if it is integrally and directly related to the performance of your duties. This factor should be interpreted narrowly.

- Otherwise, an item is a perquisite or personal benefit if it confers a direct or indirect benefit that has a personal aspect, without regard to whether it may be provided for some business reason or for the convenience of the Company, unless it is generally available on a non-discriminatory basis to all employees. This factor should be interpreted broadly.

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[104] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(F).

[105] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(G) and Instruction 1 to Item 402(k)(2)(vii).

[106] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(H).

[107] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(I). Note that this only needs to be disclosed if the amounts were not factored into the grant date fair value required to be reported for the stock or option award itself. The drafter will need to confirm with the Company whether that was the case.

[108] SEC Release 33-8732, 34-54302, p. 74 (August 29, 2006).

The following are some examples of items that would qualify as perquisites or other personal benefits: (i) club memberships not used exclusively for business entertainment purposes; (ii) personal financial or tax advice; (iii) personal travel using vehicles owned or leased by the Company; (iv) personal travel otherwise financed by the Company; (v) personal use of other property owned or leased by the Company; (vi) housing and other living expenses (including but not limited to relocation assistance and payments for you to stay at your personal residence); (vii) security provided at a personal residence or during personal travel; (viii) commuting expenses (whether or not for the Company's convenience or benefit); and (ix) discounts on the Company's products or services not generally available to employees on a nondiscriminatory basis.

Description of Other Fiscal Year [Insert Last Fiscal Year] Compensation	**Dollar Value**

QUESTION 20. Director Legacy Program *(Directors Only)*

Does the Company have a "director legacy" or "charitable awards" program in which you participate?[109] For the purposes of this question, programs in which the Company has agreed to make donations to one or more charitable institutions in your name, payable by the Company currently or on a designated event, such as your retirement, (as well as similar programs) are considered "director legacy" or "charitable awards" programs.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please provide a description of the material terms of, and the total dollar amounts payable under, each such program:

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[109] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 402(k)(2)(vii)(G) and Instruction 1 to Item 402(k)(2)(vii).

QUESTION 21. Boards of Directors and Committees *(Directors Only)*[110]

(a) Please state whether you attended the prior year's annual meeting of stockholders.[111]

ANSWER: *YES* ☐ *NO* ☐

(b) Please state below the total number of meetings of the board of directors (including regularly scheduled and special meetings) held during Fiscal Year **[Insert Last Fiscal Year]**:[112]

Number of meetings: __________

(c) During Fiscal Year **[Insert Last Fiscal Year]**, did you attend all meetings of the board of directors of the Company? If your answer is "*NO*," please indicate the number of meetings you missed.[113]

ANSWER: *YES* ☐ *NO* ☐

Number of meetings missed: __________

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[110] Schedule 14A, Item 7(d). See Regulation S-K, Item 407(b). This item also requires disclosure of the Company's policy regarding board members' attendance at annual meetings.

[111] Schedule 14A, Item 7(d). See Regulation S-K, Item 407(b)(1).

[112] Schedule 14A, Item 7(d). See Regulation S-K, Item 407(b)(1).

[113] Schedule 14A, Item 7(d). See Regulation S-K, Item 407(b)(1).

(d) Please complete the table below regarding the committees of the Company's board of directors. Please specify if you served as a member of any committee of the board of directors for less than the full fiscal year and complete the table for the portion of the fiscal year during which you served:[114]

	Board Has Committee	I am a Member	Number of Meetings Held During Fiscal Year [Insert Last Fiscal Year]	Number of Meetings I Attended During Fiscal Year [Insert Last Fiscal Year]
(i) Audit	Yes ☐ No ☐	Yes ☐ No ☐		
(ii) Compensation	Yes ☐ No ☐	Yes ☐ No ☐		
(iii) Nominating **[/Corporate Governance[115]]**	Yes ☐ No ☐	Yes ☐ No ☐		
(iv) Other:	(list name of committee)	Yes ☐ No ☐		
	(list name of committee)	Yes ☐ No ☐		

[114] Schedule 14A, Item 7(d). See Regulation S-K, Item 407(b)(1).
[115] Include if the Company is listed on the NYSE. See NYSE Listed Company Manual § 303A.04.

SECURITY OWNERSHIP

QUESTION 22. Stock Ownership

(a) Please state in the table below the type and number of the Company's equity securities *beneficially owned* by you and/or which you have the right to acquire (through the exercise of options, warrants or otherwise) on or before **[Insert Date Sixty (60) Days After the Most Recent Practicable Date Prior to the Anticipated Filing]**. Include in this table all of the Company's equity securities that are: (i) registered in your name, including shares registered in your name as trustee, executor, custodian, pledgee, agent or nominee, either alone or with others; (ii) owned *beneficially* by you or any *associate* of yours; or (iii) registered in the name of a nominee or in street name, including any shares held for the account of any of the above.[116] If you do not have sole voting and investment power over any of the securities, please so indicate in the table below.

Name of Record Owner	Type of Security	Number of Shares	Type of Ownership (trust, partnership, direct, personal, etc.)

(b) Please state the following information in the table below regarding all *stock options* you hold: (i) the grant date, (ii) the number of shares subject to the originally granted options, (iii) the number of shares remaining subject to the options, and (iv) the schedule or terms of any vesting or exercise provisions.[117]

Grant Date	Number of Shares Originally Subject to Option	Number of Shares Remaining Subject to Option	Vesting Schedule

[116] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

[117] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

(c) Do you hold any warrants, convertible debt or other securities (other than options) or rights to acquire securities of the Company?[118] If your answer is "*YES*," please describe the securities or rights below.

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(d) Do you share voting and/or investment control over any shares of the Company's securities?[119] If your answer is "*YES*," please provide below a brief description of any *arrangement* concerning the shared control and the number of shares subject to the *arrangement*. "Shared voting power" and "shared investment power" are generally applied to securities held as tenants in common and in cases where you are a co-trustee or where someone's signature and approval other than your own are necessary to vote or sell the securities.

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(e) Are any of the Company's securities that you *beneficially own* pledged as security (e.g., pledged to a bank or broker in connection with a loan or margin account) or subject to a negative pledge (e.g., a promise by a borrower to a lender not to convey securities to a third party or otherwise encumber them)?[120] If your answer is "*YES*," please provide below a brief description of the nature of any such pledge, the type and amount of securities subject to the pledge, and the amount outstanding under the pledge. Please also provide a brief description of the material terms of the pledge *arrangement*.

ANSWER: *YES* ☐ *NO* ☐

[118] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

[119] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

[120] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403(b) and instructions thereto. See also Exchange Act Rule 13d-3(d)(1). See also Regulation S-K Compliance and Disclosure Interpretations, Question 129.04.

Description, if applicable:

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QUESTION 23. Disclaimer of Beneficial Ownership

Do you wish to disclaim *beneficial ownership* of any of the shares reported in response to Question 23?[121]

Note: Whether you make such a disclaimer is, of course, entirely a matter of your own decision. You may wish to consult with counsel in this connection as a disclaimer may be important not only in connection with the securities laws, but also because, without it, your reporting the ownership of such shares might be construed as an admission of ownership by you for other purposes, such as short-swing trading liabilities.

ANSWER: *YES* ☐ *NO* ☐

If the answer is "*YES*," please complete the table below with the requested information regarding the person(s) who should be shown as the *beneficial owner(s)* of the shares in question.

Class of Stock	Number of Shares Beneficially Owned	Name of Actual Beneficial Owner	Relationship of Such Person to You

QUESTION 24. Interest in Subsidiaries

Do you beneficially own any equity securities of any *subsidiary* of the Company? If your answer is "*YES*," please list your interest(s) in the table below.[122]

ANSWER: *YES* ☐ *NO* ☐

Name of Subsidiary	Securities Owned	Date Acquired

[121] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-4.

[122] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403(b) and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

QUESTION 25. 5% Stockholders

Do you know of any person (including yourself and your *associates*) who is the *beneficial owner* of more than 5% of any class of the Company's equity securities? If your answer is "*YES*," please provide the requested information in the table below to the extent you know such information.[123]

ANSWER: *YES* ☐ *NO* ☐

Shareholder's Name and Address	Title of Securities	Amount Held	Percentage Owned	Nature of Ownership ("Direct" or "Indirect")*

Note: Please explain the nature of any indirect ownership (e.g., "indirectly, as trustee for children," "indirectly, by spouse," "indirectly, by trust," etc.).

QUESTION 26. Voting Arrangements

Do you know of any voting trust or similar agreement or *arrangement* pursuant to which more than 5% of the Company's outstanding common stock is held or is to be held? If your answer is "*YES*," please describe below.[124]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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[123] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403 and instructions thereto. See also Exchange Act Rule 13d-3(d)(1).

[124] Form 10-K, Item 12; Schedule 14A, Item 6. See Regulation S-K, Item 403(b) and Instruction 7 thereto. See also Exchange Act Rule 13d-3(d)(1).

TRANSACTIONS AND RELATIONSHIPS

QUESTION 27. Transactions with Company

(a) Has there been any *transaction* [since the beginning of **[Insert Last Fiscal Year]**], or is there any currently proposed *transaction*, to which the Company or any of its *affiliates* was or is to be a participant, which exceeds $120,000 in amount <u>and</u> in which you or any *related person* had or will have a direct or indirect interest?[125] The amount of the interest is to be computed without regard to the amount of any profit or loss involved in the transaction.[126]

In the case of a *transaction* involving a lease or otherwise providing for periodic payments or installments, include the aggregate amount of all periodic payments or installments due on or after the beginning of the last fiscal year, including any required or optional payments due during or at the conclusion of the lease or other transactions providing for periodic payments or installments.[127] In the case of a transaction involving indebtedness, include the largest amount of all indebtedness outstanding at any time since the beginning of the last fiscal year and all amounts of interest payable on it during the last fiscal year.[128] The following items may be excluded from the calculation of the amount of indebtedness: amounts due from the related person for purchases of goods and services subject to usual trade terms, for ordinary business travel and expense payments and for other transactions in the ordinary course of business.[129]

Examples of possible interests which must be disclosed are: You or any of your *associates* (i) has been, is now, or proposes to be a shareholder holding in excess of ten percent (10%) of the Company's stock, an officer, director or employee of a major creditor, customer or supplier of the Company or any *subsidiaries* or has an interest

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[125] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b) and Item 22(b). See Regulation S-K, Item 404(a) and instructions thereto Item 404(a) only requires disclosure of material interests, but this question is designed to elicit information to allow the drafter and the Company to determine what is material. Note also that certain interests are not required to be disclosed pursuant to the instructions to Item 404(a).

[126] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b). See Regulation S-K, Item 404(a)(4), but the question is designed to elicit information to allow the drafter and the Company to determine if any of the exceptions apply.

[127] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b). See Regulation S-K, Instruction 3(a) to Item 404(a).

[128] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b). See Regulation S-K, Instruction 3(b) to Item 404(a).

[129] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b). See Regulation S-K, Instruction 4(a) to Item 404(a). Note also that in the case of indebtedness, if the lender is a bank, savings and loan or broker-dealer you may also omit certain disclosures in some circumstances as described in Instruction 4(c) to Item 404(a).

in any such creditor, customer or supplier; (ii) is a seller, buyer, lessee or lessor of property to, or from, the Company or any *subsidiary*; (iii) is the lender or guarantor of a loan made to, or is a borrower from, the Company or any *subsidiary*; (iv) is the debtor under an obligation which the Company or any *subsidiary* guarantees; and (v) is a buyer of securities or evidences of indebtedness from the Company or any *subsidiary*. If applicable, such transaction(s), the name of any such *associate(s)* and the nature of your relationship(s) with such *associate(s)* should be included. If any of your *immediate family members* are employed by the Company or any of its *subsidiaries* and such person's annual compensation exceeds $120,000, such relationship should be disclosed.

ANSWER: *YES* ☐ *NO* ☐

If your answer to question (a) is "*YES*," please (i) name the *related person* and briefly describe the basis on which the person is a *related person*, (ii) briefly describe the *related person's* interest in the *transaction*, including their position(s) or relationship(s) with, or ownership in, a firm, corporation or other entity that is a party to, or has an interest in, the *transaction*, (iii) note the approximate dollar value of the amount involved in the transaction (in the case of indebtedness, please indicate the largest aggregate amount of principal outstanding, the amount outstanding as of the latest practicable date, the amount of principal and interest paid during the relevant period, and the rate or amount of interest payable on the indebtedness. Please also indicate any other information regarding the *transaction* or the *related person* in the context of the *transaction* that is material in light of the circumstances of the particular transaction.[130]

Description, if applicable:

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[130] Form 10-K, Item 13; Schedule 14A, Item 5(b)(1)(xi), Item 7(b). See Regulation S-K, Item 404(a)(6).

(b) Other than those you have described elsewhere in this Questionnaire, has there been any *transaction* since [the beginning of Fiscal Year **[Insert Last Fiscal Year]]**, or is there any currently proposed *transaction*, to which the Company or any of its *affiliates* was or is to be a participant, and in which you or any of your *family members* had or will have a direct or indirect interest?[131] If your answer is "*YES*," please describe below.

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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QUESTION 28. Entities You Control[132]

Do you control, either directly or indirectly, any entities?

ANSWER: *YES* ☐ *NO* ☐

If your answer is "yes", please list all entities that you control, either directly or indirectly. If you have indirect or direct control over an entity, which in turn controls another entity, both entities are considered controlled by you and should be listed below.

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[131] This question is designed to elicit information that does not otherwise fall within the general scope of Item 404(a) but that may otherwise be material, or may, upon further investigation, fall within the general scope of Item 404(a). It is also designed to elicit information that, while not disclosable under Item 404(a), may need to be categorized by type and disclosed under Item 407(a)(3).

[132] This question is for the purpose of soliciting information which may need to be disclosed pursuant to FASB ASC 850, *Related Party Disclosures*. The adoption of Auditing Standard No. 18 by the Public Company Accounting Oversight Board has focused auditor attention on the controls and procedures utilized to collect the information necessary to satisfy the accounting standard.

QUESTION 29. Entities Over Which You Can Exert Significant Influence[133]

Can you exert significant influence, either directly or indirectly, over any entities, to the extent that the entity may be prevented from fully pursuing its own separate interests with regard to any transactions with the Company and its affiliates? A relationship that meets this level of influence should be identified even if there are no current or anticipated transactions between the entity and the Company and its affiliates.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "yes", please list all entities over which you can exert significant influence, either directly or indirectly. If you can exert significant influence, either directly or indirectly, over an entity which in turn can exert significant influence over another entity, both entities should be listed below.

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QUESTION 30. Other Employment and Directorships[134]

Are there any entities, other than those already listed in your responses to other questions in this Questionnaire, with which you serve as a member of the board of directors or have any other employment relationship, even if the directorship and/or employment relationship does not result in your ability to exert control or significant influence over the entity as described above?

ANSWER: *YES* ☐ *NO* ☐

If your answer is "yes", please list all such entities and indicate your position with the entity.

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[133] FASB ASC 850, *Related Party Disclosures*.
[134] FASB ASC 850, *Related Party Disclosures*.

QUESTION 31. Family Relationships[135]

Please list the individuals, and any of their affiliations in which they control or significantly influence an entity to the extent that the entity might be prevented from fully pursuing its own separate interests with regard to any transactions with the Company and its affiliates, who, in your judgement, might control or influence you, or who might be controlled or influenced by you, because of your family relationship. In most cases, this definition would include your spouse, children and other family members living in the same household as you. It may also include a parent, stepparent, sibling, in-law, family members to whom you provide or receive significant monetary support, or any other relatives in a position to have control or influence on you, or to be controlled or influenced by you.

Family Relationships

Names	Affiliations

QUESTION 32. Contracts with the Company

Are you, or is any *associate* of yours, a party to any contract (including any management contract or compensatory plan, contract or *arrangement*) with the Company or in which the Company or any *subsidiary* has a beneficial interest, or to which the Company has succeeded by assumption or assignment, which is to be performed in whole or in part at or after the end of the Company's last fiscal year, or which was entered into within the Company's last two (2) fiscal years? If your answer is "*YES,*" please describe below.[136]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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[135] FASB ASC 850, *Related Party Disclosures.*
[136] Form 10-K, Item 15. See Regulation S-K, Item 601(b)(10).

QUESTION 33. Personal Loans from the Company

Have you received at any time during the previous 24 months, or do you currently have outstanding any loan or extension of credit in the form of a personal loan from the Company or any of its *affiliates*?[137]

ANSWER: *YES* ☐ *NO* ☐

Has the Company or any of its *affiliates* arranged such a loan or an extension of credit in the form of a personal loan from any third party during the same time period?[138]

ANSWER: *YES* ☐ *NO* ☐

Is any such loan or extension of credit proposed to be extended to you during Fiscal Year **[Insert Current Fiscal Year]**?[139]

ANSWER *YES* ☐ *NO* ☐

If you answered "*YES*" to any of these questions, please describe below the material terms of the loan or extension of credit, including the original principal amount, the current balance and the material terms of the loan (including term, interest rate, etc.). Please also describe any modifications, amendments, renewals or forgiveness of such loans or extensions of credit made during the previous 24 months or intended to be made during Fiscal Year **[Insert Current Fiscal Year]** to any pre-existing loans or extensions of credit.

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[137] See Sarbanes-Oxley Act § 402. See also Cal. Corp. Code § 1502.1(a)(5) and § 2117.1(a)(5).
[138] See Sarbanes-Oxley Act § 402. See also Cal. Corp. Code § 1502.1(a)(5) and § 2117.1(a)(5).
[139] See Sarbanes-Oxley Act § 402. See also Cal. Corp. Code § 1502.1(a)(5) and § 2117.1(a)(5).

QUESTION 34. Compensation Committee Interlocks and Insider Participation

(a) During the last three (3) fiscal years, have you participated in deliberations of the Company's board of directors (or compensation committee) concerning executive officer compensation? If your answer is "*YES*," please describe the details below.[140]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(b) During the last three (3) fiscal years, have you (i) served as a member of the compensation committee (or other board committee performing equivalent functions or in the absence of any such committee, the entire board of directors) of another entity, which had an *executive officer* who served as a director or member of the compensation committee (or other board committee performing equivalent functions or in the absence of any such committee, the entire board of directors) of the Company or (ii) served as a director of another entity which had an executive officer who served as a member of the compensation committee (or other board committee performing equivalent functions or in the absence of any such committee, the entire board of directors) of the Company? If your answer is "*YES*," please describe the relationship below.[141]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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[140] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e) and instruction thereto.

[141] Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e) and instruction thereto.

QUESTION 35. Adverse Interests

Do you or any *associate* or *family member* of yours have an interest adverse to that of the Company or any of its *affiliates* in any pending or contemplated legal proceeding (including administrative proceedings and investigations by governmental authorities) to which the Company or any of its *affiliates* is or will be a party or of which any of its or their property is or will be the subject? If your answer is "*YES*," please describe.[142]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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QUESTION 36. Legal Proceedings; Investigations

Do you know of any legal, regulatory or administrative proceeding brought or contemplated by any governmental authority (including but not limited to antitrust, price-fixing, tax, environmental, copyright or patent litigation) to which the Company or any *subsidiary* is or may be a party or of which the property of the Company or any *subsidiary* is subject? If your answer is "*YES*," please give the details below.[143]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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QUESTION 37. Compensation Consultants

(a) **[**Other than **[Insert Compensation Consultant Name]**, which the **[Insert Committee Name]** has engaged, are**]** [Are] you aware of any compensation consultant that has been engaged by the Board or any committee of the Board? If your answer is "*YES*," please give details below. For all compensation consultants engaged (including **[Insert Compensation Consultant Name]**), please describe to the extent of your

[142] Form 10-K, Item 3; Form 10-Q, Item 1; Schedule 14A, Item 7(a) and Instruction 7(d)(3) to Item 14. See Regulation S-K, Item 103, Instruction 4.

[143] Form 10-K, Item 3; Form 10-Q, Item 1; Schedule 14A, Item 7(a) and Instruction 7(d)(3) to Item 14. See Regulation S-K, Item 103, Instruction 4.

knowledge, each such consultant's name, the committee (if not engaged by the Board) that has engaged such consultant, the amount paid or agreed to be paid to such consultant, and the material elements of the instructions or directions given to the consultants with respect to the performance of their duties under the engagement.[144]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(b) **[**Other than **[Insert Compensation Consultant Name]**, which management of the Company has engaged, are**]** [Are] you aware of any compensation consultant that has been engaged by management of the Company? If your answer is "*YES*," please give details below. For all compensation consultants engaged (including **[Insert Compensation Consultant Name**]), please describe to the extent of your knowledge, each such consultant's name, the committee (if not engaged by the board of directors) that has engaged such consultant, the amount paid or agreed to be paid to such consultant, and the material elements of the instructions or directions given to the consultants with respect to the performance of their duties under the engagement.[145]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(c) Do you have any business or personal relationship with: (i) any individual consultants employed by [**[Insert Compensation Consultant Name]]**[the compensation consultant described above]; (ii) [**[Insert Compensation Consultant Name]]**[the compensation consultant described above]; (iii) any other individual compensation consultant employed by a compensation consulting firm engaged by the board of directors, the compensation committee, or any other committee of the board of directors; or (iv) any other compensation consulting firm engaged by the board of directors,

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[144] Note, if the identity of the compensation consultant is not known, delete the bracketed language. Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e)(3)(iii).

[145] Note, if the identity of the compensation consultant is not known, delete the bracketed language. Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e)(3)(iii).

the compensation committee, or any other committee of the board of directors? If your answer is "*YES*," please give details below, describing the nature of the relationship and identifying the individual compensation consultant and/or compensation consulting firm with whom you have the relationship:[146]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

(d) Do you have any knowledge of, or reason to believe, that there is an actual or potential conflict of interest between (i) yourself or the Company, its directors or its executive officers and (ii) [**[Insert Compensation Consultant Name]**][the compensation consultant described above] (including its individual consultants) or any other compensation consultant (including its individual consultants) that has been engaged by the board of directors, the compensation committee or any other committee of the board of directors? If your answer is "*YES*," please give details below, describing the nature of the relationship, identifying the individual compensation consultant and/or compensation consulting firm, and the nature of the actual or potential conflict of interest:[147]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

(e) Please provide the information requested in Questions 37(c) and (d) with respect to any other advisors or counsel (including individual advisors or counsel associated with an advisory firm or law firm) that the [**Insert Committee Name**] has selected or from whom the [**Insert Committee Name**] has obtained advice (either directly or indirectly).

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[146] Note, if the identity of the compensation consultant is not known, delete the bracketed language. Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e)(3)(iii).

[147] Note, if the identity of the compensation consultant is not known, delete the bracketed language. Form 10-K, Item 11; Schedule 14A, Item 8. See Regulation S-K, Item 407(e)(3)(iii).

Description, if applicable:

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QUESTION 38. Foreign Corrupt Practices Act

(a) In connection with your response to this question, the following instructions apply:

(i) Your answers should relate to the activities or conduct of the Company and any *affiliate* of the Company, as well as to the conduct of any person who has acted or is acting on behalf of or for the benefit of any of them. Persons who have acted or are acting on behalf of or for the benefit of any entity include, but are not necessarily limited to, directors, officers, employees, agents, consultants and sales representatives.

(ii) Your answers should relate not only to activities or conduct within the United States, but outside the United States as well.

(iii) The terms “payments” and “contributions” include not only giving cash or hard goods but also giving anything else of value (e.g., services or the use of property).

(iv) The term “indirectly” means an act done through an intermediary. Payments to sales agents or representatives that are passed on in whole or in part to purchasers, or compensation or reimbursement to persons in consideration for their acts, are examples of acts done through intermediaries.

(v) Your answers should include not only matters of which you have direct personal knowledge, but also matters which you have reason to believe may have existed or occurred (for example, you may not “know” of your own personal knowledge that contributions were made by the Company to a political party in a foreign land, but, based upon information which has otherwise come to your attention, you may nonetheless have “reason to believe” that such a contribution was made. In that case, your response would be “*YES*.”)

(b) Do you have any knowledge or reason to believe that any of the activities or types of conduct enumerated below have been or may have been engaged in, either directly or indirectly, at any time:

(i) Any bribes or kickbacks to government officials or their relatives, or any other payments to such persons, whether or not legal, to obtain or retain business or to receive favorable treatment with regard to business.

ANSWER: *YES* ☐ *NO* ☐

(ii) Any bribes or kickbacks to persons other than government officials, or to relatives of such persons, or any other payments to such persons or their relatives, whether or not legal, to obtain or retain business or to receive favorable treatment with regard to business.

ANSWER: *YES* ☐ *NO* ☐

(iii) Any contributions, whether or not legal, made to any political party, political candidate or officeholder.

ANSWER: *YES* ☐ *NO* ☐

(iv) Any bank accounts, funds or pools of funds created or maintained without being reflected on the corporate books of account, or as to which the receipts and disbursements therefrom have not been reflected on the books of account.

ANSWER: *YES* ☐ *NO* ☐

(v) Any receipts or disbursements, the actual nature of which has been "disguised" or intentionally mis-recorded on the corporate books of account.

ANSWER: *YES* ☐ *NO* ☐

(vi) Any fees paid to consultants or commercial agents that exceeded the reasonable value of the services purported to have been rendered.

ANSWER: *YES* ☐ *NO* ☐

(vii) Any payments or reimbursements made to the Company's personnel to enable them to expend time or to make contributions or payments of the kinds or for the purposes referred to in subparts (i) – (vi) above.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*" to any of the foregoing questions, please describe the details of the subject transaction below:

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QUESTION 39. Description of *Associates*

Please note in the following table the full name, form (e.g., partnership, corporation, etc.), nature of business done by, and principal place of business of each *associate* of yours referred to in the answers to this Questionnaire and your relationship with such *associate(s)*, if applicable.[148]

Name	Form of Organization (if applicable)	Nature of Business	Principal Place of Business	Relationship

QUESTION 40. Change in Control

(a) Do you know of any *change in control* of the Company that has occurred during any of the Company's last three (3) fiscal years or during the Company's current fiscal year? If your answer is "*YES*," please provide a brief description of the *change in control*.[149]

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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(b) Do you know of any *arrangement*, including any pledge by any person of securities of the Company, the operation of which may at a subsequent date result in a *change in control* of the Company?[150] If your answer is "*YES*," please provide a brief description of the *arrangement(s)*.

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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[148] Form 10-K, Item 13; Schedule 14A, Items 7(b). See generally Regulation S-K, Item 404.
[149] Form 10-K, Item 11; Schedule 14A, Item 6(d). See Regulation S-K, Item 403(c).
[150] Form 10-K, Item 11; Schedule 14A, Item 6(d). See Regulation S-K, Item 403(c).

QUESTION 41. Regulatory Investigations

(a) Have you been involved in, or has any inquiry, investigation, lawsuit or disciplinary action been initiated against you by any regulatory or professional organization, including, but not limited to, the SEC, any state securities commission, FINRA (formerly NASD) or any foreign regulatory authority?

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please provide a detailed description of the applicable inquiry, investigation, lawsuit or disciplinary action, including a chronology and current status.

Description, if applicable:

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(b) Do you know of any inquiry, investigation, lawsuit or disciplinary action initiated against the Company, any of its officers, directors, principals, *associates*, *affiliates*, predecessors, or five percent (5%) stockholders by any regulatory organization including, but not limited to, the SEC, any state securities commission, FINRA (formerly NASD) or any foreign regulatory authority?

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please provide a detailed description, to the best of your knowledge, of any applicable inquiry, investigation, lawsuit or disciplinary action, including a chronology and current status.

Description, if applicable:

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QUESTION 42. Indemnification

Other than pursuant to a statutory provision or provision of the Company's charter or bylaws, do you know of any *arrangement* in which a director or officer of the Company is insured or indemnified in any manner against liability that he may incur in

his capacity as such, including, without limitation, any indemnification agreement with the Company? If your answer is "*YES*," please provide a brief description of the *arrangement(s)* in the space below.

ANSWER: *YES* ☐ *NO* ☐

Description, if applicable:

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QUESTION 43. Accounting Matters

(a) Do you believe that the systems of internal accounting controls of the Company in place during the Company's last fiscal year provided reasonable assurances that:

(i) Transactions were executed in accordance with management's general or specific authorization?

ANSWER: *YES* ☐ *NO* ☐

(ii) Transactions were recorded as necessary (a) to permit preparation of financial statements in conformity with generally accepted accounting principles (or other applicable criteria) and (b) to maintain accountability for assets?

ANSWER: *YES* ☐ *NO* ☐

(iii) Access to assets was permitted only in accordance with management's general or specific authorization?

ANSWER: *YES* ☐ *NO* ☐

(iv) The recorded accountability for assets was compared with the existing assets at reasonable intervals and appropriate action was taken with respect to any differences?

ANSWER: *YES* ☐ *NO* ☐

If you answered "*NO*" to any of subparts (i)–(iv), please explain your response on a separate sheet of paper and attach it to the Questionnaire.

(b) Do you know of any changes in the systems of internal accounting controls of the Company or any *subsidiary* that would result in a negative answer to any of the questions set forth in paragraph (a) above when applied to the Company's last three (3) fiscal years or to the Company's current fiscal year?

ANSWER: *YES* ☐ *NO* ☐

(c) Are you aware of any disagreements between the Company and its accountants?[151]

ANSWER: *YES* ☐ *NO* ☐

(d) Are you aware of any management letters prepared by the accountants for the Company identifying any reportable conditions?

ANSWER: *YES* ☐ *NO* ☐

QUESTION 44. Director Independence and Qualifications[152] (*Directors and Director Nominees Only*)

(a) Have you or any *family member* been employed within the past three (3) years by the Company or any parent or *subsidiary* of the Company?[153]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

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(b) **[Have you or has any *family member* accepted, either directly or indirectly, compensation in any form from the Company or any parent or *subsidiary* of the Company in excess of $120,000 during any period of twelve (12) consecutive months within the past three (3) years? <u>Do not</u> include compensation for board or committee service, compensation paid to a *family member* who is a non-executive employee of the Company or any parent or *subsidiary* of the Company, benefits under a tax-qualified retirement plan, and non-discretionary compensation. Note that excluded compensation to family members**

[151] Schedule 14A, Items 9(d), 13(a)(4) and 14, and Instruction 7(d)(9) to Item 14; Form 10-K, Item 9. See Regulation S-K, Item 304.

[152] This question covers only Nasdaq and NYSE director independence requirements. If the Company is listed on another exchange, please supplement with other relevant requirements accordingly. Please note that pursuant to Schedule 14A, Item 7(d) and Item 407(d)(2) of Regulation S-K, if the Company's board of directors has appointed a "non-independent" director as a member of the Company's audit committee, the Company is required to disclose the nature of the relationship that makes such director not independent and the reason for the board of directors' determination to appoint such person to the Company's audit committee.

[153] Rule 5605(a)(2) of the Nasdaq Marketplace Rules; NYSE Listed Company Manual § 303A.02(b)(i) and commentary thereto; and Exchange Act Rule 10A-3(b)(1)(ii). See also Schedule 14A, Item 7(c); Regulation S-K, Item 407(a); and Nasdaq Marketplace Rule 5605(c)(2)(A) (applicable to audit committee members). Note that service as an interim executive officer of the listed company does not disqualify a director from being considered independent. See IM 5605 Definition of Independence – Rule 5605(a)(2) of the Nasdaq Marketplace Rules and NYSE Listed Company Manual § 303A.02(b)(i) and commentary thereto.

should still be disclosed in Question 28.[154]] [Have you or any family member received during any twelve-month period within the last three (3) years, more than $120,000 in direct compensation from the Company or any parent or *subsidiary* of the Company (other than director and committee fees and pension or other forms of deferred compensation for prior service, provided that such compensation is not contingent in any way on continued service)? You need not consider compensation received by a director for former service as an interim executive officer. Also, do not consider compensation received by immediate family members for service as a non-executive employee of the Company or any parent or *subsidiary* of the Company. You need not consider individuals who are no longer *family members* as a result of legal separation or divorce, or those who have died or become incapacitated.[155]]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*" to either question, please describe:

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(c) Is any *family member* currently, or has any *family member* been within the past three (3) years, employed by the Company or by any parent or *subsidiary* of the Company as an *executive officer*?[156] **[You need not consider individuals who are no longer *family members* as a result of legal separation or divorce, or those who have died or become incapacitated.[157]]**

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please name such *family member* and indicate the *executive officer* position.

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[154] Rule 5605(a)(2)(B) of the Nasdaq Marketplace Rules. See also Schedule 14A, Item 7(c). See also Regulation S-K, Item 407(a).

[155] NYSE Listed Company Manual § 303A.02(b)(ii) and commentary thereto.

[156] Rule 5605(a)(2) (C) of the Nasdaq Marketplace Rules and NYSE Listed Company Manual § 303A.02(b)(i) and commentary thereto. See Schedule 14A, Item 7(c). See also Regulation S-K, Item 407(a).

[157] NYSE Listed Company Manual, General Commentary to Section 303A.02(b).

(d) **[Are you, or is a *family member*, a partner, controlling shareholder or *executive officer* of any entity or organization (including law firms[158] and charitable entities) to which the Company or any parent or *subsidiary* of the Company made, or from which the Company or any parent or *subsidiary* of the Company received, payments in the current or in any of the past three (3) fiscal years for property or services (other than payments which arose solely from investments in the securities of the Company or any parent or *subsidiary* of the Company and payments under non-discretionary charitable contribution matching programs) that exceed five percent (5%) of the recipient's consolidated gross revenue for that year, or $200,000, whichever is greater?[159]] [(1) Are you currently an employee of another entity (including any charitable organization) that has made payments to, or has received payments from, the Company or any parent or *subsidiary* of the Company for property or services in an amount which, in any of the last three (3) fiscal years, exceeds the greater of $1,000,000 or 2% of such other entity's consolidated gross revenues; (2) Is any *family member* currently an *executive officer* of another entity (including any charitable organization) that has made payments to, or has received payments from, the Company or any *subsidiary* for property or services in an amount which, in any of the last three (3) fiscal years, exceeds the greater of $1,000,000 or 2% of such other entity's consolidated gross revenues?[160] You need not consider individuals who are no longer *family members* as a result of legal separation or divorce, or those who have died or become incapacitated.]**

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*" to either question, please describe:

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(e) **[Are you or is a *family member* presently employed as an *executive officer* of another entity where any of the *executive officers* of the Company or any parent or *subsidiary* of the Company have served on the compensation committee (or other body performing similar functions) of such other entity in the current year or any of the past three (3) years?[161]] [Are you or is any *family member* currently, or within the last three (3) years have you or has any *family member* been,**

[158] See IM-5605 of the Nasdaq Marketplace Rules.

[159] Rule 5605(a)(2)(D) of the Nasdaq Marketplace Rules. See also Schedule 14A, Item 7(c). See also Regulation S-K, Item 407(a).

[160] NYSE Listed Company Manual § 303A.02(b)(v) and commentary thereto. See also Schedule 14A, Item 7(c). See also Regulation S-K, Item 407(a).

[161] Rule 5605(a)(2)(E) of the Nasdaq Marketplace Rules. See also Regulation S-K, Item 407(e).

an *executive officer* of another entity where any of the present *executive officers* of the Company or any parent or *subsidiary* of the Company at the same time serve or served on the other entity's compensation committee (or board of directors or other committee performing similar functions)?[162] You need not consider individuals who are no longer *family members* as a result of legal separation or divorce, or those who have died or become incapacitated.]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

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(f) **[Are you or is any *family member* a current partner of the outside auditor of the Company or any parent or *subsidiary* of the Company, or have you or has any *family member* been a partner or employee of the outside auditor in the past three (3) years and worked on the audit of the Company or any parent or *subsidiary* of the Company during that time?[163]] [(1) Are you or a *family member* a current partner of a firm that is the internal or external auditor of the Company or any parent or *subsidiary* of the Company; (2) Are you a current employee of such a firm; (3) do you have a *family member* who is a current employee of such a firm and personally works on the audit of the Company or any parent or *subsidiary* of the Company; or (4) were you or a *family member* within the last three (3) years (but no longer) a partner or employee of such a firm and personally worked on the audit of the Company or any parent or *subsidiary* of the Company during that time?[164]]**

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

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(g) Except as already noted elsewhere in the Questionnaire, to assist the Company in determining your independence pursuant to the Exchange Act, have you accepted at any time, or is there any proposed *arrangement* for you to accept, either directly or indirectly, any consulting, advisory or other compensatory fee from the Company or

[162] NYSE Listed Company Manual § 303A.02(b)(iv) and commentary thereto. See also Regulation S-K, Item 407(e).

[163] Nasdaq Marketplace Rule 5605(a)(2)(F).

[164] Section 303A.02(b)(iii) of the NYSE Listed Company Manual.

any of its *subsidiaries*?[165] For purposes of this question, "indirect" includes acceptance of such a fee by your spouse, minor children or stepchildren, and any of your children and stepchildren that share a home with you.[166] It also includes acceptance of such a fee by any entity that provides accounting, consulting, legal, investment banking or financial advisory services to the Company or any of its *subsidiaries* and in which you are a partner, member or officer, or in which you occupy a similar position; provided, however, that it does not include entities in which you are a limited partner or non-managing member, or those for which you occupy similar positions where you have no active role in providing services to the entity.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please provide a description, including amounts paid or payable on your behalf:

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(h) ***[Compensation Committee]*** *Members only* – The Company's board must consider your sources of compensation in determining your independence and eligibility to serve as a member of the [**Insert Name of Compensation Committee**]. This includes consideration of whether you receive compensation from any other person or entity that would impair your ability to be independent of management in connection with the duties of a compensation committee member or make independent judgments about the Company's executive compensation. For this purpose, please identify any sources of your compensation (other than any compensation identified in response to any other question in this Questionnaire) that could impair your ability to make independent judgments about the Company's executive compensation.[167]

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[165] Exchange Act Rule 10A-3(b)(1)(ii)(A) and Exchange Act Rule 10C-1(b)(1)(ii)(A). Nasdaq Marketplace Rule 5605(c)(2)(A)(ii) makes compliance with this SEC rule, along with all of the independence requirements of Exchange Act Rule 10A-3(b)(1), an explicit requirement for all audit committee members. While the NYSE and Nasdaq do not have a similar bright-line test for compensation committee independence, NYSE Listed Company Manual § 303A.02(a)(ii)(A) and revised Nasdaq Marketplace Rule 5605(d) make this a consideration the board of directors should take into account when determining independence for purposes of compensation committee members.

[166] See SEC Release No. 34-47654, Section I.A.2.

[167] Rule 5605(d)(2); NYSE Listed Company Manual § 303A.02

(i) Please indicate whether any of the following relationships exist:[168]

(i) Do you own or control, directly or indirectly, more than 10% of any class of the Company's voting securities?

ANSWER: *YES* ☐ *NO* ☐

(ii) Are you an *executive officer*, employee, general partner or managing member of the Company or any of its *affiliates*?

ANSWER: *YES* ☐ *NO* ☐

(iii) Are you otherwise an *affiliate* of the Company or any of its *affiliates* (other than in your capacity as a member of the Company's board of directors)? (Please consider any current or past relationship, circumstance, agreement or *arrangement* pursuant to which you or an entity in which you are an officer, general partner or managing member could be deemed to be an *affiliate* of the Company or any of its *affiliates*.)

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*" to any of these questions, please state the reason(s):

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(j) **[Have you participated in the preparation of the financial statements of the Company or any of its current *subsidiaries* at any time during the past three (3) years?[169]]**

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please describe:

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[168] Rule 5605(c)(2)(A)(ii) of the Nasdaq Marketplace Rules; NYSE Listed Company Manual § 303A.06; Exchange Act Rules 10A-3(b)(1)(ii)(B) and 10A-3(e)(1)(iii). Please note that Nasdaq "recommends" that a listed company disclose in its proxy statement if any director is deemed independent but falls outside the safe harbor provisions of Exchange Act Rule 10A-3(e)(1)(ii). See IM-5605-4 of the Nasdaq Marketplace Rules. NYSE Listed Company Manual § 303A.06(b) requires that all audit committee members meet both the requirements of Exchange Act Rule 10A-3(b)(1) and the requirements of NYSE Listed Company Manual § 303A.02.

[169] Rule 5605(c)(2)(A)(iii) of the Nasdaq Marketplace Rules.

(k) Please identify and describe any material relationship you or any of your *family members* currently have (or have had within the past three years) with any charitable organization or other non-public entity. Such relationships may include, but are not limited to, relationships as a partner, controlling shareholder, director or *executive officer* of the applicable organization or entity. Please include in your response the name of the applicable organization or entity, your relationship thereto and the applicable dates of such relationship.[170]

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(l) Please identify and describe any relationships you have with any other director or *executive officer* of the Company (other than serving as a director of the Company), whether personal or professional. This could include serving in some capacity in a charitable organization or other non-public entity, overlapping membership in an association or club and any other relationship in which you periodically interact with such person.[171]

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(m) Please provide any additional information that would be relevant, appropriate or helpful for the Company's board of directors to consider when evaluating your ability to exercise independent judgment in carrying out the responsibilities of a director and when determining whether you qualify as "independent" within the meaning of that term under the federal securities laws and the rules of **[Nasdaq] [the NYSE]**.[172] Please include in your response any information regarding relationships between you,

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[170] This question permits the Company to inquire about overlapping affiliations as a component of its general independence review. See, e.g., the concerns raised in *In re Oracle Corp. Derivative Litig.*, 808 A.2d 1206 (Del. Ch. 2002), *summary judgment granted for defendant directors by*, *In re Oracle Corp. Derivative Litig*., 2004 Del. Ch. LEXIS 177 (Del. Ch. Nov. 24, 2004). Note: the questionnaire could be revised to provide to the respondents a list of entities to which the Company donates, with a question to the respondents inquiring whether they have any relationships with any of the listed entities.

[171] This question also addresses concerns raised in *In re Oracle Corp. Derivative Litig.*, 808 A.2d 1206 (Del. Ch. 2002), *summary judgment granted for defendant directors by*, *In re Oracle Corp. Derivative Litig*., 2004 Del. Ch. LEXIS 177 (Del. Ch. Nov. 24, 2004).

[172] Rule 5605(a)(2) of the Nasdaq Marketplace Rules; NYSE Listed Company Manual § 303A.02 and commentary thereto. See also Regulation S-K, Item 407(a)(3), which requires disclosure of the types of transactions, relationships or arrangements, if any, that were not disclosed pursuant to Item 404(a) but which the board considered in determining that the particular director was independent under the relevant listing standards.

your *family members* or your *associates* on one hand, and the Company or any of its *affiliates* on the other hand, that has not been fully described elsewhere in the Questionnaire. Such relationships may be either direct or as a partner, member, shareholder or officer of an organization or entity that has a material relationship with the Company or any of its *affiliates*. Further, such relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships, among others.

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QUESTION 45. Financial Experience and Expertise *(Directors and Director Nominees Only)*

The Company is required pursuant to the Exchange Act to determine and disclose whether it has at least one "audit committee financial expert" (as defined by the SEC) serving on its audit committee.[173] Additionally, the Company's audit committee members must meet certain minimum financial experience and expertise thresholds pursuant to **[Nasdaq] [NYSE]** rules. Please respond to the following questions and requests if you are currently a member of the Company's audit committee or if you may be eligible to serve on the audit committee in the future.

(a) Are you able to read and understand fundamental financial statements, including the Company's balance sheet, income statement, and cash flow statement?[174]

ANSWER: *YES* ☐ *NO* ☐

[173] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 407(d)(5) and instructions thereto (which clarify that the disclosure is only required in a registrant's annual report). NYSE Listed Company Manual § 303A.12(c) requires the Company to submit an executed Written Affirmation to the NYSE annually and each time there is a change in the board or in any of these committees: nominating/corporate governance, compensation and audit. Nasdaq Marketplace Rule 5605(c)(4) requires the Company to provide notice to Nasdaq immediately upon learning of noncompliance with audit committee requirements; Rule 5625 requires prompt notification to Nasdaq when an executive officer becomes aware of material noncompliance with the Rule 5600 Series.

[174] Rule 5605(c)(2)(A)(iv) of the Nasdaq Marketplace Rules. Although this qualification is only required for members of the Company's audit committee, it is advisable for the board to know which members would be eligible to serve on the Company's audit committee if the need arose. Additionally, the commentary to NYSE Listed Company Manual § 303A.07(a) states that each member of the audit committee must become financially literate (if not already literate) within a reasonable period of time after his or her appointment to the audit committee.

(b) Please describe any past employment experience in finance or accounting or any other comparable experience, education or background in finance or accounting (including whether you have previously served as a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities).[175]

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(c) To assist the Company's board of directors in determining whether you meet the definition of an "audit committee financial expert," please list below any experience that may be helpful in the board's determination. Pursuant to SEC rules, an "audit committee financial expert" is a person who has <u>each</u> of the following attributes[176]:

(i) An understanding of generally accepted accounting principles and financial statements;

(ii) The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;

(iii) Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the Company's financial statements, or experience actively supervising one or more persons engaged in such activities;

(iv) An understanding of internal controls and procedures for financial reporting; and

(v) An understanding of audit committee functions.

In your response, please address whether the above-listed qualifications were obtained through any of the following means:

(A) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor, or experience in one or more positions that involve the performance of similar functions;

[175] Rule 5605(c)(2)(A) of the Nasdaq Marketplace Rules; NYSE Listed Company Manual § 303A.07(a) and commentary thereto.

[176] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 407(d)(5)(ii) and (iii). Note that the safe harbor described by Regulation S-K, Item 407(d)(5)(iv) emphasizes that a designation of audit committee financial expert does not impose additional duties, obligations or liability on the director; this information may be important to the directors filling out the questionnaire.

(B) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions;

(C) Experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing or evaluation of financial statements; or

(D) Other relevant experience that would be appropriate for the Company's board of directors to consider in determining your financial literacy or sophistication.

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(d) **[Do you currently serve, or have you been selected for future service, on an audit committee of any public company besides the Company?]**[177]

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please list the name of each public company on whose audit committee you currently or will serve.

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QUESTION 46. Iran Sanctions[178]

Under the Iran Threat Reduction and Syria Human Rights Act of 2012 (ITRA) the Company is required to disclose in its annual or quarterly filings under the Exchange Act whether it, or any affiliate, has during the period covered by the report knowingly engaged in any activity prohibited by the ITRA.

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[177] NYSE Listed Company Manual § 303A.07(a) and commentary thereto.

[178] The Iran Threat Reduction and Syria Human Rights Act of 2012 (ITRA) requires any company that must file annual or quarterly reports under Section 13(a) of the Exchange Act to disclose in those reports whether, during the period covered by the subject report, it or any affiliate has knowingly engaged in certain sanctionable activities under the act. The company may prefer to utilize a different means to solicit this information from directors and officers and therefore omit it from this questionnaire. Note also that ITRA requires disclosure of any sanctionable activities under the act in quarterly as well as annual reports, so annual solicitation of this information may not be sufficient for the company's needs.

Are you aware of the Company, or any affiliate, knowingly engaging in any of the following activities during the past 2 years?

- Development of Iran's petroleum resources, production of refined petroleum products in or exportation of refined petroleum products from Iran, or development of Iran's weapons of mass destruction (WMD) or other military capabilities;
- Transactions with financial institutions facilitating terrorist organizations or acts, sanctioned-party activities, WMD development or other prohibited activities in Iran as described in the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA);
- Transactions with financial institutions engaging in transactions benefitting the Iranian Revolutionary Guard Corps, as described in Section 104(d)(1) of CISADA;
- Transfers of goods or technologies to Iran that are likely to be used to commit human rights abuses;
- Transactions with terrorists whose property is blocked pursuant to Executive Order 13224;
- Transactions with WMD proliferators whose property is blocked pursuant to Executive Order 13382; and
- Transactions with the government of Iran as defined in Section 560.405 of Title 31 of the Code of Federal Regulations, without specific authorization of the government of the United States.

ANSWER: *YES* ☐ *NO* ☐

If your answer is "*YES*," please provide any information relevant, appropriate or helpful in the Company's evaluation of its obligations under the ITRA.

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REPORTING OBLIGATIONS

QUESTION 47. Reporting Obligations[179]

If you are an *executive officer*, director or owner of 10% of any class of the Company's equity securities, you are subject to the reporting requirements of Section 16(a) of the Exchange Act and the rules promulgated thereunder. These rules may require you to file, within forty-five (45) days of the end of the Company's fiscal year, an Annual Statement of Changes in Beneficial Ownership on Form 5 with the SEC reflecting certain of your transactions in the Company's equity securities.

It is not necessary to make this annual Form 5 filing if: (i) you have not engaged in any transactions in the Company's equity securities during the past year which require annual reporting on Form 5, or if you have made a prior, voluntary disclosure of such transactions on Form 4 prior to the date the Form 5 is due; and (ii) you have no holdings or transactions which you were otherwise required to report during Fiscal Year **[Insert Last Fiscal Year]** and which were not reported to the SEC.

NOTE: If you have already returned a separate Form 5 Certification or provided a Form 5 to the Company, you do not need to complete this question.

(a) On the basis of a review of all transactions in the Company's equity securities during Fiscal Year **[Insert Last Fiscal Year]** and all filings made by you or on your behalf with the SEC during such period, are you required to file a Form 5 with the SEC for the past fiscal year? **(Answering "No" shall constitute your representation that no Form 5 filing is required, and your agreement that the Company may retain this Questionnaire and provide it to the SEC upon request.)**

ANSWER: *YES* ☐ *NO* ☐

If you answered "*YES,*" please state the transactions that should be reported to the SEC.

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(b) Did you file any reports on Form 3 or Form 4 later than the deadline for filing such reports during Fiscal Year **[Insert Last Fiscal Year]** or any prior fiscal year (excluding any late reports that have previously been disclosed in the Company's proxy statements)?

ANSWER: *YES* ☐ *NO* ☐

[179] Form 10-K, Item 10; Schedule 14A, Item 7(b). See Regulation S-K, Item 405.

If you answered "*YES*," please state the details of the transaction or provide the date on which the late Form 3 or Form 4 report was filed with the SEC.

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If any information furnished by me in this questionnaire becomes inaccurate, incomplete <u>or otherwise changes</u>, I will promptly advise the Company to that effect and furnish any supplementary information that may be appropriate as a result of any developments, including the passage of time and any new relationships that may develop in the future.

The foregoing answers are correctly and fully stated to the best of my knowledge, information and belief after a reasonable investigation.

____________________	__________________________
Date	*Signature of Officer or Director*
	Print Name: ____________________

DEFINITIONS

An *affiliate* is a person or entity that directly or indirectly through one or more intermediaries controls, is controlled by, or is under common control with, another person or entity. The Company's *executive officers* would be considered *affiliates* of the Company.

Arrangement includes any contract, arrangement, agreement or understanding, whether written or oral.

Associate includes: (i) any corporation or entity (other than the Company) of which you are an officer, director or partner or of which you are, directly or indirectly, the beneficial owner of 10% or more of any class of equity securities; (ii) any trust or other estate in which you have a substantial beneficial interest or as to which you serve as trustee or in a similar capacity; (iii) your spouse; (iv) any relative of your spouse or any relative of yours who has the same home as you or who is a director or officer or key executive of the Company; and (v) any partner, syndicate member or person with whom you have agreed to act in concert with respect to the acquisition, holding, voting or disposition of shares of the Company's securities.

A *beneficial owner* of a security includes:

(i) any person who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise has or shares:

  (a) voting power, which includes the power to vote, or to direct the voting of, such security; and/or

  (b) investment power, which includes the power to dispose, or to direct the disposition of, such security.

(ii) any person who, directly or indirectly, creates or uses a trust, proxy, power of attorney, pooling arrangement or any other contract, arrangement or device with the purpose or effect of divesting such person of beneficial ownership; and

(iii) a person who has the right to acquire beneficial ownership of such security, as defined in clause (i) above, within sixty (60) days, including but not limited to any right to acquire: (a) through the exercise of any option, warrant or right, (b) through the conversion of a security, (c) pursuant to the power to revoke a trust, discretionary account, or similar arrangement, or (d) pursuant to the automatic termination of a trust, discretionary account or similar arrangement.

Shares *beneficially owned* by you include not only securities you hold for your own benefit, but also securities others hold for your benefit (regardless of whether or

how they are registered) such as, for example, securities held for you by custodians, brokers, relatives, trustees, and securities held for your account by pledgees, securities owned by a partnership in which you are a general or limited partner, and securities owned by any corporation which is or should be regarded as a personal holding corporation of yours. Bonus award shares held by a plan trustee, but as to which you cast votes and/or receive dividends, are deemed beneficially owned notwithstanding whether or not your complete rights in such shares have vested.

Change in control means a change in the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person or the Company, whether through the ownership of voting securities, by contract or otherwise.

A *control person* of a specified person or entity is a person who, directly or indirectly, through one or more intermediaries, controls the specified person or entity.

Equity Incentive Plan means any Incentive Plan or a portion of an Incentive Plan under which awards are granted that fall within the scope of Financial Accounting Standards Board's Accounting Standards Codification No. 718, *Stock Compensation*, as modified or supplemented. Such awards generally would include stock awards (restricted or otherwise), stock option awards and any other equity instruments.

Executive officer means the president, principal financial officer, principal accounting officer or controller, any vice president in charge of a principal business unit, division or function (such as sales, administration or finance), any other officer who performs a policy-making function or any other person who performs similar policy-making functions for the Company (or other entity that may be indicated).

Family member **[means a person's spouse, parents, children and siblings, whether by blood, marriage (including "in-law" relationships) or adoption, and anyone residing in the person's home.[180]] [means a person's spouse, parents, children, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and anyone (other than domestic employees) who shares the person's home. *Family member* does not include those who are legally separated or divorced, who are incapacitated, or who have died.[181]]** Please note that due to differences between SEC rules and the rules of Nasdaq **[the NSYE],** the definitions of *family member* and *immediate family member* are slightly different.

Immediate family member means a person's child, stepchild, parent, stepparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-

[180] Rule 5605(a)(2) of the NASD Marketplace Rules.

[181] General commentary to NYSE Listed Company Manual § 303A.02(b).

law or sister-in-law of such person, and any other individual (other than a tenant or employee) sharing the person's household. *Immediate family member* includes (1) only individuals who are currently related to the primary reporting person (e.g., a person who is divorced from a director's daughter would no longer be a son-in-law whose transactions must be reported) and (2) only those persons who are related by blood or step relationship to the primary reporting person or his or her spouse.[182] Please note that due to differences between SEC rules and the rules of Nasdaq **[the NYSE]**, the definitions of *family member* and *immediate family member* are slightly different.

Incentive Plan means any plan providing compensation intended to serve as incentive for performance to occur over a specified period, whether such performance is measured by reference to financial performance of the Company or an *affiliate*, the Company's stock price, or any other performance measure.

Member means any individual, partnership, corporation or other legal entity admitted to membership in FINRA (formerly NASD), and any officer or partner of such a *member* or the executive representative of such a *member* or the substitute for such a representative.

Non-Equity Incentive Plan means any incentive plan or portion of an incentive plan that is not an *Equity Incentive Plan*.

Promoter includes:

(i) Any person who, acting alone or in conjunction with one or more other persons, directly or indirectly takes initiative in founding and organizing the business or enterprise of an issuer; or

(ii) Any person who, in connection with the founding and organizing of the business or enterprise of an issuer, directly or indirectly receives in consideration of services or property, or both services and property, 10% or more of any class of securities of the issuer or 10% or more of the proceeds from the sale of any class of such securities. However, a person who receives such securities or proceeds either solely as underwriting commissions or solely in consideration of property shall not be deemed a *promoter* within the meaning of this paragraph if the person does not otherwise take part in founding and organizing the enterprise.

Related person means any director or executive officer of the Company, any director nominee, any *immediate family member* of a director or executive officer of the Company, any security holder who owns more than 5% of any class of the

[182] Regulation S-K Compliance and Disclosure Interpretations, Interpretation 230.01.

Company's voting securities (i.e., common stock and preferred stock are treated as separate classes), and any *immediate family member* of such a security holder.

SARs are stock appreciation rights payable in cash or stock, including *SARs* payable in cash or stock at the election of the Company or the holder.

Stock options includes all options, warrants, or rights to purchase securities of the Company, other than those issued to security holders as such on a pro rata basis.

Subsidiary includes any company of which more than 50% of the voting shares are owned by the Company.

Transaction includes, but is not limited to, any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness) or any series of similar transactions, arrangements or relationships.

Underwriter includes an underwriter, underwriters' counsel, financial consultants and advisers, finders, members of the selling or distribution group, any *member* participating in the public offering and any and all other persons associated with or related to the foregoing.

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