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Proposed Rules Expand Compensation and Corporate Governance Disclosure Requirements for Public Companies

On July 10, 2009, the Securities and Exchange Commission (SEC) published proposed amendments to Regulation S-K and to Forms 10-Q, 10-K and 8-K to expand the current compensation and corporate governance disclosure requirements for proxy and information statements, annual reports and registration statements, and accelerate the deadline to report voting results from public company shareholder meetings. If these proposed amendments are approved, they will be effective for the 2010 proxy season. The SEC established a 60-day comment period for the proposal, which ends September 15, 2009.

The Proposed Amendments

The rules proposed by the SEC include the following amendments:

Additional Compensation Discussion and Analysis Disclosure Regarding the Effect of a Company's Overall Compensation Policies on Risk Management

The proposed amendments to the Compensation Discussion and Analysis (CD&A) requirements are intended, in part, to highlight the relationship of a company's overall compensation policies to risk. They apply to a company's broader compensation policies and overall compensation practices for employees generally, including non-executive officers, if risks arising from those compensation policies or practices may have a material effect on the company. In explaining its reasons for this change, the SEC cited concerns that the current market turmoil was due in part to compensation policies (particularly at large financial institutions) that created short-term incentives misaligned with the long-term well-being of the companies, as opposed to more "well designed" incentives that would encourage "innovation and

appropriate levels of risk taking." To address these issues, the SEC is proposing to require additional CD&A discussion of the level of risk employees may be encouraged to take to achieve their compensation objectives, but only in those cases where risks arising from such compensation policies or practices may have a **material** impact on the company. The amendment does not alter existing disclosure requirements concerning named executive officers.

The proposed rule includes a non-exhaustive list of examples of situations in which the presence of certain compensation policies may require additional disclosure, including:

- at a business unit of a company that carries a significant portion of the company's risk profile;
- at a business unit where compensation is structured significantly different than other units within the company;
- at business units that are significantly more profitable than others within the company;
- at a business unit where compensation expense represents a significant portion of the unit's revenues;
- and
- areas where significant variation from the overall risk and reward structure of the company exists.

Companies may want to review and analyze the current structure and application of their compensation policies to determine whether risks arising from those policies and practices may have a material effect on the company. If a company identifies additional areas where disclosure may be necessary, the company and its Compensation Committee may wish to consider what the disclosure might include, and evaluate whether a modification to the policy is necessary prior to the 2010 proxy season.

Revisions to Equity Award Valuations in the Summary Compensation Table

The proposed amendment to the Summary Compensation Table and Director Compensation Table revises the disclosure of stock awards and option awards to require reporting of the aggregate "grant date fair value" of these awards (computed in accordance with FAS 123R), in place of the currently mandated disclosure of the dollar amount recognized with respect to such awards for financial statement reporting purposes for each fiscal year (also computed per FAS 123R). The SEC believes that this change will allow investors to better evaluate the amount of equity compensation awarded to each director and named executive officer (NEO) during each covered year and, therefore, may provide a more accurate indication of which individuals the company intended to compensate most highly for each period. The proposal would reverse a last-minute decision by the SEC to abandon this approach in favor of the existing disclosure requirement when the current rules were adopted in

2006. The SEC's proposed transition guidance would require application of this change to the equity award values reported for NEOs for all three years covered by the Summary Compensation Table in a corporation's 2010 proxy statement. If applying this proposed amendment would change which executives are considered NEOs, then the Summary Compensation Table would have to be revised accordingly.

Additional Disclosure Describing Specific Qualifications of Directors and Nominees

The proposals would expand proxy statement disclosures regarding the qualifications of directors and director nominees in the following three respects:

requiring additional disclosures concerning the particular experience, qualifications, attributes or skills that qualifies each director or director nominee to serve on the company's board of directors as of the time of the filing, including qualification to serve as a member of any board committee on which the person serves or is selected to serve (if then known) in light of the company's business and structure;

requiring directors or director nominees to disclose any positions they have held as a director of other public companies at any time during the past five years (as opposed to the existing requirement to disclose only current directorships); and

extending the period in which directors and director nominees would be required to disclose their involvement in certain legal proceedings under Item 401(f) of Regulation S-K from 5 years to 10 years.

New Disclosure Describing the Company's Leadership Structure and the Board's Role in Risk Management

The proposed rules would require an additional disclosure concerning the company's leadership structure, including a discussion of why the company believes that the chosen structure best serves the interests of the company based upon the following considerations:

whether and why the company has chosen to combine or separate the principle executive officer and board chair positions; and

where the board chair and principal executive positions are combined, a discussion of whether and why the company has designated a lead independent director to chair meetings of the independent directors, and the specific role the lead independent director plays in the company's leadership.

The proposed amendments also require additional disclosure about the board's role in the company's risk management process, including the relationship between the board and senior management in managing the material risks facing the company (which the SEC noted could include management of credit risks, liquidity risks, and operational risks, among others). The proposal suggests that such disclosure cover:

how the board implements and manages its risk management function (e.g., through the board as a whole or through a committee, such as the audit committee);

whether the person(s) who oversee risk management report(s) directly to the board as a whole, to a committee (such as the audit committee), or to one of the other standing committees of the board; and

whether and how the board, or the designated board committee, monitors risk.

These additional disclosures are intended to provide increased transparency for investors concerning the issue of how a company's board functions in relation to the risk management process.

New Disclosure Detailing the Nature of the Company's Relationship to Compensation Consultants

The proposals would require additional specified disclosures regarding the fees paid to outside compensation consultants and their affiliates where they play any role in determining or recommending the amount or form of executive or director compensation, **if** they also provide other services to the company (such as benefits administration, human resources consulting or actuarial services). According to the SEC, the combination of these additional services with an advisory role in executive compensation could "create the appearance, or risk, of a conflict of interest that could call into question the objectivity of the consultants' executive pay recommendation." In these instances, the amendments would require the company to disclose the following:

the nature and extent of all additional services provided to the company or its affiliates by the compensation consultant and its affiliates during the past fiscal year;

the aggregate fees paid for such additional services, as well as the aggregate fees paid for determining or recommending the amount or form of executive or director compensation;

whether management made, recommended, screened, or reviewed the decision to engage the compensation consultant to provide non-executive compensation services; and

whether the board of directors or the compensation committee has approved all of such services provided by the compensation consultant in addition to executive compensation services.

Companies and their Compensation Committees may wish to review their current relationships with compensation consultants, focusing on identifying any conflicts of interest to determine whether additional disclosure would be necessary, and whether modifications to the relationship would be advisable prior to the 2010 proxy season.

Changes to How Shareholder Voting Results are Reported

The SEC proposed transferring disclosure of shareholder voting results from Forms 10-Q and 10-K to Form 8-K. This change would require a company to file a Form 8-K describing the shareholder voting results within four days following the meeting at which the vote was held.

Submitting Comments

Comments may be submitted to the SEC in support of, or in opposition to, the proposed amendments through the SEC's Internet Comment form, via e-mail or via mail in triplicate, addressed to:

Elizabeth M. Murphy
Secretary, Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

All comment submissions, regardless of the method employed, must reference "File Number S7-13-09" in the subject line. The comment period ends on September 15, 2009.

What This Means to You

Public companies are advised to begin considering the potential impacts of the required disclosures by examining their current disclosure practices with respect to compensation including policies and practices as they relate to risk-taking behavior by employees, their current director nominee qualification requirements, their relationships with any compensation consultants, their existing leadership structures, and how they report the results of shareholder votes.

Contact Info

If you have any questions about this or any other corporate governance matters, please contact your Husch Blackwell Sanders attorney.

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