

## CORPORATE AND SECURITIES LAW

*Alert*

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY &amp; SIMS PLC

SEC Releases Proposed Rules on Corporate Governance,  
Executive Compensation and Proxy Solicitation

July 15, 2009

On Friday, July 10, 2009, the SEC released proposed rules to enhance certain compensation and corporate governance disclosures. Additionally, the proposed rules clarify certain proxy rules and address issues that have arisen in the proxy solicitation process. The SEC has requested comments on each of these proposals, and we expect that the proposed rules may undergo some revision before becoming final. What follows is a brief summary of the proposed rules.

**Enhanced Director and Nominee Disclosure**

The SEC is proposing amendments to Item 401 of Regulation S-K to require additional disclosure about the backgrounds of directors and nominees for director. The proposed amendments would require disclosure of the following new items:

- **Director experience and qualifications.** The proposed amendments would require companies to briefly discuss for each director or person nominated to become a director the specific experience, qualifications, attributes or skills that qualify that person to serve as a director for the company at the time the disclosure is made, and as a member of any committee the person serves on or is chosen to serve on (if known), in light of the company's business and structure. If material, the disclosure would cover more than the past five years, and include information about the person's risk assessment skills, particular areas of expertise or other relevant qualifications. The SEC is also seeking comment on whether disclosure should be required regarding additional factors that a nominating committee considers when selecting someone for a position on the board, such as diversity.
- **Directorships held within the last five years.** The proposal would require disclosure of any directorships at public companies held by each director or nominee for director at any time during the past five years, even if the director or nominee for director no longer serves on that board.
- **Expanded time period for which disclosure of legal proceedings is required.** The proposed amendments would lengthen from five to 10 years the time during which disclosure

is required of any material legal proceedings in which a director or nominee for director was involved.

### Description of Company Leadership Structure

The SEC is proposing adding a new disclosure requirement to Item 407 of Regulation S-K that would require a description of a company's leadership structure. This disclosure would include the following items:

- **Justification of leadership structure.** Companies would be required to indicate why they have determined their leadership structures are appropriate given their specific characteristics or circumstances. The proposed amendments would also require companies to disclose whether the same person serves as both principal executive officer and chairman of the board, or whether two individuals serve in those positions. If one person serves as both principal executive officer and chairman of the board of a company, the company would be required to disclose whether it has a lead independent director and describe the specific role the lead independent director plays in the leadership of the company.
- **Board's role in risk management.** The proposal would require companies to disclose the extent of their board of directors' role in their risk management and the effect this has on the company's leadership structure.

### Enhanced Compensation Disclosures

In the context of compensation disclosures, the SEC is proposing two amendments to Item 402 of Regulation S-K.

- First, the proposal would require a company to discuss and analyze its compensation policies and practices for employees generally, including non-executive officers, if the risks arising from those compensation policies or practices could potentially have a material effect on the company. A footnote to the proposal also clarifies that risk disclosure is already required in the CD&A to the extent such risk considerations are a material aspect of the company's compensation policies or decisions for the named executive officers.
- Second, the proposal would revise the disclosure of stock and option awards in the Summary Compensation Table and Director Compensation Table to require disclosure of the aggregate grant date fair value of stock and option awards for the covered fiscal year (computed in accordance with FAS 123R) instead of the dollar amount recognized for financial statement reporting purposes for the covered fiscal year.
- In addition to the executive compensation disclosure amendments contained in the proposal and requests for comments on those amendments, the SEC has issued a broad call for executive compensation disclosure comments, including comments with respect to: expanding compensation disclosure to all executive officers; stricter requirements regarding performance target disclosure; the relationship between the CD&A and the Compensation Committee Report; requiring disclosure concerning "hold to retirement" and clawback

provisions; requiring disclosure of internal pay equity ratios; and requiring quantitative disclosure of the benefits to executives of gross-ups.

### **Compensation Consultant Disclosures**

The SEC is also proposing amendments that would require companies to provide additional disclosure about compensation consultant relationships and fees. Under the proposed amendments, companies would be required to disclose fees paid to compensation consultants that played any role in determining or recommending the amount or form of executive or director compensation and also provided additional services to the company (i.e. benefits administration, human resources consulting, or actuarial services). The fee disclosure would require: (1) the aggregate fees for determining or recommending the amount or form of executive and director compensation and (2) the aggregate fees paid to the consultants (and their affiliates) for any additional services provided. In addition to the fee disclosure, the proposed amendments would require a description of the nature and extent of the additional services provided to the company by the compensation consultant and its affiliates in the last fiscal year. Companies would also be required to disclose: (1) whether the decision to engage the compensation consultant or its affiliates for non-executive compensation services was made, recommended, subject to screening or reviewed by management; and (2) whether the board of directors or the compensation committee has approved all of these services in addition to executive compensation services.

### **Reporting of Voting Results on Form 8-K**

As has been urged by some observers, the SEC's proposed rules generally would require companies to disclose shareholder voting results on a Current Report on Form 8-K within four business days of the date of the meeting at which a vote was held (or shareholder action was otherwise taken), rather than in the next Form 10-Q or Form 10-K, as under the current rules. The proposed rules provide that if the matter to be voted on is a contested election of directors and the final results are not definitively determined by the end of the meeting, companies will be required to disclose preliminary voting results on Form 8-K within four business days after the meeting and will be required to disclose final voting results on an amended Form 8-K within four business days after the results are certified.

### **Clarification of Certain Proxy Solicitation Rules**

The SEC's proposed rules also would clarify certain proxy solicitation rules. In particular, the proposed rules would codify recent SEC no-action guidance that a non-management party soliciting votes for its nominees in a short-slate proxy fight may round out its slate (up to the total number of director positions then subject to election) by soliciting authority to vote for the nominees of another non-management party (that is not part of the same group as the soliciting non-management party) in addition to being permitted to solicit authority for some of management's nominees. (The current SEC rules do not explicitly give a non-management party the right to round out its slate with the nominees of another non-management party.)

These proposed rules, in conjunction with the SEC's proposed proxy access rules which were released on June 10, create an interesting construct with respect to the ability of shareholders to pick their preferred candidates in a contested director election. The SEC's proposed proxy

access rules create a form of universal ballot with respect to shareholder director nominees nominated under the new Rule 14a-11; under these rules, a proxy card distributed by a registrant must allow shareholders to vote for any combination of management's nominees and/or Rule 14a-11 nominees. However, to the extent that shareholder nominees are nominated outside of the Rule 14a-11 process (through a proxy statement distributed by a dissident shareholder), shareholders will generally not be entitled to mix and match their preferred choice of management and dissident shareholder candidates unless they vote in person at the company's meeting. This is because, under applicable SEC rules, if a shareholder completes a registrant's proxy card, the shareholder will only be entitled to vote for some or all of management's nominees (and any Rule 14a-11 nominees) listed on this proxy card, while if the shareholder completes the proxy card of a dissident shareholder, the shareholder will only be entitled to vote for some or all of the nominees listed on the dissident's proxy card (which will include all of the dissident's nominees, and may include some of the nominees of management and/or another dissident shareholder).

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