

M A Y E R
B R O W N
R O W E
& M A W

Understanding the New Executive Compensation Rules

Thursday, September 14, 2006

Edward S. Best

Marc H. Folladori

Michael L. Hermsen

Wayne R. Luepker

Laura D. Richman

David A. Schuette

Mayer, Brown, Rowe & Maw LLP

Topics to be Covered

- Presentations
 - An Overview of the New Rules
 - Compensation Discussion and Analysis
 - Compensation Committee Report
 - New and Revised Tabular Disclosures
 - Defining and Disclosing Perks
 - New Director Compensation Disclosures
 - New Related Party Transaction Disclosure
 - Disclosure Controls and Procedures
 - Form 8-K and Compensation Disclosure
- Roundtable Discussion
 - How the New Rules Will Impact Compensation Committee Procedures and Decisions

Overview of New Rules

- Key objectives
 - Greater context for quantitative presentations
 - More comprehensive and focused quantitative presentations
 - Enhanced disclosure of retirement, deferred compensation and post-termination benefits
 - Greater attention to perquisites disclosure
 - Streamlined current reporting on Form 8-K

Overview of New Rules

- New Rules
 - CD&A
 - Compensation Committee Report
 - Compensation Committee Procedures
 - Total Compensation
 - Holdings of Equity-Related Interests Received As Compensation
 - Retirement and Post-Employment Benefits

Overview of New Rules

- New Rules (Cont.)
 - Director Compensation
 - Form 8-K Disclosure of Executive Compensation Arrangements
 - Related Person Transactions
 - Corporate Governance Disclosure
 - Disclosure of Pledges
 - Plain English

Overview of New Rules

- *Timing and Transition*
 - The new rules will generally apply to proxy statements for companies whose fiscal year ends on or after December 15, 2006 and to Securities Act registration statements filed or amended on or after that date
 - The new requirements with respect to the summary compensation table are to be phased in on a going-forward basis and do not require companies to restate disclosure relating to fiscal years prior to 2006
 - The summary compensation table will include only one fiscal year's compensation information for the 2007 proxy season. An additional year of disclosure will be included over each of the next two years, until three full fiscal years are presented in the summary compensation table
 - The Form 8-K amendments are effective for events that occur on or after November 7, 2006

Compensation Discussion and Analysis

- The heart of the new executive compensation disclosure rules
- Provides an overview for the compensation tables and narrative discussion that follows
- Appears at the beginning of the compensation disclosure
- A principles based explanation of the compensation decisions for the named executive officers
- No boilerplate

Differences Between CD&A and Prior Compensation Committee Report

- The CD&A is a company report
- More analysis is required
- Specific discussion of all named executive officer compensation
- The CD&A is filed, not furnished
- The CD&A is subject to a plain English requirement

Questions to be Covered in the CD&A

- What are the objectives of the company's compensation program?
- What is the compensation program designed to reward?
- What is each element of compensation?
- Why does the company choose to pay each element of compensation?
- How does the company determine the amount for each element of compensation?
- How does each element of compensation and the company's decisions regarding that element fit into the company's overall compensation objectives and affect decisions regarding other elements of compensation?

Examples of Issues to Cover in the CD&A

- Policies for allocating between long-term and currently paid out compensation
- Policies for allocating between cash and non-cash compensation, and among different forms of non-cash compensation
- For long-term compensation, the basis for allocating compensation to each different form of award
- The basis for determining when an award is granted
- What specific items of corporate performance are taken into account in setting compensation policies and making compensation decisions

Additional Examples of Issues to Cover

- How specific elements of compensation are structured and implemented to reflect items of
 - the company's performance, and
 - the executive's individual performance
- Policies and decisions regarding the adjustment or recovery of awards or payments if performance measures are restated or adjusted in a manner that would reduce the award or payment
- The factors considered in decisions to increase or decrease compensation materially
- How compensation or amounts realizable from prior compensation are considered in setting other elements of compensation
- The basis for selecting the particular triggering events for termination or change-in-control payments

More Issues to Cover

- The impact of accounting and tax treatments of a particular form of compensation
- The company's equity or other security ownership requirements or guidelines, and any company policies regarding hedging the economic risk of such ownership
- Whether the company engaged in any benchmarking of total compensation or any material element of compensation, identifying the benchmark and, if applicable, its components
- The role of executive officers in the compensation process
- Any other principle, policy or decision that is material₁₁

Timeframe to be Covered in the CD&A

- Depends on facts and circumstances
- Relevant decisions from the prior fiscal year(s)
- Actions in the subsequent fiscal year

Option Discussion

- Enhanced Disclosure in two general categories
 - Timing of particular grant dates
 - Methods used to select terms such as exercise price

Questions to be Answered for Timing of Options

- Is there a program, plan or practice to time grants in coordination with release of material non-public information?
- How does timing of option grants to executives fit in the context of option grants to employees generally?
- What is the compensation committee's role in approving such a program or practice?
- What is the role of the executive officers in option timing?
- Are option grant dates for new executive officers coordinated with the release of material non-public information?
- Does the company time the release of non-public information to affect the value of executive compensation?

Other Option Issues

- Is exercise price based on stock price on a date other than the actual grant date?
- Are formulas used to set price?
- Address option grants to directors as well as option grants to employees

Discussion of Individual Employees

- Covers all named employees, not just the CEO
- If material differences in compensation policies among named executive officers, discuss separately
- Otherwise, policies and decisions may be discussed as a group

Implications of the CD&A Being Filed

- Part of the proxy statement and other filings
- Subject to liability under Section 14 of the Exchange Act governing proxies as well as Section 18 liabilities under the Exchange Act for misleading statements
- If incorporated into a Securities Act filing such as a registration statement, it is also subject to Securities Act liabilities
- Subject to CEO and CFO certifications

New Compensation Committee Report

- A more streamlined report
- Must state that
 - the Compensation Committee reviewed and discussed the CD&A with management, and
 - based on the review and discussion, the Compensation Committee recommended that the CD&A be included in the 10-K and proxy statement
- The Compensation Committee Report remains furnished, not filed
- The Compensation Committee Report provides an underpinning for the CEO and CFO certifications

Transitioning from the Old Compensation Committee Report to the New CD&A

- CD&A is a new project
- Likely to be time-consuming to prepare the initial CD&A
- Some of the disclosures that are needed may be found in the existing Compensation Committee Report, but more detail needed
- Expect SEC scrutiny of the CD&A

Performance Graph

- Retained, but not as part of compensation disclosures
- Now part of the market information of Item 201 of Regulation S-K
- Performance graph will be part of the annual report, not proxy statement

Plain English Requirements

- Clear concise section
- Short sentences
- Active voice
- Everyday word, not jargon or technical terminology
- Descriptive headings
- Tabular presentations where appropriate

2006 Summary Compensation Table

- Major changes:
 - Principal financial officer is automatically a named executive officer
 - All numbers in the table are to be presented in dollars
 - A total column has been included as the last column
 - Deferred compensation must be included in the appropriate column in the year earned

2006 Summary Compensation Table

- Major changes (continued):
 - Stock Awards and Option Awards are to be presented at their FAS 123R value
 - The LTIP Payouts column has been replaced by a Non-Equity Incentive Plan Compensation column
 - A new column has been added to report the change in pension value and above-market or preferential earnings on non-qualified deferred compensation
 - Repriced or materially modified options are to be included at their incremental FAS 123R value

2006 Summary Compensation Table

- Major changes (continued):
 - The All Other Compensation column is to include all other compensation earned by a named executive officer that has not otherwise been reported in the table including:
 - Perquisites in excess of \$10,000 in the aggregate
 - Amounts paid or accrued pursuant to a termination or employment or a change-in-control
 - Annual company contributions to defined contribution plans
 - Insurance premiums paid by the company with respect to life insurance for the benefit of a named executive officer

2006 Summary Compensation Table

- Major changes (continued):
 - Tax gross-ups
 - Earnings paid on stock or option awards that were not factored into the FAS 123R calculation
 - The FAS 123R value of company securities purchased at a discount from the market price unless the discount is generally available

2006 Grants of Plan-Based Awards

- Reflect all plan-based awards made during the last fiscal year
- Separate columns will reflect:
 - The grant date
 - Non-equity incentive plan awards
 - Equity incentive plan awards
 - All other stock awards
 - All other option awards
 - The exercise or base price of option awards

2006 Grants of Plan-Based Awards

- Each grant must be separately disclosed
- Additional columns must be added if:
 - Closing price of stock on date of grant is less than exercise price of option
 - If date of board action is different than grant date
 - Awards under a non-equity incentive plan are denominated in units or other rights

2006 Grants of Plan-Based Awards

- Narrative disclosure to accompany the Summary Compensation Table and Grants of Plan-Based Awards table
- Discuss the additional material factors necessary to understand the information disclosed in the previous two tables, which may include:
 - Material terms in employment agreements
 - Repricing or material modification of terms of outstanding awards
 - Material terms of awards made during the year
 - An explanation of the amount of salary and bonus in proportion to total compensation
- So-called Katie Couric provision has been reproposeed for additional comment

2006 Outstanding Equity Awards at Fiscal Year-End

2006 OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

Name	Option Awards					Stock Awards			
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$)
Principal Executive Officer									
Principal Financial Officer									
Named Executive Officer 1									
Named Executive Officer 2									
Named Executive Officer 3									

2006 Outstanding Equity Awards at Fiscal Year-End

- Separate columns will reflect:
 - Number of securities underlying unexercised options that are exercisable
 - Number of securities underlying unexercised options are that unexercisable
 - Number of securities underlying unexercised unearned options under equity incentive plans
 - The option exercise price
 - The option expiration date

2006 Outstanding Equity Awards at Fiscal Year-End

- Separate columns will reflect: (cont.)
 - Number of shares of stock that have not vested
 - Market value of shares of stock that have not vested
 - Number of shares underlying awards under equity incentive plans that have not vested
 - Market value of shares underlying awards under equity incentive plans that have not vested
- Each outstanding option grant must be reported on a separate line item

2006 Option Exercises and Stock Vested

2006 OPTION EXERCISES AND STOCK VESTED

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
Principal Executive Officer				
Principal Financial Officer				
Named Executive Officer 1				
Named Executive Officer 2				
Named Executive Officer 3				

2006 Option Exercises and Stock Vested

- The table will disclose:
 - The number of shares acquired upon the exercise of an option
 - The value received upon exercise of an option
 - The number of shares acquired upon the vesting of restricted stock
 - The value realized upon vesting of restricted stock

2006 Pension Benefits

2006 PENSION BENEFITS

Name	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefit (\$)	Payments During Last Fiscal Year (\$)
Principal Executive Officer				
Principal Financial Officer				
Named Executive Officer 1				
Named Executive Officer 2				
Named Executive Officer 3				

2006 Pension Benefits

- For each plan that provides for payments or benefits at, following or in connection with retirement, this table will disclose:
 - Plan name
 - Number of years of credited service
 - Present value of the accumulated benefit under the plan
 - Any payments made during the last fiscal year

2006 Pension Benefits

- Discuss the material factors necessary to understand the information disclosed in the table, which may include:
 - Material terms and conditions of benefits available under the plan
 - Specific elements of compensation included in applying the benefit formula
 - If a named executive officer participates in more than one plan, the reasons for each plan
 - Company policies with regard to such matters as granting extra years of service

2006 Nonqualified Deferred Compensation

2006 NONQUALIFIED DEFERRED COMPENSATION

Name	Executive Contributions in Last FY (\$)	Registrant Contributions in Last FY (\$)	Aggregate Earnings in Last FY (\$)	Aggregate Withdrawals/ Distributions (\$)	Aggregate Balance at Last FYE (\$)
Principal Executive Officer					
Principal Financial Officer					
Named Executive Officer 1					
Named Executive Officer 2					
Named Executive Officer 3					

2006 Nonqualified Deferred Compensation

- This table will disclose:
 - Executive contributions during the last fiscal year
 - Company contributions during the last fiscal year
 - Aggregate earnings during the last fiscal year
 - Aggregate withdrawals and distributions during the last fiscal year
 - Aggregate balance at last fiscal year end

2006 Nonqualified Deferred Compensation

- Discuss the material factors necessary to understand the information disclosed in the table, which may include:
 - Types of compensation permitted to be deferred, and any limitations on the extent to which deferral is permitted
 - Measures for calculating interest and other plan earnings, quantifying interest rates and other earnings measures applicable during the last fiscal year
 - Material terms with respect to payouts, withdrawals and other distributions

2006 Nonqualified Deferred Compensation

- Narrative disclosure to accompany the Pension Benefits table and Nonqualified Deferred Compensation table
- Discuss the specific aspects of any written or oral agreement that provides for payments at, following or in connection with resignation, severance, retirement or termination of a named executive officer, including:

2006 Nonqualified Deferred Compensation

- Specific circumstances that would trigger payment
- Estimated payments and benefits that would be paid in each covered circumstance
- Specific factors used to determine the appropriate payment and benefit level
- Material conditions applicable to the receipt of payments or benefits
- Any other material features

Perquisites Disclosure Controversy

- *In the Matter of General Electric Company*, Adm. Proceeding Rel. No. 50426 (Sept. 23, 2004)
- *In the Matter of Tyson Foods Inc. and Donald Tyson*, Lit. Rel. No. 19208 (April 28, 2005)
- *SEC v. G. Gadel and D. Skrypek*, Lit. Rel. No. 19270 (June 7, 2006)
- *Cardinal Equity Value Partners v. infoUSA* (“That Other Guy From Omaha,” G. Morgenson, The New York Times, sec. 3, page 1, Aug. 27, 2006)

Perquisites Under New Rules

- Perquisites and personal benefits disclosures included in “All Other Compensation” column of Summary Compensation Table (SCT)
- Exception to rule that “all compensation must be disclosed”
 - If aggregate value of all perks and personal benefits for an individual is < \$10,000, then no disclosure of perks is required

Perquisites Under New Rules

- However, if aggregate value > \$10,000, then each perk and personal benefit must be identified in a footnote to the SCT
- And, for each perk or personal benefit valued at greater of (i) \$25,000 and (ii) 10% of total value of all perks, its value must also be disclosed in a footnote
 - Must also describe methodology of valuation or cost calculation for each of these perks

Perquisites Under New Rules

- Note that former rules permitted exclusion of perks if aggregate amount was the lesser of (i) \$50,000 and (ii) 10% of the total annual salary + bonus of NEO
- The identified perks must be described in a manner that identifies the particular nature of the benefit received
 - For example, benefits such as clothing, artwork and housekeeping services can't be characterized as "travel & entertainment"

Definition of Perquisites

- “Perquisites” intentionally not defined – requires application of a two-part test:
 - Is it integrally and directly related to performance of executive’s duties?
 - If not, then does it confer a direct or indirect benefit that has a personal aspect?
 - Unless benefit is generally available on a non-discriminatory basis to all employees
 - Whether it may be provided for a business reason or the company’s convenience is irrelevant

Definition of Perquisites

- “Integrally & directly related” to job performance narrowly construed – *e.g.*, may be
 - Office space at company business location
 - Reserved parking spot closer to facilities “but not otherwise preferential”
 - Additional secretarial services for company matters
 - Travel to and from business meetings
 - Travel and entertainment

Definition of Perquisites - Examples

- Club memberships not used exclusively for business entertainment
- Personal financial or tax advice
- Personal travel using vehicles owned or leased by the company
- Personal travel financed by the company
- Housing and other living expenses
- Personal secretary
- Relocation assistance
- Commuting expenses, whether or not provided for company's convenience or benefit
- Security provided at a personal residence or during personal travel
- Discounts on the company's products or services that are not generally available to employees on a non-discriminatory basis
- Investment management services

Perquisites and Personal Benefits

- Whether the company has determined that an expense is an “ordinary” or “necessary” business expense for tax or other purposes is irrelevant to inquiry
- Perks and personal benefits disclosures now also required for directors
- “Aggregate incremental cost” to company is proper measure to value perks
 - Don’t use IRS valuation guidelines

Directors Compensation

- New director compensation table very similar to the SCT for NEOs
- Directors' compensation is only disclosed for most recent fiscal year, not past 3 years
- No requirement to disclose in this table amounts paid to NEO who also serves as a director
 - Proper place to disclose is in SCT with a footnote indicating what amounts contained in SCT reflect compensation as a director

Director Compensation Table

Name	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Comp. (\$)	Change in Pension Value and Non-qualified Deferred Comp Earnings	All Other Comp. (\$)	Total (\$)
Dir. 1							
Dir. 2							
Dir. 3							

Director Compensation Table

- Disclosure rules for the directors' table are substantially the same as those for the SCT
 - Awards under director legacy or charitable awards programs under "All Other Compensation" column
 - Would also require disclosure of
 - Perquisites
 - Tax gross-ups and other tax reimbursements
 - Director termination or retirement payments
 - Consulting fees
 - Dollar value of premiums paid by the company for life insurance for the director's benefit

Director Compensation Table

- Narrative disclosure is required to describe material factors necessary to an understanding of the table – for example:
 - Breakdown of fees paid to director (retainers, meeting fees, committee service, committee chair service)
 - Standard/different compensation arrangements
- Footnote disclosure is required of aggregate number of stock awards and option awards outstanding at fiscal year end
- Grouping of directors on single line permitted if there are identical elements and amounts of compensation

Related Person Transactions

- Overview
 - Increase, from \$60,000 to \$120,000, in the minimum size of a reportable related person transaction
 - new emphasis on “principles based” disclosure
 - subject to a more limited number of exceptions
 - greater emphasis on materiality judgments
 - integration of existing disclosure requirements regarding (i) indebtedness, (ii) business relationships and (iii) in the case of newly public companies, transactions with promoters
 - new disclosure requirements concerning policies for reviewing and approving related person transactions
 - expanded disclosure concerning board determinations about director independence
 - “Plain English” rules apply

Related Person Transactions

- “*Related persons*” continues to include
 - directors
 - executive officers
 - nominees for election as a director
 - immediate family members of such person
- “Immediate family member” has been expanded to include
 - stepchildren and stepparents
 - any person sharing the household of a person otherwise considered a related person

Related Person Transactions

- A beneficial owner of 5% or more of any class of the company's voting securities and any immediate family member will generally be considered a "related person"
- Former related persons
 - A transaction that meets the \$120,000 threshold will need to be disclosed if the person who has the material interest was a related person at any time during the past fiscal year, even if at the end of the fiscal year or at the time the report or statement is to be filed the person was or is no longer a related person

Related Person Transactions

- Expanded Definition of “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
 - Not limited to transactions in which the company (or a subsidiary) is a “party”
 - “involvement in a transaction ... that ... encompasses situations where the company benefits from a transaction”
 - This broad definition is intended to capture the business relationships with companies with which a director is associated that previously were separately covered by Reg. S-K Item 404(b)

Related Person Transactions

- *\$120,000 Threshold for Disclosure*
 - Any transaction involving more than \$120,000 in which a company has in its past fiscal year participated (directly or indirectly), or currently proposes to participate, and in which a “related person” has a direct or indirect material interest, must be disclosed
 - If an amount in excess of \$120,000 is involved in a transaction, the transaction will be subject to the disclosure requirement, even if by reason of a periodic payment or similar provision a transfer of less than \$120,000 in value has occurred or is provided for in a single fiscal year

Related Person Transactions

- *Materiality*
 - The materiality of a director's interest is "to be determined on the basis of the significance of the information to investors in light of all the circumstances" taking into consideration "the relationship of the related persons to the transaction, and with each other, [and] the importance of the interest to the person having the interest...."

Related Person Transactions

- Expanded Description of Transaction
 - Former requirement was to include “brief description”
 - New rules require disclosure of
 - name and relationship of related person
 - related person’s interest in the transaction
 - approximate dollar value of transaction
 - approximate dollar value of related person’s interest
 - any other information regarding the transaction or the related person in the context of the transaction that is material to investors in light of the circumstances of the particular transaction

Related Person Transactions

- Policies and Procedures
 - Must disclose company's policies and procedures for reviewing and approving (or ratifying) related person transactions
 - types of transactions covered by the policies
 - standards to be applied to approval of transactions
 - persons responsible for applying the policies
 - whether the policies are in writing and, if not, how they are evidenced
 - Also must disclose if any related person transaction required to be disclosed in the past year was not subject to existing review and approval policies, or was subject to policies but the policies were not followed

Related Person Transactions

- Interplay of New Related Person Disclosure and “Non-Employee Director” Status Under Section 16b-3
 - Rule 16b-3 provides an exemption from “short-swing” profit recovery for any equity transaction between the company and its directors or officers where the transaction is approved by a committee of “non-employee directors”
 - Definition of “non-employee director” under Rule 16b-3 has been modified to be consistent with new related person transaction disclosure requirements
 - Definition bars from such status a director as to whom related person transaction disclosure was required in the most recent past fiscal year
 - Under new rules, disclosure may now be required with respect to some directors where it was not required before and disclosure may no longer be required with respect to a director where it used to be (for example, because the \$60,000 reporting threshold has been raised to \$120,000

Related Person Transactions

- Applicability to Foreign Private Issuers
 - Item 7.B of Form 20-F which requires disclosure of transactions or loans with affiliates, associates, key management personnel, etc. has not been amended
 - Under Instruction 2 to amended Item 404, “more detailed” related person disclosure will be required in a Form 20-F to the extent such information is otherwise made publicly available or required to be disclosed by the issuer’s home jurisdiction or a market on which its securities are listed or traded

Corporate Governance Disclosures

- Overview
 - New rules update and expand existing disclosure requirements concerning independence of directors and certain corporate governance practices
 - New Item 407 consolidates all governance-related disclosure requirements

Corporate Governance Disclosures

- Committee charters no longer need to be filed periodically with proxy statement as long as they are on the Company's website
- New rules more closely align SEC's director independence disclosure requirements with NYSE and Nasdaq disclosure requirements

Corporate Governance Disclosures

- Director Independence Disclosure
 - identify each independent director that served during the fiscal year (even those that have retired or are not standing for reelection) and each nominee who would qualify as an independent director using independence standards established by the board in compliance with applicable listing standards
 - identify each non-independent member of the audit, nominating and compensation committee or, if the company does not have such a committee, identify each director who would not be considered independent for purposes of service on such a committee
 - disclose any exemption to the applicable listing standards pertaining to director independence the company is relying on (e.g., controlled company, foreign private issuer) and explain the basis on which the company concluded that the exemption applies

Corporate Governance Disclosures

- Director Independence Disclosure
 - disclose whether any company-specific independence standard (e.g., categorical standards) are available on the company's web site
 - if not, disclose such standards as an appendix to proxy statement once every three years or, if amended in a material respect, the next proxy statement
 - disclose for each director or nominee determined to be independent any category or type of transaction, relationship or arrangement that is not disclosed as a related person transaction but that was considered by the board in making its independence determination.
 - disclosure must be sufficiently detailed so that the nature of the transaction, relationship or arrangement is readily apparent

Corporate Governance Disclosures

- Compensation Committee Disclosure
 - compensation committee operations and a narrative description of procedures for the consideration of executive and director compensation
 - whether the compensation committee has a charter (and if it does, it must make the charter available through its web site or as an appendix to its annual proxy statement)
 - the scope of the committee's authority
 - the extent to which the committee may delegate authority and to whom

Corporate Governance Disclosures

- Compensation Committee Disclosure (cont'd)
 - the identity of any consultant that played a role in determining or recommending the amount or form of executive or director compensation
 - whether the consultant was engaged by the compensation committee or another individual
 - the nature and scope of the assignment as well as the material elements of the instructions or directions that were provided to the consultant
- Focus of disclosure is on process as opposed to CD&A where focus is on substance or results of decisions

Suggestions for Complying with New Requirements

- Review company's policies for the review and approval of related person transactions and confirm they are consistent with listing standards and determine whether any changes are appropriate
- If no such written policy, consider adopting one
- Codes of conduct should be reviewed and revised as necessary so that provisions for review and approval of conflict of interest transactions on the part of directors and executive officers are consistent with the practices for related person transactions
- Implement procedures so that accounts payable and other departments can flag potential transactions for disclosure or independence consideration

Suggestions for Complying with New Requirements

- Determine whether the change to the definition of non-employee director under Rule 16b-3 and new disclosure standards under Item 404 affect the eligibility of any director to serve on the compensation committee
- Consider possible revisions to the compensation committee charter
- Clarify roles in compensation determinations as new disclosures will need to cover the roles of directors, executive officers and consultants in the process of considering and determining executive and director compensation
- Revisit and inventory the activities of any compensation consultant

Suggestions for Complying with New Requirements

- Make sure that all compensation of non-named executive officers is approved by the compensation committee
 - Compensation paid to executive officers who are not NEOs may be disclosable under Item 404(a) if not approved by the compensation committee
 - Stock exchange listing requirements generally require compensation committee approval of compensation paid to all executive officers
 - Companies should make sure that all elements of compensation paid to non-NEOs (or at least those elements exceeding \$120,000) have been identified and approved by the compensation committee

Suggestions for Complying with New Requirements

- Update director and officer questionnaires for rule changes
- Review any standards of director independence to ensure that they provide sufficient guidance as to the categories of relationships that the board has determined do not impair a director's independence, including any standards that are based on the SEC's related person transaction disclosure requirements
- Determine whether company wants to disclose any such standards on its website or periodically in its proxy statement

Suggestions for Complying with New Requirements

- Review all transactions, relationships or arrangements with directors that, although they need not be disclosed as related person transactions under the new requirements were or will be considered by the board when determining a director's independence
- Revise, if necessary, the company's timetable relating to the preparation of its Form 10-K and proxy statement to account for the additional work necessary to satisfy the new requirements

Disclosure Controls and Procedures

- Identify new information required (e.g. increase in pension value)
- Identify persons responsible (may include third parties such as actuaries)
- Establish time frame for gathering information
- Revise checklists/timelines/responsibility assignments in light of the foregoing
- Revise director and officer questionnaires
 - related party transactions
 - pledges of stock

Disclosure Controls and Procedures

- CD & A must also be covered by disclosure controls; that section is filed not furnished
 - CEO and CFO may look to new compensation committee report to support certification
- Start early

Revisions to Form 8-K

- Effective for events that occur on or after November 7, 2006
- Departures of additional persons covered
- Executive compensation arrangements removed from Item 1.01 and Item 1.02 (entry into, and termination of, material contract)
- Executive compensation arrangements now covered by Item 5.02

Expansion of Item 5.02 of Form 8-K

- Prior to amendments, Item 5.02 covered hiring and termination of CEO, President, CFO, CAO or COO (“covered officers”)
- As amended, Item 5.02 requires reporting of departure of any “named executive officer”, even if the person does not hold one of the above titles

Executive Compensation Arrangements Moved from Items 1.01 and 1.02 to Item 5.02

- Currently, a material contract triggering Form 8-K filing is tied to definition of material contract under S-K Item 601
- Because compensatory arrangements with “named executive officers” and directors are required to be filed under S-K Item 601 without regard to materiality, an avalanche of Form 8-K filings followed adoption of current rules
- S-K Item 601 definition retained under Items 1.01 and 1.02, but compensatory arrangements with executives and directors carved out and moved to Item 5.02
- New standard designed to capture only “unquestionably or presumptively” material events

Executive Compensation Arrangements Requiring Form 8-K Filing Under Item 5.02

- In connection with triggering events (Items 5.02(c) and (d)):
 - Any material plan, contract or arrangement to which a covered officer or director is a party or in which he or she participates that is entered into or materially amended in connection with one of the triggering events specified in Item 5.02(c) [hiring of new officers] or 5.02(d) [appointing new director], or any grant or award to any such person, or modification thereto, under such plan, contract or arrangement in connection with such event
 - Previously Item 5.02 only required a description of any “employment agreement” entered into in connection with appointment of specified officers

Executive Compensation Arrangements Requiring Form 8-K Filing Under Item 5.02

- Whether or not in connection with triggering event (Item 5.02(e)):
 - Any material compensatory plan, contract or arrangement in which the CEO, CFO or any named executive officer participates, is adopted, or is materially amended, or a material grant or award is made under the plan to such person; UNLESS the grant or award is materially consistent with the previously disclosed terms of such plans or arrangements and is disclosed in next proxy statement/annual report
 - Note that changes to director compensation arrangements not a triggering event unless in connection with appointment of new director
 - Should mean fewer Form 8-K filings for executive compensation arrangements

Executive Compensation Arrangements Requiring Form 8-K Filing Under Item 5.02

- Finally, if salary or bonus is omitted in most recent proxy statement/annual report because it was unavailable at time of filing, a Form 8-K is required when it becomes available
 - previously, reporting could be deferred until following year
 - not likely to occur very often

Other Form 8-K Matters

- For purposes of Item 5.02 only “named executive officer” means a person disclosed as such in most recent SEC filing that required summary compensation table
 - clarifies reporting obligations when executive departs in early January for example
- Only a brief description is required
- S-K Item 601 still applies as before for determining which executive compensation arrangements must be filed as exhibits to Forms 10-K/10-Q

Other Form 8-K Matters

- Safe harbor for failure to file Form 8-K extended to Item 5.02(e)
 - no loss of Form S-3 eligibility
- Item 1.01 caption need not be included if Form 8-K reports other events and information required by Item 1.01 is otherwise included. (e.g. date of agreement, names of parties)