

Implementing the SEC's New Proxy Disclosure Rules

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Webcast Briefing
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Overview

- On December 16, 2009, the SEC approved rules that will require enhanced proxy disclosure about corporate governance and compensation matters
- New Disclosures
 - ▶ Risks arising from compensation policies
 - ▶ The board's role in overseeing risk
 - ▶ Board leadership structure
 - ▶ Board diversity
 - ▶ Director qualifications
 - ▶ Fees paid to compensation consultants

Overview (cont'd)

- Revised Disclosures
 - ▶ Reporting of stock and option awards
 - ▶ Legal proceedings involving directors and executive officers
 - ▶ Timeline for reporting voting results

Effective Date of New Rules

- Compliance with New Proxy Disclosure Rules
 - ▶ Companies with fiscal year ends on or after December 20, 2009 must comply if filing a definitive proxy statement on or after February 28, 2010 (regardless of when the preliminary proxy statement is filed)
 - ▶ Companies with fiscal year ends on or after December 20, 2009 that file a definitive proxy statement prior to February 28, 2010 and companies with fiscal year ends before December 20, 2009 are not required to comply
 - ▶ Companies that are not required to comply may voluntarily early comply with the change in how equity awards are reported in the Summary Compensation Table and the Directors Compensation Table only if they also early comply with all of the other new requirements. Companies can voluntarily and selectively early comply with any of the other disclosure enhancements
- Compliance with New Rules for Reporting Voting Results
 - ▶ Companies with annual meetings taking place on or after February 28, 2010 must comply (regardless of when the proxy statement was mailed to shareholders), and companies with annual meetings taking place before February 28, 2010 do not have to comply

Risks Arising From Compensation Policies

- Rule requires narrative disclosure about compensation policies and practices for employees, including non-executive officers, if the policies and practices create risks that “are reasonably likely to have a material adverse effect” on the company
- Rule provides examples of situations that may trigger disclosure, including compensation policies and practices:
 - ▶ at a business unit that has a significant portion of the company’s risk profile;
 - ▶ at a business unit with compensation structured significantly differently than other units;
 - ▶ at a business unit that is significantly more profitable than other units;
 - ▶ at a business unit where compensation expense is a significant percentage of the unit’s revenues; and
 - ▶ that vary significantly from the overall risk and reward structure of the company

Risks Arising From Compensation Policies (cont'd)

- Focus on compensation arrangements that are likely to promote risk-taking behavior that could have a significant and damaging impact on the company's operations
- “Reasonably likely” materiality standard is same as MD&A standard for risk-oriented disclosures of known trends and uncertainties
- Company-level assessment of materiality
- Assessment can take into account mitigating or offsetting arrangements or controls designed to limit risks of compensation arrangements
 - ▶ Controls-oriented: internal or supervisory controls to monitor risk
 - ▶ Compensation-oriented: design features such as clawbacks, deferrals, more-than one year performance periods

Risks Arising From Compensation Policies (cont'd)

- Rule includes examples of the types of information to be disclosed if this disclosure is required
- SEC Release states that the materiality standard is expected to result in a smaller number of companies making risk disclosures
- Disclosure not required in the Compensation Discussion and Analysis (as proposed), but instead will be a separate compensation-related disclosure in the proxy statement
- Companies do not have to affirmatively state that they've determined that the risks arising from their compensation policies are not reasonably likely to have a material adverse effect

Board's Role in Overseeing Risk

- Rule requires disclosure of the extent of the board's role in the process of overseeing risk
 - ▶ Where risk oversight sits at the board level (for example, whether the whole board or a committee oversees risk)
 - ▶ How management provides the relevant information to the board
 - ▶ The effect, if any, of the risk oversight function on the board's leadership structure

Board Leadership Structure

- Rule requires disclosure of whether the company combines or separates the roles of Chairman of the Board and Chief Executive Officer
- If the roles are combined, disclosure is required of whether the company has a lead director and the specific role the lead director plays in the leadership of the board
- Companies also must disclose why the company's leadership structure is appropriate for it

Board Diversity

- Rule requires disclosure of whether, and if so how, a company's nominating/governance committee or board considers diversity in identifying director nominees
- If the nominating/governance committee or board has a “policy with regard to the consideration of diversity,” disclosure about how the policy is implemented and how the board or committee assesses the effectiveness of the policy is required
- The SEC did not define “diversity” so that companies are free to develop and disclose their own standards and address matters such as diverse business experience

Director Qualifications

- Rule requires, for each director and nominee, individualized disclosure of the experience, qualifications, attributes, or skills that led to the conclusion that the individual should serve as a director
 - ▶ Disclosure is required for all directors, including those not up for reelection in a particular year
- Rule also requires disclosure of all public company directorships held by directors and nominees during the past five years (as opposed to current directorships only)

Legal Proceedings

- Rule expands the disclosure of legal proceedings involving directors and executive officers to cover a 10-year period (rather than only a 5-year period)
- Rule also expands the types of legal proceedings to include:
 - ▶ Mail or wire fraud
 - ▶ Violations of federal or state securities, commodities, banking or insurance laws, or any settlement to these actions
 - ▶ Disciplinary sanctions
 - Mail or wire fraud or fraud in connection with any business entity
 - Violations of federal or state securities, commodities, banking or insurance laws, or any settlement to these actions
 - Disciplinary sanctions imposed by a stock, commodities or derivatives exchange or other self-regulatory organization

Planning Steps for Implementing the Rules

- Update D&O questionnaires
- Revise governance guidelines and board committee charters as needed
- Prepare management and board for new disclosures
- Schedule sufficient board and committee time for discussion of director qualifications and compensation policies and risk

Compensation Consultants

- Existing consultant standard remains: describe any role of compensation consultants in determining or recommending the amount or form of executive and director compensation and who engaged them
- No disclosure is required where consultant's only role is advising on broad-based plans or providing surveys that are not customized or are customized based only on parameters not developed by the consultant

Compensation Consultants (cont'd)

- If the board or compensation committee engaged its own consultant to provide advice or recommendations on executive or director compensation, and the consultant or its affiliates provide other services to the company in excess of \$120,000 during the fiscal year, then the company must disclose:
 - ▶ Aggregate fees for work on executive/director compensation and aggregate fees for the other services
 - ▶ Whether the decision to engage the consultant for the other services was made or recommended by management
 - ▶ Whether the board or compensation committee approved the other services
- If the board or compensation committee has not engaged its own consultant, but management has engaged a consultant to provide advice or recommendations on the amount or form of executive and director compensation, and the consultant or its affiliates provide additional services to the company in excess of \$120,000 during the fiscal year, the company must disclose aggregate fees for work on executive/director compensation and aggregate fees for work on the other services

Reporting of Stock and Option Awards

- Rule requires disclosure of aggregate grant date fair value of stock and option awards in the Summary Compensation Table and Director Compensation Table
 - ▶ Currently, companies disclose the amount recognized for financial reporting purposes
 - ▶ This may alter the composition of a company's named executive officers
- Grant-date value of performance-based equity awards is based on the probable outcome of such conditions at the date of grant
 - ▶ For many awards, this will mean payout at “target” performance
 - ▶ Footnote disclosure is required of the grant-date value assuming payout at “maximum” performance
- Assumptions still provided via footnote; grant-by-grant values still reported in Grants of Plan-Based Awards table

Reporting of Stock and Option Awards (cont'd)

- Transition Rules
 - ▶ Determine 2009 named executive officers based on new rules
 - ▶ If those persons were named executive officers for 2007 or 2008, recompute the equity award values for the year in which they were named executive officers
 - Companies can use the amounts reported in the Grants of Plan-Based Awards table, except that performance-based equity awards should be reported based on the probable outcome
 - ▶ Compensation for a person who is a named executive officer for 2009 and who was a named executive officer for 2007 but not for 2008 must be reported for all three fiscal years
 - ▶ Companies are not required to include different individuals for any preceding fiscal year based on this recomputation

Disclosure of Annual Meeting Vote Results

- Rule requires filing a Form 8-K within four business days of the annual meeting, disclosing the annual meeting's voting results
 - ▶ Currently, companies must report results on Form 10-Q
 - ▶ If final results are not known within four business days, companies can file preliminary results and an amended Form 8-K within four business days of the availability of final results
 - ▶ Companies will not be required to report voting results on Form 10-Q or Form 10-K

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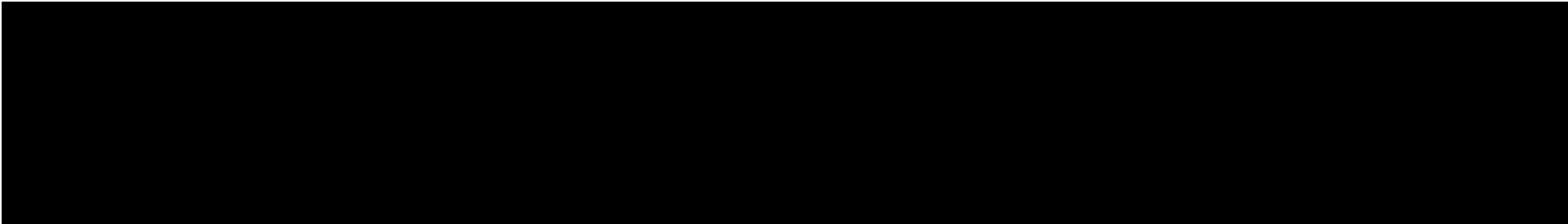
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