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SECURITIES LAW UPDATE January 26, 2010

SEC AMENDS PROXY RULES FOR 2010 PROXY SEASON

As you may know, the Securities and Exchange Commission (SEC) adopted a series of new proxy rules on December 16, 2009. The new rules are applicable to all registrants with fiscal years ending on or after December 20, 2009 and whose definitive proxy materials are filed on or after February 28, 2010. Accordingly, most registrants will be subject to all of the new proxy rules for the upcoming proxy season. Smaller reporting companies (SRCs) have not been exempted form the new rules, with one notable exemption mentioned below. Additionally, this is a good time to recall two other proxy-related developments in the last year, one affecting broker voting on election of directors and the other dealing with disclosure of the results of elections for directors.

Because this Memorandum is reviewed by many persons who are not attorneys, we have avoided statutory and SEC rule references and have tried to address the new requirements in plain English and incorporating practice tips for the implementation of the new rules during the upcoming proxy season. We are happy to discuss the rules in greater detail as required.

The principal areas where the new rules apply are summarized below:

I. Corporate Governance

A. The registrant must disclose whether there is or is not separation between the CEO and the Chairman of the Board. If there is no separation, then the registrant must disclose if there is a lead director and what functions the lead director performs. Additionally, all registrants must disclose why the leadership structure they have chosen is appropriate for their company. This requirement should be regarded as requiring a *justification* from those registrants who do not separate the CEO and Chairman positions. Note, however, that surveys indicate that the majority of registrants still do not separate these functions.

B. The risk management oversight function of the Board must be described. Note that the final rules do not require or even suggest that the Board should be engaged in risk management. Under the final rules, this is a disclosure of process of the oversight function (e.g. done by a committee or the Board as a whole), including how risk management information is provided by management

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to the Board. This strongly suggests that companies should review their corporate governance processes and institute appropriate procedures if they are not already in place. Additionally, NYSE-listed companies should be aware that having such process(es) is a requirement of the NYSE.

C. Increased information must be provided about all director nominees (and all directors on staggered boards whether or not they are standing for election this year). As a result of certain specific changes in time periods regarding legal proceedings, board positions and a few other items, it will be necessary to modify director and officer questionnaires to incorporate the new times frames. The enhanced information also includes new disclosure about specific experience, attributes and skills that qualify the director/nominee for the Board, as of their last re-nomination including in the case of long-serving directors. Specific disclosure tailored to each director is required, rather than boilerplate applicable to all directors/nominees. Because of the potentially sensitive nature of such disclosure, it is recommended that review drafts of new director biographies and related disclosures be provided early for director review and input.

D. Registrants must disclose if the Nominating Committee has a diversity policy for directors. If there is, the registrant must disclose how the policy is implemented and how effective the policy is. Additionally, with or without such a policy, the registrant should indicate if the Nominating Committee considers diversity in considering Board nominees. Note that the SEC has not defined “diversity policy” nor is there an affirmative requirement that registrants have a diversity policy. Registrants should review their Nominating Committee charters to make sure that the charter is not dispositive on the issue one way or the other. Absent a specific statement in a Nominating Committee charter that there is a diversity policy, it is assumed that practice will develop such that a large number of registrants will state that they do *not* have such a policy and will thereby not have to make the additional disclosures about the implementation and effectiveness of such policy.

E. As mentioned above, note that under new NYSE rules applicable to broker-dealers, elections of directors are no longer routine matters. Therefore, absent instructions from the beneficial owners of shares held in street name, directors will no longer be able to use their discretion to vote for election of directors. Because the NYSE rule is applicable to broker-dealers, the rule in effect applies to all registrants. Individual companies should assess the impact of this rule on the ability to reach quorum if the only item(s) on the annual meeting agenda are non-routine matters.

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F. Remember also that during 2009, the SEC changed the reporting of the results of elections for directors from a 10-Q or 10-K disclosure (typically the second quarter 10-Q for fiscal year companies) to an 8-K disclosure. Note also that the SEC counts the meeting date as the first day; therefore, the 8-K must be filed no later than three business days following the meeting date, not four business days following the meeting date. If the registrant only has preliminary voting results, the registrant may file the preliminary results and shall amend the 8-K when the final results of the tabulation are completed.

II. Compensation

A. If a registrant's compensation policy for all its employees (not just named executive officers (NEOs) or executive officers) is reasonably likely to have a material adverse effect on the company as whole, the registrant must discuss compensation policy as it relates to risk management. As a corollary, additional risk factors in the 10-K may be appropriate. Accordingly, registrants should be in a position to answer this question before their 10-Ks are filed. Note that the final rules adopted a higher threshold requiring disclosure than the proposing release and a large number of registrants will conclude that the threshold triggering disclosure has *not* been met. However, in order to properly reach that conclusion, an internal risk assessment must be done by the registrant, which should be properly documented. (It is this risk assessment that should be completed before the 10-K in case additional risk factors are required to be disclosed in addition to proxy disclosure.) The SEC has given no guidance on what, how or by whom the risk assessment should be conducted, although it gives some examples in the adopting release of examples of things that could increase risk. Best practices would suggest that it is the Audit Committee, with input from the Compensation Committee should conduct the assessment. The assessment must consider factors that increase risk and may also consider mitigating factors that reduce risk. Note that there is no disclosure required to say that a risk assessment has been done or what the results of the assessment are. In other words, if an assessment has been done and the conclusion is that the compensation policy is not reasonably likely to have a material adverse effect on the company as a whole, the registrant is permitted to remain silent and not state the negative result. **SRCs ARE EXEMPT FROM THIS NEW RULE.**

B. The Summary Compensation Table (SCT) has been revised with respect to valuation of awards. The SEC has reversed the 123R accounting that has been in place the last few years and returned to the previous approach of showing the full fair value of the award in the year it is granted. This will require significant revision to the SCT but there are also transition rules for previous

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years. On the one hand, values for all years (two years for SRCs and three years for other registrants) reported on in the SCT must be recalculated and restated in the 2010 proxy statement. On the other hand, registrants need not refile their proxy statements for prior years because of the changes nor determine *de novo* who would or would not have been an NEO under the new rules had they been in effect for the prior years. Note that, in many cases, the changes to SCT will likely result in seemingly large increases in compensation to NEOs. Registrants may use footnotes to explain these seeming anomalies, just as footnotes are currently used for general SCT disclosure enhancement.

C. Existing disclosure about the compensation consultant has been tweaked but the basic test remains unchanged. If the Compensation Committee has engaged its own consultant and the registrant also pays that consultant more than $120,000 for other services, the total amount of payments to the consultant and additional disclosure must be included. If the Compensation Committee has not engaged its own consultant and the registrant pays a compensation consultant more than $120,000 for all services, the amount of payments to the consultant and additional disclosure must be included. It is highly recommended that registrants and Compensation Committee are mindful of these thresholds and stay below them in order not to trigger the increased “conflicts of interest” disclosure that the rule addresses.

If you have questions regarding the new rules, recommended timing in order to prepare and file a proxy statement in a timely manner under the new rules, further practice tips or specific fact patterns, please contact:

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