# Management Alert

# SEC Proposes Revisions to Proxy Disclosure of Executive Compensation

On July 10, the United States Securities and Exchange Commission (SEC) released a proposal to make several revisions to the manner in which executive compensation is disclosed in a public company's annual proxy, and related matters. If adopted, the revisions would apply to the 2010 proxy season.

For the most part, the proposed revisions represent fine-tuning of the comprehensive revision of the compensation disclosure requirements adopted by the SEC in 2006. They also contain new disclosure requirements that reflect public perception surrounding the causes of the current financial crisis—particularly the perception that incentive policies focused on short-term results have encouraged excessive risk-taking. This alert outlines some of the principal revisions proposed by the SEC, which include:

## *Disclosure of Effect of Compensation Practices on Risk*

The SEC has proposed an addition to the Compensation Discussion & Analysis (CD&A) section of the proxy discussing the manner in which the company's overall compensation policies can create incentives for employees that affect the company's risks, and the procedures the company has in place to manage such risks. This section of the CD&A would not be limited to the five most highly compensated officers, but would require a discussion of the manner in which bonus and other compensation plans and policies may create incentives for *all employees* to cause the company to engage in risky behavior that could have a material effect on the company. The proposal contains a number of specific issues that may need to be addressed in this section, including the extent to which the company has implemented policies to offset the tendency of incentive plans to reward short-term risk taking behavior, such as clawbacks and mandatory bonus deferrals.

## *Additional Disclosure About Directors and Nominees*

The proposal would require that a proxy discuss the qualifications of directors and nominees for positions on the board of directors, with specific reference to the relevance of the director's or nominee's qualifications to the business of the company. The proposal would also require disclosure of all other board memberships held by each director or nominee during the prior five years (right now, only current memberships need be disclosed), and would expand the requirement to disclose legal proceedings in which directors and nominees (and executive officers) have been involved from the prior five years to 10 years.

## *Discussion of Leadership Structure*

The proposal would require a discussion of the company's leadership structure and the philosophy behind the structure. Most notably, this would require companies to explain why the company has chosen to combine (or separate) the roles of chairman and CEO. The proxy would also be required to describe the role of the board of directors in the company's risk management.

## Disclosure of Services Performed by Compensation Consultants

The proposal would require the company to disclose whether any other services have been performed for the company by compensation consultants and, if so, the amount of fees paid for such services.  Although the SEC proposal would only require disclosure, Treasury Secretary Geithner has suggested that the administration may introduce legislation that would actually prohibit compensation consultants from performing other services for the company, reflecting a perception that compensation consultants who receive other business from the company have a conflict of interest that may cause them to recommend excessive compensation for senior management.

## Reporting of Stock and Option Grant Value

Reversing a last-minute decision made when the current compensation disclosure rules were finalized in 2006, the new proposal would require that the total fair value of stock and option awards as of the grant date be included in the Summary Compensation Table.  At present the Summary Compensation Table includes the amount of compensation expense that the company must recognize each year under generally accepted accounting principles.  The SEC explained that the total fair value as of the grant date is a more meaningful figure in evaluating an executive's total compensation.  In addition, the current market crisis has caused the amount of income recognized on an annual basis to be negative in years following the year of the original grant, which the SEC believes unrealistically reduces an executive's total reported compensation.  To avoid duplication, the total fair value of grants will be deleted from the Grants of Plan-Based Awards table.

## Accelerated Reporting of Shareholder Votes

Under the proposal, the result of shareholder votes would be reported on a Form 8-K, which generally must be filed within four business days of the shareholders meeting.  Currently, the results of shareholder votes do not need to be reported until the company's next quarterly (10-Q) or annual (10-K) report.

## Changes in Proxy Solicitation Rules

The SEC has also proposed changes to the rules governing the proxy solicitation process, specifically the circumstances in which a person communicating with shareholders must comply with the disclosure requirements applicable to a proxy solicitation.  These changes would generally facilitate actions by minority shareholders and shareholder activists, including "just say no" campaigns in which a shareholder urges other shareholders to withhold votes in favor of management proposals.  The new rules would also codify recent SEC guidance by facilitating "short slate" proxy solicitations, in which the person soliciting the proxy does so in order to vote for one or two specific candidates for the board, but also receives the discretion to vote for other board candidates (whether company nominees or other shareholder nominees) not listed in that person's solicitation.

*For more information about the SEC proposal, please register for our upcoming webinar "Reassessing and Disclosing Executive Pay in the New Regulatory Environment" on July 30, or contact any Employee Benefits & Executive Compensation attorney on our website (www.seyfarth.com/EmployeeBenefits).*

SEYFARTH SHAW LLP
ATTORNEYS

Breadth. Depth. **Results.**

www.seyfarth.com