

# Akerman Practice Update

CORPORATE

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## SEC Proposes Amended Proxy Disclosure and Solicitation Rules

On July 10, 2009, the Securities and Exchange Commission (“Commission”) published its proposed amendments to the proxy disclosure rules in the areas of executive compensation and corporate governance and to the proxy solicitation rules. The principal aspects of the rule proposal are summarized below. If adopted, the proposed amendments will be effective for the 2010 proxy season. To see the Commission’s proposal, click [\[here\]](#).

### Disclosure in CD&A of compensation policies and practices that affect risk and the management of risk

The proposal would require a company to include in its Compensation Discussion and Analysis (“CD&A”) a new section providing information about how overall compensation policies for employees create incentives that can affect the company’s risk and the management of that risk. The Commission in its proposing release, stated its belief that a principles-based discussion on broader

compensation policies is necessary in situations where the policies may create risk to the company that may not be apparent from a discussion solely focused on executive compensation policies. This new disclosure is in addition to the current requirement that CD&A address the level of risk that a company’s named executive officers may be encouraged to take to receive incentive bonus compensation from the company.

The rule proposal provides examples of compensation policies and practices that might require disclosure if material:

- at a business unit of the company that carries a significant portion of the company’s risk profile;
- at a business unit with compensation structured significantly differently from the other units within the company;
- a business unit that is significantly more profitable than others within the company;

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- at business units where the compensation expense is a significant percentage of the unit's revenue; and
- that vary significantly from the overall risk and reward structure of the company, such as where bonuses are awarded upon accomplishment of a task, while the income and risk to the company from the task extends over a significantly longer period of time.
- the issuer's policies regarding adjustments in compensation policies to address changes in risk profile;
- material adjustments the issuer has made to its compensation policies or practices to address changes in risk profile; and
- the extent to which the issuer monitors its compensation policies to determine whether its risk management objectives are being met with respect to incentivizing employees.

The Commission states that this is a non-exclusive list of compensation practices that may have a potential to raise material risks to the company. The Commission then lays out several illustrative examples of the types of issues that company's may need to address regarding their compensation policies and practices that may give rise to risk that may have a material effect on the company:

- the general design philosophy of compensation policies for employees whose behavior would be most affected by the incentives established by the policies as they relate to or affect risk taking;
- the issuer's risk assessment in structuring compensation policies and in awarding and paying compensation;
- how compensation policies relate to the realization of risks resulting from employee actions in the short-term and in the long-term, such as through claw backs and holding periods;

The proposal reflects the Commission's view that application of this required disclosure will need to be tailored to the facts and circumstances of the company.

The release seeks comments on a number of issues, including whether the discussion should be mandatory only for certain sizes of companies or certain industries and whether discussions of all of the examples of issues should be required.

### Revisions to the Summary Compensation Table

The proposal would modify the reporting of stock and option awards in the Summary Compensation Table and the Director Compensation Table. Specifically, disclosure of the grant date fair value of such awards, as opposed to the current disclosure based on the expense recorded in the financial statements in accordance with FAS 123R, would be required. The Commission stated its belief in the release that the inclusion of grant date fair values will provide more meaningful disclosure

of total compensation awarded to executives, and noted that some companies already include an alternative table in their CD&A discussions to illuminate their compensation decision-making processes.

Since the Commission adopted its current framework of executive compensation disclosure in 2006, the current rules regarding the reporting of the value of stock and option awards has been criticized by investors, practitioners and commentators as being potentially misleading and confusing to investors. This proposal seeks to remedy this deficiency. Further, the changes as proposed would not change the current structure under which disclosure of specific compensation is required for the principal executive officer, the principal financial officer, and the three most highly compensated executive officers.

The proposed change in methodology, however, could significantly alter the total compensation reported for executive officers and therefore affect which executive officers are included in the Summary Compensation Table. The Commission is considering whether to require companies reporting compensation data following effectiveness of the rule amendments to present recomputed disclosure in the Summary Compensation Table for prior fiscal years in order to preserve year over year comparability. However, the Commission indicated that it would not require companies to include different named executive officers for any fiscal year prior to the most recent year being reported based on a recomputation of total compensation for prior fiscal years.

## Compensation Consultants

The proposal would require companies to include additional disclosures regarding compensation consultants. If a compensation consultant or its affiliates played a role in determining the amount or form of compensation for a company's executives or directors and provided other services to the company, then the company would be required to disclose the nature of the other services provided, the aggregate fees received by the consultant and its affiliates for these additional services, whether the decision to engage the compensation consultant for any other services was recommended or made by management, and whether the company's compensation committee or board approved the consultant's provision of such other services. These disclosure requirements would not apply where the compensation consultant's only role in determining the amount or form of compensation related to broad-based, nondiscriminatory plans such as 401(k) or health insurance plans.

## Director Qualifications and Experience

The proposal would require enhanced disclosure regarding the qualifications and experience of directors and director nominees, mandating a discussion of the specific experiences and skills relevant to service as a director and, where applicable, as a committee member, with respect to a particular company. In addition, the Commission would require a five year look-back period for disclosure

of other public company directorships held (currently, disclosure is required only of presently held directorships) and would increase the look-back period for legal proceedings from five to 10 years. The revisions are intended to provide investors with more information regarding whether a particular director and the entire board composition is an appropriate choice for the particular company.

The Commission noted, among other things, that the capacity to assess risk and respond to complex financial and operational challenges can be important attributes for directors of a public company.

## Board Leadership Structure

The proposal would require disclosure of the company's board of directors leadership structure, including disclosure discussing why that structure is best for the particular company. The required disclosure would include whether and why the principal executive officer and board chair positions are combined, and, if they are combined, whether the company has a lead independent director and a description of the role of the lead independent director. The proposal would also require discussion of the board of directors' role in the company's risk management process (for example, whether it is managed through the board as a whole or through a committee, such as the audit committee) and the relationship between the board and senior management in managing material risks facing the company. The Commission solicited comment in the release on whether

additional disclosures regarding board structure should be required, such as how a company determines the size of its board and the number of independent directors on its board.

## Current Reporting of Voting Results

The proposal would require current reporting on Form 8-K of the results of any vote taken at a shareholder meeting. Currently, voting results may be reported in the company's next report on Form 10-K or 10-Q. The Commission believes that because matters voted upon at shareholder meetings often involve issues that directly impact shareholder interests, such as board composition, executive compensation issues or changes in shareholder rights, that current reporting is appropriate. The proposed change to Form 8-K includes an instruction that if the matter voted on at the meeting relates to a contested election of directors and the voting results are not definitively determined at the end of the meeting, the company should report the preliminary voting results within four business days after they are determined and file an amended report within four business days after the final voting results are certified.

## Clarifications to the Proxy Solicitation Rules

The proposed amendments also seek to clean up a number of ambiguities in the proxy solicitation rules. The proposed rules, among other things:

- permit a person soliciting support for a "short slate" of director nominees to round out its short slate by seeking

authority to vote for nominees named in any other person's proxy statement, rather than only nominees named the company's proxy statement as permitted under current Rule 14a-4(d), subject to the satisfaction of certain conditions;

- clarify that a person who provides a shareholder with an unmarked copy of a management proxy card and requests the shareholder to return the proxy card directly to management is not providing a "form of revocation," which would prevent the person providing such proxy card from taking advantage of the exemption from the proxy rules under Rule 14a-2(b) for solicitations by non-management parties who are not seeking proxy authority and do not have a substantial interest in the subject matter of the solicitation;
- clarify that the requirement under Rule 14a-2(b)(1) that a soliciting person not have a substantial interest in the subject matter of the solicitation is applicable even if the soliciting person is not a holder of securities of the class being solicited; and
- clarify that a condition specified by a soliciting person as to the conditions under which it may or may not be permitted to vote shares for which it has obtained proxy authority must be objectively determinable.

### What to Expect

The Commission has requested comments on a number of issues in connection with the proposed rules. Comments must be submitted by September 15, 2009. It is widely expected that proposed rule amendments regarding the matters dealt with in this proposal are likely to be approved effective for the 2010 proxy season.

As a result of the proposal, company management and boards of directors may

wish to begin the process of gathering the information that will be required to comply with the expanded disclosure requirements. Further, if they have not done so already, boards of directors would be wise to consider the issues raised in the proposal in their consideration of compensation matters, particularly with respect to risk and the management of risk. Further, nominating committees should be thinking about the issues raised in this proposal in considering the selection or retention of board members.

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The summary set forth herein is intended to be general in nature and does not constitute legal advice with respect to any particular situation. No legal or business decision should be based solely on its contents. If you would like further information or help in assessing how the proposed rules might affect your company, please contact your principal lawyer at the firm or one of the Akerman shareholders listed below:

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