

Client Alert

A report
for clients
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of the firm January 2006

SEC Votes To Propose Changes to Disclosure Rules for Executive Compensation and Related Matters

On January 17, 2006, the SEC voted to publish for comment proposed amendments to disclosure requirements for executive compensation, related party transactions, director compensation and independence, other corporate governance matters, and security ownership of officers and directors. The proposals would address disclosure in proxy statements, annual reports and registration statements. In addition, the proposals would require that the proposed disclosure be provided in plain English. The proposals would also modify current Form 8-K reporting requirements regarding compensation arrangements.

New Compensation Discussion and Analysis Section

Under the proposals, a new section for compensation discussion and analysis would replace the currently required compensation committee report. Unlike the current compensation committee report, the proposed new compensation discussion and analysis section would constitute company disclosure and would be considered to be filed under the Exchange Act. The new section would require disclosure regarding the company's objectives and implementation of its executive compensation programs, including elements of compensation and the reasons for choosing them.

Other Executive Compensation

The proposals would modify currently required tabular disclosure as well as require additional

narrative disclosure of compensation of the principal executive officer, principal financial officer, and the three other highest paid executive officers and the directors. The proposals would amend executive compensation disclosure according to three broad categories: compensation over the last three years; holdings of outstanding equity-related interests received as compensation that are the source of future gains; and retirement plans and other post-employment payments and benefits.

Reorganized Summary Compensation Table

The Summary Compensation Table would require compensation disclosure for the past three years and would be reorganized to require additional information, including the following:

- a new column reporting total compensation;
- a dollar value for all stock-based awards, including stock and stock options, measured at grant date fair value, computed pursuant to Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 123;
- the "All Other Compensation" column would include the aggregate increase in actuarial value of pension plans accrued during the year and all earnings on deferred compensation that is not tax-qualified; and
- the threshold for disclosing perquisites would be reduced to \$10,000 and interpretive guidance would be provided for determining what is a perquisite.

Two supplemental tables would report Grants of Performance-Based Awards and Grants of All Other Equity Awards.

Disclosure of Outstanding Equity Interests

Disclosure regarding outstanding equity interests would include:

- the Outstanding Equity Awards at Fiscal Year-End Table, which would show outstanding awards representing potential amounts that may be received in the future; and
- the Option Exercises and Stock Vested Table, which would show amounts realized on equity compensation during the last year.

Disclosure of Retirement Plans

Retirement plan and post-employment disclosure would include:

- the Retirement Plan Potential Annual Payments and Benefits Table, which would disclose annual benefits payable to each named executive officer;
- the Nonqualified Defined Contribution and Other Deferred Compensation Plans Table, which would disclose year-end balance, and executive contributions, company contributions, earnings and withdrawals for the year; and
- disclosure of payments and benefits (including perquisites) payable on termination or change in control, including quantification of these potential payments and benefits.

Director Compensation

A new Director Compensation Table, similar to the Summary Compensation Table, and related narrative would require disclosure of director compensation for the last year.

Related Party Transactions, Director Independence and Other Corporate Governance Matters

Principal changes to the disclosure provisions regarding related party transactions would include requiring disclosure regarding policies and procedures for approving related party transactions, an expansion of the categories of related persons and a change in the threshold for disclosure from \$60,000 to \$120,000. The proposals would be more principles-based, and would require disclosure if the company is a participant in a transaction in which a related person has a direct or indirect material interest.

Proposed new Item 407 of Regulations S-K and S-B would require:

- disclosure of whether each director and director nominee is independent;
- a description of any relationships not otherwise disclosed that were considered when determining whether each director and director nominee is independent; and
- disclosure of any audit, nominating and compensation committee members who are not independent.

New Item 407 would also consolidate corporate governance-related disclosure requirements currently set forth in a number of places in the proxy rules and Regulations S-K or S-B. This would include disclosure regarding board meetings and committees, including nominating and audit committees. New Item 407 would also require similar disclosure regarding compensation committees and a narrative description of their procedures for determining executive and director compensation.

Security Ownership of Officers and Directors

The proposals would require disclosure of the number of shares pledged by management.

Form 8-K

The proposals would amend Form 8-K to require disclosure of employment arrangements and material amendments thereto, for named executive officers. In addition, the proposals would consolidate all Form 8-K disclosure regarding employment arrangements under a single item.

Plain English

The proposals would require companies to prepare most of the information described above using plain English principles.

A more detailed summary of the SEC's actions can be found on the SEC's website at <http://www.sec.gov/news/press/2006-10.htm>.

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