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About Allen Matkins

Allen Matkins Leck Gamble Mallory & Natsis LLP is a California law firm with more than 230 attorneys practicing out of seven offices in Los Angeles, Century City, Orange County, Del Mar Heights, San Diego, San Francisco and Walnut Creek. The firm's broad based areas of focus include corporate, real estate, construction, real estate finance, business litigation, employment and labor law, taxation, land use, bankruptcy and creditors' rights, intellectual property and environmental. more...

Six Questions Every Public Company Should Ask Now to Prepare for its 2010 Proxy Statement and Form 10-K

The Securities and Exchange Commission (SEC) recently adopted amendments to its disclosure rules. As a result of these amendments, companies will be required to make new or revised disclosures about:

- compensation policies and practices;
- stock and option awards to executives and directors;
- potential conflicts of interests involving compensation consultants;
- director and board of director nominee qualifications and legal proceedings;
- board of director leadership structure; and
- the board of directors' role in risk oversight.

To help prepare for these new disclosures, we think companies should ask the following six questions:

1. Do my company's compensation policies and practices involve risks that are reasonably likely to have a material adverse effect on the company?
   The recent economic collapse has caused the SEC to focus increasingly on risk and risk management. Last fall, the SEC even created a new Division of Risk, Strategy, and Financial Innovation. The SEC rule amendments require a company to discuss its policies and practices for compensating employees (not simply officers) as they relate to risk management practices and risk-taking incentives. This disclosure is required to the extent that risks arising from the company's compensation policies and practices are "reasonably likely" to have a material adverse effect on the company. This disclosure is not part of a company's Compensation Discussion and Analysis (CD&A). In adopting this change, the SEC has provided a non-exclusive list of compensation policies and practices that could trigger a discussion. These are compensation policies and practices:
   - 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 than other units within the company;
   - At a business unit that is significantly more profitable than others within the company;
   - At a business unit where the 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, such as when bonuses are awarded upon accomplishment of a task, while the income and risk to the company from the task extend over a

significantly longer period of time.

Smaller reporting companies (as defined by the SEC) are not required to provide this new disclosure.

2. How independent are my company's compensation consultants?
   Many companies engage consultants to make recommendations on the appropriate compensation levels for directors and officers, to design incentive plans, and to provide information concerning industry and peer group compensation practices. Sometimes, these consultants provide other services to the company. In the SEC's view, fees from these other services could create a conflict of interest for these consultants. To address this concern, the SEC now requires disclosure of compensation consultant fees in specified circumstances. In general, disclosure will be required when a consultant's fees for non-executive compensation consulting services exceed $120,000 during the company's fiscal year.

3. What led my company's board of directors to conclude that each director and each director nominee should serve as a director?
   Companies must disclose for each director and any nominee for director the particular experience, qualifications, attributes and skills that led the board of directors to conclude that a person should serve as a member of the board of directors. This new disclosure is required with respect to all directors, including those who are not standing for reelection in a particular year. The SEC is not, however, requiring that a company disclose the specific experience, qualifications or skills that qualify a person to serve as a committee member. However, this disclosure is required if an individual is chosen as a director or nominee because of a specific qualification, attribute or experience relating to service on a specific committee.

4. Does my company’s board (or nominating committee) consider diversity in identifying nominees for directors?
   Many companies have adopted a diversity policy with respect to board candidates. Companies are now required to disclose whether, and if so how, a nominating committee considers diversity in identifying nominees for election to the board of directors. If a company has a policy with respect to consideration of diversity in identifying director nominees, the company is required to disclose how the policy is implemented and the nominating committee's (or board's) assessment of the effectiveness of that policy. The SEC's rule does not define "diversity" – allowing each company to define the term in a manner that it considers appropriate. Moreover, the SEC rule does not require companies to adopt a diversity policy.

5. Does my company separate the chairman of the board and chief executive officer functions?

In the last few years, many companies have received stockholder proposals advocating the separation of the positions of chairman of the board and chief executive officers. The SEC is now requiring that a company disclose whether and why it has chosen to combine or separate these two positions. If a company has combined these positions, the company is required to disclose whether it has a lead independent director and, if so, the role of the lead independent director. In making the required disclosure, a company must state why it believes that its leadership structure is appropriate in light of its specific characteristics or circumstances.

6. What is the board's role in oversight of company risk?

   In response to the recent economic turmoil, regulators and many investors have focused on issues of risk management. In adopting the recent rule amendments, the SEC stated that it is persuaded that "risk oversight is a key competence of the board". Consequently, the SEC now requires companies to disclose the extent of the board's role in the risk oversight of the company, such as how the board administers its oversight function.

Additional Rule Changes

The SEC's rule amendments also make changes to the disclosures in the Summary Compensation Table and Director Compensation Table. Previously, the SEC had required that companies disclose the amount recognized for financial reporting purposes for stock and option awards. Now, companies are required to disclose the aggregate grant date fair value of these awards (computed in accordance with FASB ASC Topic 718). The SEC has also adopted special instructions for awards subject to performance conditions. To facilitate year-to-year comparisons, companies are required to recomputed disclosure for each of the preceding fiscal years required to be in the table.

Until now, companies were required to report voting results in its Form 10-Q or Form 10-K with respect to any matter submitted to the vote of shareholders. The SEC's new rules require companies to disclose on Form 8-K the results of a shareholder vote. This information must be filed within four business days after the end of the meeting at which the vote was held.

The SEC has also increased certain director and officer disclosure requirements. For example, it has lengthened the time period during which disclosure of legal proceedings involving directors, director nominees, and executive officers is required from five to ten years. The SEC is also requiring disclosure of additional legal proceedings involving these persons.

Effective Date

If a company's fiscal year ends on or after December 20, 2009, its Form 10-K and proxy statement must be in compliance with the new proxy disclosure requirements if filed on or after February 28, 2010. If such an issuer is required to file a preliminary proxy statement and expects to file its definitive proxy statement on or after February 28, 2010, then the preliminary proxy statement must

be in compliance with the new proxy disclosure requirements, even if filed before February 28, 2010. If such an issuer files its 2009 Form 10-K before February 28, 2010 and its proxy statement on or after February 28, 2010, the proxy statement must be in compliance with the new proxy disclosure requirements. If the issuer's fiscal year ends before December 20, 2009, its 2009 Form 10-K and related proxy statement are not required to be in compliance with the new proxy disclosure requirements, even if filed on or after February 28, 2010.

The foregoing is a summary only of some of the SEC's rule amendments. It is not intended and should not be construed as legal advice. You can obtain a copy of the Release from the SEC's website here. If you are interested in learning more, please contact us.

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