Corporate & Securities

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Corporate & Securities Advisory

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# Preparation for 2012 Fiscal Year-End SEC Filings and 2013 Annual Shareholder Meetings

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As our clients and friends know, each year Mintz Levin provides an analysis of the regulatory developments that impact public companies as they prepare for their fiscal year-end filings with the Securities and Exchange Commission (SEC) and their annual shareholder meetings. This memorandum discusses key considerations to keep in mind as you embark upon the year-end reporting process in 2013.[1]

***Year 3 of Say-on-Pay: Smaller Reporting Companies Must Now Comply.*** 2013 marks the third year of "say-on-pay" for companies other than smaller reporting companies,[2] as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and related SEC rulemaking. The non-binding shareholder vote on say-on-pay asks shareholders to approve companies' executive compensation arrangements as disclosed in the proxy statement pursuant to Item 402 of Regulation S-K. A separate vote, referred to as the "say-on-frequency" vote, requires companies to ask shareholders once every six years how often they want to conduct future say-on-pay votes: once a year, once every two years, or once every three years.

Smaller reporting companies must propose both the say-on-pay and the say-on-frequency votes for the first time this year, in connection with annual or other meetings of shareholders at which directors are to be elected that take place after January 21, 2013. Although these companies are still not required to include a Compensation Discussion and Analysis (CD&A) section in their proxy statements, we expect that many of these companies will provide an advocacy section in their proxy statements, explaining the rationale behind their compensation practices, similar to the executive summaries we have been seeing over the last year in larger companies' filings. With respect to the say-on-frequency vote for smaller reporting companies, as with larger companies, we expect that shareholders will vote for yearly say-on-pay even if the company recommends a vote once every two or three years. ISS will vote against directors next year if a company implements a say-on-frequency vote that is less frequent than the vote that receives a majority of the votes cast at the meeting.

For further detail on the final say-on-pay rules, please review our client alert available at http://www.mintz.com/newsletter/2011/Advisories/0917-0210-NAT-SEC/web.htm.

Overall voting results on say-on-pay were not meaningfully different in 2012 as compared to 2011, with shareholder support averaging around 90% across all companies. The overwhelming majority of companies with a failed say-on-pay vote in 2012 received significant investor support for their say-on-pay proposal in 2011. Based on this trend, say-on-pay is now perceived as a year-to-year item, in which success in past years is no guarantee of success in the current or future years, and companies should not become complacent about achieving the necessary support, even if they have enjoyed strong support in prior years. The advent of say-on-pay has caused companies to write their compensation-related disclosure in their proxy statements, in particular the CD&A section, with both advocacy and disclosure in mind. With smaller reporting companies added into the mix this year, there will be a significant increase in the number of say-on-pay proposals to be reviewed by ISS and other proxy advisory firms, so the more clearly the company's say-on-pay message is communicated, the easier it may be for shareholders to review and take action on the required votes.

Last year we saw a trend of companies including an executive summary at the beginning of the proxy statement in an effort to highlight key messages, clearly define the company's views on pay for performance, and ensure the company has a reasonable narrative to support its decisions for last year's pay. This year, a trend of disclosing "realizable pay" is developing. Many companies believe that the summary compensation table overstates executive pay due to the values ascribed to stock options and unvested equity awards[3] which leads to a distorted view of pay for performance alignment. Therefore, companies are adding a supplemental "realizable pay" table to assist shareholders in understanding the executive compensation value actually transferred during a fiscal year which shows the value of equity that may be realized based on actual stock performance as of a specified date. In addition beginning with annual meetings on or after February 1, 2013, ISS will look at realizable pay at S&P 500 companies when the firm's quantitative analysis results in a "high or medium" concern that a company's compensation policies are not linked to overall corporate performance and will also look at realized and/or realizable pay at other companies to assist it in determining whether the company demonstrates a strong commitment to a pay-for-performance philosophy.[4]

As it did last year, ISS will continue to review say-on-pay proposals by making a quantitative assessment of the CEO's pay and performance relative to the company's peers over one and three years and of the absolute alignment between the trend in CEO pay and a company's total shareholder return (TSR) over the prior five fiscal years. However, after receiving much criticism, ISS has revised its approach as to how it chooses a company's peer group and will now take into account a company's self-selected peer group to guide industry selections and will to some extent relax its requirements relating to size of peer group companies considered in order to prioritize peers more closely related in terms of industry as chosen by a company. These quantitative measures are intended to identify outlier companies that have demonstrated significant misalignment between CEO pay and company performance over time. In cases where alignment appears to be weak, further in-depth analysis will determine causal or mitigating factors, such as the mix of performance- and non-performance-based pay, grant practices, the impact of a newly hired CEO, and the rigor of performance programs.[5]

Although ISS originally proposed adding hedging and pledging as additional problematic pay practices under its qualitative pay-for-performance analysis, it instead moved its policy regarding these practices to its board of director approval policy for 2013. A company that allows its executive officers or directors to hedge company stock or pledge a significant portion of company stock may receive an "against" or "withhold" vote for directors individually, committee members, or the entire board. ISS has not established a bright-line test for what constitutes "significant" pledging, but it has indicated that a determination of whether pledging is significant is going to be based primarily on the number of shares pledged as a percentage of the number of shares outstanding, market value, and trading volume in the company's stock as well as the company's current views on future pledging arrangements. ISS views both hedging and pledging as adverse to shareholder interests because these practices sever the alignment of directors and executive officers' interests with shareholders by reducing the director or officer's economic exposure to holding company stock while maintaining voting rights. ISS believes that pledging, which often occurs in connection with a margin loan, can have a detrimental effect on a company's stock price in the event of forced sales to meet a margin call and such forced sales could also violate a company's insider trading policies. Companies should review their policies on hedging and pledging company stock and consider disclosing such policies in their proxy statements this year.

In assessing executive compensation, boards of directors should bear in mind that their ultimate goal is not to secure a successful say-on-pay vote, but rather to attract, retain, and incentivize executives who will contribute to the long-term value of the company. Directors should be aware of the executive compensation guidelines that ISS and similar groups promote, but should not allow this to override their own judgments as to the compensation programs and policies that are best for their companies. Directors should participate with management in soliciting favorable say-on-pay votes from major shareholders in order to overcome a negative recommendation by ISS.[6]

In addition, although say-on-pay has resulted in increased shareholder litigation based on compensation decisions, in which the board, compensation committee members, and executives are all named as defendants, the legal ramifications are limited. The Dodd-Frank Act expressly states that the shareholder vote "may not be construed" to "create or imply any change to the fiduciary duties of a company or its board of directors" or to "create or imply any additional fiduciary duties." This status quo was affirmed in January 2012, when a federal court dismissed a suit against bank directors arising out of a negative say-on-pay vote, finding that the Dodd-Frank Act did not alter directors' duties and that a negative vote does not suffice to rebut the business judgment protection for directors' compensation decisions. Similarly, in October 2012, a federal court and a state court separately refused to enjoin shareholder say-on-pay votes despite allegations of inadequate executive compensation disclosure. Although sufficiently bad facts could result in a contrary outcome, directors of companies incorporated in Delaware should generally take comfort that, if they act in good faith and with appropriate care, their compensation determinations will not be second-guessed or the subject of significant enhanced liability.

However, class action law suits alleging that boards of directors breached their fiduciary duties by approving purportedly deficient proxy statement disclosure and claiming that shareholders need more information in order to cast an informed vote seem to be on the rise and more successful than director duty claims. Over 20 of these actions have been filed. Plaintiffs are typically bringing these cases in state court and seek an injunction against the upcoming annual meeting until sufficient disclosure is provided in the proxy statement in order for shareholders to make an informed decision. The threat of an enjoined annual meeting has pushed several companies into providing additional disclosures, thereby justifying a fee award to plaintiff's counsel. Although plaintiffs have had only mixed results with these lawsuits, there have been enough successes to believe that this trend will continue in 2013. Companies with a low or negative say-on-pay vote and companies seeking authorization for new or additional shares to be issued pursuant to equity incentive plans should take a careful look at their disclosure to ensure that it complies with proxy statement disclosure requirements as well as consider enhanced disclosures to reduce the possibility of litigation. Many companies have boilerplate compensation policy language that is vulnerable to being exploited by plaintiffs and which is not necessary to provide an accurate and reasonable basis for a company's compensation decisions.

***SEC Rules on Compensation Consultant Conflicts of Interest.*** For proxy and information statements for annual meetings of shareholders (or special meetings in lieu of annual meetings) at which directors will be elected occurring on or after January 1, 2013, public companies are required to comply with new Item 407(e)(3)(iv) [7] of Regulation S-K, which requires companies to provide proxy disclosure about any conflicts of interest raised by the work of compensation consultants involved in "determining or recommending" executive or director compensation. [8] The SEC disclosure requirement extends to compensation consultants retained by the compensation committee or management, and to consultants advising on director compensation as well as executive compensation.

Companies will need to conduct an assessment to determine whether any conflicts exist, taking into account six factors set forth in Rule 10C-1(b)(4) under Section 10C of the Exchange Act. We expect that this final review will be undertaken by the compensation committee. This rule was added to the Exchange Act by Section 952 of the Dodd-Frank Act, concerning issuers' use of compensation consultants and related conflicts of interest.

These factors are:

- Whether the entity employing the compensation adviser provides any other services to the company;
- How much the entity who employs the compensation adviser has received in fees from the company, as a percentage of that entity's total revenue;
- What policies and procedures have been adopted by the entity employing the compensation adviser to prevent conflicts of interest;
- Whether the compensation adviser has any business or personal relationship with a member of the compensation committee;
- Whether the compensation adviser owns any stock of the company; and
- Whether the compensation adviser or the entity employing the adviser has any business or personal relationship with an executive officer of the company.

This assessment will involve participation by the company's compensation consultants, since much of the relevant information will be in their possession, and the assessment will need to be complete before companies finalize their 2013 proxy statements. Companies should check with their compensation consultants to see what conflicts analyses the consultants have done and should consider sending each consulting firm a questionnaire that asks questions regarding the business and personal relationships between the consultants and the company in order for the compensation committee to adequately address whether any conflicts of interest exist. In addition, we have updated our form of Director and Officer Questionnaire to include questions designed to collect information about any business and personal relationships directors or officers have with compensation consultants.

Although not required, as we have seen with the risk assessment disclosure requirement, many companies are opting to make an affirmative statement in their proxy statements regarding these matters in order to show that they have complied with the new disclosure obligation on compensation consultant conflicts of interest.

***SEC Approves New Listing Standards Regarding Compensation Committees and Consultants.*** As directed by the SEC all national securities exchanges [9] including the NASDAQ Stock Market LLC (Nasdaq) and the New York Stock Exchange, Inc. (NYSE) have finalized changes to their corporate governance requirements for companies listed on an exchange relating to compensation committee member independence and the powers and duties of such committees. These rules were required in response to new Rule 10C-1 promulgated pursuant to Section 10C of the Exchange Act which was added through the adoption of Section 952 of the Dodd-Frank Act and will prohibit the continued listing of any equity security of a company that is not in compliance with these new rules. [10] The new listing standards address:

- the independence requirements of the members of the compensation committee;
- compensation committees' authority to retain compensation advisers and be given the funding to hire them;
- the requirement for compensation committees to evaluate independence of any compensation advisers before hiring them; and
- the requirement for compensation committees to be directly responsible for the appointment, compensation, and oversight of the work of any compensation adviser.

These rules apply not only to compensation consultants, but also to other types of advisers to the compensation committee, such as outside legal counsel. However, the rules carve out the same exceptions for certain consultants as set forth in Item 407 of Regulation S-K. In addition, the rules do not:

- require compensation committees to retain independent legal counsel;
- preclude a compensation committee from hiring legal counsel that is not independent from the company; or
- preclude a compensation committee from obtaining advice from in-house counsel or outside counsel retained by the issuer or management.

Although the NYSE rules currently require listed companies to have a compensation committee comprised of at least two members who are independent directors and a written charter containing certain requirements, current Nasdaq rules do not. The revised rules will now require Nasdaq-listed companies to have a compensation committee composed entirely of independent directors instead of the current requirement that allows the majority of the independent members of the board of directors to make executive compensation decisions and a written charter covering certain key authorities and responsibilities. Nasdaq's definition of independence is more stringent than what the SEC mandated under Rule 10C-1 and specifically prohibits any compensation committee members from accepting, directly or indirectly, any consulting, advisory, or other compensatory fee, other than for board service, from an issuer or any subsidiary thereof consistent with current audit committee member requirements. [11] This particular requirement will not be applicable until the committee member's term on the compensation committee commences. Both exchanges have adopted similar affiliation rules as discussed below.

Under the NYSE listing rules, when determining the independence of any director for service on the compensation committee, the company's board of directors is required to consider all factors relevant to determining whether a director would have a material conflict of interest that would impair the director's ability to make independent judgments including, but not limited to:

- the source of the director's compensation, including any consulting, advisory, or other compensatory fee, paid by the company or any subsidiary thereof to the director; and
- whether the director is affiliated with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer, and determine whether such affiliation would impair the director's judgment as a member of the compensation committee.

The NYSE has not developed any bright line tests for independence in this area. The NYSE notes that when considering the sources of a director's compensation in determining independence for purposes of compensation committee service, the board should consider whether the director receives compensation from any person or entity that would impair his or her ability to make independent judgments about the listed company's executive compensation. Similarly, when considering any affiliate relationship a director has with the company, a subsidiary of the company, or an affiliate of a subsidiary of the company, in determining independence for purposes of compensation committee service, the board should consider whether the affiliate relationship places the director under the direct or indirect control of the listed company or its senior management, or creates a direct relationship between the director and members of senior management, in each case of a nature that would impair his or her ability to make independent judgments about the listed company's executive compensation.

Unlike with audit committees the SEC has acknowledged that for the affiliation test, some affiliations, such as those resulting from significant stock ownership, may in fact be appropriate and affiliate status should not, by itself, be considered an automatic disqualification for compensation committee service.

A company listed on Nasdaq must have a formal, written compensation committee charter, and certify to Nasdaq that it has adopted a charter and will review and reassess its adequacy on an annual basis. The charter must:

- specify the scope of the committee's responsibilities and how it carries out those responsibilities, including structure, process, and membership requirements;
- specify the committee's responsibility for determining (or recommending to the board for determination) the compensation of the CEO and all other executive officers;
- provide that the CEO may not be present during voting or deliberations on his or her compensation; and
- specify the committee's responsibilities and authority with respect to retaining advisers, funding advisers and reviewing the independence of advisers as discussed above.

We have updated our form of Compensation Committee charter to include the above requirements.

A smaller reporting company is not subject to the requirements of these new compensation committee rules, except that a smaller reporting company must have, and certify that it has and will continue to have, a compensation committee of at least two members, each of whom must be an independent director as defined under the current Nasdaq or NYSE independence rules. In addition, a smaller reporting company must certify that it has adopted a formal written compensation committee charter or board resolution that specifies certain of the content discussed above; however, it will not need to incorporate into its charter or board resolutions provisions regarding authority to retain and fund compensation consultants, counsel, and advisers and responsibility to consider the independence of compensation consultants, counsel, and advisers, nor will Nasdaq companies be required to review and reassess the adequacy of the charter or board resolutions annually.

The stock exchange rules other than the standards relating to the independence of committee members become effective on July 1, 2013. Companies are to have independent committee members by the earlier of the first annual shareholders meeting after January 15, 2014 or, if no meeting has been held then, by October 31, 2014.

***Cybersecurity Disclosure Expanded Through Comment Letters.*** [12] "There are only two types of companies: those have been hacked, and those that will be. Even that is merging into one category: those that have been hacked and will be again." These important words from FBI Director Robert Mueller at the 2012 RSA information security conference should be heeded by every officer or director of a public company. Last year's memorandum included details on the SEC's Cybersecurity Guidance issued in October 2011. [13] Since this guidance was issued, the SEC has issued comment letters to companies across various industries that provide insight helpful to companies crafting their cybersecurity disclosures this year. The SEC has issued comments to many companies requesting that they expand their risk factor disclosures in future filings to include both actual and potential cybersecurity threats that exist within the company and with third-party vendors. In some cases, the SEC noted that companies should include disclosure relating to cybersecurity risks even if the company had determined that this risk was not material to the company.

For example, in response to SEC comments, American International Group (AIG) agreed to expand its risk factor disclosure to include the following: "Like other global companies, we have from time to time, experienced threats to our data and systems, including malware and other virus attacks, unauthorized access, systems failures and disruptions." [14] The company added this language despite the fact that it did not believe that any incidents to date had "materially affected" its business or financial position. [15]

Amazon disclosed in its Form 10-K that the failure to prevent security breaches could expose the company and its customers to risks, but the SEC requested the company to go further and disclose the occurrence of a breach that was reported on the website of its subsidiary, Zappos.[16] Amazon argued that since Zappos was not material to its consolidated revenues, the attack did not have a material impact on its business.[17] Amazon added that a month after the attack, Zappos' revenue rose to pre-attack levels. However, the SEC commented that Amazon should disclose that it has experienced cyber-attacks and breaches.[18] Amazon agreed to revise its risk factor disclosure to include that "[s]ome subsidiaries had past security breaches, and, although they did not have a material adverse effect on our operating results, there can be no assurance of a similar result in the future."[19]

In its correspondence with Amazon, the SEC requested that the company "describe how third-party technology and systems…fit into [the] business operations and confirm the risks presented by…reliance on the third-party technology and systems….".[20] Similarly, in a comment letter to CIT Group, the SEC sought disclosure of actual and potential breaches experienced by third-party vendors and stated that the company should "clearly state in your risk factor that your third-party vendors have experienced attacks that affected some of your customers."[21]

Given the SEC's continued focus on cybersecurity, companies should not wait for further federal regulation to set standards for "best practices," but should assess their risks and develop risk factor disclosure based on those risks and also review their business description, financial statements, and legal proceedings, as appropriate.

***Conflict Minerals Rules.*** During 2012, the SEC finalized its highly controversial rulemaking required under the Dodd-Frank Act regarding conflict minerals–related disclosure. Section 1502 of the Dodd-Frank Act provides that the SEC shall require companies to disclose whether or not their products contain so-called "conflict minerals," defined as tin, gold, tantalum, or tungsten that are mined from the Democratic Republic of Congo and nine of its neighboring countries. This provision was included in the Dodd-Frank Act at the request of legislators who believe that the process of mining for and producing these particular minerals in certain countries is contributing to a grave, ongoing humanitarian crisis in that region of Africa. Congress' intent is that this required disclosure will "enhance transparency" surrounding the use of these minerals, such that consumers will be able to make more informed decisions about purchasing a variety of products based on companies' direct or indirect involvement in the conflict minerals trade.

Beginning in calendar year 2013, all public companies making filings pursuant to Sections 13(a) and 15(d) of the Exchange Act, including smaller reporting companies and foreign private issuers, are subject to the conflict mineral rules. Investment companies registered under the Investment Company Act of 1940 are not subject to the rule. The SEC rules require disclosure on a calendar year basis of an assessment of whether products contain these minerals. Public companies will be required to disclose via EDGAR on a new form, known as Form SD ("Specialized Disclosure Report"), by May 31 of the year following the assessment if certain facts are present based on what the company determines in its conflict minerals evaluation. The first of these reports will be due by May 31, 2014.

The SEC's rules release provides in-depth guidance on how to maneuver through the rules using a three-step process. Companies must make a determination as to whether any conflict minerals are necessary to the functionality or production of a product manufactured, or contracted to be manufactured by the issuer (step one). If so then the company must then perform a "reasonable inquiry" into where the conflict minerals originated, and make disclosure of their efforts and conclusions on a Form SD (step two). If a company makes a determination that it manufactures (or contracts to have manufactured) a product using conflict minerals that originate or may originate from the Democratic Republic of Congo or one of the adjoining countries, it must conduct a supply chain due diligence analysis and include an additional Conflict Minerals Report as well as an auditors' report as an exhibit to its Form SD (step three).

If conflict minerals are not necessary to the functionality or production of a product manufactured, or contracted to be manufactured, by an issuer, the issuer will not be subject to the conflict mineral rules and no further action and no filing of a Form SD will be necessary.

A group of business organizations recently filed an administrative legal challenge to the conflict minerals rules. If the rules are stayed pending resolution of the challenge, this could delay the first filing deadline, but in the meantime, companies should move forward with their assessments in order to be prepared to make the necessary disclosure by May 2014.

***The Iran Threat Reduction and Syria Human Rights Act of 2012.*** On August 10, 2012, President Obama signed the Iran Threat Reduction and Syria Human Rights Act of 2012 into law. This act added new Section 13(r) to the Exchange Act, which includes specific disclosure obligations for companies that are engaged in, or affiliated with entities that are engaged in, commercial activity with Iran and Syria, or nationals of those countries. While the SEC was not required to engage in any rulemaking under Section 13(r), it has issued Compliance and Disclosure Interpretations addressing questions that have arisen under that section. The disclosures required by Section 13(r) must be included in periodic reports that are required to be filed on or after February 6, 2013. As such, the disclosure requirements of Section 13(r) cover activities engaged in during all of 2012 (for calendar year-end companies), despite the act having been signed in August.

Among other things, Section 13(r) covers a broad scope of commercial activity conducted by reporting companies with the "Government of Iran," unless the activity has been specifically authorized by a U.S. federal department or agency. The Government of Iran is defined for this purpose to include all of that government's political subdivisions, agencies, and instrumentalities, entities owned or controlled directly or indirectly by the government, persons acting directly or indirectly for or on behalf of the government or any of its owned or controlled entities, and any other person who may be determined by the U.S. Office of Foreign Assets Control to fall within the definition of the Government of Iran.

This definition would encompass entities that are organized under the laws of Iran, including most transactions with Iranian financial institutions, individuals and entities located in Iran (and, in the case of persons whose assets have been frozen pursuant to executive orders dealing with terrorism or the proliferation of weapons of mass destruction or United Nations Security Council resolutions relating to Iran, some individuals who reside outside of Iran), and non-Iranian entities that are owned or controlled by any of these persons and entities.

Among the transactions that would require disclosure under Section 13(r) are transactions relating to Iran's energy industry; transactions facilitating Iran's procurement or proliferation of weapons or terrorism; and the transfer of technology or services to Iran that are likely to be used in connection with human rights abuses in Iran, including the restriction of the free flow of unbiased information and the disruption, monitoring, or restriction of free speech.

The disclosure requirement does not contain a materiality threshold with respect to the need to disclose any of these activities. As such, even a very small transaction in terms of dollar size or overall significance could result in the need to provide this disclosure.

In addition, under Section 13(r), companies may be liable for, and have to provide disclosure regarding, conduct that is known or should have been known to have been engaged in by their affiliates. For this purpose, the term "affiliate" includes any "person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the issuer." This definition is interpreted to include directors and executive officers, subsidiaries and entities controlled by the issuer, and controlling shareholders, to the extent the shareholder has the power to direct or cause the direction of the management and policies of the issuer as a result of its ownership.

There is no requirement to affirm the absence of any activity covered by Section 13(r), if an issuer and its affiliates have not engaged in any Iran-related activities subject to disclosure under the Act. These requirements relate to any company that files periodic reports under Section 13(a) of the Exchange Act, including smaller reporting companies and foreign private issuers.

An issuer that is required to make disclosure under Section 13(r) must also file a concurrent notice with the SEC detailing the information included in the annual report filing, which will be posted on the SEC's website and sent to the President and Congressional committees. The President will then be required to initiate an investigation within 180 days to determine whether and to what extent sanctions should be imposed on the reporting issuer.

***Other Sections of the Dodd-Frank Act Are Still Subject to Rulemaking.*** The Dodd-Frank Act contains several other sections that will impact companies' proxy statements in coming years, including the requirements to provide disclosure on measuring pay for performance, the ratio between CEO compensation and other employees' compensation, hedging of shares by employees and directors, and clawback of "erroneously awarded compensation." Although it has been some time since the passage of the Dodd-Frank Act, these sections of the Dodd-Frank Act remain subject to SEC rulemaking, and the SEC has not set a timetable for issuance of proposed regulations. We will update our clients and friends separately as these rules are proposed and issued.

***"Proxy Plumbing."*** In July 2010, the SEC issued a concept release on the U.S. proxy system.[22] This release, which has come to be known as the "proxy plumbing" release, addresses three principal questions regarding the current proxy system in the United States: whether the SEC should take steps to enhance the accuracy, transparency, and efficiency of the voting process; whether the SEC's rules should be revised to improve shareholder communications and encourage greater shareholder participation in the shareholder meeting process;

and whether the voting power held by shareholders is aligned with the economic interest of such shares. No rulemaking has yet been issued by the SEC in response to this concept release, but we understand that the SEC is continuing to evaluate the issues it raised in that document. In addition the SEC is also looking at proxy advisory firms and the role they play in shaping shareholder votes. Although the SEC has no ability to regulate these firms, the SEC is concerned about the lack of competition and the sway they seem to have over the voting decisions by many institutional investors.

## 2013 Periodic Report Filing Deadlines

For companies that qualify as large accelerated filers and have fiscal years ending on December 31, annual reports on Form 10-K are due 60 days after fiscal year-end (Friday, March 1, 2013).[23] Form 10-K reports continue to be due 75 days following fiscal year-end for accelerated filers[24] (Monday, March 18, 2013 for December 31 year-end companies) and 90 days after fiscal year-end for non-accelerated filers (Monday, April 1, 2013 for December 31 year-end companies).

In addition, Form 10-Q reports filed by accelerated filers and large accelerated filers continue to be due 40 days after the close of the fiscal quarter. The deadline for Form 10-Q reports for non-accelerated filers continues to be 45 days after the close of the fiscal quarter.

These changes do not affect the existing proxy statement filing deadline of 120 days after fiscal year-end for companies that choose to incorporate by reference from their definitive proxy statements the disclosure required by Part III of the Form 10-K.

## Board of Director and Committee Membership

Each year as part of the year-end reporting process, we recommend that companies carefully examine the membership profiles of their board and board committees. Sarbanes-Oxley, the SEC rules issued under Sarbanes-Oxley, and the listing requirements of Nasdaq, NYSE, and NYSE MKT (formerly NYSE AMEX) relating to board and committee membership requirements all impact who may serve.[25] Mintz Levin has prepared a director independence and qualification checklist to assist with this analysis, and we encourage you to evaluate each director and director nominee to ensure continued compliance with these requirements.

## Shareholder Approval of Equity Compensation Plans

Nasdaq, NYSE, and NYSE MKT all require shareholder approval for the adoption of equity compensation plans and arrangements for employees, directors, and consultants and for any material modification of such plans and arrangements, including the addition of new shares to a plan. Exemptions from the shareholder approval requirement continue to be available for inducement grants to new employees if such grants were approved by a compensation committee or a majority of the company's independent directors and promptly following the grant a press release is issued specifying the material terms of the award, including the name of the recipient and the number of shares issued, and in certain situations relating to an acquisition or merger. An exemption from the shareholder approval requirement is also available for certain tax-qualified, non-discriminatory employee benefit plans (such as plans that meet the requirements of Section 401(a) of the Internal Revenue Code and Employee Stock Purchase Plans meeting the requirements of Section 423 of the Internal Revenue Code), provided that such plans are approved by the issuer's compensation committee or a majority of the issuer's independent directors. Equity plans adopted prior to June 30, 2003 are unaffected under this rule, until a material modification is made to such a plan.

As noted above, companies considering option repricing programs in light of significant declines in their stock prices should note that such programs may require shareholder approval, depending on the terms of the equity compensation plan under which the options were granted. In the event that shareholder approval is required, the company will need to file a preliminary proxy statement with the SEC, which would not be required for approval of a new plan or an amendment to an existing plan.

Companies should review their existing equity compensation plans as part of their year-end reporting preparation in order to determine whether shareholder approval will need to be obtained for new plans, increases in the numbers of shares available under old plans, option repricing programs, or material plan amendments. This is another area that ISS continues to weigh in on heavily both with respect to the number of shares to be authorized under the plan and some of the substantive disclosure within the plan itself so plenty of time should be allotted to proposals in this area.

## Other Year-End Considerations

We also recommend that companies take the opportunity while planning their year-end reporting to consider what amendments may be necessary or desirable to their corporate documents over the coming year that may require shareholder approval. Some items to consider are:

- Does the company have enough shares authorized under its certificate of incorporation to achieve all of its objectives for the year, including acquisitions for which it may want to use its stock as currency?
- Does the company have adequate shares available under its equity compensation plans to last throughout the year?
- Are there other material changes that should be made to the company's equity compensation plans that would require shareholder approval?
- Has the company reviewed its charter and by-laws to assess any anti-takeover measures in place?

To the extent that a company expects any proposal in its proxy statement to create controversy among its shareholder base, it may want to consider hiring a proxy solicitor to assist with the process of seeking the requisite shareholder vote.

## Mintz Levin Website: Publications

We would also like to call your attention to the many client advisories and alerts regarding topics of current interest that are available to you on our website, www.mintz.com. New alerts and advisories are posted frequently, and we hope that you will find the information to be useful.

Please contact the Mintz Levin attorney who is responsible for your corporate and securities law matters if you have any questions or comments regarding this information. We look forward to working with you to make this year's annual reporting process as smooth as possible.

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View Mintz Levin's Corporate & Securities attorneys.

### Endnotes

1 We invite you to review our memorandum from last year, which analyzed regulatory changes that were new for fiscal year 2011, and we would be happy to provide you with another copy upon request.

2 Smaller reporting companies are those that have less than $75 million in public float as of the last business day of their most recently completed second fiscal quarter.

3 The SEC requires equity awards be valued as of their grant date fair value, which value is a formula based on certain assumptions that is supposed to represent the potential value of the award over the life of the award if fully realized.

4 See ISS US 2013 Compensation Policy Updates FAQs at www.issgovernance.com/policy/2013/USCompensationFAQ which discusses how ISS will calculate a company's realizable pay.

5 The ISS 2013 policy in evaluating say-on-pay is available on its website at http://www.issgovernance.com/docs/EvaluatingPayForPerformance2012.

6 Companies must be mindful of Regulation FD (Fair Disclosure) and not disclose material nonpublic information selectively nor risk sending mixed messages from the disclosures contained in the company's proxy statement or other SEC filings when speaking with stockholders.

[7] Item 407(e)(3)(iii) of Regulation S-K continues to require disclosure of "any role of compensation consultants in determining or recommending the amount or form of executive and director compensation," including the identity of the compensation consultant; whether the consultant was retained directly by the compensation committee or any other person (such as management); the nature and scope of the consultant's assignment and the material elements of any instructions given to the consultant; and, if the consultant was paid fees in excess of $120,000 during the fiscal year for providing other services to the corporation, the aggregate fees paid to the compensation consultant for all services provided.

[8] As set forth currently in Item 407 of Regulation S-K, the rule does not require an assessment of a compensation consultant whose role is limited to consulting on a broad-based plan that does not discriminate in favor of executive officers or directors of the company, and that is available generally to all salaried employees; or who solely provides information (such as survey data) that is not customized for a particular company or that is customized based on parameters that are not developed by the adviser, and about which the adviser does not provide advice.

[9] Companies listed on the OTC Bulletin Board (OTCBB) and the OTC Markets Group (previously known as the Pink Sheets and Pink OTC Markets) are not required to comply with these rules unless their securities also are listed on a national securities exchange. In addition, limited partnerships, companies in bankruptcy proceedings, registered open-end management investment companies, controlled companies, and foreign private issuers continue to be exempt.

[10] Please see Release No. 33-9330, available on the SEC's website at http://www.sec.gov/rules/final/2012/33-9330.pdf (the "Adopting Release").

[11] This does not include fees received as a member of the board or any committee thereof, nor will it include receipt of fixed amounts under a retirement plan, including deferred compensation, for prior service with an issuer.

[12] The authors wish to thank Cynthia Larose, Member in Mintz Levin's Corporate & Securities Practice, and Amy Malone, Associate in Mintz Levin's Corporate & Securities Practice, for their assistance with this portion of the memorandum.

[13] Securities and Exchange Commission, CF Disclosure Guidance: Topic No. 2, Cybersecurity (October 13, 2011).

[14] Letter dated May 21, 2012 to the Division of Corporate Finance, available at http://www.sec.gov/Archives/edgar/data/5272/000119312512242072/filename1.htm.

[15] Letter dated April 18, 2012 to the Division of Corporate Finance, available at http://www.sec.gov/Archives/edgar/data/5272/000119312512168967/filename1.htm.

[16] Staff Comment Letter dated March 12, 2012 to Amazon.com, Inc., available at http://www.sec.gov/Archives/edgar/data/1018724/000000000012012577/filename1.pdf.

[17] Letter dated April 9, 2012 to the Division of Corporation Finance, available at http://www.sec.gov/Archives/edgar/data/1018724/000119312512155627/filename1.htm.

[18] Staff Comment Letter dated April 18, 2012 to Amazon.com, Inc., available at http://www.sec.gov/Archives/edgar/data/1018724/000000000012019757/filename1.pdf.

[19] Letter dated May 3, 2012 to the Division of Corporation Finance, available at http://www.sec.gov/Archives/edgar/data/1018724/000119312512208583/filename1.htm.

[20] See *supra* note 17.

[21] Staff Comment Letter dated July 6, 2012 to CIT Group, Inc., available at http://www.sec.gov/Archives/edgar/data/1171825/000000000012035281/filename1.pdf.

[22] Concept Release on the U.S. Proxy System (Release No. 34-62495, July 14, 2010), *available at* http://www.sec.gov/rules/concept/2010/34-62495.pdf.

[23] *Large accelerated filers* are domestic companies that meet the following requirements as of their fiscal year-end:

- have a common equity public float of at least $700 million, measured as of the last business day of their most recently completed second fiscal quarter (i.e., for calendar fiscal year-end companies, this test would be applied as of June 30, 2012);
- have been subject to the reporting requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, for at least 12 months;
- have previously filed at least one Annual Report on Form 10-K; and
- do not qualify as small business issuers under SEC rules.

[24] *Accelerated filers* are those that meet all of the above tests but have a common equity public float of at least $75 million,

but less than $700 million, measured as of the last business day of their most recently completed second fiscal quarter (i.e., for calendar fiscal year-end companies, this test would be applied as of June 30, 2012).

[25] Please see our advisory dated November 2003 entitled “Changes to Corporate Governance Standards for Nasdaq-Listed Companies” for a further description of these changes.