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Companies Should Not Take Lightly the Need for Full Compliance with the SEC's Executive Compensation Disclosure Rules

As calendar year companies work on preparing their 2011 proxy statement materials, we wanted to report on a recent development that highlights the importance of a company's full disclosure of, and compliance with, the SEC's executive compensation disclosure rules.

By way of background, there were several additional executive compensation disclosure requirements added by the Dodd-Frank Act (*see* our July 16, 2010, July 26, 2010 and October 21, 2010 blogs), in addition to the amendments to the disclosure rules adopted by the SEC in December 2009 (*see* our December 18, 2009 blog), that will be in effect for the 2011 proxy season. Additionally, it appears that the SEC is likely to adopt final rules on Say-on-Pay on January 25, 2011. Therefore, as discussed below, failure to provide full disclosure may lead to negative consequences for both the company and its executives officers.

On January 12, 2011, the SEC charged NIC, Inc. and four of its current or former executive officers with failing to disclose to investors more than $1.18 million in perquisites paid to its former CEO over a six-year period. These perquisites included NIC, Inc. footing the bill for vacations, computers, a car, flight training, spa and health club and day-to-day personal living expenses for its former CEO, his girlfriend, and his family. Additionally, the SEC claimed that NIC, Inc. failed to disclose that it paid thousands of dollars per month for its former CEO to live in a Wyoming ski lodge and commute by private aircraft to his office at NIC's headquarters. Moreover, the SEC alleged that NIC and its executives falsely represented to investors that its former CEO worked virtually for free from 2002 to 2005, and then continued to materially understate the perquisites that its former CEO received in 2006 and 2007. In connection with this investigation, the SEC's Division of Enforcement emphasized that "[p]ublic disclosure of executive perks helps investors evaluate whether corporate assets are being used wisely or squandered." NIC, its former CEO and CFO, and its current CEO agreed to pay a combined $2.8 million to settle the SEC's charges against them without admitting or denying the allegations, in addition to various non-monetary penalties. The SEC's litigation continues against NIC's current CFO.

We expect that the SEC will make good on its statements to compel companies to amend their filings if there is material noncompliance in the Compensation Discussion and Analysis ("CD&A") and related disclosure sections. This stated resolve of the SEC to ensure compliance with its executive compensation disclosure rules, as evidenced in the NIC, Inc. investigation and charges, along with the added requirements of the Dodd-Frank Act including Say-on-Pay, provide further impetus for companies to faithfully discharge their duties with respect to executive compensation disclosure. As we have mentioned in our previous blogs, companies particularly may want to consider:

- Reviewing their existing CD&A and tabular/narrative sections to ensure that they provide clear and comprehensive disclosure;

- Reviewing their golden parachute arrangements and determine if such arrangements are appropriate, defensible and transparent; and
- Examining and confirming full disclosure of perquisites received by the company's executive officers and directors.

Accordingly, and especially in light of Say-on-Pay, compensation committees should consider evaluating their executive compensation programs and disclosures, perhaps utilizing the assistance of its own advisors and legal counsel, from a fresh perspective with an objective of effecting improvements to the maximum extent possible. Failure to do so could provoke comments from the SEC which could then force the company to have to amend its SEC filings or even subject the company and its officers to more severe consequences.

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