



SOCIETY OF CORPORATE SECRETARIES  
& GOVERNANCE PROFESSIONALS

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# Small and Mid Cap Companies: Streamlining Corporate Governance

## Practical Perspectives



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# I. Introduction - Life as Small or Mid-Cap General Counsel

- Disadvantages:
  - Resource limitations
    - In-house
    - Outside
  - Largely the same compliance requirements
  - May have more entrepreneurial culture



# I. Introduction - Life as Small or Mid Cap General Counsel

- Advantages:
  - Resources close at hand
  - Resources easily accessible
  - Stockholder base more concentrated
  - “Fly beneath the radar”



## **II. Board Management**

### ***Practical Suggestions for Board and Committee Activities/Functions/Actions***

- Composition of Board
  - Management, investors, consultants, large company directors
- Best practices vs. requirements
- Administrative challenges
  - Software options
  - Drafting agendas, minutes and consents
  - Board packages
  - Board use of company resources



## III. Managing Disclosure

### *Overview of Regulation FD*

- Disclosure requirements:
  - Whenever an issuer (or a person acting on its behalf) intentionally discloses material nonpublic information, it must make the disclosure publicly, rather than selectively to analysts or other market professionals or to stockholders who are likely to trade on the information.
  - If an issuer inadvertently discloses material nonpublic information on a selective basis, the issuer must promptly disseminate the same information publicly.
  - Regulation FD does not apply to communications with the press, rating agencies, customers and vendors nor does it require disclosure if the information is shared with someone under a duty or contract to keep it confidential.



## Regulation FD Liability

- Penalties for violating Regulation FD include monetary penalties, cease and desist orders, and injunctions.
- No private right of action exists to enforce FD.
- Selective disclosure in violation of FD does not by itself create liability under 10b-5, but liability for tipping and insider trading under Rule 10b-5 may still exist.



## Regulation FD Actions

SEC can enforce through administrative action and potential civil action.

- Recent actions provide practical guidance
  - SEC v. Christopher A. Black, Case No. 09-CV-0128 (S.D. Ind., September 24, 2009)  
(<http://sec.gov/litigation/complaints/2009/comp21222.pdf>) – A robust compliance program can be important in minimizing the impact of regulatory enforcement even in the face of a Regulation FD violation.
    - The CFO of American Commercial Lines, Inc. (ACL), selectively disclosed material, nonpublic information to a limited number of analysts without simultaneously making that information available to the public.
    - The SEC brought an action against the CFO but not against ACL.



## Regulation FD Actions (continued)

- SEC v. Christopher A. Black (continued)
  - The SEC cited several factors in determining not to bring an enforcement action against ACL:
    - corporate environment of compliance (e.g., training, policies).
    - CFO acted alone, outside of control systems.
    - Promptly filed Form 8-K.
    - Prompt self-reporting to the SEC.
    - Extraordinary cooperation with the staff's investigation.
    - Remedial measures (e.g., adoption of additional controls).



## Adopt Effective FD Procedures

- Executive training and education on disclosure.
- Establish guidelines and procedures to avoid selective disclosure of material, non-public information in private communications.
  - KISS
- Determine who speaks for company.
- Help ensure that information that is disclosed to third parties, including information contained in SEC filings, is accurate, timely, consistent and understandable.



## Form 8-K Current Report Compliance

- Educate and track Form 8-K triggers.
- Process to notify appropriate personnel.



## Periodic Disclosures

- Management's discussion and analysis (Form 10-K and 10-Q)
- Risk Factors
- Proxy statement
  - Who is drafting?
  - Compensation disclosures
  - Changes regarding corporate governance disclosures
- Drafting resources
- Other disclosures



## Periodic Disclosures (continued)

- Scaled disclosure for “smaller reporting companies”
  - generally applies to companies with public common equity float of less than \$75 million.
  - reduced disclosure for items including the following Regulation S-K Items:

Item 101	Description of business
Item 201	Market price of and dividends on registrant’s common equity and related stockholder matters
Item 301	Selected financial data
Item 302	Supplementary financial information
Item 303	Management’s discussion and analysis of financial condition and results of operations
Item 305	Quantitative and qualitative disclosures about market risk
Item 402	Executive compensation
Item 404	Transactions with related persons, promoters and certain control persons
Item 407	Corporate governance
Item 503	Prospectus summary, risk factors, and ratio of earnings to fixed charges
Item 504	Use of proceeds
Item 601	Exhibits



## Disclosure/Risk Management Considerations

- Disclosure committee or disclosure team
  - Proximity of disclosure team members to ensure easy informal flow of information.
    - Issue spotting
  - Review of periodic and current event SEC filings and other disclosures.
- Roles of various parties - board members, audit committee, CEO, CFO, COO, disclosure committee, general counsel, internal auditors, external auditors, outside advisors.
- Challenges of disclosure of Non-GAAP financial measures (Regulation G compliance considerations based on disclosure context).



## Disclosure/Risk Management Considerations (continued)

- Policies - record retention, FCPA, OFAC regulations, employee code of conduct (NASDAQ 5610; NYSE 303A.10) and code of ethics (SOX 406).
  - simpler policies may facilitate increased understanding and compliance by employees
  - up the ladder reporting (SOX 307)
- Documentation of risk management actions – documentation may be beneficial in the event procedures or actions are questioned/investigated.



## Internal Controls Over Financial Reporting

- Management overrides - concentration of management authority and reduced segregation of control functions may reduce internal controls, so proper procedures more important.
- The deadline for 404(b) auditor attestation for smaller public companies has been extended to annual reports covering fiscal years ending on or after June 15, 2010.
  - See SEC press release regarding the extension (<http://www.sec.gov/news/press/2009/2009-213.htm>) and SEC adopting release regarding the extension (<http://www.sec.gov/rules/final/2009/33-9072.pdf>).



## IV. Other Resources

- SEC release regarding adoption of scaled disclosure for Smaller Reporting Companies (<http://www.sec.gov/rules/final/2007/33-8876.pdf>)
  - See also Regulation S-K Item 10(f)
- Nasdaq Corporate Governance Rules (<http://nasdaq.cchwallstreet.com/>)
  - See Rule 5600 series – Corporate Governance Requirements
- Nasdaq Press Release, October 5, 2009 - The NASDAQ Listing and Hearing Review Council Seeks Comments From Issuers On Corporate Governance Best Practices (<http://www.nasdaq.com/newsroom/news/newsroomnewsStory.aspx?textpath=pr2009\ACQPMZ200910051500PRIMZONEFULLFEED174632.htm&year=10/05/2009%20+3%3a00PM>)
- NYSE Corporate Governance Rules (<http://nysemanual.nyse.com/LCM/Sections/>)
  - See Rule 303A series – Corporate Governance Standards
- NYSE Press Release, September 1, 2009 - NYSE Forms “Commission on Corporate Governance” to Examine U.S. Corporate Governance (<http://www.nyse.com/press/1251799796551.html>)
- SEC Press Release, October 2, 2009 - Small Public Companies to Begin Providing Audited Assessment of Internal Controls Over Financial Reporting in Nine Months (<http://www.sec.gov/news/press/2009/2009-213.htm>)



## Selected Regulation FD Enforcement Actions

- SEC v. Christopher A. Black, Case No. 09-CV-0128 (S.D. Ind., September 24, 2009).
- In the Matter of Electronic Data Systems Corporation, Release No. 34-56519 (Sept. 25, 2007).
- In re Flowserve, Litigation Release No. 19154 (March 24, 2005).
- SEC v. Siebel Systems, Inc., Kenneth A. Goldman and Mark D. Hanson, 384 F.Supp.2d 694 (S.D.N.Y., 2005) (dismissed claim for failure to state a cause of action under Reg FD); *see also* In the Matter of Siebel Systems, Inc., Release No. 34-46896, Litigation Release No. 17860 (Nov. 25, 2002).
- In the Matter of Senetek PLC, Litigation Release No. 34-46895 (Sept. 16, 2004).
- SEC v. Schering-Plough Corporation, Litigation Release No. 18740 (Sept. 9, 2003).
- In the Matter of Raytheon Company and Franklyn A. Caine, Release No. 34-46897 (Nov. 25, 2002).
- In the Matter of Secure Computing Corporation and John McNulty, Release No. 34-46895 (Nov. 25, 2002).
- Report of Investigation in the Matter of Motorola, Inc., Release No. 34-46898 (Nov. 25, 2002).



# Questions?



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