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SEC Adopts Expanded Governance and Executive Compensation Disclosures

Yesterday, the SEC adopted final rules that broaden the scope of required executive compensation and corporate governance disclosures and require 8-K reporting of shareholder vote results. The full text of the rules is available at http://www.sec.gov/rules/final/2009/33-9089.pdf.

Effectiveness. The rules become effective on February 28, 2010 and generally will apply to the 2010 proxy season. It is not entirely clear from the release whether a proxy statement filed prior to February 28, 2010 with respect to an annual meeting occurring after that date must comply with the new rules. Companies should monitor whether the SEC provides additional guidance on this point and other interpretive issues that may arise.

Board Involvement in Risk Oversight. The rules require a description in proxy statements of the board's role in company risk oversight. In contrast to the proposed rules, which would have applied to the board's involvement in "risk management," the final rules recognize that company executives are responsible for day-to-day management, subject to the direction and oversight of the board.

Qualifications and Experiences of Directors. The rules expand required disclosures about directors and director nominees, mandating an annual discussion of the specific experiences and skills relevant to service as a director. In addition, the rules impose longer look-back periods for disclosure of other directorships (5 years) and of legal proceedings (10 years), with an expansion of the types of disclosable legal proceedings. Companies should update their D&O questionnaires to address the new requirements.

Board Diversity. The rules require companies to disclose in their proxy statements whether, and if so, how, the nominating committee considers diversity in board composition. If the nominating committee has a policy regarding board diversity, the company must describe how the nominating committee implements, and assesses the effectiveness of, the policy. For purposes of this disclosure, each company may define diversity as it deems appropriate, and may consider any number of factors, such as professional experience, education, race, gender or national origin.

Leadership Structure. The rules require a proxy statement description of, and explanation for, the board's leadership structure, including whether and why a company has chosen to combine or separate the CEO and Chairman positions, and whether and why a company has a lead independent director (and, if so, such person's responsibilities).

Valuation of Equity Compensation Awards. The rules require valuation of equity awards in the Summary Compensation Table and Director Compensation Table based on the grant date fair value of awards made during the covered year, rather than the accounting expense recognized during the covered year for all outstanding awards. For performance awards, grant date fair value will be based on the probable outcome of the performance conditions, with footnote disclosure regarding award value in the event of "maximum performance." Under the rules, companies must re-calculate amounts (including amounts reflected in the total compensation column) for each preceding fiscal year required in the table, but do not have to change the individuals who constitute named executive officers as a result of the recalculations.

Risk and Broad-Based Compensation Programs. To the extent that risks arising from a company's compensation programs for employees *generally* (not just executives) are *reasonably likely to have a material adverse effect* on the company, the rules require a stand-alone discussion, independent from the Compensation Discussion & Analysis, of the company's compensation programs as they relate to risk management and risk-taking incentives. The "reasonably likely to have a material adverse effect" threshold under the final rules will require less speculative disclosures than the proposed "may have a material affect" standard would have required.

Compensation Consultants. The rules require disclosure of fees paid to compensation consultants and their affiliates under certain circumstances. Unlike the proposed rules, the final rules do not require disclosure of the nature and extent of additional services provided by the compensation consultant and its affiliates. Companies should implement appropriate disclosure controls to track consulting fees and to determine whether circumstances require disclosure.

Accelerated Disclosure of Shareholder Vote Results. The rules shift disclosure of shareholder vote results from periodic filings to Form 8-K, which must be filed within four business days of the relevant shareholder meeting. If final voting results are not available within the applicable time frame, a company must report preliminary results on Form 8-K within four business days of the meeting and must disclose final results on an amendment to the Form 8-K within four business days of determination.

Proxy Solicitation Rules. The SEC did not take action with respect to proposed rules regarding the proxy solicitation process, choosing to defer consideration of those rules pending consideration of the SEC's proposal to require companies to include directors nominated by shareholders in company proxy statements and proxy cards.

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The final rules include a number of key new disclosure requirements that will impact the 2010 proxy season. Given the relatively short time frame, companies promptly should begin to review and digest the new rules, to prepare the required disclosures and to discuss with their boards the nature and scope of the new disclosures.

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