

**SEC PROPOSES NEW EXECUTIVE COMPENSATION DISCLOSURE RULES**

On January 27, 2006, the Securities and Exchange Commission (the “SEC”) proposed rules regarding new disclosure requirements for executive and director compensation, Form 8-K filings, related party transactions, director independence and corporate governance matters. As proposed, these new rules represent a major revision of executive and director compensation disclosure requirements and may force companies to reexamine their executive compensation practices.

Comments may be submitted to the SEC until April 10, 2006. The SEC hopes to have final rules in place for the 2007 proxy season. This memorandum identifies actions that should be considered now and provides a summary of the major features of the proposed rules.

**What Companies Should Do Now**

Although the proposed rules will not be effective until the 2007 proxy season, they provide some interpretive guidance for disclosure during the 2006 proxy season and insight into what may be required for 2007 and beyond.

**Review Current Disclosure of Perquisites.** Although the existing perquisite disclosure rules and dollar thresholds will continue to apply for the 2006 proxy season, the proposed rules offer extensive guidance into the SEC’s thinking as to what constitutes a compensatory perquisite subject to disclosure and the manner and extent to which perquisites should currently be disclosed. In light of the SEC’s recent actions against Tyson Foods, Inc.<sup>1</sup> for inadequate perquisite disclosure and the existing requirement for “clear, concise and understandable disclosure of *all* plan and non-plan compensation,” companies should review their current compensation practices relating to perquisites to determine whether all perquisites are currently being fully and accurately disclosed.

**Review Current Compensation Policies and Objectives.** One of the main features of the proposed rules is the new Compensation Discussion and Analysis, which will replace the Compensation Committee Report on Executive Compensation. This will require disclosure of each company’s compensation practices and policies and the role that executive officers play in the compensation process. As companies establish and administer existing compensation arrangements and set compensation levels for the 2006 fiscal year, compensation committees and senior management will need to evaluate carefully how their current policies, decisions and involvement would be disclosed under the proposed rules and consider what structural changes may be appropriate.

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<sup>1</sup> In the Matter of Tyson Foods, Inc. and Donald Tyson, Exchange Act Release No. 51625 (April 28, 2005).

**Related-Party Transaction Review and Approval Policies.** As part of the revision to related-party transaction disclosure, the proposed rules would require disclosure of a company's policies and procedures for the review, approval or ratification of related-party transactions, including identification of any transactions required to be reported that were not subject to review, approval or ratification under the company's existing policies, or where such policies and procedures were not followed. Companies should examine their current policies and procedures regarding review, approval or ratification of related-party transactions, adopt changes if appropriate or establish policies if none currently exist.

**Review Employees Covered Under 162(m)-Compliant Plans.** The proposed rules would require disclosure on the basis of "total compensation" for the last fiscal year, rather than salary and bonus, as is currently the case. They would also require disclosure for the chief financial officer, regardless of his or her level of compensation. As a result, the group of officers disclosed by companies for compensation earned in 2006 and beyond could be different than the group disclosed in this year's proxy. Section 162(m) of the Internal Revenue Code limits the deductibility of compensation paid to "Covered Employees" unless the compensation is "performance-based." Section 162(m) also refers back to the SEC's executive compensation disclosure rules to determine "Covered Employees," so a company's Covered Employees for 2006 compensation may change as well. Companies should therefore try to determine now those individuals for whom disclosure under the proposed rules would be required for next year's proxy, and may want to take steps now, as they establish bonus programs for 2006, to include those individuals in Section 162(m)-compliant plans.

### **Executive Compensation Disclosure**

The proposal divides the executive compensation disclosure into four sections:

- (I) A Compensation Discussion and Analysis, providing narrative disclosure of a company's compensation objectives and policies, intended to give context to the compensation disclosure provided elsewhere;
- (II) A revised Summary Compensation Table disclosing compensation with respect to the last three fiscal years, supplemented by (i) two additional tables covering Grants of Performance-Based Awards and Grants of All Other Equity Awards, providing back-up information for certain data in the Summary Compensation Table, and (ii) narrative explanatory disclosure to these tables;
- (III) Tabular disclosure covering holdings of equity-based awards as of the end of the last fiscal year and exercises and vesting of equity-based awards during the last fiscal year; and
- (IV) Tabular and narrative disclosure of retirement and other post-employment compensation, including deferred compensation plans and compensation payable upon a change in control or termination of employment.

## ***I. Compensation Discussion and Analysis***

The new Compensation Discussion and Analysis (CD&A) would replace the Compensation Committee Report on Executive Compensation and would require a narrative description of the material elements of a company's compensation objectives and policies for named executive officers. In light of the expanded disclosure under the CD&A, the Performance graph would also be eliminated. The CD&A would address the following six questions:

1. What are the objectives of the company's compensation programs?
2. What is the compensation program designed to reward and not reward?
3. What is each element of compensation?
4. Why does the company choose to pay each element?
5. How does the company determine the amount (and, where applicable, the formula) for each element?
6. How does each element and the company's decisions regarding that element fit into the company's overall compensation objectives and affect decisions regarding other elements?

The CD&A is intended to be comprehensive, covering post-termination compensation arrangements as well as arrangements applicable during employment. Examples of issues that would potentially be appropriate for a company to address in the CD&A include:

- Policies for balancing (i) immediate and long-term compensation, (ii) cash and non-cash compensation, and (iii) different forms of non-cash compensation;
- For long-term compensation, the basis for allocating compensation to each different form of award;
- For equity-based compensation, how the determination is made as to when the award is granted;
- What specific items of corporate performance are taken into account in setting compensation policies and making compensation decisions;
- How specific elements of compensation are structured to reflect individual performance;
- The factors considered in decisions to increase or decrease compensation materially;
- How prior compensation is considered in setting future compensation;
- The impact of accounting and tax treatments of a particular form of compensation;
- The company's equity or other security ownership requirements or guidelines and any company policies regarding hedging the economic risk of such ownership;

- Whether the company engaged in any benchmarking of total compensation, or any material element of compensation, identifying the benchmark and its components; and
- The role of executive officers in the compensation process.

As is currently the case, companies would not be required to disclose target levels with respect to specific quantitative or qualitative performance-related factors, or any factors or criteria involving confidential commercial or business information, the disclosure of which would have an adverse effect on the company.

The CD&A would be considered “filed” with the SEC, unlike the current Compensation Committee Report which is simply “furnished,” and would therefore be subject to Regulations 14A and 14C under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and to potential liability under Section 18 of the Exchange Act. In addition, to the extent that the CD&A and any other disclosure regarding executive officer and director compensation or other matters is included or incorporated by reference into a periodic report, the disclosure would be subject to the certifications that CEOs and CFOs are required to make under the Sarbanes-Oxley Act of 2002.

## ***II. Summary Compensation Table and Supplemental Tables***

### **A. Summary Compensation Table**

Under the proposed rules, the Summary Compensation Table (the “SCT”) would continue to serve as the principal disclosure vehicle for executive compensation. The SCT would continue to require disclosure of compensation for named executive officers for each of the company’s last three completed fiscal years. However, a transition rule would allow the new disclosure to be phased in over the first three years after the final rules become effective, so that compensation for the years prior to the first year the rules become effective would not have to be restated in the new format. As a result, for the first year that the revised SCT becomes effective, disclosure will only cover the last completed fiscal year.

#### SUMMARY COMPENSATION TABLE

Name and Principal Position	Year (\$)	Total (\$)	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Stock Incentive Plan Compensation (\$)	All other Compensation (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)

***Named Executive Officers (“NEOs”) Column.*** The revised SCT would cover the principal executive officer, the principal financial officer, and the three other most highly compensated executive officers. The addition of the principal financial officer, regardless of compensation level, is a change from the current requirements. Consistent with the current treatment of principal executive officers, anyone who served as a principal financial officer at any time during the fiscal year, even if he or she is not serving as the principal financial officer at the end of the

fiscal year, would be included in the SCT. As is currently the case, up to two additional executive officers for whom disclosure would have been required but for the fact that they were no longer serving as executive officers at the end of the fiscal year would also be included.

The most highly compensated executive officers would be identified on the basis of “total compensation” for the last fiscal year, not solely on annual salary and bonus for the last fiscal year, as is currently the case. The current \$100,000 threshold used to determine whether any of the three most highly compensated executive officers needs to be disclosed has been retained, but would also be based on total compensation, rather than just salary and bonus, as under current rules. The proposed rules would eliminate the current exclusion for compensation that is “non-recurring and unlikely to continue,” but retain the exclusion for cash compensation relating to overseas assignments. Such nonrecurring compensation would be included in determining whether an executive was one of the highest-paid executive officers.

**Total Compensation Column.** A new column (proposed column (c)) would require disclosure of the total dollar amount of compensation for each NEO. This column would aggregate the total dollar value of each form of compensation quantified in the columns that would follow it (columns (d) through (i)).

**Salary and Bonus Columns.** The Salary and Bonus columns (proposed columns (d) and (e) respectively), would be retained substantially in their current form, including reporting compensation that was earned, but for which payment was deferred. However, footnote disclosure would be required for any such amounts which were deferred. Where salary and bonus cannot be calculated in time to include these amounts in the SCT, the proposal would require the company to disclose in a footnote when the calculation is expected to be made and to report the amounts on Form 8-K when they become calculable.

**Stock Awards Column.** The Stock Awards column (proposed column (f)), would disclose the dollar value of awards without “option-like” features that derive their value from the company’s equity securities or permit settlement by issuance of the company’s equity securities, such as restricted stock, restricted stock units, phantom stock, phantom stock units, common stock equivalent units and other similar instruments. The dollar value for these awards would be based on their grant date fair value as determined pursuant to FAS 123R for financial reporting purposes. Equity-based awards subject to performance-based conditions would also be included in this column, as well as earnings on these equity-based awards such as dividends or dividend equivalents.

**Option Awards Column.** The Option Awards column (proposed column (g)), would disclose options, stock appreciation rights, and similar equity-based compensation awards with option-like features. However, instead of reporting the number of securities underlying the awards, as is currently required, this column would require disclosure of the grant date fair value of the award as determined pursuant to FAS 123R for financial reporting purposes. This column would also include the fair value of any previously awarded options or stock appreciation rights that are repriced or materially modified during the fiscal year.

**Non-Stock Incentive Compensation Column.** The Non-Stock Incentive Compensation Column (proposed column (h)), would report the dollar value of all non-equity-based amounts *earned* during the fiscal year (*i.e.* in the year when the performance criteria are satisfied, whether or not payment is actually made) pursuant to performance-based incentive plans. *Grants* of these awards would not be reported in the SCT but rather would appear in the Grants of Performance-Based Awards Table in the year of grant. This column would be limited to performance-based awards where the relevant performance measure is not based on the price of the company's equity securities and the award may not be settled by issuance of a company's equity securities. As is the case with stock and option awards, earnings on non-stock incentive compensation would be required to be included in this column as well.

**All Other Compensation Column.** The All Other Compensation column (proposed column (i)), would disclose all compensation not required to be included in another column. Any item of compensation that exceeds \$10,000 would be separately identified and quantified in a footnote. Items less than \$10,000 (other than perquisites, discussed below) would be included in the column, but footnote disclosure would not be required. This column would include disclosure of:

- All earnings on compensation that is deferred on non-tax-qualified defined contribution plans. (Current disclosure is limited to "above-market" earnings only.)
- The aggregate increase in actuarial value of defined benefit plans (including tax-qualified and non-tax-qualified supplemental plans) accrued during the year.
- The value of perquisites and other personal benefits, unless the aggregate amount of such compensation is less than \$10,000, in which case no such disclosure would be required. Footnote disclosure would be required for each particular perquisite to the extent the value of such perquisite is the greater of \$25,000 or 10% of the total perquisites. The same perquisites disclosure thresholds apply to director compensation disclosure as well.
- The proposal provides interpretive guidance as to what the SEC considers to be a perquisite. The SEC's view is that an item is a perquisite if it confers a direct or indirect benefit that has a personal aspect, without regard to whether it may be provided for some business reason or for the convenience of the company (*e.g.*, use of company-provided aircraft, yachts or other watercraft, commuter transportation services, additional clerical or secretarial services devoted to personal matters or investment management services), unless it is generally available on a non-discriminatory basis to all employees. An item is NOT a perquisite if it is integrally and directly related to the performance of the executive's duties (*e.g.*, office space at a company business location, a reserved parking space that is closer to business facilities but not otherwise preferential and additional clerical or secretarial services devoted to company matters). As is currently the rule, the value of a perquisite should be determined based on the company's incremental cost of providing the benefit to the executive and not on the cost attributed for Federal income tax purposes.
- Amounts paid or accrued in connection with any termination of employment or a change in control.
- Company contributions or other allocations to vested and unvested defined contribution plans.

- The dollar value of any life insurance premiums.
- Tax gross-ups and other tax reimbursements.
- Discounts on the purchase of company securities.

The proposal seeks public comment as to whether the information in the All Other Compensation column would be better disclosed in a supplemental table.

### B. Grants of Performance-Based Awards Table

Because the value of certain performance-based awards is not required to be disclosed in the SCT until earned, the Grants of Performance-Based Awards table would supplement the SCT by including information regarding the grant of all performance-based awards to each NEO during the last fiscal year. This column would include grants of non-equity-based awards, equity-based awards (e.g. awards of options, restricted stock and similar instruments with performance-based features) and the estimated future payout values for these awards. For purposes of this table, awards would be considered performance-based if they are subject to either a performance condition, or a market condition, as those terms are defined in FAS 123R.

#### GRANTS OF PERFORMANCE-BASED AWARDS

Name	Performance-Based Stock and Stock-based Incentive Plans: number of shares, units or other rights (#)	Performance-Based Options: number of securities underlying Options (#)	Non-Stock Incentive Plan Awards: number of units or other rights (#)	Dollar amount of consideration paid for award, if any (\$)	Grant Date for Stock or Option Awards	Performance or other period until vesting or payout and Option expiration date	Estimated Future Payouts		
							Threshold (\$ or #)	Target (\$ or #)	Maximum (\$ or #)
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)

### C. Grants of All Other Equity Awards Table

The Grants of All Other Equity Awards table would supplement the SCT by disclosing, for each NEO, certain material terms of equity-based awards granted in the last fiscal year that are not performance-based (*i.e.* where the payout or future value is tied to the company's stock price, and not to other performance criteria).

#### GRANTS OF ALL OTHER EQUITY AWARDS

Name	Number of Securities Underlying Options Granted (#)	Exercise or Base Price (\$/Sh)	Expiration Date	Number of Shares of Stock or Units Granted (#)	Vesting Date	Grant Date
(a)	(b)	(c)	(d)	(e)	(f)	(g)

#### **D. Narrative Disclosure to SCT and Supplemental Tables**

The proposed rules require additional narrative disclosure following the SCT and the related supplemental tables to give context to the tabular disclosure. The narrative description would include any additional material information necessary to an understanding of the information disclosed in the tables. This may include, among other things, disclosure of the following:

- The material terms in employment agreements with the NEOs.
- Repricing or other material modifications of any outstanding option or other stock-based awards during the last fiscal year. This disclosure would replace the current Ten-Year Option/SAR Repricings table.
- Disclosure for up to three employees who were *not* executive officers during the last fiscal year, whose *total compensation* for the last fiscal year was greater than that of any of the NEOs. Required disclosure would include the amount of each such employee's total compensation for the last fiscal year and a description of his or her job position. The individuals would not need to be named.
- The terms of performance-based awards which could include a general description of the formula or criteria to be applied in determining the amounts payable, the vesting schedule, a description of the performance-based conditions, whether dividends or other amounts would be paid, the applicable rate and whether that rate is preferential and any other material conditions applicable to the award.
- Any material waiver or modification of any specified performance target, goal or condition to payout under any reported incentive plan payout.
- Information regarding defined benefit and deferred compensation plans, such as material assumptions underlying the determination of the amount of increase in actuarial value of defined benefit or actuarial plans or the methodology for determining earnings on deferred compensation plans.

### ***III. Outstanding and Exercised Equity Awards***

#### **A. Outstanding Equity Awards at Fiscal Year-End**

The Outstanding Equity Awards at Fiscal Year-End table would require disclosure of all equity awards outstanding as of the end of the last fiscal year for each NEO where the ultimate outcome has not yet been realized. This would require disclosure of the number and value of awards such as stock options, stock appreciation rights, restricted stock, restricted stock units and other equity awards, including those subject to performance benchmarks. The disclosure would include awards that have been transferred by an executive. Disclosure of the market value of unvested restricted stock awards would replace the current footnote disclosure of the market value of restricted stock. Footnote disclosure would be required indicating the expiration dates for stock options, stock appreciation rights, and similar instruments held at fiscal year-end and the vesting dates for stock awards.



## OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

Name	Number of securities underlying unexercised Options (#) Exercisable/Unexercisable	In-the-money amount of unexercised Options (\$) Exercisable/Unexercisable	Number of shares or units of stock held that have not vested (#)	Market value of shares or units of stock held that have not vested (#)	Incentive Plans: Number of nonvested shares, units or other rights held (#)	Incentive Plans: Market or payout value of nonvested shares, units or other rights held (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)

**B. Option Exercises and Stock Vesting**

The Option Exercises and Stock Vested Table would require disclosure for each NEO of the amounts realized upon the exercise of stock options and similar equity-based compensation with option-like features and the vesting of stock and similar equity-based compensation during the last fiscal year. The table would also require disclosure of the grant date fair value for these awards, as previously reported in the SCT. This table expands upon the current disclosure requirements in the Aggregated Option/SAR Exercises in Last Fiscal Year table by adding the value of vested stock awards.

## OPTION EXERCISES AND STOCK VESTED

Name of NEO	Number of Shares acquired on exercise or vesting (#)	Value realized upon exercise or vesting (\$)	Grant date fair value previously reported in SCT (\$)
(a)	(b)	(c)	(d)
Options			
Stock			

**IV. Post-Employment Compensation**

The proposed rules would significantly revise the current rules regarding the disclosure of post-employment compensation. The current Pension Plan Table would be replaced by a new table for defined benefit plans and an additional new table would be required to disclose information regarding non-qualified defined contribution plans. In addition, new narrative disclosure would be required regarding other potential post-employment compensation arrangements, including compensation payable upon a change in control.

### A. Retirement Plan Potential Annual Payments and Benefits Table

Companies would be required to disclose an estimate of the retirement benefits payable to each of the NEOs at normal retirement age and early retirement age, if applicable, under any defined benefit plan or arrangement. This would include payments under both tax-qualified and non-qualified plans. A separate line of tabular disclosure would be required for each plan or arrangement in which a NEO participates. The value of benefits would be computed assuming that compensation remained the same as for the last fiscal year.

#### RETIREMENT PLAN POTENTIAL ANNUAL PAYMENTS AND BENEFITS

Name	Plan Name	Number of years credited service (#)	Normal retirement age (#)	Estimated normal retirement annual benefit (\$)	Early retirement age (#)	Estimated early retirement annual benefit (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)

The tabular disclosure would be followed by narrative disclosure of the material factors necessary to an understanding of each plan or arrangement disclosed. Examples of such narrative disclosure could include, among other things, the following information:

- Material terms and conditions of benefits, including the retirement benefit formula, eligibility standards, and early retirement arrangements.
- The amount of any lump sum distribution that would be available on election as of the end of the company's last fiscal year, including the valuation methodology and material assumptions applied in quantifying such amount.
- The specific elements of compensation, such as salary and various forms of bonus, included in applying the benefit formula.
- Reasons for participation in multiple plans.
- Company policies with regard to granting extra years of credited service.

### B. Nonqualified Defined Contribution and Other Deferred Compensation Plans

A new table would require, for each NEO, disclosure of contributions, earnings and distributions during the last fiscal year and balances as of the end of the last fiscal year under nonqualified defined contribution and other deferred compensation plans. Footnote disclosure to the table, acknowledging the extent to which amounts were previously reported in the SCT for the last fiscal year and prior fiscal years, would mitigate the appearance of "double counting."

**NONQUALIFIED DEFINED CONTRIBUTION  
AND OTHER DEFERRED COMPENSATION PLANS**

Name	Executive contributions in last FY (\$)	Registrant contributions in last FY (\$)	Aggregate earnings in last FY (\$)	Aggregate withdrawals/distributions (\$)	Aggregate balance at last FYE (\$)
(a)	(b)	(c)	(d)	(e)	(f)

A narrative description following the table would require disclosure of any material factors necessary to an understanding of the information provided in the table. Examples of such narrative disclosure could include, among other things, the following information:

- The type of compensation permitted to be deferred, and any limitations on the extent to which deferral is permitted.
- The measures for calculating interest and other plan earnings, quantifying interest rates and other earnings measures applicable during the company's last fiscal year.
- Material terms with respect to payouts, withdrawals and other distributions.

**C. Other Potential Post-Employment Payments**

The proposed rules would require narrative disclosure of specific aspects of any written or unwritten arrangement that provides for payments at, following, or in connection with (i) the resignation, severance, retirement or other termination (including constructive termination) of a NEO, (ii) a change in his or her responsibilities, or (iii) a change in control of the company. Unlike the current disclosure requirements, which limits disclosure to those amounts that exceed \$100,000, all such payments would need to be disclosed. The disclosure must be quantitative, even where uncertainties exist as to amounts payable, in which case the company would be required to make reasonable estimates and disclose material assumptions underlying such estimates. Narrative disclosure of the following information would be required:

- The specific circumstances that would trigger payments or other benefits under the termination or change-in-control arrangements.
- The estimated payments and benefits that would be provided in each termination circumstance, and whether they would or could be lump-sum or annual installment payments, disclosing the duration and by whom they would be provided.
- The specific factors used to determine the appropriate payment and benefit levels under the various circumstances that would trigger payments or provision of benefits.
- Any material conditions or obligations applicable to the receipt of payments or benefits such as non-compete, non-solicitation, non-disparagement or confidentiality covenants.
- Tax gross-ups.
- Any other material features necessary for an understanding of the provisions.

### Director Compensation Disclosure

The proposed rules would require, for every director, compensation to be disclosed in a Director Compensation Table (DCT) similar to the SCT. Disclosure would only be required for the last completed fiscal year. Narrative disclosure would follow the table and would describe any material factors necessary to an understanding of the DCT, including, for example, a breakdown of types of fees.

#### DIRECTOR COMPENSATION

Name	Total (\$)	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Stock Incentive Plan Compensation (\$)	All Other Compensation (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)

The “All Other Compensation” Column for directors would include the following items:

- All perquisites and other personal benefits if the total is \$10,000 or greater.
- All earnings on compensation that is deferred on a basis that is not tax-qualified.
- All tax reimbursements.
- Annual company contributions or other allocations to defined contribution plans.
- Discount stock purchases.
- Aggregate annual increase in actuarial value of all pension plans.
- All consulting fees.
- Awards under director legacy or charitable award programs.
- The dollar value of any insurance premiums paid by, or on behalf of, the company for life insurance for the director’s benefit.

Additionally, the outstanding equity awards at fiscal year end for each director would need to be disclosed in a footnote. The proposed rules would allow grouping of directors in a single row if all elements and amounts of compensation are the same for all directors. Instructions to the DCT would be the same as for the SCT.

### Form 8-K Disclosure

The SEC acknowledged in the proposed rules that the 2004 amendments to Form 8-K, which significantly expanded the number of events subject to Form 8-K reporting, have resulted in executive compensation disclosures that are much more frequent and accelerated than those included in a company’s proxy statement and that such disclosure has not always been “unquestionably or presumptively material” as was the intent for the accelerated Form 8-K

disclosure. The proposed rules would revise Items 1.01 and 5.02 of Form 8-K to limit the information required and consolidate the Form 8-K reporting of executive compensation matters into one Item. As such, a company's annual proxy statement would continue to be the primary vehicle for disclosure of executive and director compensation information, unless such information was "unquestionably or presumptively material."

Currently, Item 1.01 requires disclosure of a company's entry into a material definitive agreement (including certain executive compensation arrangements) outside of the ordinary course of the company's business and any material amendment to any such agreement. By cross reference to Item 601 of Regulation S-K, all management contracts and compensatory arrangements with a company's NEOs and directors are deemed to be material. In addition, Item 5.02 currently requires disclosure of (i) the appointment or departure of a company's principal officers and directors and (ii) a brief description of the material terms of any employment agreement between the company and any principal officer upon his or her appointment.

Form 8-K disclosure would be revised as follows:

- Disclosure of a company's entry into or material amendment of executive compensation arrangements would be shifted from Item 1.01 to Item 5.02(e), and the concept that all compensatory arrangements with NEOs are deemed material would be eliminated. This disclosure would now cover only compensation arrangements with a company's current principal executive officer, principal financial officer and NEOs for the previous fiscal year, and would be limited to a brief description of any material compensatory arrangement or material amendment thereto. As is currently the case, grants or awards (or modifications thereto) under a compensatory arrangement that are materially consistent with the previously disclosed terms of such compensatory arrangement need not be disclosed under Item 5.02(e), provided the grants or awards (or modifications) are properly disclosed in the proxy statement (or other filing as required).
- The disclosure required under Item 5.02(b), regarding retirement, resignation or termination of employments would be expanded to include *all* NEOs for the prior fiscal year.
- The disclosure required under Items 5.02(c) and (d) upon the appointment of a new principal officer or director would be expanded beyond just employment agreements to include a brief description of any other material plan, contract or arrangement with such principal officer or director that is entered into or materially amended, and any grant or award under any such arrangement in connection with such appointment.
- Where the salary or bonus of any NEO cannot be calculated in time to be included in the SCT, disclosure of such information will be required on Form 8-K when the amounts become calculable.
- The safe harbor for failure to make a timely 8-K filing from liability under Section 10(b) of the Exchange Act and for Form S-3 eligibility that currently exists for Item 1.01 would be extended to Item 5.02(e), provided the information is included in the required periodic report for the period during which the applicable event occurred.

### **Beneficial Ownership Disclosure**

The proposed rules would require disclosure in a footnote to the beneficial ownership table of the number of shares pledged by each NEO, director and director nominee as collateral for a loan from the company. The proposed rules would also require disclosure of the beneficial ownership of directors' qualifying shares.

### **Related-Party Transaction Disclosure**

The proposed rules would significantly revise and reorganize the disclosure of related-party transactions under Item 404 or Regulation S-K as follows:

- Item 404(a) would contain the general disclosure requirement for related-party transactions, including those involving indebtedness (previously in Item 404(c)).
- Item 404(b) would require disclosure of a company's policies and procedures for the review, approval or ratification of related-party transactions.
- Item 404(c) would require disclosure regarding promoters of a company.

Proposed Item 404(a) would combine current Items 404(a) and (c) and would require disclosure of any transaction since the beginning of the company's last fiscal year or any currently proposed transaction in which the company was or is a *participant* if the amount involved exceeds \$120,000 and in which any related person had, or will have, a direct or indirect material interest. The \$120,000 threshold is an increase over the current \$60,000 threshold. The proposal would eliminate certain bright line disclosure requirements and instead would impose a principles-based materiality analysis for disclosure. The proposal would also add an instruction that a person is not deemed to have an indirect "material" interest within the meaning of Item 404(a) if that interest arises only from the person's position as a director of a related party or if the person's direct or indirect interest is less than a 10% equity interest in the related party.

Item 404(b), which currently requires disclosure of certain business relationships, would be amended to require a description of the policies and procedures established by the company and its board of directors for the review, approval or ratification of any related party transaction required to be reported in Item 404(a). This disclosure may include, among other things, the following:

- The types of transactions covered by such policies.
- The standards to be applied pursuant to such policies and procedures.
- The persons or groups of persons on the board of directors responsible for applying such policies and procedures.
- A statement of whether such policies and procedures are in writing and, if not, how such policies and procedures are evidenced.

In addition, companies would be required to identify any transaction required to be reported pursuant to Item 404(a) where such policies and procedures did not require review, approval or ratification or where such policies and procedures were not followed.

Proposed Item 404(c) would require registrants filing a registration statement on Form S-1 or Form 10 to identify any promoter during the past five fiscal years and indicate the nature and amount of anything of value received by each promoter from the registrant and the nature and amount of any assets, services or other consideration received by the registrant.

### **Corporate Governance**

The proposed rules would create a new Item 407 of Regulation S-K, which would consolidate and expand upon existing disclosure requirements regarding director independence and corporate governance. Specifically, proposed Item 407 would consolidate the disclosure of (i) director independence, (ii) information relating to the number of board meetings and attendance thereof and (iii) information relating to the composition, policies and procedures of the nominating, audit and compensation committees. Among the significant new disclosure requirements are the following:

- Director Independence. The proposed rules would require the identification of each director, or director nominee, as appropriate, who is independent under the independence standards applicable to the company and each non-independent director who is a member of the compensation, nominating or audit committee. In addition, companies would be required to disclose relationships or arrangements not otherwise disclosed pursuant to Item 404(a) that were considered when determining the independent status of a director or director nominee.
- Compensation Committee. The proposed rules would require disclosure about the compensation committee similar to that currently required with respect to the nominating and audit committees. Specifically, the proposed rules would require disclosure of the identity of each committee member, whether the committee has a charter and a narrative description of the processes and procedures for consideration and determination of executive and director compensation, including (i) the scope of authority of the committee, (ii) the committee's ability to delegate that authority, (iii) the name and role of any compensation consultant who advised the committee with respect to executive and director compensation decisions, including whether such consultant was engaged by the committee or another person, (iv) any contact between the consultant and any executive officer and (v) the role any executive officer played in determining or recommending the amount or form of executive or director compensation.

### **Plain English Rule**

Finally, the proposed rules would require companies to prepare their executive and director compensation, related person transactions, beneficial ownership and corporate governance disclosures using plain English principles, including the following standards:

- Use clear and concise sections, paragraphs and sentences.
- Use definite, concrete everyday words.
- Use the active voice.
- Avoid multiple negatives.
- Use a tabular presentation or bullet lists for complex material, wherever possible.
- Avoid legal jargon and highly technical business and other terminology.
- Avoid vague “boilerplate” explanations that are imprecise and readily subject to different interpretations.

\* \* \* \* \*

The foregoing is a summary of the principal provisions of the proposed rules. If you wish to obtain additional information regarding the proposed rules, please contact Frank A. Daniele (212-728-8216, [fdaniele@willkie.com](mailto:fdaniele@willkie.com)), Stephen T. Lindo, (212-728-8242, [slindo@willkie.com](mailto:slindo@willkie.com)), J. Pasco Struhs (212-728-8109, [pstruhs@willkie.com](mailto:pstruhs@willkie.com)), Lauren Charme Fishkoff (212-728-8954, [lfishkoff@willkie.com](mailto:lfishkoff@willkie.com)) or the partner who regularly works with you.

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