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Securities Alert

SEC Proposes Compensation Committee and Consultant Independence Rules

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On March 30, 2011, the Securities and Exchange Commission issued proposed rules to implement the provisions of Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The proposed rules would direct the national securities exchanges to adopt new listing standards related to compensation committees and compensation advisers and would require new disclosure concerning the use of compensation advisers and conflicts of interest. A complete copy of the proposing release (Release No. 33-9199) is available at www.sec.gov/rules/proposed/2011/33-9199.pdf.

New Listing Standards Related to Compensation Committees and Compensation Advisers

The proposed rules would direct the national securities exchanges to adopt new independence and other listing standards for listed companies that have a committee of the board of directors that oversees executive compensation. Under the new listing standards, each member of the compensation committee must be a member of the board of directors and must be independent, as determined by new independence standards to be developed by the exchanges. In developing a definition of independence, the exchanges would be required to consider all relevant factors, including the sources of compensation paid to a director (such as any consulting, advisory or other compensatory fees) and whether the director is affiliated with the company or its subsidiaries or affiliates.

The new listing standards also would require that a listed company's compensation committee be given the authority and funding to retain outside compensation advisers (including compensation consultants, independent legal counsel and other advisors) and be directly responsible for the appointment, compensation and oversight of such advisers. Compensation committees would not be required to select advisers that are independent. However, when selecting outside advisers, the compensation committee must consider certain independence factors, including whether the adviser is providing any other services to the company, the amount of fees received by the adviser from the company and the policies and procedures adopted by the adviser to prevent conflicts of interest. The compensation committee also must consider whether the adviser has any business or personal relationship with members of the compensation committee and whether the adviser owns any shares of the company.

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New Disclosure Rules Concerning Compensation Consultants and Conflicts of Interest

The proposed rules also would require all registrants to include proxy disclosure indicating whether their compensation committee retained or obtained the advice of a compensation consultant and whether the work of the consultant raised any conflict of interest and, if so, the nature of the conflict and how it is being addressed. While current proxy disclosure rules require disclosure only if a compensation consultant is involved "in determining or recommending the amount or form of executive or director compensation," the proposed rules would require disclosure if a compensation committee "retained or obtained the advice of a compensation consultant" (regardless of whether there was a formal engagement of, or any payment of fees to, the consultant for its advice). The proposed rules also would eliminate the current disclosure exemption for services that are limited to consulting on broad-based, non-discriminatory plans and the provision of non-customized benchmark data, but would retain the current fee disclosure requirements and the exemptions from those requirements.

Timing and Applicability of the New Rules

All comments on the proposed rules must be received by April 29, 2011. Pursuant to Section 952 of the Dodd-Frank Act, the SEC must adopt final rules by July 16, 2011. The proposed rules would require that the national securities exchanges obtain final SEC approval of their new listing standards within one year of the date on which the final rules are published in the Federal Register. At this time, it is unclear whether the new independence requirements will be in place for the 2012 proxy season.

Under the proposed rules, the national securities exchanges would be permitted, subject to SEC review, to exempt smaller reporting companies from the compensation committee listing requirements.
