



**SEC Adopts New Rules on Listing Standards for
Compensation Committees and Compensation Advisers**

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On Wednesday, June 20, 2012, the Securities and Exchange Commission adopted a new rule directing national securities exchanges and associations that list equity securities (collectively, “exchanges”) to adopt listing standards concerning compensation committees of public company boards of directors and the compensation advisers that those committees retain. The SEC also adopted certain related amendments to its proxy disclosure rules.

The rule and the amendments were adopted pursuant to Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”), which requires the SEC to direct the exchanges to adopt certain listing standards relating to:

- the independence of the members of compensation committees,
- the committee’s authority to retain compensation advisers, and
- the committee’s responsibility for the appointment, compensation and work of any compensation adviser.

Additionally, Section 952 requires every public company to disclose in its proxy materials for annual meetings of shareholders whether its board’s compensation committee retained or obtained the advice of a compensation consultant. The provision also requires a company to disclose whether the work of the compensation consultant has raised any conflict of interest and, if so, the nature of the conflict and how the conflict is being addressed.

The New Listing Standards

Independence of Compensation Committee Members

New Rule 10C-1 under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), requires the exchanges to adopt listing standards that require each member of a company’s compensation committee to be a member of the board of directors and to be “independent.” Rule 10C-1 does not define independence. Instead, each exchange is required to develop a definition applicable to compensation committee members after considering relevant factors, including, but not limited to:

- The source of compensation of a member of the board of directors, including any consulting, advisory or other compensatory fee paid by the issuer to such director; and

- Whether the board member is affiliated with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer.

Authority and Funding of the Compensation Committee

Rule 10C-1 also requires the exchanges to adopt listing standards providing that:

- The compensation committee of a listed company may, in its sole discretion, retain or obtain the advice of a compensation adviser (defined to include compensation consultants, independent legal counsel and other advisers);
- The compensation committee will be directly responsible for the appointment, compensation and oversight of the work of any compensation advisers; and
- The listed company must appropriately fund the payment of reasonable compensation to the compensation adviser, as determined by the compensation committee.

Compensation Adviser Selection

Rule 10C-1 also requires the exchanges to adopt listing standards providing that a compensation committee may select a compensation adviser only after considering the following six independence factors:

- Whether the person that employs the compensation adviser is providing any other services to the issuer;
- The amount of fees received from the issuer by the person who employs the compensation adviser, as a percentage of that person's total revenue;
- What policies and procedures have been adopted by the person that employs the compensation adviser to prevent conflicts of interest;
- Whether the compensation adviser has any business or personal relationship with a member of the compensation committee;
- Whether the compensation adviser owns any stock of the company; and
- Whether the compensation adviser or the person employing the adviser has any business or personal relationship with an executive officer of the issuer.

The rule notes that the exchanges may impose their own factors, in addition to the six required above.

Applicability

The rule clarifies that the new listing standards must apply to any committee of the board that performs functions typically performed by a compensation committee, whether or not the committee is also charged with other functions or is formally designated as a compensation committee. The listing standards concerning director independence, consideration of any compensation adviser's independence and responsibility for appointment, compensation and oversight of compensation advisers must also apply to board members who oversee executive compensation matters on behalf of the board in the absence of a formal committee.

Exemptions and Opportunities to Cure

The following four categories of companies are exempt from the compensation committee independence requirements of rule 10C-1:

- Limited partnerships;
- Companies in bankruptcy proceedings;
- Open-end management investment companies registered under the Investment Company Act of 1940; and
- Any foreign private issuer that discloses in its annual report the reasons that the foreign private issuer does not have an independent compensation committee.

In addition, controlled companies and smaller reporting companies are exempt from all of the requirements of the new compensation committee listing standards.

Rule 10C-1 also authorizes the exchanges to exempt a particular relationship from the independence requirements applicable to compensation committee members and authorizes the exchanges to exempt other categories of issuers. As with all listing standards, the exchanges would need to seek the approval of the SEC before adopting any additional exemptions.

Rule 10C-1 also requires the exchanges to provide issuers with a reasonable opportunity to cure any noncompliance with the new listing requirements. The rule also allows exchanges to provide that if a compensation committee member ceases to be independent for reasons outside the member's reasonable control, that person may, with notice to the exchange, remain a member of the compensation committee until the earlier of the next annual

shareholders' meeting of the company or one year from the event causing the member to no longer be independent.

New Proxy Disclosures

Item 407(e)(3) of Regulation S-K currently requires issuers subject to the federal proxy rules to disclose in proxy statements information about their use of compensation consultants, including specific information about fees paid to consultants. Those requirements will remain in effect as they currently exist. Under newly adopted Item 407(e)(3)(iv) of Regulation S-K, if the work of any compensation consultant that has played a role in determining or recommending the amount or form of executive and director compensation has raised any conflict of interest, issuers will now also be required to disclose the nature of the conflict and how the conflict is being addressed. An instruction to the new rule states that the six factors listed in Rule 10C-1(b)(4) (noted above under "Compensation Adviser Selection") should be considered in determining whether a conflict of interest exists.

As with the existing disclosure requirements regarding compensation consultants, the new disclosures will be required in any proxy or information statement for an annual meeting (or special meeting in lieu of an annual meeting) at which directors are to be elected and will not apply to consultants advising only on broad-based plans or providing non-customized benchmark data.

Effectiveness

The new rule and rule amendments will take effect 30 days after publication in the Federal Register. Each exchange that lists equity securities must propose listing standards that comply with the new rule no later than 90 days after effectiveness and the SEC must approve the new listing standards within one year after effectiveness.

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