

Corporate and Securities

August 2006

The SEC's New Executive Compensation Rules: Highlights of the New Rules

Background

On August 11, 2006, the Securities and Exchange Commission ("SEC") adopted final rules that substantially revamp the disclosure requirements for public companies with respect to executive and director compensation, related-party transactions, director independence and other corporate governance matters, and security ownership of officers and directors under the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act"). The SEC had issued proposed rules in February 2006 (the "Proposed Rules") to address a disclosure scheme that was last substantially revised in 1992. The release (Rel. No. 33-8732; 34-54302; IC-27444) setting forth the final rules is available on the SEC's website at: <http://www.sec.gov/rules/final/2006/33-8732.pdf>.

This Client Memorandum summarizes the effects of the new rules on domestic public companies that do not qualify for the SEC's small business reporting scheme and highlights some of the major differences between the final rules adopted by the SEC and the Proposed Rules. The new rules generally require less detailed disclosure by small business issuers.

This Client Memorandum will be followed in the coming weeks by additional Client Memoranda that will each focus on a specific aspect of the new rules in greater detail.

Executive Overview

The primary focus of the final rule changes is improved and expanded disclosure of executive and director compensation. Key elements of the new rules affecting compensation disclosure include:

- requiring a Compensation Discussion and Analysis section in proxy statements or Form 10-Ks that would address the material factors underlying compensation policies and the decisions underlying the information disclosed in the compensation tables, including a company's option grant policies;

- expanding the scope and detail of the existing executive compensation disclosure tables and supplementing the tabular disclosure with narrative explanation;
- reorganizing executive compensation disclosure into three categories focusing on: current compensation, holdings of equity-related interests and retirement and other post-termination benefits;
- requiring disclosure of an annual "all-in" compensation number that includes the current value of every form of compensation paid during or with respect to the year;
- requiring that CFOs be included in the "named executive officers" whose compensation is disclosed, regardless of the level of their compensation;
- requiring that director compensation be disclosed in a table that would include every form of compensation paid to directors, including perquisites; and
- requiring that disclosure regarding executive and director compensation be drafted in "plain English".

In addition to changes in the executive and director compensation rules, the new rules also:

- modify the Form 8-K filing requirements with respect to material contracts related to director and officer compensation;
- realign and somewhat expand required disclosure with respect to related-party transactions;
- consolidate and expand required disclosure with respect to director independence and other corporate governance matters; and
- refine the disclosure requirements regarding beneficial ownership of issuer securities.

Executive Compensation

The Commission's final rules retain the tabular approach to compensation disclosure in Item 402 of Regulation S-K and reiterate the requirement that all elements of compensation must be included in the tables. The final rules also require disclosure of a single figure for total compensation and a new Compensation Discussion and Analysis, or CD&A, section that consists of a general discussion and analysis of compensation and specific material information regarding tabular items where necessary to an understanding of the tabular disclosure.

Compensation Discussion and Analysis

The new CD&A section is intended to be an overview that provides context for a company's compensation disclosure. This section will explain material elements of compensation for named executive officers, including the objectives of the company's compensation program, what the compensation program is designed to reward, each element of compensation, why the company chooses to pay each element, how the company determines the amount for each element and how 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 SEC believes that the disclosure in the CD&A regarding corporate performance policies will spur a broader discussion than the boilerplate typically included in the former version of the Compensation Committee Report.

The CD&A, which effectively replaces the Compensation Committee Report in its current form, is intended to provide investors with perspective regarding the numbers and narrative that follow it. The scope of the CD&A is designed to be comprehensive, requiring a discussion of both in-service and post-termination compensation arrangements. The SEC does not want this disclosure to be boilerplate. Forward-looking information in the CD&A falls within the existing safe harbor for forward-looking disclosure.

The new rules include a non-exclusive list of matters potentially appropriate for a company to address in the CD&A. This list largely tracks the list included in the Proposed Rules, with two additions:

- policies and decisions regarding the adjustment or recovery of awards or payments if the relevant performance measures upon which they are based are restated or otherwise adjusted in a way that would have reduced the size of the awards or payments; and

- the basis for selecting particular triggering events in post-termination agreements (*e.g.*, the rationale for using a single trigger in the event of a change of control).

In spite of a number of comments objecting to the Proposed Rules' treatment of the CD&A as soliciting material that is considered part of the proxy statement and any other filing in which it is included or incorporated by reference, the SEC retained this approach in the final rules. Since the CD&A will be deemed filed with the SEC, it will be subject to Regulations 14A and 14C and to the liabilities of Section 18 of the Exchange Act. The CD&A also will be covered by the certifications that principal executive officers and principal financial officers are required to give under the Sarbanes-Oxley Act of 2002 to the extent that the disclosure and any other disclosure related to executive officer and director compensation of other matters is included or incorporated by reference into a periodic report.

In light of the amount of public attention that has recently been focused on option grant practices, particularly "backdating" and "spring loading", the SEC's adopting release makes it clear that companies must address matters relating to executives' option compensation in CD&A, particularly as they relate to the timing and pricing of stock option grants. For example, if a company has a program, plan or practice to select the option grant dates for executive offices in coordination with the release of material non-public information, the company should disclose that fact in the CD&A. In addition, companies should also discuss any program, plan or practice of awarding options and setting the exercise price based on the stock's price on a date other than the actual grant date, including the use of an average price to set the exercise price.

Compensation Committee Report and Performance Graph

The Proposed Rules would have eliminated the Compensation Committee Report and the performance graph. In the final rules, however, the SEC decided to retain a Compensation Committee Report requirement and the Performance Graph. The Compensation Committee Report under the new rules will, however, differ dramatically from the report previously required. In its new format, the Compensation Committee Report will simply consist of a statement over the names of the members of the compensation committee of whether:

- the compensation committee has reviewed and discussed the CD&A with management; and

- based on the review and discussions, the compensation committee recommended to the board of directors that the CD&A be included in the company's Annual Report on Form 10-K and, as applicable, the company's proxy or information statement.

The Compensation Committee Report must be included or incorporated in the Annual Report on Form 10-K, but will be considered "furnished" rather than "filed". The SEC noted in the adopting release that the CEO and CFO will be able to look to the Compensation Committee Report in providing their certifications of the company's Annual Report on Form 10-K.

The performance graph will be retained in substantially the same form as currently required. Instead of appearing in the proxy statement, however, the performance graph will now appear in the annual report to security holders that accompanies or precedes the proxy or information statement relating to an annual meeting of shareholders.

Compensation Tables

The final revisions to Item 402 of Regulation S-K include a reorganization of the compensation tables and their related narrative disclosure into three general categories:

- compensation with respect to the last fiscal year and the two preceding fiscal years, as reflected in a revised Summary Compensation Table;
- holdings of equity-based interests that relate to compensation or are potential sources of future compensation, focusing on compensation-related equity-based interests that were awarded in prior years and are "at risk", as well as recent realization on these interests, including through vesting of restricted stock or the exercise of options and similar instruments; and
- retirement and other post-employment compensation, including retirement and deferred compensation plans, other retirement benefits and other post-employment benefits, such as those payable in the event of a change of control of the company.

Current Compensation

Summary Compensation Table. This table will continue to be the principal form of disclosure regarding executive compensation. The revised table will include the named executive officers' compensation for each of

the last three years, whether or not actually paid out. *See Appendix Table 1.* The new rules also require that all compensation, including equity grants, be disclosed in dollars.

The SEC adopted the changes to the Summary Compensation Table substantially as proposed, including basing the reported value of equity compensation awards on the grant date fair value of the award determined according to Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123, "Share-Based Payment" (FAS 123R), for financial reporting purposes.

In a change from the Proposed Rules, the final rules eliminated the proposed requirement for a footnote to the applicable columns identifying the amount of each that was deferred. The final rules also added a column to the Summary Compensation Table for the annual change in actuarial value of defined benefit plans and above-market or preferential earnings on nonqualified deferred compensation plans, which would have been included in the All Other Compensation Column under the Proposed Rules. This change also eliminated the proposed requirement to report in the Summary Compensation Table the full amount of earnings on nonqualified deferred compensation by limiting the amount in the new column to above market or preferential earnings.

The Proposed Rules would have required companies to include in the Summary Compensation Table the full fair value of any equity award that was repriced or materially modified during the year. In response to comments, the SEC will now only require that the incremental increase in fair value that results from the repricing or modification be reported in the table.

Grants of Plan-Based Awards Table. The Proposed Rules would have required two supplemental tables to follow the Summary Compensation Table. In the final rules, the SEC combined these into a single new table and eliminated some of the proposed columns in order to simplify the presentation. The Grants of Plan-Based Awards Table will include information regarding both equity and non-equity incentive plan awards, all other stock awards and all other option awards. *See Appendix Table 2.* If the exercise price of a stock option included in the table is less than the closing market price of the underlying security on the date of grant, a separate, adjoining column must be added to the table to disclose that market price on the date of grant. In addition, if the grant date is different than the date on which the compensation committee or the full board of directors

approved the grant, a separate, adjoining column must be added to the table to show the date of approval.

Narrative Disclosure to Tables. The SEC's final revisions to Item 402 will require narrative disclosure to supplement the Summary Compensation Table and the Grants of Plan-Based Awards Table. The narrative will describe any additional material factors necessary to an understanding of the information disclosed in the tables. Unlike the CD&A described above, which focuses on broad topics regarding the objectives and implementation of executive compensation policies, this narrative disclosure focuses on and provides context to the quantitative disclosures in the tables. Material factors will vary for each company, but may include, among other factors, descriptions of the material terms in the named executive officers' employment agreements, whether written or unwritten. In the adopting release, the SEC also suggested that the narrative disclosure might include an explanation of the level of salary and bonus in proportion to total compensation.

The SEC did not adopt the proposal to require narrative disclosure of compensation information with respect to up to three additional employees who were not executive officers during the year and whose total compensation was greater than that of any of the named executive officers. Instead, the SEC has solicited additional comment on a modified version of the proposal that would only require narrative disclosure with respect to three additional employees who meet the income test and are responsible for significant policy decisions at the company or a significant subsidiary or principal business unit, division or function of the company.

Exercises and Holdings of Previously Awarded Equity

This section will disclose information regarding equity compensation that has previously been awarded and remains outstanding (*i.e.*, unexercised or unvested equity). This section also will disclose amounts realized on this type of compensation during the most recent fiscal year when, for example, a named executive officer exercises an option or his or her stock award vests. The tables in this section replace the currently required Aggregated Option/SAR Exercises in the Last Fiscal Year and Fiscal Year-End Option/SAR Values tables.

Outstanding Equity Awards at Fiscal Year-End Table. This table discloses outstanding awards under stock option plans, restricted stock plans, equity incentive

plans and similar plans, as well as the market-based values of the options, rights, shares or units, as applicable, as of the company's most recent fiscal year end. In the adopting release, the SEC modified the columns applicable to unexercised options, stock appreciation rights and similar instruments with option like features to require disclosure of the numbers of exercisable and unexercisable securities underlying unexercised instruments, the exercise or base price and the expiration date. The table also includes a column disclosing the number of securities underlying unexercised unearned options awarded under equity incentive plans. *See Appendix Table 3.*

Option Exercises and Stock Vested Table. This table reflects the amounts received upon exercise of options or similar instruments or the vesting of stock or similar instruments during the most recent fiscal year. This table is similar to the current Aggregate Options/SAR Exercises in Last Fiscal Year and Fiscal Year-End Options/SAR Values table, except that this table also covers the vesting of restricted stock and similar instruments. *See Appendix Table 4.* The final rules eliminate the proposed requirement to repeat in this table the grant date fair market value of these instruments, which in practice will already have been disclosed in the Summary Compensation Table for the year in which they were awarded.

Post-Employment Compensation

The final rules significantly change the disclosure regarding post-employment compensation. The current pension plan table, alternative plan disclosure and some of the other narrative descriptions have been replaced with a table regarding defined benefit pension plans along with enhanced narrative disclosure. A second new table and narrative disclosure will disclose information regarding nonqualified defined contribution plans and other deferred compensation. The final rules also include revised requirements regarding disclosure of compensation arrangements that are triggered upon termination of an executive officer and upon changes in control of a company.

Pension Benefits Table. In a significant departure from the Proposed Rules, the final rules adopted by the SEC will require disclosure in this table of the present value of the current accrued benefit under each pension plan covering a named executive officer computed as of the end of the company's last completed fiscal year. The table will also include the number of years of service credited to each named executive officer under each plan and any payments received by the named executive

officers under each plan during the last completed fiscal year. See *Appendix Table 5*. Following the table, a required narrative will include a description of material factors necessary to an understanding of each plan disclosed in the table.

Nonqualified Deferred Compensation Table. This new table, which was renamed in the adopting release, will disclose contributions, earnings, withdrawals or distributions, and balances under nonqualified deferred compensation plans. See *Appendix Table 6*. The earnings reported in this table, unlike the Summary Compensation Table, will include all earnings rather than being limited to above market or preferential earnings. The table will be followed by a narrative description of material factors necessary to an understanding of the disclosure in the table.

Termination or Change in Control Provisions. The final rules include key changes to current requirements regarding descriptions of termination or change in control provisions. Disclosure will be required regarding specific aspects of any written or unwritten arrangement that provides for payments at, following, or in connection with the resignation, severance, retirement or other termination (including constructive termination) of a named executive officer, a change in his or her responsibilities or a change in control of the company.

A company will be required to provide quantitative disclosure of post-termination benefits even where uncertainties exist as to amounts payable under these plans and arrangements. If uncertainties exist regarding the provision of payments or benefits or the amounts involved, the company would be required to make reasonable estimates and disclose material assumptions underlying those estimates in its disclosure. In the final rules, the SEC added an instruction that requires companies to calculate the post-termination benefits disclosed based on the following two assumptions:

- the triggering event took place on the last business day of the company's last completed fiscal year; and
- the price per share of the company's securities is the closing market price as of that date.

Officers Covered

The named executive officers for purposes of Item 402 disclosure will consist of the principal executive officer, the principal financial officer and the other three most highly compensated executive officers. There is no change to the current requirement to also include up to

two additional individuals for whom disclosure would have been required but for the fact that they were no longer serving as executive officers as of the end of the last completed fiscal year. As is currently the case with principal executive officers, disclosure regarding a principal financial officer will be required even if he or she was no longer serving in that capacity at the end of the last completed fiscal year.

The Commission's proposed rules would have determined the most highly compensated executive officers based on total compensation for the most recent fiscal year, rather than focusing only on salary and bonus as under the current rules. The final rules keep the broader approach, but exclude from the calculation the increase in pension value and nonqualified deferred compensation above-market or preferential earnings. As proposed, the final rules also change the dollar threshold for disclosure of named executive officers other than the principal executive officer and the principal financial officer to \$100,000 of relevant total compensation for the last fiscal year.

Interplay of Items 402 and 404 of Regulation S-K

The new rules require disclosure of all transactions between the company and a third party if the primary purpose of the transaction is to provide compensation to a named executive officer under Item 402. The proposals also eliminate a current provision that permits the exclusion of these types of transactions from Item 402 if they are disclosed in Item 404 and require disclosure of these types of transactions under Item 402 in all cases.

Other Changes

Currently, a company may omit disclosure information about group life, health, hospitalization, medical reimbursement or relocation plans that do not discriminate in scope, terms or operation, in favor of executive officers or directors of the company and that are available to all salaried employees. The new rules delete relocation plans from this exclusion. The new rules also change the definition of "plan" so that it is more principles-based.

Director Compensation

The Commission's final rules revise Item 402 of Regulation S-K, as proposed, to require tabular disclosure for all director compensation along with narrative disclosure of additional material information. The Director Compensation table is similar to the

proposed Summary Compensation Table, but presents information only for the company's last completed fiscal year. The table includes columns for fees paid or earned in cash, stock awards, option awards, non-stock incentive plan compensation, change in pension value and nonqualified deferred compensation earnings, all other compensation and total compensation. *See Appendix Table 7.*

In a simplification of the Proposed Rules, the final rules require footnote disclosure only of the aggregate numbers of stock awards and option awards outstanding at year end. The required narrative disclosure that will follow the table will describe any material factors necessary to an understanding of the table, such as a breakdown of types of retainer, meeting and other fees, as well as any option grant practices applicable to directors. The final rules do not provide for supplementary tables regarding director compensation.

Form 8-K Revisions

To address confusion as to what types of executive and director compensation plans and agreements must be disclosed as material contracts pursuant to Item 1.01 of Form 8-K, the SEC has adopted revisions to Items 1.01 and 5.02 of Form 8-K. These revisions clarify what types of executive and director compensation arrangements must be disclosed in "real time" pursuant to Form 8-K. The final rules substantially track the Proposed Rules.

Item 1.01 of Form 8-K has been revised to eliminate employment compensation arrangements from the definition of material contracts covered by Item 1.01. The SEC also has amended the instructions to Form 8-K to provide that in a Form 8-K where Item 1.01 and at least one other Item are applicable it will not be necessary to include the number and caption of Item 1.01, so long as the information required by Item 1.01 is provided under the number and caption of the other applicable Item(s).

Item 5.02 has been revised to expand the list of persons covered, expand the disclosures required and add two new triggering events.

Persons Covered. Item 5.02 currently requires the filing of a Form 8-K upon the appointment or departure of a principal executive officer, principal financial officer, principal accounting officer, principal operating officer or any person performing a similar function ("principal officers") or of a director. The proposed rules would extend required Item 5.02 disclosure to the retirement,

resignation or termination of "named executive officers". In the adopting release, the SEC added an instruction that clarifies that for purposes of Item 5.02 the named executive officers are the persons for whom disclosure was required in the most recent SEC filing that required Summary Compensation table disclosure.

Disclosure Required. The final rules expand Item 5.02 to require the disclosure in any Item 5.02 Form 8-K triggered by the appointment of a principal officer or the election of a director of:

- any material plan, contract or arrangement to which a principal officer, named executive officer or director is a party or in which he or she participates that is entered into or materially amended in connection with the Item 5.02 triggering event; and
- any material grant or award to any principal officer, named executive officer or director, or modification thereto, under any such plan, contract or arrangement in connection with the Item 5.02 triggering event.

The new rules include an instruction to Item 5.02 to make it clear that a company would not be required to provide information with respect to plans, contracts and arrangements to the extent that they do not discriminate in scope, terms or operation in favor of executive officers or directors of the company and are available generally to all salaried employees. The adopting release notes that it is sufficient to provide a brief description of the matters specified in Item 5.02, rather than one that complies with Item 402 of Regulation S-K.

Triggering Events. The final rules add two new triggering events that require the filing of a Form 8-K pursuant to Item 5.02(e). First, an Item 5.02 Form 8-K is required if a company enters into, adopts or otherwise commences, or materially modifies or amends, a material compensatory plan, contract or arrangement, whether written or unwritten, with the company's principal executive officer or principal financial officer or a named executive officer. An Item 5.02 Form 8-K also is triggered by a material grant or award (or modification thereof) under a plan, contract or arrangement, unless: (i) the grant or award (or modification thereof) is consistent with the original terms of the plan, contract or arrangement, and (ii) the grant or award (or modification thereof) is disclosed when Item 402 of Regulation S-K so requires.

The SEC recognized in the proposed revisions to Item 402 of Regulation S-K that, in some cases, a company will not have determined the salary or bonus of a named

executive officer when disclosure of those amounts is required by Item 402. Accordingly, the new rules allow a company to note in its Item 402 disclosure that these amounts have not yet been determined. When there is a payment, grant, award, decision or other occurrence that results in the undisclosed amounts being determinable in whole or in part, an Item 5.02 Form 8-K would be filed to disclose the amounts.

As proposed, the final rules extend the safe harbor relating to liability under Section 10(b) and Rule 10b-5 of the Exchange Act and Form S-3 eligibility requirements to cover any late filing of Form 8-K required by Item 5.02(e) of Form 8-K.

Beneficial Ownership

The new rules add two additional disclosure items with respect to beneficial ownership of issuer securities. First, if any shares beneficially owned by a director, director nominee or named executive officer have been pledged, the number of shares pledged must be disclosed in a footnote to the beneficial ownership table. Second, any directors' qualifying shares must be included in the beneficial ownership disclosure.

Certain Relationships and Related Transactions Disclosure

The SEC has adopted significant revisions to the related-party transaction disclosure requirements. These revisions to Item 404 of Regulation S-K take a more principles-based approach and move away from the bright-line materiality tests of the current requirements. The proposed revisions increase the threshold for disclosure from \$60,000 to \$120,000 and eliminate the distinction between indebtedness and other types of related-party transactions. Companies also must disclose their policies and procedures for the review, approval and ratification of reportable related-party transactions.

Related-Party Transaction Disclosure Requirements. As adopted, Item 404(a) sets forth a broad principle for disclosure, requiring a company to describe any transaction (or series of similar transactions) since the beginning of its last fiscal year and any currently proposed transaction in which it was or is to be a participant where the amount involved exceeds \$120,000 and in which any related person had or will have a direct or indirect material interest. As is currently the case, materiality is determined based on the significance of the information to investors in light of all the circumstances and the significance of the interest to the person having

the interest. The relationship of the related persons to the transaction and each other, as well as the amount involved, are among the factors considered in assessing materiality. The adopting release clarifies that the \$120,000 threshold is not a bright-line materiality standard. Rather, transactions above the threshold trigger a materiality analysis to determine if the related person has a direct or indirect material interest.

Where disclosure is required under the new rules, the company must describe:

- the related person's relationship to the company;
- the person's interest in the transaction, including that person's position or relationship with, or ownership in, a firm, corporation or other entity that is a party to or has an interest in the transaction;
- the dollar value of the amount involved in the transaction and of the related person's interest in the transaction; and
- any other information about the transaction or the related person that is material to investors in light of the particular transaction.

Certain types of transactions are specifically excluded from the new disclosure requirements. Under the final rules, related-party disclosure is not required for executive officer or director compensation if it is disclosed under Item 402 of Regulation S-K. In addition, compensation to an executive officer who is not a "named executive officer" for purposes of Item 402 need not be disclosed if:

- he or she is not an immediate family member of a related person;
- the compensation would have been disclosed under Item 402 if he or she were a named executive officer; and
- the compensation committee (or independent directors performing a similar function) approved, or recommended that the board of directors approve, the compensation.

As a result, a company would need to disclose compensation in excess of \$120,000 paid to a non-named executive officer as a related-party transaction unless the compensation committee or another independent board committee approved, or recommended that the full board of directors approve, the material terms of that officer's compensation. Similarly, a company would need to disclose any compensation in excess of \$120,000 paid to an immediate family member of a related person.

In moving to a more principles-based approach, the final rules eliminate the bright-line disclosure standards for certain business relationships of directors and director nominees currently set forth in Item 404(b), thereby subjecting those relationships to the \$120,000 test of revised Item 404(a). This could result in the disclosure of relationships under Item 404(a) that under current rules would not have to be disclosed based on SEC Staff guidance that if disclosure under Item 404(b) is not required, then disclosure under Item 404(a) is not required. While the increased dollar threshold mitigates the potential impact, this change is significant since a director would not qualify as a “non-employee director” under Rule 16b-3 if he or she were involved in a reportable related-party transaction.

Approval of Related-Party Transactions. As proposed, the revised version of Item 404(b) requires a description of the material features of a company’s policies and procedures for the review, approval or ratification of related-party transactions reportable under Item 404(a). The material features may include the types of transactions covered, the standards to be applied and the persons responsible for applying the policies and procedures. Disclosure is also required regarding transactions disclosed under Item 404(a) that did not require review, approval or ratification under the company’s policies and procedures, or as to which the policies and procedures were not followed.

Corporate Governance

The final rules consolidate and slightly expand current disclosure requirements regarding director independence and corporate governance matters substantially as proposed. This disclosure is contained in new Item 407 of Regulation S-K.

Director Independence. New Item 407 requires companies to identify independent directors and director nominees, as well as any non-independent members of the audit, compensation and nominating committees. Independence determinations would be based on the independence requirements contained in the NYSE or Nasdaq listing standards, as applicable.

A company is required to disclose whether the definitions of independence applicable to its board and committee members are posted on its web site or, alternatively, to include the definitions as an appendix to its proxy statement at least once every three years. For each director serving during any part of the year and each director nominee who is identified as independent, the final rules require a description by specific type or

category of any related-party transaction not reportable under Item 404(a) that was considered by the board in determining that the independence standards were met, resulting in the disclosure of numerous immaterial transactions that are not currently required to be disclosed.

Board Committees. New Item 407 requires disclosure regarding compensation committees similar to the currently required disclosure for audit and nominating committees. Companies would have to describe their processes and procedures for the consideration and determination of executive and director compensation. The new rules also require a company to post its audit committee, compensation committee and nominating committee charters on its web site or include the charters as an appendix to its proxy statement at least once every three years.

Existing Governance Disclosure. Certain existing disclosure requirements regarding governance have been consolidated under new Item 407, including disclosure regarding board meetings, the audit committee and its processes, audit committee financial experts, the nominating committee and its processes, compensation committee interlocks and insider participation, shareholder communications and annual meeting attendance.

Plain English

As expected, the final rules require information disclosed under Items 402, 403, 404 and 407 of Regulation S-K to be presented in accordance with the SEC’s plain English principles.

Effectiveness

The rules become effective after their publication in the federal register as follows:

- for Forms 8-K, for triggering events that occur 60 days or more after publication of the final rules in the *Federal Register*;
- for Forms 10-K, for fiscal years ending on or after December 15, 2006;
- for proxy statements that are filed on or after December 15, 2006 that are required to include Item 402 and 404 disclosure for fiscal years ending on or after December 15, 2006; and
- for registration statements (including post-effective amendments) that are filed with the SEC on or after December 15, 2006 that are

required to include Item 402 and 404 disclosure for fiscal years ending on or after December 15, 2006.

effect, two years' information for the second year, and three years' information for the third year and thereafter.

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For more information on the foregoing or other securities matters, please contact the authors of this client memorandum (Troy M. Calkins at 312-569-1150, Kimberly K. Rubel at 312-569-1133 or George C. McKann at 312-569-1127), any member of the Gardner Carton & Douglas LLP Securities Practice Group, or your regular Gardner Carton & Douglas LLP contact.

The SEC adopted a three-year phase in for compliance with the new summary compensation table and Item 404(a) disclosure. This approach will not require companies to restate compensation or related-party disclosure for fiscal years in which they previously were required to apply the current rules. So, for example, the new compensation tables would present only one fiscal year's information for the first year the new rules are in

APPENDIX

Table 1

SUMMARY COMPENSATION TABLE

Name and Principal Position (a)	Year (b)	Salary (\$) (c)	Bonus (\$) (d)	Stock Awards (\$) (e)	Option Awards (\$) (f)	Non-Equity Incentive Plan Compensation (\$) (g)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$) (h)	All Other Compensation (\$) (i)	Total (\$) (j)
PEO ¹	_____ _____ _____								
PFO ¹	_____ _____ _____								
A	_____ _____ _____								
B	_____ _____ _____								
C	_____ _____ _____								

¹: "PEO" refers to principal executive officer and "PFO" refers to principal financial officer.

Table 2

GRANTS OF PLAN-BASED AWARDS

Name (a)	Grant Date (b)	Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Stock Awards: Number of Shares of Stock or Units (#) (i)	All Other Option Awards: Number of Securities Underlying Options (#) (j)	Exercise or Base Price of Option Awards (\$/Sh) (k)
		Threshold (\$) (c)	Target (\$) (d)	Maximum (\$) (e)	Threshold (\$) (f)	Target (\$) (g)	Maximum (\$) (h)			
PEO										
PFO										
A										
B										
C										

Table 3**OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END**

Name (a)	Option Awards					Stock Awards			
	Number of Securities Underlying Unexercised Options (#) Exercisable (b)	Number of Securities Underlying Unexercised Options (#) Unexercisable (c)	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Options (#) (d)	Option Exercise Price (\$) (e)	Option Expiration Date (f)	Number of Shares or Units of Stock That Have Not Vested (#) (g)	Market Value of Shares or Units of Stock That Have Not Vested (\$) (h)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#) (i)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$) (j)
PEO									
PFO									
A									
B									
C									

Table 4**OPTION EXERCISES AND STOCK VESTED**

Name (a)	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#) (b)	Value Realized on Exercise (\$) (c)	Number of Shares Acquired on Vesting (#) (d)	Value Realized on Vesting (\$) (e)
PEO				
PFO				
A				
B				
C				

Table 5**PENSION BENEFITS**

Name (a)	Plan Name (b)	Number of Years Credited Service (#) (c)	Present Value of Accumulated Benefit (\$) (d)	Payments During Last Fiscal Year (\$) (e)
PEO				
PFO				
A				
B				
C				

Table 6**NONQUALIFIED DEFERRED COMPENSATION**

Name (a)	Executive Contributions in Last FY (\$) (b)	Registrant Contributions in Last FY (\$) (c)	Aggregate Earnings in Last FY (\$) (d)	Aggregate Withdrawals/Distributions (\$) (e)	Aggregate Balance at Last FYE (\$) (f)
PEO					
PFO					
A					
B					
C					

Table 7**DIRECTOR COMPENSATION**

Name (a)	Fees earned or paid in cash (\$) (b)	Stock Awards (\$) (c)	Option Awards (\$) (d)	Non-Equity Incentive Plan Compensation (\$) (f)	All Other Compensation (\$) (f)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$) (g)	Total (\$) (h)
A							
B							
C							
D							
E							