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Weil

A Baker's Dozen of Challenges for the 2013 10-K and Proxy Season – and Beyond

As US public companies approach the 2013 10-K and proxy season, we highlight a "baker's dozen" of disclosure and corporate governance challenges they will face. In Part I, we discuss challenges that are new – or attracting a heightened level of attention – for the upcoming season. In Part II, we discuss challenges that public companies will need to meet later in 2013 or for the 2014 season. Throughout this Alert, we suggest "***what to do now***."

In addition to "known" challenges, the prospect of a new SEC Chairman with a prosecutorial background could lead to changes in agency priorities and policies affecting not only public companies, but also the broader capital markets. In nominating Mary Jo White, a renowned former US Attorney who prosecuted terrorists, mobsters and securities law violators alike, the President emphasized the need for "tough cops on the beat to enforce the law." Assuming Senate confirmation, Ms. White can be expected to build on significant changes made to the SEC's enforcement program by another former federal prosecutor, the departing Enforcement Division Director Robert Khuzami. It is also likely that she will press forward with Congressionally-mandated rulemaking projects in such diverse areas as derivatives, executive compensation and small business capital formation. Other potential areas of focus for the SEC during the second term of the Obama presidency include money-market regulatory reform and high-frequency electronic trading.

Highlights of What's New for the 2013 Season:

1. Proxy statement innovations – and new litigation risks
2. Disclosure of compensation consultant conflicts of interest
3. Changes in proxy advisory firm analysis of pay-for-performance and new voting policies on hedging and pledging of company stock
4. Disclosure – and broader sanctions – for dealings involving Iran
5. Emphasis on auditor "skepticism"
6. Still-hot topics in financial disclosure
7. Compliance spotlight: Rule 10b5-1 plans, antibribery statutes and use of social media

Highlights of What's Coming Later in 2013 or for the 2014 Season:

8. New standards on compensation committee and adviser independence
9. Change in proxy advisory firm voting policy on board responsiveness to shareholder votes
10. Emphasis on two-way communication between auditors and audit committees
11. More "foreign policy": disclosure of "conflict minerals" and governmental resource extraction payments
12. Reliance on "commercial end-user" exception for clearance of swaps
13. Additional disclosure requirements on the horizon (perhaps)

Part I: New or Heightened Challenges for the 2013 Season

Challenge 1: Make the Proxy Statement More Readable (and Win Votes) – And Watch Out For New Litigation Risks Linked to Proxy Disclosure and Director Compensation

A. Proxy Disclosures to Consider for 2013

Over the past two years, the need to garner support for management say-on-pay proposals has spurred an evolution of proxy statement disclosure to improve readability and tone. Concerned that the increasing length and complexity of proxy statements were leading some investors to rely on proxy advisory firm summaries, companies have begun to provide their own high level summaries at the front of the document. Other innovations include letters from the board to set a tone of openness and highlight key achievements or approaches; executive summaries of the compensation discussion and analysis (CD&A); shareholder-friendly graphics; "at a glance" director matrices describing skills, independence, age and tenure; and the embedding of electronic navigation tools. Companies are also expanding their disclosures regarding their shareholder engagement efforts.

In preparing this year's proxy statement, special attention should be paid to Item 402(b)(1)(vii) of Regulation S-K, which requires that companies address whether and, if so, how the company considered the results of the prior year's say-on-pay vote. Even companies that received strong support will need to describe steps taken by the company to respond to shareholder concerns and how the results factored into the company's decision-making on compensation. Companies that received less than 70% of the votes cast in favor of the say-on-pay vote should expect greater scrutiny by proxy advisory firms, and risk a negative vote recommendation for members of the compensation committee and potentially the full board of directors if, in the advisor's view, the company has failed to respond adequately to the prior year's vote.

B. Latest Plaintiffs' Attack – Seeking to Enjoin Vote at Annual Meeting

Imagine, shortly after mailing the proxy statement for a fairly routine annual meeting, receiving a lawsuit seeking to enjoin one or more votes at the meeting unless the company first supplements its proxy statement with more detailed executive compensation disclosures. This is what has been happening in the past year at numerous public companies. Plaintiff law firms have filed complaints seeking to enjoin the vote on a company's say-on-pay proposal, a new or amended compensation plan, and even charter amendments to increase authorized shares. Generally, these lawsuits are putative class actions brought in the state court of the company's principal place of business (rather than Delaware). They claim the directors breached their fiduciary duties (and the company aided and abetted such breach) by not providing adequate disclosure in the proxy statement to enable shareholders to make informed voting decisions on these items. With only a few weeks until the annual meeting, a company is faced with a dilemma: (a) quickly settle, providing some additional disclosures and agree to pay the plaintiff law firm's fees, or (b) defend and face the uncertainty and expense of litigation and the prospect of postponing the vote on the complained of items (and the complexities attendant to any postponement). Last year, a number of companies, such as WebMD, settled after a brief fight (WebMD is reported to have agreed to pay the plaintiff

law firm at least $250,000). Some companies, such as Brocade, settled after the plaintiff obtained a preliminary injunction (the Brocade settlement included the payment of $625,000 in plaintiff attorneys fees). Other companies, such as Clorox, were able to have courts dismiss the lawsuits, and yet for others, such as Microsoft, the plaintiffs withdrew the lawsuit prior to a court ruling.

What to Do Now?

- ***Be Prepared***. Since they will need to react swiftly, companies should consider, even at the drafting stage of the proxy statement, the strategies for handling a potential injunction action. Expert testimony has been critical in cases that have been successfully defended to date. In any event, companies should monitor litigation facing other companies. Many plaintiff law firms (Faruqi & Faruqi LLP being the most prolific in this area) announce on their websites when they launch an investigation with respect to a company (usually within days after the proxy statement is filed).
- ***Focus on Disclosures***. In light of the claims that have been made by plaintiffs, a company seeking approval to increase a plan's share reserve should consider disclosing: (a) the number of shares currently available for issuance; (b) why the current reserve is insufficient; (c) the dilutive impact; and (d) possibly, the methodology used to determine the number of additional shares requested (*e.g.,* burn rate estimates). Companies should focus on providing information that is material to investors, not just more information. A company should review its peers' disclosures to ensure it is not an outlier.
- ***Avoid Surprises in the Board Room.*** In-house counsel should advise management and the board of directors of this new litigation risk relating to the upcoming annual meeting. Companies should review their board and compensation committee processes, particularly relating to new share reserve amounts and benchmarking. Board and compensation committee minutes can create a strong record.
- ***Be Ready With An Adjournment Procedure.*** Under appropriate circumstances a company may determine to adjourn or postpone the vote on an item. Company personnel should evaluate in advance the legal and administrative procedures and impediments to taking such action.

C. Equity Awards to Non-Employee Directors: Business Judgment Rule or Entire Fairness?

A case decided by the Delaware Court of Chancery places a spotlight on a typical design feature of equity plans that may raise fiduciary duty issues for equity awards to non-employee directors. Most public companies have stockholder-approved equity plans from which non-employee directors receive equity awards as part of their fees. Although historically the amounts of such awards had been determined based on a formula included in the plan, more recently companies have used plans where directors have had discretion in determining the equity amounts they award themselves. In *Seinfeld v. Slager*,[1] the court concluded that the non-employee director defendants, in awarding themselves equity under the company's shareholder-approved plan, might not be entitled to business judgment rule protection (and therefore would be subject to Delaware's "entire fairness" standard of review

for the interested transaction). In denying the defendants' motion to dismiss, the court noted that the company's plan conferred upon the directors "the theoretical ability to award themselves as much as tens of millions of dollars per year, with few limitations" and that "there must be some meaningful limit imposed by the stockholders on the Board for the plan to receive . . . the blessing of the business judgment rule." The plan at issue in *Seinfeld* had an annual per-person limit of 1.25 million shares, which could have theoretically represented $21.7 million of grant date value or more, according to the court.

> ***What to Do Now?*** Companies should review equity plans and assess whether there are meaningful limits on the value of equity that non-employee directors can award themselves. If there is not, companies may wish to consider including a sublimit in a future plan amendment or a new plan (*e.g.,* an annual per-person limit on the number or dollar value of shares that may be granted to a non-employee director). The *Seinfeld* court's opinion cited the case of *In re 3COM Corp. Shareholders Litigation,*[2] where the Chancery Court determined that the option plan at issue had "sufficiently defined terms" and found that the defendant directors were entitled to the benefit of the business judgment rule. Company counsel should review the *Seinfeld* and *3COM* cases and monitor developments in this area.

Challenge 2: New SEC Disclosure Requirement for Compensation Consultant Conflicts of Interest – Requires Diligence and Assessment by Compensation Committee

New Item 407(e)(3)(iv) of Regulation S-K requires companies to disclose, in any proxy statement filed in connection with an annual or special meeting of shareholders at which directors are to be elected, the nature of any conflict of interest raised by the work of compensation consultants, and how the conflict is being addressed.[3] The new rule applies to consultants who had any role in determining or recommending the amount or form of either executive or director compensation during the last completed fiscal year, regardless of whether they were retained by the compensation committee or by management.

To satisfy this new requirement, the compensation committee must add a conflicts of interest assessment to its already extensive agenda of actions to take before the filing of the proxy statement. The following six factors are among those the committee must consider in determining whether a conflict exists:

- The provision of other services to the company by the firm that employs the consultant;
- The amount of fees received from the company by the firm that employs the consultant, as a percentage of the total revenue of the firm that employs the consultant;
- The policies and procedures of the firm that employs the consultant that are designed to prevent conflicts of interest;
- Any business or personal relationship of the consultant with a member of the compensation committee;
- Any stock of the company owned by the consultant; and

- Any business or personal relationship of the consultant or the firm employing the consultant with an executive officer of the company.

Item 407(e)(3)(iv) does not expressly require disclosure as to the absence of conflicts ("negative disclosure"). However, many companies that have already filed proxy statements for their 2013 annual meetings have disclosed that their compensation committees have conducted the required conflicts assessments and included a statement confirming the absence of any conflicts.

> ***What to Do Now?*** All companies should adjust disclosure controls and procedures to ensure that information relating to compensation consultant conflicts of interest is captured and that appropriate disclosures in the proxy statement are made, if required. Companies will need to update their D&O Questionnaires and make inquiries of compensation consultants and their firms. In addition, as discussed in Challenge 8 below, NYSE and Nasdaq companies should be mindful that new listing standards require, effective July 1, 2013, the compensation committee to consider the same six factors prior to engaging or receiving advice from *any* compensation adviser, including compensation consultants, outside legal counsel or other advisers.

Challenge 3: Proxy Advisory Firms Change Pay-for-Performance Analysis and Adopt New Voting Policies on Hedging and Pledging of Company Stock

This season, the influence of proxy advisors will continue to be felt not only on say-on-pay votes but also on votes outside the realm of compensation. ISS and Glass Lewis have each revised their proxy voting policies, as discussed in detail in our Alert dated December 21, 2012 at http://www.weil.com/files/upload/Weil_Alert_Corp_Gov_SEC_2012FINAL2.pdf. We highlight two significant areas below.

A. How Proxy Advisors Will Evaluate Pay-for-Performance in 2013

The alignment of executive compensation with company performance has become the central focus of ISS's vote recommendation for say-on-pay. ISS's methodology has been criticized for its reliance on a set of theoretical peer companies based on Global Industry Classification Standards ("*GICS*"), which can result in the inclusion of peers that have little relation to the company and the exclusion of peers that are closely related. ISS has also been criticized for relying on theoretical compensation as reported in the proxy statement's summary compensation table rather than actual or "*realized*" pay. ISS's new policies for 2013 attempt to address both of these criticisms. See our Client Alert for a detailed description.[4]

(1) Peer Group Composition: More Attention to Self-Selected Peers

For 2013, ISS's selected peer group for a subject company will generally continue to include 14 to 24 companies. However, the new methodology incorporates information from the subject company's self-selected pay benchmarking peer group in order to identify and prioritize GICS industry groups beyond the subject company's own GICS classification. The methodology initially focuses on an 8-digit GICS industry classification to identify peers that are more closely related in terms of industry. When selecting peers, the methodology prioritizes peers that are in the subject company's peer group, maintain the company size near

the median of its peer group, and that have chosen the subject company as a peer. This new approach is broadly similar to the Glass Lewis approach (effective July 2012), which considers a company's self-selected peers and the peers disclosed by the company's self-selected peers.

Even though ISS has said that it will take into consideration a company's self-selected peers, ISS FAQs clarify that a company's self-selected peers may not always appear in the ISS peer group, even if they meet ISS's size constraints (for example, if inclusion would lead to over-representation of a particular industry in the ISS peer group). In addition, ISS peer groups will not include privately-held or foreign-domiciled companies that are not domestic issuers for SEC filing purposes (*i.e.,* Form 10-K filers). Likewise, ISS will not incorporate market indices and broad benchmarking surveys in its peer group, even if a company uses such benchmarking tools.

(2) Realizable Pay: New Qualitative Consideration

Under its revised policy, ISS will compare CEO "*realizable pay*" (as defined by ISS and not the company) with grant date pay in its pay-for-performance analysis to reflect final payouts of performance-based awards or changes in value due to stock price movements. Realizable pay will be comprised of cash paid, equity-based grants made, changes in pension value and nonqualified deferred compensation earnings and "all other compensation" (such as perquisites) paid during a particular performance period. Realizable pay will be calculated using stock price at the end of the period, and will be based on equity award values for earned awards or target values for ongoing awards.

ISS has suggested in FAQs that companies include disclosure of ongoing or completed performance-based equity awards to facilitate ISS's calculation of realizable pay. Here is an example:

Grant Date	***Threshold Payout (#)***	***Target Payout***	***Maximum Payout***	***Performance Period****	***Target/Actual Earned Date***	***Actual Payout***
3/1/2009	100,000	150,000	200,000	1 year	6/1/2010	180,000
3/1/2010	150,000	200,000	250,000	3 years	6/1/2012	Not yet determined

*Performance period does not include time-vesting requirement.

According to ISS FAQs, ISS's research reports for S&P 500 companies will include a chart comparing realizable pay to granted pay over a three-year period (which for 2013 will consist of fiscal years 2010 through 2012). ISS may explore the underlying reasons behind why realizable pay is lower or higher than granted pay. Moreover, ISS will consider realizable pay for all companies in determining whether the company demonstrates a strong commitment to a pay-for-performance philosophy.

What to Do Now? Companies should try to "run the numbers" using ISS's new peer group methodology. ISS updated its peer groups using the new methodology in early January and will update them again in July 2013 and August 2013. (ISS has indicated in FAQs that companies with later fiscal year ends will be given an opportunity after the 2013 proxy season to communicate changes to peer groups.) Companies should

also review ISS's FAQs regarding the additional details ISS might need in a company's proxy statement to compute ISS's realizable pay to avoid ISS resorting to assumptions. Despite these changes in ISS's methodology, however, companies should not expect any significant impact on this year's pay-for-performance grades from ISS. According to ISS, for the overwhelming majority (>95%) of companies, it expects that its quantitative screen concern levels would not be affected by the new peer group methodology. Furthermore, ISS will continue to use the Summary Compensation Table's total compensation, *i.e.,* granted pay and pay opportunities, for its all-important initial quantitative screening of pay-for-performance. Only when there is a "high" or "medium" concern from the quantitative screen will it perform an in-depth qualitative review, which among other things, would include a comparison of granted pay to realizable pay (as defined by ISS). Such consideration may mitigate or exacerbate pay-for-performance concerns.

B. Any Hedging or Significant Pledging of Company Stock: A New Reason ISS Will Recommend a Vote Against Directors

For 2013, ISS has clarified that it considers "*any amount*" of hedging or "*significant pledging*" of company stock by executive officers or directors, regardless of whether such stock was purchased on the open market or received as equity compensation, as a "material failure of risk oversight." This clarification elevates hedging and pledging in ISS's view to the same level as bribery, large or serial regulatory fines or sanctions and significant adverse legal judgments or settlements. ISS will recommend a negative vote on directors if directors or executive officers have hedged any amount or pledged a significant amount of company stock. Whether a "*significant*" amount of stock has been pledged will be assessed by "measuring the aggregate pledged shares in terms of common shares outstanding or market value or trading volume." Where executives or directors currently have pledged a significant amount of company stock, ISS's policies outline several factors it considers when determining its voting recommendation.

What to Do Now? Companies should determine whether executives and directors hedge or pledge company stock. SEC rules currently require (i) disclosure in the CD&A of company policies regarding hedging, if material to shareholders' understanding of the company's compensation policies and decisions, and (ii) footnote disclosure to the beneficial ownership table of the number of shares pledged as collateral security. The SEC has not yet begun rulemaking required by the Dodd-Frank Act with respect to disclosure as to whether any employee or director is permitted to hedge against losses on company stock. Companies should also review their insider trading and other relevant policies and consider whether such policies should be amended to address hedging and pledging by executives and directors (and perhaps by all employees). Because the meanings of the terms "hedging" and "pledging" are subject to interpretation, a company will need to consider its policy carefully (*e.g.,* should a short position on the S&P 500 index be considered "hedging"?).

C. *A Caveat about Responding to Negative Recommendations from Proxy Advisory Firms*

Companies should carefully consider how to respond to negative vote recommendations from proxy advisory firms, whether on say-on-pay or other matters. Companies receiving a negative recommendation should reach out to the proxy advisory firm immediately to seek to correct any misstated fact or address any apparent misunderstanding. In some instances, it may be possible to obtain a revised recommendation by undertaking a change to targeted practices. Such a change would require disclosure in a supplemental filing with the SEC. Companies may also consider supplemental filings to respond to negative recommendations. Note, however, that some institutional investors may view a "bash ISS" filing as unduly argumentative or as highlighting a failure to communicate effectively in proxy materials in the first instance.

Challenge 4: New SEC Disclosure (and Broader Sanctions) for Dealings Involving Iran - Requires Global Diligence on the Company and its Affiliates

In August 2012, the President signed into law the Iran Threat Reduction and Syria Human Rights Act of 2012 (the "Iran Threat Reduction Act"). The Iran Threat Reduction Act is one of a "humanitarian triad" of highly prescriptive disclosure requirements dictated by Congress that focus on achieving humanitarian or foreign policy objectives largely unrelated to the central purposes of the federal securities laws: protecting investors and facilitating efficient capital formation and market trading. (The other two, discussed in Challenge 11 below, were imposed by the Dodd-Frank Act and require disclosure relating to "conflict minerals" and resource extraction payments made to governments around the world.) The Iran Threat Reduction Act expanded the disclosure obligations of US and non-US reporting companies, and the sanctions regime applicable to US reporting companies, for dealings involving Iran. For a detailed discussion of the requirements of the Iran Threat Reduction Act, see our Alert dated January 8, 2013 at http://www.weil.com/files/upload/Weil_Alert_Corp_Gov_SEC_Jan_2013.pdf, and for a discussion of related Compliance and Disclosure Interpretations (CDIs) issued by the SEC staff, see our Alert dated December 12, 2012 at http://www.weil.com/files/upload/Weil_Alert_SEC_Corp_Gov_December_12_2012.pdf.

A. *Disclosure*

Section 219 of the Iran Threat Reduction Act added Section 13(r) to the Securities Exchange Act of 1934 (the "Exchange Act"). New Section 13(r) requires a reporting company to provide disclosure in its annual and quarterly reports – beginning with the first report required to be filed after February 6, 2013 (even if actually filed before that date) – if the company or any of its affiliates has "knowingly" engaged during the reporting period in certain enumerated activities subject to US trade sanctions involving Iran or specified Iranian entities or nationals as well as certain other non-Iranian persons or entities deemed to promote terrorist activities and/or the proliferation of weapons of mass destruction. The staff has made clear that, even though the Iran Threat Reduction Act was not enacted until August 2012, new Section 13(r) covers activities dating back to January 1, 2012 (unless otherwise indicated in the Act's amendments to existing trade sanctions legislation).

When disclosure is required, the company must provide in its periodic report a detailed description of the nature and extent of the activity, the gross revenues and net profits attributable to the activity, and whether the company or affiliate intends to continue the activity. The company must also concurrently file with the SEC, via EDGAR, a separate notice on new form type IRANNOTICE indicating that the requisite disclosure has been made in a periodic report. The SEC in turn has a duty to report this disclosure to the President and specified Congressional committees. It is up to the President (through the Treasury Department's Office of Foreign Asset Control) to investigate and determine whether to impose sanctions on the company or the affiliate. Since Section 219 amends Section 13 of the Exchange Act, however, the SEC has the authority to pursue any violation of the new Section 13(r) disclosure requirements, regardless of whether any of the underlying activities ultimately are deemed by the Executive Branch to have violated statutory trade restrictions.

The staff has made clear in a CDI that the broad definition of the term "affiliate" set forth in Exchange Act Rule 12b-2 will govern the construction of Section 13(r). As a result, reporting companies will have to consider the activities of joint ventures and other non-consolidated entities anywhere in the world that might fall within the SEC's sweeping "affiliate" definition: any "person who directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with" the reporting company. In this connection, because Section 13(r) applies to enumerated activities "knowingly" engaged in by *either* the reporting company *or* its affiliates, the reporting company's ignorance of an affiliated entity's violation of the relevant provisions of the US trade sanctions regime may not be a defense to an SEC charge of a Section 13(r) disclosure violation**.**

Accordingly, reporting companies subject to Section 13(r) will have to identify potential "affiliates" and undertake an appropriate degree of inquiry to satisfy themselves that a particular affiliate's activities do not trigger disclosure in the upcoming Form 10-K (or 20-F) or 10-Q. During a January 2013 conference, a member of the senior SEC staff suggested that it would be appropriate for companies to take a common-sense, reasonable approach in identifying "affiliates" for purposes of Section 13(r) disclosure, citing the following example: Assume that the CEO of large-cap Company X serves on large-cap Company Y's board of directors. Thus, Company X CEO is technically an "affiliate" of both Company X and Company Y under Rule 12b-2. Does this mean that Company X and Company Y are affiliated because they are under the "common control" of a single individual (applying the "common control" element of the Rule 12b-2 definition of "affiliate")? A reasonable, common-sense analysis of these facts would indicate "no." But the answer might differ if one individual was a controlling stockholder of two small-cap companies with minimal public floats.

Two additional points regarding Section 13(r) underscore the need for careful scrutiny of global business activities in preparing upcoming Forms 10-K and/or 10-Q. First, Section 13(r) has no materiality threshold, which means that potentially sanctionable conduct involving even *de minimis* levels of revenue or profit will be covered (unless otherwise excluded under the predicate sanctions legislation or Presidential Executive Orders listed in Section 13(r)). In addition, because the information prescribed by Section 13(r) must be disclosed in a periodic report, it will be subject to certification by the CEO and CFO under Section 302 and 906 of the Sarbanes-Oxley Act of 2002.

B. Sanctions

US reporting companies should be aware that a separate provision of the Iran Threat Reduction Act – Section 218 – has expanded the US sanctions regime to encompass the activities of foreign subsidiaries and other entities that are "owned or controlled" by a US company after February 6, 2013. The term "owned or controlled," for Section 218 purposes, includes (a) ownership of a 50% or greater equity stake, by vote or value, in the foreign entity; (b) a majority of the entity's board seats; or (c) control of the management, policies or personnel decisions of the entity. US companies have the opportunity, on or before February 6, 2013, to divest or terminate business activities involving foreign subsidiaries that have engaged in heretofore permissible business dealings involving the Government of Iran. Note that Section 218 is not as broad in scope as Section 219, which, in contrast, applies to all reporting companies – including foreign private issuers that are not subject to Section 218 – and uses the expansive Exchange Act Rule 12b-2 definition of "affiliate."

> ***What to Do Now?*** Companies should collect information on their global business dealings, and those of their domestic and foreign affiliates, for 2012 in its entirety. Companies that identify potentially covered activities will need to analyze them with a view toward Section 13(r)-mandated disclosure. In addition, companies may need to modify their disclosure controls and procedures relevant to the preparation of periodic reports and the filing of an IRANNOTICE with the SEC to ensure proper collection and analysis in future quarterly and annual reports. Finally, companies also will have to re-examine and revise, as appropriate, their director and officer questionnaires, as well as their ethics codes and other relevant compliance policies and procedures, with a view toward compliance with all applicable aspects of the Iran Threat Reduction Act. It may be necessary to negotiate with major shareholders (who might be "affiliates") for access to the required information. Last, but not least, Section 218 will require US companies to re-examine, and possibly restrict, the activities of foreign subsidiaries with respect to Iran and other countries, persons or entities targeted by OFAC sanctions.

Challenge 5: Emphasis on "Skepticism" from the Auditors

Just as auditors began to gear up for calendar 2012 audits, the PCAOB's Office of Chief Auditor sent a strong message on the need to apply "professional skepticism" to financial statement audits. Staff Audit Practice Alert No. 10, *"Maintaining and Applying Professional Skepticism in Audits*," defines professional skepticism as "an attitude that includes a questioning mind and a critical assessment of audit evidence."[5] The Practice Alert indicates that, while beneficial throughout an audit, this attitude is particularly important where there are significant management judgments or transactions outside the ordinary course of business, such as nonrecurring reserves, financing transactions or related party transactions "that might be motivated solely, or in large measure, by an expected or desired accounting outcome," and in planning and performing audit procedures to address the risk of fraud.

> ***What to Do Now?*** Companies should be prepared for a greater degree of challenge to management representations and/or a greater focus on inconsistencies in audit evidence. The latter may be especially true when the auditor is engaged in evaluating matters such as (1) whether uncorrected misstatements identified during the audit result

in material misstatement of the financial statements; (2) potential management bias in making accounting estimates, selecting and applying accounting principles, or selectively correcting misstatements identified during the audit and identifying additional adjusting entries that offset misstatements accumulated by the auditor; and (3) whether the financial statements contain the information essential for a fair presentation.

Challenge 6: Not New – But Still Hot – Topics in Financial Disclosure

Although not new, the financial disclosure issues discussed below were highlighted by senior SEC legal and accounting staff during conferences held in late 2012 and early 2013. The staff's continuing focus suggests that they may be less patient with perceived disclosure deficiencies during this year's review and comment process.

A. Impact of Hurricane Sandy

As they have done in the case of previous natural disasters, the staff will be paying close attention to how companies disclose the effects of Hurricane Sandy in upcoming annual reports. Public companies affected adversely by Sandy should assess the storm's impact on their business, including the effects of flooding, loss of power, property damage, loss of transportation, increases in insurance rates, and other business disruptions. Insurance companies facing large pay-outs likewise need to consider Sandy's implications for their own financial condition and results of operations. We recommend that companies consult the SEC's 2010 interpretive release on climate change for disclosure guidance.[6] Companies that stand to benefit financially from hurricane clean-up work should engage in the same analysis, albeit through a more positive framework of projected profitability.

B. Cybersecurity

While cybersecurity has been on the radar screen of both the SEC and Congress for some time, regulatory and legislative attention has heightened recently in the wake of reports of serious cyber attacks on large US banks. Companies need to give careful consideration to their vulnerability to cybersecurity breaches, and the materiality of actual incidents of breach, in light of their existing disclosure obligations relating to risk factors, MD&A (as a "material known trend, event or uncertainty"), loss contingencies and other key line-items in the financial statements, and any other portions of their periodic reports that might be implicated (*e.g.,* legal proceedings and description of business). These areas are emphasized in the disclosure guidance set forth in the Division of Corporation Finance's 2011 Disclosure Guidance Topic No. 2, "*Cybersecurity*."[7]

Companies should keep in mind that their disclosure obligation is not static. The SEC staff believes companies should be assessing their cybersecurity risks regularly for material changes – including but not limited to any cyber breach – with a view toward providing updated disclosure, if necessary, in the next Form 10-K or 10-Q, or perhaps even in a Form 8-K if a particular event triggers a current reporting duty (*e.g.,* the need for Regulation FD-compliant disclosure should the company seek to address rumors of customer account hacking). Particular attention should be paid, in preparing the upcoming Form 10-K, to the need for material updates to risk factors, PSLRA "meaningful cautionary statements" language, and the "known trends and uncertainties" disclosure requirements of the MD&A.

To illustrate a typical staff comment, if the staff believes a company may have experienced a material cyber breach based on news reports, it will ask why the company's risk factors continue to speak in terms of hypothetical cyber risks where an actual breach is rumored to have occurred, and there is no discussion of material loss contingencies arising from the reported breach. As is apparent from many of its comments in this area, the reviewing staff not only examines the required disclosures contained in periodic reports, but also checks web-based and other, more traditional media accounts, analyst reports and other sources of information about a particular company's experience with cyber attacks and the potential impact of an attack on the company's performance.

C. Exposure to European Sovereign and Non-Sovereign Debt

Given the protracted volatility of the European markets, particularly within the Eurozone, the SEC staff continues to remind multinational companies to consult the disclosure guidance on the risks of both direct and indirect exposure to European debt, whether sovereign or non-sovereign, as outlined in the Division of Corporation Finance's Disclosure Guidance Topic No. 4, "*European Sovereign Debt Exposures.*"[8] Although ostensibly aimed at financial institutions, the staff has advised that all companies with material European debt holdings should consult this guidance in identifying and analyzing the magnitude of default risks on foreign debt on a country-by-country basis, and any risk mitigation efforts. If material, the guidance recommends that such debt be disclosed on a country-by-country basis, with disclosures segregated by country and type of debt (sovereign and non-sovereign), counterparty, total gross (funded and unfunded), unfunded, gross and net funded exposures, and the effects of credit default protection in arriving at net exposure.

Companies with direct or indirect exposures to Eurozone debt, both sovereign and non-sovereign, should review the staff's disclosure guidance when preparing their upcoming annual reports. In some instances, the staff has requested a specific explanation of how the company defines "indirect" exposure, how such risks are managed, and either a description of stress-testing or the results of a sensitivity analysis. Keep in mind that outside auditors also have been pressed by the PCAOB staff to ask probing questions of a corporate audit client with material holdings of European debt.[9]

D. Material Loss Contingencies

Although the Financial Accounting Standards Board decided in mid-2012 not to move forward with its controversial proposal regarding material loss contingencies, the SEC staff has continued to target this area for review and comment in an effort to ensure that companies are complying with the current standard, Accounting Standards Codification ("*ASC*") Topic 450 (formerly known as Statement of Financial Accounting Standards No. 5, or "*SFAS 5*"). Under ASC 450-20, companies are required to accrue an estimated loss for a litigation loss contingency if information available before the financial statements are issued indicates that it is both probable that a liability has been incurred, and a loss (or a range of losses) can be reasonably estimated. Even where no accrual is necessary because a loss is not considered "probable" and/or cannot be reasonably estimated, the company must disclose the loss contingency in its financial statement footnotes if there is at least a "reasonable possibility" – defined as "more than a remote" likelihood – that a loss or an additional loss (above an amount already accrued) has been incurred. This footnote disclosure must address

the nature of the contingency and either give an estimate of the loss or range of losses, if material, or state that such an estimate cannot be made. For several years now, the SEC staff has emphasized the importance of an MD&A discussion of material pre-accrual lost contingencies as a disclosable "known trend or uncertainty."

The SEC accounting staff has confirmed that it is still taking aim at such practices as suddenly revealing an accrual in the financial statement footnotes without any advance warning at the "reasonably possible" stage in the footnotes and/or the MD&A (if material) — whether in the form of an estimated loss or range of losses, or a representation that such losses are not reasonably estimable, accompanied by a meaningful qualitative discussion. The staff is highly skeptical of "surprise" accruals because it expects such disclosures to begin at the "reasonably possible" stage and evolve as the facts and circumstances surrounding the litigation change. In addition, the staff is asking for disclosures relating to third-party recoveries (i.e. insurance and indemnification agreements). In an effort to be sensitive to attorney-client privilege and defense strategy concerns, the staff will permit discussion of loss contingencies stemming from multiple proceedings on an aggregate basis. In all instances, however, the staff is calling for more transparency regarding the variability of the management assumptions and judgments underpinning amounts that are either accrued (when losses are "probable") or disclosed (when losses are "reasonably possible" and susceptible of quantification). Last but not least, the staff will continue to push back hard on company representations that loss contingencies at the "reasonably possible" stage cannot be estimated.

E. Liquidity Implications of Limits on "Repatriation" of Foreign Earnings

In light of continued economic uncertainty within and outside the US, information about liquidity, including the ability to repatriate cash allocated to non-US subsidiaries (even if denominated in US dollars and/or held in US bank accounts for the benefit of these subsidiaries), remains an important area of concern for the SEC. The staff has recommended that in appropriate cases – for example, when a US company's disclosures reflect a significant amount of foreign earnings for which there has been little or no tax provision – the MD&A should explain, as a material trend or uncertainty, that cash resources held by a foreign subsidiary or subsidiaries may not be available to the US parent company (either in whole or in part) in the event of a liquidity crunch, at least without incurring a significant tax liability. The staff will frequently ask about: (1) the amount of foreign cash and cash equivalents compared to the total amount of cash and cash equivalents as of year-end; (2) quantifying the amount of "foreign" cash where the funds are not readily convertible into other currencies and related liquidity implications; (3) disclosure of the fact that if the foreign cash and cash equivalents are needed for operations in the US, the company would be required to accrue and pay US taxes to repatriate these funds; and (4) disclosure regarding a company's intent to reinvest these foreign amounts outside the US on a permanent basis, and whether its current plans indicate some need to repatriate the foreign amounts to fund its US operations. Companies with substantial international operations should evaluate, with a view to possible risk factor and MD&A disclosure, the validity of the assumption often made that earnings of a foreign subsidiary will not be repatriated (meaning that they will not be subject to US income tax, resulting in a tax rate reconciliation item).

F. Deferred Tax Assets

The need for valuation allowances for deferred tax assets in the current uncertain economic environment remains a "front-burner" issue for the SEC accounting staff, because of the significant management judgments involved in projecting future realization of those assets. US GAAP requires that companies reduce deferred tax assets ("DTAs") by a valuation allowance to the extent that, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50%) that some portion or all of the DTAs will not be realized.[10] Last year the staff was concerned that companies were not taking appropriate allowances against DTAs because they viewed the downturn as an aberration; this year the staff is focused on whether companies experiencing a return to profitability should be reversing such allowances in accordance with GAAP. The ultimate question, again, is whether it is more likely than not that a specific DTA will be realized in the future, which entails projection of future profitability.

As the staff has indicated, companies considering whether to reverse a previously recognized tax valuation allowance should consider these factors: (1) the magnitude and duration of past losses; (2) the magnitude and duration of the company's current profitability (i.e. is it sustainable?); and (3) changes in the first two factors that drove losses in the past and that are now driving profitability. The staff has cautioned that management's forecasts underpinning a DTA realizability analysis should be consistent with other forecasting – the example given was goodwill and other intangible asset impairment analysis. And management should evaluate its financial forecasting track record in considering the reliability of current forecasts. We recommend that companies be prepared for staff comments this year on valuation allowances, particularly any reversals, and management's basis for concluding that it is more likely than not that a material DTA will be realizable. Contemporaneous documentation of judgments made, and clear, candid disclosure in the tax footnote and the MD&A (*e.g.,* if income tax accounting is a critical accounting estimate), should ease the company's way through the staff review and comment process.

G. Segments

Many companies have responded to volatile economic conditions by restructuring their operations, leading in some cases to significant changes in how they manage their businesses. Alert to the possibility that some companies may not have reassessed their definitions of GAAP segments in light of these developments, the SEC staff will continue to check during the review process on the consistency between a company's definition of its segments for financial reporting purposes and how the company describes its businesses in press releases, investor presentations and other "informal" web-based disclosure platforms (including the company's own website). As part of this review process, the staff also will consider how the market views the company, examining analyst reports and other third-party sources of information about the company. If the staff spots apparent discrepancies, it will ask probing questions and may even request access to the reporting packages provided to the company's chief operating decision maker (whose understanding and management of the business are key to defining operating segments), the board of directors and/or the audit committee.

Once again, the SEC accounting staff is urging companies to make sure that their decisions on both identification and aggregation of segments are re-examined periodically as facts and circumstances change and, once made, are appropriately analyzed and documented. Improper

aggregation of operating segments raises additional staff concerns regarding possible concealment of material goodwill impairment risks (see below), because the appropriate determination of operating segments is critical to GAAP-prescribed goodwill impairment testing. Finally, the staff announced that it will be focusing in 2013 on whether corporate MD&As drill down to the segment level in discussing results of operations.

H. Goodwill Impairment

Goodwill impairment remains a favorite SEC staff candidate for critical accounting estimate treatment in the MD&A, particularly given the extreme sensitivity of fair-value focused goodwill impairment testing to adverse economic conditions. Current US GAAP requires companies to use a two-part test to determine whether goodwill is impaired at least once a year, and more frequently if certain events or circumstances signal possible impairment. Step One consists of determining whether the fair value of a reporting unit – defined in terms of the company's GAAP-prescribed operating segments (discussed above) – is less than its carrying amount, including goodwill. If the answer is No, there is no recordable impairment, but if the answer is Yes, the company must go on to Step Two. Under Step Two, the company must measure the amount of impairment loss to be recorded. A recent change to GAAP, permits companies to make an initial, qualitative assessment of whether a reporting unit's fair value is less than its carrying amount before undertaking the familiar two-step analysis. However, the staff has cautioned that this so-called "Step Zero" does not permit evasion of the required two-step testing process.

While complimenting companies on their responsiveness to staff requests, made during last year's 10-K season, to disclose the risks of material impairment in the MD&A in situations where a company barely passed Step One (i.e. the carrying value of a reporting unit or units is at risk of exceeding fair value)[11], the SEC accounting staff recently indicated that many companies fail to disclose sufficient information where an impairment charge actually is taken in the current reporting period. The staff reminded companies recording a material impairment charge that they should: (1) disclose the events that triggered the charge, any changes in the underlying business or environment and the key assumptions affected; and (2) explain the timing of the charge (*e.g.,* why not taken earlier). If interim (intra-fiscal year) testing was performed, the staff recommends that companies disclose that the testing occurred and describe both the trigger(s) and testing results – even if the company "*passed*" Step One. The reasoning here is that such disclosure helps investors understand the ongoing impairment risk and what factors have changed since the company filed its last annual report (and conducted the annual testing). In addition, through comment letters, the staff has been evaluating the propriety of how some companies are allocating assets and liabilities to reporting units when performing the goodwill impairment test.

I. Non-GAAP Financial Measures

The SEC staff continues to comment on the use of non-GAAP financial measures, focusing on inconsistencies between the financial metrics disclosed in public documents filed with the SEC and non-filed communications with investors (such as earnings calls, press releases and analyst presentations). While the SEC staff has allowed companies greater flexibility in using non-GAAP financial measures in their public filings, the staff has made clear that such flexibility does not extend to permitting the use of misleading non-GAAP presentations in

any context, whether in an SEC filing or during a webcast earnings call. Particular areas of staff concern, as reflected in recent comment letters and speeches, include the removal of recurring cash expenses that are necessary to operate a business (*e.g.,* marketing costs), and the adjustment of GAAP financial measures for pension expenses (*e.g.,* the omission of "non-cash pension expense," which may confuse investors because pension liabilities are typically settled in cash). Another serious staff concern identified during a late 2012 conference is the inclusion of a full non-GAAP income statement in a press release or an SEC-filed document, which the staff believes gives the non-GAAP financial measure undue prominence and thus may be misleading. Companies should carefully evaluate the information they present in public filings and non-filed investor communications to ensure it is consistent, including when both non-GAAP measures and GAAP measures are presented.

Challenge 7: Spotlight on Compliance

"Compliance" is the deceptively benign rubric for a host of regulatory challenges keeping the CLO, the CCO and countless others at public companies up at night. While many compliance issues are specific to a company's operations, we highlight below three that are applicable to a broad spectrum of public companies.

A. Rule 10b5-1 Plans

Recent media reports indicate that federal prosecutors and the SEC have opened a new front in their three-year war against insider trading, targeting the use of "pre-arranged trading plans" established by corporate executives under Exchange Act Rule 10b5-1.[12] Certain corporate executives are alleged to have misused these plans, either to avoid losses by selling their companies' stock prior to the announcement of negative news, or by capturing potential gains through the purchase of company stock at a lower price before positive news is released. Members of Congress also are said to be investigating these reports, which could put additional pressure on the SEC to act on a recent request from the Council of Institutional Investors ("CII") to amend or further interpret Rule 10b5-1.[13]

Under Rule 10b5-1(c) in its current form, an insider who wishes to rely on the affirmative defense that a purchase or sale of securities was not made "on the basis of" material, non-public information in violation of Exchange Act Section 10(b) and Rule 10b-5 may adopt a binding trading plan that contains fixed parameters or otherwise bars the insider from exercising any subsequent influence over how, when or whether to trade. The insider must not be aware of material, non-public information regarding the company when establishing or modifying a plan. Moreover, the plan must be entered into in good faith and not as part of any scheme or plan to evade the prohibitions against insider trading. While the rule does not provide express guidance, the staff has warned that modifications and terminations of plans are among the circumstances that can raise issues of good faith.

The CII's request urges the SEC to mandate (pursuant to interpretive guidance or amendments to Rule 10b5-1) that companies adopt the following protocols and guidelines to address perceived abuses:

- Companies and their insiders should only be permitted to adopt Rule 10b5-1 plans during a company's open trading windows.

- There should be a mandatory "cooling-off period," preferably of three months or more, between adoption of a plan and execution of the first trade under the plan.
- Companies and their insiders should be prohibited from adopting multiple, overlapping Rule 10b5-1 plans.
- Companies and their insiders should not be permitted to make frequent modifications or cancellations of their plans.

What to Do Now? In light of the current critical governmental and investor focus on Rule 10b5-1 plans, now is a good time for all public companies to re-examine their existing policies and procedures regarding the use of these plans by "classic" insiders – executive officers and directors – as well as by the companies themselves (*e.g.,* for stock buybacks). We recommend that the responsible board committee or full board be briefed on the specific criticisms, and how the company's insider trading compliance program stacks up against them. At the end of the day, effective board oversight in this area is essential to protect the company, the board of directors – and the executives who use these plans themselves – against the risk of liability or reputational harm.

B. US and UK Anti-Bribery Statutes

On November 14, 2012, the US Department of Justice and the SEC issued their long-awaited joint "Resource Guide to the US Foreign Corrupt Practices Act." The 120-page guide provides a single source on a broad range of FCPA compliance and enforcement issues. The guide describes the analytical framework used by the two federal agencies in reviewing issues arising under the FCPA and, in particular, in considering whether to sue a company. It also consolidates, in one authoritative document, the various DOJ opinion letters, hypotheticals, practice tips and interpretations that collectively provide the framework for establishing and maintaining an effective compliance program. The guide tackles such difficult substantive issues as types of travel, training, and gift expenses that are likely to be viewed by the government as acceptable, as well as those that will likely invite further scrutiny. Perhaps most important, the guide reaffirms the value of maintaining a clear and concise FCPA policy and robust compliance program and confirms that vigorous US governmental enforcement efforts will continue.

What to Do Now? We recommend that companies review the guide's "Hallmarks of Effective Compliance Programs" with their legal counsel and use it as framework to evaluate, and if necessary, update their compliance programs, keeping in mind that individual companies will have different compliance needs. The "Hallmarks" include:

- A commitment from senior management and a clearly articulated corporate policy against corruption;
- A code of conduct and compliance policies and procedures outlining responsibilities for compliance;
- Oversight, autonomy and resources provided to one or more specific senior executives to implement the compliance program;
- Risk assessment of FCPA violations;

- Training and continuing advice to directors, officers, relevant employees, and, where appropriate, agents and business partners;
- Incentives and disciplinary measures to enforce the compliance program;
- Due diligence and monitoring of third-party payments;
- Mechanism for confidential reporting and internal investigations; and
- Periodic testing and review of compliance program.

Companies in the M&A market should consult the guide's detailed discussion of successor liability in the mergers and acquisitions context. Not surprisingly, the SEC and DOJ encourage acquiring companies to conduct extensive FCPA due diligence on potential targets, promptly report any FCPA violations identified to the government, and integrate acquired companies into their FCPA and other corporate compliance programs as quickly as possible. In addition, companies should consult the guide when analyzing other issues with potential FCPA implications, such as making charitable payments in a foreign country or vetting potential business partners in foreign jurisdictions.

Companies subject to the UK Bribery Act likewise should take proactive steps to ensure compliance with that statute. While there has yet to be a full prosecution under the UK Bribery Act involving corruption in a commercial context, on October 9, 2012, the Serious Fraud Office (SFO), which is the principal prosecuting authority in the UK, issued further guidance on its likely approach to prosecutions. This guidance reflects a tougher line taken by the SFO under its new director, emphasizing that self-reporting is no guarantee of non-prosecution, and that facilitation payments are unlawful under the UK law. On the other hand, it reiterates previous guidance to the effect that ordinary business entertainment and gifts are acceptable under the UK law.

C. Use of Social Media

Companies are increasingly active participants in the social media sphere, relying on such outlets as Facebook, Twitter, YouTube channel, and corporate blogs, to market their products and connect with customers. Although these platforms provide new commercial and investor relations opportunities, they also present challenges in complying with the disclosure requirements of applicable securities laws.

One set of concerns arises in the realm of Regulation FD compliance, particularly when social media communications are made by FD "authorized persons." For instance, disclosure via a social media post may not be considered an FD-compliant means "reasonably designed to provide broad, non-exclusionary distribution of the information to the public." Thus, if, for example, a company officer "tweets" previously undisclosed material information to her 200,000 Twitter followers, this communication alone may not be considered adequate "public" disclosure for FD purposes, even if members of the press are among those followers. Social media also presents a *timing* concern – many companies use social media to supplement information that has been disseminated to the public (for example, using Twitter to "tweet" highlights from a disseminated earnings release), but companies need to ensure that the supplemental social media post does not precede the public availability of the information via an 8-K or other FD-compliant means. Senior SEC staff recommended during a January 2013 conference that companies apply the guidelines for FD-compliant website usage outlined in a 2008 SEC interpretive release, in determining whether "authorized"

corporate communications made via interactive social media satisfy the requirements of Regulation FD.[14]

The SEC has shown signs of enhanced concern regarding the use of social media as a corporate communications tool. Companies have received staff comment letters asking about CEO usage of Twitter and other forms of social media to "front-run" the company's release of earnings and other important information. On December 5, 2012, Netflix disclosed in a Form 8-K that both the company and the CEO had received a Wells Notice arising from following post on his Facebook account at a time when such information had not already been publicly disclosed: "Congrats to Ted Sarandos, and his amazing content licensing team. Netflix monthly viewing exceeded 1 billion hours for the first time ever in June." For a detailed discussion, see our Alert dated December 2012 at http://www.weil.com/files/upload/Weil_Alert_Sec_Lit_Enforcement_Dec_21_2012.pdf.

Social media communications can also present securities law compliance concerns outside the realm of Regulation FD. One illustration is the recent case of Zipcar: following the announcement of Avis' plans to acquire the company, Zipcar's CEO posted the following tweet: "@bostonglobe weighs in on the revolution we started at @zipcar http://b.globe.com/130ybZW."[15] As the announced transaction still required shareholder approval, Zipcar filed the Twitter post with the SEC as proxy soliciting material.

> ***What to Do Now?*** Companies should be aware of how their directors, executives and other employees are using social media, whether for marketing, customer or investor relations purposes, or all of the above, while taking care not to discourage employee communications protected by federal labor law (*e.g.,* organizational activities). In addition, senior management and the board (or an appropriate committee) should review company policies and internal controls related to social media usage. The board should make sure that the company has established a clear compliance policy that specifically addresses the use and misuse (*e.g.,* to disclose confidential corporate information) of social media, including who is authorized to communicate for the company and in what circumstances. This policy should be reinforced regularly through appropriate training at all levels within the company. Companies also should monitor the comments made on social media outlets in which they participate, decide whether and how they will respond to third-party comments in accordance with the federal securities laws and other applicable laws, rules and regulations, and memorialize this protocol in the policy. Even if a company uses social media only to amplify other recognized distribution channels, the company should still be cognizant of the timing of posts and ensure that, where necessary, they are coordinated properly with disclosure made for purposes of FD compliance.

Part II: Challenges Coming Later in 2013 or for the 2014 Season

Challenge 8: New Listing Standards on Compensation Committee and Adviser Independence

New NYSE and Nasdaq listing standards relating to the independence of compensation committees and their advisers were approved by the SEC on January 11, 2013. The new standards apply to any company with listed equity securities, other than controlled companies and certain other listed companies specifically exempted by the exchanges. In approving the listing standards, the SEC did not take the opportunity to align the NYSE and Nasdaq standards where they differ. For a detailed discussion of the new standards, including certain open interpretive issues, see our Alert dated January 28, 2013 at http://www.weil.com/files/upload/Weil_Alert_SEC_CG_January_2013.pdf.

What to Do Now? Companies should start to prepare for the following:

- ***Required Independence Assessment of Advisers.*** Beginning July 1, 2013, a compensation committee may select or receive advice from a compensation consultant, legal counsel or other adviser only after conducting an independence assessment. In making its assessment, the compensation committee must consider the same six factors that must be considered now in determining whether a consultant's work raises a conflict of interest that requires proxy disclosure pursuant to new Item 407(e)(3)(iv) of Regulation S-K (see Part I, Item 2 above). A committee is not precluded from using a non-independent adviser, but it must first conduct the requisite assessment.
- ***New, Enhanced Standards for Compensation Committee Independence.*** New, enhanced independence criteria for compensation committee members must be satisfied by the earlier of the first annual shareholders meeting after January 15, 2014 or October 31, 2014. Supplementing the existing listing requirements that members of the compensation committee be independent, the NYSE and Nasdaq listing standards now also require that the board of directors take into account two factors enumerated in Exchange Act Section 10C-1(b)(1) in determining whether a director is eligible for service on the compensation committee. It is here that the stock exchanges' standards differ.
  - The NYSE does not impose any bright-line tests for compensation committee member independence. For NYSE-listed companies, the board of directors must *consider* all factors specifically relevant to whether a director has a relationship to the listed company that is material to his or her ability to be independent from management in connection with performing the duties of a compensation committee member, including but not limited to: (1) the source of compensation of the director, including any consulting, advisory, or other compensatory fees paid by the listed company to the director, and (2) whether the director is affiliated with the company, a subsidiary of the company or an affiliate of a subsidiary of the company. There is no look-back period.
  - Nasdaq, in contrast, has imposed a bright-line test that prohibits a compensation committee member from accepting directly or indirectly any consulting, advisory or other compensatory fee from the company or any subsidiary. This test mirrors

the bright-line audit committee independence test under Exchange Act Rule 10A-3. In determining whether a director is eligible to serve on the compensation committee, Nasdaq also requires the board to *consider* whether the director is affiliated with the company, a subsidiary of the company or an affiliate of a subsidiary of the company to determine whether such affiliation would impair the director's judgment as a member of the compensation committee. As in the case of the NYSE standard, there is no look-back period.

Under the new listing standards, the board must consider a director's status as an affiliate in order to determine whether such director is eligible to serve on the compensation committee. In comparison, Exchange Act Rule 10A-3 automatically disqualifies an affiliated director from audit committee service. The stock exchanges have noted that significant share ownership or affiliation with a significant stockholder will not be a bar to a finding of independence for compensation committee members. Therefore, a designee of a significant stockholder, who may not qualify for service on the audit committee, could still qualify for service on the compensation committee.

- ***Expanded Compensation Committee Responsibility and Authority over Advisers and Related Charter Amendments.*** Compensation committee charters must be revised by July 1, 2013 to reflect certain responsibilities and authority over advisers specified in the new listing standards. For a Nasdaq-listed company that has not yet established a committee (see below), the independent directors must undertake the new responsibilities and authority by July 1, 2013.
- ***Formal Compensation Committee and Charter Requirements for Nasdaq Companies.*** Nasdaq companies that do not have a compensation committee or formal written charter will need to have them in place by the earlier of the first annual shareholders meeting after January 15, 2014 or October 31, 2014. The charter is now required to include certain enumerated responsibilities of the compensation committee, so even Nasdaq companies that already have a formal written charter will need to review the charter for compliance with the new requirements.

Challenge 9: Emphasis on Two-Way Communication Between Auditors and Audit Committees

On December 17, 2012, the SEC approved PCAOB Auditing Standard No. 16, *Communications with Audit Committees* ("AS 16"), and related amendments to other PCAOB standards.[16] AS 16 is intended to foster constructive two-way discussions between audit committees and auditors, particularly about areas of the financial statements (or the audit or review process) that involve high degrees of uncertainty, subjectivity or judgment or that have been the subject of significant deliberation, debate – or even tension – between the auditor and management. AS 16 also formalizes the audit committee's role in engaging the outside auditor, clarifying that auditors must establish an understanding of terms of their engagement with the audit committee, rather than company management. For a detailed discussion of the new requirements, see our Alert dated September 10, 2012 at http://www.weil.com/files/upload/NY_Briefing_SEC_Corp_Gov_September_2012.pdf.

AS 16 and the related amendments will take effect for audits and reviews of fiscal periods beginning on or after December 15, 2012. Thus, for calendar year companies, the new

standard will apply to the auditor's review of the financial statements for the first quarter of 2013 and to engagement of the auditor for the 2013 audit (which usually takes place in the first quarter).

> ***What to Do Now?*** Nothing prevents early application of AS 16. Audit committees of calendar year companies should consider asking their auditors to accelerate its application, at least in key areas, when presenting the results of the 2012 audit. Audit committees that have not already done so should also consider using the upcoming annual engagement process as an opportunity to apply the new guidance set forth in PCAOB Release No. 2012-0003, *Information for Audit Committees about the PCAOB Inspection Process.*[17] This guidance, applicable at any time, encourages audit committees to ask, and auditors to answer, questions about the outcome of PCAOB inspections of the audit firm.

Challenge 10: Change in Proxy Advisory Firm Voting Policy on Board Responsiveness to Shareholder Votes – Be Prepared to Act Quickly

ISS will continue, for the 2013 season, its policy of recommending a negative vote where, in its view, the board "failed to act" on a proposal that received either support of (a) a majority of shares cast the previous year and also one of the two years prior to that, or (b) the majority of shares *outstanding* the previous year. Up until this season, ISS would recommend against the entire board (other than new nominees, who are considered case-by-case). This season, ISS will recommend against individual directors, committees or the entire board as it deems appropriate.

A significant policy change will occur for the 2014 season. ISS will accelerate its determination of non-responsiveness and recommend a negative vote if the board "*failed to act*" on a shareholder proposal supported by *a majority of votes cast just the previous year*.

Under ISS's current policy, to be judged "responsive" will generally require "full implementation" of the shareholder proposal. If implementation of the shareholder proposal requires a shareholder vote, ISS will expect a management proposal designed to implement the earlier shareholder proposal on the next annual meeting ballot. If the board's response to the proposal involves less than full implementation, ISS will consider the following factors in determining its recommendation:

- Subject matter of the proposal;
- Shareholder support and opposition to the proposal at prior meetings;
- Board outreach to shareholders after the vote (as disclosed);
- Board actions in response to engagement with shareholders;
- Continuation of the underlying issue as a voting item on the ballot (as either a shareholder or management proposal); and
- Other factors as appropriate.

For additional information on how ISS will evaluate "full implementation" of a variety of specific shareholder proposals, see our Alert dated December 21, 2012 at http://www.weil.com/files/upload/Weil_Alert_Corp_Gov_SEC_2012FINAL2.pdf.

What to Do Now? The ISS policy change will increase the already significant pressure on boards to act in line with shareholder viewpoints, even where the vote result is non-binding. In this environment, it is important for boards and their counsel to apply the engagement techniques honed in the context of say-on-pay to shareholder proposals generally. In particular, boards should engage with their largest shareholders to seek support; consider ways of addressing shareholders' expressed views that the board believes may be acceptable from the company's perspective; and be prepared to negotiate with shareholder proposal proponents. Boards should also consider enhanced solicitation efforts with respect to management proposals and director nominees, particularly where there may be circumstances or reasons to believe that a proposal and/or one or more directors may receive a significant negative vote.

Challenge 11: New SEC Disclosure Requirements for Conflict Minerals and Governmental Resource Extraction Payments – More "Foreign Policy" Requiring Global Diligence

Together with Section 13(r) added to the Exchange Act by the Iran Threat Reduction Act, Exchange Act Sections 13(p) and 13(q), added by the Dodd-Frank Act, comprise the "humanitarian triad" of new disclosure obligations. The SEC has adopted final rules implementing both Sections 13(p) and (q), as discussed below.

A. Conflict Minerals

All reporting companies, whether US or non-US, will need to evaluate whether they are subject to the SEC's new rules on "conflict minerals" disclosure covering calendar year 2013. If the answer is yes, the company will have to file a new report on Form SD with the SEC by May 31, 2014. There is a one-time grandfather provision that enables a potentially affected company to exclude conflict minerals deemed "outside the supply chain" prior to January 31, 2013.

Section 13(p) of the Exchange Act imposes a new annual disclosure and reporting requirement on reporting companies that use "conflict minerals" originating from the Democratic Republic of Congo or an "adjoining" country (the "Covered Countries").[18] The term "conflict minerals" means gold and the three T's – tantalum, tin and tungsten – and a disclosure obligation arises if any such conflict minerals are "necessary to the functionality or production of a product" that is either manufactured by the company, or by a third party with which the company contracts for such manufacture. There is no *de minimis* exception.

Despite their seeming complexity, the requirements of new Rule 13p-1 and Part 1 of Form SD (applicable to conflict minerals) boil down to three basic analytical steps:

- **Step One** requires any reporting company, regardless of its size or country of origin, to determine whether "it … [has] conflict minerals that are necessary to the functionality or production of a product manufactured or contracted by that registrant to be manufactured…."
- **Step Two** comes into play only if the answer to the question posed in Step One is "yes," and requires the company to conduct a good-faith, "reasonable country of origin inquiry" that has been "reasonably designed" to determine whether any of its conflict minerals either originated in a Covered Country or was derived from recycled

or scrap materials. Regardless of the outcome of this inquiry, the company will have to file – and post on its website – a Form SD that discloses certain information about its inquiry in accordance with line-items set forth in Section 1 of the Form.

- **Step Three** is triggered if the company knows or has reason to believe that its necessary conflict minerals may have originated in the Covered Countries, and may not have come from recycled or scrap sources. In this case, the company will have to exercise "due diligence" on the source and chain of custody of those minerals using the only nationally or internationally recognized due diligence framework now in existence – the guidance approved by the Organisation for Economic Co-operation and Development (OECD). Depending on the outcome of the diligence process, the company may be required to file an audited Conflict Minerals Report as an exhibit to its Form SD, and post this information on its website. (A temporary exception to the audit requirement will be available for a category of "necessary" conflict minerals classified as "DRC conflict undeterminable.") The independent auditor must opine on whether the company's due diligence measures conform, in all material respects, with the OECD guidance and whether the company's description is consistent with the process it actually undertook. The SEC has indicated that a company may retain its independent auditor to conduct a conflict minerals audit without necessarily impairing the auditor's independence for the financial statement audit.

Companies should not defer consideration of the new conflict minerals rules and, if necessary, the development of appropriate compliance policies and procedures, in the hope that these rules will be stricken in the action now pending in the US Court of Appeals for the District of Columbia Circuit. Even if these rules ultimately are invalidated in a judicial context, the emergence of initiatives focusing on trade in conflict minerals, at the state level in this country and abroad,[19] and the extensive investment in compliance measures already made by various companies in sectors such as electronics and jewelry, suggest that competitive considerations alone, coupled with the heightened expectations of customers and other stakeholders (including certain activist investors), would prompt many global companies voluntarily to follow the OECD Due Diligence Guidance and provide related disclosure. In any event, if the current rules were to be overturned, the SEC would be forced to go back to the drawing board to discharge its statutory mandate – this is not a situation where, as in the case of proxy access, Congress has authorized but not required the SEC to implement a Dodd-Frank provision.

What to Do Now? Companies should conduct their initial Step One assessment immediately to determine whether the new rules will be applicable to them and whether the Step Two and/or Step Three inquiry will be necessary. To conduct Step One, companies should identify any products (including any necessary packaging) that the company manufactures, or contracts with a third party to manufacture, that might contain conflict minerals. Companies should not forget that this assessment must include product components that may be manufactured by other companies. In this connection, companies should identify any conflict minerals eligible for exclusion because they are "outside the supply chain" on or before January 31, 2013. Assuming the new rules are applicable, companies also should develop, and train responsible employees on adherence to, the requisite compliance policies and procedures – including those relating to disclosure controls and procedures and internal control over

> financial reporting – and prepare the board of directors to undertake oversight responsibilities in this area.

For more detail on the new rules, the content of the SD Report and recommendations on what to do now, see our Alert dated January 8, 2013 at http://www.weil.com/files/upload/Weil_Alert_Corp_Gov_SEC_Jan_2013.pdf.

B. Governmental Resource Extraction Payments

New Section 13(q) of the Exchange Act is aimed at "increase[ing] the transparency of payments made by oil, natural gas and mining companies to governments for the purpose of the commercial development" of these natural resources, thereby "help[ing] to empower citizens of these resource-rich countries to hold their governments accountable for the wealth generated by those resources." It requires all Exchange Act reporting companies, US and non-US, that are "resource extraction issuers" to disclose specified information annually regarding any payment made during the reporting period that is not *de minimis* (defined as a payment or series of payments of $100,000 or more) to a foreign government, or to the US federal government, for the purpose of "commercial development of oil, natural gas or minerals." Companies must disclose not only their own such payments, but also any such payments made by a "subsidiary" or other entity under the "control" of the company.

A "resource extraction issuer" is defined as a reporting company that is engaged in the "commercial development of oil, natural gas, or minerals." "Commercial development" includes exploration, extraction, processing, and export of oil, natural gas or minerals, or the acquisition of a license for any such activity. This definition is intended to capture only activities that are directly related to the commercial development of the covered resources, and not ancillary or preparatory activities. Generally speaking, the types of payments that must be disclosed include taxes, royalties, license and other fees, production entitlements, bonuses, dividends and infrastructure improvements, and the payments must be disclosed in a variety of way, including by project and by government.

A resource extraction issuer will be required to file annually a new Form SD no later than 150 days after the close of the company's fiscal year. The new rules apply to companies whose fiscal years end after September 30, 2013, with the first Form SD due no later than May 30, 2014 for calendar year companies.

> ***What to Do Now?*** Companies should assess now whether the new rules apply to them, either directly or pursuant to the activities of subsidiaries and/or "controlled" entities. If it is a resource extraction issuer, the company should review its disclosure controls and procedures to ensure that the requisite information to comply with the new rules can be accurately collected and reported in 2014.

Challenge 12: Reliance on the "Commercial End-User" Exception for Clearance of Swaps

Non-financial public companies that use derivatives to hedge exposure to business and/or market risks must decide relatively soon whether to rely on the "commercial end-user" exception ("End-User Exception") to the Dodd-Frank Act's requirement that transactions involving "swaps" (regulated by the CFTC), "security-based swaps" (regulated by the SEC)

and "mixed swaps" (regulated by both the CFTC and the SEC) must be cleared through a derivatives clearing organization and executed on an appropriate facility. Final determinations regarding reliance on the CFTC rule implementing the End-User Exception for swaps,[20] and/or the corresponding rule for security-based swaps proposed (but not yet adopted) by the SEC,[21] will not be required until at least September 2013 (assuming the company is not a "financial entity").[22] However, companies should be taking steps now to identify all current and reasonably foreseeable hedging transactions with a view toward board-level assessment of both the availability and desirability of election of the End-User Exception for each relevant type of derivatives transaction subject to mandatory clearance.

To qualify for the End-User Exception, a company that files periodic reports with the SEC must:

- not be a "financial entity";
- use each swap (or security-based or mixed swap, as the case may be) to "hedge or mitigate commercial risk";
- satisfy certain recordkeeping and reporting obligations which, among other things, relate to the company's election of the exception for non-cleared derivatives and its ability generally to meet the financial obligations arising from entry into such derivatives; and
- ensure that an "appropriate committee" of the board of directors (or the full board) is authorized to review and approve – and in fact has reviewed and approved – all company decisions to enter into non-cleared swaps (or security-based swaps, as the case may be). Such approval must be obtained *before* the company may rely on the End-User Exception, on at least an annual basis or more frequently in the event of a change in the company's hedging strategy.

Note that a company that is otherwise eligible to rely on the End-User Exception will retain the option to clear transactions involving any swap, security-based swap or mixed swap that regulators decide must be cleared as Dodd-Frank implementation continues. In some instances, the board or authorized committee may decide that clearance and settlement on an organized market may be more cost-effective, depending on the outcome of still-pending regulatory and market decisions regarding margin and minimum counterparty capital requirements for non-cleared swaps, and such other factors as the company's own liquidity needs and the degree of counterparty credit risk it is willing to incur.

What to Do Now? A reporting company's determination whether to elect the End-User Exception for each swap, security-based swap or mixed swap ultimately designated for clearance necessarily will demand a comprehensive analysis of the company's global hedging activities, including but not limited to those of affiliates.[23] If the company elects to rely on the End-User Exception, the board of directors will have to decide which committee (or committees, depending on the particular company and its derivatives usage) will be responsible for review and approval of non-cleared derivatives,[24] authorize that committee or committees to act and make the corresponding modifications to the relevant committee charter or charters, and adopt the appropriate policies and procedures at the board or committee level (as appropriate). As noted above, the CFTC has stated that these policies and procedures must be reviewed on at least an annual basis by the responsible committee or

committees or by the full board. Because the SEC has not yet adopted its version of the End-User Exception applicable to security-based swaps, companies should monitor that agency's rulemaking regularly to ascertain its views on this important governance issue.

Challenge 13: Additional Disclosure Requirements on the Horizon (Perhaps)

A. Some Unfinished Business Under the Dodd-Frank Act

Although it has not yet begun rulemaking and does not have a legislative deadline for completing its work, the SEC has indicated in its Unified Agenda of Regulatory and Deregulatory Actions (the Unified Agenda)[25] that it expects to propose and adopt final rules in 2013 with respect to the following outstanding and, in some cases, highly controversial Dodd-Frank mandates:

- Disclosure of the relationship between executive compensation actually paid and the company's financial performance;
- Disclosure comparing the CEO's compensation to that of the company's other employees (so-called "pay equity");
- Disclosure of whether employees or directors are permitted to hedge against losses on their company stock; and
- Stock exchange listing rules requiring listed companies to develop, implement and disclose a "clawback" policy with respect to executive compensation.

B. Corporate Political Contributions

Potentially sparking even more controversy, the SEC also indicated in its Unified Agenda that the Division of Corporation Finance will consider whether to recommend that the SEC propose rules in 2013 on disclosure of corporate political contributions. The SEC agenda notes that the rulemaking is in the "Proposed Rule Stage" and a notice of proposed rulemaking could be released by April 2013. Since the Supreme Court's decision in *Citizens United*,[26] which paved the way for unlimited political spending by corporations, the Center for Political Accountability, the Committee on Disclosure of Corporate Political Spending and other shareholders and groups have advocated heightened transparency of political corporate spending.[27] Others, including the SEC's two Republican commissioners, have voiced their opposition to new disclosure rules.

Note a significant number of public companies already make disclosures in their proxy materials about corporate political spending – some, but not all, in response to shareholder proposals. Additionally, more than half of the S&P 100 companies already disclose their political spending, generally on their websites. We also note that at least one institutional shareholder is pursuing litigation to obtain information about a company's political spending. On January 3, 2013, the New York State Comptroller, who oversees the New York State Common Retirement Fund, filed suit in Delaware seeking access to Qualcomm's books and records related to its political spending after the company reportedly denied the fund's request to view such materials last year.

Endnotes

[1] Seinfeld v. Slager, C.A. No. 6462-VCG (Del. Ch. June 29, 2012), available at http://courts.delaware.gov/opinions/download.aspx?ID=174870.

[2] 1999 WL 1009210, at *1 (Del. Ch. Oct. 25, 1999).

[3] Item 407(e)(3)(iv) applies to all companies subject to the proxy rules (whether or not listed on an exchange). *See* SEC Release No. 33-9330, Listing Standards for Compensation Committees, available at http://www.sec.gov/rules/final/2012/33-9330.pdf.

[4] Available at http://www.weil.com/files/upload/Weil_Alert_Corp_Gov_SEC_2012FINAL2.pdf.

[5] Audit Practice Alert No. 10, "Maintaining and Applying Professional Skepticism in Audits" (Dec. 4, 2012), available at http://pcaobus.org/Standards/QandA/12-04-2012_SAPA_10.pdf.

[6] SEC Rel. No. 33-9106 (Feb. 2, 2010), available at http://www.sec.gov/rules/interp/2010/33-9106.pdf.

[7] Available at www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm.

[8] Available at http://www.sec.gov/divisions/corpfin/guidance-topic4.htm.

[9] Audit Practice Alert No. 9, "Assessing and Responding to Risk in the Current Economic Environment" (Dec. 6, 2011), available at http://www.pcaobus.org/Standards/QandA/12-06-2011_SAPA_9.pdf.

[10] ASC 740-40-30-16 through 30-23.

[11] The Division of Corporation Finance staff's position is outlined in Section 9510 of the Financial Reporting Manual available at http://www.sec.gov/divisions/corpfin/cffinancialreportingmanual.pdf.

[12] S. Pulliam, J. Eaglesham & R. Barry, "Insider-Trading Probe Widens," Wall St. J., Dec. 10, 2012. *See* M. Siconolfi, "Pension Funds Seek Insider Curbs," Wall St. J., Dec. 31, 2012; R. Barry, S. Pulliam & J. Eaglesham, "Big Sales by Big Lots Brass," Wall St. J., Dec. 11, 2012; P.J. Henning, "The Fine Line Between Legal, and Illegal Insider Trading," NYT, Dec. 10, 2012; S. Pulliam & R. Barry, "Investors Call for More Disclosure of Executive Trades," Wall St. J., Nov. 29, 2012; J. Lahart, "Heard on the Street: Timing is Everything," Wall St. J., Nov. 28, 2012; S. Pulliam & R. Barry, "Executives' Good Luck in Trading Own Stock," Wall St. J., Nov. 27, 2012.

[13] Letter from Jeff Mahoney, General Counsel, Council of Institutional Investors to SEC Chairman Elisse B. Walter, dated Dec. 28, 2012, available at http://www.sec.gov/rules/petition/2013/petn4-658.pdf.

[14] Available at http://www.sec.gov/rules/interp/2008/34-58288.pdf.

[15] *See* Peter Lattman, "Zipcar Makes S.E.C. Filing After C.E.O.'s Twitter Message," NY Times Dealbook, Jan. 4, 2013.

[16] Available at http://pcaobus.org/Rules/Rulemaking/Docket030/Release_2012-004.pdf.

[17] Available at http://pcaobus.org/Inspections/Documents/Inspection_Information_for_Audit_Committees.pdf.

[18] Conflict Minerals, SEC Rel. No. 34-67716 (Aug.22, 2012) at 6-7, [77 FR 56273], available at http://www. sec.gov/rules/2012/34-67716.pdf.

[19] In the United States, for example, California and Maryland have passed laws barring state governmental contracting with companies that fail to comply with the disclosure requirements of Section 1502 of the Dodd-Frank Act and the SEC's implementing rules. *See* CAL. PUB. CONT. CODE § 10490 (West through 2012 Session); MD CODE ANN., STATE FIN. AND PROC. § 14- 413 (LEXIS through 2012 Session). Outside the United States, the European Commission expressed support in early 2012 for the OECD's Due Diligence Guidance. *See* Communication from the European Commission to the European Parliament, the Council and the European Economic and Social Committee, "Trade, growth and development: Tailoring trade and investment policy for those countries most in need" (Jan. 2012) at 15, available at http://trade.ec.europa.eu/doclib/docs/2012/january/tradoc_148992.EN.pdf.

[20] *See* CFTC, End-User Exception to the Clearing Requirement for Swaps, 77 Fed. Reg. 42560 (July 19, 2012), available at http://www.cftc.org/LawRegulation/FederalRegister/FinalRules/2012-17291.

[21] *See* SEC, End-User Exception to Mandatory Clearing of Security-Based Swaps, SEC Rel. No. 34-63556 (Dec. 15, 2010), available at http://www.sec.gov/rules/proposed/2010/34-63556.pdf.

[22] The CFTC has published a phased-in compliance schedule giving eligible commercial end-users of particular swaps subject to the Dodd-Frank clearing requirements up to 270 days after publication of a final clearing determination by the CFTC in the Federal Register to make an election to use the End-User Exception. *See* CFTC, Swap Transaction Compliance and Implementation Schedule: Clearing Requirement Under Section 2(h) of the CEA, 77 Fed. Reg. 44441 (July 30, 2012), available at http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-18383a.pdf. To date, the CFTC has designated for clearing certain interest rate swaps and credit default index swaps, thereby triggering the running of the 270-day timetable. CFTC, Clearing Requirement Determination, 77 Fed. Reg. 74283 (Dec. 13, 2012), available at http://www.cftc.gov/LawRegulation/FederalRegister/FinalRules/2012-29211. In addition, the U.S. Treasury Department has exercised its authority under Dodd-Frank to exempt foreign-exchange swaps and foreign exchange forwards from the statutory definition of "swap." While this means that FX swaps and FX forwards will not be subject to clearing, trade execution and margin requirements otherwise applicable to swaps, these exempt transactions are still covered by Dodd-Frank swap reporting and certain other requirements. *See* Department of the Treasury, Determination on Foreign Exchange Swaps and Foreign Exchange Forwards under the Commodity Exchange Act, available at http://www.treasury.gov/press-center/press-releases/Pages/tg1773.aspx.

[23] Both the SEC and CFTC have indicated that entities controlled by an SEC registrant must obtain board approval in order to invoke the End-User Exception. According to the

CFTC's adopting release, a parent registrant's board or board committee may authorize swaps of its affiliates.

[24] Such approval may be obtained on a general basis at least annually, or instead for each individual derivatives transaction that must be cleared. The determination of which option to choose lies with the board or appropriate committee(s).

[25] Available at http://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201210&RIN=3235-AL36.

[26] *Citizens United v. Federal Election Commission*, 558 U.S. 310 (U.S. 2010).

[27] Committee on Disclosure of Corporate Political Spending petition for rulemaking available at http://www.sec.gov/rules/petitions/2011/petn4-637.pdf.

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