

# INSIGHTS

## THE CORPORATE & SECURITIES LAW ADVISOR

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### SECURITIES DISCLOSURE

#### Considerations for Changes in Directors or Executive Officers of a US Public Company

*When a public company makes changes in corporate leadership, including in its directors and executive officers, there are reporting and other consequences that must be considered. Among these are SEC filings and stock exchange notifications.*

**By Laura D. Richman and  
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In connection with changes in corporate leadership, including the election or appointment of a new director, the resignation or retirement of a director, the appointment of certain officers, and the resignation, retirement or termination of certain officers, there are reporting consequences and certain other matters for a public company to consider.

#### Election or Appointment of a New Director

##### Form 8-K Filing

If a new director is elected by a method other than by a vote of security holders at an annual or

special meeting convened for that purpose (such as by election or appointment by the company's board of directors), the company must file an Item 5.02 Form 8-K with the US Securities and Exchange Commission (SEC) reporting that event within four business days of election or appointment, even if the director's term begins at a later date.<sup>1</sup> The Form 8-K must identify the new director, provide the date of election or appointment, describe any arrangements or understandings between the new director and any other person with respect to the director's election, disclose any board committees on which the director is expected to serve and describe any related person transactions with respect to the new director.

If, in connection with the director's election or appointment, the company:

- enters into a material plan, contract or arrangement, written or unwritten, to which the director is a party or in which the director participates,
- materially amends an existing such plan, contract or arrangement, or
- makes or modifies any grant or award to the director under any such plan, contract or arrangement,

the Form 8-K also needs to describe the terms of such action.

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The Form 8-K must include a brief description of the newly appointed director's compensatory and other agreements and arrangements, even if they are consistent with the previously disclosed arrangements for other directors. However, this requirement may be satisfied by cross-referencing the description from the company's most recent proxy statement or Form 10-K.<sup>2</sup>

## Section 16 Filings

If the company has any class of equity securities registered under the Securities Exchange Act of 1934 (Exchange Act), a new director will need to file a Form 3 within 10 days of becoming a director. Directors need to report whether or not they own any common stock or other equity securities of the company, including derivative securities relating to those securities whether or not issued by the company. The Form 3 reports the total amount of each equity security owned, but does not give details of specific transactions that occurred before the individual became a director. If the new director is granted any equity awards, or otherwise acquires any such equity securities, in conjunction with becoming a director, the new director will need to file a Form 4 within two business days of such transaction. As a practical matter, it makes sense to file the Form 3 before or with the filing of the Form 4, so Form 3 filings for new directors are often made before the 10 calendar day deadline.

Section 16 forms must be filed electronically with the SEC via EDGAR and posted on the company's website. To file the necessary Forms 3, 4 and 5 (Form 5 is used to report certain transactions exempt from Section 16(b), such as gifts, that need not be reported currently on Form 4), the director must have EDGAR access codes. Directors who have already served as a director, an executive officer or a principal accounting officer of another public company may have effective EDGAR access codes. If the new director does not have currently valid EDGAR access codes, the director must submit

a notarized Form ID to the SEC in order to obtain them. It is helpful to do this in advance of the election or appointment, if practicable, or promptly following such election or appointment, so that the required Form 3 and 4 filings can be timely filed.

If the company undertakes to file Forms 3, 4 and 5 on the director's behalf, the company should have the director sign a power of attorney appointing one or more company personnel as attorneys-in-fact who are authorized to sign such filings. This power of attorney needs to be filed as an exhibit to a Form 3 or Form 4 filed with SEC.

Companies should advise each new director that if the director is late in filing any Section 16 forms, the company will need to disclose the late filings, by name, in the company's proxy statement.

## Stock Exchange Notifications

Companies that are listed on the New York Stock Exchange (NYSE) need to provide information about new directors to the NYSE. If the new director is elected at an annual meeting of shareholders, information about the director will be included in the annual affirmation submitted to the NYSE. When a director is elected or appointed between annual meetings, the company will need to submit an interim affirmation to the NYSE to report the new addition to the board. If the new director is added to the audit, compensation or nominating/corporate governance committee, that also will have to be reported in the NYSE affirmation.

Nasdaq does not have a comparable notice requirement. However, if the addition of a new director causes a violation of the Nasdaq corporate governance rules (such as causing the board or directors to have a majority of non-independent directors), the company would need to notify Nasdaq of the violation.

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## Independence Determinations

If the company intends for the new director to qualify as an independent director, the company should gather the information necessary for the board of directors to make that determination. Many companies require potential directors to complete a questionnaire to gather the necessary information. This questionnaire could be the company's most recent directors' and officers' questionnaire, or it could be a comparable questionnaire designed specifically for potential directors. The questionnaire also should elicit information regarding any related person transactions to be disclosed in the Form 8-K as well as information regarding the director's qualifications to serve on a committee.

## Agreements

If a company has standard agreements with directors, such as an indemnification agreement, the company should be sure that the new director signs such agreements with the company.

Any contract or compensatory arrangement (or written description of such arrangement if no formal document exists) with a new director, or in which a new director participates, generally must be filed with the company's Form 10-Q or Form 10-K for such period, unless a standard form has already been filed.

## Director's Securities Law Obligations

The company should inform new directors of their obligations and potential liabilities under applicable securities laws. For example, companies should explain that insiders must not trade in the company's securities while in possession of material non-public information, or disclose such information to others. New directors should be given copies of the company's insider trading policy and be informed of trading restrictions, such as "black-out" or "window" periods and pre-clearance procedures. Companies also should make new directors aware of their potential personal liability

for disgorgement of "short-swing" profits made from matching non-exempt purchase and sales of the company's equity securities within any period of less than six months under Section 16(b) of the Exchange Act.

## Orientation

Director orientation is a topic that NYSE-listed companies must provide for in their corporate governance guidelines. Companies should be sure they are complying with their stated orientation policies when a new director is appointed to the board.

## Company Policies

The company should provide new directors with copies of its code of conduct, emphasizing which provisions are applicable to directors.

If the company has stock ownership guidelines applicable to directors, the company should inform new directors of the number of shares they are expected to own and the deadline by which such ownership must be attained. The company should communicate to the director whether, and the extent to which, equity awards may count towards compliance with the stock ownership guidelines and any penalty for non-compliance.

The company should deliver copies of any applicable hedging or pledging policies to the new director. If any of the shares owned by the director are pledged as collateral, the company may want to encourage the director to terminate such pledge arrangements to avoid disclosure in future proxy statements.

## Insider Loans

The Sarbanes-Oxley Act added Section 13(k) to the Exchange Act, generally prohibiting issuers from making, maintaining or arranging for personal loans to directors and executive officers. Accordingly, any impermissible outstanding

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loans should be paid off prior to a director's election or appointment.

## **Resignation, Retirement or Refusal to Stand for Re-Election by a Director**

### **Form 8-K Filing**

If a director resigns, is removed or notifies the company that he or she refuses to stand for re-election, the company will need to file an Item 5.02 Form 8-K reporting that fact and the date of such event. As discussed below, additional disclosure will be needed if a director's resignation or refusal to stand for re-election is the result of a disagreement between the director and the company, or if a director has been removed for cause.

The company does not need to file a Form 8-K to report that the board of directors or its nominating committee has decided not to re-nominate a director for a new term (other than as a result of receipt of the director's notification of refusal to stand for re-election). However, if a director resigns upon receiving notice that the company does not intend to nominate him or her for re-election, the company would have to file a Form 8-K. A company is not required to file a Form 8-K to report the death of a director.<sup>3</sup>

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***The notice is the triggering event regardless of when the director's service actually ends.***

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The Form 8-K is due within four business days of the triggering event. In the case of a departing director's notice of resignation, retirement or refusal to stand for re-election, the notice is the triggering event regardless of when the director's service actually ends. For example, if a director who is designated by a company's majority shareholder gives notice that he will resign if the majority shareholder sells its entire holdings of

issuer stock, the notice triggers an obligation to file a Form 8-K (which should clearly indicate the nature of the contingency and the extent to which the resigning director can control the occurrence of the contingency).<sup>4</sup> Because the Form 8-K must disclose the effective date of resignation or retirement, a second Form 8-K may be required to report the actual date board service ends.

The company's Form 8-K disclosure will need to be more extensive if a director resigns or refuses to stand for re-election as a result of a disagreement with the company, or if the director is removed for cause. Under these circumstances, the Form 8-K also will need to provide a brief description of the disagreement and disclose the board committee positions that such director held at the time of the event. If the director gives the company written correspondence surrounding the resignation, refusal or removal, that correspondence would have to be filed as an exhibit to the Form 8-K. By the day of filing a Form 8-K reporting a director's departure in such circumstance, the company must provide the director with a copy of its Item 5.02 disclosure. The director then has the opportunity to provide the company, as promptly as possible, with a letter either agreeing with the company's disclosures or stating the respects in which the director disagrees. If the company receives such a response from the director, it must amend its Form 8-K within two business days of receipt, filing the response as an exhibit.

### **Section 16 Filings**

No Form 4 is due as the result of a director's resignation or retirement. However, transactions on the date the director resigns or retires may need to be reported on Form 4. Also, after ceasing to be a director, the former director will need to file a Form 4 to report any non-exempt transactions made within six months of an opposite-way, non-exempt transaction that occurred while serving as a director or officer. (A post-termination purchase is an opposite of a pre-termination sale and a post-termination sale is the opposite of a pre-termination purchase.)

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If any Form 4 is filed by a person who is no longer a director or officer of the company, that individual should check the exit box in the upper left-hand corner of the form to indicate that the individual is no longer subject to Section 16 with respect to the company.

### **Stock Exchange Notifications**

NYSE-listed companies must file an interim affirmation within five business days to report the departure of a director (other than as a result of the expiration of the director's term). Unlike the Form 8-K, there is no exception in the NYSE notification requirement for reporting the death of a director. If a departing director was a member of the audit, compensation or nominating/corporate governance committee, the interim affirmation also would need to report the changes to the composition of the affected committees.

Nasdaq does not have a comparable notice requirement. However, if the departure (or death) of the director caused a violation of the Nasdaq corporate governance rules (such as causing the board or directors to have a majority of non-independent directors), the company would need to notify Nasdaq of the violation.

### **Former Director's Securities Law Obligations**

A person may not buy or sell securities of a company based on material non-public information obtained from the company or one of its representatives even after that person no longer serves as a director of the company. Some companies expressly apply their insider trading policies, including black-out or window periods and pre-clearance procedures, to former directors for a period of time. Departing directors should be reminded of these requirements.

A person who ceases to be a director will remain subject to short-swing liability pursuant to Section 16(b) of the Exchange Act for new, non-exempt purchases or sales only if they

are made within less than six months of a non-exempt, opposite-way transaction that occurred while that person served as a director or officer.

### **Treatment of Equity Awards**

The company should review the terms of any outstanding equity awards, such as unvested options or restricted stock, held by the departing director to determine if any of them are forfeited or accelerated. It would be useful for the company to remind the departing director of any deadlines to exercise equity awards and of any awards that will be lost upon the director's departure.

### **Appointment or Designation of Certain Officers**

#### **Form 8-K**

The company must file an Item 5.02 Form 8-K within four business days of appointing or designating a new principal executive officer, president, principal financial officer, principal accounting officer, principal operating officer, or person performing similar functions (collectively referred to as Form 8-K reporting officers). This Form 8-K would need to disclose the name and position of the officer and the date of appointment or designation. It also would have to provide the officer's age, positions with the company, term as an officer, arrangements with any persons pursuant to which such individual was selected as an officer, family relationships with directors or executive officers, a five-year business experience description and information about any related person transactions with respect to such officer.

If, in connection with the appointment of the Form 8-K reporting officer, the company

- enters into a material plan, contract or arrangement, written or unwritten, to which the officer is a party or in which the officer participates,

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- materially amends an existing such plan, contract or arrangement, or
  - makes or modifies any grant or award to the officer under any such plan, contract or arrangement,

the Form 8-K also will need to describe the terms of such action.

While a Form 8-K generally is due within four business days of the occurrence of the triggering event, if the company intends to publicly announce the appointment of a Form 8-K reporting officer by means other than the Form 8-K, such as via a press release, it may delay the Form 8-K filing until the day on which it otherwise makes a public announcement of the appointment. However, the company may not delay disclosure of the resignation of the officer formerly holding that position to correspond with the announcement of the new officer.<sup>5</sup>

The company is not required to file a Form 8-K to report the appointment or designation of any officer not listed above, even if the officer is an executive officer, but it may, of course, issue a press release or furnish an Item 7.01 Form 8-K (or file an Item 8.01 Form 8-K) to announce such appointment.

## Section 16 Filings

If the company has any class of equity securities registered under the Exchange Act, an individual who is newly appointed as an executive officer, and any new controller or other principal accounting officer, whether or not otherwise an executive officer, (each, a Section 16 reporting officer), will need to file a Form 3 within 10 days of appointment. Section 16 reporting officers need to report whether or not they own any common stock or other equity securities of the company, including derivative securities relating to those securities whether or not issued by the company. The Form 3 reports the total amount of each equity security owned, but does not give details of specific transactions that occurred before the individual became

a Section 16 reporting officer. If the new Section 16 reporting officer receives any equity awards, or otherwise acquires any such equity securities in conjunction with becoming a Section 16 reporting officer, that officer will need to file a Form 4 within two business days of such transaction. As a practical matter, it makes sense to file the Form 3 before or with the Form 4, so Form 3 filings for new Section 16 reporting officers are often made before the 10 calendar day deadline.

Section 16 forms must be filed electronically with the SEC via EDGAR and posted on the company's website. To file the necessary Forms 3, 4 and 5, the Section 16 reporting officer must have EDGAR access codes. Section 16 reporting officers who already have served as a Section 16 reporting officer or director of another public company may have effective EDGAR access codes. If the new Section 16 reporting officer does not have currently valid Edgar access codes, the officer must submit a notarized Form ID to the SEC in order to obtain them. It is helpful to do this in advance of becoming a Section 16 reporting officer, if practicable, or promptly following such appointment, so that the required Form 3 and 4 filings can be timely made.

If the company undertakes to file Forms 3, 4 and 5 on the officer's behalf, the company should have the officer sign a power of attorney appointing one or more company personnel as attorneys-in-fact who are authorized to sign such filings. This power of attorney needs to be filed as an exhibit to a Form 3 or 4 filed with SEC.

Companies should advise each new Section 16 reporting officer that if the officer is late in filing any Section 16 forms, the company will need to disclose the late filings, by name, in its proxy statement.

## Stock Exchange Notifications

Section 204.10 of the NYSE-listed company manual requires prompt notice of changes to executive officers. NYSE-listed companies can

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report such changes via the NYSE's interactive web-based tool, [egovdirect.com](http://egovdirect.com), or by submitting a written notice to their listing representative. There is no comparable requirement for Nasdaq companies.

### **Officer Designations**

To the extent that the board of directors wants to treat a newly hired officer as an executive officer, controller or principal accounting officer, or to promote an existing employee to such status, it is useful for there to be formal board action to make such designation because many disclosure and reporting obligations and filing deadlines under applicable securities laws are tied to such status.

### **Agreements**

If a company has standard agreements with executive officers or Section 16 reporting officers, such as an indemnification agreement, the company should be sure that the new officer signs such agreements with the company.

If the new officer becomes a named executive officer, any contract or compensatory arrangement (or written description of such arrangement if no formal document exists) with that officer or in which that officer participates generally must be filed as an exhibit to the company's Form 10-Q or Form 10-K for such period, unless a standard form has already been filed.

### **Officer's Securities Law Obligations**

The company should inform new officers of their obligations and potential liabilities under applicable securities laws. For example, the company should explain that insiders must not trade in the company's securities while in possession of material, non-public information, or disclose such information to others. New officers should be given copies of the company's insider trading policy and be informed of trading restrictions, such as black-out or window periods and

pre-clearance procedures. Companies also should make new Section 16 reporting officers aware of their potential personal liability for disgorgement of short-swing profits made from matching non-exempt purchase and sales of the company's equity securities within any period of less than six months under Section 16(b).

If a new officer already works for the company, that individual should be familiar with some of the securities law concepts discussed above, but there may be some new elements as a result of the executive officer or Section 16 reporting officer designation. In any event, promotion to executive officer or Section 16 reporting officer status is a good time to remind the individual of securities law obligations and liabilities.

### **Company Policies**

The company should provide newly hired officers with copies of its code of conduct. The company should emphasize to any newly designated executive officers (or other special category of officer) any code of conduct provisions now applicable to them, as opposed to all employees.

If the company has stock ownership guidelines applicable to officers, the company should inform new officers of the number of shares they are expected to own and the deadline by which such ownership must be attained. The company should communicate to the officer whether, and the extent to which, equity awards may count toward compliance with the stock ownership guidelines and any penalty for non-compliance.

The company should deliver copies of any applicable hedging or pledging policies to new officers. If any of the shares owned by an executive officer are pledged as collateral, the company may want to encourage the executive officer to terminate such pledge arrangements to avoid disclosure in future proxy statements.

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## Insider Loans

The Sarbanes-Oxley Act added Section 13(k) to the Exchange Act, generally prohibiting issuers from making, maintaining or arranging personal loans to directors and executive officers. Accordingly, any impermissible outstanding loans should be paid off prior to an executive officer's appointment.

## Resignation, Retirement or Termination of Certain Officers

### Form 8-K

If a Form 8-K reporting officer or any named executive officer (i.e., one of the persons listed in the summary compensation table of the most recent proxy statement), retires, resigns or is terminated from that position, the company must file an Item 5.02 Form 8-K. The Form 8-K must disclose that fact and the date of such event. The resignation, retirement or termination of any other executive officer does not trigger a Form 8-K filing. A Form 8-K is not required to report the death of an executive officer.<sup>6</sup>

The Form 8-K is due within four business days of the triggering event. In the case of a departing officer's notice of resignation or retirement, the notice may be the triggering event regardless of when the officer's employment actually ends. In any event, unless the Form 8-K that is filed to report a notice of resignation, retirement or termination discloses the actual retirement, resignation or termination date, a second Form 8-K may be required to report such event's effective date.

"Termination" includes a situation where one of the specified officers has been demoted or has had responsibilities removed such that the individual no longer functions in the same position, even if the individual remains employed.<sup>7</sup> A Form 8-K also is required when a principal

financial officer temporarily turns those duties over to another person (both at the time of the stepping down and replacement of the principal financial officer and at the time the original principal financial officer returns and the temporary principal financial officer departs).<sup>8</sup>

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***"Termination" includes a situation where one of the specified officers has been demoted or has had responsibilities removed.***

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If the officer who resigns, retires or is terminated was a named executive officer in the most recent proxy statement (or other SEC filing requiring executive officer compensation disclosure) and the company:

- enters into a consulting or other post-retirement compensatory plan contract or arrangement (whether or not written) as to which such named executive officer participates or is a party,
- materially amends such plan, contract or arrangement, or
- makes or modifies a material grant under such plan, contract or arrangement,

the Form 8-K will have to provide a brief description of the terms and conditions of the plan, contract or arrangement, and the amounts payable. Additionally, the plan, contract or arrangement must be filed as an exhibit to the company's Form 10-Q or Form 10-K for such period.

## Section 16 Filings

No Form 4 is due as a result of the resignation, retirement or termination of a Section 16 reporting officer. However, transactions on the date the officer resigns or retires may need to

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be reported on Form 4. Also, after ceasing to be a Section 16 reporting officer, the officer will need to file a Form 4 to report any non-exempt transactions within six months of an opposite-way, non-exempt transaction that occurred while serving as a Section 16 reporting officer or director. If any Form 4 is filed by a person who is no longer a Section 16 reporting officer or director of the company, that individual should check the exit box in the upper left-hand corner of the form to indicate that the individual is no longer subject to Section 16 with respect to the company.

### Stock Exchange Notifications

Section 204.10 of the NYSE-listed company manual requires a company to provide prompt notice of changes to executive officers. Unlike the Form 8-K, there is no exception in the NYSE notification requirement for reporting the death of an executive officer. NYSE-listed companies can report such changes via the NYSE's interactive, web-based tool, [egovdirect.com](http://egovdirect.com), or by submitting a written notice to their listing representative. There is no comparable requirement for Nasdaq companies.

### Former Officer's Securities Law Obligations

A person may not buy or sell securities of the company based on material non-public information obtained from the company or one of its representatives even after that person leaves the company or is no longer an officer. Some companies expressly apply their insider trading policies, including black-out or

window periods and pre-clearance procedures to former employees for a period of time. Departing employees should be reminded of these requirements.

A person who ceases to be a Section 16 reporting officer will remain subject to short-swing liability pursuant to Section 16 for new, non-exempt purchases or sales only if they are made within less than six months of a non-exempt, opposite-way transaction that occurred while that person served as a Section 16(b) reporting officer or director.

### Treatment of Equity Awards

The company should review the terms of any outstanding equity awards, such as unvested options or restricted stock, held by the departing executive officer to determine if any are forfeited or accelerated. It would be useful for the company to remind the departing officer of any deadlines to exercise equity awards and of any awards that will be lost upon the officer's departure.

### Notes

1. See Exchange Act Form 8-K Compliance and Disclosure Interpretations (C&DI), Question 117.07, available at <http://www.sec.gov/divisions/corpfin/guidance/8-kinterp.htm>.
2. See C&DI, Question 117.16.
3. See C&DI, Question 217.04.
4. See C&DI, Question 217.03.
5. See C&DI, Question 217.06.
6. See C&DI, Question 217.04.
7. See C&DI, Question 117.03.
8. See C&DI, Question 217.02.

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