Preparing for the 2013 Proxy and Annual Reporting Season

The time has come for calendar year public companies to begin planning for the 2013 proxy and annual reporting season. Key issues for the upcoming season are summarized below.

Say-on-Pay

Public companies now have two years of mandatory say-on-pay experience and precedents to draw upon when drafting the say-on-pay proposals for their proxy statements. The say-on-pay requirement makes a clear, user-friendly explanation of compensation very valuable. The compensation discussion and analysis (CD&A) section of the proxy statements, which often begins with an executive summary of the executive compensation program, is a key component of the say-on-pay process. Some companies also have used proxy statement summaries and supporting text within the say-on-pay section of the proxy statement to succinctly highlight the reasons why they believe their executive compensation programs should be approved.

Companies need to discuss in the CD&A the extent to which compensation decisions were impacted by the results of the say-on-pay vote. Because the 2012 proxy season was the first year for many issuers to have to make this disclosure, companies may want to review precedent from the 2012 proxy season to see how others handled it. Compensation committees should be reminded of this reporting obligation so that their deliberations can, if they so choose, specifically address the results of the say-on-pay advisory vote. However, because the say-on-pay vote is non-binding, compensation committees are not compelled to take any actions in response to the shareholder advisory vote.

In the event that a proxy advisory firm recommends that its clients vote against a company's executive compensation, the company should consider whether it wants to prepare letters, presentations or scripts, further explaining its compensation decisions and rebutting the report containing the negative recommendation. Any such materials should be filed with the Securities and Exchange Commission (SEC) as additional proxy materials.

While shareholders, for the most part, approved their companies' executive compensation proposals, often by wide margins, there were more instances of say-on-pay proposals receiving the affirmative vote of fewer than 50 percent of the votes cast in the 2012 proxy season than occurred in the 2011 proxy season, although the number of such failed votes was relatively small. Companies should be aware that litigation has been filed against a number of companies and their boards of directors where say-on-pay proposals failed to garner majority approval. Even if such lawsuits do not prevail on the merits, the costs of litigation can be expensive and may hurt the reputations of the defending companies and their compensation committee members.

Outreach to key investors can be an important element of a successful say-on-pay vote. Before the proxy season gets fully underway, it would be worthwhile for the investor relations department to contact any large shareholders that voted against executive compensation at the last annual meeting to discuss the reasons for the negative vote. This dialogue should deal with the investor's concerns, and should not involve any solicitation for the upcoming say-on-pay vote.

Say-When-On-Pay

Because the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) only requires companies to hold an advisory vote on the frequency of say-on-pay proposals (often called a "say-when-on-pay" vote) once every six years, it is likely that few companies will include a say-when-on-pay proposal in their 2013 proxy statements.

However, any company that has a management-sponsored say-when-on-pay proposal in its proxy statement must disclose the policy it adopts regarding frequency of say-on-pay votes—after taking into account the shareholder advisory say-when-on-pay vote—no later than 150 calendar days after the annual meeting, but at least 60 calendar days prior to the company's deadline for submission of shareholder proposals under Rule 14a-8 for the next annual meeting. This disclosure would generally be accomplished in, or in an amendment to, the Form 8-K reporting voting results pursuant to Item 5.07.

Compensation Committee Independence and Compensation Consultants

Listing Standards. In June 2012, the SEC adopted rules relating to compensation committee independence as well as to selection and use of compensation consultants and other advisers. New Rule 10C-1 under the Securities Exchange Act of 1934 (Exchange Act) implements the Dodd-Frank Act requirement for listing standards relating to compensation committees, addressing both compensation committee independence and compensation committee selection of compensation consultants, legal counsel or other advisers. The exchanges must have final listing standards regarding the independence requirements for compensation committee members that comply with the SEC's final rule not later than June 27, 2013.

Rule 10C-1 requires the exchanges to consider relevant factors when determining independence requirements for compensation committee members, including, but not limited to:

- The source of a board member's compensation, including any consulting, advisory or other compensatory fee paid by the issuer to such board member; and
- Whether a board member is affiliated with the issuer, a subsidiary of the issuer or an affiliate of a subsidiary of the issuer.

The SEC left it to the exchanges to determine the details of compensation committee listing standards not expressly mandated by the Dodd-Frank Act, subject to SEC approval. Both the New York Stock Exchange and the Nasdaq Stock Market have submitted proposed amendments to their respective listing standards to the SEC for review, but neither exchange has proposed any additional factors for boards of directors to consider when determining the independence of compensation committee members.[1]

Because the schedule set forth in the SEC's adopting release does not require final listing standards with respect to compensation committees to be effective until June 27, 2013, new Rule 10C-1 does not directly impact the upcoming proxy season for calendar year companies. The NYSE has proposed that its listed companies have until the earlier of their first annual meeting after January 15, 2014, or October 31, 2014, to comply with its new compensation committee independence standards, and until July 1, 2013, to comply with

the other provisions of its amended listing standards.

Nasdaq proposes that its listed companies would have to comply with the changes relating to compensation committee responsibilities and authority, such as the authority to retain and fund compensation advisers and the obligation to consider adviser independence factors, immediately upon the effectiveness of the amended Nasdaq listing standards. Nasdaq-listed companies would have until the earlier of their second annual meeting after Nasdaq's amended listing rules are approved, or December 31, 2014, to comply with the balance of its rule changes.

Rule 10C-1 also addresses compensation adviser conflicts of interest by providing that a compensation committee may select such compensation consultant, legal counsel or other adviser only after taking into consideration the following factors, as well as any other factors identified by the relevant exchange in its listing standards:

- The provision of other services to the issuer by the person that employs the compensation consultant, legal counsel or other adviser;
- The amount of fees received from the issuer by the person that employs the compensation consultant, legal counsel or other adviser, as a percentage of the total revenue of the person that employs the compensation consultant, legal counsel or other adviser;
- The policies and procedures of the person that employs the compensation consultant, legal counsel or other adviser that are designed to prevent conflicts of interest;
- Any business or personal relationship of the compensation consultant, legal counsel or other adviser with a member of the compensation committee;
- Any stock of the issuer owned by the compensation consultant, legal counsel or other adviser; and
- Any business or personal relationship of the compensation consultant, legal counsel, other adviser or the person employing the adviser with an executive officer of the issuer.

Neither the proposal submitted by the NYSE, nor the proposal submitted by Nasdaq, to implement Rule 10C-1 contained any additional factors for compensation committees to consider with respect to compensation consultants, legal counsel or other advisers.

Disclosure of Compensation Consultant Conflicts of Interest. When it adopted Rule 10C-1, the SEC also amended Item 407(e)(3) of Regulation S-K, addressing disclosure of compensation consultant conflicts of interest. This new disclosure requirement applies to the upcoming proxy season. Public companies must include any disclosure required by this new rule in proxy statements or information statements filed in relation to annual meetings (or special meetings in lieu of annual meetings) that occur on or after January 1, 2013, at which directors will be elected.

Existing Item 407(e)(3)(iii) of Regulation S-K requires companies to disclose the role of compensation consultants in determining or recommending the amount or form of executive and director compensation. Companies must identify the consultants, state who retained the consultants, describe the nature and scope of the assignment and, in certain circumstances, disclose the aggregate fees paid to the consultants.

If any compensation consultants whose work must be disclosed pursuant to Item 407(e)(3)(iii) have a conflict of interest, new Item 407(e)(3)(iv) requires disclosure of the nature of such conflict and how the conflict is being addressed, regardless of whether the compensation committee, management or any other board committee retained the consultant. In determining whether a conflict of interest exists for disclosure purposes, companies should

consider the same factors that Rule 10C-1 requires compensation committees to consider when hiring compensation consultants.

Item 407(e)(3)(iv) does not require disclosure of potential conflicts of interest or of an appearance of a conflict of interest; disclosure is only required if a compensation consultant has an actual conflicts of interest. Consulting on broad-based plans and providing non-customized benchmark data will not require conflicts of interest disclosure under this new rule. Item 407(e)(3)(iv) does not require disclosure with respect to compensation advisers other than consultants.

Nasdaq Compensation Committee Requirements. Nasdaq does not currently require its listed companies to have a separate compensation committee—Nasdaq's listing rules have permitted executive compensation to be determined, or recommended to the board of directors, by a compensation committee consisting solely of independent directors or by independent directors constituting a majority of the board, with only independent directors voting. In its proposed amendment to its listing standards, Nasdaq is seeking to require listed companies to have a standing compensation committee, with a minimum of two members. Therefore, Nasdaq companies that do not have separate compensation committees should begin planning for this new requirement.

For more information about the new compensation committee independence and compensation consultant conflict of interest disclosure, see our Legal Update dated June 28, 2012 entitled "SEC Adopts Compensation Committee Listing Standards and Compensation Consultant Disclosure Rules."[2]

Other Pending Dodd-Frank Regulation

Pay-for-Performance. The Dodd-Frank Act requires the SEC to adopt rules regarding pay-for-performance. Under these rules, companies will have to disclose material information that shows the relationship between executive compensation actually paid and the financial performance of the company, taking into account any change in the value of the shares of stock and the dividends of the company. The SEC has not yet proposed rules for this disclosure requirement and is not currently publishing a target time frame for such proposal. It seems unlikely that a rule on this subject could be proposed and finalized in time to impact the 2013 proxy season. Nevertheless, it is important to monitor this pending regulation because it is possible that the final disclosure requirements might influence upcoming decisions to be taken by compensation committees.

Internal Pay Comparison. The Dodd-Frank Act also requires an internal pay comparison, disclosing the median of the annual total compensation of all employees of the company except the CEO, the annual total compensation of the CEO and the ratio of the two numbers. As with pay-for-performance, the SEC is not currently identifying a target date for these proposed rules. Although the internal pay comparison rules are not likely to be required in 2013 proxy statements for calendar year companies, public companies should follow this rulemaking very carefully. Many companies, particularly global companies, are likely to find an internal pay comparison challenging to implement. It is possible that various employment databases will need to be coordinated and that information will have to be gathered for all employees in a different fashion than is currently in use. It is not clear what effective date the SEC will adopt for this new requirement, but it will take planning and time for companies to achieve compliance with its requirements.

Hedging. The SEC still needs to propose regulations to implement the Dodd-Frank Act requirement for companies to disclose whether employees and directors are permitted, directly or indirectly, to hedge market value of securities granted as compensation. Companies are

already required to disclose any policies regarding hedging the economic risk of owning company securities pursuant to Item 402(b)(2)(xiii) of Regulation S-K. It generally makes sense for companies to wait until the SEC adopts final rules before adopting or amending a hedging policy that is designed to be responsive to the Dodd-Frank Act hedging requirement.

Clawbacks. Under the Dodd-Frank Act, the SEC must direct stock exchanges to prohibit listing if a company does not develop a policy with respect to recovery of incentive-based compensation. Unlike the comparable Sarbanes-Oxley Act provision, under the Dodd-Frank Act, the clawback policy will need to cover both current and former executive officers, not just the CEO and the CFO. The Dodd-Frank Act clawback provision applies to any accounting restatement due to material non-compliance, whether or not the executive officer is responsible for the misconduct that led to the misstatement. This is another important area to follow closely, involving both SEC and stock exchange rule making. Companies may wait for the final rules before adopting or amending a clawback policy for the purposes of complying with this Dodd-Frank Act requirement (although some companies may chose to adopt some form of clawback provision before then, to the extent they perceive a corporate governance benefit from doing so).

Vote Reporting by Institutional Investment Managers. While the SEC proposed rules in October 2010 requiring institutional investment managers to disclose how they voted on executive compensation, final rules have not yet been adopted. When this reporting requirement is finalized, the reports will be a resource that companies can use to gauge how some large institutional shareholders feel about a company's executive compensation program. When such reports become available, companies may wish to review them to determine where targeted investor outreach on executive compensation issues may be productive.

Proxy Access and Shareholder Proposals

The US Court of Appeals for the District of Columbia vacated Rule 14a-11 under the Exchange Act, which was the SEC's proxy access rule. This rule would have required public companies to include shareholder nominees for director in company proxy materials in certain circumstances. Although its proxy access rule was vacated, the SEC's amendment of Rule 14a-8, the shareholder proposal rule, became effective on September 20, 2011. As amended, Rule 14a-8(i)(8) no longer provides a basis for companies to exclude from their proxy materials shareholder proposals to amend governing documents relating to nomination procedures implementing proxy access or disclosures relating to shareholder nominations, subject to specified exceptions in the rule.

As a result of the SEC's proxy access rule being struck down, proxy access during the 2012 proxy season was addressed on a company-by-company basis through the shareholder proposal mechanism—a procedure sometimes referred to as private ordering. While nomination procedures no longer provide grounds to exclude proxy access shareholder proposals, other grounds for excluding shareholder proposals from an issuer's proxy statement can apply to proxy access proposals, when applicable.

During the 2012 proxy season, some proxy access proposals were successfully excluded because they (i) contained multiple proposals, (ii) described ownership requirements by cross-referencing SEC rules in a manner that made the proposal impermissibly vague or (iii) created conflicts with existing bylaw provisions. Many of the issues that provided grounds for proxy access shareholder proposals to be successfully excluded from issuer proxy statements during 2012 are matters that proponents can rectify when drafting proposals for the 2013 proxy season. As a result, it is likely that it will be more difficult to exclude proxy access shareholder proposals from 2013 proxy statements.

A company receiving a proxy access shareholder proposal should promptly evaluate it for procedural deficiencies—such as being received after the deadline, being submitted by someone who does not meet the eligibility requirements, being too long or constituting multiple proposals—so that the company has time to comply with the steps necessary to seek exclusion of the proposal from its proxy statement on procedural grounds. The company should also analyze whether any of the non-procedural bases set forth in Rule 14a-8(i) provide an argument for exclusion of the specific proposal received.

Companies receiving proxy access shareholder proposals may want to consider including management proxy access proposals in their proxy statement containing terms which they find more acceptable. A shareholder proposal is excludable if it conflicts with a management proposal appearing in the same proxy statement. Before taking that step in response to a proxy access shareholder proposal, however, a company may want to assess with a proxy solicitor and/or its investor relations department what the likelihood would be for that shareholder proposal to be approved. Also, such companies should realize that even if they are able to exclude a proxy access shareholder proposal by including a management proposal on that subject, shareholders in future years could submit proposals to amend the proxy access provisions so adopted.

Specialized Disclosures

Conflict minerals. As required by the Dodd-Frank Act, the SEC adopted a final rule regarding disclosure of the use of conflict minerals originating in the Democratic Republic of the Congo or an adjoining country. The conflict minerals disclosure rule applies to any company that files reports with the SEC under Section 13(a) or Section 15(d) of the Exchange Act if conflict minerals are necessary to the functionality or production of a product manufactured or contracted to be manufactured by that company. The disclosure requirements apply to foreign private issuers as well as to domestic issuers and to smaller reporting companies. There is no *de minimis* exception.

The centerpiece of the final conflict minerals rule is Form SD, a new form created specifically for specialized disclosures. Form SD, if required for conflict minerals disclosure, is prepared on a calendar year basis, regardless of a company's fiscal year, and is due on May 31 of each year, commencing May 31, 2014. Depending on the factual circumstances, a company may be required to engage in supply chain due diligence, obtain an independent private sector audit relating to its due diligence and prepare a Conflicts Mineral Report as an exhibit to its Form SD filing. Although the conflict minerals disclosure is not part of the annual report process, the reports due in 2014 will relate to the entire 2013 calendar year, so companies subject to the rule should consider implementing conflict minerals disclosure controls and procedures before the end of 2012.

Determining whether, and to what extent, a company is required to make conflict minerals disclosure involves a three-step process. The first step involves an analysis of whether a company is subject to the rule. If so, the second step is to conduct a reasonable country of origin inquiry to determine whether the conflict minerals originated in the Democratic Republic of the Congo or an adjoining country. Depending upon the outcome of that inquiry, the company may be required to proceed to the third step, which involves supply chain due diligence and may require the preparation of a Conflict Minerals Report. For more information regarding the conflict minerals disclosure rules, see our Legal Update dated September 5, 2012, entitled "US Securities and Exchange Commission Adopts Final Conflict Minerals Disclosure Rule."[3]

Mine Safety. The Dodd-Frank Act requires companies that filed periodic reports under the

Exchange Act to disclose mine safety and health standards in their annual and quarterly reports filed with the SEC. In addition, mining companies that are subject to Form 8-K requirements must file a Form 8-K when they receive certain notices from the Mine Safety and Health Administration. Final SEC mine safety rules became effective on January 27, 2012. The rules require domestic and foreign issuers to disclose specified mine safety violations on a mine-by-mine basis in their annual reports. Domestic issuers must also disclose such information in their quarterly reports. The new rules also added Item 1.04 to Form 8-K to report certain mine safety orders or notices. For further information about the mine safety disclosure rules, see our Legal Update dated January 26, 2012, entitled "U.S. Securities and Exchange Commission Adopts Dodd-Frank Mine Safety Rules."[4]

Resource Extraction Issuers. Resource extraction issuers, i.e., oil, natural gas and mining companies that file annual reports with the SEC, will need to file a Form SD with the SEC to disclose certain information on payments they make to the US government and foreign governments for the purpose of the commercial development of oil, natural gas or minerals. This report must be filed not later than 150 days after the end of their fiscal year. While most resource extraction issuers will not need to file a Form SD until 2014, affected companies should nonetheless begin a review of their systems and controls for financial accounting and financial reporting to determine what additional procedures and processes they may need in order to report the payments required to be disclosed. For further information about this requirement, see our Legal Update dated September 4, 2012, entitled "SEC Adopts Dodd-Frank Resource Extraction Payments Disclosure Rules."[5] On October 10, 2012, a lawsuit was filed challenging both the rules adopted by the SEC and the statutory provision authorizing the rule. The SEC has not yet responded to the litigation so it remains unclear whether implementation of the rule will be delayed pending the outcome of the litigation.[6]

Recent SEC Interpretations

Cybersecurity. Although there are no current disclosures rules expressly relating to cybersecurity, the staff of the SEC's Division of Corporation Finance identified existing regulations that it believes can require disclosure of cybersecurity risks and cyber incidents in CF Disclosure Guidance: Topic No. 2, entitled, "Cybersecurity."[7] For example, the staff stated that if the risk of cyber incidents is among the most significant factors that make an investment in the company's securities risky, cybersecurity should be disclosed as part of risk factors. The cybersecurity risk disclosure would need to describe the nature of the material risks in this area and how each such risk affects the company. To place the risk in context, the company may need to disclose known or threatened cyber incidents.

According to the staff's cybersecurity disclosure guidance, cybersecurity risks and cyber incidents would need to be described in the management's discussion and analysis if the costs or other consequences represent an event, trend or uncertainty that is reasonably likely to have a material effect on results of operations, liquidity or financial consideration, or cause reported financial information to be not indicative of future results or conditions. MD&A disclosure would also be needed if it is reasonably likely that a cyber attack could lead to reduced revenues or increased protection costs, if material. If a company's products, services, customer or supply relationships or competitive conditions are materially affected by cyber incidents, disclosure would be needed in the business section.

The staff noted that litigation regarding a cyber incident may need to be disclosed. The staff also identified situations that could require disclosures in financial statements prior, during

or after a cyber incident. If cyber incidents pose a risk to a company's ability to record, process, summarize and report information required in SEC filings, the staff suggested that management should consider whether there are any deficiencies in the company's disclosure controls and procedures that need to be addressed.

Cybersecurity disclosures were raised by the staff in comments on annual reports for the year ended December 31, 2011.[8] In issuing these comments, the SEC not only reviewed disclosures contained in filed periodic reports, but, in some cases, based comments on other public information, such as material posted on the company's website.

When preparing upcoming annual reports, it would be prudent for public companies to review the staff's cybersecurity guidance to determine whether cybersecurity is a topic that they need to address.

Sovereign Debt. In CF Disclosure Guidance: Topic No. 4, entitled, "European Sovereign Debt Exposures,"[9] the staff of the SEC's Division of Corporation Finance provided disclosure guidance directed at financial institutions regarding debt exposure in European countries experiencing a higher risk of default. The staff indicated that such exposure should be provided separately by country, with sovereign and non-sovereign exposures segregated. The staff also suggested that companies consider separately disclosing their gross unfunded commitments. Finally, the staff suggested that companies provide information regarding hedges in order to present an amount of net funded exposure.

The guidance suggested specific items to be considered with respect to gross funded exposure (including countries, type of counterparty and categories of financial instruments), unfunded exposures, total gross exposures (funded and unfunded), effects of credit default protection to arrive at next exposure, other risk management disclosures and post-reporting date events. Companies with direct or indirect exposures to sovereign debt should review this guidance when preparing their upcoming annual reports.

Iran Sanctions Disclosure

The Iran Threat Reduction and Syria Human Rights Act of 2012 requires any company that is required to file annual or quarterly reports under Section 13(a) of the Exchange Act (which includes companies listed on a US securities exchange) to disclose in those reports whether, during the period covered by the subject report, it or any affiliate has knowingly engaged in certain sanctionable activities relating to:

- Development of Iran's petroleum resources, production of refined petroleum products in or exportation of refined petroleum products from Iran, or development of Iran's weapons of mass destruction (WMD) or other military capabilities, as described in Section 5(a) or (b) of the Iran Sanctions Act of 1996;
- Financial institutions facilitating terrorist organizations or acts, sanctioned-party activities, WMD development or other prohibited activities in Iran as described in the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA);
- Financial institutions engaging in transactions benefitting the Iranian Revolutionary Guard Corps, as described in Section 104(d)(1) of CISADA;
- Transfers of goods or technologies to Iran that are likely to be used to commit human rights abuses, as described in Section 105A of CISADA;
- Transactions with terrorists whose property is blocked pursuant to Executive Order 13224;
- Transactions with WMD proliferators whose property is blocked pursuant to Executive Order 13382; and
- Transactions with the government of Iran as defined in Section 560.405 of Title 31 of the Code of Federal Regulations, without specific authorization of the government of the United States.

The required disclosure would need to include a description of each such activity, specifying the nature and extent of the activity, the gross revenues and net profits attributable to the activity, if any, and whether the issuer or affiliate intends to continue the activity.

If an issuer is required to report this activity in its annual or quarterly report, it must also separately file with the SEC, at the same time it files its annual or quarterly report, a notice that such disclosure is contained in the report. Upon receiving such a notice, the SEC must promptly transmit the report to the President and to certain House and Senate committees. Upon being so notified, the President must initiate an investigation to determine whether the reported activities violate any Iran sanctions and accordingly penalties should be imposed as a result of the reported activities.

The new law does not expressly define affiliate. However, given other provisions of the new law, the term should be viewed as encompassing foreign subsidiaries. And, unless the SEC provides other guidance in this area, it is reasonable to conclude that the affiliate concept used in other SEC rules would apply, which could subject public companies to disclosure responsibilities for actions taken by controlling persons such as directors, officers and large stockholders.

Because the activities identified above must be reported in annual reports, the disclosure will be subject to liability under Section 18 of the Exchange Act and covered by the CEO and CFO certifications. Therefore, public companies should consider whether they need to adopt a disclosure control designed to determine if any reportable activities by affiliates have occurred.

The disclosure obligation imposed by this Act is effective for quarterly and annual reports filed after February 6, 2013. Therefore, it is applicable to upcoming annual reports for calendar year companies. For more information concerning the ramifications of this act, see our Legal Update dated August 14, 2012 entitled "United States Enacts New Round of Iran Sanctions."[10]

XBRL

The staff of the SEC's Division of Risk Strategy and Financial Innovation has published several observations from reviews of interactive financial data, the most recent in December 2011.[11] These reports provide useful guidance regarding practices for implementing XBRL. In addition, both the Division of Corporation Finance and the Office of Interactive Disclosure have published FAQs.[12]

When XBRL rules first became mandatory, Item 406T of Regulation S-T provided a temporary exemption from liability for the interactive data files where there was a good faith attempt to comply with the rule and a prompt amendment upon the filer becoming aware of non-compliance. However, Item 406T was expressly made a temporary section. It provides liability protection only for interactive date files submitted to the SEC less than 24 months after the electronic filer first was required to submit an interactive data file to the SEC, not taking into account any grace period. Thereafter, an interactive data file is subject to the same liability provisions as the related official SEC filing. Companies that have been providing interactive data for 24 months or more should recognize that XBRL compliance errors could potentially give rise to liability. Rule 406T expires on October 31, 2014.

PCAOB Audit Committee Communications Requirements

In August 2012, the Public Accounting Oversight Board adopted Auditing Standard No. 16, *Communications with Audit Committees* subject to SEC approval. Once approved by the SEC, Auditing Standard No. 16 will supersede AU section 380, *Communication With Audit Committees*, and AU section 310, *Appointment of the Independent Auditor*. Because the PCAOB anticipates that this new auditing standard will

be effective for audits of fiscal years beginning on or after December 15, 2012, the new standard will not impact audits of current fiscal years, although it is possible that some audit firms might increase their communications with audit committees before then.

Item 407(d)(3)(i)(B) of Regulation S-K, describing the requirements of the audit committee report that must be contained in proxy statements, still references AU section 380 with respect to communications between the audit committee and the auditors. Presumably, the SEC will change this reference to Auditing Standard No. 16 before that standard is effective. Ultimately, therefore, the wording of the audit committee report may need to change when describing such communications, but not during the 2013 annual report and proxy season.

For further information about the new PCAOB audit committee requirements, see our Legal Update dated August 27, 2012 entitled "Public Accounting Oversight Board Pronouncements Regarding Communications with Audit Committees and PCAOB Inspection Information."[13]

Director and Officer Questionnaires

Companies should consider adding a question on their directors and officers questionnaires to determine if their directors or officers have any business or personal relationships with a compensation consultant retained, or proposed to be retained, by the company or the compensation committee.

Although final compensation committee independence standards may not be finalized until after the 2013 annual report and proxy season, compensation committee independence questions may be helpful for compensation committee composition planning purposes. Based on Rule 10C-1 and the proposed NYSE and Nasdaq listing standards, questions could be added to the directors and officers questionnaires to elicit information concerning the source of compensation committee members' compensation and whether a compensation committee member is affiliated with the company, any subsidiaries of the company or any affiliate of a subsidiary of the company.

As a disclosure control with respect to the upcoming requirement of the Iran Threat Reduction and Syria Human Rights Act of 2012, companies may want to add questions to their directors and officers questionnaires addressing the sanctionable activities identified by that act. Because the directors and officers may be construed as affiliates, the questions should ask about their activities, as well as what they know about company activities.

If you have any questions regarding the 2013 proxy and annual report season, please contact the author of this Legal Update, Laura D. Richman, at +1 312 701 7304, or any of the lawyers listed below or any other member of our Corporate & Securities group.

David S. Bakst
+1 212 506 2551
dbakst@mayerbrown.com

John P. Berkery
+1 212 506 2552
jberkery@mayerbrown.com

Edward S. Best
+1 312 701 7100
ebest@mayerbrown.com

Bernd Bohr
+44 20 3130 3640
bbohr@mayerbrown.com

Robert E. Curley
+1 312 701 7306
rcurley@mayerbrown.com

Paul De Bernier
+1 213 229 9542
pdebernier@mayerbrown.com

Marc H. Folladori
+1 713 238 2696
mfolladori@mayerbrown.com

Robert F. Gray
+1 713 238 2600
rgray@mayerbrown.com

Lawrence R. Hamilton
+1 312 701 7055
lhamilton@mayerbrown.com

Michael L. Hermsen
+1 312 701 7960
mhermsen@mayerbrown.com

Philip J. Niehoff
+1 312 701 7843
pniehoff@mayerbrown.com

Dallas Parker
+1 713 238 2700
dparker@mayerbrown.com

Elizabeth A. Raymond
+1 312 701 7322
eraymond@mayerbrown.com

Laura D. Richman
+1 312 701 7304
lrichman@mayerbrown.com

David A. Schuette
+1 312 701 7363
dschuette@mayerbrown.com

Jodi A. Simala
+1 312 701 7920
jsimala@mayerbrown.com

Frederick B. Thomas
+1 312 701 7035
fthomas@mayerbrown.com

J. Kirk Tucker
+1 713 238 2500
ktucker@mayerbrown.com

Endnotes

[1] The NYSE proposed rule change is available at http://www.nyse.com/nysenotices/nyse/rule-filings/pdf?file_no=SR-NYSE-2012-49&seqnum=2 and the Nasdaq proposed rule change is available at http://nasdaq.cchwallstreet.com/NASDAQ/pdf/nasdaq-filings/2012/SR-NASDAQ-2012-109.pdf.

[2] Available at http://www.mayerbrown.com/SEC-Adopts-Compensation-Committee-Listing-Standards-and-Compensation-Consultant-Disclosure-Rules-06-28-2012/

[3] Available at http://www.mayerbrown.com/US-Securities-and-Exchange-Commission-Adopts-Final-Conflict-Minerals-Disclosure-Rule-09-05-2012/.

[4] Available at http://www.mayerbrown.com/publications/US-Securities-and-Exchange-Commission-Adopts-Dodd-Frank-Mine-Safety-Rules-01-26-2012/.

[5] Available at http://www.mayerbrown.com/SEC-Adopts-Dodd-Frank-Resource-Extraction-Payments-Disclosure-Rules-09-04-2012/.

[6] See *American Petroleum Institute et al. v. Securities and Exchange Commission*, case number 1:12-cv-01668, in the US District Court for the District of Columbia.

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

[8] For example, Amazon, American International Group, Google, Eastman Chemical, Hartford Financial Services Group and Quest Diagnostics each received cybersecurity comments from the SEC during 2012.

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

[10] Available at http://www.mayerbrown.com/United-States-Enacts-New-Round-of-Iran-Sanctions-08-14-2012/

[11] See http://www.sec.gov/spotlight/xbrl/staff-review-observations-121311.shtml

[12] See http://www.sec.gov/divisions/corpfin/guidance/interactivedatainterp.htm and http://www.sec.gov/spotlight/xbrl/staff-interps.shtml.

[13] Available at http://www.mayerbrown.com/Public-Accounting-Oversight-Board-Pronouncements-Regarding-Communications-with-Audit-Committees-and-PCAOB-Inspection-Information-08-27-2012/.

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