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# Client Alert

## Public Company Update: SEC Director Comments on Latest Executive Compensation Disclosures

by David R. Lamarre

**The Director of the SEC's Division of Corporation Finance, John White, recently provided a preview of the areas that are under particular scrutiny, as the SEC's Staff reviews the first wave of proxy statements filed under the new executive compensation disclosure rules.<sup>1</sup>**

**Review Report in Fall 2007.** As is well known, the Division has placed a high priority on its review of this Spring's proxy statements. In his recent remarks, Director White confirmed that the SEC will publish a report on those reviews this Fall. The rest of his speech provided some "early snapshots" (as he put it) of how the Director feels the rules are working in practice.

**"Analysis (Or Lack Thereof)" in CD&A.** Mr. White noted the complaints from some analysts and investors that the new Compensation Discussion and Analysis sections have given short shrift to "analysis" – the "A" in "CD&A." He encouraged companies to see the new CD&A as an *opportunity* to explain their compensation policies, and to help investors make sense of the detailed tables and other information that the new rules require. He also emphasized that "When we look at your CD&A disclosures, Corporation Finance will be looking to see if you've answered the 'how'...and the 'why' questions rather than merely the 'who, what, where and when'." However, in response to suggestions that the SEC amend its rules to require specific analyses in CD&A (and to that extent, move away from the new rules' overall "principles-based" approach), the Director related that "I have my own doubts about the effectiveness of such an approach. I cannot say, obviously, that the time will never come for such a rule change, but in my opinion, we are not there yet."

<sup>1</sup> May 3, 2007 speech, transcribed at <http://www.sec.gov/news/speech/2007/spch050307jww.htm>. See SEC Release No. 33-8732A, "Executive Compensation and Related Person Disclosure," August 29, 2006, available at [www.sec.gov/rules/final/2006/33-8732a.pdf](http://www.sec.gov/rules/final/2006/33-8732a.pdf), and our September 8, 2006 bulletin, "SEC Adopts New Rules for Executive Compensation and Related Party Disclosure," available on [www.pillsburylaw.com](http://www.pillsburylaw.com).

**Length and Density of Disclosures.** Director White also alluded to the recent publicity about the sheer length of some recent proxy statements, and commentary calling for less detail rather than more. In response, he expressed the view that detailed disclosure is not objectionable so long as it is organized in appropriate “layers,” permitting an investor who is interested in one topic to easily find the relevant details (while permitting other investors to ignore that topic, as they see fit). In his words, CD&A should be seen as “the top layer,” providing context and a “guide” to the detailed disclosures that follow.

**Performance Targets.** Director White also noted the large number of companies whose most recent proxy statements did not disclose specific performance targets for executive incentives, ostensibly on grounds of competitive sensitivity. Some investors, he said, have complained that many of these omissions seem inconsistent with the new disclosure rules. He stated that the Staff would be “taking a hard look” at this, since (in his view) investors feel that this disclosure is important. Even where the company is justified in omitting specific targets under the new rules, Director White also appears to feel that relatively few companies have provided an adequate indication of how difficult the (undisclosed) targets would be to achieve. Investors, he said, “want to know whether or not the targets are real targets or are more akin to shadows and are going to result in essentially guaranteed awards,” which may require more specific disclosure than (e.g.) statements that the targets are intended to be difficult to achieve. His remarks strongly suggested that this will be an area of focus in Staff reviews, and could well be the subject of rulemaking to “recalibrate the rules.”

**Disclosure about the role of the CEO.** The Director also stated that he has some “initial concerns” about the extent to which proxy statements contain sufficiently “robust” disclosure about CEOs’ roles in their companies’ compensation processes. He encouraged companies (and their CEOs) to focus on questions such as:

- Did the CEO have the ability to call or attend even portions of compensation committee meetings?
- Did she meet with any consultants used by the compensation committee?
- Did the CEO retain or have access to any other compensation consultants who influenced the company’s executive compensation?
- What input did the CEO have as compensation packages were being crafted?

This appears to be another area of Staff focus.

**General Level of Staff Scrutiny.** More generally, the Director’s remarks evinced some sympathy for the fact that this has been the first year for companies to prepare disclosures under a “principles-based” approach – and CD&A, in particular. However, while he did state that the Division would have “sensitivity and respect for the principles-based nature of the new disclosure regime,” Director White warned that that does not mean that the Staff will not “ask hard questions” or refrain from commenting on perceived disclosure deficiencies: “As with our review process generally, some of our comments will be satisfied by future disclosures, but some companies may find themselves needing to file amended Reports on Form 10-K this year. We are taking all of this very seriously,” he added.

**Expectations for Next Year.** Director White also noted that “Our expectations for the second year will be higher.” Public companies will be well advised to allow extra time, when planning for their 2008 proxy statements, to permit them to resolve any Staff comments on this year’s proxy statement – and even if not previ-

ously reviewed, to revisit their 2007 disclosures in light of the Fall 2007 review report, the Director's remarks, and any other public statements by the Staff.

### Live Links

Speech by SEC Staff: Keeping the Promises of Leadership and Teamwork: The 2007 Proxy Season and Executive Compensation Disclosures; U.S. Securities and Exchange Commission; May 3, 2007

Executive Compensation and Related Person Disclosure; Securities and Exchange Commission; August 29, 2006 (436-page PDF)

SEC Adopts New Rules for Executive Compensation and Related Party Disclosure, Pillsbury Winthrop Shaw Pittman LLP Client Alert; September 8, 2006 (13-page PDF)

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