

# NYSE Proposes New Compensation Committee Listing Standards

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## Standards implement Dodd-Frank requirements without additional bright line tests

On October 1, 2012, the New York Stock Exchange amended its proposed listing standards issued on September 25, 2012 regarding compensation committees and their advisers, as called for by new SEC Rule 10C-1 under the Securities Exchange Act of 1934, which in turn was mandated by the Dodd-Frank Act.

**Committee Independence.** The NYSE proposes to retain its current general independence standards for directors, which include certain bright line tests as well as requiring that the Board of Directors make an affirmative determination that "the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company)." The Exchange is not proposing to add any new bright line independence criteria in response to SEC Rule 10C-1. Instead, it is proposing to amend the general standard to require that in making its independence determinations with respect to compensation committee members, the Board must consider "all factors specifically relevant to determining whether a director has a relationship to the listed company which is material to that director's ability to be independent from management in connection with the duties of a compensation committee member," including the factors identified in Rule 10C-1. These factors are:

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

Thus, rather than identifying specific factors, the NYSE repeats the factors identified in SEC Rule 10C-1 (which restates the factors listed in the Dodd-Frank Act) and shifts the onus to the listed company to determine if there are any other factors relevant to compensation committee independence.

The NYSE commentary states that when considering the sources of a director's compensation, the Board should consider whether the source of the compensation would impair the director's ability to make independent judgments about the company's executive compensation. Similarly, when considering the director's affiliate relationships, the Board should consider whether the relationship places the director under the direct or indirect control of the listed company or its senior management, or creates a direct relationship with senior management, that would impair the director's ability to make independent judgments about the company's executive compensation. The NYSE release also states the Exchange's belief that rather than being a negative factor, share ownership in the listed company is a positive factor for compensation committee members because all shareholders have the same economic interest in ensuring that executive compensation is not excessive.

**Compensation Committee Advisers.** Previously-adopted NYSE listing standards contained provisions substantially similar to those of SEC Rule 10C-1 regarding committee authority to retain compensation advisers. The NYSE proposed listing standards delete the prior provisions and replace them with a largely verbatim statement of the requirements of Rule 10C-1 regarding the committee's authority to retain advisers and its responsibility to consider the independence of any such advisers. These requirements are as follows:

- The compensation committee must have the ability, in its sole discretion, to retain or obtain the advice of a compensation consultant, independent legal counsel, or other adviser (collectively, "compensation advisers").
- The compensation committee must be directly responsible for the appointment, compensation, and oversight of the work of any compensation adviser that it retains.
- The listed company must provide adequate funding, as determined by the compensation committee, for payment of reasonable compensation to compensation advisers retained by the committee.
- Before selecting or obtaining advice from a compensation adviser (other than in-house legal counsel), the committee must consider "all factors relevant to that person's independence from management," including the following:
  - The provision of other services to the listed company by the person that employs the compensation adviser (the "consulting entity").
  - The amount of fees received from the listed company by the consulting entity as a percentage of its total revenue
  - The policies and procedures of the consulting entity that are designed to prevent conflicts of interest.
  - Any business or personal relationship of the individual compensation adviser with a member of the compensation committee.
  - Any stock of the listed company owned by the individual compensation adviser (which standard has been interpreted in the SEC release as including stock owned by their immediate families).
  - Any business or personal relationship of the individual compensation adviser or the consulting entity with an executive officer of the listed company.

As with the listing standard regarding committee member independence, the NYSE does not add to the factors listed in SEC Rule 10C-1, but expands on the rule by providing that listed companies are to consider any additional factors that may be relevant to a compensation adviser's independence from management.

The provisions regarding compensation advisers are required to be set forth in the compensation committee charter.

**Cure Periods.** Consistent with Rule 10C-1, the NYSE is proposing to allow a compensation committee member who ceases to be independent for reasons outside his or her reasonable control

to remain a member of the compensation committee until the earlier of the company's next annual meeting or one year from the event that caused the loss of independence, provided the company notifies the Exchange of the loss of independence. However, the NYSE proposes to limit this cure period to circumstances where the committee continues to have a majority of independent directors.

**Exemptions from Listing Standards.** Companies currently exempt from the NYSE's compensation committee listing standards would continue to be exempt from the revised standards. These include "controlled companies," defined as companies of which more than 50% of the voting power for the election of directors is held by an individual, group or another company. Foreign private issuers are permitted to follow their home country practices instead of the NYSE requirements if they publicly disclose (in the manner required by NYSE listing standards) the significant differences between the NYSE listing standards and the home country practices followed instead.

Companies that subsequently become subject to the listing standards, for example upon an IPO or on emergence from bankruptcy, would be generally subject to the existing phase-in schedules for committee member independence.

**Smaller Reporting Companies.** Smaller reporting companies that are listed on the NYSE are currently subject to the compensation-related listing standards. The Exchange is proposing to continue this treatment with the exception that smaller reporting companies would be exempt from the new compensation committee independence provisions of Rule 10C-1 as well as from the requirement that the committee consider the independence of its compensation advisers.

**Effective Dates.** The NYSE is proposing that the changes to its listing standards would generally become operative on July 1, 2013, but that the additional independence standards for compensation committee members would not become effective until the earlier of (i) the first annual meeting after January 15, 2014, or (ii) October 31, 2014.

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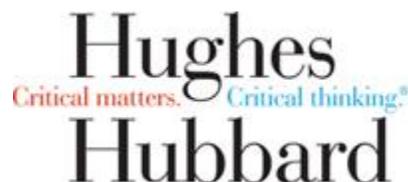
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