

**MEMO# 25065**

April 5, 2011

# **SEC Proposal Regarding Listing Standards for Compensation Committees; Your Comments Requested by April 13th**

[25065]

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TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 18-11  
ETF ADVISORY COMMITTEE No. 21-11  
SEC RULES COMMITTEE No. 27-11 RE: SEC PROPOSAL REGARDING LISTING STANDARDS FOR COMPENSATION COMMITTEES; YOUR COMMENTS REQUESTED BY APRIL 13TH

The Securities and Exchange Commission recently issued a proposal to implement Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. This provision, which added Section 10C to the Securities Exchange Act of 1934, requires the Commission to adopt rules directing the national securities exchanges to prohibit the listing of any equity security of an issuer that is not in compliance with Section 10C's compensation committee and compensation adviser requirements. [\[1\]](#) According to the Release, in enacting Section 10C, Congress intended to require that board committees that set compensation policy consist only of independent directors and to provide shareholders of public companies with additional disclosure involving compensation practices.

Although compensation committees generally are used by operating companies, the proposal also generally would apply to registered investment companies. The Release requests comment on whether the Commission should: (1) exempt any types of issuers, such as registered management investment companies, from some or all of the requirements of Section 10C; or (2) defer to the exchanges for exemptions from Section 10C's requirements. [\[2\]](#) The Release also specifically notes that open-end and closed-end management investment companies registered under the Investment Company Act are generally exempt from current exchange listing standards that require listed issuers to either have a compensation committee or to have independent directors determine, recommend, or oversee specified executive compensation matters. [\[3\]](#)

Comments on the proposal are due to the Commission by April 29th. ICI will be drafting a

comment letter seeking an exemption for registered investment companies. If you have any comments that you would like to be considered for inclusion in the comment letter, please email them to Dorothy Donohue at [ddonohue@ici.org](mailto:ddonohue@ici.org) as soon as possible, but no later than April 13, 2011.

The proposal is summarized below. [\[4\]](#)

**Applicability of Listing Requirements.** The exchanges would be required to adopt listing standards that would be applicable to any committee of the board that oversees executive compensation, whether or not formally designated as a compensation committee.

**Independence Requirements.** Each member of a compensation committee would be required to be a member of the issuer's board of directors and independent. The exchanges would be required to develop a definition of independence applicable to members of the compensation committee after considering certain factors. [\[5\]](#) Open-end management investment companies registered under the Investment Company Act of 1940 are exempt from this requirement. [\[6\]](#)

**Compensation Advisers.** A compensation committee of a listed issuer would be permitted, in its sole discretion, to retain, or obtain the advice of, a compensation consultant, independent legal counsel, or other adviser. [\[7\]](#) Each listed issuer would be required to provide for appropriate funding for payment of reasonable compensation to these entities. The compensation committee would be required to consider certain enumerated independence factors before selecting a compensation adviser, legal counsel or other advisers to the committee.

**Opportunity to Cure Defects.** The exchanges would be required to establish procedures (if their existing procedures are deemed inadequate) for an issuer to have a reasonable opportunity to cure any noncompliance with Section 10C's requirements before its securities could be delisted.

**Implementation of Listing Requirements.** The exchanges would be required to issue, or modify, their rules, subject to Commission review, to conform their listing standards to any rules that the Commission adopts as a result of the proposal.

**Exemptive Authority.** Section 10C(f)(3) of the Exchange Act provides that the Commission's rules shall authorize the exchanges to exempt any category of issuer from the requirements of Section 10C. The Release notes that the Commission is preliminarily of the view that it should be up to the exchanges to propose the categories of issuers to be exempted from Section 10C's requirements, subject to Commission review in the rule filing process. The Release explains that the exchanges may be in the best position to identify the types of common relationships that are likely to compromise the ability of an issuer's compensation committee to make impartial determinations on executive compensation. Likewise, the exchanges may be in the best position to determine the types of issuers that should be exempted from the other compensation committee listing requirements. Therefore, the Commission did not propose exempting any issuer or any relationship from the rules implementing Section 10C, (other than exempting certain issuers, including open-end investment companies, from compensation committee independence requirements, as described above).

**Compensation Consultant Disclosure and Conflicts of Interest.** Section 10C(c)(2) of the Exchange Act requires each issuer to make certain disclosures with respect to

compensation committees in any proxy material for a shareholder meeting,. The Release notes that the disclosure is required to appear in response to Item 407 of Regulation S-K, which does not apply to registered investment companies. [8]

Transition and Timing. Dodd-Frank requires the Commission to issue rules directing the exchanges to prohibit the listing of issuers not in compliance with Section 10C by July 16, 2011. According to the Release, the Act did not establish a specific deadline by which the related exchanges' listing standards must be in effect. The Commission proposes requiring each exchange to: (i) provide the Commission proposed rules or rule amendments that comply with the Commission's final rule no later than ninety days after publication of the Commission's final rule in the Federal Register; and (ii) have final rules approved by the Commission in place no later than one year after publication of a final Commission rule in the Federal Register. Section 10C(c)(2)'s compensation consultant and conflict of interest disclosures would not be required for proxy statements filed in definitive form before the effective date of Commission rules implementing Section 10C(c)(2).

Dorothy M. Donohue  
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#### **endnotes**

[1] See SEC Release Nos. 33-9199; 34-64149, dated March 30, 2011, which is available at <http://www.sec.gov/rules/proposed/2011/33-9199.pdf> ("Release"). The Release states that Section 10C does not require a listed issuer to have a compensation committee or a committee that performs functions typically assigned to a compensation committee. The Release further states that Commission rules do not currently require, and the proposal would not mandate, that an issuer establish a compensation committee.

[2] See Release at p. 41.

[3] See NYSE Listed Manual Section 303A.00; Nasdaq Rule 5615(a)(5); NYSE Arca Rule 5.3; and NYSE AMEX LLC Company Guide Section 801.

[4] New Exchange Act Rule 10C-1 would implement the compensation committee listing requirements, and amendments to Regulation S-K would require disclosure related to compensation consultants.

[5] The Release states that the Commission has proposed deferring to the exchanges, rather than proposing, to exempt any relationships from the independence requirements.

[6] The Release notes that current exchange listing standards generally require listed issuers (other than registered management investment companies) either to have a compensation committee or to have independent directors oversee compensation matters.

[7] The Release states that the Commission does not construe Dodd-Frank as requiring compensation committees to hire independent legal counsel or the other named advisers.

[8] See Release at note 101.

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