

August 25, 2011

ASSOCIATION OF CORPORATE COUNSEL

Back to School CLE Symposium

DODD-FRANK ACT—IMPACT ON PUBLIC COMPANIES

Seminar Discussion Outline

- Overview of Dodd-Frank and Other Changes for Disclosure and Governance Requirements
 - Compensation Matters
 - Proxy Access
 - Governance Matters
 - Specialized Disclosure Requirements
-



DODD-FRANK OVERVIEW

Overview of New and Upcoming Dodd-Frank Requirements

- Dodd-Frank Wall Street Reform and Consumer Protection Act (“DF”) enacted July 21, 2010
- Changes impact both disclosure and governance matters
- Required rules have been adopted and required rulemaking by SEC, CFTC and exchanges remains in process

Dodd-Frank Overview

- **Compensation-Related Matters: Governance and Disclosure**

- Compensation Committee Independence (*DF 952(a); SEC proposed rule issued March 30, 2011; final rules expected August - December 2011*)
- Compensation Adviser Independence (*DF 952(a); SEC proposed rule issued March 30, 2011; final rules expected August - December 2011*)
- Compensation Clawback Policies (*DF 954; SEC rules delayed, proposed rules expected August - December 2011*)

Dodd-Frank Overview – cont'd

- **Compensation Disclosure**

- Advisory Votes on Compensation (*DF 951; SEC adopted Rule 14a-21; DF 951 requirement effective 1/21/2011*)
- Advisory Vote on Golden Parachutes (*DF 951; SEC adopted Rule 14a-21; S-K Item 402(t)*)
- Pay versus Performance (*DF 953(a); SEC to propose rules, expected August – December 2011*)
- CEO Pay versus Median Employee Pay (*DF 953(b); SEC to propose rules, expected August – December 2011*)
- Employee or Director Hedging Policies (*DF 955; SEC to propose rules, expected August – December 2011*)

- **Say-on-Pay and Say-on-Frequency were effective for the 2011 proxy season**
 - **Review disclosures and disclosure requirements in light of SEC comments**
-

Dodd-Frank Overview – cont'd

- **Other Dodd-Frank Disclosure and Governance Provisions**

- Proxy access (*DF 971; EA 14(a); SEC adopted Rule 14a-11*)
 - SEC rule vacated by court decision
- CEO/Chairman separation policies (*DF 972; SEC adopted disclosure rules in Dec. 2009 – see prior rule in Item 407(h) of Regulation S-K and 2010 proxy disclosure; SEC may update disclosure rules in response to DF provision*)
- Ban on discretionary authority of brokers to vote in election of directors, executive compensation and other significant matters, as determined by SEC (*DF 957; SEC to adopt rules; NYSE already prohibits brokers from exercising discretionary authority with respect to director elections and approval of equity compensation plans*)

Dodd-Frank Overview – cont'd

- Board Oversight of Risk (DF 723 and 763; SEC and CFTC to propose rules) – Approval of Swap Transactions (applicable for issuers, particularly if claiming end-user clearing exception) (SEC has proposed several rules and issued orders delaying effectiveness of many DF provisions)
 - Conflict Minerals Provision (*DF 1502; SEC proposed rule issued 12/15/2010*)
 - Mine Safety Disclosure (*DF 1503; SEC proposed rule issued 12/15/2010*)
 - Resource Extraction Issuer Payments to U.S. federal and foreign governments (*DF 1504; SEC proposed rule issued 12/15/2010*)
 - Rules for 1502, 1503 and 1504 were not effective by statutorily established deadline.
-



COMPENSATION MATTERS

Advisory Vote on Compensation (DF 951; EA 14A(a))

- “Say on Pay” and Frequency Votes
- Dodd-Frank requirement was effective January 21, 2011 (6 months after Act), SEC final Rule 14a-21 adopted January 25, 2011
- Say on Pay and Frequency votes were required in 2011 proxy season
- Requirements for 2011 public company proxy materials
 - **Say on Pay:** separate resolution subject to non-binding, advisory vote, on the compensation of the NEOs as disclosed in CD&A and related compensation tables, to be included
 - for first shareholder meeting occurring after January 21, 2011; and
 - in proxy materials at least once every three years thereafter.
 - **Say on Frequency:** separate proposal for non-binding, advisory vote to determine whether say-on-pay advisory vote should occur at least every one, two or three years, to be included
 - for first shareholder meeting occurring after January 21, 2011; and
 - in proxy materials at least once every six years thereafter.

Say on Pay

- **Compensation for completed fiscal year:** Dodd-Frank requirement covers executive compensation for the completed fiscal year, as disclosed in the proxy.
 - **Effective for 2011 proxy season:** Effective for annual meetings or special meetings for the election of directors occurring after January 21, 2011.
 - **Impact on 2011 proxy statements**
 - **Drafting focus:** Compensation disclosure and CD&A, with clear titles and subtitles, as disclosure is subject to a shareholder vote.
 - **SEC focus:** Full disclosure, compliance with S-K 402, plain English and conciseness. Inclusion of an executive summary to CD&A.
 - **Impact on compensation practices:** Substantively, compensation committees will continue to move away from elements of compensation that are disfavored by ISS, such as perquisites, tax gross-ups and single trigger arrangements upon a change of control.
-

Say on Pay – cont'd

- **Say on Pay proposal**

- **Policies and procedures insufficient:** A proposal to approve the company's compensation policies and procedures is insufficient under the SEC rules; requirement is to solicit stockholder vote on actual compensation as disclosed in the proxy statement.
- **Disclosure regarding prior votes:** CD&A must describe whether and, if so, how a company's compensation policies and decisions have taken into account the results of prior shareholder advisory votes on executive compensation; this disclosure provides a roadmap for activists to monitor a company's compliance with advisory compensation votes.
- **Non-binding vote:** The proxy statement must disclose the non-binding nature of the vote.

Say on Frequency

- **Effective for 2011 proxy season:** Effective for annual meetings or special meetings for the election of directors occurring after January 21, 2011.
- **Format of proxy card**
 - **Single proposal:** Frequency vote must be included in a single proposal, preferably with four boxes on the proxy card: 1 year, 2 years, and 3 years, and abstain.
 - **Discretionary authority:** If the proxy card omits the “abstain” box, the company loses discretionary authority to vote signed proxies as to which no choice is specified.

Say on Frequency – cont'd

- **Board recommendations**

- **Discretionary authority:** The Board is not required to recommend in favor of any particular frequency. However, if no recommendation is made by the Board as to frequency, the company loses discretionary authority to vote signed proxies as to which no choice is specified.
- **Non-binding vote:** The proxy statement should make clear that shareholders are not voting to approve or disapprove the issuer's recommendation, and that the vote is non-binding.

Say on Pay / Say on Frequency

- **Lessons Learned from 2011 Proxy Season**

- Say on Frequency voting standard – majority or plurality
 - Say on Frequency recommendations (Russell 3000/June 23, 2011)
 - Annual 81%
 - Biennial 1%
 - Triennial 18%
 - Say on Pay results (Russell 3000/June 23, 2011)
 - 36 companies failed to receive majority approval
 - 71% of companies had shareholder approval of at least 90%
 - 23% of companies had shareholder approval of between 70% and 90%
 - 6% of companies had shareholder approval of between 50% to 65%
 - 2% of companies had shareholder approval of less than 50%
 - ISS and Glass Lewis recommendations were influential
 - If pay-versus-performance rules are effective for 2012, the importance of the proxy advisors' focus on pay-for-performance will be increased.
-

Advisory Vote on Golden Parachutes (DF 951; EA 14A(b))

- **SEC Rule 14a-21**

- Rule 14a-21 requires a soliciting person to make additional disclosures and seek a non-binding advisory vote in a proxy statement for a meeting (after April 25, 2011) at which shareholders are asked to approve an acquisition, merger, consolidation or proposed sale of all or substantially all of the assets of the issuer.
- Person making the solicitation will be required to disclose any agreements or understandings that the person has with any NEOs of the issuer (or of the acquiring issuer, if such issuer is not the acquiring issuer) concerning any type of compensation that is based on or otherwise relates to the proposed transaction.
 - New table required under item 402(t) of Regulation S-K.
- Limited benefits from proactively subjecting golden parachute arrangements to say-on-pay vote in advance. As of June 23, 2011, only 16 companies had submitted golden parachute arrangements to a say-on-pay vote at an annual meeting.

Pay Versus Performance (DF 953(a); EA 14(i))

- **Dodd-Frank mandates pay versus performance disclosure**
 - **Item 402 of Regulation S-K to be amended:** Dodd-Frank requires amendment of Item 402 disclosure to include pay versus performance.
 - **Disclosure required:** Information that shows the relationship between executive compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends or distributions of the issuer. May include a graphic representation, possibly similar to stock price performance graph.
 - **Where disclosure is required:** Proxy or consent solicitation statements for an annual meeting of shareholders.
 - **When will disclosure be required:** The SEC Staff's current schedule indicates the implementing rules will be proposed in the August - December 2011 timeframe and the final rules adopted in January - July 2012.
 - **Current Focus:** Compensation committees should consider whether the vesting and payment of new awards demonstrates link between pay and performance.

Internal Pay Equity Disclosure (DF 953(b))

- **Dodd-Frank mandates internal pay equity disclosure**
 - **Item 402 of Regulation S-K to be amended:** Dodd-Frank requires the SEC to amend Item 402 to require disclosure of internal pay equity.
 - **Disclosure required:** Registrants must disclose the CEO's total annual compensation, the median total annual compensation of all employees other than the CEO and the ratio of the two amounts.
 - **How compensation is calculated:** Total annual compensation for the CEO and all other employees will be calculated as total compensation in the summary compensation table, as in effect on July 20, 2010.
 - **Where disclosure is required:** Dodd-Frank requires the disclosure to appear in specified filings and documents, including Securities Act registration statements, and Exchange Act periodic and current reports (including annual reports on 10-K), and proxy and information statements.
 - **When will disclosure be required:** The SEC Staff's current schedule indicates the implementing rules will be proposed in the August - December 2011 timeframe and the final rules adopted in January - July 2012.

Internal Pay Equity Disclosure – cont'd

- **The disclosure requirement raises significant issues**
 - **Concerns with calculation of total compensation:** Some companies are expressing concerns that they will be unable to comply with this new disclosure requirement or that compliance will be difficult and costly.
 - Companies may ask the SEC to give companies for which compliance is impossible or impracticable some relief in the rules, but the SEC may not have statutory leeway to grant that relief.
 - **Large employers may face significant challenges:** Companies with large numbers of employees may face problems in determining the median total annual compensation of all employees other than the CEO.
 - Problems include gathering and processing the necessary information on which to make the determination of the median employee total compensation.
 - **Ratios may reflect significant pay “inequities”:** The ratio of many, if not most, companies will reflect a significant differential in CEO and median employee compensation. Ratios of multi-national companies having significant numbers of employees in low wage countries will have their ratios exaggerated by the inclusion of those low wage employees.

Internal Pay Equity Disclosure – cont'd

- **Preparing for internal pay equity disclosure**
 - **Assess pay and personnel data:** Companies should assess their work forces and compensation structures to determine if compliance will present problems or even be possible.
 - **Assess systems:** In particular, companies should consider whether their accounting, payroll and information systems are able to produce the information necessary to prepare the disclosure.
 - **Prepare disclosures and shareholder communications:** Companies should consider and plan for how they will address with their shareholders and employees a ratio that will reflect what will appear to some observers to be a significant pay inequity.
 - **Comment to the SEC:** Companies who find that making internal pay equity calculations will be costly or impossible should send comment letters to the SEC so that practical concerns can be addressed in the final rules.

Compensation Committee Independence (DF 952(a); EA 10C)

- **New Standards:** Now requires EVERY compensation committee member to be “independent”
- **“Independence”:** to be defined by stock exchanges after considering relevant factors, including:
 - source of director’s compensation, including any consulting, advisory or other compensatory fees paid by the issuer; and
 - whether the director is affiliated with the issuer, its subsidiaries or an affiliate.
- **Similar to audit committee independence requirements**
- **Current Focus:**
 - Review compensation committee charter and consider anticipated independence standards
 - Revise D&O questionnaires
 - Evaluate independence of current compensation committee members
 - As discussed below, also identify any relationships or independence concerns with compensation committee consultants or other advisers.

Compensation Adviser Independence (DF 952(a); EA 10C)

- Combination of new governance and disclosure requirements
- Compensation committee may only select a compensation consultant, legal counsel or other adviser after taking into account independence factors to be identified in rules by SEC, including:
 - other services provided to issuer;
 - amount of fees received from issuer;
 - conflict of interest policies;
 - business and personal relationships; and
 - adviser ownership of issuer stock.
- Compensation committee must have the authority, in its sole discretion, to retain or obtain advice of independent legal and other advisers, including compensation consultants.
- Compensation committee must be directly responsible for appointment, compensation and oversight of work of compensation consultant.
- ~~SEC clarifies that the proposed rules relating to “independent legal counsel” are not meant to prevent the compensation committee from conferring with the company’s in-house counsel or outside counsel retained by the company.~~

Compensation Adviser Independence – cont'd

- **Disclosure requirements**

- Proxy materials for annual meetings or special meetings in lieu of annual meetings held after July 20, 2011 must disclose whether:
 - compensation committee retained or obtained advice of a compensation consultant; and
 - the consultant's work raised any conflicts of interest (not defined), and if so, the nature of the conflict of interest and the manner in which it is being addressed.

Compensation Clawback Policies (DF 954; EA 10D)

- **Three-year Clawback:** Dodd-Frank requires exchange-listed issuers to enact clawback policies requiring the recovery of excess incentive-based compensation paid during the three-year period preceding a restatement due to a material non-compliance with financial reporting requirements under securities laws.
- **Expanded Scope:** Requirement is broader than most current voluntarily adopted policies.
- **Broader than SOX:** Requirement differs from SOX, and Dodd-Frank requirement open to many interpretive and legal issues, as noted in table on the following slide.
- **Timeline:** The SEC Staff's current schedule indicates that the implementing rules will be proposed August – December, 2011.

Compensation Clawback Policies - cont'd

- **Current Focus:** Issuers should begin considering existing or contemplated future incentive programs and the potential impact of the new mandatory clawback policy. Consider including provisions in newly adopted plans, award agreements and compensation contracts that the awards and compensation are subject to the provisions of DF and clawback policies adopted by the company in the future.

Compensation Clawback Policies – cont'd

	SOX 304	DF 954
Applicable Officers	CEO/ CFO	Current and former "executive officers"
Look-back period	1 yr following issuance of information restated	3 yrs prior to restatement
Compensation subject to clawback	Bonuses, equity and other incentive based compensation, profits from sales of securities	"Incentive-based compensation" (including stock options awarded as compensation)
Threshold	Misconduct	Material noncompliance with applicable accounting principles (no personal knowledge or participation required)
Right of Action	SEC enforcement actions only	SEC enforcement actions and private, derivative actions on behalf of the issuer

Director and Employee Hedging Policies (DF 955; EA14(j))

- Dodd-Frank mandates that the SEC must require issuers to disclose in their annual meeting proxy statement whether they permit their directors and employees to hedge the risk of their investments in equity securities.
- Dodd-Frank's mandate appears to require disclosure of the policy as to hedging of all equity securities, not just those of the reporting issuer.
- **Timeline:** The SEC Staff's current schedule indicates that the implementing rules will be proposed August – December 2011.
- **Current Focus:** An issuer should assess its policy now and consider what it will have to disclose. If the issuer does not have a policy or the policy allows hedging, the issuer should consider adopting or changing its policy to limit or prohibit hedging, at least by its directors and executive officers.



PROXY ACCESS

Proxy Access (DF 971; EA 14(a); Rule 14a-11)

- **Shareholders and proxy access**

- **What is Proxy Access?:** The term “proxy access” is short-hand for the right of shareholders meeting certain requirements to include their nominees for election as directors in a company’s proxy materials.
- **Dodd-Frank and SEC Rules:** Dodd-Frank authorized, but did not require, the SEC to adopt rules providing for proxy access. The SEC quickly adopted proxy access rules applying generally to companies subject to the proxy rules. The rules were to be effective on November 15, 2010.
- **The SEC rules have been struck down:** The Business Roundtable and U.S. Chamber of Commerce sued the SEC seeking judicial review of the rules. The SEC stayed the rules’ effectiveness pending the judicial review and therefore the rules were not effective for the 2011 proxy season.
 - On July 22, 2011, the U.S. Court of Appeals for the District of Columbia Circuit (“DC Circuit”) vacated Rule 14a-11. The decision is primarily based upon the failure of SEC to properly assess the cost-benefit analysis of the rule. The decision did not affect the amendments to Rule 14a-8.

Proxy Access – cont'd

- **Looking Forward:**

- **SEC's Options:** The SEC may appeal the DC Circuit decision, it may return to the rulemaking process in an effort to address the issues raised by the DC Circuit, or it may forego mandatory proxy access.
 - **Private Ordering Remains:** The amendments to Rule 14a-8 allowing shareholders to propose modifications to the company's governing documents were not affected. The amendments are still subject to the SEC stay. If the SEC lifts the stay, the focus in 2012 may be on shareholder proposals to include proxy access procedures. Consider recent changes in the Delaware General Corporation Laws.
 - **No Effect on 2012 Proxy Season:** It seems unlikely that the proxy access rules will be in effect for the 2012 proxy season.
 - **Review Advance Notice Provisions:** Companies should review their advance notice bylaw provisions to ensure they provide an effective advance notice mechanism for shareholder proposals and shareholder nominations.
-

GOVERNANCE MATTERS

Whistleblower Provisions (DF 922; EA 21F)

- On May 25, 2011, the SEC issued final Regulation 21F to implement the whistleblower directive under DF. The final rule became effective August 12, 2011.
- **Bounty Payments:** To qualify for an award, an individual will have to satisfy and comply with the SEC's requirements:
 - **Eligibility:** Satisfy the eligibility standards. Generally excludes: members, officers or employees of SEC, PCAOB, DOJ and other agencies; auditors and attorneys; internal compliance personnel
 - **Voluntary:** A submission must be voluntarily made. A submission is voluntary if it is made before the whistleblower receives a "request, inquiry or demand" or if the whistleblower does not have a duty to report to the SEC the violation.
 - **Original Information:** The submission must include "original information." Information about a possible violation not already known by the SEC will be considered "original" if derived from the individual's "independent knowledge or independent analysis." Exclusions include information obtained through attorney-client privilege, audits, and received by a person through the entity's oversight process.

Whistleblower Provisions – cont'd

- **Leads to a successful enforcement action:** The original information must lead to a successful enforcement proceeding where the SEC obtains monetary sanctions in excess of \$1 million.
- Designated procedures must be followed and forms are required to be filed to submit information.
- The amount of the award is within a 10% floor and a 30% cap.
- **Retaliation:** A whistleblower who provides information is protected from retaliation, whether or not the SEC brings a successful action.
- **Not required to report internally:** The new rules do not require whistleblowers to report first through the company's internal compliance system in order to be eligible for an award. The SEC does attempt to incentivize internal reporting.

Whistleblower Provisions – cont'd

- **Looking Forward:**


- **Review Policies:** The new rules will likely increase the number of complaints. Companies should review existing procedures and cultivate a culture of compliance.
- **Internal Reporting:** Companies should develop programs that encourage employees to report internally and educate and train employees on the benefits of internal reporting. However, policies cannot purport to restrict whistleblowing to the SEC.
- **Response Plan:** Companies should take action to promote compliance and enhance the chances that the SEC will refer any whistleblower matters to the company for investigation. Establish an action plan that will allow the company to respond quickly to internal whistleblower complaints and SEC notifications.

Board Committee Approval of Certain Swap Transactions (DF 723 and 763; CEA 2(j) and EA 3C)

- Dodd-Frank requires an “appropriate committee” of the board of any public company that engages in derivatives activities to review and approve the decision to enter into “swap transactions” that rely on “commercial end-user” exemptions.
- Dodd-Frank set a goal of one year from enactment (July 16, 2011) for the rules to be implemented. The SEC and CFTC did not complete their rulemaking by this date.
- To avoid market disruptions, the SEC and CFTC issued orders identifying which provisions became effective on July 16, 2011 and deferring the effective date of other provisions.
 - The requirement for approval of swap transactions by an appropriate board committee has been delayed pending further rulemaking by the SEC and CFTC.

Board Committee Approval of Certain Swap Transactions – cont'd

- **Actions to Consider:**

- Assess the company's derivatives requirements (interest rate swaps, oil and gas swaps) and conditions for "commercial end-user" exemption.
 - Consider which board committee should be responsible for approving the transactions. Review the committee's charter and amend it as necessary when the rules become effective.
 - Develop internal controls to ensure requisite transactions are presented to the committee for review and approval.
-
- 

SPECIALIZED DISCLOSURE REQUIREMENTS

Conflict Minerals (DF 1502)

- Section 1502 of Dodd-Frank and the proposed rules require companies that file Exchange Act reports to provide disclosure regarding conflict minerals “necessary to the functionality or production of a product manufactured by the company.”
- **Conflict Minerals:** Conflict minerals include the following and any other minerals determined by the Secretary of State to be financing conflict in the Democratic Republic of Congo or an adjoining country (the “DRC Countries”):
 - **Cassiterite**, a metal ore commonly used to produce tin, which is used in alloys, solders for pipe joints and electronic circuits;
 - **Columbite-tantalite**, a metal ore from which tantalum is extracted, which is used in electronic components such as cell phones, computers, digital cameras and an alloy for making carbide tools;
 - **Gold**, used for jewelry but also in electronics, communications and aerospace equipment; and
 - **Wolframite**, a metal ore used to produce tungsten, which is used in metal wires, electrodes and electrical contacts.

Conflict Minerals – cont'd

- **Determining applicability of disclosure rules:**

- First, does the company manufacture products for which conflict materials are necessary to their functionality or production?
 - If no, disclosure is not required.
- Second, if yes, make a reasonable inquiry to determine if any such minerals originated in a DRC Country.
 - The SEC did not define steps a company must take in the determination.
 - If no, the company must disclose this determination in its annual report and on its website, along with country of origin.
- Third, if yes or unsure, the company must exercise further diligence on the source and chain of custody and provide disclosure about this process in a “conflicts mineral report” furnished as an exhibit to its annual report.

- **Timeline:** Companies subject to the rules will be required to provide their initial disclosure in their annual report for the first full fiscal year following the SEC’s adoption of the final rules.

-
- Final rules were expected in April 2011. The SEC’s current schedule is that final rules are expected August – December 2011.

Mine Safety (DF 1503)

- Section 1503 of Dodd-Frank and the proposed rules require companies that file Exchange Act reports to provide disclosure about mine safety.
- **Effective Date:** The disclosure requirements became effective on August 20, 2010 notwithstanding the absence of final implementing rules.
- **Coal or other mine:** The definition of a coal or other mine is much broader than may be expected.
 - “Coal or other mine” includes traditional excavation activities for minerals in non-liquid form as well as lands, structures, facilities, etc. used in the milling of such minerals.
- Interagency Agreement between the Mine Safety and Health Administration (“MSHA”) and the Occupational Safety and Health Administration (“OSHA”)
 - Due to uncertainty of jurisdictional authority, the Interagency Agreement attempts to clarify the agencies’ authority and defines certain terms.

Mine Safety- cont'd

- Milling is the treating of the crude crust of the earth to produce the consumer derivative. Milling includes crushing, grinding, pulverizing, sizing, pelletizing, washing and several other processes.
- Minerals are also defined and in addition to typical metals, the definition includes nonmetals including sand, gravel and limestone
- **Scope of Disclosure:** Each periodic report is required to identify each mine of which the company or a subsidiary is an operator and disclose, for each mine:
 - the total number of violations, orders and assessments from MSHA;
 - the number of mining-related fatalities; and
 - pending legal action before the Federal Mine Safety and Health Review Commission.

Mine Safety – cont'd

- The proposed rules would require the disclosure in an exhibit to the Form 10-Q and Form 10-K. Current reporting varies, but is typically referenced in the “Other Information” item and then set forth in an exhibit.
- **Form 8-K:** In addition to the foregoing disclosures, a Form 8-K is triggered by the receipt of:
 - an imminent danger order issued under Section 107 of the Federal Mine Safety and Health Act of 1977;
 - written notice from MSHA of a pattern of certain designated violations; and
 - written notice from MSHA that the mine has the potential to have such pattern.
- The proposed rules include the Form 8-K requirement as a safe-harbor. The effect of a missed Form 8-K is uncertain until the rules become final.

Mine Safety – cont'd

- **Takeaway:**

- This disclosure requirement is much broader than many people may expect. A gravel grinding facility separate and apart from the source of the gravel may be a “mine” for purposes of this disclosure.
- If any operations are subject to inspections by MSHA, the operation or facility likely will be within the scope of the required disclosure.

Disclosures for Payments by Resource Extraction Issuers (DF 1504)

- Section 1504 of Dodd-Frank and the proposed rules require companies that file Exchange Act reports and that are engaged in the commercial development of oil, natural gas or minerals (as “Resource Extraction Issuer”) to disclose payments made to governmental entities for the purpose of commercial development of oil, natural gas or minerals.
- **Commercial development of oil, natural gas or minerals:** The SEC proposed to define this to include:
 - exploration;
 - extraction;
 - processing;
 - export;
 - other significant actions relating to oil, natural gas or minerals; and
 - the acquisition of a license for any of these activities.

The definition does not generally include transportation activities other than for export.

Disclosures for Payments – cont'd

- **Payment:** A payment is an amount paid that:
 - is made to further the commercial development of oil, natural gas or minerals;
 - is not de minimis; and
 - includes taxes, royalties, fees (including licensing fees), production entitlements and bonuses.
- **What payments require disclosure:** Payments made:
 - during the fiscal year covered by the annual report;
 - by a Resource Extraction Issuer, its subsidiaries or any entities it controls;
 - to the U.S. federal government or a foreign government; and
 - for the purpose of the commercial development by oil, natural gas or minerals.

Disclosures for Payments – cont'd

- **Required disclosure:**

- The payment information to be disclosed includes:
 - the type and total amount of payments made for each project;
 - the type and total amount of payments made to each government;
 - the total payment amounts (by category);
 - the currency used for the payments;
 - the financial period when the payments were made;
 - the business segment of the issuer that made the payments;
 - the government that received the payment and the country where the government is located; and
 - the project of the company related to the payments.
 - The disclosure would be set forth in an exhibit to the company's annual report. The payment disclosure would not be required to be audited although the SEC requested comment on this.
-

Disclosures for Payments – cont'd

- **Timeline:**

- The SEC did not adopt final rules by the April 15, 2011 deadline. The current schedule is to adopt final rules August – December 2011.
 - The disclosure will be required for the annual report for the first fiscal year ending on or after the first anniversary of the date on which the SEC issues the final rules.

- **Looking Forward:** If your company is a Resource Extraction Issuer:

- consider whether countries where the company operates prohibit disclosure of payment information;
- consider if existing contractual agreements prohibit disclosure of payment information;
- consider how “project” and “de minimis” will be defined since these are not defined by the SEC; and
- determine if existing systems and disclosure controls and procedures are sufficient to track and collect information and report the required payment information.