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## **NYSE & Nasdaq Listing Standards Amendments**

### *Implications for Compensation Committees*

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#### **Introduction**

On January 11, 2013, the SEC approved amendments to the listing standards of the NYSE and Nasdaq, which are substantially similar to those proposed in September 2012.<sup>1</sup> These amendments relate to the independence of compensation committees members, the authority of the compensation committee, and its responsibilities when retaining advisors. The listing standards implement the SEC's final rules (Final Rules) on these matters pursuant to the Dodd Frank Act.<sup>2</sup>

As noted below, these standards and rules will be of particular relevance for all of our inter-listed clients.

#### **Compensation Committee Composition & Independence**

Both exchanges require that issuers have fully independent (as detailed below) standing compensation committees.<sup>3</sup> These committees are to be governed by formal and written compensation committee mandates outlining certain responsibilities and authorities.

In assessing the independence of compensation committee members, boards of NYSE-listed issuers will need to consider (in addition to existing independence tests) the following factors and whether these factors impair a director's ability to make independent judgments regarding executive compensation:

- Sources of a director's compensation including consulting or other compensatory fees from the issuer (or other source);
- If a director has an affiliate relationship with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer; and
- All other factors that materially affect a director's ability to be independent in his/her capacity as a compensation committee member.

In addition to the independence considerations under the NYSE requirements, compensation committee members of **Nasdaq-listed** issuers will be prohibited from accepting (directly or indirectly)

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<sup>1</sup> The NYSE approval order can be found [here](#) and the NASDAQ approval order can be found [here](#).

<sup>2</sup> SEC final rules were effective July 27, 2012. For more information please see Hugessen's Briefing on the topic [here](#).

<sup>3</sup> The current NYSE rules (which require fully independent compensation committees) do not specify the minimum number of committee members required, however, **the Nasdaq amendments require that the compensation committee be composed of at least two members.**

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consulting, advisory or other compensatory fees from an issuer or subsidiary. **This prohibition is notably more stringent than Canadian requirements.**

While issuers must consider the stock ownership of a director when assessing independence, both exchanges state that a significant ownership stake by a director will not necessarily act as a bar to an independence finding.

***The aforementioned rules will apply the earlier of a) an issuer's first AGM after January 15, 2014, or b) October 31, 2014.***

### **Compensation Committee Advisors**

Under the amended listing standards, both exchanges require that issuers provide compensation committees the authority to retain, oversee and pay compensation consultants, legal counsel and other advisors (to be documented in the committee charter). These advisors are not required to be independent *per se*, however, a compensation committee must consider factors affecting the advisor's independence before obtaining advice, including:

1. Any other services provided by the advisor or entity that employs the advisor (the Firm) to the issuer;
2. The fees paid by the issuer to the Firm relative to the Firm's total revenue;
3. The Firm's policies and procedures to prevent conflict of interest;
4. Any business or personal relationships the advisor or the person employing the advisor has with the company's executive officer(s);
5. Any business or personal relationships the advisor has with the compensation committee members; and
6. The advisor's stock ownership in the issuer (including stock ownership of such advisor's immediate family members).

Both exchanges make independence assessment exemptions for in-house legal counsel or any advisor whose role is limited to advising on broad-based compensation plans or providing non-customized data.

***The above listed rules take effect July 1, 2013.***

Additionally, under the SEC's Final Rules, issuers are required to (effective **January 1, 2013**) disclose in their proxy statements whether the compensation committee retained or obtained advice from a compensation consultant, whether this raises any conflicts of interest (to be determined using the six

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independence factors listed above as guidance) and, if so, the nature of the conflict and how it is being addressed.<sup>4</sup> Note that this disclosure rule is a requirement of the **company**, while the assessment of compensation consultant independence is a **compensation committee** requirement.

The importance of independent compensation advice for the effective functioning of compensation committees has already been widely acknowledged. While the listing standards fall short of mandating advisor independence, they place the onus on the compensation committee to consider certain key independence issues. We continue to believe that independent advice, from advisors that do not provide broader services to an issuer, is critical for ensuring against real (or perceived) conflicts of interest.

### **Implications and Next Steps for Foreign Private Issuers**

Both exchanges provide foreign private issuers<sup>5</sup> (e.g. most Canadian inter-listed companies) with exemptions from these listing standards so long as they follow the corporate governance requirements of their home country. In order to be exempt, the **NYSE** requires that these issuers disclose (in their Form 20-F) the significant ways in which their corporate governance practices differ from NYSE requirements. Similarly, **Nasdaq** requires these issuers disclose each requirement they do not follow (and disclose the applicable home country policy). Additionally, if a foreign private issuer does not have an independent compensation committee, it must disclose the reason it does not. Foreign private issuers are also exempt from these SEC's compensation consultant conflict disclosure rules.

In practice, we expect that most foreign private issuers will adopt these listing standards and disclosure rules, in particular those relating to compensation committee member independence. To ensure compliance with the new listing standards, compensation committees will need to:

- Establish written policies and monitoring procedures for evaluating compensation committee member independence and assess the independence of current committee members;
- Review their compensation committee charters and revise, as necessary, to ensure the compensation committee is provided with the power to retain and fund advisors;
- Revise or establish written policies and procedures for evaluating the independence of consultants and establish procedures for assessing consultant conflicts of interest;

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<sup>4</sup> This disclosure is not required for advisors consulting on broad-based plans only or those who provide only non-customized pay data.

<sup>5</sup> The SEC defines a foreign private issuer as, "any foreign issuer other than a foreign government, except for an issuer that has more than 50% of its outstanding voting securities held of record by U.S. residents and any of the following: a majority of its officers and directors are citizens or residents of the United States, more than 50% of its assets are located in the United States, or its business is principally administered in the United States."

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- If not yet completed, issuers will need to prepare compensation consultant disclosure per the SEC Final Rules. For the sake of efficiency, issuers should tie the process under which the compensation committee assesses an advisor's independence with that used to determine whether any conflict disclosure is required; and
- For **Nasdaq-listed** issuers, certify compliance with the applicable requirements (to be done no later than 30 days after the applicable implementation deadline).<sup>6</sup>

For assistance in preparing for these additional processes or for an assessment of what your company will need to do to comply with the new rules, please contact any of the persons below.

Toronto:	Ken Hugessen at	416-868-4422	<a href="mailto:khugessen@hugessen.com">khugessen@hugessen.com</a>
	Georges Soaré at	416-868-4416	<a href="mailto:gsoare@hugessen.com">gsoare@hugessen.com</a>
	David Crawford at	416-868-4418	<a href="mailto:dcrawford@hugessen.com">dcrawford@hugessen.com</a>
	Christine Vinette at	416-868-4419	<a href="mailto:cvinette@hugessen.com">cvinette@hugessen.com</a>
Calgary:	Scott Munn at	403-441-6297	<a href="mailto:smunn@hugessen.com">smunn@hugessen.com</a>

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<sup>6</sup> The certification form will be available via Nasdaq's Listing Center website prior to the effective date of the Nasdaq rules.