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Corporate Governance: An Overview of Public Company Requirements

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The Sarbanes-Oxley Act of 2002 has had a dramatic effect on public companies. Sarbanes-Oxley, which became law on July 30, 2002, was the first comprehensive federal legislation to impose significant corporate governance requirements on public companies and to address the responsibilities of corporate executives and board members. The Act touched almost every aspect of corporate governance and imposed new standards on boards of directors, officers, auditors, and counsel. Following the enactment of Sarbanes-Oxley, the Securities and Exchange Commission (SEC) adopted numerous regulations implementing the law, and each of the major stock exchanges—the New York Stock Exchange (NYSE) and the Nasdaq Stock Market, Inc. (Nasdaq)—adopted new listing standards in an effort to strengthen the corporate governance practices of listed companies. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) became law. The following is a summary of the corporate governance provisions of Sarbanes-Oxley and Dodd-Frank, and the corporate governance criteria adopted by the NYSE and Nasdaq, updated through June 27, 2011. Implementation of the corporate governance provisions in Dodd-Frank will require the SEC to propose and adopt new regulations over the next several months. Some of these regulations have been proposed.

I. Director Independence

Sarbanes-Oxley and Dodd-Frank

Sarbanes-Oxley and Dodd-Frank impose no requirements regarding director independence in general. However, Rule 10A-3 under the Securities Exchange Act of 1934 (the Exchange Act), adopted pursuant to Sarbanes-Oxley, requires the stock exchanges to impose independence requirements on members of audit committees. Dodd-Frank requires the SEC to adopt rules requiring the stock exchanges to impose independence criteria on members of compensation committees. This is discussed in **Section II** below. The compensation committee requirements have not yet been adopted by the SEC. Dodd-Frank's compensation committee requirements are summarized in **Section III** below.

NYSE

- Each NYSE-listed company must have a board composed of a majority of independent directors.
    - Controlled companies (those for which more than 50% of the voting power is held by an individual, a group, or another company) are not required to have a majority of independent directors on their boards (but are required to have audit committees composed entirely of independent directors as discussed in **Section II** below).
    - A controlled company that chooses to take advantage of the director independence exemption must disclose that choice in its annual proxy statement or, if the company does not file an annual proxy statement, in the company's annual report on Form 10-K or Form 20-F.

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- Under the NYSE Listing Guidelines, the determination of independence is a two-step process. Individuals who fall within five specified categories of relationships with the listed company are per se not independent. These relationships are as follows:

- A director who is an employee, or whose immediate family member is an executive officer, of the company will not be considered independent until three years after the end of such employment relationship.

  - Employment as an interim Chairman or CEO would not disqualify a director from being considered independent following conclusion of that employment.

  - An "immediate family member" includes a person's spouse, parents, children, siblings, mothers- and fathers-in-law, sons- and daughters-in-law, brothers- and sisters-in-law, and anyone (other than employees of the person) who shares such person's home.

- A director who has received, or whose immediate family member has received, more than $120,000 per year in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (as long as such compensation is not contingent in any way on continued service), during any 12-month period in the prior three years will not be independent.

  - If a person who received more than $120,000 per year in direct compensation from the company dies or becomes incapacitated, the presumption of nonindependence applicable to his or her immediate family members will immediately cease upon such death or determination of incapacity.

- A director who is, or whose immediate family member is, a current partner of a firm that is the company's internal or external auditor; a director who is a current employee of such a firm; a director who has an immediate family member who is a current employee of such a firm and who personally works on the company's audit; or a director who was, or whose immediate family member was, within the last three years a partner or employee of such a firm and personally worked on the listed company's audit within that time, will not be considered independent.

- A director who is employed, or whose immediate family member is employed, as an executive officer of another company where any of the listed company's present executives serve on that company's compensation committee will not be considered independent until three years after the end of such service or the employment relationship.

- A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of a company that makes payments to, or receives payments from, the listed company for property or services in an amount which, in any single fiscal year, exceeds the greater of $1 million, or 2% of such other company's consolidated gross revenues, will not be considered independent until three years after falling below such threshold.

  - Any reference above to "company" includes any parent or subsidiary in a consolidated group with the listed company.

- Assuming the board member does not fall within any of the foregoing categories, he or she will qualify as independent if the board of directors affirmatively determines that he or she has no material relationship with the listed company. The company will be required to disclose determinations of independence in its annual proxy statement or, if the company does not file an annual proxy statement, in the company's annual report on Form 10-K or Form 20-F. To assist in making this independence determination, a company is allowed to adopt categorical standards regarding material relationships. So long as these categorical standards are disclosed, the company can simply disclose that no independent director has any relationship other than as permitted by the categorical standard. For example, a company may determine

that ordinary course dealings between a director and the company not involving amounts in excess of a specified sum are categorically immaterial. This relieves the board from having to consider and the company from having to disclose a long list of clearly immaterial transactions.

- Newly public companies must be compliant with the board composition rules within 12 months after their listing.

Nasdaq

- The board of directors of any Nasdaq-listed company must be composed of a majority of independent directors.
  - Controlled companies are not required to have a majority of independent directors (but are required to have audit committees composed entirely of independent directors as discussed in **Section II** below).
- A director who is, or at any time during the past three years was, employed by the company or by any parent or subsidiary of the company will not be considered independent.
- A director who accepts or has a family member who accepts any payments from the company, or any parent or subsidiary of the company, in excess of $120,000 during any period of 12 consecutive months within the preceding three years, other than certain permitted payments (including directors' fees), will not be considered independent.
  - A family member is defined as "a person's spouse, parents, children and siblings, whether by blood, marriage, or adoption, or anyone residing in such person's home."
  - Permitted payments include compensation for board or board committee service, payments arising solely from investments in the company's securities, compensation paid to a family member who is a nonexecutive employee of the company or a parent or subsidiary of the company and benefits under a tax-qualified retirement plan, or nondiscretionary compensation.
- A director who is a family member of an individual who is, or at any time during the past three years was, employed by the company or by any parent or subsidiary of the company as an executive officer will not be considered independent.
- A director who is, or has a family member who is, a partner in, or a controlling stockholder or an executive officer of, any organization to which the listed company made, or from which the listed company received, payments for property or services in the current or any of the past three fiscal years that exceed 5% of the recipient's consolidated gross revenues for that year, or $200,000, whichever is more (other than certain permitted payments), will not be considered independent.
  - Permitted payments in this instance include payments arising solely from investments in the company's securities, and payments under nondiscretionary charitable contribution matching programs.
- A director who is, or has a family member who is, employed as an executive officer of another entity at any time during the past three years where any of the executive officers of the listed company serves on the compensation committee of such other entity will not be considered independent.
- A director who is, or has a family member who is, a current partner of the company's outside auditor, or was a partner or employee of the company's outside auditor and worked on the company's audit at any time during the past three years, will not be considered independent.

- Nasdaq intends any reference to a "parent or subsidiary" in the definition of independence to cover entities that the listed company controls and consolidates with its financial statements as filed with the SEC.

II. Audit Committees

Sarbanes-Oxley

- Rule 10A-3 under the Exchange Act directs the stock exchanges to adopt listing criteria requiring each listed company to have an audit committee composed of independent directors (as defined in Rule 10A-3).
    - Where an issuer is one of two dual holding companies, those companies may designate one audit committee for both companies so long as each member of the audit committee is a member of the board of directors of at least one of such dual holding companies.
- To be considered independent, a member of an audit committee of an issuer that is not an investment company may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee:
    - Accept directly or indirectly any consulting, advisory, or other compensatory fee from the issuer or any subsidiary of the issuer during the year in which he or she serves on the committee. Compensatory fees do not include fees for board and board committee service or fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the listed issuer (as long as such compensation is not contingent in any way on continued service); or
    - Be an "affiliated person" of the issuer or any subsidiary of the issuer.
- The rule provides for certain limited exemptions from the independence requirement for audit committee members.
- The rule defines "affiliate" and "affiliated person" to mean "a person that, directly or indirectly, through one or more intermediaries, controls or is controlled by, or [is] under common control with," the issuer or any subsidiary of the issuer.
- The rule also includes a "safe harbor." A person who is not an executive officer or beneficial owner, directly or indirectly, of 10% or more of any class of voting stock of the issuer will be deemed not to control the issuer. There is, however, no presumption that a holder of 10% or more is an affiliated person.
- The audit committee must be directly responsible for the appointment, compensation, retention, and oversight of the outside auditors. Additionally, the outside auditors must report directly to the audit committee.
- The audit committee must have the authority to engage independent counsel and other advisers as it determines necessary to carry out its duties.
- The issuer must provide appropriate funding for the audit committee.
- The audit committee must establish procedures for the receipt, retention, and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters, and the confidential, anonymous submission by employees of the issuer of concerns regarding questionable accounting or auditing matters.

- In addition, Section 10A of the Exchange Act requires the audit committee to approve, in advance, any audit or nonaudit services provided by the outside auditors. Approval by the audit committee of any permitted nonaudit work must be disclosed to the company's stockholders. The scope of the nonaudit work that outside auditors are permitted to provide to the company has been narrowed considerably.

- In its annual reports, an issuer will be required to publicly disclose that its board of directors has determined that the company either (i) has at least one audit committee financial expert serving on its audit committee, or (ii) does not have an audit committee financial expert serving on its audit committee. A company that does not have an audit committee financial expert must explain in the report why it does not have such an expert. Furthermore, an issuer must disclose whether the audit committee financial expert is independent of management.

- An "audit committee financial expert" is a person who has an understanding of generally accepted accounting principles and financial statements; the ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves; experience preparing, auditing, analyzing, or evaluating complex financial statements; an understanding of internal controls; and an understanding of the audit committee function.

- Newly listed issuers, including companies that have recently become publicly held, have the benefit of a one-year transition period before they are required to be fully compliant with the audit committee listing criteria.

- The SEC's proxy rules require an audit committee report in a domestic company's proxy statement for any annual meeting at which directors are to be elected.

NYSE

- Listed companies must have an audit committee that satisfies the requirements of Rule 10A-3 under the Exchange Act.

- Each listed company must have an audit committee composed of at least three independent directors.

    - To be considered independent, audit committee members must meet all requirements for independence set forth in Rule 10A-3 of the Exchange Act, as well as the NYSE requirements for independence as listed above in **Section I**.

- Each member of the audit committee must be financially literate, as such qualification is interpreted by the board in its business judgment, or must become financially literate within a reasonable period of time after his or her appointment to the audit committee.

- Additionally, at least one member of the audit committee is required to have accounting or related financial management expertise, as the company's board interprets such qualification in its business judgment.

- While the NYSE does not require that a listed company's audit committee include a person who satisfies the definition of audit committee financial expert (see **Section II** above), a board may presume that such a person has accounting or related financial management experience.

- If an audit committee member simultaneously serves on the audit committee of more than three public companies, and the listed company does not limit the number of audit committees on which its audit committee members may serve, each board will be required to determine that such simultaneous service would not impair the ability of such member to effectively serve on the listed company's audit committee, and to disclose such determination.

- The audit committee must have a charter that addresses the committee's purpose and sets forth the duties and responsibilities of the committee.

- The audit committee charter must provide for an annual performance evaluation of the audit committee.

- The audit committee must, among other things, obtain and review an annual report by the independent auditor regarding the firm's internal quality-control procedures, discuss the audited financial statements with the independent auditor and management, and report regularly to the board of directors.

- Each listed company must have an internal audit function to assist its audit committee and board of directors.

Nasdaq

- Each listed company must have an audit committee of at least three members.

  - Each audit committee member is required to (i) satisfy all Nasdaq requirements for independence (as detailed in **Section I** above); (ii) meet the criteria for independence set forth in Rule 10A-3; (iii) not have participated in the preparation of the financial statements of the listed company or any current subsidiary of the company at any time during the past three years; and (iv) be able to read and understand fundamental financial statements, including a company's balance sheet, income statement, and cash flow statement. Additionally, each issuer must certify that it has, and will continue to have, at least one member of the audit committee who has past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including being or having been a chief executive officer, chief financial officer, or other senior officer with financial oversight responsibilities.

  - One director who is not independent (as detailed in **Section I** above) but otherwise meets the criteria set forth in Section 10A(m)(3) of the Exchange Act and the rules thereunder, and is not a current officer or employee of the company or a family member of such person, may be appointed to the audit committee if the board, under exceptional and limited circumstances, determines that membership on the committee by the individual is required by the best interests of the company and its stockholders.

    - The board must disclose, in the next annual proxy statement subsequent to such determination (or, if the listed company does not file a proxy statement, in its annual report on Form 10-K or Form 20-F), the nature of the relationship and the reasons for that determination.

    - A member appointed under the exceptional and limited circumstances exception will not be permitted to serve on the committee for longer than two years, and also will not be permitted to chair the audit committee.

- The audit committee must have a written charter and must have the specific audit committee responsibilities and authority necessary to comply with Rule 10A-3.

III. Compensation Committees

Sarbanes-Oxley and Dodd-Frank

Sarbanes-Oxley does not address compensation committees.

Dodd-Frank directs the SEC to require the stock exchanges to impose independence requirements for compensation committee membership and to promote independence and oversight of compensation committee consultants, legal counsel, and other advisers. The independence criteria that are stated in Dodd-Frank

compensation committee membership are similar to the independence criteria for audit committee membership in Sarbanes-Oxley. Dodd-Frank requires that the independence criteria for compensation committee consultants, legal counsel, and other advisers be "competitively neutral." In April 2011, the SEC proposed regulations to implement the provisions of Dodd-Frank dealing with Compensation Committees. These proposed regulations, which are subject to public comment, give the stock exchanges some latitude in adopting listing criteria to implement Dodd-Frank. The proposed regulations have not been adopted yet and none of the stock exchanges has yet proposed the related listing criteria.

NYSE

- Listed companies currently must have a compensation committee composed entirely of independent directors.
    - The compensation committee must have a written charter that addresses, among other things, the committee's purpose and sets forth the duties and responsibilities of the committee.
    - The compensation committee charter should provide for an annual performance evaluation of the compensation committee.
    - The compensation committee will also be required to produce a compensation committee report on executive compensation, as required by SEC rules, to be included in the company's annual proxy statement or annual report on Form 10-K filed with the SEC.
- Controlled companies are exempt from the NYSE compensation committee requirements.

Nasdaq

- Although Nasdaq's rules do not currently require a compensation committee, they do require the compensation of the CEO of a listed company, as well as that of all other executive officers, to be determined or recommended to the board for determination either by a majority of the independent directors or by a compensation committee composed solely of independent directors.
- Under Nasdaq's current listing criteria, if the compensation committee is composed of at least three members, one director, who is not independent and is not a current officer or employee or a family member of such person, will be permitted to be appointed to the committee if the board, under exceptional and limited circumstances, determines that such individual's membership on the committee is required by the best interests of the company and its stockholders.
    - The board must disclose, in the next annual meeting proxy statement subsequent to such determination (or, if the listed company does not file a proxy, in its annual report on Form 10-K or Form 20-F), the nature of the relationship and the reasons for the determination.
    - A member of the compensation committee appointed under the exceptional and limited circumstances exception will not be permitted to serve on the committee for longer than two years.
- Controlled companies are exempt from the requirement of independent director approval of executive compensation.

IV. Nominating Committees

Sarbanes-Oxley and Dodd-Frank

Neither Sarbanes-Oxley nor Dodd-Frank addresses nominating committees. However, amendments to the proxy rules promulgated since Sarbanes-Oxley require a domestic company that does not have a standing nominating committee to disclose the basis for the view of its board that it is not appropriate to have such a committee. If a public company does have a nominating committee, disclosure regarding its composition and function is required in the company's proxy statement.

The SEC has adopted rules requiring domestic public companies to include stockholder nominated candidates for board membership in their proxy materials. The SEC has delayed the effectiveness of these rules pending the resolution of litigation challenging the SEC's rulemaking.

NYSE

- A listed company must have a nominating/corporate governance committee composed entirely of independent directors.
  - The nominating/corporate governance committee must have a charter that addresses the committee's purpose and sets forth the goals and responsibilities of the committee.
  - The nominating/corporate governance committee charter should provide for an annual performance evaluation of the nominating/corporate governance committee.
  - If a listed company is legally required by contract or otherwise to provide third parties with the ability to nominate directors, the selection process of such directors need not be subject to the nominating committee process.
- Controlled companies are exempt from the NYSE nominating/corporate governance committee requirements.

Nasdaq

- Nasdaq does not require listed companies to have a nominating/corporate governance committee, but it does require all director nominees to be selected or recommended for the board's selection either by a majority of independent directors or by a nominating committee composed solely of independent directors.
  - If the nominating committee is composed of at least three members, one director, who is not independent and is not a current officer or employee or a family member of such person, will be permitted to be appointed to the committee if the board, under exceptional and limited circumstances, determines that such individual's membership on the committee is required by the best interests of the company and its stockholders.
    - The board must disclose, in the next annual meeting proxy statement subsequent to such determination (or, if the listed company does not file a proxy, in its annual report on Form 10-K or Form 20-F), the nature of the relationship and the reasons for the determination.
    - A member of the nominating committee appointed under the exceptional and limited circumstances exception will not be permitted to serve on the committee for longer than two years.

- Nasdaq requires each listed company to certify that it has adopted a formal written charter or board resolution, as applicable, addressing the nominations process and such related matters as may be required under the federal securities laws.

- The above provisions do not apply in cases where either the right to nominate a director legally belongs to a third party or the company is subject to a binding obligation that requires a director nomination structure inconsistent with these provisions and the obligation pre-dates the date the provisions were approved.

- Controlled companies are exempt from the requirement of independent director approval of nominations.

V. Compensation

Dodd-Frank

Dodd-Frank requires a periodic, nonbinding, shareholder vote on executive compensation. This shareholder vote must take place at least once every three years, with the frequency of the vote to be determined by shareholders at least once every six years. Institutional investment managers will be obligated to disclose their votes on these resolutions.

Dodd-Frank requires that the SEC adopt rules to requiring national securities exchanges and national securities associations to enact listing standards that will require issuers (1) to provide disclosure of compensation policies relating to incentive based compensation and (2) to enact clawback policies (not limited to instances of misconduct) that allow issuers to recover any incentive-based compensation from current or former executive officers for the prior three years in the event of a financial restatement due to material noncompliance with any financial reporting requirement under the securities laws.

Dodd-Frank requires the SEC to adopt regulations requiring companies to disclose in their proxy statements for annual meetings the relationship between the amount of executive compensation actually paid to executive officers and the financial performance of their company.

The SEC's proxy rules require that domestic public companies prepare a “compensation discussion and analysis” (CD&A), including extensive tabular and narrative disclosure of compensation paid to their most senior and highly compensated executives. The rules also require that the compensation committee report disclose whether the committee has reviewed and discussed the CD&A with management and whether the committee has recommended to the board of directors that the CD&A be included in the proxy statement.

NYSE

- A stockholder vote is required to approve all equity-compensation plans and material revisions thereto, except (i) employment inducement options, (ii) in certain merger and acquisition contexts, and (iii) tax-qualified plans under Sections 401(a) and 423 of the Internal Revenue Code, as well as certain parallel excess plans.

    - An “equity-compensation plan” is a plan or other arrangement that provides for the delivery of equity securities (either newly issued or treasury shares) of the listed company to any employee, director, or other service provider as compensation for services. Even a compensatory grant of options or other equity securities that is not made under a plan is, nonetheless, an equity-compensation plan for these purposes.

    - The following are not considered equity-compensation plans: (i) plans that are made available to stockholders generally, such as typical dividend reinvestment plans; and (ii) plans that merely allow employees, directors, or other service providers to elect to buy shares on the open market

or from the listed company for their current fair market value, regardless of whether the shares are delivered immediately or on a deferred basis, or the payments for the shares are made directly or by giving up compensation that is otherwise due (for example, through payroll deductions).

- A broker may not vote a customer's shares on any equity-compensation plan proposal submitted to the stockholders for approval unless the broker has received voting instructions from the customer. This rule applies to all broker-dealers that are member firms of the NYSE, and therefore restricts their ability to vote customers' shares regardless of whether the companies' shares are listed on the NYSE.

Nasdaq

- Stockholder approval is required for all stock option plans or other equity-compensation plans and any material amendment of such plans.
- An exemption applies for inducement grants to new employees if such grants are approved by an independent compensation committee or a majority of the independent directors. A company must promptly disclose in a press release the material terms of any inducement grant (including each recipient of a grant and the number of shares involved) issued in reliance upon this exception.
- An exemption is available for certain tax-qualified plans and for parallel nonqualified plans, or plans that merely provide a convenient way to purchase shares on the open market or from the listed company at fair market value, as long as those plans are approved by the listed company's compensation committee or a majority of the independent directors.
- Exemptions also apply for plans relating to an acquisition or a merger, and for plans that provide for warrants or rights offered generally to all stockholders.

VI. Codes of Conduct

Sarbanes-Oxley

- A public company is required to disclose in its annual report whether it has adopted a code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. If a company has not adopted a code of ethics, the company must disclose the reason.
- A domestic company is required to disclose on Form 8-K within four business days:
- The nature of any amendment to the company's code of ethics that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions; and
- The nature of any waiver, including an implicit waiver, from a provision of the code of ethics granted by the company to one of these specified officers, the name of the person to whom the company granted the waiver, and the date of the waiver.

NYSE

- An NYSE-listed company must adopt and disclose a code of business conduct and ethics for directors, officers, and employees.

- Only the board of directors or a board committee can authorize a waiver of the code for executive officers or directors, and any such waiver must be promptly disclosed to the company's stockholders.
- Each listed company must include its code of business conduct and ethics on its website, and each annual report filed with the SEC must state that the code of business conduct and ethics is available on the website and that the information is available in print to any stockholder.

Nasdaq

- Each Nasdaq-listed company is required to adopt a code of conduct applicable to all directors, officers, and employees.
- The code of conduct must comply with the definition of a "code of ethics" set forth in Section 406 of Sarbanes-Oxley.
- The code of conduct must provide for an enforcement mechanism that ensures prompt and consistent enforcement of the code, protection for persons reporting questionable behavior, clear and objective standards for compliance, and a fair process by which to determine violations.
- Waivers of the code of conduct for directors or executive officers must be approved by the board of directors and disclosed in a current report on Form 8-K.
- Companies must make their codes of conduct publicly available.

VII. Certifications

Sarbanes-Oxley

- The chief executive officer and the chief financial officer of a public company must provide a separate written statement with each periodic report that contains financial statements certifying that (1) the report complies with the requirements of Section 13(a) or 15(d) of the Exchange Act, and (2) the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the company.
- Any CEO or CFO who provides the certification knowing that the report does not meet the standards can be fined or imprisoned, or both.
- The CEO and the CFO of the company must also file separate certifications with each annual and quarterly report that:
    - The certifying officer has reviewed the report.
    - To the certifying officer's knowledge, the report does not contain any untrue statement of material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which the statements were made, not misleading with respect to the period covered by the report.
    - To the certifying officer's knowledge, the financial statements and other financial information included in the report fairly present, in all material respects, the financial condition and results of operations and cash flows of the company as of, and for, the periods presented in the report.
    - The certifying officers (i) are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting; (ii) have designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed

under their supervision to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to them by others within those entities, particularly during the period in which the report is being prepared; (iii) have evaluated the effectiveness of the disclosure controls and procedures; (iv) have presented in the report their conclusions about the effectiveness of the controls as of the end of the relevant period; (v) have disclosed to their outside auditors and audit committee all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting and any fraud involving management or other employees who have a significant role in the company's internal controls; and (vi) have disclosed in the report any change in the internal control over financial reporting that could affect those controls, including any corrective actions.

- The certifications must be filed separately with the SEC as exhibits to the periodic reports to which they relate.

NYSE

- The CEO of a listed company must certify annually that he or she is not aware of any violations by the company of NYSE corporate governance standards.
    - This certification is required to be disclosed in the company's annual report or, if the company does not prepare an annual report to stockholders, in the company's annual report on Form 10-K filed with the Commission.
    - A listed company must notify the NYSE promptly in writing after any executive officer of the listed company becomes aware of any noncompliance with the NYSE's corporate governance provisions.
    - A listed company must provide the NYSE with an annual "affirmation" detailing how it has complied with the various corporate governance listing criteria, including specific identification of independent directors and specific references to the location of required disclosures.

Nasdaq

- A listed company must notify Nasdaq promptly after any executive officer becomes aware of *any* noncompliance with Nasdaq's corporate governance requirements.

VIII. Directors/Officers

Sarbanes-Oxley

- No public company may extend, maintain, or renew an extension of credit or arrange for the extension of credit in the form of a personal loan, to a director or executive officer.
- The CEO and CFO of a public company that restates its financial statements as a result of misconduct will have to forfeit any bonuses, incentives, equity-based compensation, and profits on sales of company stock realized during the 12-month period following the first public issuance of the financial document or report containing the inaccurate financial statements.
- The SEC has the authority to freeze any extraordinary payments by the company to any of its directors or officers while an investigation is ongoing.
- The SEC may bar a person who has violated Section 17(a) of the Securities Act of 1933 or Section 10(b) of the Exchange Act, or the rules and regulations promulgated thereunder, from serving as a public company director or officer.

- Directors, officers, and 10% stockholders of domestic companies are required to report changes in their beneficial ownership on Form 4 within two business days after the relevant transaction. Additionally, Forms 3, 4, and 5, related to reporting of beneficial ownership, must be filed electronically with the SEC via EDGAR. A company must post Forms 3, 4, and 5 on its website.

- Directors and executive officers are prohibited from buying or selling equity securities during a pension fund blackout period.

- An outside auditing firm is prohibited from performing audit services for an issuer if the CEO, CFO, CAO, controller, or any other person in a financial oversight role at the issuer was employed by the outside auditor and participated in any capacity in the audit of that issuer during the one-year period preceding the initiation of the current audit.

- Officers and directors, and persons acting under the direction of an officer or director, are prohibited from taking any action to coerce, manipulate, mislead, or fraudulently influence the auditor of the company's financial statements, if that person knew or should have known that such action, if successful, could result in rendering the financial statements materially misleading.

NYSE

- The NYSE continues to encourage listed companies to establish orientation programs and continuing education programs for directors.

- Nonmanagement directors are required to meet in regularly scheduled executive sessions without management present.

  - NYSE-listed companies must disclose a method for interested parties to communicate directly with the presiding director of such executive sessions, or with the nonmanagement directors as a group.

Nasdaq

- Nasdaq requires that an issuer provide Nasdaq with prompt notification after an executive officer of the issuer becomes aware of any material noncompliance by the issuer with Nasdaq's listing requirements.

- The independent directors must meet in regularly scheduled executive sessions at which only independent directors are present.

IX. Disclosure

Sarbanes-Oxley and Dodd-Frank

- As directed by Section 404 of Sarbanes-Oxley, the SEC adopted a rule requiring a registered company to include in its annual report a report of management on the company's internal control over financial reporting.

  - The internal control report must include (i) a statement of management's responsibility for establishing and maintaining adequate internal controls, (ii) management's assessment of the effectiveness of the company's internal controls including disclosure of any material weaknesses, (iii) a statement identifying the framework used by management to evaluate the effectiveness of internal controls, and (iv) a statement that the independent auditors have issued an attestation report on management's assessment of the company's internal controls over financial reporting.

- A company must also file, as part of its annual report, the attestation report of the registered public accounting firm that audited the company's financial statements.

- Management must evaluate, on a quarterly basis, any change in the company's internal controls over financial reporting that is reasonably likely to materially affect the company's internal controls over financial reporting.

- Periodic reports that contain financial statements must reflect all material correcting adjustments that have been identified by the public company's outside auditors in accordance with GAAP and related SEC rules.

- Companies must provide disclosure about off-balance-sheet transactions in registration statements, annual reports, and proxy or information statements that are required to include financial statements.

- The SEC's proxy rules require disclosure in domestic companies' proxy statements of the responsibilities or operations of the audit, compensation, and nominating committees.

- Dodd-Frank permanently exempts issuers whose worldwide public float is less than $75 million from Sarbanes-Oxley's requirement to have their independent auditors issue an attestation report on the company's internal control over financial reporting and management's assessment of those controls. All public companies remain subject to the requirement to have internal controls for financial reporting and to have an annual assessment from their management as to the effectiveness of such controls.

NYSE

Disclosure requirements under the NYSE rules are detailed in other sections of this White Paper.

Nasdaq

- A going-concern qualification in an audit opinion must be promptly disclosed through the issuance of a press release.

- Nasdaq's rule on the disclosure of material information has been harmonized with SEC Regulation FD so that issuers may use Regulation FD-compliant methods, as long as the public is provided adequate notice and granted access.

X. Foreign Issuers

Sarbanes-Oxley and Dodd-Frank

- Sarbanes-Oxley applies to both domestic and foreign issuers, including the provisions regarding audit committees, codes of ethics, and certifications by executive officers in periodic reports.

- The SEC may, by rule, exempt foreign issuers from certain provisions of Sarbanes-Oxley, but its authority to do so is limited.

    - *Compensation Committees*: Dodd-Frank expressly exempts foreign private issuers from the requirement to have an independent compensation committee as long as they disclose why they do not have such a committee. For foreign private issuers which opt to follow this requirement, Dodd-Frank provides guidance on the factors that the U.S. stock exchanges should consider in defining who is an "independent" director, and in particular whether the director receives any remuneration from, or is affiliated with, the issuer.

- *Compensation Consultants, Legal Counsel, and Other Advisors*: Listing standards will apply to foreign private issuers listed in the U.S., unless the SEC uses its exemptive authority to continue its practice of allowing foreign private issuers to follow the corporate governance practices of their home country, provided that the differences are disclosed.

- *Exemption for Smaller Issuers*: Dodd-Frank's exemption for issuers which have a market capitalization of less than $75 million from the requirement to include an auditor attestation regarding their internal control over financial reporting applies to foreign private issuers.

NYSE

- NYSE-listed companies that are foreign private issuers are permitted to follow home country practice in lieu of the new corporate governance requirements, except that such companies will be required to:

    - Have an audit committee that satisfies the requirements of Rule 10A-3;

    - Notify the NYSE in writing after any executive officer becomes aware of any noncompliance with any applicable provision of Rule 10A-3; and

    - Provide a brief, general summary of the significant ways in which its governance differs from those followed by domestic companies under NYSE listing standards.

- Listed foreign private issuers are permitted to provide this disclosure either on their websites (provided they are in English and accessible from the United States) or in their annual reports as distributed to stockholders in the United States.

Nasdaq

- Nasdaq's rules provide that foreign private issuers are not required to perform any act that is contrary to a law, rule, or regulation of any public authority exercising jurisdiction over such issuer or that is contrary to generally accepted business practices in the issuer's country of domicile. Additionally, Nasdaq may provide exemptions from its listing standards as may be necessary or appropriate to carry out this intent.

- A foreign private issuer that receives an exemption from Nasdaq's listing requirements will be required to disclose in its annual report filed with the SEC each requirement from which it is exempted, and describe the home country practice, if any, followed by the issuer in lieu of these requirements. In addition, a foreign private issuer making its initial public offering or first United States listing on Nasdaq would be required to disclose any such exemptions in its registration statement.

XI. Miscellaneous

Sarbanes-Oxley and Dodd-Frank

- The SEC must review disclosures made by each public company, including the financial statements, at least once every three years.

- Mirroring the NYSE's Rule 452, Dodd-Frank prohibits brokers from voting on matters related to the election of directors, executive compensation or other significant matters as determined by the SEC, unless the broker has received voting instructions from the beneficial owner of the shares the broker holds.

- Dodd-Frank requires the SEC to adopt rules requiring disclosure in proxy statements for annual meetings as to whether a company's directors and employees are permitted to hedge their holdings of

the company's equity securities.

- Sarbanes-Oxley provides for protections for "whistleblowers" against retaliation by a public company or its officers, directors, or agents.
  - Dodd-Frank significantly expands protection and incentives for whistleblowers that were enacted as part of Sarbanes-Oxley:
    - Expands protection to any employee who complains to the SEC, regardless of whether the employee *reasonably* believes the complained-of conduct constitutes fraud;
    - Increases statute of limitations from 90 to 180 days;
    - Eliminates an employer's ability to enforce waivers of whistleblowers' rights or remedies, or to require arbitration of claims of retaliation through pre-dispute agreements;
    - Grants parties to retaliation cases in federal district court a right to trial by jury;
    - Clarifies that the Sarbanes-Oxley Act's retaliation provisions cover employees of subsidiaries and affiliates of public companies whose financial information is included in the consolidated financial statements of such public company; and
    - In any action involving sanctions in excess of $1 million, compensates whistleblowers with up to 30%, but not less than 10%, of the amount of the sanctions (within sole discretion of the SEC).

NYSE

- Listed companies must adopt and disclose corporate governance guidelines.
- The NYSE can issue a public reprimand letter to any listed company that violates an NYSE listing standard.

Nasdaq

- Nasdaq requires a review of all related-party transactions for potential conflicts of interest on an ongoing basis by the listed company's audit committee or another independent body of the board of directors.
- A material misrepresentation or omission by an issuer to Nasdaq may result in the company's being delisted.
- Nasdaq can deny relisting to an issuer based upon a corporate governance violation that occurred while that issuer's appeal of the delisting was pending.

The members of the Morgan Lewis Securities Practice are available to advise public companies and their directors and officers with respect to all aspects of corporate governance, including the Sarbanes-Oxley Act of 2002, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, and the corporate governance rules of the SEC and the stock markets.

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