

Securities Regulation and Compliance Alert

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SEC Proposes New Rules on Hedging Policy Disclosures

On February 9, 2015, the U.S. Securities and Exchange Commission (SEC) released proposed rules to implement Section 955 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). Dodd-Frank amended Section 14 of the Exchange Act to add paragraph (j), which directs the SEC to issue rules requiring companies to disclose whether they permit employees and directors to hedge the company's securities.

The proposed rules would add the following new paragraph (i) to Item 407 of Regulation S-K:

(i) **Employee, officer and director hedging.** In proxy or information statements with respect to the election of directors, disclose whether the registrant permits any employees (including officers) or directors of the registrant, or any of their designees, to purchase financial instruments (including prepaid variable forward contracts, equity swaps, collars, and exchange funds) or otherwise engage in transactions that are designed to or have the effect of hedging or offsetting any decrease in the market value of equity securities —

(1) Granted to the employee or director by the registrant as part of the compensation of the employee or director; or

(2) Held, directly or indirectly, by the employee or director.

The proposed rules would require this hedging policy disclosure in any proxy statement or information statement with respect to the election of directors and would generally apply to all companies subject to the federal proxy rules, including smaller reporting companies, emerging growth companies, business development companies and registered closed-end investment companies with shares listed and registered on a national securities exchange. The proposed rules largely parallel Section 14(j) of the Exchange Act, but include some "principles-based" expansions with respect to the types of transactions covered and the location of the disclosure, as well as some additional clarifications and instructions.

Importantly, neither Section 14(j) of the Exchange Act nor the proposed rules require companies to prohibit hedging or to otherwise adopt practices or a policy addressing hedging by any category of individuals. Rather, as described in the proposing release, the proposed rules are aimed at disclosure and providing "transparency to shareholders ... about whether employees or directors are permitted to engage in transactions that mitigate or avoid the incentive alignment associated with equity ownership."

It is also important to note that many companies already include proxy disclosure concerning their hedging policies in their Compensation Discussion & Analysis

(CD&A) because Item 402(b) of Regulation S-K, which requires disclosure of material information necessary to an understanding of a company's compensation policies, includes hedging policies as an example of the kind of information that should be provided, if material. The proposed rules however, would require broader and more specific disclosures and would apply to additional categories of companies.

Comments on the proposed rules are due 60 days after publication in the Federal Register, and the new disclosure requirements regarding hedging policies will not be effective until the SEC adopts final rules. Companies should consider reviewing their hedging policies in light of the disclosure that may be required and identifying revisions to their current hedging policy disclosures that may be needed for future proxy statements.

A copy of the proposed rules can be found [here](#). For additional information on the proposed rules, including both positive and negative commentary thereon by certain SEC commissioners, please see the [press release](#) issued by the SEC, the [joint statement](#) issued by Commissioners Daniel M. Gallagher and Michael S. Piwowar and the [statement](#) issued by Commissioner Luis A. Aguilar.