Insights: Alerts

Nasdaq Requires Listed Company Disclosure of Third Party Compensation Agreements with Directors and Nominees

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Nasdaq has amended its listing rules to require listed companies to publicly disclose compensation or other payments by third parties to company directors or nominees for director. The new rule, which is designated as Marketplace Rule 5250(b)(3), with additional guidance provided at IM-5250-2, will become effective on August 1, 2016.

New Rule 5250(b)(3)

What must be disclosed? New Rule 5250(b)(3) requires that a Nasdaq listed company disclose the material terms of all agreements and arrangements between any director or nominee for director and any person or entity other than the company (referred to as a "third party") relating to compensation or other payment in connection with such person's candidacy or service as a director of the company. The terms "compensation" and "other payment" are not limited to cash payments and are intended to be interpreted broadly. Exempted from this disclosure requirement are agreements and arrangements that: (i) relate only to reimbursement of expenses in connection with candidacy as a director; (ii) existed prior to the nominee's candidacy (including as an employee of the third party), as long as the company has disclosed the nominee's relationship with the third party in a proxy or information statement or annual report; or (iii) have been disclosed in opposition proxy solicitation materials or in a Form 8-K in the current fiscal year.

When must disclosure be made? Disclosure must be made no later than the date on which the company files or furnishes a proxy or information statement in connection with the company's next shareholders' meeting at which directors are elected (or, if the company does not file proxy or information statements, no later than when the company files its next Form 10-K). In addition, the disclosure must be made a least annually until the earlier of the resignation of the director or one year following the termination of the agreement or arrangement. New Rule 5250(b)(3) does not separately require the initial disclosure of newly entered into agreements or arrangements, provided that disclosure is made for the next shareholders' meeting at which directors are elected.

Where must disclosure be made? Under the new rule, the disclosure must be provided on the company's website or in the proxy or information statement for the next shareholders' meeting at which directors are elected (or, if the company does not file proxy or information statements, in its Form 10-K).

What if the company didn't learn of the compensation agreement or arrangement prior to the time disclosure was required to be made? If a company discovers an agreement or arrangement that should have been disclosed but wasn't, it must make the required disclosure promptly by filing a Form 8-K, where required by SEC rules, or by issuing a press release. Thereafter, the company must comply with the annual disclosure requirements described above. A

listed company is not considered to be out of compliance with listing requirements if the company has undertaken reasonable efforts to identify all third party compensation agreements or arrangements with directors or nominees, including asking each director or nominee in a manner designed to allow timely disclosure, and makes the required disclosure promptly upon discovery of the agreement or arrangement.

Analysis and Implications for Listed Companies

A typical situation where third party compensation agreements may arise is where an individual is nominated or proposed for nomination by a shareholder and has an agreement with the shareholder whereby the shareholder agrees to provide compensation to its nominee in exchange for the nominee's agreement to seek election and serve as a director. Nasdaq believes that any such material third party compensation arrangements are relevant to shareholders and may impact their voting decisions in director elections.

Because a listed company is not likely a party to a third party compensation arrangement, it may not be aware of the arrangement. New Rule 5250(b)(3), however, puts the onus of disclosure on the company, but deems the company to be in compliance, even if it is unaware of the compensation agreement or arrangement, as long as it makes reasonable efforts to identify disclosable third party compensation arrangements. Accordingly, listed companies should include in their annual directors' and officers' questionnaires a question that would elicit the information required to be disclosed under the new rule. A sample question to be added to questionnaires appears below. As always, questionnaires should be distributed to directors and nominees shortly after fiscal year end, with a requirement that completed questionnaires be returned quickly so that there will be adequate time to draft compliant disclosure. The questionnaire also should be given to newly appointed directors.

Sample Question for Listed Company Directors' and Officers' Questionnaire

Question: Are you a party to any agreement or arrangement with any person or entity other than [Name of Company] (a "Third Party"), relating to compensation or other payment in connection with your candidacy or service as a director of [Name of Company]? No information is required with respect to agreements and arrangements that: (i) relate only to reimbursement of expenses in connection with your candidacy as a director; (ii) existed prior to your candidacy (including as an employee of the Third Party), provided the Company has disclosed your relationship with the Third Party in a proxy or information statement or annual report (unless after such disclosure your compensation is materially increased specifically in connection with your candidacy or service as a director); or (iii) have been disclosed in [Name of Company]'s proxy materials or a Form 8-K in the current fiscal year.

___Yes ___No

If you answered yes, please attach a copy of the agreement or describe the material terms of the arrangement:

Related People








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