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January 4, 2007

SECURITIES ALERT

SEC AMENDS EXECUTIVE COMPENSATION DISCLOSURE RULES RELATING TO EQUITY COMPENSATION AWARDS

In a surprise move, on December 22, 2006, the SEC adopted "interim final rules" that amend the executive compensation disclosure rules adopted by the SEC in July 2006. The new rules will be effective immediately upon publication in the *Federal Register* and will apply to 2007 proxy statements and annual reports. Although the interim final rules are effective immediately, they are subject to a 30-day comment period and consequently may be further revised.

The new rules are principally designed to more closely align the reporting of equity-based compensation awards with the related expense reflected in a company's financial statements under FAS 123R. Under FAS 123R, the compensation cost of stock and option awards is recognized over the period in which the employee is required to provide service in exchange for the award. The SEC's executive compensation disclosure rules that were adopted in July 2006 had required that the amount reported in the Summary Compensation Table be the full grant date fair value of the award. Many commentators had expressed concerns that disclosure of the full grant date fair value would overstate compensation earned relative to service rendered for a year and would not necessarily reflect the cost to the company or the benefit to the named executive officer since the actual amounts earned in later years could be substantially different.

In response to these comments, the SEC's new rules require equity-based awards to be reported in the Summary Compensation Table in an amount equal to the dollar amount recognized for such awards for the fiscal year in accordance with FAS 123R, subject to certain qualifications. The full grant date fair value, however, must continue to be reported, but in a new column that has been added to the Grants of Plan-Based Awards Table.

The new rules are intended to provide investors with more complete and useful disclosure about executive compensation and to make the actual cost of executive and director compensation easier to understand. Key aspects of the new rules are summarized below.

SUMMARY COMPENSATION TABLE

- As discussed above, the dollar amount reported in the Stock Awards and Option Awards columns will be the dollar amount of compensation cost recognized for the

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fiscal year in accordance with FAS 123R, before reflecting forfeitures, which are discussed in more detail below. Compensation cost will include both the amounts recorded as compensation expense in a company's income statement for the fiscal year as well as any amounts earned by an officer that have been capitalized on the company's balance sheet for the fiscal year. These new rules more closely align the reporting of equity awards to the amounts that are disclosed in the company's financial statements under FAS 123R.

- In determining the dollar amount of compensation cost recognized, FAS 123R requires a company to estimate at the grant date the number of awards with service-based vesting conditions that will be forfeited. The new rules do not include this estimate of forfeitures in the compensation cost of the award, but rather assume that the named executive officer will perform the requisite service to vest in the award. If the officer ultimately fails to perform the requisite service and forfeits the award, the amount of compensation cost previously disclosed in the Summary Compensation Table will be deducted in the period during which the award is forfeited. Any such forfeitures of awards must also be described in a footnote to the Summary Compensation Table.

- If an award is classified as a "liability" award under FAS 123R, such as an award with a cash-based settlement, the fair value of the award is re-measured at each financial statement reporting date through the date the award is settled. Under the new rules, these re-measurements of "liability" awards, whether positive or negative, must be reported in the Summary Compensation Table for such year.

- The compensation cost for awards with performance-based vesting conditions will only be reported in the Stock Awards and Option Awards columns if it is probable that the performance condition will be achieved. If achievement of a performance condition is not immediately probable, but becomes probable in a subsequent period after the grant date, the proportionate amount of compensation cost based on service previously rendered must be disclosed in the Summary Compensation Table during such subsequent period. Similarly, if achievement of a performance condition was probable, but in a later period became improbable, the amount of compensation cost previously disclosed must be reversed during the period in which achievement of the performance condition became improbable. The reversal of a previously disclosed amount, whether due to forfeiture or a change in the probability of achieving a performance condition, could lead to the disclosure of a negative number in the Stock Awards or Option Awards columns.

- Because FAS 123R became effective for companies in 2006 and did not apply to stock and option awards that were granted in earlier years, the SEC is requiring companies to utilize the FAS 123R modified prospective transition method for purposes of these disclosure rules, without regard to whether such companies have adopted this method for financial reporting purposes. Under this method, a proportionate share of the grant date fair value of equity awards outstanding at the date FAS 123R was adopted will be recognized in the financial statements until those awards are settled.

- The new rules also revise the disclosure regarding salary or bonus forgone at the election of a named executive officer in favor of receiving a non-cash form of compensation. The prior rules allowed companies to choose whether to report such forgone amounts in the Salary or Bonus columns, or the Stock Awards or Option Awards columns. The new rules require companies to report the forgone amount in the Salary or Bonus columns, with footnote disclosure of non-cash compensation that refers to the Grants of Plan-Based Awards Table where the stock, option or non-equity incentive plan award elected is reported.

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GRANTS OF PLAN-BASED AWARDS TABLE

- The new rules revise the Grants of Plan-Based Awards Table by adding a new column (column (l) entitled "Grant Date Fair Value of Stock and Option Awards") to show the full grant date fair value of each equity award on a grant-by-grant basis, computed in accordance with FAS 123R.
- This new column must also reflect the incremental fair value of repriced or materially modified options, stock appreciation rights and similar option-like instruments computed as of the repricing or modification date in accordance with FAS 123R. This disclosure must be made on a grant-by-grant basis.

DIRECTOR COMPENSATION TABLE

- The amendments to the Summary Compensation Table discussed above also revise the corresponding columns in the Director Compensation Table in a similar fashion.
- Because the rules do not have a corresponding Grants of Plan-Based Awards Table for directors, the new disclosures required in column (l) for named executive officers as discussed above must be provided for directors through footnote disclosure to the Director Compensation Table.

DETERMINATION OF NAMED EXECUTIVE OFFICERS

Although the new rules do not amend the definition of named executive officer, such rules will impact the determination of the officers who comprise this group. A company's named executive officers consist of the principal executive officer, the principal financial officer and the three other most highly compensated executive officers who were serving as executive officers at fiscal year end. The determination of these three additional officers is based on total compensation for the fiscal year as reflected in column (j) of the Summary Compensation Table, excluding the change in pension value and nonqualified deferred compensation earnings reflected in column (h) of the table. The identity of these three officers may differ under the new rules because only the FAS 123R compensation cost rather than the full grant date fair value will be reflected in the Stock Awards and Option Awards columns and the compensation cost of pre-2006 awards will be reflected in these columns to the extent required by the modified prospective transition method.

CONTACT INFORMATION

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