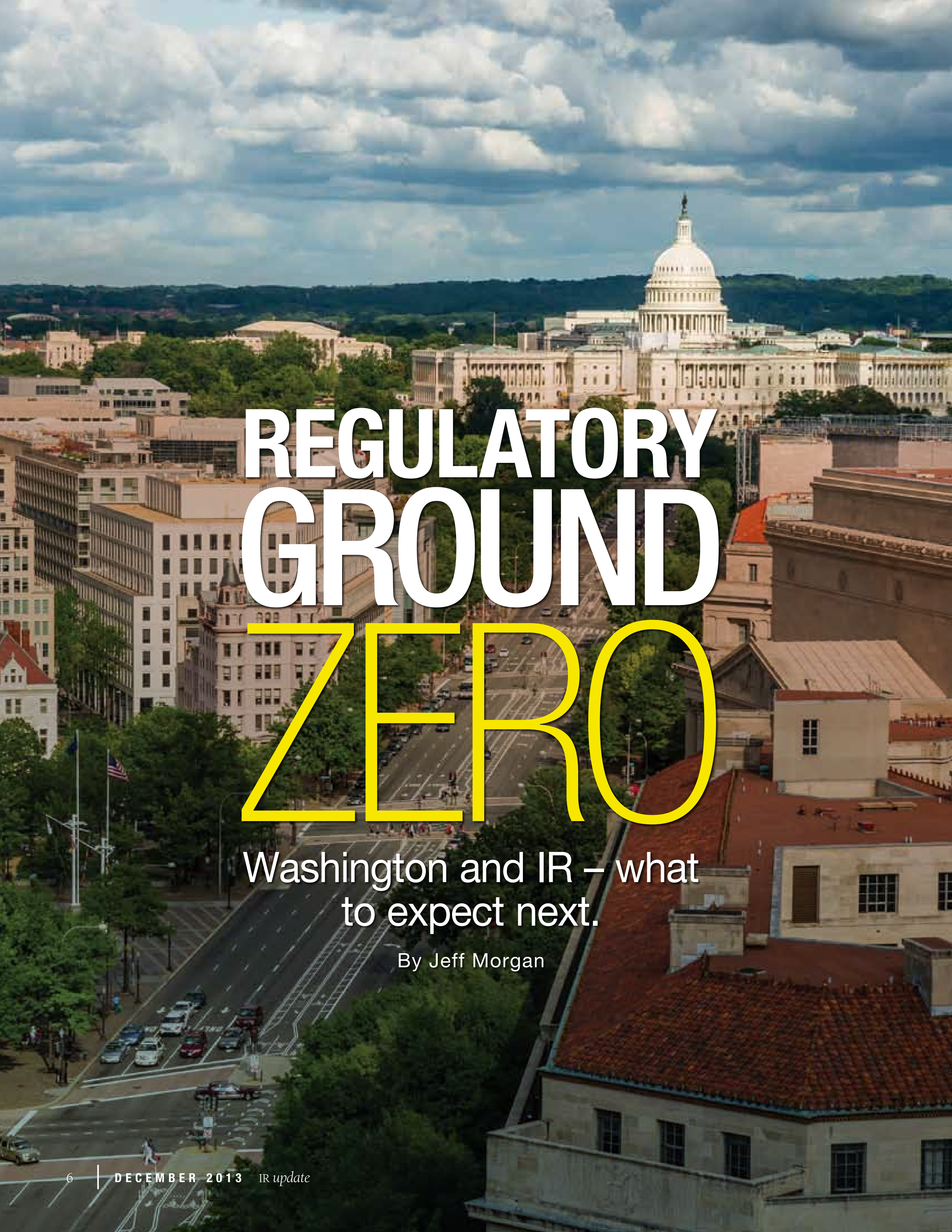

REGULATORY GROUND ZERO

Washington and IR – what to expect next.

By Jeff Morgan

AMERICANS AND IROS HAVE A LOVE/HATE RELATIONSHIP WITH WASHINGTON, DC.

This has come through loud and clear during my tenure as NIRI President and CEO since 2008.

But it's complicated. In speaking with members, you tell me that you can't stand what's happening in DC, yet it's often the first thing I'm asked about, and many of you believe that Washington could do more to help IROs in their jobs.

In surveys, you sometimes say that we talk too much about Washington, yet regulation is ranked as the top topic you want to read about in *IR Update*. Similarly, regulatory sessions often score highest on NIRI Annual Conference attendee surveys.

I understand your frustration and also the inability to look away from the national "train wreck" here in Washington. We are a country with shared concerns, but with serious ideological differences regarding solutions. This plays out in how we choose to allocate federal spending, our views about the fundamental mission of companies, and ultimately in our overall economic growth.

Throw into this mix the notion that regulators (in our case, the Securities and Exchange Commission) have become tools for politicians, and our profession and capital markets are ground zero for what I've been referring to in my chapter presentations as a collision between public companies, DC, and IR.

SEC Staffing and Agenda

To set the stage, let's review recent activity at the SEC. The agency has experienced significant turnover at all leadership levels over the last several years. This unsettled environment has caused some disruptions in the agency's productivity.

The good news is, with the recent appointment of new Chairwoman Mary Jo White, there is now a full complement of five commissioners, with none scheduled to complete their term before 2015. At that point, one commissioner is scheduled to depart each year through 2019.

We've also seen the recent appointment of Keith Higgins, the new head of the Division of Corporation Finance, whom the NIRI Board met with in September. There have been a variety of other recent staff leadership changes as well.

Now fully staffed, I expect the SEC to turn to its outstanding agenda items. Let's review several of these and also a few of NIRI's.

Dodd-Frank

Congress passed Dodd-Frank in 2010, and as of early September and across all agencies involved, about 40 percent of the 400 rulemaking requirements are complete, 28 percent have been proposed, and 32 percent have not yet been proposed.

Notable rulemaking yet to be proposed by the SEC includes rules regarding pay-for-performance disclosure, hedging by employees and directors, and recovery of executive compensation or clawbacks.

The SEC also owes a report to Congress on its study of the costs and benefits of real-time short-sale position reporting, and it may also consider adopting rules on trade reporting, data elements, and real-time public reporting for security-based swaps.

The most recent movement in the Dodd-Frank mandates was the CEO pay-ratio disclosure proposal issued by the SEC in September. NIRI submitted a comment letter, warning that the proposed rule would impose significant costs on issuers while generating disclosures that may confuse many investors and subject companies to unfair peer comparisons. NIRI asked the SEC to narrow the scope of the employees covered by the rule and allow companies to use existing federal wage data to calculate their pay ratios.

Once approved by the SEC (likely in 2014), this disclosure will be used by the press and labor activists to compare and contrast CEO to employee pay. Companies with December 31 fiscal years likely will have to make their first disclosures in the spring of 2016.

I anticipate that corporate comparisons and industry comparisons are just two of the many other ways the media will use this information to create headline-grabbing news that IR professionals and others will have to address. While institutional investors say they find the information to be of little value, consumers, employees, proxy advisory firms, and others will use this information to evaluate your company.

Public companies also face a Dodd-Frank "conflict minerals" disclosure mandate, which will prove quite costly for issuers that use these minerals and have complex supply chains. Unless blocked by a court, most companies will have to submit new conflict mineral reports to the SEC by June 2, 2014.

Shareholder Transparency

NIRI joined with the NYSE and the Society of Corporate Secretaries & Governance Professionals in February in a petition to the SEC requesting Form 13F reform to reduce the filing period of institutional equity ownership positions from 45 days to two days after quarter end.

We believe the current filing delay withholds timely release of material information from the market; that the original objectives underlying 13(f) support reducing the delay period; that the arguments for maintaining a 45-day delay period are unpersuasive given the advances in technology since rule approval in the 1970s; and that a reduction would better align with public company best practices.

Improved ownership transparency has been a consistent theme in my discussions with members. As such, NIRI has made this one of its primary regulatory reform issues, and has made the case repeatedly to the SEC in our annual NIRI Board/SEC staff meetings.

Just as we would like better investor ownership transparency, the institutional investing community wants nothing to do with this improvement, and will use its own advocacy efforts to fight any changes. So this is a long-term goal for NIRI, but small wins, like the SEC recent change to the 13(f) confidential filings process, show the SEC is paying attention to this issue. Next year we hope to see the SEC issue a study on short-selling disclosure that would recommend more disclosure, and that would add energy to a full review of shareholder transparency rules.

JOBS Act

Signed into law in 2012, the Jumpstart Our Business Startups Act, or JOBS Act, includes a number of elements that may have a bearing on our profession. It does the following:

- Creates a new category of "emerging growth" companies (with an IPO after December 2011 and less than $1 billion in sales) that will enjoy some Sarbanes-Oxley and Say-on-Pay exemptions.
- Eliminates the prohibition on general solicitation for Rule 506 Regulation D offerings and sales under Rule 144A.
- Increases the number of investors that a private company may have from 500 to 2,000.
- Creates a new crowdfunding exemption from state and federal securities law registration where issuers and investors may communicate via the Internet in connection with the issuance of new securities provided they meet certain conditions.

The JOBS Act implications are still developing, but my view is that it has the potential to influence IR in several ways. It may:

- Improve the IPO market, leading to more IR jobs.
- Drive demand for private company IR or at least upgraded private company financial communication.
- Lead to larger hedge funds.
- Affect pre-IPO IR, which is changing due to the new confidential S-1 filing option.
- Trigger, many fear, more fraud or boiler-room investment ads, as well as abuse of the "accredited" investor related to the new crowdfunding capital raising process.

Proxy Mechanics

It seems like a lifetime ago that the SEC issued its proxy mechanics concept release in 2010 asking for comments on how to improve the U.S. proxy voting system. The Commission's attention was subsequently diverted to a raft of congressionally mandated Dodd-Frank rulemaking.

The relevant issues included proxy fees, proxy advisors, end-to-end proxy voting integrity, and direct shareholder communication – OBO/NOBO (Objecting Beneficial Owners/Non-Objecting Beneficial Owners). These issues remain outstanding, and NIRI and other organizations like the Shareholder Communications Coalition continue to press for reform.

PUBLIC COMPANIES ALSO FACE A DODD-FRANK "CONFLICT MINERALS" DISCLOSURE MANDATE, WHICH WILL PROVE QUITE COSTLY FOR ISSUERS THAT USE THESE MINERALS AND HAVE COMPLEX SUPPLY CHAINS.

Current State of Affairs

Fast forward three years and where are we today?

On proxy fees, the NYSE Proxy Fee Advisory Committee (PFAC) recommended new fees (lower fees for large issuers, higher fees for smaller); fee alignment and oversight on Notice & Access fees; stratified NOBO lists enabling issuers to acquire certain portions of their NOBO lists; and an enhanced broker Internet platform, which would provide incentives for brokers to offer electronic proxy voting to their customers.

In October, the SEC finally approved the PFAC proposal. Following this action, a new chapter opens on the next steps required to move toward improved shareholder engagement via proxy mechanisms.

NIRI still desires fee transparency as explained in our March 2013 SEC comment letter. NIRI believes that a third-party audit of proxy distribution fees is the best way to ensure that fees are reimbursed fairly, equitably, and objectively, thereby eliminating the vested interests of those involved directly and indirectly in the process. The PFAC proposal does not include a recommendation to initiate an independent audit of these fees. Without transparency, many issuers will continue to question the accuracy of proxy fees.

Regarding proxy advisor and shareholder communication reform, NIRI testified before Congress on these issues in June. NIRI's concerns about proxy advisory firms stem from the fact that they remain largely unregulated and unsupervised, while substantial concerns have been raised by companies and academics about: (1) a lack of transparency concerning their standards, procedures, and methodologies; (2) the risk that their voting recommendations may be based on incorrect factual information; and (3) the inherent conflicts of interest posed by several of their business practices. In response to these concerns, which have been expressed by other business groups, the SEC scheduled a December 5 roundtable on proxy advisors. We continue to be hopeful that Washington will act to ensure these firms meet minimum standards.

Fundamental Disclosure Reform?

It remains to be seen how many of the above non-mandated items the "new" SEC will address. It is not uncommon for a new SEC regime to turn the page on past priorities and focus on different areas.

So it was with great interest that I read Chairwoman White's October speech in which she seemed to suggest that our current public company disclosure structure is leading to information overload, and that the SEC might use its JOBS Act emerging growth company disclosure requirements review as a jumping-off point for a broader, more comprehensive review that, ". . .will move us forward on the path to more optimal disclosure. It is an important priority for me." I am sure you will agree that it is an important priority for NIRI members as well as we move into 2014.

I also expect the SEC, exchanges, and others to continue in 2014 to have discussions and evaluate issues related to how our capital markets function, and how they ought to function in the name of fairness and investor protection. The technical hiccups in our markets during the last several years have highlighted the need for issuers to keep a close eye on these developments.

In conclusion, while Washington is often a source of irritation for us all, it is an area that affects IR and is part of the evolving landscape that also includes the overall evolution in capital markets, changing communication mediums, and changing demands from investors.

The benefit of this ongoing uncertainty is that it has led IR professionals to be highly adaptable to changing expectations. So as we head into 2014, let's hope for productivity in Washington that leads to positive change for IROs, our companies, and the investing community. IRU

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