

# Securities Update

## SEC ISSUES UPDATED GUIDANCE ON FORM 8-K FILING REQUIREMENTS

On April 3, 2008, the SEC Staff issued updated guidance regarding Form 8-K disclosure requirements. The update includes guidance on amendments to Form 8-K that became effective on December 29, 2006, regarding disclosure of compensatory arrangements with executive officers, which had not previously been addressed in the SEC's guidance. In addition, the updated guidance incorporates and, in some places, modifies existing interpretations regarding Form 8-K that were previously found in two separate SEC publications: (i) *The Manual of Publicly Available Telephone Interpretations*, dated July 1997 and (ii) *Frequently Asked Questions Regarding the Use of Non-GAAP Financial Measures*, dated June 13, 2003. Finally, the updated Form 8-K guidance contains clarifications on a number of new topics.

In this Securities Update, we highlight key aspects of the updated Form 8-K guidance. Since the largest group of updates relates to compensation arrangements with executive officers and the retention and termination of directors and executive officers, we have provided a summary of these updates first. We then describe other updates and changes to the Form 8-K guidance. In general, we have not repeated interpretations that were contained in the previous version of the guidance or that were incorporated from the other SEC publications described above.

### Compensatory Arrangements of Certain Officers [Item 5.02(e)]

Item 5.02(e) of Form 8-K requires the filing of a Form 8-K upon the adoption or amendment of a material compensatory plan in which the company's principal executive officer, principal financial officer, or a named executive officer participates, or the making or amendment of a material grant or award under any such plan to any such person. This item became effective on December 29, 2006 and was not previously addressed in the SEC's Form 8-K guidance. The new guidance provides as follows:

- (1) *Equity compensation plans.* If the adoption or amendment of a material equity compensation plan in which named executive officers are eligible to participate is subject to shareholder approval, the obligation to file a Form 8-K is triggered upon receipt of shareholder approval. In addition, termination of a material equity compensation plan also triggers a filing obligation under Item 5.02(e).
- (2) *Cash bonus plans.* The adoption of a material cash bonus plan in which named executive officers are eligible to participate triggers an obligation to file a Form 8-K even if no specific performance goals or bonus opportunities have been communicated to plan participants.

The White & Case LLP Securities Update provides a brief overview of some of the latest legislative, regulatory and judicial actions, policy statements and decisions that affect public and private companies.

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- (3) *Specific performance goals.* The adoption of specific performance goals and business criteria does not trigger an obligation to file a Form 8-K if those goals and criteria are materially consistent with the terms of the plan previously disclosed (e.g., the plan disclosed that goals would be based on EBITDA and the goals and criteria set EBITDA targets).
- (4) *Cash awards.* Payment of a cash award to a named executive officer upon determining that applicable performance goals and criteria have been satisfied does not trigger an obligation to file a Form 8-K, provided that the payment was consistent with the terms of the plan as previously disclosed. However, disclosure on Form 8-K is required if (i) the payment was inconsistent with the previously disclosed terms of the plan or (ii) performance criteria were not satisfied and the payment was made on a discretionary basis *even if the plan provided for the exercise of discretion.*

Notwithstanding the foregoing, disclosure under Item 5.02(e) is not required upon payment of a cash bonus to a named executive officer pursuant to that officer's employment contract when that contract provides that the amount of the bonus is to be determined by the compensation committee in its sole discretion. Under this circumstance, disclosure will instead be included in the company's Compensation Discussion and Analysis in its Form 10-K (the CD&A).

### Practical Implication

The distinction drawn by the SEC in the previous two paragraphs appears to turn on whether the decision to grant the award was permitted to be made on an entirely discretionary basis compared to a situation where it involved an exercise of discretion after a named executive officer failed to meet agreed performance targets.

- (5) *Competitive harm.* Disclosure of target levels with respect to specific quantitative or qualitative performance is not required if such disclosure would result in competitive harm for the company. This is consistent with the approach adopted for such information in the CD&A.

## Election and Termination of Directors [Items 5.02(b) and 5.02(d)]

Item 5.02(b) requires the filing of a Form 8-K upon the retirement, resignation, removal, or refusal to stand for re-election of any of a company's directors. Item 5.02(d) requires the filing of a Form 8-K upon the election of a new director. The new guidance provides as follows:

- (1) *Resignation, retirement or refusal to stand for re-election.* The resignation, retirement or refusal to stand for re-election by a director is triggered by a notice of a decision to resign, retire or refuse to stand for re-election, irrespective of whether such notice is conditional or subject to acceptance. Mere discussion or consideration of resignation, retirement or refusal to stand for re-election do not trigger an Item 5.02(b) reporting obligation.

### Practical Implication

Companies should ensure that their disclosure controls and procedures will result in any notice by a director of a decision to resign, retire or refuse to stand for re-election from a director being provided promptly to the company's general counsel so that appropriate disclosure can be made.

- (2) *Election to the board.* The election of an individual to the board other than by a vote of security holders must be disclosed as of the date of such election, even if the date on which the director's term begins is at a later date. The disclosure provided under Item 5.02(d) should include the date on which the term begins.

## Appointment and Termination of Certain Executive Officers [Items 5.02(b) and 5.02(c)]

Item 5.02(b) requires the filing of a Form 8-K upon the retirement, resignation or termination of a company's principal executive officer, president, principal financial officer, principal accounting officer, principal operating officer or any person performing similar functions, or any named executive officer. Item 5.02(c)

requires the filing of a Form 8-K upon the appointment of the company's principal executive officer, president, principal financial officer, principal accounting officer, principal operating officer, or any person performing similar functions.

- (1) *Temporary termination.* A temporary termination of a principal financial officer (e.g., a temporary transfer of his or her duties to another person) triggers an obligation to file a Form 8-K to report that the original principal financial officer has temporarily stepped down. A subsequent "re-appointment" triggers a new Form 8-K filing.
- (2) *Timing of obligation tied to notice.* The obligation to file a Form 8-K under Item 5.02(b) is triggered by a notice of termination provided to a named executive officer pursuant to the terms of his or her employment agreement, not by the date on which employment actually ends.
- (3) *Delay until public announcement.* The instructions to Item 5.02(c) permit a company to delay disclosure on Form 8-K of the appointment of a new principal executive officer, president, principal financial officer, principal accounting officer, principal operating officer, or person performing similar functions until the date that the company makes a public announcement of such appointment. The SEC has clarified that the announcement of the appointment of such individual to the board of directors (under Item 5.02(d)) and of any compensatory plan or contract (under Item 5.02(e)) may also be delayed until such announcement.

## Material Definitive Agreements [Items 1.01 and 1.02]

Item 1.01 requires the filing of a Form 8-K upon the entry into, or the amendment of, a material definitive agreement not made in the ordinary course of business. Item 1.02 requires the filing of a Form 8-K upon the termination, otherwise than by expiration on its stated termination date or as a result of all parties completing their obligations, of a material definitive agreement not made in the ordinary course of business provided that such termination is material to the company.

- *Description required.* Item 1.01(a)(2) of Form 8-K requires "a brief description of the terms and conditions of the agreement or amendment that are material to the registrant." Mere incorporation by reference of an agreement (e.g., when the agreement is filed as an exhibit to the Form 8-K) does not satisfy the disclosure requirement. Accordingly, it may make sense in the case of agreements that are particularly brief to disclose all of the terms of the agreement in the body of the Form 8-K.

## Completion of the Acquisition or Disposition of Assets [Item 2.01]

Item 2.01 requires the filing of a Form 8-K upon the completion by the company of acquisition or disposition of a significant amount of assets.

- *Timing of obligation tied to disposition.* Item 2.01 of Form 8-K, which calls for disclosure of the acquisition or disposition of a significant amount of assets, does not require disclosure of the execution of a contract to acquire or dispose of the assets. However, there may still be an obligation to report the execution of the contract under Item 1.01 regarding the execution (or material amendment) of a material definitive agreement not made in the ordinary course of business.

## Triggering Events that Accelerate or Increase a Direct Financial Obligation or an Obligation Under an Off-Balance Sheet Arrangement [Item 2.04]

Item 2.04 requires the filing of a Form 8-K upon the occurrence of certain events that accelerate or increase a direct financial obligation or an obligation under an off-balance sheet arrangement.

- (1) *Voluntary redemptions.* A voluntary redemption of convertible notes by a company is not a triggering event for the purposes of Item 2.04.

(2) *Notices of default.* Even if a company disagrees with a legitimacy of a notice of default and brings the matter to arbitration under the terms of the applicable loan agreement, Item 2.04 is still triggered by the notice of default. The company may disclose in the Form 8-K the reasons for its belief that no event of default has occurred.

### Notice of Delisting or Failure to Satisfy a Continued Listing Rule or Standard; Transfer of Listing [Item 3.01]

Item 3.01 requires the filing of a Form 8-K upon (a) receipt from the national securities exchange or national securities association that maintains the principal listing for any class of the company's common equity of a notice of delisting or failure to satisfy a continued listing rule or standard, (b) the provision by the company to such exchange or association of a notice of the company's material noncompliance with a rule or standard for continued listing on the exchange or association, (c) the receipt by the company of a public reprimand letter, or (d) the withdrawal of the listing from the national securities exchange or transfer of the listing or quotation to another securities exchange or quotation system.

- *OTC trading.* A company whose securities are traded on the OTC Bulletin Board is not required to file a Form 8-K under Item 3.01 upon submitting a listing application to a stock exchange or upon approval of such application. This is because the OTC Bulletin Board is neither an automated inter-dealer quotation system of a registered national securities association nor a stock exchange as required by Item 3.01.

#### Practical Implication

In addition to the different types of companies whose securities are traded on the OTC Bulletin Board, the securities of companies that enter Chapter 11 proceedings are generally delisted from Nasdaq, the NYSE or AMEX

and subsequently trade on the OTC Bulletin Board. The above interpretation clarifies that such companies can submit an application to relist on an exchange without triggering a disclosure requirement under Item 3.01 of Form 8-K.

### Unregistered Sales of Equity Securities [Item 3.02]

Item 3.02 requires the filing of a Form 8-K upon the sale of equity securities in a transaction that is not registered under the Securities Act of 1933.

- (1) *Stock option grants.* A grant of stock options pursuant to an employee stock option plan that does not constitute a "sale" or "offer to sell" under Section 2(a)(3) of the Securities Act need not be reported as an unregistered sale of securities under Item 3.02.

#### Practical Implication

A grant of stock options for compensatory purposes is generally not considered a sale or offer to sell and therefore is not required to be registered or subject to an exemption from registration.<sup>1</sup> Conversely, the issuance of shares upon the exercise of stock options is required to be registered or subject to an exemption from registration (and would generally be registered on Form S-8 in the case of a company that is subject to reporting obligations under the Exchange Act). As a result, the practical implications of the guidance are limited in the context of stock options. Nevertheless, one would expect that interpretation also applies to a grant of bonus shares, which, subject to certain conditions, is not considered a sale or offer to sell and could involve the issuance of more than one percent of a class of a company's outstanding shares.<sup>2</sup>

<sup>1</sup> Manual of Publicly Available Telephone Interpretations (July 1997) at G.61.

<sup>2</sup> See *Release No. 33-6188*, 1 Fed. Sec. L. Rep. (CCH) ¶ at 2073-15 n.84 (Feb. 1, 1980).

(2) *Unregistered sales of certain shares.* The sale, in an unregistered transaction, of shares of a class of equity securities that *is not currently outstanding* in excess of one percent of a company's outstanding shares triggers a reporting obligation under Item 3.02.

#### Practical Implication

Public companies rarely issue shares of a new class of securities. However, if such an issuance is made in any amount, it triggers a reporting obligation under Item 3.02 because it will, by default, result in the issuance of more than one percent of the class. Voluntary filers are more likely to engage in such issuances and should be aware of this requirement.

(3) *Agreements to issue securities.* Item 3.02 of Form 8-K is triggered when a company enters into an agreement that is enforceable against the company to issue securities to a third party in exchange for services from that party. The triggering event is the execution of the agreement, not the provision of the services or the issuance of securities.

(4) *Agreements to sell certain warrants or options.* Item 3.02 of Form 8-K is triggered when a company enters into an agreement for the unregistered sale of warrants or options to purchase equity securities or notes convertible into equity securities if the one percent volume threshold in Item 3.02 is exceeded with respect to the underlying equity securities. If the initial Form 8-K discloses the maximum amount of underlying equity securities that may be issued, a subsequent Form 8-K need not be filed upon exercise of the warrant or options or conversion of the notes.

#### Practical Implication

Issuers entering into a convertible note purchase agreement (or a similar agreement with respect to the unregistered issuance of securities convertible or exercisable for equity securities) should disclose in the initial Form 8-K filed under Item 3.02 the maximum amount of equity securities that may be issued. This will avoid the need to file another Form 8-K upon issuance of such securities.

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