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Considering Director Independence

Since the enactment of the Sarbanes-Oxley Act of 2002, public company boards of directors have been operating in an environment of increased emphasis on and regulation of director independence. New York Stock Exchange and Nasdaq Stock Market listing standards and Securities and Exchange Commission rules have established both subjective and objective mandates for director independence. Moreover, institutional investors and proxy advisory firms have adopted their own, often differing and demanding, expectations about director independence.

The broad inquiries that boards must now undertake in connection with independence determinations necessarily intertwine with the conflicts involved in related person transactions and the business and personal activities of directors outside of the boardroom. Not all outside transactions and relationships impugn a director's independence. But, in the new world order of corporate governance, it is clear that public company boards must have appropriate controls and procedures to ensure that directors constantly consider all of the transactions and relationships that may impact their independence or trigger affirmative disclosure obligations.

To assist boards in addressing these issues, this advisory summarizes the patchwork of director independence criteria resulting from the NYSE and Nasdaq listing standards, SEC rules and perspectives of institutional investors.¹ We also highlight disclosure obligations triggered by related person transactions. Finally, we present for directors' consideration certain points regarding the need to monitor continually the transactions and relationships that impact independence determinations and related person disclosure obligations, so as to avoid noncompliance with applicable regulatory standards. This is not, however, a "how to" manual regarding the adoption of policies and procedures to identify and evaluate director independence, related person transactions and other personal and business relationships. Rather, it is a reminder that these topics are tightly interwoven and dynamic, as well as a recommendation that directors stay alert and perceptive throughout the year to changes in their status that may affect their independence or otherwise require disclosure.

¹ There are currently pending proposed amendments to the NYSE's corporate governance listing standards for approval by the SEC. See Amendment No. 2 to SEC File No. 2005-81 (filed with the SEC on Jun. 20, 2007), available at [http://apps.nyse.com/commdata/pub19b4.nsf/docs/0345D4493935539A85257300007745F7/\\$FILE/NYSE-2005-81%20A-2.pdf](http://apps.nyse.com/commdata/pub19b4.nsf/docs/0345D4493935539A85257300007745F7/$FILE/NYSE-2005-81%20A-2.pdf) (the "NYSE Amendments"). If adopted as proposed, the amendments would amend the listing standards by eliminating disclosure obligations that are duplicative with, or otherwise addressed by, the SEC's disclosure requirements under Item 407 of SEC Regulation S-K. This advisory notes such proposals where relevant.

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DIRECTOR INDEPENDENCE STANDARDS

A summary of the various independence standards applicable to directors of public companies follows. In the main, this involves a review of the explicit regulatory tests that public company directors must meet in order to satisfy independence requirements. This section also highlights the independence criteria developed by Institutional Shareholder Services (“ISS”) and the Council of Institutional Investors (“CII”), often bell-weather for the views of public and ERISA pension plan investors.

NYSE and Nasdaq Listing Standards Regarding Director Independence

The NYSE and Nasdaq listing standards require that the majority of directors of a listed company be independent within 12 months of the company’s listing date.² Subject to the requirements of Rule 10A-3 under the Securities Exchange Act of 1934 (discussed below), board committees must be completely independent by the same date.³ The NYSE and Nasdaq listing standards require that the company’s board of directors make independence determinations based on both subjective and objective criteria. The following sections address the subjective independence criteria and *Appendix A* summarizes the objective independence criteria adopted by the NYSE and Nasdaq.⁴

² The NYSE and Nasdaq provide a controlled company (*i.e.* a company with respect to which an individual, group or another company holds greater than 50% of its voting power) with exemptions from board and committee composition requirements.

There are also exemptions from the NYSE and Nasdaq corporate governance listing standards for foreign private issuers. The NYSE listing standards permit foreign private issuers to follow home country practices in lieu of the NYSE corporate governance requirements (other than requirements related to audit committees, submissions of written affirmations, and disclosures of significant ways in which the foreign private issuer’s home country governance practices differ from those under the NYSE listing standards). Nasdaq listing standards require a foreign private issuer to request that Nasdaq grant an exemption from its corporate governance listing standards when such standards are contrary to (A) law or regulation of public authorities exercising jurisdiction over the foreign private issuer or (B) generally accepted business practices in the issuer’s home country. Nasdaq will not grant any exemption that would be contrary to the federal securities laws. Foreign private issuers that receive exemptions from compliance with Nasdaq corporate governance listing standards must disclose in their annual reports filed with the SEC (and, if applicable, registration statements in connection with initial public offerings) each requirement from which they are exempted and describe the home country practice, if any, followed in lieu of such requirement.

³ A company listing on the NYSE or Nasdaq in connection with its initial public offering may transition into compliance with board committee composition requirements. To this end, the audit, compensation and nominating committees of such company are required to (i) include one independent member at the time of initial listing, (ii) be composed of a majority of independent members within 90 days following initial listing, and (iii) be completely independent within one year of initial listing. The NYSE distinguishes between the audit committee and the compensation and nominating committees, however, for what constitutes initial listing. For purposes of nominating and compensation committee composition requirements, the NYSE considers a company to be listing in conjunction with an initial public offering if, immediately prior to listing, it does not have a class of common stock registered under the Exchange Act. For audit committee composition requirements, the NYSE considers a company to be listing in conjunction with an initial public offering only if the company was not, immediately prior to the effective date of a registration statement, *required* to file reports with the SEC under Section 13(a) or 15(d) of the Exchange Act. The NYSE Amendments would treat the listing of securities of a company that was a voluntary filer as a listing in connection with an initial public offering. A company that is listing on the NYSE in connection with its emergence from bankruptcy or because it has ceased to be controlled company may also phase in independent nominating and compensation committees and its independent board majority on the same schedule as a company listing in connection with its initial public offering. Nasdaq does not distinguish between the audit committee and the compensation and nominating committees with respect to what constitutes initial listing on Nasdaq. Nasdaq determines initial listing based on whether the company, immediately prior to listing on Nasdaq, was required to file reports with the SEC under Section 13(a) or 15(d) of the Exchange Act.

⁴ See NYSE Listed Company Manual §303A.01 and Nasdaq Marketplace Rule 4350 for the NYSE’s and Nasdaq’s, respectively, subjective independence criteria.

NYSE Subjective Criteria. Under the NYSE listing standards, a director is only independent if the board affirmatively determines that the director has no material relationship with the listed company, either directly or as a partner, shareholder or officer of an organization that has a relationship with the listed company.⁵ The NYSE views a director's relationship with a listed company's management as one that should be considered as being between the director and the listed company. NYSE commentary provides that, in making independence determinations, it is best for boards to broadly consider all relevant facts and circumstances, including from the point of view of both the director and the persons or organizations with which the director has relationships.

NYSE listing standards also require listed companies to disclose in their proxy statements or Forms 10-K the identity of their independent directors and the basis for any board determination that any relationship or transaction is immaterial. Boards of NYSE-listed companies may adopt categorical standards to assist them in making independence determinations and make a general disclosure if a director meets such standards. Listed companies must disclose such standards and specifically explain the bases of independence determinations for directors who do not meet such standards. Proposed amendments to the commentary to NYSE Listed Company Manual § 303A.02(a), however, would eliminate these disclosure obligations (although not the duties imposed on listed company board's to make such independence determinations), because they are included among the disclosure obligations imposed on public companies under Item 407(a) of SEC Regulation S-K.⁶

Nasdaq Subjective Criteria. Under Nasdaq listing standards, a director is considered independent only if the director is not an officer or employee of the listed company and the listed company's board affirmatively determines that the director does not have any relationship which would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. Nasdaq-listed companies are required to disclose the identity of their independent directors in their proxy statements or Forms 10-K. Unlike the current NYSE listing standards, the Nasdaq listing standards do not require disclosure of relationships or transactions determined by the board not to interfere with a director's independent exercise of judgment in carrying out his or her responsibilities as a director.⁷

Nasdaq-listed companies are afforded a grace period in which to cure noncompliance with Nasdaq's director independence requirements if the noncompliance is due to a vacancy on the board or to one director ceasing to be independent due to circumstances beyond the director's control. In such instances, the listed company generally must regain compliance by the earlier of its next annual shareholders meeting or one year from the occurrence of the event that led to the noncompliance. However, if the company's annual meeting occurs no later than 180 days following the event that caused the member to no longer be independent, the company has 180 days from the date of such event to regain compliance. Listed companies that rely on this cure period must notify Nasdaq immediately upon learning of the event or circumstance that caused the noncompliance.

⁵ A "material relationship" for purposes of NYSE listing standards may include a commercial, industrial, banking, consulting, legal, accounting, charitable or familial relationship.

⁶ See the NYSE Amendments.

⁷ Disclosure of these transactions, however, is required under Item 407(a)(3) of SEC Regulation S-K. See "SEC Rules Regarding Director Independence" below.

Special Independence Requirements Applicable to Board Committees

In addition to the general requirement that boards of listed companies have a majority of independent directors, there are special rules requiring that all members of listed companies' audit, compensation and nominating committees, to the extent established, must be independent.⁸

Special Requirements for Audit Committees. Through the Sarbanes-Oxley Act, Congress required the SEC to direct national securities exchanges and national securities associations to prohibit the listing of any security of an issuer that does not have an audit committee that complies with the requirements set forth in Section 301 of the Act.⁹ In accordance with this mandate, the SEC adopted Exchange Act Rule 10A-3, which established minimum requirements for audit committees to be included in the listing standards of national securities exchanges and national securities associations. Both the NYSE and Nasdaq have adopted listing standards applicable to audit committees of listed companies that are consistent with the SEC's minimum requirements under Rule 10A-3(b), including the SEC's independence standard for audit committee members under Rule 10A-3(b)(1).¹⁰ In addition, audit committee members of NYSE- and Nasdaq-listed companies must meet the general director independence standards established by the NYSE or Nasdaq (as applicable).¹¹

⁸ NYSE-listed companies are required to establish separate audit, nominating and compensation committees, or with respect to nominating or compensation committees, delegate the responsibilities of those committees to other separate board committees. Nasdaq-listed companies are required to establish separate audit committees, but may delegate the responsibilities of the nominating and compensation committees to a majority of the board's independent directors in lieu of establishing separate compensation or nominating committees. All public companies that determine not to establish separate nominating or compensation committees must disclose the basis for such determination in their proxy statements. See Items 407(c) and 407(e) of SEC Regulation S-K.

⁹ Section 301 of the Sarbanes-Oxley Act requires that the audit committee of each listed issuer

- be composed of independent directors;
- be responsible for the appointment, compensation and oversight of the issuer's independent auditors;
- establish procedures for
 - the receipt, retention, and treatment of complaints received by the issuer regarding accounting, internal accounting controls, or auditing matters; and
 - the confidential, anonymous submission by the issuer's employees of concerns regarding questionable accounting or auditing matters;
- have the authority to engage independent counsel and other advisers; and
- have appropriate funding (as determined by the audit committee) for payment of compensation to any such advisors retained by the audit committee and the company's independent auditors.

¹⁰ To be considered independent under Exchange Act Rule 10A-3(b)(1), a director who is an audit committee member may not, other than in his or her capacity as a member of the audit committee, the board or any other board committee

- accept directly or indirectly any consulting, advisory or other compensatory fee from the issuer or any subsidiary (excluding, unless applicable listing criteria provide otherwise, receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the issuer, provided that such compensation is not contingent in any way on continued service); or
- be an affiliated person of the issuer or any subsidiary thereof.

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In addition to meeting these special independence requirements, audit committee members must satisfy competence qualifications. Under the NYSE listing standards,

Under Rule 10A-3(e)(1), an “affiliated person” is one who directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the issuer or any subsidiary thereof, and, any of the following:

- an executive officer of an affiliate;
- a director who also is an employee of an affiliate;
- a general partner of an affiliate; or
- a managing member of an affiliate.

The SEC has a safe harbor to prevent certain beneficial owners of the issuer’s equity securities from being deemed to control the issuer (or any subsidiary thereof). A person will not be deemed to control an issuer (or any subsidiary thereof) if such person is not

- a beneficial owner, directly or indirectly, of more than 10% of any class of voting equity securities of the issuer (or any subsidiary thereof); and
- an executive officer of the issuer (or any subsidiary thereof).

Under Rule 10A-3(e)(8), “indirect” acceptance by a member of an audit committee of any consulting, advisory or other compensatory fee includes acceptance of such a fee by

- the member’s spouse, minor child or stepchild or a child or stepchild sharing a home with the member, or
- by an entity
 - in which such member is a partner, member, an officer such as a managing director occupying a comparable position or executive officer, or occupies a similar position (except limited partners, non-managing members and those occupying similar positions who, in each case, have no active role in providing services to the entity), and
 - which provides accounting, consulting, legal, investment banking or financial advisory services to the issuer or any subsidiary of the issuer.

Therefore, for example, a director who is a partner in a law firm would not be independent for audit committee purposes if the director’s law firm provided any services to the company or any subsidiary of the company.

See Exchange Act Rule 10A-3(e)(1)(ii).

¹¹ In what may be viewed as an expansive interpretation of its audit committee independence standards, Nasdaq has notified a listed company that it did not view as independent an audit committee member who, three months prior to his appointment to the board, received a grant of 45,000 non-exercisable stock options in consideration for providing consulting services to the company. The agreement between the former consultant and the listed company provided that if the consultant were later appointed to the listed company’s board, the stock option grant would be in lieu of the initial stock option grant of 45,000 shares made to non-employee directors upon joining the board. None of the stock options had vested prior to the former consultant’s election to the board, and the former consultant did not receive any additional stock options upon joining the board. Nevertheless, Nasdaq required that the former consultant’s stock options be valued in accordance with the Black-Scholes option pricing model as of the grant date and deemed the former consultant not independent under Nasdaq listing standards. Nasdaq viewed the receipt of such stock options as the receipt of payment from the company in excess of \$60,000 (the then-applicable monetary threshold for independence determinations under Nasdaq listing standards) for other than compensation for board or board committee service. See Current Report on Form 8-K of Applied Materials, Inc. (filed Mar. 20, 2006).

- audit committee members must be financially literate (as determined in the business judgment of the listed company's board),¹² and
- with respect to any member of an NYSE-listed company's audit committee who serves on the audit committees of more than three public companies, if the listed company does not limit the number of audit committees on which its audit committee members may serve to three or less, the listed company's board must make an express determination that such simultaneous service does not impair the member's ability to serve effectively on the listed company's audit committee.¹³ The listed company is required to disclose any such determination in its proxy statement or Form 10-K.

Under Nasdaq listing standards, audit committee members must

- be able to read and understand a company's fundamental financial statements, and
- not have participated in the preparation of the listed company's (or its subsidiaries') financial statements at any time during the past three years.¹⁴

Each public company also must disclose in its proxy statement or Form 10-K whether it has an "audit committee financial expert" on its audit committee and, if not, why not.¹⁵

¹² An audit committee of an NYSE-listed company also must include at least one member who possesses accounting or financial management expertise, as interpreted by the listed company's board in its business judgment.

¹³ Under proposed amendments to the commentary to Section 303A.07, a listed company would be required to make such a determination with respect to any director who serves on the audit committees of more than three public companies, regardless of whether the listed company limits the number of audit committees on which its audit committee members may serve.

¹⁴ Audit committees of Nasdaq-listed companies also must include at least one member who has (i) past employment experience in finance or accounting, (ii) requisite professional accounting certifications, or (iii) any other comparable experience that results in the individual's financial sophistication.

¹⁵ Under Item 407(d)(5)(ii) of SEC Regulation S-K, an "audit committee financial expert" is a person who

- understands generally accepted accounting principles and financial statements;
- is able to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;
- has experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the issuer's financial statements, or experience actively supervising one or more persons engaged in such activities;
- understands internal control over financial reporting; and
- understands audit committee functions; and

has acquired such attributes through

- education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor, or experience in one or more positions that involve the performance of similar functions;

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Special Requirements for Compensation Committees. Compensation committees must be composed entirely of independent directors. The NYSE listing standards require listed companies to establish a separate compensation committee (or delegate the responsibilities of the compensation committee to another separate committee), while Nasdaq listing standards permit a majority of a listed company's independent directors to carry out the responsibilities of the compensation committee. Under Item 407 of SEC Regulation S-K, however, a listed company that chooses not to establish a compensation committee must disclose in its proxy statement the basis for the board's view that it is appropriate for the listed company not to have such a committee and the identity of each director who participates in the consideration of executive officer and director compensation.¹⁶

Of importance for companies with share-based compensation arrangements, in order for securities transactions between issuers and their officers and directors to be exempt from Section 16(b) of the Exchange Act, committee members must satisfy the requirements for "non-employee directors" under Exchange Act Rule 16b-3(b)(3).¹⁷ Also, Committee members must qualify as "outside directors" for purposes of Section 162(m) of the Internal Revenue Code if the issuer desires to preserve the deductibility under that section of certain compensation paid to executive officers.¹⁸

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- experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions;
 - experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing or evaluation of financial statements; or
 - other relevant experience.

¹⁶ See Item 407(e)(1) of SEC Regulation S-K.

¹⁷ Under Rule 16b-3(b)(1), a "non-employee director" is a director who

- is not currently an officer or employee of the issuer or a parent or subsidiary of the issuer;
- does not receive compensation in excess of the amount that would be required to be disclosed under Item 404(a) of SEC Regulation S-K (currently \$120,000), either directly or indirectly, from the issuer or a parent or subsidiary of the issuer, for services rendered as a consultant or in any capacity other than as a director; and
- does not possess an interest in any other transaction for which disclosure would be required under Item 404(a) of SEC Regulation S-K.

Alternatively, the exemptions provided under Rule 16b-3 may be perfected by approval of the transaction at issue by the issuer's full board of directors, a committee of the issuer's board composed solely of two or more non-employee directors or a majority of the issuer's shareholders entitled to vote with respect to the transaction.

¹⁸ A director is an "outside director" for purposes of Section 162(m) if the director

- is not a current employee of the company;
- is not a former employee of the company who receives compensation for prior services (other than benefits under a tax-qualified retirement plan) during the taxable year;
- has not, at any time, been an officer of the company or a current affiliate of the company; and
- does not receive remuneration from the company, either directly or indirectly, in any capacity other than as a director. For this purpose, remuneration includes any payment (other than certain *de minimis* remuneration) in

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Special Requirements for Nominating Committees. Nominating committees must be composed entirely of independent directors. The NYSE listing standards require a listed company to establish a separate committee (or delegate the responsibilities of the nominating committee to another separate committee), while Nasdaq listing standards permit a majority of the listed company's independent directors to carry out the responsibilities of the nominating committee. Under Item 407(c)(1) of SEC Regulation S-K, a listed company that chooses not to establish a separate nominating committee must disclose in its proxy statement the basis for the board's view that it is appropriate for the listed company not to have such a committee and the identity of each director who participates in the consideration of director nominees.

NYSE and Nasdaq Cure Provisions. Both the NYSE and Nasdaq listing standards provide listed companies with the opportunity to cure unintentional non-compliance with audit committee composition requirements. If an audit committee member ceases to be independent for reasons outside of the member's reasonable control, the audit committee member is permitted to remain on the audit committee until the earlier of either the listed company's next annual shareholders' meeting or one year from the occurrence of the event that caused the member to no longer be independent.¹⁹

In addition, Nasdaq listing standards permit one director who is neither independent nor an officer or employee of the listed company or a family member²⁰ of any of the company's officers or employees, to serve on the audit, nominating or compensation committee for a maximum of two years if

- such committee consists of three or more members;
- the board, under exceptional and limited circumstances, determines that such person's membership on the committee would be in the best interests of the listed company; and
- with respect to the audit committee, such director may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee
 - accept any consulting, advisory, or other compensatory fee from the listed company; or
 - be an affiliated person of the listed company or any subsidiary thereof.²¹

Any Nasdaq-listed company taking advantage of this exception must disclose in its proxy statement or Form 10-K

exchange for goods or services received, directly or indirectly, by the director personally or any entity in which the director has a beneficial ownership interest of greater than 50%.

See Treas. Reg. §1.162-27(e)(3).

¹⁹ As noted above, Nasdaq listing standards limit the one year cure period to 180 days if the listed company's next annual shareholders' meeting takes place not later than 180 days after the occurrence of the event that caused the audit committee member to no longer be independent.

²⁰ A "family member" is a person's spouse, parent, child or sibling, whether by blood, marriage or adoption, or anyone residing in such person's home. See Nasdaq Marketplace Rule 4200(a)(14).

²¹ A director serving on the listed company's audit committee under the "exceptional and limited circumstances" exception may not serve as audit committee chair.

- the nature of the relationship precluding an independence determination with respect to such director, and
- the reasons for the board's determination that such director's membership on the committee is in the best interests of the listed company.²²

SEC Rules Regarding Director Independence

In addition to the NYSE and Nasdaq disclosure requirements concerning director independence, the SEC adds another layer of public company disclosure.²³ The SEC rules do not impose additional independence criteria, rather, the rules seek to elicit additional disclosure regarding the independence of public company boards of directors. Under Item 407 of SEC Regulation S-K, a listed company must disclose in its proxy statement or Form 10-K

- the identity of each of its directors and nominees for director determined to be independent under applicable stock exchange listing criteria;²⁴ and
- the identity of any member of the company's audit, nominating or compensation committee who is determined to not be independent under applicable stock exchange listing criteria.²⁵

Item 407 also requires each company (whether or not it is a listed company) that has adopted a definition of independence to post the definition on its website or attach the definition as an exhibit to its proxy statement once every three years.²⁶ Finally, in connection with a board's independence determinations, Item 407 requires that a company disclose, by specific category or type, any transaction, relationship or arrangement with any of the company's independent directors that was (i) not disclosed under Item 404(a), but (ii) considered by the board in determining the independence of the director.²⁷ The disclosure requirements under Item 407 are effective for a company's (other than a registered investment company) annual report or proxy disclosure regarding its first fiscal year ending on or after December 15, 2006.

Independence Criteria Adopted by Institutional Investors and Proxy Advisory Firms

Well before the mushrooming of regulatory independence requirements, institutional investors and proxy advisory firms had pressed for strengthening of standards in this area. For some time, groups such as CII and firms such as ISS have published independence criteria that synthesized views

²² See Item 407(d)(2) of SEC Regulation S-K and Nasdaq Marketplace Rule 4350(d)(2).

²³ See Item 407 of SEC Regulation S-K.

²⁴ See Item 407(a)(1) of SEC Regulation S-K.

²⁵ Item 407 of SEC Regulation S-K also requires each company that is not a "listed issuer" to disclose the identity of its independent directors and non-independent committee members. These independence determinations are to be based upon the listing criteria of a stock exchange selected by the company.

²⁶ See Item 407(a)(2) of SEC Regulation S-K.

²⁷ See Item 407(a)(3) of SEC Regulation S-K.

of members and advice to clients.²⁸ Although these standards generally are beginning to coalesce after years of divergence, they are inconsistent with and stricter than regulatory requirements. This creates a troublesome counterpoint in any effort to achieve independence harmonization. Companies are not legally required to adhere to private sector independence criteria. Nonetheless, the policies of ISS and CII are followed by numerous institutional shareholders, and the failure of directors to meet such standards may result in a high number of “withhold” votes for such directors.²⁹

Similar to the NYSE and Nasdaq listing standards, ISS recommends that a majority of a public company board be independent, whereas CII recommends that at least *two-thirds* of the board consist of independent directors. Generally, ISS defines an independent director as a director with no material connection to the company other than the director’s board seat.³⁰ CII defines an independent director as a person whose only “nontrivial” professional, familial or financial connection to the company, its chairman, CEO, or any other executive officer is his or her board seat. Both ISS and CII recommend that public companies have separate audit, compensation and nominating committees composed entirely of independent directors. Neither ISS nor CII permits exceptions to its director independence and board composition standards. Both groups recommend that shareholders withhold votes from directors who do not meet their respective independence standards.

ISS and CII also may recommend withholding votes from directors who exhibit characteristics of being overburdened by board service. ISS will recommend withholding votes from a director who

- sits on more than six public company boards (or with respect to CEOs, more than two public company boards other than the CEO’s own board), or
- attended in the company’s prior year less than 75% of the meetings of the board and board committees on which the director sat without a valid excuse.³¹

CII recommends that

- companies establish and publish guidelines specifying the number of boards on which their directors may serve;
- directors with full-time jobs should not serve on more than two boards in addition to that of the company adopting the policy (absent unusual and specified circumstances);
- CEOs be limited to serving on only one other public company board, and even then, only if the performance of the CEO’s company is in the top half of its peer group; and

²⁸ See *ISS US Corporate Governance Policy 2007 Updates*, Institutional Shareholder Services (2006); *ISS 2007 U.S. Proxy Voting Guidelines Summary*, Institutional Shareholder Services (2006); and *The Council of Institutional Investors Corporate Governance Policies*, Council of Institutional Investors (updated March 20, 2007).

²⁹ *Appendix A* to this advisory lists the specific objective independence criteria adopted by ISS and CII. The subjective criteria by which ISS and CII determine director independence are discussed in this section.

³⁰ ISS defines “material” as a standard of relationship (personal, financial or otherwise) that a reasonable person might conclude could potentially influence a director’s objectivity in the boardroom in a manner that would have a meaningful impact on the director’s ability to satisfy his or her fiduciary duties.

³¹ Under SEC rules, companies must disclose the names of directors who fail to attend at least 75% of the meetings of the board and board committees on which they are members in the prior year. See Item 407(b)(1) of SEC Regulation S-K.

- directors who attend less than 75% of the meetings of the boards and board committees on which they sit for two consecutive years should not be renominated.

RELATED PERSON DISCLOSURE

Apart from the director independence standards summarized above, there are requirements to disclose related person transactions and interests under SEC rules and the NYSE and Nasdaq listing standards.³² Under SEC rules, public companies must disclose the existence of those transactions at least annually in their proxy statements or Forms 10-K.³³

The SEC's related person disclosure rules are in Items 401, 402, 403, 404 and 407 of SEC Regulation S-K, Form 8-K and Schedule 14A. These rules require a public company to disclose

- material transactions and relationships with its directors, nominees for director or executive officers (or immediate family members³⁴ of any of the foregoing) (including indebtedness and compensation arrangements), or entities in which its directors, nominees or executive officers (or any immediate family member of any of the foregoing) hold beneficial ownership interests which, in certain instances, exceed applicable thresholds;
- beneficial ownership interests of their directors, nominees for director, executive officers and greater than 5% beneficial holders of the company's securities; and
- the interests of related persons in certain matters submitted to a vote of the company's shareholders.

The NYSE and Nasdaq do not specifically require disclosure of related person transactions; however, the entry of NYSE- and Nasdaq-listed companies into such transactions may trigger other NYSE and Nasdaq disclosure obligations.³⁵ For example, both the NYSE and Nasdaq listing standards require disclosure of waivers of the listed company's code of conduct for directors and executive officers and material noncompliance with their respective corporate governance listing standards, each of which could be triggered by a listed company's entry into a related person transaction.³⁶ In addition,

³² See *Appendix B*, which lists sources of disclosure obligations under SEC rules (including disclosure obligations under the SEC's related person disclosure rules) and applicable listing standards for related person transactions.

³³ The term "transaction" is defined under Instruction 2 to Item 404(a) of SEC Regulation S-K to include any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness), or any series of similar arrangements or relationships.

³⁴ The SEC defines "immediate family member" to include mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and stepchildren and stepparents of the primary reporting person (or her spouse).

³⁵ In conjunction with the NYSE's proposed amendments to its corporate governance listing standards, the NYSE has proposed eliminating its guidance regarding related party transactions set forth in Sections 307.00 and 314.00 of the NYSE Listed Company Manual. See NYSE Amendments.

³⁶ By way of example, the entry by a listed company into a transaction with an entity in which a director has a beneficial interest sufficient to preclude an independence determination with respect to the director must be disclosed if, because of the transaction, the listed company's board consists of less than a majority of independent directors (a violation of the NYSE and Nasdaq board composition requirements). Under Nasdaq listing standards, such disclosure would need to be made in an SEC filing under cover of Form 8-K. The NYSE listing standards do not mandate disclosure in a Form 8-K filing, but do require that the noncompliance and reason therefore be disclosed to the NYSE. In practice, however, disclosure generally is made by a Form 8-K filing.

while not always rising to the level of a related person transaction, the NYSE listing standards require disclosure of “immaterial” relationships between NYSE-listed companies and their directors that do not preclude independence determinations with respect to the “interested” directors.³⁷

In addition to disclosure obligations with respect to individual transactions and relationships, under Item 404(b) of SEC Regulation S-K, public companies also are required to disclose their policies and procedures for approval of related person transactions.³⁸ Specifically, Item 404(b) requires companies to disclose the material features of their policies and procedures for the review, approval or ratification of transactions with related persons that are reportable under Item 404(a).³⁹ The SEC provides in Item 404(b) the following non-exclusive list of features that, depending on a company’s circumstances, may be material to such policies and procedures:

- the types of transactions covered by such policies and procedures;
- the respective standards to be applied to related person transactions under such policies and procedures;
- the persons or groups, on the board of directors or otherwise, responsible for applying the policies and procedures; and
- a statement of whether the policies and procedures are in writing, and if not, how they are evidenced.⁴⁰

Item 404(b) also requires public companies to identify any transactions required to be reported under Item 404(a) that were not required to be reviewed, approved or ratified under the companies’ policies and procedures, or for which such policies and procedures were not followed.

POINTS FOR BOARD CONSIDERATION

To avoid non-compliance with applicable independence and disclosure requirements, a public company must make assessments of both director independence and the scope of the company’s required related person disclosure more frequently than the annual review undertaken in connection with the preparation of the company’s proxy statement and annual report. Although more frequent assessments necessarily will increase a board’s already significant obligations, the implementation of appropriate board policies and procedures should mitigate much of the additional work associated with additional assessments. The aim of such policies should be twofold. First, they should elicit prompt disclosure of directors’ and director nominees’ relationships and transactions that may affect independence determinations and/or trigger disclosure obligations. Second, board policies should

³⁷ As noted above, the NYSE has proposed eliminating this disclosure obligation as redundant with the disclosure obligations imposed on public companies under Item 407 of SEC Regulation S-K.

³⁸ The NYSE and Nasdaq do not require that listed companies disclose their policies and procedures for the review, approval or ratification of related person transactions, but do require listed companies to review and oversee such transactions. See NYSE Listed Company Manual §307.00 and Nasdaq Marketplace Rules 4350(h) and 4360(i). As noted above, the NYSE has proposed eliminating this requirement as a result of the SEC’s revisions to the related person disclosure regime set forth in Item 404 of SEC Regulation S-K.

³⁹ Disclosure need not be provided under Item 404(b), however, with respect to any transaction that occurred prior to a person becoming a related person if the transaction did not continue after the person became a related person. See Instruction to Item 404(b) of SEC Regulation S-K.

⁴⁰ Item 404(b)(1) of SEC Regulation S-K.

enable evaluation, at the time such transactions are approved or relationships are set in motion, of the effects of such transactions and relationships on (i) the independence of the directors or director nominees involved and (ii) the company's disclosure obligations with respect to related person transactions.⁴¹

Without cooperation from individual directors, however, board policies and procedures only have a limited effect. Directors and nominees must assume responsibility for determining whether changes in their circumstances and relationships affect their independence and for alerting their boards of such changes. Such vigilance will go a long way towards assuring that public companies can avoid (i) discovering at year-end that a director previously deemed independent is not; (ii) running afoul of applicable independence and disclosure requirements; and (iii) needing to rely on cure provisions available under the NYSE or Nasdaq listing standards to regain compliance with applicable listing criteria, and disclosing such actions to shareholders and the capital markets.

As points for consideration, directors should:

- Stay abreast, or ask to be advised regularly, of changes in applicable stock exchange listing standards, SEC regulations and other regulatory pronouncements regarding director independence and treatment of interested and related person transactions.
 - Management can facilitate such continuing director education by providing directors with regular regulatory updates.
 - Consider arranging regular presentations by the company's independent auditor and outside counsel regarding changes in regulatory requirements and "best practices." These presentations could be held in connection with other director education programs (e.g., at an annual board retreat).
- Consider implementing policies and procedures to track on a "real time" basis potential related person transactions and other relationships that may undercut independence (which can be as simple as notifying the company's general counsel or corporate secretary). These policies and procedures could include, for example,
 - maintaining a current database of entities (including non-profits) with which directors have relationships that can be cross-checked against the company's supplier, customer and other service provider lists; and
 - periodically reviewing public filings, both with the SEC and with applicable state agencies, of companies with which directors have relationships, in order to determine whether disclosure regarding the directors' relationships is consistent and thorough.
- Take responsibility, particularly if serving on multiple boards, for keeping fellow board members apprised of changes in relationships and circumstances that may call into question a prior independence determination or disclosure obligations (e.g., employment in a relevant industry, financial interests in competitors or affiliates of the company, or personal relationships with the company's executive officers). To carry out this responsibility

⁴¹ Precepts for such policies and procedures typically are rooted in the codes of conduct required under the NYSE and Nasdaq listing standards.

- know who are the company's significant suppliers, customers, service providers and competitors; and
- stay abreast of significant industry-specific events that may impact your relationships (e.g., mergers, changes in executive officers and significant business transactions).

CONCLUSION

There are high expectations today for the independence of public company directors. These expectations are played out in detailed regulatory standards and exacting disclosure obligations – requirements that are tightly connected and require constant monitoring. Public companies and their directors can no longer afford to treat this subject as a once-per-year housekeeping matter. Instead, they must stay abreast of changes in personal circumstances and remain perceptive of those situations that may undercut independence or trigger disclosure obligations. This should result in both enhanced process and posture as well as, hopefully, ever-improving governance.

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This information is not legal advice. Readers should seek specific legal advice before acting on subjects mentioned herein.

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DIRECTOR INDEPENDENCE STANDARDS

A. NYSE and Nasdaq Objective Director Independence Standards

The following table sets forth the objective standards by which director independence is determined under listing standards of the New York Stock Exchange (“NYSE”) and the Nasdaq Stock Market (“Nasdaq”).

| DISQUALIFYING FACTOR | NYSE ¹ | NASDAQ ² |
|--|---|---|
| Officer/ Employee | <p><i>Not independent if</i></p> <ul style="list-style-type: none"> ▪ director is, or within the last three years has been, employed by the listed company³ (other than former service as interim Chairman, CEO or other executive officer⁴); or ▪ an immediate family member⁵ is, or within the last three years has been, an executive officer of the listed company. | <p><i>Not independent if</i></p> <ul style="list-style-type: none"> ▪ director is, or at any time in last three years has been, employed by the company⁶ (other than former service as an interim executive officer for a term of less than one year) or family member⁷ of director is, or at any time during the past three years has been, employed as an executive officer⁴ of the company. |
| Shareholder/ Affiliate | By itself, ownership of a significant amount of stock <i>does not bar independence.</i> | By itself, ownership of a significant amount of stock <i>does not bar independence.</i> |
| Compensation Committee Interlocks | <i>Not independent if</i> director or immediate family member is, or in the last three years has been, employed as an executive officer of another company where any of the listed company's present executive officers at the same time serves or served on that company's compensation committee. | <i>Not independent if</i> director or family member is employed as an executive officer of another entity where, at any time during the past three years, any of the listed company's executive officers serve on the compensation committee of such other entity. |
| Disqualifying Transactions and Business Relationships | <p><i>Not independent if</i></p> <ul style="list-style-type: none"> ▪ director or immediate family member has received more than \$100,000⁸ in direct compensation from the listed company during any 12-month period in the last three years, <i>other than</i> <ul style="list-style-type: none"> ➤ director and committee fees and pension or other forms of deferred compensation for prior service (provided that such compensation is not contingent on continued | <p><i>Not independent if</i></p> <ul style="list-style-type: none"> ▪ director or family member accepted any compensation¹² from the company in excess of \$100,000 during any 12-month period in the last three years, <i>other than</i> <ul style="list-style-type: none"> ➤ compensation for board or committee service; ➤ compensation received by the director for former service as an executive officer of the company for a term of less than one year; ➤ non-compensatory payments arising solely from |

| DISQUALIFYING FACTOR | NYSE ¹ | NASDAQ ² |
|----------------------|--|---|
| | <p>service);</p> <ul style="list-style-type: none"> ➤ compensation received by a director for former service as an interim Chairman, CEO or other executive officer; ➤ compensation received by an immediate family member of the director for service as an employee (other than an executive officer) of the listed company; ➤ bona fide expense reimbursements;⁹ or ➤ dividend or interest income;¹⁰ or <ul style="list-style-type: none"> ▪ director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the listed company for property or services which, in any of the last three fiscal years, exceed the greater of \$1 million or 2% of <i>such other company's</i> consolidated gross revenues.¹¹ | <p>investments in the company's securities;¹³</p> <ul style="list-style-type: none"> ➤ compensation paid to a family member who is a non-executive employee of the company; ➤ benefits under a tax-qualified retirement plan, or non-discretionary compensation; ➤ non-preferential payments made in the ordinary course of providing business services (e.g., payments of interest or proceeds related to banking services or loans by an issuer that is a financial institution or payment of insurance claims by an insurer that is an insurance company), which are on terms generally available to the public; or ➤ non-compensatory loans permitted under Section 13(k) of the Exchange Act;¹³ or <ul style="list-style-type: none"> ▪ director or family member is a general partner in, or controlling shareholder or executive officer of, any organization (including charitable organizations) to which the company made, or from which the company received, payments for property or services in the current or any of the past three fiscal years that exceed the greater of (i) 5% of consolidated gross revenues of the <i>recipient</i> for that year or (ii) \$200,000, <i>excluding</i>¹⁴ <ul style="list-style-type: none"> ➤ payments arising solely from investments in the company's securities, and ➤ payments under non-discretionary charitable contribution matching programs. |

| DISQUALIFYING FACTOR | NYSE ¹ | NASDAQ ² |
|---------------------------|--|--|
| Relationship with Auditor | <p><i>Not independent if</i></p> <ul style="list-style-type: none"> ▪ director or an immediate family member is a current partner of a firm that is the listed company's internal or external auditor; ▪ director is a current employee of a firm that serves as the company's internal or external auditor; ▪ director has an immediate family member who is a current employee of a firm that is the listed company's internal or external auditor and who participates in the firm's audit, assurance or tax compliance (but not tax planning) practice; or ▪ director or an immediate family member was within the last three years (but is no longer) a partner or employee of a firm that is the listed company's internal or external auditor and personally worked on the listed company's audit within that time. | <p><i>Not independent if</i> director or family member is a current partner of the company's outside auditor, or was a partner or employee of the company's outside auditor who worked on the company's audit at any time during the past three years.</p> |

¹ NYSE Listed Company Manual, §303A and NYSE Listed Company Manual Section 303A Corporate Governance Listing Standards Frequently Asked Questions (updated as of February 13, 2004) ("NYSE FAQ"). The NYSE submitted proposed amendments to Section 303A of the NYSE Listed Company Manual to the SEC on June 20, 2007. See Amendment No. 2 to SEC File No. 2005-81, available at [http://apps.nyse.com/commdata/pub19b4.nsf/docs/0345D4493935539A85257300007745F7/\\$FILE/NYSE-2005-81%20A-2.pdf](http://apps.nyse.com/commdata/pub19b4.nsf/docs/0345D4493935539A85257300007745F7/$FILE/NYSE-2005-81%20A-2.pdf) (the "NYSE Amendments"). We have noted in this table instances in which adoption of the amendments proposed in the NYSE Amendments would modify the NYSE's existing bright line independence criteria. Except as required under Exchange Act Rule 10A-3, Section 303A generally does not apply to companies listing only preferred stock or debt securities on the NYSE.

The NYSE listing standards require that a majority of the members of the boards of NYSE-listed companies be independent and that boards make both subjective and objective inquiries in connection with director independence determinations. Under the NYSE listing standards, a director is independent only if the listed company's board affirmatively determines that the director has no material relationship with the listed company directly or as a partner, shareholder or officer of an organization that has a relationship with the listed company. In making this determination, boards must consider all relevant facts and circumstances, including from the point of view of both the director and the persons or organizations with which the director has relationships. The objective criteria required to be applied by boards of NYSE-listed companies in connection with director independence determinations are set forth in this Table A.

² Nasdaq Marketplace Rule 4200(a) and IM-4200, and Nasdaq Marketplace Rule 4350 and IM-4350-4.

Nasdaq listing standards require that a majority of the members of the boards of Nasdaq-listed companies be independent and that boards make both subjective and objective inquiries in connection with director independence determinations. Under Nasdaq listing standards, a director is considered independent only if the director is not an officer or employee of the listed company and the listed company's board affirmatively determines that the director does not have any relationship which would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The objective criteria required to be applied by boards of Nasdaq-listed companies in connection with director independence determinations are set forth in this Table A.

³ For purposes of the NYSE listing standards, "company" includes any parent or subsidiary in the listed company's consolidated group for financial reporting purposes. If the NYSE-listed company ceases to be part of a consolidated group, the three-year "look back" period is measured from the date of deconsolidation. See NYSE FAQ C.3.A. Relationships that would impact independence do not come into existence until the company that employs the director joins the listed company's consolidated group. See NYSE FAQ C.3.B.

⁴ For purposes of the NYSE and Nasdaq listing standards, "executive officer" and "officer" have the meaning specified in Exchange Act Rule 16a-1(f), regardless of whether the company in question is a public company.

⁵ References to an "immediate family member" under the NYSE listing standards refer to such person's spouse, parent, child, sibling, mother or father-in-law, son or daughter-in-law, brother or sister-in-law, and anyone (other than domestic employees) who shares such person's home. Such references do not include individuals who are no longer immediate family members as a result of legal separation or divorce, or those who have died or become incapacitated.

⁶ For purposes of Nasdaq listing standards, "company" includes any parent or subsidiary in the listed company's consolidated group for financial reporting purposes (excluding entities reflected by the issuer only as an investment in the consolidated financial statements).

⁷ Under Nasdaq listing standards, a "family member" is a person's spouse, parent, child or sibling, whether by blood, marriage or adoption, or anyone residing in such person's home. See Nasdaq Marketplace Rule 4200(a)(14).

⁸ If adopted as proposed in the NYSE Amendments, the monetary threshold applicable to the NYSE's bright line independence determinations will increase from \$100,000 to \$120,000 (which is consistent with the SEC's monetary threshold for related person transactions under Item 404 of SEC Regulation S-K).

⁹ See *NYSE Listed Company Manual Section 303A Corporate Governance Listing Standards Frequently Asked Questions* ("NYSE FAQs"), Section C: Questions Regarding Independence Determination, Question 9 (updated as of February 13, 2004), available at <http://www.nyse.com/pdfs/section303Afaqs.pdf>.

¹⁰ *Id.* at Question 8.

¹¹ The look-back provision for this test applies solely to the financial relationship between the listed company and the director's or immediate family member's current employer; it does not apply to former employment of the director or immediate family member. Contributions to tax-exempt organizations are not considered "payments" for this test. However, listed companies must disclose in their proxy statements or Forms 10-K any contributions they made to any tax-exempt organization for which an independent director serves as an executive officer if, in the preceding three years, contributions in any single fiscal year exceeded the greater of

- \$1 million or
- 2% of such tax-exempt entity's consolidated gross revenues.

¹² The interpretive material to Nasdaq Marketplace Rule 4200(a)(15) provides a non-exclusive list of examples of direct and indirect compensation that would preclude a director's independence under the rule. These examples include

- consulting or personal service contracts with a director or a family member of the director; and
- political contributions to the campaign of a director or a family member of the director.

¹³ See Nasdaq Marketplace Rule 4200(a)(15) and IM-4200.

¹⁴ Nasdaq commentary indicates that the 5% or \$200,000 measurement is intended to capture payments to entities with which a director or family member is affiliated. Under exceptional circumstances, such as where a director has direct, significant business holdings, Nasdaq commentary provides that it may be appropriate to apply the 5% or \$200,000 measurement, rather than the \$100,000 individual measurement. Nasdaq-listed companies should contact Nasdaq if they wish to apply the independence standards in that manner. Partners in law firms that are not sole proprietorships (which are subject to the \$100,000 individual measurement) are subject to the 5% or \$200,000 measurement, based on the amount of payments made to the law firm by the listed company.

B. ISS and CII Objective Director Independence Standards

The following table sets forth the objective standards adopted by Institutional Shareholder Services (“ISS”) and the Council of Institutional Investors (“CII”) for determining director independence.

| DISQUALIFYING FACTOR | ISS ¹ | CII ² |
|------------------------------|---|--|
| Officer/ Employee | <p><i>Not independent</i> if director is</p> <ul style="list-style-type: none"> ▪ an employee of the company or one of its affiliates;³ ▪ a non-employee officer of the company if among the five most highly paid individuals (excluding interim CEOs); ▪ listed as a Section 16 officer in proxy statement or Form 10-K; ▪ the current interim CEO or a former interim CEO if the service was for longer than 18 months (if the service was for 12 to 18 months, ISS will make an assessment of the interim CEO's employment agreement);⁴ ▪ a former CEO of the company or of any acquired company within the past five years; ▪ a former executive⁵ of the company, an affiliate or an acquired firm within the past five years; ▪ an executive of a former parent or predecessor firm at the time the company was sold or split off from the parent/predecessor within the past five years; ▪ an executive, former executive, general or limited partner of a joint venture or partnership with the company; ▪ a relative⁶ of <ul style="list-style-type: none"> ➤ a current Section 16 officer of the company or its affiliates; or ➤ a current employee of the company or its affiliates where additional factors raise concern (e.g., a director related to numerous | <p><i>Not independent</i> if</p> <ul style="list-style-type: none"> ▪ director is, or at any time in last five years has been, employed by the company or employed by or a director of an affiliate;⁸ or ▪ a relative⁹ of director is, or at any time during the past five years has been, employed by the company or employed by or a director of an affiliate. |

| DISQUALIFYING FACTOR | ISS ¹ | CII ² |
|--|---|--|
| | <p>employees; a company or an affiliate employs relatives of numerous board members; or the director is a non-Section 16 officer in a key strategic role)</p> <ul style="list-style-type: none"> ➤ a former Section 16 officer of company or its affiliates within the last five years; or ▪ the founder of the company but not currently an employee.⁷ | |
| Shareholder/Affiliate | <p><i>Not independent</i> if director is the beneficial owner of more than 50% of the company's voting power (which may be aggregated if voting power is distributed among more than one member of a defined group).</p> | <p>No provision</p> |
| Board Interlocks | <p><i>Not independent</i> if director or relative has an interlocking relationship¹⁰ involving members of the board of directors or its Compensation and Stock Option Committee.</p> | <p><i>Not independent</i> if director or relative is, or in the past five years has been, part of an interlocking directorate in which the CEO or other employee of the company serves on the board of a third-party entity employing the director or such relative (regardless of whether the entity is for or non-profit).</p> |
| Disqualifying Transactions and Business Relationships | <p><i>Not independent</i> if</p> <ul style="list-style-type: none"> ▪ director or relative currently provides professional services in excess of \$10,000 per year directly to <ul style="list-style-type: none"> ➤ the company, ➤ an affiliate of the company, or ➤ an individual officer of the company or any of its affiliates; ▪ director or relative is employed by a customer or supplier of the company that makes payments to, or receives payments from, the company in excess of the greater of <ul style="list-style-type: none"> ➤ \$200,000 or ➤ 5% of the recipient's gross revenues; ▪ director or relative has any | <p><i>Not independent</i> if</p> <ul style="list-style-type: none"> ▪ director or relative is, or in the past five years has been, an employee, director or greater than 20% owner of a firm <ul style="list-style-type: none"> ➤ that is one of the company's or its affiliates' paid advisors or consultants,¹² or ➤ that receives revenues of at least \$50,000 for being a paid advisor or consultant to an executive officer¹³ of the company; ▪ director or relative is, or in the past five years has been, employed by or has had a 5% or greater ownership¹⁴ interest in a third party that provides payments to, or receives payments from, the company and either <ul style="list-style-type: none"> ➤ such payments account for 1% |

| DISQUALIFYING FACTOR | ISS ¹ | CII ² |
|----------------------|---|---|
| | <p>transactional relationship with the company or its affiliates (<i>excluding</i> investments in the company through a private placement) through which the company makes or receives payments in excess of the greater of</p> <ul style="list-style-type: none"> ➤ \$200,000 or ➤ 5% of the recipient's gross revenues; <ul style="list-style-type: none"> ▪ director has any material¹¹ financial tie or other related person transactional relationship to the company; ▪ director is party to a voting agreement under which director must vote in line with management on proposals being brought to shareholder vote; or ▪ director or relative is a trustee, director or employee of a charitable or non-profit organization that receives grants or endowments from the company or its affiliates. | <p>of either party's consolidated gross revenues in any single fiscal year, or</p> <ul style="list-style-type: none"> ➤ if the third party is a debtor or creditor of the company and the amount owed exceeds 1% of either party's assets; <ul style="list-style-type: none"> ▪ director has, or in the last five years has had, a personal contract with the company, an executive officer or any affiliate of the company (regardless of amount payable thereunder); ▪ relative has paid or received more than \$50,000 in the past five years under a personal contract with the company, an executive officer or any affiliate of the company; ▪ director or relative is, or in the past five years has been, <ul style="list-style-type: none"> ➤ an employee or director of a foundation, university or other non-profit organization that receives significant grants or endowments¹⁵ from the company, an affiliate of the company, or any executive officer of the company, or ➤ a direct beneficiary of any donations to such organization; or ➤ an employee, director or a 5% or greater owner of a third-party entity that is a significant competitor of the company; or ▪ director is a party to a voting trust, agreement or proxy giving his or her decision-making power as a director to management, <i>except</i> to the extent that there is a fully disclosed and narrow voting arrangement (such as those which are customary between venture capitalists and management regarding the venture capitalists' board seats). |

| DISQUALIFYING FACTOR | ISS ¹ | CII ² |
|---------------------------|---|---|
| Relationship with Auditor | See "Disqualifying Transactions and Business Relationships" | See "Disqualifying Transactions and Business Relationships" |

¹ *ISS 2007 U.S. Proxy Voting Guidelines Summary*, Institutional Shareholder Services (2006). ISS recommends that a majority of the directors on a public company's board be independent and that all members of the company's nominating, compensation and audit committees be independent.

² *The Council of Institutional Investors Corporate Governance Policies*, Council of Institutional Investors (updated March 20, 2007). CII recommends that at least two-thirds of the directors on a public company's board be independent and that all members of the company's nominating, compensation and audit committees be independent.

³ ISS defines "affiliate" to include a subsidiary or a sibling or parent company. ISS uses 50% control ownership by the parent company as the standard for applying its affiliate designation.

⁴ ISS will review the terms of the interim CEO's employment contract to determine if it contains severance pay, long-term health and pension benefits or other such standard provisions typically contained in contracts of permanent, non-temporary CEOs. ISS also will consider if a formal search process was underway for a full-time CEO at the time.

⁵ "Executives" (officers subject to Section 16 of the Exchange Act) include the chief executive, operating, financial, legal, technology, and accounting officers of a company (including the president, treasurer, secretary, controller, or any vice president in charge of a principal business unit, division or policy function).

⁶ ISS's use of the term "relative" follows the SEC definition of "immediate family members."

⁷ ISS will consider the operating involvement of the founder with the company. Little to no operating involvement may cause ISS to deem the founder an independent outsider.

⁸ CII considers an "affiliate" relationship to be established if one entity (either alone or pursuant to an arrangement with one or more other persons), owns or has the power to vote more than 20% of the equity interest in another, *unless* some other person (either alone or pursuant to an arrangement with one or more other persons) owns or has the power to vote a greater percentage of the equity interest. Joint venture partners and general partners meet CII's definition of an affiliate, and officers and employees of joint venture enterprises and general partners are considered affiliated. A subsidiary is an affiliate if it is at least 20% owned by the company.

Affiliates also include predecessor companies. CII defines a "predecessor" as an entity that within the last five years was party to a "merger of equals" with the company or represented more than 50% of the company's sales or assets when such predecessor became part of the company.

⁹ "Relatives" include spouses, parents, children, step-children, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, aunts, uncles, nieces, nephews and first cousins, and anyone sharing the director's home.

¹⁰ "Interlocks" include (a) executive officers serving as directors on each other's compensation or similar committees (or, in the absence of such a committee, on the board) or (b) executive officers sitting on each other's boards and at least one serving on the other's compensation or similar committees (or, in the absence of such a committee, on the board).

¹¹ For purposes of ISS's director independence classification, "material" is defined as a standard of relationship (financial, personal or otherwise) that a reasonable person might conclude could potentially influence a director's objectivity in the boardroom in a manner that would have a meaningful impact on the director's ability to satisfy his or her fiduciary duties on behalf of shareholders.

¹² Advisors or consultants include, but are not limited to, law firms, auditors, accountants, insurance companies and commercial and investment banks. Individuals serving "of counsel" to a firm are considered employees of that firm.

¹³ CII defines “executive officer” to include the chief executive, operating, financial, legal and accounting officers of a company. This includes the president, treasurer, secretary, controller and any vice-president who is in charge of a principal business unit, division or function (such as sales, administration or finance) or performs a major policymaking function for the company.

¹⁴ “Ownership” refers to beneficial or record ownership, not custodial ownership.

¹⁵ A “significant grant or endowment” is a grant or endowment that exceeds the lesser of \$100,000 or 1% of the total annual donations received by the organization.

C. Special Independence Standards Applicable to Audit Committees

NYSE- and Nasdaq-listed companies are required to have audit committees consisting of at least three members, all of whom must be independent, subject, with respect to Nasdaq-listed companies, to an exception for one audit committee member under “exceptional and limited circumstances.”¹ The following table lists the independence standards applicable to audit committee members of NYSE- and Nasdaq-listed companies.

| NYSE ² | NASDAQ ³ |
|--|--|
| Committee members must <ul style="list-style-type: none"> ▪ be independent under §303A.02 of the NYSE Listed Company Manual;⁴ <i>and</i> ▪ satisfy the requirements of Exchange Act Rule 10A-3(b)(1).⁵ | Committee members must <ul style="list-style-type: none"> ▪ be independent under Nasdaq Marketplace Rule 4200(a)(15);⁶ ▪ not have participated in the preparation of the financial statements of the listed company or any current subsidiary of the listed company during the past three years; <i>and</i> ▪ satisfy the requirements of Exchange Act Rule 10A-3(b)(1).⁵ |

¹ Nasdaq permits one director who is not independent (as defined in Nasdaq Marketplace Rule 4200(a)(15)) and is not an officer or employee, or a family member of an officer or employee, of the listed company to serve on the audit committee for a maximum of two years if

- the board, under exceptional and limited circumstances, determines that such person's membership on the committee would be in the best interests of the listed company; and
- such director may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee
 - accept any consulting, advisory, or other compensatory fee from the listed company; or
 - be an affiliated person of the listed company or any subsidiary thereof.

Any listed company taking advantage of the exception must disclose in its proxy statement or Form 10-K (i) the nature of the relationship precluding an independence determination with respect to such director and (ii) the reasons for the board's determination that such director's membership on the audit committee is in the best interests of the listed company. See Nasdaq Marketplace Rule 4350(d)(2).

As required by Exchange Act Rule 10A-3, both the NYSE and Nasdaq listing standards provide listed companies the opportunity to cure unintentional non-compliance with audit committee composition requirements. If an audit committee member ceases to be independent for reasons outside of the member's reasonable control, the audit committee member is permitted to remain on the audit committee until the earlier of the listed company's next annual shareholders meeting or one year from the occurrence of the event that caused the member to no longer be independent. Nasdaq also provides a similar cure period to listed companies that fail to meet Nasdaq's audit committee composition requirements because of a vacancy on the committee. Provided that the listed company is not relying on the Rule 10A-3 cure period for another audit committee member, the listed company has until the earlier of its next annual shareholders' meeting or one year from the occurrence of the event that led to the noncompliance to fill the vacancy. However, if the company's annual meeting occurs no later than 180 days following the event that caused the vacancy, the company has only 180 days from the date of such event to regain compliance. See Nasdaq Marketplace Rule 4350(c)(1).

² See NYSE Listed Company Manual §§303.02, .06 and .07.

³ See Nasdaq Marketplace Rule 4200(a)(15) and IM-4200, and Nasdaq Marketplace Rule 4350(d) and IM 4350-4. Listings of securities (other than equity securities) of a consolidated or at least 50% beneficially owned subsidiary of a parent company that itself is listed on a national securities exchange or a national securities association subject to the requirements of Exchange Act Rule 10A-3 are not subject to Nasdaq's audit committee requirements. See Nasdaq Marketplace Rule 4350(d)(5).

⁴ The NYSE listing standards require boards of NYSE-listed companies to make both subjective and objective inquiries in connection with director independence determinations. Under the NYSE listing standards, a director is independent only if the listed company's board affirmatively determines that the director has no material relationship with the listed company directly or as a partner, shareholder or officer of an organization that has a relationship with the listed company. In making this determination, boards must consider all relevant facts and circumstances, including from the point of view of both the director and the persons or organizations with which the director has relationships. The objective criteria required to be applied by boards of NYSE-listed companies in connection with director independence determinations are set forth in Table A of this *Appendix A*.

⁵ To be considered independent under Rule 10A-3(b)(1), a director who is an audit committee member may not, other than in his or her capacity as a member of the audit committee, the board of directors, or any other board committee

- accept directly or indirectly any consulting, advisory, or other compensatory fee from the issuer or any subsidiary thereof (excluding, unless applicable listing criteria provide otherwise, receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the issuer, provided that such compensation is not contingent in any way on continued service); or
- be an affiliated person of the issuer or any subsidiary thereof.

Under Rule 10A-3(e)(1), an "affiliated person" is one who directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the issuer or any subsidiary thereof, and, any of the following:

- an executive officer of an affiliate;
- a director who also is an employee of an affiliate;
- a general partner of an affiliate; or
- a managing member of an affiliate.

The SEC has a safe harbor to prevent certain beneficial owners of the issuer's equity securities from being deemed to control the issuer (or any subsidiary thereof). A person will not be deemed to control an issuer (or any subsidiary thereof) if such person is not

- a beneficial owner, directly or indirectly, of more than 10% of any class of voting equity securities of the issuer (or any subsidiary thereof); and
- an executive officer of the issuer (or any subsidiary thereof).

Under Rule 10A-3(e)(8), "indirect" acceptance by a member of an audit committee of any consulting, advisory or other compensatory fee includes acceptance of such a fee by

- the member's spouse, minor child or stepchild or a child or stepchild sharing a home with the member, or
- by an entity
 - in which such member is a partner, member, an officer such as a managing director occupying a comparable position or executive officer, or occupies a similar position (except limited partners, non-managing members and those occupying similar positions who, in each case, have no active role in providing services to the entity), and
 - which provides accounting, consulting, legal, investment banking or financial advisory services to the issuer or any subsidiary of the issuer.

Therefore, for example, a director who is a partner in a law firm would not be independent for audit committee purposes if the director's law firm provided any services to the company or any subsidiary of the company.

⁶ Nasdaq listing standards require boards of Nasdaq-listed companies to make both subjective and objective inquiries in connection with director independence determinations. Under Nasdaq listing standards, a director is considered independent only if the director is not an officer or employee of the listed company and the listed company's board affirmatively determines that the director does not have any relationship which would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The objective criteria required to be applied by boards of Nasdaq-listed companies in connection with director independence determinations are set forth in Table A of this *Appendix A*.

D. Special Independence Standards Applicable to Compensation Committees

Compensation committee members of NYSE- and Nasdaq-listed companies are required to be independent in accordance with the applicable listing standards described above.

Certain transactions in an issuer's securities (including stock compensation arrangements) between the issuer and its officers and directors are exempted from Section 16(b) of the Exchange Act if they are approved by the issuer's board of directors or a committee of two or more "non-employee directors," as defined under Exchange Act Rule 16b-3(b)(1). To perfect the exemption for stock compensation arrangements between issuers and their officers and directors, compensation committee members must therefore be "non-employee directors."

Additionally, compensation committee members must qualify as "outside directors" for purposes of Section 162(m) of the Internal Revenue Code to preserve for the issuer the deductibility of certain compensation paid to executive officers.

The following table summarizes the criteria that must be met in order for directors to be deemed "non-employee directors" and "outside directors" for purposes of Exchange Act Rule 16b-3(b)(1) and Internal Revenue Code Section 162(m), respectively.

| EXCHANGE ACT RULE 16b-3 ¹ | INTERNAL REVENUE CODE §162(m) ² |
|--|---|
| <p>A "non-employee director" is a director who</p> <ul style="list-style-type: none"> ▪ is not currently an officer or employee of the issuer or a parent or subsidiary of the issuer; ▪ does not receive compensation in excess of the amount that would be required to be disclosed under Item 404(a) of SEC Regulation S-K (currently \$120,000), either directly or indirectly, from the issuer or a parent or subsidiary of the issuer, for services rendered as a consultant or in any capacity other than as a director; and ▪ does not possess an interest in any other transaction for which disclosure would be required under Item 404(a) of SEC Regulation S-K. | <p>An "outside director" is a director who</p> <ul style="list-style-type: none"> ▪ is not a current employee of the company; ▪ is not a former employee of the company who receives compensation for prior services (other than benefits under a tax-qualified retirement plan) during the taxable year; ▪ has not been an officer of the company; and ▪ does not receive remuneration from the company, either directly or indirectly, in any capacity other than as a director. For this purpose, remuneration includes any payment (other than certain de minimis remuneration) in exchange for goods or services received, directly or indirectly, by the director personally or any entity in which the director has a beneficial ownership interest of greater than 50%. |

¹ See Exchange Act Rule 16b-3(b)(1).

² See Treas. Reg. §1.162-27(e)(3).

**DISCLOSURE OBLIGATIONS IMPLICATED BY DIRECTOR RELATIONSHIPS
AND/OR RELATED PERSON TRANSACTIONS**

Most of the disclosure obligations for a public company relating to relationships held by its directors and to “related person” transactions apply to the company’s Form 10-K and proxy statement for the company’s annual meeting of shareholders. The following table summarizes these disclosure requirements, grouped by the focus of the disclosure indicated in the index below.

| <u>Focus of Disclosure</u> | <u>Page</u> |
|---|--------------------|
| Director Transactions | B-2 |
| Transactions with related persons..... | B-2 |
| Director Compensation | B-2 |
| Director compensation..... | B-2 |
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| Other Information Regarding Directors | B-3 |
| Information regarding directors/nominees for director..... | B-3 |
| Securities ownership..... | B-4 |
| Contributions to tax exempt organizations for which an independent director serves as an executive officer..... | B-4 |
| Substantial interest of related persons in matters subject to shareholder vote..... | B-4 |
| Noncompliance with Corporate Governance Listing Standards | B-4 |
| Notice of stock market delisting or failure to satisfy a continued listing standard..... | B-4 |
| Waivers of the Company’s Code of Conduct | B-5 |
| Waiver of the public company’s code of business conduct or ethics for director..... | B-5 |

| DISCLOSURE OF DIRECTOR RELATIONSHIPS AND RELATED PERSON TRANSACTIONS | | |
|--|--|---|
| FOCUS OF DISCLOSURE | SUMMARY OF REQUIRED DISCLOSURE | SOURCE OF DISCLOSURE OBLIGATION |
| Director Transactions¹ | | |
| <i>Transactions with related persons²</i> | <p>Describe the following with respect to any transaction³ during the company's last fiscal year or any currently proposed transaction in which the amount involved⁴ exceeds \$120,000 and in which any related person has a material interest:</p> <ul style="list-style-type: none"> ▪ name of the related person and basis on which such person is a "related person"; ▪ related person's interest in the transaction (including his or her position or relationship with, or ownership of, a firm, corporation or other entity that has an interest in the transaction); ▪ approximate dollar value of the amount involved in the transaction; ▪ approximate dollar value of the related person's interest in the transaction, computed without regard to the amount of profit or loss; ▪ for transactions involving indebtedness,⁵ <ul style="list-style-type: none"> ➤ the largest aggregate amount of principal outstanding during the period for which disclosure is provided; ➤ the amount of principal outstanding as of the latest practicable date; ➤ the amount of principal paid during the period for which disclosure is provided; ➤ the amount of interest paid during the period for which disclosure is provided; and ➤ the rate or amount of interest payable on the indebtedness. | <p>Reg. S-K Item 404(a)</p> <ul style="list-style-type: none"> ▪ Schedule 14A, Item 7 ▪ Form 10-K, Item 13 |
| Director Compensation | | |
| <i>Director compensation</i> | <ul style="list-style-type: none"> ▪ Description of arrangements under which any director is compensated for services provided as a director, including amounts | <p>Reg. S-K Item 402(k)</p> <ul style="list-style-type: none"> ▪ Schedule 14A, |

| DISCLOSURE OF DIRECTOR RELATIONSHIPS AND RELATED PERSON TRANSACTIONS | | |
|--|---|--|
| FOCUS OF DISCLOSURE | SUMMARY OF REQUIRED DISCLOSURE | SOURCE OF DISCLOSURE OBLIGATION |
| | <p>payable for committee participation and special assignments.</p> <ul style="list-style-type: none"> ▪ Director Compensation Table, similar in form and content to the Summary Compensation Table, disclosing all compensation paid to directors in a company's prior fiscal year, and accompanying narrative disclosure of any material facts necessary to an understanding of the table (including, where appropriate, disclosure regarding option timing or dating practices).⁶ | <p>Item 8</p> <ul style="list-style-type: none"> ▪ Form 10-K, Item 11 |
| <i>Director compensation plans</i> | <ul style="list-style-type: none"> ▪ For plans subject to shareholder action, <ul style="list-style-type: none"> ➤ narrative description of the material features of the plan, including the identity of the eligible participants, and ➤ tabular disclosure of the benefits to be provided under the plan (if determinable) to the company's directors, and directors who are not executive officers (as a group). ▪ For plans not subject to shareholder action, tabular and narrative disclosure required under Item 201(d) of SEC Regulation S-K. | Schedule 14A, Item 10 |
| Other Information Regarding Directors | | |
| <i>Information regarding directors/nominees for director</i> | <ul style="list-style-type: none"> ▪ Description of any arrangement or understanding between directors or nominees for director and between such person and any other person (naming such other person) pursuant to which the director or nominee was selected as such. ▪ Description of the nature of any family relationship between directors, nominees for director and executive officers. ▪ Any other public company or registered investment company directorships held by each director or nominee for director. <p><i>Note:</i> Companies not subject to Exchange Act reporting requirements for the 12 months preceding the filing of the report must include the Item 401 disclosure covering the prior five-year</p> | <p>Reg. S-K Item 401(a), (d), (e) and (g)</p> <ul style="list-style-type: none"> ▪ Schedule 14A, Item 7(b) ▪ Form 10-K, Item 10 |

| DISCLOSURE OF DIRECTOR RELATIONSHIPS AND RELATED PERSON TRANSACTIONS | | |
|--|---|--|
| FOCUS OF DISCLOSURE | SUMMARY OF REQUIRED DISCLOSURE | SOURCE OF DISCLOSURE OBLIGATION |
| | period for control persons and promoters if such items are material to a voting or investment decision. | |
| <i>Securities ownership</i> | Information regarding beneficial ownership of the company's securities by directors and nominees for director. | Reg. S-K Item 403(a) and (b) <ul style="list-style-type: none"> ▪ Schedule 14A, Item 6(d) ▪ Form 10-K, Item 12 |
| <i>Contributions to tax exempt organizations for which an independent director serves as an executive officer</i> | Commentary to §303A.02(b) requires disclosure in the listed company's proxy statement or Form 10-K of contributions by the listed company to tax exempt organizations (for which an independent director serves as an executive officer), if in the preceding three years, contributions in any single year exceeded the greater of <ul style="list-style-type: none"> ▪ \$1 million or ▪ 2% of such tax exempt entity's consolidated gross revenues. | NYSE Listed Company Manual §303A.02(b) |
| <i>Substantial interest of related persons in matters subject to shareholder vote</i> | Description of any substantial interest, direct or indirect, by security holdings (but only if the holder receives some extra or special benefit not shared on a pro rata basis by all other holders of the same class) or otherwise, of each of the following persons in the matter to be acted upon: <ul style="list-style-type: none"> ▪ if the solicitation is made on behalf of the company, each director of the company at any time since the beginning of the last fiscal year; ▪ if the solicitation is other than on behalf of the company, each participant⁷ in the solicitation; ▪ each nominee for election as a director of the company; and ▪ each associate⁸ of any of the foregoing persons. | Schedule 14A, Item 5(a) |
| Noncompliance with Corporate Governance Listing Standards | | |
| <i>Notice of stock market delisting or failure to satisfy a continued listing standard (which includes failures to satisfy</i> | <ul style="list-style-type: none"> ▪ Listed company CEO must notify NYSE or Nasdaq, as applicable, of any material⁹ non-compliance with any applicable provisions of NYSE or Nasdaq corporate governance listing standards (i.e. NYSE | <ul style="list-style-type: none"> ▪ Form 8-K, Item 3.01 ▪ NYSE Listed Company Manual §303A.12(b) ▪ Nasdaq Marketplace Rule 4350(m) |

| DISCLOSURE OF DIRECTOR RELATIONSHIPS AND RELATED PERSON TRANSACTIONS | | |
|--|--|--|
| FOCUS OF DISCLOSURE | SUMMARY OF REQUIRED DISCLOSURE | SOURCE OF DISCLOSURE OBLIGATION |
| <i>independence requirements)</i> | <p>Listed Company Manual §303A or Nasdaq Marketplace Rule 4350).</p> <ul style="list-style-type: none"> ▪ With respect to notices sent by the company to the applicable stock market notifying the stock market that the company is aware of material noncompliance with a rule or standard for continued listing, <ul style="list-style-type: none"> ➤ the date the company provided the notice; ➤ the rule or standard for continued listing the company failed to satisfy; and ➤ any action the company has determined to take regarding its noncompliance. ▪ With respect to de-listing notices received by the company, <ul style="list-style-type: none"> ➤ the date the company received the notice; ➤ the rule or standard for continued listing the company failed to satisfy; and ➤ any action the company has determined to take in response to the notice. ▪ With respect to public reprimands received by the company, <ul style="list-style-type: none"> ➤ the date of the letter or communication, and ➤ summary of the contents thereof. | |
| Waivers of the Company's Code of Conduct | | |
| <i>Waiver of the public company's code of business conduct or ethics for directors (which includes failures to satisfy conflicts of interest considerations)</i> | <ul style="list-style-type: none"> ▪ Nasdaq: <ul style="list-style-type: none"> ➤ Domestic issuers must disclose waivers within four business days of the waiver under Form 8-K. ➤ Foreign private issuers must disclose waivers under either Form 6-K or the next Form 20-F or 40-F. ▪ NYSE: <ul style="list-style-type: none"> ➤ Wavers must be disclosed to the | <ul style="list-style-type: none"> ▪ Nasdaq Marketplace Rule 4350(n) ▪ NYSE Listed Company Manual §303A.10 |

| DISCLOSURE OF DIRECTOR RELATIONSHIPS AND RELATED PERSON TRANSACTIONS | | |
|--|--|---------------------------------|
| FOCUS OF DISCLOSURE | SUMMARY OF REQUIRED DISCLOSURE | SOURCE OF DISCLOSURE OBLIGATION |
| | company's shareholders, but no express requirement to disclose the waiver under cover of Form 8-K. ¹⁰ | |

¹ "Transaction" is defined broadly to encompass any financial transaction, arrangement or relationship (including any indebtedness or guarantee of indebtedness) or any series of similar transactions, arrangements or relationships. See Instruction 2 to Item 404(a) of SEC Regulation S-K.

² "Related person" means

- any person included within any of the following categories at any time during the period for which disclosure of a related person transaction is required under Item 404(a):
 - any director or executive officer of the company;
 - any nominee for director (when the disclosure called for under Item 404(a) is presented in connection with the election of such director nominee); and
 - any immediate family member of a director, executive officer or director nominee; and
- any person included within any of the following categories when a transaction in which such person has a direct or indirect material interest existed or occurred:
 - a greater than 5% shareholder in the company for which disclosure is required under Item 403(a) of SEC Regulation S-K; and
 - an immediate family member of such shareholder.

The SEC defines "immediate family member" of a person to mean any child, stepchild, parent, stepparent, spouse, sibling, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law or sister-in-law of such person and any other person (other than a tenant or employee) sharing the household of the specified person.

With respect to a 5% shareholder and an immediate family member, Item 404(a) requires disclosure of transactions in which such persons have a direct or indirect material interest that (a) occurred or continued (such as through the ongoing receipt of payments) after the date the person became a 5% shareholder; or (b) resulted in the person becoming a 5% shareholder. Item 404(a) does *not* require disclosure of transactions that conclude before the person becomes a 5% shareholder. See Question 2.01 of *Item 404 of Regulation S-K—Transactions with Related Persons, Promoters and Certain Control Persons*, Securities and Exchange Commission Division of Corporation Finance (Updated March 13, 2007), available at <http://www.sec.gov/divisions/corpfm/guidance/execcomp404interp.htm>.

³ Information related to compensation or any other transaction need not be disclosed under Item 404 to the extent (i) such compensation is reported under Item 402(k) of SEC Regulation S-K. See Instruction 5.b. to Item 404(a) of SEC Regulation S-K.

In addition, Item 404(a) does not require disclosure of transactions in which the related person's interest arises solely as a result of

- the related person's position as a director of another corporation or organization which is a party to the transaction;
- the direct or indirect ownership by the related person and all other related persons, in the aggregate, of less than a 10% equity interest in another person (other than a partnership) which is a party to the transaction;

- both such position and ownership;
- the related person's position as a limited partner in a partnership in which the related person and all other related persons have an interest of less than 10%; or
- holding an interest in a class of equity securities of the company, and all holders of such class of equity securities receive the same benefit on a pro rata basis; or

if the transaction

- is one where the rates or charges involved are determined by competitive bids, or involves the rendering of services as a common or contract carrier, or public utility, at rates or charges fixed in conformity with law or governmental authority; or
- involves services as a bank depository of funds, transfer agent, registrar, trustee under a trust indenture, or similar services.

⁴ The "amount involved" in a transaction is calculated by determining the dollar value of the amount involved in the transaction in question, which

- in the case of leases or transactions involving installment payments, the aggregate amount of all installments due on or after the beginning of the company's last fiscal year, including any required or optional payments due during or at the conclusion of the lease or other transaction; and
- in the case of transaction involving indebtedness, the largest aggregate amount of all indebtedness outstanding at any time since the beginning of the company's last fiscal year and all amounts of interest payable on such indebtedness during such last fiscal year. See Instruction 3 to Item 404(a) of SEC Regulation S-K.

⁵ Rule 404(a) does not require disclosure of transactions involving indebtedness for a greater than 5% shareholder in the company for whom disclosure is required under Item 403(a) of SEC Regulation S-K or an immediate family member of such shareholder. See Instruction 4.b. to Item 404(a) of SEC Regulation S-K.

Amounts due from a related person to the company for purchases of goods and services subject to usual trade terms, for ordinary business travel and expense payments and for other ordinary course transactions are not required to be disclosed under Item 404(a). See Instruction 4.a. to Item 404(a) of SEC Regulation S-K.

If the company is a bank, savings and loan association, or broker-dealer extending credit under Federal Reserve Regulation T and the loans are not disclosed as nonaccrual, past due, restructured or potential problems (as defined in Item III.C.1. and 2. of Industry Guide 3, Statistical Disclosure by Bank Holding Companies), Item 404(a) disclosure may consist of a statement, if true, that the loans:

- were made in the ordinary course of business;
- were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans with persons not related to the company; and
- when made, did not involve more than the normal risk of collectibility or present other unfavorable features.

⁶ See *New Executive Compensation Disclosure Rules*, Covington & Burling LLP (August 23, 2006), available at <http://www.cov.com/files/Publication/68c16819-5dad-4c96-8386-5eca1e5f7354/Presentation/PublicationAttachment/8394ee9a-665f-4fb2-9b90-68e611a7b53d/671.pdf>, for additional information regarding SEC disclosure requirements related to director compensation and the form of the Director Compensation Table.

⁷ For purposes of Schedule 14A, the terms "participant" and "participant in a solicitation" are defined in paragraphs (a)(iii), (iv), (v), and (vi) of Instruction 3 to Item 4 of Schedule 14A.

⁸ Under Exchange Act Rule 14a-1(a), "associate" means

- any corporation or organization (other than the company or a majority owned subsidiary of the company) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of 10% or more of any class of equity securities;
- any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity; or

- any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the company or any of its parents or subsidiaries.

⁹ The NYSE has proposed requiring that listed companies promptly notify the NYSE of any noncompliance with the corporate governance requirements of Section 303A of the NYSE Listed Company Manual, regardless of materiality. See NYSE Amendments.

¹⁰ The NYSE has proposed amending Section 303A.10 of the NYSE Listed Company Manual to require that listed companies disclose such waivers within four business days following the determination to grant the waiver by distributing a press release, providing website disclosure or in a Form 8-K filed with the SEC. See NYSE Amendments.