

SEC PROPOSES MANDATED ELECTRONIC FILING AND WEBSITE POSTING OF FORMS 3, 4 AND 5

By Margaret F. Murphy and Monique A. Cenac

On December 20, 2002, the SEC released proposed rules under Section 403 of the Sarbanes-Oxley Act of 2002 (the "Act") to *require* electronic filing and website posting of beneficial ownership reports filed by insiders on Forms 3, 4 and 5.

Required Electronic Filing of Forms 3, 4 and 5

Currently, Forms 3, 4 and 5 required by Section 16 of the Securities Exchange Act of 1934 may be filed via EDGAR or in paper format. The Act requires electronic filing no later than July 30, 2003, but the SEC's proposed rules would accelerate that date. A "hardship exemption" would be available to companies if the electronic filing was attempted in good faith, but the filer experienced unanticipated technical difficulties that prevented the timely preparation and submission of the electronic filing. The SEC has also proposed minor changes to Forms 3, 4 and 5 to facilitate compliance with the electronic filing provisions.

Required Website Posting of Forms 3, 4 and 5

In addition, the SEC has proposed to require a company that maintains a corporate website to post on its website all Forms 3, 4 and 5 filed with respect to its equity securities by the end of the business day after filing. In lieu of maintaining and providing direct access to the forms, a company could satisfy the posting requirement by hyperlinking to the reports via a third-party service if the following conditions are met:

- the forms are made available in the appropriate time frame;
- access to the reports is free of charge to the user;
- the display format allows retrieval of all information in the forms;
- the medium to access the forms is not so burdensome that the intended users cannot effectively access the information provided;
- the access includes any exhibits or attachments;

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- the forms are accessible for at least a 12-month period;
- access to the forms is through the company website address the company normally uses for disseminating information to investors; and
- any hyperlink is directly to the Section 16 forms (or to a list of the Section 16 forms) as opposed to the home page or general search page of the third-party service.

The SEC intends to make the website posting requirement effective at the same time as the electronic filing requirement. However, companies are encouraged to post Section 16 reports on their websites prior to the implementation date.

Since comments on the proposed rules may be delivered to the SEC through February 10, 2003, the effective date of the proposals would be some time after February 10, 2003. ([Click here to link to the full text of the SEC's proposals.](#))

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SEC PROPOSES AUDIT COMMITTEE STANDARDS

By Kenneth J. Najder and Monique A. Cenac

On January 8, 2003, the SEC released proposed rules under Section 301 of the Sarbanes-Oxley Act of 2002 to direct the national stock exchanges and associations to prohibit the listing of any security of a public company that is not in compliance with the audit committee requirements established by Congress relating to:

- audit committee member independence;
- the audit committee's responsibility to select and oversee independent auditors;
- procedures for handling accounting complaints; and
- the authority of the audit committee to engage and pay advisors.

Audit Committee Member Independence

The Sarbanes-Oxley Act requires all audit committee members of a public company to be independent. The SEC has proposed two criteria for determining independence.

First, audit committee members would be barred from accepting any consulting, advisory or other compensatory fee from the company, other than in the member's capacity as a board or committee member. To prevent evasions, the proposed rules would bar "indirect" payments of such fees to an audit committee member, which are defined as payments to relatives or to any entity in which the member is a partner, member or principal.

Second, an audit committee member may *not* be an "affiliated person" of the company he or she serves, other than in the member's capacity as a board or committee member. Most outside directors will not be affiliated persons under the SEC's proposed definition unless they beneficially own more than 10% of the company or control it through some other relationship.

Apart from proposing two limited exemptions to these independence standards, the SEC does not currently propose to entertain exemptions or waivers on a case-by-case basis.

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Oversight of Auditors

The SEC has also proposed that audit committees be directly responsible for the appointment, compensation, retention and oversight of the work of the independent auditor, including resolution of disagreements between management and the independent auditor regarding financial reporting. Audit committees would have the authority to retain the independent auditor, including the power to terminate the independent auditor. Audit committees would also have the ultimate authority to approve all audit engagement fees and terms, as well as all significant non-audit engagements of the independent auditor.

Complaint Procedures

In addition, the SEC has proposed that audit committees establish procedures for the (i) receipt, retention and treatment of complaints regarding accounting, internal accounting controls or auditing matters, and (ii) confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters. The SEC has not proposed specific procedures.

Authority to Engage Independent Advisors

The SEC has also proposed to require audit committees to have the authority to engage independent advisors, including counsel, as it determines necessary to carry out its duties. The SEC's proposals would require companies to provide appropriate funding, as determined by the audit committee, for payment of compensation to any auditors or advisors employed by the audit committee.

Other Proposals

The SEC has proposed various other rules to update current proxy disclosure requirements and listing requirements, none of which are likely to materially affect NYSE or Nasdaq companies that have previously furnished audit committee reports in their proxy statements. The SEC's proposals permit stock exchanges to adopt additional listing standards governing audit committees, including more extensive independence requirements. The proposed rules would apply to all listed issuers regardless of size.

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Deadline for SEC's Final Rules

The Sarbanes-Oxley Act requires the new rules to become effective by April 26, 2003. Under the SEC's proposals, the new requirements must be operative by the national stock exchanges and associations no later than the first anniversary of the publication of the SEC's final rule in the Federal Register. Comments on the proposed rules should be delivered to the SEC no later than February 18, 2003. ([Click here to link to the full text of the SEC's proposals.](#))

Please remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues you may contact the head of our Corporate and Securities practice group:

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