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Management Alert

SEC Issues Interpretive Guidance On New Executive Compensation Disclosure Rules

The Securities and Exchange Commission recently issued interpretive guidance on the new executive compensation disclosure rules. In addition to interpreting the new rules in a question and answer format, the guidance also updates interpretations under the former rules that were contained in the Manual of Publicly Available Telephone Interpretations. Below are highlights of some items discussed in the interpretive guidance.

Compensation Discussion and Analysis (CD&A)

The same disclosure provisions governing disclosure about option grants in the CD&A also apply to restricted stock and other non-option equity awards. Accordingly, it may be appropriate to discuss the timing and pricing procedures of all equity awards in the CD&A.

A company must include a discussion in the CD&A assessing the level of difficulty for achieving an undisclosed target if the company is relying on the CD&A instructions that permit information regarding performance targets to be withheld.

Equity Awards

The valuation assumptions of all equity awards reported in the Summary Compensation Table (SCT) must be disclosed or properly cross-referenced in a footnote to the SCT, not just the assumptions for awards made in the last completed fiscal year.

Additionally, awards made after the close of a fiscal year which relate to an executive's performance in that completed fiscal year are reported in the Grant of Plan-Based Awards Table (GPBAT) for the year of grant, and in the SCT in accordance with FAS 123(R) (generally with expensing beginning in the year of grant). The award may need to be discussed, however, in the CD&A for the completed fiscal year.

An equity incentive plan award denominated in dollars but payable in stock should be disclosed in the GPBAT by including the dollar value and a footnote to explain that it will be paid out in the number of shares equal to the dollar amount at the time of the payout. In this limited circumstance, and if all the awards in this column are structured in this manner, it is acceptable to change the captions to show "$" instead of "#."

Performance-Based Cash Compensation

Even if negative discretion is used to determine the amount actually paid, amounts paid under a cash incentive plan not subject to FAS 123(R), that is intended to serve as incentive for performance, where the outcome of the performance target is substantially uncertain when established, and where the target is communicated to the executive in advance, are reportable in the SCT as "non-equity incentive plan compensation," not under the bonus column of the SCT. This means that awards under the typical Section 162(m) compliant cash incentive plan will be shown in the GPBAT in the year of grant at levels much higher than may be actually paid. If discretion is used to increase the amount over and above the amount earned by satisfying the performance measure, the increase is reported in the bonus column of the SCT.

Deferred Compensation

Earnings on amounts credited under a nonqualified excess deferred compensation plan, which is operated in tandem with respect to the investment alternatives offered under a tax-qualified plan, generally are not reported in the SCT as "above-market" or "preferential earnings." The SEC noted that this reporting position may not be available for top-hat plans or SERPs that bear no relationship to a company's tax-qualified plans.

Perquisites

Where the aggregate perquisite disclosure of $10,000 is met or exceeded, a perquisite or other personal benefit must be separately identified by type in a footnote even if it has no aggregate incremental cost to the company. However, disclosure is not required when an executive fully reimburses the company for its total cost of a perquisite or other personal benefit.

Pension Benefits

The earliest age at which a named executive officer may receive an unreduced pension benefit under the terms of an applicable pension plan must be used to calculate the actuarial present value of that executive officer's accumulated pension benefit for purposes of the Pension Benefits Table. The older or "normal" retirement age may also be included as an additional column.

Director Compensation

Director compensation disclosure is required for any person who served as a director during any part of the last completed fiscal year even if the person was no longer a director at the end of the fiscal year or will not stand for re-election the next year.

Employee-directors (who are not named executive officers) who do not receive compensation for their service as a director do not need to be included in the Director Compensation Table. A footnote or narrative disclosure must explain that the director is an executive officer, other than a named executive officer, who does not receive any additional compensation for services provided as a director.

Conclusion

The guidance largely either clarifies application of the new executive compensation disclosure rules or reaffirms and/or updates prior Staff telephone interpretations that were originally issued under the former executive compensation disclosure rules. While the guidance provided is helpful and informative, we are aware that companies are encountering a variety of issues as they prepare their 2007 proxies, as related to their individual facts and circumstances.

A complete copy of the Staff Compliance and Disclosure Guidance is available at the SEC's website at http://www.sec.gov/divisions/corpfin/guidance/execcomp402interp.pdf.

If you have questions or require further guidance with respect to the new executive compensation disclosure requirements or any of the SEC's reporting requirements, please contact Mary Fragola (mfragola@seyfarth.com), Art Meyers (asmeyers@seyfarth.com), Mary Samsa (msamsa@seyfarth.com) or the Seyfarth Shaw attorney with whom you normally work.

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