



## SEC's Proposed Rules on Executive Compensation

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Presented by ACC's Corporate & Securities Law Committee and Morgan, Lewis & Bockius LLP



Association of Corporate Counsel  
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## General Observations

- Comprehensive disclosure of all items of compensation
- Combination of tabular disclosure and narrative description
- Basic principles: Identify and quantify
- Limited relief for small business issuers

## Basic Structure

- Compensation discussion and analysis
- Seven tables of disclosure for executive officers
- Narrative discussion of severance agreements and change-in-control benefits and estimation of dollar amounts
- Director compensation table
- Plain English disclosure

## Required Tables

- Current compensation:
  - Summary compensation table
  - Two supplemental tables for current performance-based and non-performance-based awards
- Equity compensation:
  - Table for outstanding equity awards at year end
  - Table for option exercises and stock vesting

## Required Tables (cont'd)

- Post-employment compensation:
  - Table for estimated annual retirement benefits under defined benefit plans
  - Table for nonqualified defined contribution and other deferred compensation plans
- Director compensation:
  - Cash and equity compensation for last fiscal year

## Impact on Current Item 402 Disclosure

- Elimination of compensation committee report: Replaced by compensation discussion and analysis
- Elimination of stock price performance graph
- Elimination of ten-year option/SAR repricings table

## Covered Executive Officers

- All individuals serving as principal executive officers at any time during the last fiscal year
- All individuals serving as principal financial officers at any time during the last fiscal year
- The three most highly compensated executive officers at end of fiscal year other than the principal executive and financial officers

## Covered Executive Officers (cont'd)

- Up to two additional former officers who would have been included had they continued in executive officer status
- For last two categories of covered individuals, compensation threshold is \$100,000 of total compensation for the year

## Covered Individuals

- Narrative disclosure of position and total compensation of up to three additional persons who are not executive officers and whose total compensation exceeded that of any of the named executive officers

## Compensation Discussion and Analysis

- Narrative disclosure must address six principal topics:
  - Objectives of the compensation programs
  - What the programs are designed to reward and not reward
  - Elements of compensation
  - Reason for each element
  - Determination of the amount of each element
  - Relationship of each element to others and to overall compensation objectives

## Compensation Discussion and Analysis (cont'd)

- Must address both in-service and post-termination compensation arrangements
- The CD&A will be considered part of the filed proxy statement or any other filing in which it is included:
  - Potential liability under '33 and '34 Acts
  - CEO and CFO certifications

## Compensation Discussion and Analysis (cont'd)

- Discussion and analysis of the material factors underlying compensation policies and decisions
- Examples of material information in CD&A:
  - Long vs. short-term comp. allocation policy
  - Cash vs. non-cash comp. allocation policy
  - Timing of equity awards
  - Corporate performance measures
  - Individual performance measures
  - Discretion re performance bonuses
  - Factors considered when materially changing comp.
  - Whether and how benchmarking was used
  - Role of executive officers in determining executive compensation

## Compensation Discussion and Analysis (cont'd)

- Not required to disclose target levels, or have confidential criteria if disclosure would have an adverse effect on company

## Current Compensation

- All compensation must be disclosed
- Summary compensation table includes the following columns, expressed in dollars:
  - Total compensation
  - Salary
  - Bonus
  - Stock awards
  - Option awards
  - Non-stock incentive plan compensation
  - All other compensation

## Summary Compensation Table

Name and Principal Position	Year	Total (\$)	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Stock Incentive Plan Compensation (\$)	All Other Compensation (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)
PEO <sup>55</sup>	_____							
	_____							
	_____							
PFO <sup>69</sup>	_____							
	_____							
	_____							
A	_____							
	_____							
	_____							
B	_____							
	_____							
	_____							
C	_____							
	_____							
	_____							



## Current Compensation

- Stock and option awards are to be included at their grant date fair value, as determined under FAS 123R for financial accounting purposes
  - Options or SARs that are repriced or materially modified must be disclosed at total fair value as modified

## Current Compensation (cont'd)

- All Other Compensation column:
  - Must include all other compensation
  - Must identify each item of compensation that exceeds \$10,000, quantified in a footnote
  - Must include earnings on deferred compensation
  - Must include increase in actuarial value of benefits accrued during the year under defined benefit plans (qualified plans and supplemental plans)

## Current Compensation (cont'd)

- Must disclose perquisites unless aggregate amount is less than \$10,000
- Must identify each disclosed perquisite
- If a perquisite is valued at the greater of \$25,000 or 10% of the total perquisites, must disclose its value
- Must quantify and identify tax gross-ups
- Must include amounts paid or accrued in connection with termination of employment or change of control

## “All Other Compensation” (Suggested, not required)

Name	Perquisites and Other Personal Benefits	Earnings on Deferred Compensation	Tax Reimbursements	Discounted Securities Purchases	Payments/Accruals on Termination Plans	Registrant Contributions to Defined Contribution plans	Increase in Pension Actuarial Value	Insurance Premiums	Other
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
PEO									
PFO									
A									
B									
C									

## Current Compensation

- Two supplemental tables for current compensation:
  - Grants of performance-based awards
  - Grants of all other equity awards

## Grants of Performance-Based Awards

Name	Performance-Based Stock and Stock-based Incentive Plans: number of shares, units or other rights (#)	Performance-Based Options: number of securities underlying Options (#)	Non-Stock Incentive Plan Awards: number of units or other rights (#)	Dollar amount of consideration paid for award, if any (\$)	Grant Date for Stock or Option Awards	Performance or other period until vesting or payout and Option Expiration Date	Estimated future payouts		
							Threshold (\$ or #)	Target (\$ or #)	Maximum (\$ or #)
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
PEO									
PFO									
A									
B									
C									

## Grants of All Other Equity Awards

Name	Number of Securities Underlying Options Granted (#)	Exercise or Base Price (\$/Sh)	Expiration Date	Number of Shares of Stock or Units Granted (#)	Vesting Date	Grant Date
(a)	(b)	(c)	(d)	(e)	(f)	(g)
PEO						
PFO						
A						
B						
C						

## Equity Compensation

- Two equity compensation tables:
  - Equity that has previously been awarded and remains outstanding (unexercised or unvested)
  - Amounts realized upon exercise of options or SARs or upon vesting of other equity awards

## Outstanding Equity Awards at Fiscal Year-End

Name	Number of securities underlying unexercised Options (#) Exercisable/Unexercisable	In-the-money amount of unexercised Options (\$) Exercisable/Unexercisable	Number of shares or units of Stock held that have not vested (#)	Market value of shares or units of Stock held that have not vested (\$)	Incentive Plans: Number of nonvested shares, units or other rights held (#)	Incentive Plans: Market or payout value of nonvested shares, units or other rights held (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)
PEO						
PFO						
A						
B						
C						

## Option Exercises and Stock Vested

Name of Executive Officer	Number of Shares Acquired on Exercise Or Vesting (#)	Value Realized Upon Exercise Or Vesting (\$)	Grant Date Fair Value Previously Reported in Summary Compensation Table (\$)
(a)	(b)	(c)	(d)
PEO - Options Stock			
PFO - Options Stock			
A - Options Stock			
B - Options Stock			
C - Options Stock			

## Post-Employment Compensation

- Defined benefit retirement plan benefits:
  - Table showing estimate of retirement benefits payable at normal retirement age and early retirement age
  - Narrative explanation

## Retirement Plan Potential Annual Payments and Benefits

Name	Plan name	Number of years credited service (#)	Normal retirement age (#)	Estimated normal retirement annual benefit (\$)	Early retirement age (#)	Estimated early retirement annual benefit (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)
PEO						
PFO						
A						
B						
C						

## Post-Employment Compensation

- Nonqualified defined contribution plan benefits:
  - Table showing contributions, earnings and account balances
  - Narrative explanation

## Nonqualified Defined Contribution and Other Deferred Compensation Plans

Name	Executive contributions in last FY (\$)	Registrant contributions in last FY (\$)	Aggregate earnings in last FY (\$)	Aggregate withdrawals/distributions (\$)	Aggregate balance at last FYE (\$)
(a)	(b)	(c)	(d)	(e)	(f)
PEO					
PFO					
A					
B					
C					

## Termination or Change-in-Control Arrangements

- Narrative disclosure must address:
  - Specific circumstances triggering payment
  - Estimated payments and benefits and method of payment
  - Specific factors used to determine payment levels under various triggering circumstances
  - Material conditions to payments and benefits:
    - Non-compete, non-solicitation, non-disparagement
  - Other material features
- Quantitative disclosure required even where uncertainties exist

## Director Compensation

- Table disclosing director compensation (one-year table)
  - Includes all compensation
  - Includes perquisites if total is \$10,000 or more
  - Footnote disclosure of outstanding equity awards
- Narrative explanation



## Director Compensation Table

Name	Total (\$)	Fees earned or paid in cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Stock Incentive Plan Compensation (\$)	All Other Compensation (\$)
(a)	(b)	(c)	(d)	(e)	(f)	(g)
A						
B						
C						
D						
E						

## Other Reforms

- Related-party disclosure reformatted
  - \$120,000 reporting threshold
- Director independence disclosure
- Corporate governance disclosure
  - Including new compensation committee disclosure
- Disclosure of pledged shares
- Form 8-K reforms

## What Should Companies Be Doing in 2006?

- Tally sheets
  - See [compensationstandards.com](http://compensationstandards.com) website for sample tally sheets
- Total compensation review
- Perquisites analysis

## What Should Companies Be Doing in 2006?

- Analysis of compensation objectives and how the various elements of compensation achieve the objectives
- SEC comment period
  - Comment period ends April 10, 2006

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