



Executive Compensation Disclosure

In 2006, the SEC finalized a wide-ranging expansion of the disclosure required by public companies of the compensation paid to their top executives. The rules affect disclosure in proxy statements, annual reports and registration statements.

The rules require disclosure of the compensation of the principal executive officer (PEO), principal financial officer (PFO), and the three other highest paid executive officers by total compensation (“Named Executive Officers” or “NEOs”), as well as the directors of a company.

This paper primarily focuses on the rules as they apply to nonqualified deferred compensation plans. The rules differ with respect to defined contribution plans and defined benefit plans and are discussed separately below. Rules as they affect other executive benefit plans are noted after the discussion of nonqualified deferred compensation plans.

NOTE

In recognition that the compensation arrangements of small business issuers (generally companies with revenues and public equity float of less than \$25 million) are less complex than other public companies, the SEC subjects these issuers to less onerous disclosure requirements, outlined at the end of this paper.

Summary of Rules as They Affect Nonqualified Defined Contribution Plans

Disclosure of nonqualified defined contribution plan benefits is required in:

- The Summary Compensation Table
- The Nonqualified Deferred Compensation Table

Nonqualified defined contribution plans include all voluntary executive deferral plans, including 401(k)-mirror plans, as well as any plan in which the company credits an executive with contribution amounts and earnings. Such plans may also be referred to as account balance plans. If the company promises a specified benefit under a plan, for example 60% of final average salary at retirement, their benefit would be disclosed under the defined benefit plan disclosure rules described further below.

The Summary Compensation Table

The Summary Compensation Table (SCT) is the principal vehicle for showing total compensation for NEOs over the last three fiscal years. The SCT will look something like this:

1	2	3	4	5	6	7	8	9	10
Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation	Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$)	All Other Compensation (\$)	Total (\$)
PEO	____								

PFO	____								

A	____								

B	____								

C	____								

Salary, bonus, and other compensation that is deferred under a nonqualified deferred compensation plan must be disclosed in the proper column (e.g., if a deferral would otherwise have been paid as salary then the deferral should be reported as Salary in Column 3 along with any salary that was paid and not deferred).

Above-market or preferential earnings credited to account balances in a nonqualified defined contribution plan are reported in Column 8 of the SCT. If there is no above-market or preferential earnings credited, then earnings are not reported in the SCT.

Under All Other Compensation (Column 9), the company must report any other compensation for the year that the company does not report in another column of the SCT. This includes company contributions or other allocations to vested and unvested defined contribution plans.

Note that *distributions* from a nonqualified plan of any type are *not* reportable in the SCT.

Nonqualified Deferred Compensation Table

Companies must disclose both executive and company contributions, as well as all earnings, withdrawals, distributions and balances under all nonqualified defined contribution plans in the Nonqualified Deferred Compensation Table (NDCT). In contrast to the SCT, *all* earnings must be reported here, even if earnings reflect a market rate of return. The NDCT will look like this:

1	2	3	4	5	6
Name of Executive Officer	Executive Contributions in Last Fiscal Year (\$)	Employer Contributions in Last Fiscal Year (\$)	Aggregate Earnings in Last Fiscal Year (\$)	Aggregate Withdrawals/ Distributions (\$)	Aggregate Balance at Last Fiscal Year End (\$)
PEO					
PFO					
A					
B					
B					

A narrative disclosure must follow the NDCT describing the material factors necessary to an understanding of the table information, including:

- Type(s) of compensation permitted to be deferred;
- Limitations on deferrals;
- Measures of calculating interest or other plan earnings;
- Quantifying interest rates, and other earnings measures applicable during the company's last fiscal year; and
- Material terms with respect to payouts, withdrawals, and other distributions.

In addition, the narrative disclosure should quantify the extent to which amounts reported in the contributions and earnings columns are reported as compensation in the last completed fiscal year in the SCT as well as amounts reported in the Aggregate Balance at Last Fiscal Year End column (Column 6) that have previously been reported as compensation to the NEO in the SCT for previous years. The idea behind this is to show how much of the compensation reported in the NDCT has already been reported in the SCT. The intent is to limit the amount of compensation that would otherwise be double-counted.

Disclosure in the NDCT does *not* include contributions to, or earnings within, a qualified plan, such as a 401(k) plan. Compare this treatment with the treatment below of qualified defined benefit plans below.

Summary of Rules as They Affect Nonqualified Defined Benefit Plans

Nonqualified defined benefit plan disclosure is required in:

- The Summary Compensation Table
- The Pension Benefits Table

Summary Compensation Table

The SCT must include, in Column 8, the change in actuarial present value of accumulated pension benefits. (Note: this value is included in the Total Compensation reported in the last column (Column 10), but it is *not* used to determine who is an NEO.)

Pension Benefits Table

The Pension Benefit Table (PBT) includes for each defined benefit plan in which an NEO participates, including *both* qualified and nonqualified plans, the plan name, the number of years of credited service under the plan, the present value of accumulated benefits, and payments made during the last fiscal year:

1	2	3	4	5
Name of Executive Officer	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefit (\$)	Payments During Last Fiscal Year (\$)
PEO				
PFO				
A				
B				
B				

Following the PBT, there must be additional narrative disclosure of all material factors necessary to an understanding of each plan covered by the PBT. While material factors will vary depending upon the facts, examples of such factors listed by the SEC include:

- The material terms and conditions of payments and benefits available under the plan, including the plan's normal retirement payment and benefit formula and eligibility standards, and the effect of the form of benefit elected on the amount of annual benefits.
- If any NEO is currently eligible for early retirement under any plan, identify that named executive officer and the plan, and describe the plan's early retirement payment and benefit formula and eligibility standards.
- The specific elements of compensation (e.g., salary, bonus, etc.) included in applying the payment and benefit formula, identifying each such element.
- With respect to NEOs' participation in multiple plans, the different purposes for each plan.
- Policies with regard to such matters as granting extra years of credited service.

Other Benefits

Perquisites

Unless the aggregate amount of perquisites and other personal benefits for an NEO is less than \$10,000, a company must disclose in the SCT, the amount of perquisites and other personal benefits for a named executive officer, and each perquisite or other personal benefit must be identified in a footnote to the table. Furthermore, if a perquisite or other personal benefit is valued at the greater of \$25,000 or 10% of the total perquisites and other personal benefits for the NEO, the value must be described in a footnote that identifies the particular nature of the benefit received (e.g., clothing, jewelry, artwork, or theatre tickets financed by a company cannot be characterized generally as “travel and entertainment”).

Examples of items that must be disclosed as perquisites or other personal benefits include:

- Club memberships not used exclusively for business entertainment purposes
- Personal financial or tax advice
- Personal travel using vehicles owned or leased by the company
- Personal travel otherwise financed by the company (e.g., use of the company’s aircraft)
- Personal use of other property owned or leased by the company

Perquisites and other personal benefits must be valued based on the company’s aggregate incremental cost of providing the benefit and not on the cost attributed to the benefit for Federal income tax purposes. In addition, footnote disclosure of the methodology for computing the aggregate incremental cost for the benefits is required.

Life Insurance

Under All Other Compensation (Column 9) of the SCT, the company must report the dollar value of any insurance premiums paid by the company with respect to any life insurance for the benefit of an NEO. This is a change from prior law which required, with respect to an endorsement split dollar plan, for example, the disclosure of the value of the death benefit protection. The current requirement will in many cases significantly overstate the benefit provided by the company with respect to life insurance benefits provided to an executive and will certainly overstate the value of an endorsement split-dollar benefit.

Other Insurance Products including Disability or LTC Insurance

Any other premiums paid on an insurance product for an NEO would likewise be included in the All Other Compensation column (Column 9). This would include payments of disability premiums and presumably would also include premium paid on long-term care insurance premiums even if those premiums are not considered compensation to the NEO for tax purposes.

Proxy Rules Applicable to Small Business Issuers

A “small business issuer” is defined as a company that meets all of the following criteria:

- Has revenues of less than \$25,000,000;
- Is a U.S. or Canadian issuer;
- Is not an investment company and is not an asset-backed issuer; and
- If a majority owned subsidiary, the parent corporation is also a small business issuer.

Provided however, that an entity is not a small business issuer if it has a public float (the aggregate market value of the issuer's outstanding voting and nonvoting common equity held by nonaffiliates) of \$25,000,000 or more.

Small business issuers will be required to provide, along with related narrative disclosure:

- The Summary Compensation Table;
- The Outstanding Equity Awards at Fiscal Year-End Table; and
- The Director Compensation Table.

Small business issuers will be required to provide information in the Summary Compensation Table only for the last two fiscal years. In addition, small business issuers will be required to provide information for fewer named executive officers, namely the principal executive officer and the two most highly compensated officers other than the principal executive officer. Neither the Nonqualified Deferred Compensation Table nor the Pension Benefits Table are required. Pension plan disclosure will not be required in the Summary Compensation Table; however, above-market earnings in nonqualified deferred compensation plan will be required.

However, in lieu of tabular disclosure of nonqualified benefits, the rules call for a narrative disclosure of the material terms of each plan that provides for the payment of retirement benefits, or benefits that will be paid primarily following retirement, including but not limited to tax-qualified defined benefit plans, supplemental executive retirement plans, tax-qualified defined contribution plans and nonqualified defined contribution plans.