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Comprehensive Compensation℠

# CLIENT ALERT

## Final SEC Rules: What's Changed?

The SEC's final rules for disclosure of executive compensation, adopted July 26, deviate from the agency's earlier thinking in a number of key respects. This document summarizes the key changes made following extensive public commentary on the agency's initial draft. Please check our Website to obtain a more detailed analysis of the rules when the SEC's final text is released, as well as to register for a Webinar on August 10 about the new rules.

1. **New disclosure of details regarding stock option programs, policies and practices –** Reacting to recent controversy over the pricing and dating of stock option grants, the SEC will require companies to provide additional information on option grant practices including:

(A) ***Clear Tabular Disclosure of:***

- The grant date fair value
- The FAS 123R grant date
- The closing market price on the grant date, if it is greater than the award exercise price
- The date of Committee action, if the grant date differs from the date the Compensation Committee approved the grant

In addition, the company must include a narrative description of the methodology used to determine the different exercise price.

(B) ***Additional Narrative Disclosure in the CD&A –*** Companies must provide details regarding the scheduling of annual option awards; any grants made outside of normal practice; and the methodology used to determine option exercise prices.

The CD&A also must address specific questions such as:

- Are option grants for current or new employees ever timed in coordination with the release of material non-public information?
- Does the company plan to time the release of material nonpublic information in order to affect the value of executive compensation?
- Are there differences between the company's grant practices for executives as opposed to employees?
- What were the roles of the Compensation Committee and the executive officers in determining or approving option grants?

Narrative disclosure also will be required if a company has a program of awarding options and setting exercise prices on dates other than actual grant date or if a company determines the exercise price of option grants by using formulas.

2. **Calculation of compensation for purposes of determining which employees will be listed in the Summary Compensation Table ("SCT") will exclude earnings on non-qualified deferred compensation ("NQDC") and increases in actuarial pension value.**

3. **More narrow definition proposed for "Top 3 Other Employees" –** Following criticism of what was widely dubbed the "Katie Couric" rule, the SEC revised its proposal that companies disclose the job description and compensation of up to three non-executive employees whose total pay exceeded any of the NEOs' compensation. Disclosure would be required only by "large accelerated filers" and only for those employees who have significant policy-making powers at the parent company, a significant subsidiary, principal business unit, division or function of the company. The SEC specifically stated that the new requirement will exclude investment bankers, traders, entertainment personalities or professional athletes who lack such a policy making role. The SEC staff plans to submit this revision for public comment.

4. **The Compensation Committee Report (CCR) will be retained –** This will be a brief report stating that following review and discussion of the CD&A with management, the Compensation Committee recommends to the full board that the CD&A be included in the annual report.

5. **The Pension Benefits Table will require disclosure of the actuarial present value of each named executive officer's accumulated benefit under each pension plan, calculated using standardized assumptions**.

6. **Only above-market earnings on NQDC plans will be included as compensation on NQDC plans for purposes of the SCT.**

7. **Dividends on restricted stock will not be included as compensation in the SCT.**

8. **Clarification of transaction/termination payments –** Calculations should assume that the event occurred on the last day of the registrant's fiscal year and use the closing share price on that date.

9. **The current Performance Graph will be retained –** However, the graph will no longer be part of compensation disclosure provisions.

10. **Transition period extended –** New disclosure requirements will apply to filers with fiscal years ending on or after 12/15/06, rather than the earlier proposal to cover companies with fiscal years beginning within 90 days following adoption of the new rules. The new 8-K rules will apply 60 days after publication in the Federal Register.

*- July 31, 2006*