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# The SEC Proposes New Pay-for-Performance Disclosures

On April 29, 2015, the U.S. Securities and Exchange Commission (SEC) voted three-to-two to adopt proposed rules to implement Section 14(i) of the Securities Exchange Act of 1934, which was added by Section 953(a) of the Dodd-Frank Act. The proposed rules add a new Item 402(v) to Regulation S-K to require disclosure about the relationship between executive compensation “actually paid” and a company’s financial performance in a new “Pay Versus Performance” (PVP) table as well as a related narrative.

## Determining Compensation “Actually Paid”

Based on the requirement in the Dodd-Frank Act that the pay-for-performance disclosure be based on compensation actually paid, the SEC proposal requires companies to disclose a new measure of executive pay, which it believes more closely aligns with an executive’s realized compensation for a given year.

As proposed, this new measure of “executive compensation actually paid” for each fiscal year is calculated as the total compensation reported in the Summary Compensation Table (SCT) of a company’s proxy statement, with two adjustments:

1. Certain pension costs would be excluded (e.g. the actuarial value of pension benefits not earned during the applicable year); and
2. Amounts included in total compensation from the “Stock Awards” and “Option Awards” columns of the SCT (which reflect grant date-based compensation cost to the company) would be replaced with an amount representing the fair value of equity awards on the vesting date during the covered fiscal year.

In addition, each such adjustment would be described in a footnote to the PVP table.

**Proposed New “Pay Versus Performance” Table**

| Year<br><br>(a) | Summary Compensation Table Total for PEO<br><br>(b) | Compensation Actually Paid to PEO<br><br>(c) | Average Summary Compensation Table Total for non-PEO Named Executive Officers<br><br>(d) | Average Compensation Actually Paid to non-PEO Named Executive Officers<br><br>(e) | Total Shareholder Return<br><br>(f) | Peer Group Total Shareholder Return<br><br>(g) |
|-----------------|---|--|--|---|-------------------------------------|--|
|                 |   |  |  |   |                                     |  |

The proposed rules add a new PVP compensation table to a company’s proxy or information statement that would include, for each of the company’s last five fiscal years, the following information:

Compensation actually paid (determined as described above), to the principal executive officer, and separately, the average compensation actually paid to the other named executive officers listed in the SCT;

Financial performance of the company, measured as the company’s total shareholder return (TSR) and a peer group’s cumulative TSR for each of the past five fiscal years. The peer group would either be (1) the same peer group used for the stock performance graph, or, if applicable, (2) the peer group reported in the company’s compensation discussion and analysis section of the proxy statement; and

For comparison purposes, the total compensation already reported in the SCT for the principal executive officer and the average for the other named executive officers.

Companies would be required to tag the elements in this table in an interactive data format using eXtensible Business Reporting Language (XBRL). The interactive format is intended to facilitate

comparisons among companies and analysis of changes in information for a single company over time.

## **Narrative Disclosure**

Under the proposed rule, the PVP table must be accompanied by a “clear description” of the relationship between the executive compensation actually paid and the company’s TSR, as well as the relationship between the company’s TSR and the TSR of its selected peer group. This disclosure may be described as a narrative, graphically, or a combination of the two.

## **Covered Companies**

The proposed rules would apply to all reporting companies except for foreign private issuers, registered investment companies and emerging growth companies. Smaller reporting companies would be subject to the disclosure requirements on a modified basis (e.g., information for only the last three completed fiscal years and no peer group TSR).

## **Timing**

If the proposed rules are finalized, companies will be required to provide the information described above for three years in their first covered proxy statement, phasing into the full five-year disclosure by adding another year in each of next two proxies. Similarly, smaller reporting companies initially will be required to provide two years of pay versus performance information, phasing in the third year in the next year’s proxy.

## **What This Means to You**

Comments will be accepted by the SEC for 60 days after the proposed rules are published in the Federal Register. Final rules could be adopted as early as this fall and effective for the 2016 proxy season. However, given the political controversy surrounding the proposed rules, public debate and Congressional pressure may push final rules further into the future.

## **Contact Us**

If you have questions about the proposed rules or other related topics, please contact Jeff Haughey at 303.749.7231.