

# HR & Tax Alert



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## SEC - new disclosure rules for executive pay

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### Executive Summary

On 26 July 2006, the US Securities and Exchange Commission ("SEC") adopted comprehensive final rules relating to the disclosure of executive compensation. The new rules are the first major overhaul of the SEC disclosure guidelines relating to executive compensation in over 14 years and are designed to ensure that companies state in plain English the total compensation paid to the company's top executives. This Alert outlines the main changes.

### New Rules Regarding Disclosure of Executive Compensation

The final rules will affect disclosures made in proxy statements, annual reports and registration statements, e.g. annual reports on Form 10-K, and will apply for fiscal years ending on or after 15 December 2006. (Although certain disclosures, such as disclosures on Form 8-K, will need to be made prior to this date). Companies with an SEC filing requirement or with a US connection will need to consider how the new rules will apply to them. Some of the key requirements of the new rules include:

- A new Compensation Discussion and Analysis ("CD&A") section will be required. The CD&A will be a principles-based discussion and overview explaining the specific policies and decisions related to the compensation of the company's named executive officers. The CD&A will be considered a "filed" document and will therefore be part of the disclosure subject to

certification by a company's principal executive officer and principal financial officer.

- A new furnished Compensation Committee Report will be included and will require a statement as to whether the Compensation Committee has reviewed and discussed the CD&A with management, and based on this review and discussion, has recommended to the Board that it be included in the company's annual report on Form 10-K and proxy statement.
- A Summary Compensation Table ("SCT") will be included and will serve as the principal disclosure vehicle for executive compensation. It will provide a three-year summary of salary, bonus, equity and non-equity awards, pension benefits and all other compensation not reported in the other columns of the table including perquisites (perquisites subject to an aggregate de minimis limit of \$10,000) and a column showing the aggregated total compensation. The SCT is designed to enable investors and other interested parties to compare the overall compensation of executives across different companies. The SCT will be supplemented by an additional table entitled Grants of Plan Awards setting out details of awards granted. Where it is material, companies will be required to disclose performance targets for incentive plans in the narrative disclosure or in the CD&A (unless such disclosure would result in competitive harm to the company).

- A new Director Compensation Table will provide tabular disclosure of director compensation for the most recent fiscal year in a format similar to the SCT. A narrative disclosure will also be required.
- Disclosure relating to outstanding equity related compensation and holding will be required. The company will be required to disclose in the CD&A its plans and practices relating to the grant of options and in particular the timing of option grants in coordination with the release of material non-public information and the selection of exercise prices which differ from the underlying stock's price on grant date. The company will also be required to specifically disclose the full Statement FAS 123(R) grant date fair value of an option, the FAS 123(R) grant date and disclosure of the date when the Compensation Committee took action on an option grant if that date is different from the date of grant.
- Other disclosure requirements include tabular disclosure about retirement and post-employment compensation which requires disclosure of the actuarial present value of each named executive officer's accumulated pension benefit computed using the same assumptions (except for the normal retirement age) and measurement period as used for financial statement purposes under generally accepted accounting principles; a narrative description of any arrangements that provide for payments or benefits with regard to any termination of a named executive officer, a change in responsibilities or a change in control of the company (including a reasonably estimated quantification of amounts payable in such circumstances); the disclosure of related persons transactions and director independence.

#### **Next Steps**

This Alert is only a brief overview of some of the key issues relating to the new SEC rules. We will continue to keep you updated of further developments as they arise.

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