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SEC Proposes Rules for Pay for Performance Disclosure

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On April 29, 2015, the Securities and Exchange Commission proposed rules requiring companies to disclose the relationship of executive pay to performance as required by Section 953 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Under Dodd-Frank, the SEC was required to adopt rules requiring public companies to disclose in any proxy or consent solicitation material for an annual meeting of shareholders a clear description of any compensation required to be disclosed by the issuer under Item 402 of Regulation S-K, including information that shows the relationship between executive compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends of the issuer and any distributions. If adopted, these rules would require issuers to disclose, in tabular format, compensation “actually paid” to their principal executive officer and an average of the compensation “actually paid” to their other named executive officers over a five-year period for large issuers. In addition, issuers would be required to disclose their total shareholder return, or TSR, along with that of a peer group, for the same five-year period.

More specifically, the tabular disclosure includes:

- The PEO’s total compensation for each year as reported in the Summary Compensation Table;
- The executive compensation actually paid to the PEO for each year;
- The average total compensation paid to each of the other NEOs for each year as reported in the Summary Compensation Table;
- The average executive compensation actually paid to each of the other NEOs for each year;
- Total shareholder return; and
- Peer group total shareholder return (not required for smaller reporting companies).

In addition to the tabular presentation, issuers would be required to describe the relationship between executive compensation actually paid and the issuer’s TSR, and the relationship between the issuer’s TSR and peer group TSR. Such description could be in narrative or graphic form.

In order to capture the Dodd-Frank required measure of "executive compensation actually paid," the proposed rules define compensation "actually paid" in a highly prescriptive manner. Compensation "actually paid" would be calculated as follows:

- Begin with total compensation from the Summary Compensation Table;
- Subtract the change in the actuarial present value of the accumulated benefit under all defined benefit and actuarial pension plans reported in the Summary Compensation Table;
- Add the service cost (as defined in FASB ASC Topic 715) under all defined benefit and actuarial pension plans;
- Subtract compensation reported in the Summary Compensation Table related to stock and options awards; and
- Add the fair value as of the vesting date for any stock or option awards that vested during the year being reported.

Amounts added or subtracted pursuant to the calculation method described above must be disclosed in footnotes to the table. Smaller reporting companies would only make the adjustments described above for stock and option awards.

Although the proposed tabular disclosure would be added to Item 402, the disclosure may appear anywhere in the issuer's proxy statement. The disclosure would comprise executive compensation disclosure and would therefore be subject to an issuer's say-on-pay vote. Notably, the proposed rules would require the tabular disclosure, related footnotes and additional disclosure to be provided in tagged data format using eXtensible Business Reporting Language (XBRL) to assist investors with comparing results among issuers.

The proposed rules do not apply to emerging growth companies, registered investment companies or foreign issuers. The information is required to be reported for five years for most issuers, beginning with three years in the first year of reporting and phasing in an additional year until five years is reached. Smaller reporting companies are required to report the information for three years, beginning with two-year reporting. Newly reporting companies may begin with one year.

The SEC has requested public comment on the proposed rules, raising several specific questions in the proposing release. Comments must be received on or before the date that is 60 days after the proposed rules are published in the Federal Register.

The full text of the proposed rule may be found ***here.***