

# Everything Perquisites: The 101 Training Course

**Presentation for:**  
Executive Compensation Webinar Series  
August 8, 2019

**Presentation by:**  
Emily Cabrera  
[EmilyCabrera@HuntonAK.com](mailto:EmilyCabrera@HuntonAK.com)  
281.602.0829

# Housekeeping: Technical Issues and Questions

- Technical issues
  - If you are having difficulty viewing this presentation, please call ReadyTalk Support toll free at 800.843.9166 or e-mail at [help@readytalk.com](mailto:help@readytalk.com)
  
- Questions during this presentation
  - We encourage questions (even though your audio lines are muted)
  - To submit a question, simply type the question in the blank field on the right-hand side of the menu bar and press return
  - If time permits, your questions will be answered at the end of this presentation. And if there is insufficient time, the speaker will respond to you via e-mail after this presentation

# Housekeeping: Recording, CE Credits and Disclaimer

- Recording
  - This presentation is being recorded for internal purposes only
- Continuing education credits
  - A purpose of the webinar series is to provide FREE CE credits
  - To that end, each presentation is intended to provide 1 credit hour in the following areas:
    - CLE: 1 credit hour (CA, FL, GA, NC, NY, TX and VA)
    - CPE: 1 credit hour (Texas)
    - HRCI: This activity has been approved for 1 (HR (General)) recertification credit hours toward California, GPHR, PHRI, SPHRI, PHR, and SPHR recertification through the HR Certification Institute
    - SHRM: This program is valid for 1 PDC for the SHRM-CPSM or SHRM-SCPSM
  - If you have any questions relating to CE credits, please direct them to Anthony Eppert at [AnthonyEppert@HuntonAK.com](mailto:AnthonyEppert@HuntonAK.com) or 713.220.4276
- Disclaimer
  - This presentation is intended for informational and educational purposes only, and cannot be relied upon as legal advice
  - Any assumptions used in this presentation are for illustrative purposes only
  - No attorney-client relationship is created due to your attending this presentation or due to your receipt of program materials

# About Emily Cabrera



Emily Cabrera, Associate  
Hunton Andrews Kurth LLP  
Tel: +1.281.602.0829  
[EmilyCabrera@HuntonAK.com](mailto:EmilyCabrera@HuntonAK.com)

- Emily practices in the areas of taxation, executive compensation and employee benefits
  
- Before entering private practice, Emily:
  - Obtained her B.A. at Harvard University
  - Obtained her J.D. from the University of California at Berkeley School of Law
    - Membership Development Editor, California Law Review
    - Law and Economics Fellowship
    - Prosser Prize for Property and Corporate Tax Law
    - Fenwick Tax Award
  
- Emily is licensed to practice in:
  - Texas
  - California

## Upcoming 2019 Webinars

- Upcoming 2019 webinars:
  - Preparing for Proxy Season: Start Now (Annual Program) (9/12/2019)
  - Stock Ownership Policies & Clawback Policies: Design Pointers (10/10/2019)
  - Employee Stock Purchase Plans: The Introductory Course (11/14/2019)
  - How to Design Restrictive Covenants & Economic Forfeitures (12/12/2019)
  
- Sign up here: <https://www.huntonak.com/en/insights/executive-compensation-webinar-schedule.html>

## Our Compensation Practice – What Sets Us Apart

- Compensation issues are complex, especially for publicly-traded issuers, and involve substantive areas of:
  - Tax,
  - Securities,
  - Accounting,
  - Governance,
  - Surveys, and
  - Human Resources
  
- Historically, compensation issues were addressed using multiple service providers, including:
  - Tax lawyers,
  - Securities/corporate lawyers,
  - Labor & employment lawyers,
  - Accountants, and
  - Survey consultants

# Our Compensation Practice – What Sets Us Apart (cont.)

- The members of our Compensation Practice Group are multi-disciplinary within the various substantive areas of compensation. As multi-disciplinary practitioners, we take a holistic and full-service approach to compensation matters that considers all substantive areas of compensation



# Our Compensation Practice – What Sets Us Apart (cont.)

- Our Compensation Practice Group provides a variety of multi-disciplinary services within the field of compensation, including:

## Traditional Consulting Services

- Surveys
- Peer group analyses/benchmarking
- Assess competitive markets
- Pay-for-performance analyses
- Advise on say-on-pay issues
- Pay ratio
- 280G golden parachute mitigation

## Corporate Governance

- Implement “best practices”
- Advise Compensation Committee
- Risk assessments
- Grant practices & delegations
- Clawback policies
- Stock ownership guidelines
- Dodd-Frank

## Securities/Disclosure

- Section 16 issues & compliance
- 10b5-1 trading plans
- Compliance with listing rules
- CD&A disclosure and related optics
- Sarbanes Oxley compliance
- Perquisite design/related disclosure
- Shareholder advisory services
- Activist shareholders
- Form 4s, S-8s & Form 8-Ks
- Proxy disclosures

## Design/Draft Plan

- Equity incentive plans
- Synthetic equity plans
- Long-term incentive plans
- Partnership profits interests
- Partnership blocker entities
- Executive contracts
- Severance arrangements
- Deferred compensation plans
- Change-in-control plans/bonuses
- Employee stock purchase plans
- Employee stock ownership plans

## Traditional Compensation Planning

- Section 83
- Section 409A
- Section 280G golden parachutes
- Deductibility under Section 162(m)
- ERISA, 401(k), pension plans
- Fringe benefit plans/arrangements
- Deferred compensation & SERPs
- Employment taxes
- Health & welfare plans, 125 plans

## International Tax Planning

- Internationally mobile employees
- Expatriate packages
- Secondment agreements
- Global equity plans
- Analysis of applicable treaties
- Recharge agreements
- Data privacy



# Purpose of this Presentation

- **Overview:** Perquisites and other personal benefits (referred to herein together as “perks”) are one of the biggest hot button issues relating to executive pay. In addition, the SEC has recently taken enforcement action in cases where perks were not properly disclosed. Therefore, it is more important than ever that issuers have the necessary tools and procedures to ensure that perk disclosure in the proxy statement is accurate and complete
  
- The purpose of this discussion is to cover:
  - Identifying a perk;
  - Examples of perks;
  - Disclosure of perks in the Summary Compensation Table (“SCT”);
  - Valuation of perks;
  - Disclosure of perks in the CD&A;
  - SEC Enforcement Activity; and
  - Practical advice

## What is a Perk?

- The item in question is a perk if:
  - The item is NOT “integrally and directly related to the performance of the executive’s duties”; and
  - The item confers a direct or indirect benefit on the executive that is personal in nature, regardless of whether a business purpose exists or if the item was provided for the convenience of the issuer, unless it is generally available on a non-discriminatory basis
  
- **Step #1**: Is the item integrally and directly related to the performance of the executive’s duties?
  - More stringent standard than the business purpose test
  - Whether the item qualifies as an “ordinary” and “necessary” business expense for tax purposes is NOT determinative as to whether the item qualifies as a perk under SEC rules
  - The analysis draws a critical distinction between an item that an issuer provides because the executive needs it to do the job, making it integrally and directly related to the performance of duties, and an item provided for some other reason, even where that other reason can involve both company benefit and personal benefit
  
- Items that may have a business purpose, but are considered perks by the SEC include:
  - Security arrangements provided by the issuer
  - Use company aircraft for personal travel that is required by the issuer to enable executive to be called back to work more easily

## What is a Perk? (cont.)

- If the answer to Step # 1 is Yes, the item is not a perk. Otherwise, move to Step #2
- **Step #2:** Does the item confer a direct or indirect benefit that has a personal aspect, regardless of whether a business purpose exists or if the item was provided for the convenience of the issuer, unless it is generally available on a non-discriminatory basis?
- How do you determine whether a benefit is provided on a non-discriminatory basis?
  - Non-Discriminatory
    - An item is generally available to all employees on a non-discriminatory basis if it is available to those employees to whom it lawfully may be provided (e.g., available to all domestic employees or employees with “accredited investor” status)
  - Discriminatory
    - Available only to employees in the same job category or at the same pay scale

## Examples of Perks

- Car Allowance
- Car Insurance
- Club Dues
- Club Initiation Fee
- Commission for Sale of Home
- Commuting Expenses
- Computer Equipment
- Corporate Residence
- Costs Associated with Expatriate Work Assignment
- Currency Exchange Arrangements
- Discounts on Company's Products/Services Not Generally Available to All Employees
- Excess Liability Insurance
- Executive Office Benefits
- Financial Consulting/Planning Services
- Gas Allowance
- Goods and Services Differential (For Foreign Service)
- Home Office Costs
- Home Security
- Housing Allowance
- Legal Expenses
- Life Insurance Premiums
- Living Expenses
- Long Term Disability Insurance
- Medical and Dental Claims/Premiums
- Parking Fees
- Payments for Staying in Personal Residence while on Business Travel
- Personal Liability Insurance
- Personal Travel on Corporate Aircraft
- Personal Use of Company-Provided Administrative Support
- Physical Exam/Voluntary Health Screening
- Relocation Allowance
- School Tuition
- Secured Parking
- Security Concerning Fraudulent Data Access
- Spouse/Family Member Tag-Along on Business Travel
- Spouse Attendance at Company Events
- Stipend for Effective Company Representation in the Community
- Supplemental Accidental Death and Dismemberment Insurance
- Tax Equalization Payments
- Tax Gross-Ups
- Tax Return Preparation
- Telephone Services
- Trips Awarded to Top Sales Performers
- Use of Company Products and Services
- Use of Corporate Travel Agency for Personal Travel
- Use of Executive Dining Room
- Wellness Reimbursement (For Fitness Related Activities)
- Wireless Network for Computer Use

## Proxy Disclosure Rules – SCT (General Rule)

- Perks are reported in the “All Other Compensation” column of the SCT
  - No disclosure is required if the aggregate value of all perks provided to a named executive officer is less than \$10,000
  - If the aggregate value of perks provided to a named executive officer is greater than \$10,000:
    - The value of all perks must be disclosed in the table;
    - Each type of perk must be identified by type in a footnote (general categories such as travel and entertainment are not sufficient);
    - The value of any perk that exceeds the greater of \$25,000 or 10% of the aggregate value of all of the perks must be quantified and disclosed in a footnote;
    - Value of a perk is determined on the basis of the incremental cost of the perk;
    - If footnote quantification is required, the methodology to compute the aggregate incremental cost should be included in a footnote; and
    - The requirement for identification and quantification applies only to the last fiscal year
  
- Companies may include a separate table for all items under “All Other Compensation” or specifically for perks to more clearly present the required disclosures

## Proxy Disclosure Rules – SCT (Specific Cases)

- **Gross-Ups:** All “gross-ups” are separately required to be disclosed under the “All Other Compensation” column
  - For tax gross-ups in particular, even if the associated perk is eligible for exclusion (or would not require identification or quantification), the amount of any related tax gross-up must be included
  - Subject to distinct rules relating to the requirement to identify and quantify
  - The tax gross-up payment should be included in the same year as the related perk regardless of when paid
  
- **Reimbursements:** If the executive officer fully reimburses the issuer for the item’s total cost, it should not be considered a perk for proxy disclosure purposes
  
- **No Incremental Cost Perks:** If the threshold for perk disclosure is met, then even perks with no aggregate incremental cost to the issuer should be separately identified by type, even though no value relating to such perk is reported in the “All Other Compensation” column

## Proxy Disclosure Rules – SCT (Specific Cases) (cont.)

- **Perk allowance:** Companies may not avoid disclosure of perks by using an allowance approach as opposed to incurring the costs directly. Companies should identify generally the perks towards which the allowance can be spent, reference the specific items for which the named executive officers have used the allowance in the prior year and disclose whether the committee has any discretion in providing additional monies above the allowance in any given year
- **Director's perks:** Perks for directors are reportable under the "All Other Compensation" column in the Director Compensation Table, subject generally to the same rules as govern disclosure in the SCT

## Valuation (General)

- An issuer must value perks on the basis of the aggregate incremental cost to the issuer
  - This value may differ from the value the issuer uses for tax purposes
  - The SEC Staff takes the view that how an issuer computes the aggregate incremental cost depends on the particular facts and circumstances
  - Investors should be provided with the material information they need in order to understand the valuation, its context, and the particular facts and circumstances of those perks
- Companies will need to develop a methodology in order to value perks, which can be difficult and require judgments about the allocation of costs between the issuer and the executive
- An issuer's incremental cost may include foregone corporate tax deductions
  - Internal Revenue Code Section 274(e) limits the deductibility of expenses associated with any "entertainment" expense, including the personal use of corporate aircraft by an issuer's executives and directors who are subject to Section 16 of the Exchange Act to the amount recognized as income by the executive or director using the aircraft
- The methodology should be reasonable, since it may have to be explained in the proxy statement in plain English



## CE Credit Verification Code

As a result of the firm's recent merger to become Hunton Andrews Kurth, we are now offering additional types of credit for our webinar programs. Our Continuing Education policies have changed slightly to align with the rules for these new types of credit. Please write the code down on the Verification Form which was provided in the invitation and reminder e-mail for this program. If you do not have this form, please capture the code any way you can, and we will provide another copy of the form in a follow-up e-mail.

**CODE:  
HAK7458**

Please return the completed Verification Form to Kelli Lilienstern  
[Kellililienstern@HuntonAK.com](mailto:Kellililienstern@HuntonAK.com)

## Valuation (Private Aircraft Usage)

- The issuer cannot compute the aggregate incremental cost of personal use of company aircraft by using the amount it attributes to an executive for federal income tax purposes (e.g., under the Standard Industry Fare Level, or SIFL, rules) or the cost of first-class airfare
- Note that reimbursements for personal aircraft travel need to be vetted for compliance under FAA regulations, which can limit such reimbursement in certain circumstances
- Typically, companies exclude the fixed costs associated with owning and operating the aircraft, but include variable costs such as fuel costs, catering, crew expenses, landing and hangar fees
  - The SEC also has noted that incremental costs could be associated with repositioning or “deadhead” flights
- The two most typical approaches to valuing personal aircraft usage are:
  - Calculating the direct and indirect variable costs of the specific flight; and
  - Calculating the average cost per mile or per hour to operate the aircraft during the year and then assign a value to the personal use based on the number of hours or miles flown

## Valuation (Private Aircraft Usage - Examples)

- Example of Method #1 (NYSE Market Cap of 40+ Billion Company)
  - “We generally measure incremental cost by the additional variable costs attributable to personal use, and we disregard fixed costs that do not change based on usage. Incremental cost for personal use of company-owned aircraft was determined by including fuel cost, landing fees, on-board catering and variable maintenance costs attributable to personal flights and related unoccupied positioning, or ‘deadhead,’ flights.”
  
- Example of Method #2 (NYSE Market Cap of 25+ Billion Company)
  - “To calculate this cost, the Company determines the total variable annual operating cost for each aircraft, such as fuel, trip-related maintenance, landing and parking fees, crew expenses, supplies and catering. The total variable operating cost is then averaged for all flight hours flown and multiplied by the total number of personal flight hours for each NEO. Fixed annual costs that do not change based on usage, such as pilots’ salaries, home hangar expenses, general taxes, routine maintenance and insurance, are excluded from the incremental cost calculation. If an aircraft flies empty before picking up or after dropping off a passenger flying for personal reasons, and the empty flight is not related to any other business-related travel, this ‘deadhead’ segment is included in the incremental cost calculation for determining personal use.”

## Proxy Disclosure Rules – CD&A

- Overall policy on the use of perks should be addressed in the Compensation Discussion and Analysis (“CD&A”)
- While it is unlikely that the value of any perks provided to an issuer’s named executive officers will comprise a material portion of their executive compensation package, the issuer’s approach to perks is an important subject for shareholders
- How to address perks in the CD&A:
  - Address where perks fit into the overall executive compensation objectives and how they affect decisions regarding other elements
  - State whether perks represent a material component of the issuer’s executive compensation
  - To the extent that the issuer provides some level of perks, it is important to identify the category of benefits provided, explain why they are provided (e.g., efficiency or security), and describe any limitations or conditions that the issuer applies to this compensation component

## Additional Disclosure Obligations

- Perk policies that are guidelines likely do not trigger filing under Item 5.02(e) of Form 8-K. However, perk policies that mandate certain benefits may be of the type of “plan, contract or arrangement” that is reportable under Item 5.02(e), if material
- The SEC Staff has stated that a written arrangement whereby officers are provided company cars and other perks would not be considered a compensatory contract for the purpose of the exhibit filing requirements of Item 601(b)(10)(iii), provided that the perk is separately identified in the proxy statement

## SEC Enforcement

- The SEC has periodically initiated enforcement actions relating to perk disclosure
- Over the past several years, there have been monetary settlements with the SEC relating to perk disclosure ranging from \$0 to \$1.75 million
- Where disclosure failures are due to failures of corporate controls, the SEC will require the appointment of an independent consultant to review and oversee the implementation of stricter corporate policies and procedures

## SEC Enforcement (Case Study)

- July 2018: An issuer settled an allegation by the SEC that the issuer failed to properly disclose approximately \$3mm of perks over a 4-year period
  - As background, the issuer applied the wrong standard in its determination of whether an item is a perk (*i.e.*, it appeared to have applied a business purpose standard to the job of the individual, which is an incorrect standard)
  - The perks in question consisted of:
    - Personal use of company aircraft,
    - Sporting events,
    - Club memberships,
    - Use of a personal assistant's time, and
    - Board membership fees to a charitable organization
  - According to the SEC, the issuer failed to:
    - Have adequate processes and procedures in place so as to ensure proper reporting
    - Adequately train employees responsible for drafting the CD&A
  - As a result, the issuer entered into a settlement offer with the SEC that:
    - Fined the issuer \$1.75mm (a high amount relative to the value of \$3mm in perks)
    - Ordered the issuer to retain an independent consultant for a 1-year period in order to assess the issuer's policies and procedures for complying with SEC compensatory securities laws (and the issuer must implement any recommended changes)
    - Ordered the issuer to be subject to compliance monitoring for 2 years

## Practical Thoughts

- To ensure current and on-going compliance, issuers should assess whether sufficient control measures exist
  - Individuals responsible for preparing executive compensation disclosure should be
    - Familiar with the SEC's perk disclosure standards, and
    - Empowered to find the information within the issuer to provide accurate disclosure
  - Develop steps to identify perks and procedures for tracking personal usage
  - Review reimbursement policies and procedures with the SEC's disclosure standard in mind
  - Provide additional training on identifying perks, calculating the aggregate incremental cost of such perks, tracking perks and disclosing the same
    - Plug coming . . . wait for it . . . wait for it . . . our Firm can provide such training onsite or remotely via webinar
  
- Review D&O questionnaires
  - Regularly update questionnaire to elicit information about possible perks
  - Include expansive perk-orientated questions
  - Provide examples of what might constitute a perk
  - Leave time for reviewers to analyze the responses and prepare the appropriate disclosures



## Practical Thoughts (cont.)

---

- Consider whether the following procedures should be implemented:
  - Compensation Committee prior to any perks being provided to executive officers or, alternatively, approval of a perk policy
  - Pre-clearance procedure before an officer or director is reimbursed for certain items that arguably could be a perk

## Don't Forget Next Month's Webinar

---

- Title:
  - Preparing for Proxy Season: Start Now (Annual Program)
  
- When:
  - 10:00 am to 11:00 am Central
  - September 12, 2019