

SEC Issues Revised Rules Regarding Stock Based Compensation

In an unexpected move, on December 22, 2006, the Securities and Exchange Commission (the "Commission") released updated rules regarding stock awards and option awards in order to provide disclosure of the compensation cost recognized by the registrant over the requisite service period under Financial Accounting Standards Board Statement of Financial Accounting Standards No 123 (revised 2004) Shares-Based Payment (FAS 123R). These rules are currently in effect. The Commission believes that this revised disclosure will provide a full and more useful picture of executive compensation and will provide investors with a clearer view of the annual compensation earned by named executive officers ("NEOs") and the annual compensation costs to registrants, consistent with the registrants' financial statement reporting. As described below, the revised disclosure amends the Summary Compensation Table, the Grants of Plan-Based Awards Table and the Director Compensation Table.

Summary Compensation Table


The Stock Awards and Option Awards columns of the Summary Compensation Table will reflect the compensation cost recognized for the requisite period under FAS 123R and will include the compensation cost recognized in the financial statements with respect to awards granted in the subject fiscal year and the previous fiscal years. All assumptions made in the valuation shall be discussed in the financial statements, the footnotes to the financial statements or Management's Discussion and Analysis and a footnote in the Summary Compensation Table should make reference to such discussion. In addition, footnote disclosure is required for awards that are forfeited in the year.

Awards that are classified as equity awards under FAS 123R have a set compensation cost on a year-to-year basis; whereas, liability awards under FAS 123R are measured at fair value on the grant date and re-measured at each financial statement reporting date until the date the awards are settled under FAS 123R. These re-measurements of liability awards will be reflected in the Summary Compensation Table for each re-measurement year. Since FAS 123R did not become effective until 2006, the Commission is requiring registrants to utilize the FAS 123R modified prospective transition method for this disclosure even if the registrants have not adopted that method for financial statement reporting purposes. The modified prospective transition method affects the treatment of equity awards and liability awards that were made prior to 2006.

In a variation from FAS 123R, with regard to the service-based vesting of awards, the compensation cost recognized will not include an estimate of forfeitures related to service-based vesting conditions and will reflect the assumption that the NEO will perform the requisite service to vest in the award. If an NEO forfeits the award in the future, the amount of previously reported compensation cost will be deducted in the period in which the award is forfeited. This could lead to a negative number in the Stock Awards or Option Awards column during the year of forfeiture. With regard to performance-based vesting conditions, the compensation cost will be disclosed in the Summary Compensation Table only if it is probable that the performance condition will be achieved. If the performance condition is not probable of being achieved on the grant date, but becomes probable in the future, the portion of the compensation cost based on service previously rendered will be disclosed during the period in which the achievement of the performance condition becomes probable. Alternatively, if a performance condition was previously considered probable and later is no longer considered probable, the compensation cost previously disclosed will be subtracted in the period in which it is determined that achievement of the performance condition is no longer probable. Once again, this could lead to a negative number in the Stock Awards or Option Awards column in the year in which it is determined that the achievement of the performance condition is no longer considered probable.

One exception is that awards granted to a retirement eligible NEO who is entitled to retain the award at retirement is not considered to have a substantive service requirement, and the full grant date fair value is to be recognized during the year of grant.

Any salary or bonus that is foregone at the election of an NEO in favor of receiving non-cash compensation shall be included in the Salary or Bonus column, as applicable, and not in the Stock Awards or Option Awards column. There will be footnote disclosure referencing the Grants of Plan-Based Awards Table where the non-cash compensation is reported.



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Grants of Plan-Based Awards Table

A new column has been added to the Grants of Plan-Based Awards Table to reflect, on a grant-by-grant basis, the grant date fair value information under FAS 123R that is no longer required in the Summary Compensation Table. In addition, for repriced or materially modified options, stock appreciation rights and similar option-like instruments, the Grants of Plan-Based Awards Table will include, on a grant-by-grant basis, the incremental fair value computed as of the repricing or modification date in accordance with FAS 123R.

Director Compensation Table

In order to be consistent with the Summary Compensation Table, the Director Compensation Table has been revised in the same manner as the Summary Compensation Table described above. However, since there is not a Grants of Plan-Based Awards Table for directors as there is for NEOs, the information set forth above under the Grants of Plan-Based Awards Table, on a grant-by-grant basis, shall be disclosed in a footnote to the Director Compensation Table in accordance with FAS 123R.

Recommended Actions

Although the Commission believes that the amendments to the Summary Compensation Table may reduce potential fluctuations in total compensation resulting from year-to-year differences in equity awards and provide more consistency in the classification of NEOs, registrants should review the list of executive officers that they thought would be NEOs for the 2006 since these new rules may have caused the actual NEOs, other than the principal executive officer or the principal financial officer, to be different than originally thought.

If you should have any questions regarding these proposed rules, please contact any of the following members of the Public Companies Practice Group.



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