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Navigating the Executive Benefits Landscape
with The Todd Organization

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Proxies and Executive Benefits Discussions

With proxy season approaching, public companies face renewed scrutiny on their executive compensation practices. Against this backdrop, it is important that companies describe their practices in the best light possible to show how they are both aligned with shareholder interests and creating greater shareholder value.

Shareholder-Friendly Executive Benefits

One area where companies can better explain executive compensation and show how it is in the interests of shareholders pertains to their non-qualified benefit plans. A more accurate description is beneficial to both the covered executives and shareholders.

Proxy statements seldom make clear that executives can lose these benefits. Yet, by definition, non-qualified benefit plans must be subject to a substantial risk of forfeiture. In the event of bankruptcy, this means the executives become general, unsecured creditors for the full amount of the promised benefits. Because of this risk, which continues while the executives are being paid in retirement, non-qualified plans help ensure that executives will run companies responsibly, for the long term, avoiding reckless risks.

Proxy Language on the Plans

The following language is typical of how many companies describe one of their executive benefit plans in the proxy:

“Executive officers, including the Named Executives, are eligible for contributions to a Supplemental Executive Retirement Plan (“SERP”). The Committee annually approves contributions to each executive’s individual account with a designated contribution percentage of their total compensation. Benefits under the SERP are subject to a five-year vesting requirement.”

What typically follows is then a description of the plan, i.e., the formula for calculating the SERP benefit, the payout alternatives, and vesting provisions.

However, the risk factor is largely, if not completely, ignored.

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One way to address this oversight is by adding language similar to the following.

"The SERP is an 'unfunded' plan. It is considered a general contractual obligation of the Company and is subject to the claims of the Company's creditors. In the event that the Company becomes insolvent, the participants will be unsecured general creditors of the Company. This status with respect to these benefits aligns the interests of the participants with the long-term interests of the Company and its shareholders."

When companies fail to fully and accurately describe their executive benefits practices in proxies, they do a disservice to executives, leaving them subject to unfair criticism, while also providing incomplete information to shareholders. Furthermore, SERPS (and other non-qualified benefit plans) are often the largest executive benefits that companies will provide and often account for more than 50 percent of an executive's retirement income, a point that companies may wish to consider noting in the proxy as well.

Other Important Considerations

Depending on a company's situation, it may wish to communicate other information about its executive benefits plans, whether in the proxy or other forums. Non-qualified benefit plans can be structured so that they have minimal, if any, impact on shareholders. A number, in fact, directly contribute to earnings and shareholder value based on stable, long-term financing methods that can be employed.

Non-qualified benefits are also not restricted to the top executives at companies whose compensation must be dissected in proxies. Non-qualified plans can play an important role in the retirement planning of many executives currently earning over $150,000 annually who face significant restrictions on what they can contribute to and receive from qualified plans, such as 401(k) plans. As such, it is hard to contend that non-qualified plans are an unfair perk, as they restore retirement planning parity with other employees.

With many well-managed, responsible companies facing the heat and scrutiny over executive compensation, it can be quite a relief to be able to cite how executive benefits are one of the most responsible programs companies can have – for both executives and shareholders.

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