

## Disclosing Personal Security Arrangements

In recent years, the confluence of a growing global economy and turbulent geopolitical events has led many companies to provide extensive security arrangements for their executives. And while most organizations firmly believe that these arrangements serve a legitimate corporate purpose – ensuring the safety of their key decision-makers and their families, the SEC considers these expenditures to confer a “personal benefit” to the covered executives and, therefore, to be reportable as a “perquisite.” As a result, these amounts must be disclosed in corporate proxy statements.

While, generally, the use of perquisites and other personal benefits has declined dramatically over the past decade, we continue to see the disclosure of personal security arrangements, particularly once a company has reached a certain size and prominence thereby raising the profile of – and risks to – its Chief Executive Officer and other executives.

Although the costs of providing perquisites and other personal benefits to a company’s executives is relatively small when compared to the value of their overall compensation packages, investors remain interested in a company’s “perk” practices; typically closely scrutinizing its disclosure of this subject. Given this interest and the likelihood that personal security arrangements, if provided, may be one of the most costly items to be disclosed, companies should draft the required disclosure carefully.

### Disclosure Requirements

Under the rules of the Securities and Exchange Commission, a company must disclose in the “All Other Compensation” column of its Summary Compensation Table, among other things, any perquisites or other personal benefits received by its named executive officers for the covered fiscal year (unless the aggregate amount of such compensation is less than \$10,000). In the case of personal security arrangements, if the total value of all perquisites and other personal benefits is \$10,000 or more, this disclosure will consist of (i) the identity of any named executive officer for whom personal security arrangements were provided, (ii) the nature of such arrangements, (iii)

the aggregate incremental cost to the company of such arrangements (if the value exceeds the greater of \$25,000 or 10% of the total amount of perquisites and other personal benefits for that executive), and (iv) a description of the methodology used to compute the company’s aggregate incremental cost.

Unlike most other perquisites, many companies believe that the provision of personal security arrangements constitutes a reasonable business expense and not the receipt of a personal benefit. Frequently, before approving security-related expenditures, a Board of Directors will commission a “security study” to document the existence of a *bona fide* business-oriented security concern and as a predicate to the creation of a formal security program. (Typically, for federal income tax purposes, such a study is a prerequisite to the deductibility of expenses incurred for security services.) From the company’s perspective, this expense is integrally and directly related to the performance of its executives’ duties; necessary to ensure their safety, particularly where they frequently travel internationally or their celebrity makes them an inviting target for kidnapping or other personal injury.

Notwithstanding these beliefs, the SEC has expressly stated that it considers expenditures incurred to ensure the personal safety of a named executive officer to be a disclosable perquisite. Specifically, the Commission has held that business purpose or convenience does not affect the treatment of an item as a perquisite where it is not integrally and directly related to the performance by the executive of his or her job. Accordingly, a company’s decision to provide an item of personal benefit for security purposes does not affect its characterization as a perquisite. For example, a company policy that for security purposes an executive (or an executive and his or her family) must use company aircraft or other company means of travel for personal travel, or must use company or company-provided property for vacations, does not affect the conclusion that the item provided is a perquisite or personal benefit.

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## Disclosing Personal Security Arrangements (continued)

In addition, companies should be aware that Institutional Shareholder Services, Inc. (“ISS”), the major proxy advisory firm, has singled out personal security arrangements for criticism. Specifically, on multiple occasions, as part of its qualitative evaluation of an executive compensation program, ISS has questioned the costs of such arrangements, deeming them “excessive” in the context of the limited number of companies that disclose providing security protection for their executives.

As reflected below, these tensions between a company’s belief that security arrangements have become a necessary and integral component for the performance of an executives’ job, the views of the major proxy advisory firms, and the SEC’s position is frequently addressed in the disclosure describing these arrangements.

### Model Disclosure

While any disclosure of the expenses incurred for the personal security arrangements of one or more named executive officers needs to be tailored to the specific facts and circumstances, the disclosure on the following page should serve as an effective starting point for disclosing these expenses attributable to a named executive officer. In addition, we recommend the disclosures in the definitive proxy statements of [Exxon Mobil Corporation](#) and [Facebook, Inc.](#) as comprehensive examples of how this information can be presented.

### Personal Security Disclosure by Technology and Life Sciences Companies

Generally, perquisites and other personal benefits tend to represent a nominal portion of the pay packages of most technology and life sciences company executives.

Compensia monitors the compensation practices of the most prominent technology companies headquartered in the San Francisco Bay Area (primarily in Silicon Valley). We call this group, which consists of the largest companies in the computer/hardware, internet/software, and semiconductor sectors (but excluding companies that conducted their initial public offering in the last completed fiscal year), the Bay Area Tech 120. In addition, we monitor the compensation practices of the most prominent companies in the life sciences sector (many of which are also headquar-

tered in the San Francisco Bay Area). We call this group the Life Sciences 80.

For 2015 (the most recent year for which data is available):

- Only nine of the companies in the Bay Area Tech 120 (7.5%) disclosed personal security arrangements for one or more of their named executive officers during the year. In five instances, these arrangements were limited to the company’s Chief Executive Officer. The aggregate incremental cost to the company of such arrangements varies significantly, ranging from approximately \$12,000 to approximately \$4,256,000, with a median cost of approximately \$360,000.

Not surprisingly, only the largest companies in the Bay Area Tech 120 appear to provide personal security arrangements for one or more of their executives. Each of the companies disclosing personal security arrangements had a market capitalization of at least \$12 billion (as of June 30, 2016) and five of these companies (Apple, Facebook, Google, Hewlett-Packard Enterprises, Intel, and Oracle) have market capitalizations in excess of \$150 billion.

- Only five of the companies in the Life Sciences 80 (6.25%) disclosed personal security arrangements for one or more of their named executive officers during the year. The aggregate incremental cost to the company of such arrangements ranged from approximately \$9,000 to approximately \$86,000, with a median cost of approximately \$14,000.

As noted, in contrast to their Bay Area Tech 120 counterparts, the disclosed personal security arrangements were much smaller in amount.

### Need Assistance?

Compensia has extensive experience in helping companies prepare the executive compensation disclosure in the proxy materials for their Annual Meeting of Shareholders, as well as analyze the potential impact on the various SEC disclosure requirements on their executive compensation programs. If you would like assistance in preparing your executive compensation disclosure, or if you have any questions on the subjects addressed in this Thoughtful Disclosure Alert, please contact Mark A. Borges. ■

## Disclosing Personal Security Arrangements (continued)

### Model Disclosure

The personal safety and security of our employees, including our executives, is of the utmost importance to us and our shareholders. [Based on the recommendation of an independent, third-party security study and our security policy, we require our [Chief Executive Officer/named executive officers] (as well as their spouses and dependent children when they accompany them) to use, as much as practicable, company-provided transportation for all business and personal travel. We require these security measures for the company's benefit because of the importance of these executives to our company, and we believe that the costs of our overall security program are appropriate and necessary.

These services include the [initial procurement, installation, and] maintenance of security measures for our Chief Executive Officer's personal residence, personal security during business-related and personal travel, the use of private aircraft for business and personal travel, secure automobile transportation, and computer-related expenses. The Compensation Committee believes the amounts paid by the company for these services are reasonable, necessary, and for our company's benefit. [None of these security-related costs constitute taxable income for our [Chief Executive Officer/named executive officers]]

Although we view the security services provided for our [Chief Executive Officer/named executive officers] as a necessary and appropriate business expense, because they may be viewed as conveying a personal benefit to [him/her/them], we have reported the aggregate incremental costs to the Company of these services in the "All Other Compensation" column of the Summary Compensation Table.

The Compensation Committee reviews and approves the security budget and the specific security concerns justifying the security services for our Chief Executive Officer/named executive officers] [each year/periodically].

## About Compensia

Compensia, Inc. is a management consulting firm that provides executive compensation advisory services to Compensation Committees and senior management.

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