Debevoise & Plimpton

Debevoise In Depth

2025 Executive Compensation Reminders for Public Companies

December 20, 2024

As the 2025 executive compensation season approaches, public companies face a swiftly evolving regulatory and market landscape. Heightened scrutiny of perquisites ("perks") and ESG metrics, shifting noncompete laws, and enhanced disclosure obligations for option awards mean compensation committees, in-house counsel and HR professionals must anticipate and respond to emerging challenges. Below are nine key issues and reminders to guide compensation planning and disclosure for 2025.

1. Understand Securities Disclosure and Tax Implications of Executive and Director Perks

As companies consider new or enhanced perquisites for CEOs, other named executive officers and directors—including executive security arrangements following the tragic death of the UnitedHealthcare CEO—they should remain mindful of both SEC disclosure and tax implications.

From a securities standpoint, the SEC views **executive security arrangements** as disclosable perks, even if the company considers them necessary business expenses. Under Item 402 of Regulation S-K, the aggregate incremental cost to the company of providing the perk or personal benefit must be reported in the "All Other Compensation" column of the Summary Compensation table.

On the tax side, however, the treatment differs. If an executive security arrangement meets the conditions for a "working condition fringe" under IRS regulations, company-provided security may not be taxable to the employee and may remain deductible by the company. To qualify for this exclusion, the company must demonstrate a "bona fide business-oriented security concern" in one of two ways: (1) the expenditures are part of an "overall security program" that provides 24-hour protection, including a trained bodyguard proficient in evasive driving, a specially equipped vehicle and other specified safety measures; or (2) an independent security consultant conducts a study concluding that a full "overall security program" is not necessary and provides alternative security recommendations, which the employer then consistently applies.

Personal use of corporate-owned and charter aircraft by executives and directors remains under scrutiny by both the SEC and the IRS. The SEC has brought multiple enforcement proceedings for failure to disclose perquisites properly, including personal use of corporate aircraft—most recently this week. Simply having a company policy requiring executives to use corporate aircraft for personal travel (e.g., for security reasons) does not take the personal use out of the perk category. In addition, early this year, the IRS announced that it will begin conducting dozens of audits on corporate aircraft usage by large corporations and high-income taxpayers to ensure that any personal use of company aircraft by executives, officers, employees and shareholders is properly allocated and reported for tax deduction purposes.

In-house legal and HR teams should carefully review all potential perks and benefits to ensure compliance with SEC disclosure requirements and tax rules. All executive and director perks should be appropriately disclosed in proxy statements. Companies may wish to strengthen internal controls, including establishing clear policies and procedures for approving, tracking and valuing perks to mitigate compliance risks and avoid costly enforcement actions. Special attention should be given to personal use of corporate aircraft by executives and directors, given the heightened scrutiny from both regulators and investors.

2. Revisit ESG (Including DEI) Goals in Incentive Plans

Many public companies have incorporated environmental, social and governance ("ESG") measures into their short- and long-term incentive plans, including metrics related to climate impact, broader environmental stewardship and diversity, equity and inclusion ("DEI") goals. In our 2024 Proxy Roundup, we analyzed the use of ESG metrics in cash and equity incentive plans among the 100 largest public companies and found that 71% of these companies included one or more ESG metrics in incentive compensation plans. Reporting a similar trend among the S&P 500, a recent Conference Board, ESGAUGE and FW Cook report (the "Conference Board Report") found that 77.2% of these companies incorporated ESG measures into their incentive compensation plans, according to 2024 proxy statement disclosures.

Yet, despite the increased adoption of ESG-related goals in incentive plans, institutional investors and proxy advisory firms remain concerned about the rigor and transparency of these metrics. Some institutional investors have criticized "fluffy" ESG measures perceived as inflating bonus payouts to executives without improving company performance. In parallel, proxy advisory firms desire more transparency around proxy statement disclosure of ESG measures, including the rationale for selecting ESG metrics, the target-setting process, and associated payout opportunities.

This renewed scrutiny unfolds against a backdrop of intensifying political debate. In the United States, anti-ESG sentiment has gained traction in certain states and legislative circles, and the incoming Trump administration is expected to further fuel this backlash. Compensation committees must now navigate a charged environment where some stakeholders push for robust ESG integration while others challenge the very premise of these initiatives.

The use of DEI measures in particular has come under the microscope in light of the Supreme Court's 2023 decision in *Students for Fair Admissions v. Harvard and UNC* invalidating race-conscious admissions practices in higher education. Following this decision, scrutiny of workplace DEI initiatives has intensified, accompanied by an uptick in related litigation. While our study of ESG metrics in incentive plans shows that 51% of the largest 100 public companies included a DEI metric, and the Conference Board Report found that 67% of S&P 500 companies disclosed DEI measures in 2024 proxy filings (down from 75% in 2023), these figures may shift significantly in 2025 and beyond. Because proxy statements filed in 2024 generally reflect 2023 plans, the full impact of heightened legal and political scrutiny on future DEI metrics is likely yet to be realized.

In the ongoing 2025 compensation season, we have already observed some companies reconsidering their DEI-related goals. Some are recalibrating the structure or disclosure of existing measures, especially where quantitative representation metrics could attract legal challenges. Others are removing these measures altogether. However, wholesale abandonment of DEI goals remains unlikely; many companies believe inclusive talent strategies underpin sustainable performance and long-term value.

In light of all these factors, public companies should continue to take a close look at the use of ESG measures in incentive plans during the 2025 compensation season. Companies should ensure that ESG goals included in incentive plans have a strong tie to long-term business strategy and company value and are sufficiently challenging, and consult with legal counsel to assess any attendant legal risks.

3. Enhance Disclosure for Non-GAAP Adjustments that Increase Payouts

Non-GAAP metrics are common in incentive pay programs, and proxy advisory firms and institutional investors are increasingly focused on understanding how adjustments made to these non-GAAP measures affect incentive payouts. Item 402 of Regulation S-K already requires disclosure of how incentive target levels that are non-GAAP financial measures are calculated from the issuer's audited financial statements, but disclosure practices in this area remain inconsistent.

Both Institutional Shareholder Services ("ISS") and Glass Lewis consider line-item reconciliations of non-GAAP incentive plan measures to GAAP results as a best practice. Where adjustments to non-GAAP measures *materially* increase incentive payouts, ISS and Glass Lewis expect the proxy statement to include enhanced disclosures explaining the nature of the adjustment and its impact on payouts, whether expressed as a dollar amount or percentage. ISS also expects disclosure regarding the board's rationale for the adjustment.

Insufficient disclosure of significant non-GAAP adjustments that materially increase incentive payouts can adversely affect ISS and Glass Lewis's say-on-pay recommendations. ISS considers clear disclosure of adjustments made to financial results for incentive plan purposes in its qualitative pay-for-performance-analysis, and made clear in its 2025 Executive Compensation Policies FAQs that it will also consider poor disclosure of the rationale for metric adjustments in performance-based equity programs in this analysis beginning with the 2025 proxy season (see #8 below for more information). The Glass Lewis benchmark policy guidelines also provide that, in situations where significant adjustments were applied to non-GAAP measures that materially impact incentive pay outcomes, the lack of disclosure about these adjustments may be a factor in Glass Lewis's say-on-pay recommendation.

Clear, detailed explanations of how and why adjustments were made can help foster investor confidence and mitigate the potential for adverse voting recommendations from ISS, Glass Lewis and institutional investors.

4. Comply with New Disclosure Requirements for Timing of Option Awards

Beginning with the 2025 proxy season, calendar year-end public companies must comply with new disclosure requirements relating to stock option awards and stock appreciation right ("SAR") awards granted close in time to a company's release of material non-public information ("MNPI") under Item 402(x) of Regulation S-K:

- Companies must provide **tabular disclosure** of any stock option or SAR granted to any named executive officer within a period starting four business days before, and ending one business day after, the filing or furnishing of a Form 10-Q, 10-K or 8-K that discloses MNPI (including earnings information but excluding a Form 8-K disclosing only a material new option award grant under Item 5.02(e) of that form). The tabular disclosure must include for each option or SAR (1) the award's grant date, (2) the number of securities underlying the award, (3) the per-share exercise price, (4) the grant date fair value of each award and (5) the percentage change in the market price of the underlying securities between the closing market price of the security one trading day prior to and one trading day following the disclosure of MNPI.

- Companies must also provide **narrative disclosure** describing their policies and practices on the timing of option and SAR grants in relation to the release of MNPI. This includes (1) how the board decides when to grant such awards (for example, whether such awards are granted on a predetermined schedule), (2) whether the board takes MNPI into account when determining the timing and terms of such awards and (3) whether the company has timed the disclosure of MNPI for the purpose of affecting the value of executive compensation. This disclosure is required regardless of whether grants of stock options or SARs are made close in time to the release of MNPI. This disclosure is not required for awards of restricted stock or restricted stock units.

Because Item 402(b)(2) already lists, as an example of the material information to be disclosed in the Compensation Discussion & Analysis ("CD&A") section of the proxy statement, how the determination is made as to when awards are granted, including awards of equity-based compensation such as options, proxy statements may currently include disclosure related to the timing of option and SAR awards. However, companies should assess whether any such CD&A disclosure (1) is fully responsive to the new Item 402(x) requirements and (2) reflects any changes that are made to stock option and SAR grant policies and procedures in light of these requirements. Companies that have not already done so should also consider adopting a policy governing the timing of equity grants in relation to MNPI.

Public companies should also keep in mind that, if non-routine, off-cycle equity awards are entered into in contemplation of or shortly before the planned release of MNPI, the principles outlined in Staff Accounting Bulletin No. 120 may require additional analysis and disclosure as part of an issuer's preparation and filing of financial statements.

5. Prepare for the Third Year of Pay-Versus-Performance Disclosures

As companies enter the third year of mandatory pay-versus-performance disclosures under Item 402(v), the learning curve should be lower. However, issuers should confirm their calculations of compensation actually paid and other disclosures comply with all current SEC guidance, including the three rounds of Compliance & Disclosure Interpretations published since Item 402(v) was finalized and recent public comments and comment letters issued by the Staff of the Division of Corporation Finance.

At the 56th Annual Institute on Securities Regulation conference held in November 2024, the Staff of the Division of Corporation Finance highlighted the following "practice tips," consistent with comment letters issued by the Staff during 2024:

- In disclosing the relationships between executive compensation actually paid to the CEO and the other named executive officers and the required company performance metrics, companies should explain each relationship in detail, as opposed to simply stating the numbers. The pay-versus-performance rules require a clear description (graphically, narratively or a combination of the two) of each relationship.

- Companies should disclose GAAP net income as reported in the audited income statement, which includes net income attributable to non-controlling interests.

- If the company-selected measure is a non-GAAP measure, companies should disclose how such measure is calculated from the audited financial statements, as required by the rule. A reconciliation of the non-GAAP measure in compliance with Regulation G and Item 10(e) of Regulation S-K is not required.

In general, comment letters issued during 2024 generally show that the Staff is conducting a close review of the pay-versus-performance disclosures, including probing calculations of compensation actually paid. Companies should ensure accuracy of the numbers reported in the pay-versus-performance table and compliance of the accompanying footnotes and relationship disclosures.

For a detailed discussion on the final pay-versus-performance disclosure rules, please refer to our Debevoise In Depth—Final Pay-Versus-Performance Disclosure Rules: Compliance Q&As. Our Debevoise Updates from February 2023, September 2023 and November 2023 describe the Compliance & Disclosure Interpretations published by the SEC since Item 402(v) was finalized.

6. Assess Next Steps on Dodd-Frank Clawback Policies and Recovery Analyses

Since the required adoption of Dodd-Frank clawback policies last year, some listed companies have had to prepare accounting restatements. In the event of an accounting restatement, companies are required to check one or both new clawback-related checkboxes on the cover pages of Forms 10-K, 20-F and 40-F: the first, whether the financial statements included in the filing reflect correction of an error to previously issued financial statements, and, the second, whether any of those error corrections are restatements that require a recovery analysis of incentive-based compensation received.

If both boxes are checked:

- If the company concluded that recovery of erroneously awarded compensation was not required pursuant to the company's Dodd-Frank clawback policy, the company must briefly explain why application of the policy resulted in this conclusion. Comment letters issued by the Staff of the Division of Corporate Finance, such as this one, confirm that if a company checks the second box on the 10-K cover page, the Staff expects to see disclosure about the recovery analysis consistent with this rule.

- If recovery under the Dodd-Frank clawback policy was required, the company must disclose detailed information under Item 402(w) of Regulation S-K regarding the date of the accounting restatement, the aggregate dollar amount of erroneously awarded compensation attributable to the restatement (and analysis of how the amount was calculated), the aggregate dollar amount outstanding at year-end and any amounts due that have been outstanding for 180 days or longer). If recovery is deemed impracticable, the company must disclose the amount of recovery forgone and explain the reasons.

More detail about Dodd-Frank clawback policies, including disclosure obligations under Item 402(w) is available in our prior Debevoise In Depth, SEC Adopts Final Clawback Rules.

7. Consider Expanding Clawback Policies Beyond Dodd-Frank Minimums

In October 2024, ISS issued an off-cycle update to its FAQs on executive compensation policies clarifying that, for purposes of ISS's say-on-pay vote recommendation, clawback policies must explicitly cover all time-vesting equity awards to receive credit for a "robust" clawback policy. A clawback policy that meets only the minimum Dodd-Frank requirements will not be considered robust for ISS purposes since the exchanges' listing rules issued under the SEC's Rule 10D-1 do not cover exclusively time-vesting equity awards. This was consistent with ISS's view expressed in the context of its Equity Plan Scorecard policy. However, the new FAQ highlighted a critical issue for public companies, boards and compensation committees as they prepare for the 2025 compensation season: Is it time to adopt or amend a discretionary clawback policy?

Many companies have considered adopting a recoupment policy that goes beyond the Dodd-Frank requirements, either as a separate policy or combined with the Dodd-Frank clawback policy (including by integrating the Dodd-Frank requirements into an existing recoupment policy). These broader policies often (a) cover additional triggers, such as fraud or misconduct, (b) feature a longer or shorter lookback period, (c) expand the class of covered individuals (and subject only those at fault to the policy), (d) expand the types of incentive compensation subject to recovery to include time-based awards, awards with strategic or operational metrics and/or discretionary amounts and (e) provide greater committee discretion in determining whether to pursue recovery under the policy and the amounts subject to recovery.

For a discussion of the market prevalence, proxy advisory firm views, benefits, enforcement challenges and other considerations related to discretionary clawback policies, please refer to our recent Debevoise In Depth, Rethinking Clawback Policies for the 2025 Compensation Season.

8. Stay Current on ISS and Glass Lewis Policy Changes

2024 was a good year for public companies in terms of say-on-pay vote outcomes with the lowest say-on-pay failure rate on record. Shareholder support for say-on-pay votes on average increased after recent decreases. That being said, public companies should be aware of proxy advisor and institutional shareholder views on executive compensation programs. Within the last several weeks, both ISS and Glass Lewis have updated their policies for the 2025 proxy season.

ISS posted updated 2025 FAQs on Executive Compensation Policies last week (following the earlier off-cycle update on clawback policies, described above under #7). Among other changes, ISS describes the factors it will consider in evaluating incentive program metrics, including whether the program emphasizes objective metrics that are linked to quantifiable goals (as opposed to highly subjective or discretionary metrics); the rationale for selecting metrics, including the linkage to company strategy and shareholder value; the rationale for atypical metrics or significant metric changes from the prior year; and, as discussed above under #3, the clarity of disclosure around adjustments for non-GAAP metrics and their impact on payouts.

Importantly, ISS also added a new FAQ describing changes to the pay-for-performance qualitative review relating to the evaluation of performance-vesting equity awards. Starting in the 2025 proxy season, ISS will more heavily scrutinize performance-vesting equity disclosure and design as part of its qualitative review, particularly in the context of a quantitative pay-for-performance misalignment. Typical considerations include: non-disclosure of forward-looking goals (with backward-looking disclosure at the end of the performance period carrying less mitigating weight than in prior years); poor disclosure of closing-cycle vesting results; poor disclosure of the rationale for metric changes, metric adjustments or program design; unusually large pay opportunities, including maximum vesting opportunities; non-rigorous goals that do not appear to strongly incentivize for outperformance; and overly complex performance equity structures. Multiple concerns from this list will be more likely to result in an adverse vote recommendation in the context of a quantitative pay-for-performance misalignment.

In addition, Glass Lewis published its 2025 U.S. Voting Policy Guidelines last month that apply to shareholder meetings held after January 1, 2025. Glass Lewis clarified that in evaluating executive compensation, Glass Lewis will take a holistic view and assess each executive compensation program on a case-by-case basis. Unfavorable factors will be assessed in relation to the pay program's entirety and will be evaluated for their rationale, structure and ability to align executive compensation with company performance. In addition, Glass Lewis updated its discussion of change-in-control provisions to provide that companies that allow for committee discretion over the treatment of unvested awards should commit to providing clear rationale for how such awards are treated in the event a change in control occurs.

Shareholder support for equity incentive plans improved in 2024, and the failure rate decreased from 2023's high. However, companies seeking approval of new equity incentive plans or additional shares under existing plans will still want to consider ISS and Glass Lewis equity compensation plan approaches. ISS also posted updated FAQ documents for equity compensation plans, noting that, for 2025, there are no new factors, and no changes to weightings of factors or passing scores for any of the ISS EPSC models. Glass Lewis also released a special report earlier this month on its approach to analyzing equity plan proposals under its Equity Compensation Model and equity plan proposal trends from the 2024 proxy season.

Companies should also be cognizant of the voting policies related to executive compensation programs and equity incentive plans of any large institutional shareholder.

9. Monitor Noncompete Developments and Reassess Restrictive Covenant Programs

The Federal Trade Commission ("FTC") noncompete ban, issued in April 2024, is likely headed for withdrawal by the newly constituted FTC before any definitive judicial ruling on its enforcement. Effectiveness of the FTC's noncompete ban has been held up by adverse rulings in federal courts in Texas and Florida and is currently on appeal. However, recent changes at the FTC suggest the rule will not survive. With President-elect Donald Trump's nomination of Andrew Ferguson, a current commissioner who joined the dissent to the noncompete rule, as FTC Chair and the anticipated Republican majority on the Commission, the FTC is expected to rescind the rule, rendering the ongoing legal challenges moot.

In the absence of a federal noncompete regime, regulatory attention at the state level is expected to intensify. Progressive states like California, Massachusetts, Minnesota and Washington have recently enacted stringent restrictions or outright bans, while others, such as New York, may soon follow suit, particularly for lower-wage employees. Against this backdrop, employers should remain vigilant and adapt to a legal landscape where state laws often dictate the permissibility and enforceability of noncompetes. Even where noncompetes remain permissible, a more cautious and targeted approach—focusing these agreements on employees with access to trade secrets, customer goodwill, or uniquely valuable skills—can bolster enforceability. Employers should consider reviewing and updating their form restrictive covenants, adjusting scope and duration, refining protections for confidential information and trade secrets, and incorporating state-specific modifications where needed. Ultimately, crafting narrowly tailored and strategically deployed noncompetes can help navigate the increasingly complex regulatory environment.

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As the executive compensation landscape continues to evolve, careful planning, sound governance structures, and proactive compliance measures will help companies meet regulatory, investor and market expectations. By taking these nine issues into account, public companies can position themselves for a smoother and more successful 2025 executive compensation season.

For more information about disclosure considerations for the 2025 annual reporting season, see our recent Debevoise In Depth, Key Considerations for the 2025 Proxy Season.

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Please do not hesitate to contact us with any questions.

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