Managing Disclosure on Personal Use of Corporate Aircraft

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Personal use of corporate aircraft remains a popular perquisite among many of the largest public companies. In addition to getting executives to important business destinations and enabling them to work proactively while traveling, many companies provide top executives the opportunity to use the corporate aircraft for non-business purposes, including travel to outside company board meetings, spousal travel to business events, and / or family vacation travel. The proxy-disclosed value of this perquisite varies widely, with some companies reporting amounts in excess of $200,000.

The value of this perquisite comprises a very small portion of CEOs' and other executives' total pay, typically no more than 1% to 2% annually. However, regardless of the size of the perquisite in comparison to the total pay package, the potentially adverse external optics of executives' personal use of corporate aircraft can be significant. For some, it's an example of an excessive perquisite provided to executives, thus making it an easy target for politicians and pundits. The current presidential election cycle has placed a renewed and harsh spotlight on CEO pay, creating additional scrutiny on all aspects of the compensation package. Therefore, the time may be ripe for corporate boards and compensation committees to reexamine their policies on personal use of corporate aircraft by CEOs and sometimes other executives.

To lessen adverse public scrutiny of executives' personal use of corporate aircraft, corporate boards and compensation committees could consider methods for reducing, or even eliminating, the required proxy-disclosed value of this perquisite. As described below, one effective method of accomplishing this goal, while continuing to allow CEOs access to the corporate aircraft, is through a "time sharing agreement."

Required Proxy Disclosures Covering Personal Use of Corporate Aircraft

The proxy rules require a public company to disclose in its Summary Compensation Table the aggregate incremental cost of an NEO's personal use of corporate aircraft, assuming the $10,000 disclosure threshold is met. However, the amount of compensation subject to disclosure may be reduced to the extent an NEO reimburses his or her employer for a personal flight's incremental costs through the use of a time sharing agreement (as explained below). Many CEOs have agreed with this course of action and have entered into this type of agreement.

If 100% of the incremental cost is reimbursed by the NEO, then no disclosure would be required. If less than 100% of the incremental cost is reimbursed, then a company would be obligated to disclose the non-reimbursed amount in the Summary Compensation Table with appropriate footnote disclosure, assuming again that the $10,000 disclosure threshold has been met. However, even reducing the amount that must be disclosed in the proxy can have a positive impact on how such perquisite is viewed externally.

FAA-Compliant Time Sharing Agreement

Reducing or eliminating the proxy-disclosed value of personal use of corporate aircraft, while still providing the benefit to NEOs, is more complex than a company simply requiring an executive officer to repay the incremental cost. A company must take into account regulations issued by the Federal Aviation Authority (FAA) prior to mandating and accepting such reimbursement. In particular, a company may accept reimbursement from an executive only if the parties have previously entered into a time sharing agreement. Failure to do so (or failure to enter into a FAA-compliant time sharing agreement) could expose a company to significant civil penalties.

FAA rules define a time sharing agreement to be "an arrangement whereby a person [e.g., corporate employer] leases his [its] airplane with flight crew to another person [e.g., executive officer], and no charge is made for the flights conducted under that arrangement other than for allowable expenses". Only the following expenses may be charged to an executive officer under a time sharing agreement:

- Fuel, oil, lubricants, and other additives (up to twice this expense may be charged to a covered executive officer),
- Travel expenses of the crew, including food, lodging, and ground transportation,
- Hangar and tie-down costs away from the aircraft's base of operation,
- Insurance obtained for the specific flight,
- Landing fees, airport taxes, and similar assessments,
- Customs, foreign permit, and similar fees directly related to the flight,
- In flight food and beverages,
- Passenger ground transportation, and
- Flight planning and weather contract services.

The FAA does not require an employer to charge a minimum amount, but only limits category of expenses that may be charged to an executive.

Time sharing agreements are only permitted with respect to flights conducted by U.S. registered aircraft and may only be applied to flights conducted on or after the effective date of the agreement. Retroactive application of a time sharing agreement is prohibited under FAA rules.

Prior to undertaking a time sharing agreement, a company should consult with aviation counsel to obtain an understanding of the FAA rules applicable to such agreements and other FAA rules applicable to flight operations.

Tax Implications of a Time Sharing Agreement

A time sharing agreement may result in the imposition of a federal excise tax on an executive officer, but, most often, it will reduce the executive officer's imputed income subject to federal income tax.

The IRS treats a time sharing agreement as a commercial arrangement under which it may impose a federal excise tax (FET). That is, the IRS considers an executive officer's payment of any charges imposed under a time sharing agreement for a flight no differently than a payment for a ticket on a commercial airliner. The FET is equal to 7.5% of the amount charged to and reimbursed by an executive officer under the time sharing agreement.

Under IRS rules, an executive officer's personal use of corporate aircraft results in imputed income to the executive, if the executive does not reimburse the company for the incremental costs incurred. A company may determine imputed income based on either the Standard Industry Fare Level (SIFL) rate or the fair market value rate. Typically, companies choose the SIFL rate because it results in lower imputed income than the fair market value rate.

An executive's reimbursement for allowable expenses for a given flight under a time sharing agreement would reduce dollar-for-dollar the executive's imputed income for such flight.

Related Party Disclosure of a Time Sharing Agreement

A time sharing arrangement may be subject to proxy disclosure. If amounts charged to and reimbursed by an executive officer under a time sharing agreement exceed $120,000 for a fiscal year, these reimbursements and the time sharing agreement may need to be disclosed as a related party transaction in a company's proxy. This type of disclosure should not draw significant adverse attention by investors or other parties.

Market Practice – Time Sharing Agreement

The general prevalence of time sharing agreements among large public companies is difficult to determine, as these agreements are not always publicly disclosed. However, a limited review of public company proxies reveals that some of the largest companies have entered into time sharing agreements, typically solely with their CEOs. Examples of companies that have disclosed the existence of a time sharing agreement include Discovery, FedEx, Liberty Global, Unum Group, Visa and Walgreens Boots Alliance.

The structure of disclosed time sharing agreements varies considerably among companies. Some agreements require a covered executive to reimburse for all personal travel, while others require reimbursement only after the executive exceeds a personal travel threshold (e.g., specified number of flight hours or dollar value of flights). The latter structure is likely intended, at least in part, to limit the value that will be disclosed in the company's proxy. And even when a company requires full reimbursement, a perquisite value may still show up in the proxy due to differences in calculating the proxy disclosure value versus the reimbursement costs as defined in the time sharing agreement. In addition, not all time sharing agreements consider FAA-approved expenses for calculating reimbursable flight expenses, likely due to the difficulty of obtaining the actual line-by-line expenses and separating the allowable costs for each individual flight. This is permissible, provided that the amount actually reimbursed does not exceed the FAA limit.

Conclusion

Entering into a time sharing agreement allows public companies to reduce (and even eliminate) the amount disclosed with respect to personal use of corporate aircraft, without eliminating or reducing the opportunity to provide this perquisite to senior executives. In evaluating the appropriateness of entering into a time sharing agreement, companies should consider a number of factors including:

- The complexity of determining FAA allowable costs for each personal flight,
- Any required disclosure,
- Company and employee tax implications,
- Company reimbursement policies for personal travel, and
- Applicable FAA rules.

In addition, a company should consider the appropriate internal process for approval and monitoring of time sharing agreements.

Generally, these factors should not serve as significant impediments to the implementation of a time sharing agreement.