

July 13, 2017

Reminder on CEO Pay Ratio Disclosure for 2018

Beginning in 2018, most public companies will be required to include CEO pay ratio disclosure in their proxy statements. Despite efforts to repeal, delay or limit the implementation of the SEC's pay ratio rule, it appears increasingly less likely that any of those efforts will be successful before the 2018 proxy season. As a result, companies should continue to prepare or, for those that have not yet started, begin the process of preparing the methodology they will use to develop their CEO pay ratio disclosure.

Pay Ratio Rule Requirements

The CEO pay ratio rule requires public companies to disclose the median of the annual total compensation of all employees, the annual total compensation of the CEO, and the ratio of those two amounts. Under the rule, "employee" is broadly defined and includes full-time, part-time, seasonal and temporary employees employed by a company and any of its consolidated subsidiaries, located both within and outside of the United States.

While companies will usually include this pay ratio disclosure in their proxy statements, the disclosure is required in any SEC filing that calls for executive compensation disclosure under Item 402 of Regulation S-K, including registration statements. A newly reporting company would be required to report its pay ratio for the first fiscal year following the year in which it becomes subject to the SEC's reporting requirements. Foreign private issuers, MJDS filers, emerging growth companies and smaller reporting companies are exempt from the rule. For a more detailed summary of the rule, please see our August 2015 [Alert](#).

In addition, in October 2016, the SEC's Division of Corporation Finance issued guidance – in the form of five compliance and disclosure interpretations (C&DIs) – to assist companies in preparing for compliance with the rule. The C&DIs address the selection and use of a consistently applied compensation measure, the treatment of furloughed employees, and the determination of whether a worker that provides services to a company but is employed by an unaffiliated third party (or by him or herself) will be treated as an employee for purposes of the pay ratio determination. For a brief summary of these C&DIs, please see our October 2016 [Alert](#).

Financial CHOICE Act

In June 2017, the U.S. House of Representatives passed the Financial CHOICE Act (H.R. 10), by a 283-186 vote, largely along party lines. One of the provisions of the legislation, co-sponsored by House Financial Services Committee Chairman Jeb Hensarling (R-TX), would repeal Section 953(b) of the Dodd-Frank Act, which directed the SEC to amend its rules to require the pay ratio disclosure. However, most observers believe it is unlikely that the Senate will approve the Financial CHOICE Act in its current form, if at all, before the 2018 proxy season.

SEC Reconsideration of Pay Ratio Rule Implementation

In February 2017, then-Acting SEC Chair Michael Piwowar launched a 45-day request for comment on the pay ratio rule, seeking input from companies about "any unexpected challenges" that they may have experienced in preparing to comply with the rule. He also directed the SEC staff to "reconsider the implementation of the rule based on any comments submitted and to determine as promptly as possible whether additional guidance or relief may be appropriate." To date, the SEC has received approximately 14,000 "form" letters in support of the rule and over 200

comment letters from various interested parties, including individuals, professors, corporations, pension funds, asset managers, law firms, and trade associations.

At this time, it is uncertain whether the SEC, under the new SEC Chair Jay Clayton, will repeal the rule, delay the compliance date or otherwise limit compliance with the rule. It is worth noting that the Department of Labor's controversial fiduciary duty rule was permitted to go into effect while the new administration studies the issue. More recently, a divided D.C. Circuit Court of Appeals held (2-to-1) that the EPA lacked authority to stay portions of a rule regulating fugitive methane emissions and other pollutants by the oil and gas sector. Although these rules may not present precisely the same issues as the pay ratio rule does, they demonstrate the challenges in delaying the effectiveness of a previously adopted rule that was mandated by statute.

Practical Considerations

Depending on the circumstances (whether a company has a large, global workforce or different payroll systems across multiple divisions or subsidiaries, etc.), the process for a company to identify its median employee, calculate that employee's annual total compensation, calculate the pay ratio, and prepare any accompanying narrative disclosure can be a significant and time-intensive undertaking. Since a repeal or delay of the pay ratio rule appears increasingly less likely, we recommend that companies continue to prepare or, for those that have not yet started, begin the process of preparing the methodology they will use to develop their CEO pay ratio disclosure well in advance of drafting their 2018 proxy statements. In addition, companies may want to consider the impact on its workforce of disclosing the compensation of the company's median employee.

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