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THE NEW PAY RATIO DISCLOSURE

The SEC has emphasized that the pay ratio disclosure rule was not designed to facilitate comparisons across companies. The author picks up this theme and identifies five key variables that make each company's pay ratio disclosure unique. She closes with disclosure strategies to address the potential that, despite these variables, readers will use pay ratios to compare compensation practices across companies.

By Maia Gez *

With the 2018 calendar year fast approaching, it is time to focus on one of the hottest topics for the upcoming proxy season: pay ratio. A little background first: the pay ratio rule, adopted by the SEC in August 2015 to implement Section 953(b) of the Dodd-Frank Act, generally requires public companies subject to the rule to disclose the median employee's annual total compensation, the CEO's annual total compensation, and the ratio of these two amounts.

This first-of-its kind pay equity disclosure required by SEC rules will be in the spotlight and a top focus of the 2018 proxy season for public companies – as well as for others interested in the new disclosure, such as employees, labor unions, the media, investors, and proxy advisory firms. Despite previous discussions of a possible delay, the SEC, on September 21, 2017, released interpretive guidance on the pay ratio rule and stated that the rule will require compliance by public companies as scheduled in their 2018 proxy statements.

As we approach the opening act for this new pay ratio disclosure, there are growing questions as to the implications of this new disclosure, and more specifically, how various stakeholders will use and interpret it. In essence, since the CEO's pay is already disclosed by public companies in their proxy statements, there are two new data points being introduced: (1) the median employee's annual total compensation and (2) the pay ratio itself. In its recent interpretive guidance, the SEC emphasized that each company's disclosure will be unique, and the adopting release stated that the pay ratio rule "should be designed to allow shareholders to better understand and assess a particular registrant's compensation practices and pay ratio disclosures rather than to facilitate a comparison of this information from one registrant to another."

Despite the uniqueness of the pay ratio disclosure for each public company, it is attractive for readers of this new disclosure to take the easy route and begin comparing one company's ratio to another, particularly within the same industry. In fact, a survey by the largest proxy advisory firm, ISS, found that nearly 75 percent of the investor respondents indicated that they intend to compare the ratios across companies and industry sectors, and/or assess year-on-year changes in the ratio at an individual company.

Before proceeding to compare ratios across companies, it is important to consider the inherent problems with this approach. Calculating the pay ratio

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