SEC Adopts Rule for Pay Ratio Disclosure

Rule Implements Dodd-Frank Mandate While Providing Companies with Flexibility to Calculate Pay Ratio

FOR IMMEDIATE RELEASE

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Washington D.C., Aug. 5, 2015 —
The Securities and Exchange Commission today adopted a final rule that requires a public company to disclose the ratio of the compensation of its chief executive officer (CEO) to the median compensation of its employees. The new rule, mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, provides companies with flexibility in calculating this pay ratio, and helps inform shareholders when voting on "say on pay."

"The Commission adopted a carefully calibrated pay ratio disclosure rule that carries out a statutory mandate," said SEC Chair Mary Jo White. "The rule provides companies with substantial flexibility in determining the pay ratio, while remaining true to the statutory requirements."

The new rule will provide shareholders with information they can use to evaluate a CEO's compensation, and will require disclosure of the pay ratio in registration statements, proxy and information statements, and annual reports that call for executive compensation disclosure. Companies will be required to provide disclosure of their pay ratios for their first fiscal year beginning on or after Jan. 1, 2017.

The rule addresses concerns about the costs of compliance by providing companies with flexibility in meeting the rule's requirements. For example, a company will be permitted to select its methodology for identifying its median employee and that employee's compensation, including through statistical sampling of its employee population or other reasonable methods. The rule also permits companies to make the median employee determination only once every three years and to choose a determination date within the last three months of a company's fiscal year. In addition, the rule allows companies to exclude non-U.S. employees from countries in which data privacy laws or regulations make companies unable to comply with the rule and provides a *de minimis* exemption for non-U.S. employees.
The rule does not apply to smaller reporting companies, emerging growth companies, foreign private issuers, MJDS filers, or registered investment companies. The rule does provide transition periods for new companies, companies engaging in business combinations or acquisitions, and companies that cease to be smaller reporting companies or emerging growth companies.

The rules will be effective 60 days after publication in the Federal Register.

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FACT SHEET
Pay Ratio Disclosure
SEC Open Meeting
August 5, 2015

Action
The Securities and Exchange Commission will consider whether to adopt a rule requiring public companies to disclose the ratio of the annual total compensation of the chief executive officer (CEO) to the median of the annual total compensation of the company's employees. The rule, which is mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, would provide investors with information to consider when assessing CEO compensation, while providing companies with substantial flexibility in calculating the ratio.

Highlights of the New Rule
Pay Ratio Disclosure Requirement
As required by the Dodd-Frank Act, the rule would amend existing executive compensation disclosure rules to require companies to disclose:

- The median of the annual total compensation of all its employees, except the CEO;
- The annual total compensation of its CEO; and
- The ratio of those two amounts.

Methodology for Identifying the Median Employee
To identify the median employee, the rule would allow companies to select a methodology based on their own facts and circumstances. A company could use its total employee population or a statistical sampling of that population and/or other reasonable methods. A company could, for example, identify the median of its population or sample using:

- Annual total compensation as determined under existing executive compensation rules; or
- Any consistently-applied compensation measure from compensation amounts reported in its payroll or tax records.

A company could apply a cost-of-living adjustment to the compensation measure used to identify the median employee. If a company applies this adjustment, it would need to use the same cost-of-living adjustment in calculating the median employee's annual total compensation. To provide context for this adjustment, a company electing to present the pay ratio in this manner must also disclose the median employee's annual total compensation and the pay ratio without the cost-of-living adjustment.

A company also would be permitted to identify its median employee once every three years unless there has been a change in its employee population or employee compensation arrangements that it reasonably believes would result in a significant change to its pay ratio disclosure. Also, within those three years, if the median employee's compensation changes, the company may use another employee with substantially similar compensation as its median employee.

Determination of Total Compensation
A company would be required to calculate the annual total compensation for its median employee using the same rules that apply to the CEO's compensation. "Annual total compensation" means total compensation for the last completed fiscal year, calculated using the definition of "total compensation" in existing executive compensation rules, namely Item 402(c)(2)(x) of Regulation S-K. The rule would allow companies to use reasonable estimates when calculating any elements of the annual total compensation.

Identification of Employee Population
A company would be permitted to select a date within the last three months of its last completed fiscal year on which to determine the employee population for purposes of identifying the median employee.

Subject to certain exceptions, the company would be required to include all employees – U.S. and non-U.S., full-time, part-time, temporary and seasonal – employed by the company or any of its consolidated subsidiaries in performing its pay ratio calculation. Individuals employed by unaffiliated third parties or independent contractors would not be considered to be employees of the company.

A company could exclude non-U.S. employees from the determination of its median employee in two circumstances:

- Non-U.S. employees that are employed in a jurisdiction with data privacy laws that make the company unable to comply with the rule without violating those laws. The company would be required to obtain a legal opinion from counsel on the inability of the company to obtain or process the information necessary for compliance with the rule without violating the jurisdiction's laws or regulations governing data privacy.
- Up to 5 percent of its total employees who are non-U.S. employees, including any non-U.S. employees excluded using the data privacy exemption. If a company excludes any non-U.S. employee in a particular jurisdiction, it must exclude all non-U.S. employees in that jurisdiction.

Companies would be permitted, but not required, to annualize the total compensation for a permanent employee who did not work for the entire year, such as a new hire. In contrast, full-time equivalent adjustments for part-time workers and annualizing adjustments for temporary and seasonal workers would not be permitted when calculating the required pay ratio.

Disclosure of Methodology, Assumptions, and Estimates
Companies would be required to briefly describe the methodology used to identify the median employee, and any material assumptions, adjustments (including cost-of-living adjustments), or estimates used to identify the median employee or to determine annual total compensation. If a company identifies a median employee based on a consistently applied compensation measure, it would be required to disclose the measure it used. Also, companies would be required to clearly identify any estimates used.

Additional Disclosure Permitted But Not Required
Companies would be permitted, but not required, to supplement the required disclosure with a narrative discussion or additional ratios. Any additional discussion and/or ratios would need to be clearly identified, not misleading, and not presented with greater prominence than the required pay ratio.

Filings Where Disclosure Is Required
Companies would be required to describe the information in registration statements, proxy and information statements, and annual reports that must already include executive compensation information as set forth under Item 402 of Regulation S-K.

Companies would not be required to:

- Disclose the pay ratio information in reports that do not require executive compensation information, such as current and quarterly reports.
- Update their disclosure for the most recently completed fiscal year until the company files its proxy or information statement for its annual meeting of shareholders (or annual report for companies that do not file proxy or information statements for annual meetings), but not later than 120 days after the end of the fiscal year.

Companies Subject to the Disclosure Requirement
The disclosure requirement would apply to all companies required to provide executive compensation disclosure under Item 402(c)(2)(x) of Regulation S-K. Smaller reporting companies, foreign private issuers,

MJDS filers, emerging growth companies, and registered investment companies would not be subject to the requirement.

A company subject to the pay ratio requirement would be permitted to omit from its calculation any employees obtained in a business combination or acquisition for the fiscal year in which the transaction becomes effective. The company would be required to identify the acquired business and disclose the approximate number of employees it is omitting.

Compliance Dates

Companies would be required to report the pay ratio disclosure for their first fiscal year beginning on or after January 1, 2017.

A company that had not previously been a reporting company would be required to report the pay ratio disclosure for the first fiscal year following the year in which it becomes subject to the Commission's reporting requirements, but not for any fiscal year commencing before January 1, 2017.

Background

Section 953(b) of the Dodd-Frank Act directs the Commission to amend existing rules to require companies to disclose:

- The median of the annual total compensation of all employees of the company, except the CEO;
- The annual total compensation of its CEO; and
- The ratio of those two amounts.

Under SEC rules, companies are required to provide extensive information about the compensation of its CEO and other named executive officers. Companies currently are not, however, required to disclose the same compensation information for other employees

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