SEC Moves to Complete Final Rules for Executive Compensation Disclosures

January 2016

Skadden

This article is from Skadden's *2016 Insights* and is available at skadden.com/insights/2016-insights.

Contributing Partner

Brian V. Breheny
Washington, D.C.

Law Clerk

Michael Ju
New York

Former Counsel

Ted Yu

Public companies should start preparing for the new executive compensation disclosures mandated by the Dodd-Frank Act as the Securities and Exchange Commission (SEC) moves to complete these rulemakings in the next year. The requirements could impose significant disclosure burdens on companies and increase public scrutiny of the companies' executive compensation policies.

CEO Pay Ratio. In August 2015, the SEC adopted final rules implementing the controversial CEO pay ratio disclosure requirements required by the Dodd-Frank Act. The new rules require companies to disclose the median annual total compensation for all company employees except the CEO, the CEO's annual compensation and the ratio of those two amounts. Companies are required to provide the new pay ratio disclosures for the first fiscal year commencing on or after January 1, 2017. As a result, companies with a fiscal year ending December 31, 2017, will need to disclose the pay ratio information (based on 2017 compensation) in their registration statements, annual reports on Form 10-Ks or proxy statements for 2018.

Pay Versus Performance. The pay-versus-performance disclosure requirements were proposed in April 2015 and, once adopted, would require companies to disclose the relationship between the compensation actually paid to named executive officers and the company's financial performance. The proposed rules would require companies to include in the proxy or information statements a new table with the following:

- the total executive compensation of the CEO and the average of the total compensation of the other named executive officers (NEOs), as reported in the Summary Compensation Table and already required in the proxy or information statement;
- the executive compensation actually paid to the CEO and the average of the executive compensation actually paid to the other NEOs, calculated according to the proposed rules; and
- the cumulative total shareholder return (TSR), calculated in the same manner as the performance graph already required by the SEC rules, for the company and its peer group.

Companies would be required to describe (1) the relationship between the executive compensation actually paid and the company's TSR and (2) the relationship between the company's TSR and the TSR of its peer group. While the timing of the adoption of the final rules is unclear, companies should plan for the possibility that the new pay-versus-performance requirements could go into effect as soon as the 2016 proxy season.

Hedging Disclosures. The hedging disclosure requirements, which the SEC proposed in February 2015, would require companies to disclose in their proxy or information statements whether they permit employees and directors to hedge the company's securities (such as through prepaid variable forward contracts, equity swaps, collars or any other transactions with economic consequences comparable to the purchase of these financial instruments). While the proposed rules do not prohibit hedging or require the adoption of a policy addressing hedging, companies may face greater pressure from investors and other interested groups to adopt new hedging policies or revise existing ones when the rules go into effect and disclosures about peer companies' hedging policies become available. Therefore, companies should consider reviewing the need for new or revised hedging policies for future proxy statements.

Four Times Square
New York, NY 10036
212.735.3000

skadden.com