CEO Pay Ratio Disclosures at the Tech 150 (Updated)

With the 2018 proxy season well underway, we have taken a look at the newest executive compensation disclosure item appearing in corporate proxy statements for the first time – the CEO pay ratio. Mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, beginning with proxy statements filed for fiscal years beginning on or after January 1, 2017, companies are required to disclose:

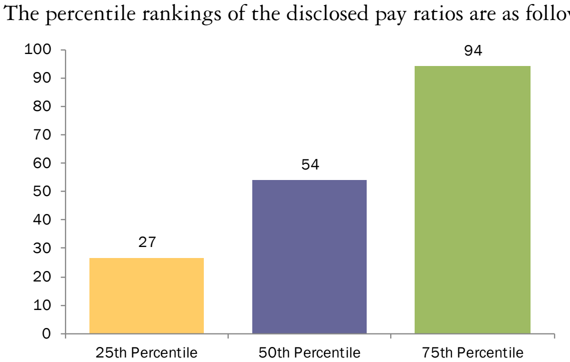
- The median of the annual total compensation of all their employees (other than their Chief Executive Officer);
- The annual total compensation of their CEO; and
- The ratio of these two amounts.

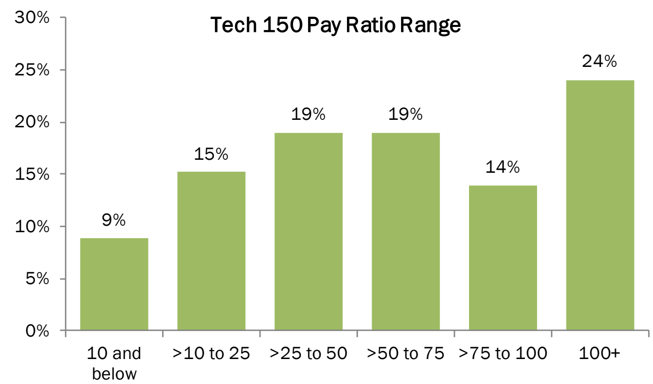
This Thoughtful Disclosure Alert summarizes our findings based on a review of the proxy statements filed since the beginning of the year by representative companies in the technology sector headquartered throughout the United States. We call this group, which consists of many of the most prominent companies in the computer/hardware, internet/software, and semiconductor sectors, the "Tech 150." As of May 10, 2018, 79 of the companies in the Tech 150 (54.0%) had filed either a definitive or a preliminary proxy statement containing the CEO pay ratio disclosure.

CEO Pay Ratios

Our review has determined the median pay ratio among the companies that have made their initial disclosure to be 54 to 1. So far, the CEO pay ratio distribution is highly concentrated below 100 to 1, with 60 of the reviewed companies (74.1%) disclosing pay ratios lower than 100 to 1. Similarly, of the 19 companies disclosing pay ratios of 100 to 1 or greater, only six companies reported ratios above 200 to 1.

The percentile rankings of the disclosed pay ratios are as follows:

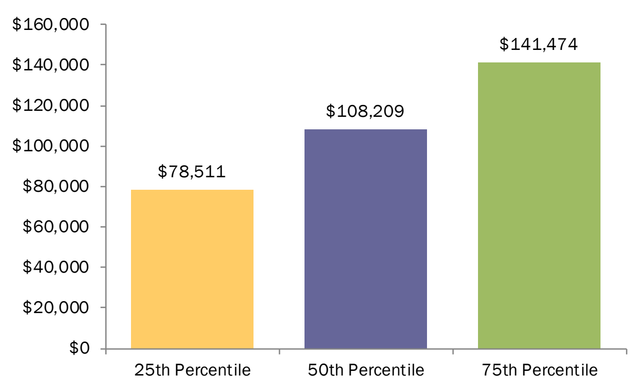




Certain prominent technology company CEOs (often founders) are well known for taking little or no compensation for serving in that role. Four companies, Square, Inc., Shutterstock, Inc., Twitter, Inc. and Instructure, Inc., have disclosed pay ratios of 0, as their respective CEOs did not receive compensation for serving as chief executive officer in 2017.

Median Employee Compensation

Our review also determined the annual total compensation of the median employee among the companies that have made their initial disclosure to be $108,209, with annual total compensation ranging from $7,782 to $256,370.



Supplemental Pay Ratios

While the CEO pay ratio rule permits companies to present additional information, including additional ratios, to supplement the

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required pay ratio, they are not required to do so. To date, 16 of the companies that we have reviewed (20.25%) have provided a supplemental ratio. These supplemental ratios have been provided for the following reasons:

Reason for Supplemental Pay Ratio	Number of Companies
Excluding CEO's new hire/promotion equity awards	5
Excluding CEO's one-time equity award	2
CEO requested reduced equity award	1
Change in timing of annual "refresh" equity awards	1
Supplemental ratio considering only U.S. employees	1
Supplemental ratio considering only full-time employees	1
Excluding CEO severance compensation	1
Supplemental ratio pro-rating CEO performance-based equity award	1
Excluding CEO performance-based compensation	1
Excluding regrant of CEO equity awards resulting from financial reporting adjustment	1
Supplemental ratio without annualizing new CEO compensation	1

Other Notable Findings

Location of Disclosure

The CEO pay ratio rule does not specify where the disclosure should be placed in a company's proxy statement. Consequently, while consistently included as part of companies' executive compensation disclosure, it is showing up in a variety of specific locations. To date, the overwhelming choice is at the end of the executive compensation disclosure, following the discussion of Potential Payments upon Termination or Change in Control, which has been the placement of more than half of the companies reviewed. The most popular locations for presenting the CEO pay ratio disclosure are as follows:

Location of Disclosure	Number of Companies Reviewed	Percentage of Companies Reviewed
After Potential Payments upon Termination or Change in Control section	51	64.6%
In CD&A	5	6.3%
After Summary Compensation Table	7	8.9%
Between CD&A and Summary Compensation Table	4	5.1%
After other compensation tables (for example, the Options Exercises & Stock Vested Table)	12	15.2%

Consistently Applied Compensation Measure

For purposes of identifying the median employee, the CEO pay ratio rule permits companies to use one or more compensation measures, as long as such measures are consistently applied across the employee population. Our review indicates that companies took full advantage in the flexibility of the rule to develop a methodology for identifying their median employee that reflected their individual situation. Reflecting the prevalence of equity awards in the technology sector, we found that total direct compensation (total cash plus equity awards) was the most popular compensation measure, employed by 44 companies (55.7%). This contrasts with other industry sectors, where broad-based equity compensation programs are less common.

The most commonly used compensation measures were as follows:

Compensation Measure	Number of Companies	% of Tech 150
Total cash compensation plus equity awards	44	55.7%
Total cash compensation	18	22.8%
Base pay or wages	5	6.3%
Total compensation (cash, equity and benefits)	5	6.3%
Form W-2 (or its equivalent) compensation	5	6.3%
Base pay plus equity awards	2	2.5%

Where equity awards are included in the compensation measure, most companies are using the grant date fair value of the award (rather than the value of the portion vesting during the year) as the amount of this pay element.

Determination of Employee Population

All of the companies reviewed have disclosed that they used a full employee census file to determine the median employee (subject to the application of the de minimis exemption in a few instances as noted below). To date, no company has indicated that it used statistical sampling to identify its median employee.

While the CEO pay ratio rule permits companies to exclude non-U.S. employees from their employee population where a country's data privacy laws prevent the procurement or processing of the relevant compensation data, to date none of the reviewed companies have disclosed their use of this exemption.

In addition, the CEO pay ratio rule contains a "de minimis" exemption, which permits the exclusion of non-U.S. employees, on an all-or-nothing basis, from one or more countries that, in the aggregate, account for 5% or less of a company's total employee population. To date, 20 companies (25.3%) have indicated their use of the de minimis exemption when determining the employee population from which they identified their median employee. While it may be premature to draw any conclusions, this outcome is likely a reflection of the relative ease with which technology companies can access compensation data for their global workforce.

Final Observations

While a sizable number of companies in the Tech 150 have yet to file their 2018 proxy statements, certain patterns are beginning to take shape. Most notably, the pay ratios being disclosed are not as large as expected. As illustrated above, the majority of the pay ratios are well below 100 to 1. On the other hand, median employee compensation is trending higher than in many other industry sectors, perhaps a reflection of the highly-educated workforce needed to power technology companies as well as the broader distribution of equity awards. Finally, as envisioned by the CEO pay ratio rule itself, companies appear to have taken a pragmatic approach to undertaking the most complex – and potentially expensive – aspect of compliance: the identification of the median employee. By tailoring their compliance methodology to their specific facts and circumstances, it appears that most companies have been able to complete this disclosure exercise without encountering undue difficulties.

As the year continues, we will see whether these trends hold firm.

Need Assistance?

Compensia has extensive experience in helping companies develop an appropriate methodology for identifying their median employee, as well draft the required disclosure that must accompany their CEO pay ratio. If you would like assistance in preparing your CEO pay ratio disclosure, or if you have any questions on the subjects addressed in this Thoughtful Disclosure Alert, please feel free to contact Mark A. Borges or Christine McGrory.

About Compensia:

Compensia, Inc. is a management consulting firm that provides executive compensation advisory services to Compensation Committees and senior management. ■

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