

# The CEO Pay Ratio Disclosure Requirement – Time to Get Started

Starting in 2018, public companies will be required to disclose in their annual report on Form 10-K, definitive proxy statement, and certain other SEC filings the ratio of the annual total compensation of their Chief Executive Officer to the median of the annual total compensation of their other employees (the “Pay Ratio Rule”). This initial disclosure will be based on the compensation paid for the first fiscal year beginning on or after January 1, 2017.

As we discussed in our recent Thoughtful Disclosure Alert (see *With CEO Pay Ratio Effective Date Looming, There’s No Relief in Sight* (May 8, 2017)), the prospects for a repeal – or even a delay – of this new disclosure requirement have dimmed considerably over the past few months. As a result, companies that will be subject to the Pay Ratio Rule should begin preparing to comply (if they haven’t already begun) in the next few weeks.

## What’s Required?

While on its face the disclosure requirement is straightforward – provide the ratio of the annual total compensation of your CEO to the annual total compensation of your median employee – for most companies the effort required to produce this ratio is likely to be significant. Foremost will be developing a process (or “methodology”) for identifying your “median employee” that is reasonable, defensible, and repeatable. The issues associated with constructing a workable methodology will depend on your company’s specific employee and compensation profiles, including the size, demographics, and location of your workforce, the location and accessibility of your compensation data, and the number and complexity of your compensation structures. In addition, once you have identified the median employee, you will need to calculate his or her annual total compensation using the same approach that applies to determining the total compensation for your named executive officers.

To assist you in understanding and complying with this new disclosure requirement, we have put together a guide, *Complying with the CEO Pay Ratio Disclosure Requirement*. In this guide, we summarize a process for identifying your

median employee and then preparing the required disclosure covering the following five steps:

- **Collect data** – Gather the relevant information about your global workforce, determine the location and accessibility of the compensation data for your workforce, and develop an understanding of your various compensation structures;
- **Determine employees** – Determine the employee population from which the median employee must be identified, including whether any employee groups may be excluded and whether any non-employee workers, such as independent contractors, must be included;
- **Compare compensation amounts** – Select a compensation measure that reasonably reflects the annual compensation of your employee population and compare their compensation over the selected employment period to identify the median employee;
- **Calculate annual total compensation** – Once the median employee has been identified, determine his or her annual total compensation for the last completed fiscal year, along with the annual total compensation of your CEO for the same period; and
- **Determine pay ratio** – Draft your disclosure, which includes the required pay ratio as well as a brief description of your methodology for identifying the median employee and any materials assumptions, adjustments, and estimates used for this purpose or to determine total compensation or any element of total compensation.

In addition to this guide, we invite you to listen to a replay of our June 22nd webinar on [complying with the Pay Ratio Rule](#). The password is **Payratio2017**.

## Need Assistance?

Compensia can assist companies in preparing their CEO pay ratio disclosure, including developing a process for identifying their “median employee.” If you would like assistance in understanding how the CEO pay ratio disclo-

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sure requirement will affect your company, preparing your initial CEO pay ratio disclosure, or if you have any questions on the subjects addressed in this Thoughtful Disclosure Alert, please contact Mark A. Borges. ■

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

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