

TYPES NOT MAPPED YET October 09, 2020 | TTR not mapped yet | Michele C. Kloeppel, Brent R. Trame, Jesse K. Doggendorf

Item 402 Pay Ratio Disclosures: Annual proxy statements filed in 2021 may need a new median employee determination

In 2015, the Securities and Exchange Commission adopted final rules under the Dodd-Frank Act that amended Item 402 of Regulation S-K to require certain public company filers to disclose in their annual proxy statements (i) the chief executive officer's total annual compensation, (ii) the total annual compensation of the median employee of the reporting company (excluding the CEO), and (iii) the ratio between the two (i.e. the CEO Pay Ratio). Smaller reporting companies, emerging growth companies and foreign private issuers are exempt from this disclosure requirement.

While the final rules were adopted by the SEC in 2015, public companies subject to this disclosure rule did not have to disclose this information until their first fiscal year beginning after January 1, 2017. Therefore, many existing public companies initially had to make their pay-ratio disclosures in their 2018 annual proxy statements. Some filers have changed their "median employee" since their original disclosure in their 2018 proxy statements due to a change in employee compensation arrangements, their employee populations or the median employee's circumstances (all in the event that the company reasonably believes such changes would result in a significant change in the disclosure). However, the final rule also requires (in addition to the significant changes above) each company to make a new determination of the company's median employee at least once every three years.

As we approach the 2021 proxy season, companies that have not made a determination regarding their median employee since their initial disclosure in their 2018 annual proxy statement are required to make a new median employee determination.

When making the median employee determination, companies must comply with the following standards:

- Companies are allowed to use reasonable estimates, assumptions and methodologies based upon their own facts and circumstances to identify the median employee.
- Companies must select a date within the last three months of the last completed fiscal year on which to determine the employee population. }
- Subject to certain limited data-privacy and "de minimis" exceptions, companies are required to include all employees (U.S. and non-U.S., full-time, part-time, temporary and seasonal), including those employees of each company's consolidated subsidiaries. Individuals employed by unaffiliated third parties (i.e., "leased" employees) and independent contractors should not be included.
- Companies are permitted to annualize the total compensation for permanent employees who have not worked a full year (i.e., new hires), but are not permitted to make full-time equivalent adjustments for part-time, temporary or seasonal workers.

The disclosures in the annual proxy statement must describe the methodology used to identify the median employee and any material assumptions, adjustments or estimates used.

Finally, when calculating the median employee's annual total compensation, companies must use the same rules they apply to determining the CEO's annual total compensation (i.e., annual total compensation for the median employee is also the sum of all of the types of compensation listed on the executive summary compensation table).



For general information concerning calculations of annual compensation (for the CEO and the median employee), the determination of the median employee and the CEO Pay Ratio, please see the press release from the SEC regarding the final rules.

If you need assistance in preparing your CEO Pay Ratio disclosures, including the process of selecting your new median employee, or have any questions, please feel free to contact [Michele Kloeppel](#), [Brent Trame](#) or [Jesse Daggendorf](#).

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