

The CEO Pay Ratio Deadline is Looming; Here's How Companies Should Prepare

With the clock ticking on the January 2018 implementation date for the CEO pay ratio— and no action taken by the SEC yet to delay the rule— here's how companies should prepare.

As we move past the midpoint of 2017, work is already underway at a number of our clients to begin preparing for the calculation and disclosure of CEO pay ratios next spring. Although many experts had anticipated the CEO pay ratio rule would be delayed or repealed as part of a broader rollback of the Dodd-Frank Act by a Republican congress, this is now looking increasingly unlikely, and companies and advisors across all industries are now resuming preparations to comply in 2018.

For some companies, the process of calculating and disclosing their CEO pay ratio will be far more complex than they assume. And for all issuers, the disclosure is potentially controversial and should be addressed with appropriate diligence, especially in the first year of implementation. Below are the key steps we recommend taking to ensure your organization stays on track:

Review (again) the SEC's [interpretative guidance](#) issued last fall.

The SEC's guidance addresses several important details that are critical to proper implementation of the CEO pay ratio rule, including:

- What employees can/should be included in the population from which the “median” employee will be identified?
- What is the range of appropriate/allowable “consistently applied compensation measures” (CACM), which can be used to identify the median employee?
- What is the period to be used in calculating a CACM?

Do one or more trial runs of your analysis to understand how your CEO pay ratio changes as you select from the range of approved methodologies.

This is an important step since the SEC's guidance clearly indicates that companies will have significant flexibility in how to determine their ratios to minimize the burden of compliance and produce as meaningful a result as possible. It will also be important to consider the longer-term implications of the choice made for 2018, as stakeholders will expect you to use a consistent methodology year-over-year. It may be preferable to use a

methodology similar to your peers to avoid controversy about how your number was calculated and this will bring more fairness to the comparisons that will inevitably be made between you and your competitors.

Learn how to put your CEO pay ratio into the right context.

To do this, companies will need to assess how their own CEO pay ratio stacks up to the ratios of their peers. Understanding what is an “expected” range of ratios in your industry, and what types of factors might justify being higher or lower in the range, will be critical when it comes to drafting meaningful disclosure, including an explanation of the ratio in your proxy statement.

Last year, as the table below illustrates, we completed preliminary research on CEO pay ratio outcomes by industry, and we continue to conduct custom research for many clients as we prepare for 2018. Early findings indicate that smaller biotech companies, which tend to have knowledge-based workforces mostly in higher-cost countries, often have quite low CEO pay ratios compared to other sectors. Larger commercial biotech firms with manufacturing operations tend to have higher ratios, followed by software and Internet companies, medical device, and finally semiconductor companies, which often have large offshore manufacturing operations that can yield low “median employee” pay levels. For more information, see our article: [In Calculating Your CEO Pay Ratio, Relativity to Peers is the New Math.](#)

Industry/Stage	Median CEO Pay Ratio
Small/Pre-commercial Biotech	10.9x
Larger/Commercial Biopharma	30.7x
Software/Internet	43.0x
Medical Device	46.0x
Semiconductors	63.0x

Source: Radford Global Technology Survey and Radford Global Life Sciences Survey

Start thinking about your actual disclosure.

While most companies won’t begin drafting their Compensation Discussion & Analysis (CD&A) in earnest until the spring, we recommend that clients get an early start on their CEO pay ratio section since it will be brand new. While it is unclear to what degree institutional investors or proxy advisors will use CEO pay ratio disclosures, we fully expect these ratios to be a point of focus for labor groups and the media. As a result, companies will want to consider providing supplementary narrative discussion with additional context for their ratio. This could include a review of market and peer trends similar to those described at a high level above, and discussion of where and why a company is positioned relative to its peers. Crafting a compelling story around the pay ratio will be an important project that should include input from both internal stakeholders and key advisors and consultants, and is best begun sooner rather than later in our opinion.

While many companies are focused on the logistics of calculating and drafting the disclosure around their CEO pay ratio, don’t neglect to think through the story you plan to tell and how that message will resonate with all of the different stakeholders who might read your disclosure. For example, your investors might use the pay ratio to make investment and proxy voting decisions; employees, on the other hand, might be interested in how their own

pay compares to the median worker. Prepare in advance for any questions from stakeholders that may arise so you're not caught off guard when proxy season comes.

To speak with a member of our compensation consulting team regarding CEO pay ratios or any other executive compensation topics, please write to consulting@radford.com.

Author Contact Information

Ram Kumar

Associate Partner, Radford
Aon | Talent, Rewards & Performance
+1.781.906.2395
rkumar@radford.com

Ed Speidel

Partner, Radford
Aon | Talent, Rewards & Performance
+1.781.906.2377
espeidel@radford.com

Nora McCord

Associate Partner, Radford
Aon | Talent, Rewards & Performance
+1.415.486.7165
nora.mccord@radford.com

Kevin Wells

Director
Aon | Talent, Rewards & Performance
+1.202.969.3295
kevin.wells@aonhewitt.com

Ted Buyniski

Partner, Radford
Aon | Talent, Rewards & Performance
+1.781.906.2389
tbyniski@radford.com

About Radford

Radford delivers talent and rewards expertise to technology and life sciences companies. We empower the world's most innovative organizations—at every stage of development—to hire, retain and engage the amazing people they need to create amazing things. Today, our surveys provide in-depth rewards insights in 80-plus countries to more than 3,000 client organizations, and our consultants work with hundreds of firms annually to design talent and rewards programs for boards of directors, executives, employees and sales professionals. Radford is part of the Talent, Rewards & Performance practice at Aon plc (NYSE: AON). For more information, please visit radford.aon.com.

About Aon Hewitt

Aon Hewitt empowers organizations and individuals to secure a better future through innovative retirement, health, and talent solutions. We advise and design a wide range of solutions that enable our clients' success. Our teams of experts help clients navigate the risks and opportunities to optimize financial security; redefine health solutions for greater choice, affordability, and wellbeing; and achieve sustainable growth by driving business performance through people performance. We serve more than 20,000 clients through our 15,000 professionals located in 50 countries around the world. For more information, please visit aon.com.

This article provides general information for reference purposes only. Readers should not use this article as a replacement for legal, tax, accounting or consulting advice that is specific to the facts and circumstances of their business. We encourage readers to consult with appropriate advisors before acting on any of the information contained in this article.

The contents of this article may not be reused, reprinted or redistributed without the expressed written consent of Radford. To use information in this article, please [write to our team](#).

© 2017 Aon plc. All rights reserved