

## Considerations For 2024 Proxy Season After Exec Pay Rules

By **Jake Downing, Jessica Stricklin and Lauren Salas Mationg** (April 20, 2023, 3:24 PM EDT)

The 2023 proxy season included additional complexity for public companies due to the U.S. Securities and Exchange Commission's pay-versus-performance disclosure rules that were adopted in August, as supplemented by SEC staff's compliance-and-disclosure interpretations on the rules released in February.

The pay-versus-performance rules generally require a tabular and narrative disclosure of the relationship between the compensation actually paid to the company's named executive officers and certain financial performance measures. The SEC indicated that the rules are intended to increase transparency and consistency with how such information is communicated to investors.

Although the long-term impact of the pay-versus-performance disclosure on investor action and executive pay practices remains to be seen, compliance with the rules creates immediate and often expensive challenges for companies, primarily due to:

- The short time frame between the release of the rules and compliance-and-disclosure interpretations and proxy filing dates for calendar year-end companies;
- The multifaceted nature of the disclosure, which includes extensive new equity valuations and analysis presented in tables, narratives and/or charts; and
- The overall ambiguity associated with the new disclosure requirements under the pay-versus-performance disclosure rules.

Given that most calendar-year companies have filed their proxy statements, there is now an opportunity to assess how the rules and compliance-and-disclosure interpretations affected the 2023 proxies and identify considerations for future proxy seasons.

### Key Considerations for the 2024 Proxy Season

*The tabular disclosure provides companies with more discretion, which may be adjusted year-to-year.*



Jake Downing



Jessica Stricklin



Lauren Salas Mationg

Unlike other proxy tables, the pay-versus-performance table provides discretion with respect to the company-selected measure column.

Specifically, companies may choose any metric that represents their most important financial performance measure linking compensation actually paid to named executive officers to performance for the most recently completed fiscal year that is not already required to be disclosed in the pay-versus-performance table.

The compliance-and-disclosure interpretations provide helpful clarification on the company-selected measure, confirming that the company-selected measure can be a derivative of any measure required to be in the pay-versus-performance table, such as relative total shareholder return or earnings per share.

However, stock price cannot be used as a company-selected measure if the only impact or link to compensation actually paid is a change in the value of the fair value of an equity-based award — for example, restricted stock units subject only to time-based vesting conditions.

Similarly, because the company-selected measure is determined based on the most recently completed fiscal year, the measure selected cannot be calculated over a multiyear period that includes the most recent year of the pay-versus-performance table.

Given the SEC's emphasis that the company-selected measure is an annual designation, for the 2024 proxy season, companies must evaluate the changes in compensation practices adopted since the prior proxy and evaluate if the previously selected measure still reflects the most important link between executive pay and performance.

While this means companies can tailor the table to better align with their individual practices, it also means they must consider a metric that is representative of all the required years of data.

***Companies should consider using a third-party vendor to calculate equity award treatment.***

The calculation of "compensation actually paid" to named executive officers under the pay-versus-performance rules requires companies to undertake multiple fair value calculations over the life cycle of an award, which may result in hundreds of additional valuations for companies that annually grant multiple equity award types.[1]

Given the complexity and time burden associated with these calculations, utilizing a third-party vendor to prepare the valuations may be especially critical, albeit expensive, for many companies to comply with the pay-versus-performance rules.

Now that there is a longer runway of time to prepare the pay-versus-performance disclosure for the 2024 proxy season, companies that intend to utilize a third-party vendor should work on engaging a vendor in advance to ensure that valuations are timely completed in accordance with the company's internal proxy filing timeline.

***The five-year look-back period will require additional calculations for the 2024 and 2025 proxy seasons.***

Under the pay-versus-performance rules, companies must report five years of historical information within the tabular disclosure table, or three years for smaller reporting companies.

However, only three years of historical information was required for the first pay-versus-performance disclosure under the transition rule, or two years for smaller reporting companies. An additional year must be added for each of the 2024 and 2025 proxy seasons — i.e., the full five years will be required for the first time in the 2025 proxy season for most companies.

Although prior-year data can be carried through for most of the columns of the pay-versus-performance table, companies will be required to include additional data rows in the upcoming years. Additionally, the total shareholder return and peer group total shareholder return will need to be recalculated over the measurement period covered by the pay-versus-performance table.

Where possible, companies may consider updating their pay-versus-performance disclosures with the data they have available in advance of proxy season.

### **Looking Forward**

Even though the pay-versus-performance rules and compliance-and-disclosure interpretations provide an outline of the required information and sample tabular disclosure, companies faced a significant amount of uncertainty in drafting the required disclosures. Most notably, there is an opportunity for additional clarity related to nonstandard company operations, such as complex mergers and acquisitions activity, recurring named executive officer turnover and off-cycle equity awards.

Once review and enforcement of the pay-versus-performance rules begin, we are likely to see continued guidance and streamlining related to structure and content. In the meantime, early initiation of the proxy drafting and review process with third-party service providers ensures that companies are reasonably interpreting and accurately applying the pay-versus-performance rules to the specifics of their individual businesses.

Finally, the pay-versus-performance rules and compliance-and-disclosure interpretations should not be considered in isolation.

The SEC has also released final rules regarding public company clawback policies, and final rules regarding human capital disclosures are forthcoming in 2023. With these, the SEC is continuing to demand a holistic view of company compensation practices, which includes increased accountability and substantive, written documentation and analysis.

Companies should recognize that each disclosure and requirement will continue to present time-intensive drafting and require input from multiple stakeholders. As such, a proactive review of these rules and early drafting practices will ensure that companies are able to comprehensively satisfy their disclosure obligations.

---

*Jake Downing is a partner, Jessica Stricklin is a senior associate and Lauren Salas Mationg is an associate at King & Spalding LLP.*

*The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.*

[1] We briefly mentioned this in our January 2023 Law360 article: <https://www.law360.com/articles/1569010/new-compensation-and-benefits-rules-demand-early-action>.