

Spotlight on Shareholder Proposals: Internal Pay Ratio Disclosure

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Section 953(b) of Dodd-Frank requires companies to disclose the internal pay ratio between the total annual compensation of their CEO and the median total annual compensation of their employees. Effectiveness of the requirement has been delayed until the SEC promulgates implementing rules. Meanwhile, companies have complained that the calculations required to comply with the disclosure requirement are burdensome and unfeasible, and proposals for Section 953(b)'s repeal have been introduced in Congress.

Against this background, it is somewhat surprising that shareholder proposals seeking disclosure of the internal pay ratio decreased in 2011, and average shareholder support for this disclosure has remained low (although it increased slightly in 2011). According to an executive compensation bulletin published by Towers Watson in June 2011, shareholder proposals with respect to internal pay ratio disclosure dropped from 9 in 2010 to 3 in 2011 (through mid-June), while average shareholder support increased from 6.2% to 9.1%.

One such example of a failed shareholder proposal is the 2011 proposal by the International Brotherhood of DuPont Workers calling for the board of directors of E. I. du Pont De Nemours to compare the "compensation packages for senior executives with that provided to the lowest paid employees." The proposal received just 5.8% in shareholder support.

Some companies already address concerns regarding internal pay equity. Examples of such "proactive" companies include Whole Foods Market, which places a cap (expressed as a multiple of the company's average wage) on executive cash compensation, NorthWestern Corporation, which voluntarily disclosed in its 2011 proxy that its targeted compensation for its CEO in 2010, excluding benefits, was 18 times the median pay of all its employees, and Goldman Sachs, which released supplemental proxy materials dedicated exclusively to its compensation practices.

A possible reason for this lack of activism may be that shareholders as a whole are less concerned with internal pay ratio disclosure than with other areas of compensation policy, such as linking pay to performance and requiring executives to retain a significant percentage of their equity.

As we wait to see where the SEC and Congress will come out on mandatory internal pay ratio disclosure, it is difficult to predict where we will end up, but one thing looks certain – shareholder proposals are not currently leading the charge.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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