

New pay versus performance disclosure requirements coming into effect for issuers providing executive compensation disclosure in accordance with U.S. rules

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The United States Securities and Exchange Commission (SEC) adopted new pay versus performance disclosure requirements which will apply to proxy statements covering fiscal years ending on or after December 16, 2022. Canadian issuers which are required to provide executive compensation disclosure in accordance with U.S. rules, or which choose to follow U.S. rules in satisfaction of Canadian executive compensation disclosure requirements, will need to comply with the new requirements.

Background

The SEC originally proposed pay versus performance rules in 2015 as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The SEC reissued its proposals for comment in 2022 and has now adopted final rules which require tabular and narrative disclosure by public companies of the relationship between amounts “actually paid” to named executive officers and the company’s financial performance.

Requirements

The new rules require a new table disclosing certain executive compensation and financial performance metrics. Under the new rules, issuers must initially disclose this information for their three most recent fiscal years, but the scope of the new rules will increase by a year over each the next two until the disclosure covers their five most recent fiscal years.^[1]

The compensation information to be included in the table is:

- total compensation of the principal executive officer (i.e., the CEO) as reported in the Summary Compensation Table,
- compensation “actually paid” to the CEO.
- average total compensation reported in the Summary Compensation Table for all named executive officers (NEOs) other than the CEO, and
- average compensation “actually paid” to all NEOs other than the CEO.

The financial measures to be included in the table are:

- the issuer's total shareholder return (TSR).
- the TSR of the issuer's peer group, as chosen by the issuer.
- the issuer's net income, and
- a financial performance measure which the issuer considers to be the most important in linking pay and performance.

In addition, the new rules require:

- a description (as a narrative, graphically or both) of the relationships between each of the financial performance measures included in the table and the compensation actually paid to the CEO and the average compensation actually paid to the other NEOs over the disclosure period.
- a description of relationship between the issuer's TSR compared to the TSR of its peer group over the disclosure period, and
- a tabular list of the financial performance measures that the issuer considers the most important in linking pay and performance for the most recently completed fiscal year, which must include the financial performance measure the issuer considers to be the most important in linking pay and performance, may include non-financial performance measures (such as ESG metrics), and may be comprised of multiple lists if different metrics apply to the CEO versus some or all of the other NEOs.

The amount of compensation "actually paid" will be the executive's total compensation from the Summary Compensation Table, adjusted for items such as the actuarial value of pension benefits, the vesting date value of equity awards that have vested, and the yearend fair value of unvested equity awards.

Issuers may provide supplementary disclosure provided that it is identified as supplemental, is not misleading, and is not presented with greater prominence than the required disclosure.

Key implications for Canadian issuers

The new disclosure rules do not apply to foreign private issuers, issuers filing under the multi-jurisdictional disclosure system, or emerging growth companies. However, Canadian issuers whose shares are listed on a U.S. exchange and who choose to provide executive compensation disclosure in accordance with SEC rules in satisfaction of Canadian executive compensation disclosure requirements will have to comply with the new requirements.

Although Canadian issuers who provide executive compensation disclosure in accordance with Canadian executive compensation disclosure rules are not required to provide pay for performance disclosure, some larger Canadian issuers currently voluntarily provide a five-year look-back table showing total direct compensation realized over the past five years. The content of such look-back tables differs from what the SEC requires under the new rules; so Canadian issuers may wish to consider whether to adjust their approach to such disclosure in light of the new SEC rules.

[1] Issuers that are Smaller Reporting Companies (SRCs) are only required to disclose information for the three most recent fiscal years (initially starting with the two most recent fiscal years) and are exempt from certain of the disclosure requirements.