

SEC Issues Third Round of Interpretive Guidance on Pay-versus-Performance Disclosures

November 29, 2023

On November 21, 2023, the Securities and Exchange Commission (the “SEC”) issued eight new Compliance & Disclosure Interpretations (“C&DIs”) and revised two prior C&DIs on the pay-versus-performance disclosures required by [Item 402\(v\)](#) of Regulation S-K.¹ Importantly, one of the revised C&DIs clarifies the meaning of “vesting” for equity awards held by retirement-eligible named executive officers (“NEOs”).

Equity Award Calculations. For each year in the pay-versus-performance table, the SEC’s rules require the issuer to calculate “compensation actually paid” for the CEO and average compensation actually paid for the other NEOs. To calculate compensation actually paid, the issuer starts with total compensation as reported in the summary compensation table and then makes the required adjustments for pension benefits and equity awards. For the equity award calculations, the first fair value disclosure of each award is made in the year of grant, and then changes in the fair value of the award are reported from year to year until the vesting date (or the date the issuer determines the award will not vest). One of the revised C&DIs and two new C&DIs address issues with respect to calculating compensation actually paid:

- **Meaning of “vesting” for awards held by retirement-eligible NEOs.** If retirement eligibility is the sole vesting condition for a stock or option award, the vesting condition is considered satisfied when the holder becomes retirement eligible. However, if retirement eligibility is not the sole vesting condition, other substantive conditions must also be considered to determine when an award has vested. The revised C&DI clarifies that such substantive conditions would include, but not be limited to, a market condition (as described in [C&DI 128D.16](#)) or a condition that results in vesting upon the earlier of the holder’s actual retirement or the satisfaction of the requisite service period. ([C&DI 128D.18](#), as revised)

¹ Our prior [Debevoise in Depth](#) provides detailed Q&As on the final pay-versus-performance disclosure rules, and our Debevoise Updates from [February 2023](#) and [September 2023](#) summarize the first two sets of C&DIs published by the SEC on this topic.

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- **Inclusion of dividends or dividend equivalents in compensation actually paid.** For the equity award calculations, the dollar value of dividends or dividend equivalents paid on stock awards prior to the vesting date should be included in the calculation of compensation actually paid unless dividends or dividend equivalents are already reflected in the fair value of stock awards or included in another component of total compensation. The import of this C&DI is that dividends or dividend equivalents that are accrued and paid on a deferred basis if and when an award vests, rather than reinvested into new awards, may not already be reflected in the fair value of the stock award and may need to be separately included in the calculation of compensation actually paid. ([C&DI 128D.23](#))
 - **If multiple CFOs serve during a given fiscal year, each NEO is included individually in the calculation of average compensation actually paid.** If two (or more) individuals served as CFO during a single covered fiscal year, for purposes of calculating average compensation actually paid to the NEOs other than the CEO, the registrant may not treat the multiple CFOs as the equivalent of one NEO. Each NEO must be included individually in the calculation of the average. The registrant should consider including additional disclosure on the impact of the inclusion of such individuals on the calculation. ([C&DI 128D.30](#))

TSR and Peer Group TSR. The pay-versus-performance table includes cumulative total shareholder return (“TSR”) for the issuer and for a peer group, which can be (1) the same index or issuers included in the stock performance graph in the issuer’s annual report under Item 201(e)(1)(ii) of Regulation S-K or (2) a peer group used in the Compensation Discussion & Analysis to help determine executive pay (a “compensation peer group”). The SEC issued the following guidance on peer group TSR:

- **2023 compensation peer group.** If the registrant uses the same peer group for 2023 as it used for 2022, in the 2024 proxy statement, the registrant should present its peer group TSR for each of the years in the table using the 2023 peer group. If the registrant changes the peer group in 2023 or in subsequent years, it is required under Item 402(v)(2)(iv) to include (a) a footnote explaining the reason(s) for this change and (b) a comparison of the registrant’s cumulative TSR with that of both the newly selected peer group and the peer group used in the immediately preceding fiscal year. ([C&DI 128D.07](#), as revised)
- **Adding or removing issuers from a peer group.** If a registrant that uses a peer group other than a published industry or line-of-business index adds or removes any company from the peer group, Item 402(v)(2)(iv) generally requires the registrant to (a) footnote the reason(s) for this change and (b) compare the registrant’s cumulative TSR to that of both the updated peer group and the peer group used in the immediately preceding fiscal year. However, the comparison described in clause

(b) is not required if (1) an entity is omitted solely because it is no longer in the line of business or industry, or (2) the changes in the composition of the index/peer group are the result of the application of preestablished objective criteria. In these two cases, a specific description of, and the bases for, the change must be disclosed, including the names of the companies deleted from the new index/peer group. This is consistent with C&DI 206.05 applicable to Item 201(e). ([C&DI 128D.27](#))

- **More than one published industry or line-of-business index used under Item 201(e)(1)(ii).** If a registrant uses more than one published industry or line-of-business index for purposes of the stock performance graph under Item 201(e)(1)(ii), the registrant may choose which index it uses for purposes of its pay-versus-performance disclosure. The registrant should include a footnote disclosing the index chosen. If the registrant chooses to use a different published industry or line-of-business index from that used by it for the immediately preceding fiscal year, it is required under Item 402(v)(2)(iv) to (a) explain, in a footnote, the reason(s) for this change and (b) compare the registrant's cumulative TSR with that of both the newly selected peer group and the peer group used in the immediately preceding fiscal year. ([C&DI 128D.24](#))
- **No broad-based equity index peer group.** A registrant may not use a broad-based equity index as a peer group for purposes of the pay-versus-performance disclosure even if the registrant discloses in its CD&A that it determines the vesting of performance-based equity awards based on relative TSR compared to the index. ([C&DI 128D.25](#))
- **Market capitalization weighting required only for a peer group that is not a published industry or line-of-business index.** The pay-versus-performance rules require the returns of each issuer in the peer group to be weighted according to the respective issuer's stock market capitalization at the beginning of each period for which a return is indicated. This requirement is applicable only if the registrant is not using a published industry or line-of-business index pursuant to Item 201(e)(1)(ii). ([C&DI 128D.26](#))

Losing SRC or EGC Status. Finally, two new C&DIs address reporting obligations for smaller reporting companies ("SRCs") and emerging growth companies ("EGCs") that lose their respective SRC or EGC status:

- **Losing SRC status.** Item 402(v)(8) allows SRCs to provide more limited pay-versus-performance disclosures. The SEC staff will not object if a registrant that loses SRC status as of January 1, 2024 continues to include scaled disclosure in its proxy statement filed not later than 120 days after its 2023 fiscal year end from which the registrant's Form 10-K will forward incorporate the pay-versus-performance

disclosure. In this case, the scaled pay-versus-performance disclosure must cover fiscal years 2021, 2022 and 2023.

Any other proxy statement filed after January 1, 2024 must include non-scaled pay-versus-performance disclosure (unless the registrant regains SRC status in subsequent years). A registrant is not required to add disclosure for a year prior to those included in the first filing with pay-versus-performance disclosure. In addition, although a registrant generally is not required to revise disclosure for prior years to conform to non-SRC status, the registrant should include (1) peer group TSR for each year included in the pay-versus-performance table, measured from the market close on the last trading day before the registrant's earliest fiscal year in the table, and (2) its numerically quantifiable performance under the company-selected measure for each fiscal year in the table. The pay-versus-performance disclosure for all fiscal years must be XBRL tagged. ([C&DI 128D.28](#))

- **Losing EGC Status.** EGCs are not required to include pay-versus-performance disclosure in their proxy statements. A registrant that loses EGC status is required to provide pay-versus-performance disclosure in any proxy statement filed after it loses its EGC status. However, the former EGC may take advantage of the transitional relief in Instruction 1 to Item 402(v), i.e., the registrant may provide the pay-versus-performance disclosure for three years, instead of five years, in the first filing in which it provides the disclosure, and may provide disclosure for an additional year in each of the two subsequent annual filings in which the disclosure is required. ([C&DI 128D.29](#))

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Please do not hesitate to contact us with any questions.



Lawrence K. Cagney
Partner, New York
+1 212 909 6909
lkcagney@debevoise.com



Simone S. Hicks
Partner, Washington, D.C.
+1 202 383 8210
sshicks@debevoise.com



Eric T. Juergens
Partner, New York
+1 212 909 6301
etjuergens@debevoise.com



Meir D. Katz
Partner, New York
+1 212 909 6615
mdkatz@debevoise.com



Jonathan F. Lewis
Partner, New York
+1 212 909 6916
jflewis@debevoise.com



Franklin L. Mitchell
Partner, New York
+1 212 909 6104
flmitchell@debevoise.com



J. Michael Snypes, Jr.
Partner, New York
+1 212 909 6319
jmsnypes@debevoise.com



Alison E. Buckley-Serfass
Counsel, Washington, D.C.
+1 202 383 8084
aebuckleyserfass@debevoise.com



Wendy D. Widman
Associate, New York
+1 212 9009 6731
wdwidman@debevoise.com