States and Municipalities Propose CEO Pay Ratio Tax

Looking to raise taxes or to make political statements, several states and municipalities have proposed tax revenue schemes tied to a public company's proxy-disclosed CEO pay ratio.

Although the fate of the CEO pay ratio disclosure may be uncertain, this has not deterred certain states and municipalities from proposing new taxes on public companies tied to a company's disclosed CEO pay ratio (or some variant). In fact, one municipality, the city of Portland, Oregon has enacted such a tax. The Portland law increases its corporate tax rate by 10% for a public company with a CEO pay ratio of 100:1 and by 25% for a public company with a CEO pay ratio of greater than 250:1. Currently, Portland's corporate tax rate is equal to 2.2% on net income derived from business conducted in Portland. Rhode Island and Minnesota currently have proposed tax rules that are substantially similar to the Portland tax provision.

In other jurisdictions, the tax proposals range from the nominal ($2,500 annual filing fee in Illinois) to the material (potential as high as 25% corporate income tax rate in Connecticut) based on the level of a company's proxy-disclosed CEO pay ratio. The Connecticut proposal would result in a maximum combined federal/state corporate income tax rate of 60% on net income derived from business conducted in the Constitution State. Rather than induce companies to reduce CEO pay ratio by increasing workers' pay (or reducing CEO pay), such a confiscatory tax rate would seem more likely to incent public companies to be cautious about doing business in Connecticut.

Some have hailed CEO pay ratio taxes as a means to address income inequality. Others believe these taxes are merely symbolic and will have no meaningful effect on general wage levels (or CEO pay) within a public company. Ultimately, this debate may be rendered moot if the CEO pay ratio rule is repealed as part of any reform of the Dodd-Frank Act or the Securities Exchange Commission indefinitely defers the implementation of the pay ratio rule. One exception is Massachusetts, its proposed tax would require public companies to calculate their CEO pay ratios based solely on U.S. payroll, whether or not the SEC pay ratio rule survives.

If the CEO pay ratio stands, we would expect other states and municipalities to jump on the CEO pay ratio tax bandwagon.

Attached to this Client Update is a summary of currently proposed or adopted CEO pay ratio taxes.

Summary of Proposed and Adopted CEO Pay Ratio Tax

Jurisdiction	Type of Fee or Taxation	Description of Legislation, Regulation or Ordinance	Current Status
Connecticut	Surtax and other amendments to state tax code	▪ Corporate income tax rate is based on CEO pay ratio as follows: — 5% for a ratio of 25:1 or less — 7.5% for a pay ratio of > 25:1 but ≤ 100:1 — 10% for a ratio of > 100:1 but ≤ 250:1 — 25% for ratio of > 250:1 ▪ Eligibility for state financial assistance and tax expenditures is denied to corporations whose CEO earns more than 100× the median employee's wages	Proposed
Illinois	Annual fee	▪ Annual fee is based on CEO pay ratio as follows: — $1,500 annual fee if CEO pay ratio between 100:1 and 250:1 — $2,500 annual fee if CEO pay ratio is > 250:1	Proposed
Massachusetts	Surtax	▪ A 2% corporate surtax is imposed if CEO or highest paid employee, whichever is greater, pay ratio is over 100:1 (based solely on U.S. workforce) ▪ *Note: this surtax is not linked to a company's disclosed CEO pay ratio*	Proposed
Minnesota	Surtax	▪ A corporate surtax is imposed based on CEO pay ratio as follows: — 10% increase in corporate income tax rate if CEO pay ratio is at least 100:1 but < 250:1 — 25% increase if CEO pay ratio is 250:1 or greater	Proposed
Portland, OR	Surtax	▪ A corporate surtax is imposed based on CEO pay ratio as follows: — 10% increase in business license fee if CEO pay ratio is at least 100:1 but < 250:1 — 25% increase in business license fee if the CEO pay ratio is 250:1 or greater	Passed; effective in 2017
Rhode Island	Surtax	▪ A corporate surtax is imposed based on CEO pay ratio as follows: — 10% increase in corporate income tax rate if CEO pay ratio is at least 100:1 but < 250:1 — 25% increase in corporate tax rate if CEO pay ratio is 250:1 or greater	Proposed
San Francisco, CA	Not known yet	▪ City supervisors Jane Kim and Hilary Ronen have requested the City Attorney's Office to draft legislation on a tax related to the CEO pay ratio	Under Consideration

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