Corporate Governance Coalition for Investor Value

March 23, 2017

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: **Acting Chairman Piwowar's February 6, 2017, Statement on the Commission's Pay Ratio Rule**

Dear Mr. Fields:

The Corporate Governance Coalition for Investor Value (the "Coalition") was formed in 2015 to provide a forum for the discussion of issues of common interest among its members to advocate for strong corporate governance policies and federal securities laws that promote long-term value creation for investors and the firms in which they invest. Coalition members represent American businesses of all sizes, from every industry sector and geographic region. These businesses produce goods and services that drive the American economy, employing and creating opportunities for millions of Americans and serving the countless communities nationwide in which the Coalition believes that strong corporate governance policies are important to provide investors with a return on investment and businesses with the capital they need to grow and operate. The Coalition welcomes the opportunity to comment on the final rules issued by the Securities and Exchange Commission (the "SEC" or "Commission") under Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), concerning the pay ratio rule.

The Coalition fundamentally believes that the pay ratio rule:

- Does nothing to advance the Commission's tripartite mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation;

- Fails to provide investors with any kind of material information to inform their decision making;
- Contributes to the phenomenon of "information overload" and makes the public company model even less attractive and;
- Imposes billions of dollars in costs upon public companies and their shareholders, distracts management from their core responsibilities, and provides no benefit to the American capital markets.

Accordingly, the Coalition strongly supports repeal of this inherently political and flawed mandate. Absent full repeal, we believe that there are several ways for the SEC to mitigate some of the more rigid aspects of the final rule. Our concerns and recommendations are laid out in greater detail below.

Discussion

Given the increased attention that investors have given executive compensation in recent years, businesses already disclose vast amounts of information regarding their compensation programs. Businesses clearly understand that investors-for good reason-want to ensure that a company's pay practices are properly aligned with long-term incentives and objectives. Section 953(b) of Dodd-Frank, however, serves no purpose other than to "shame" public companies over their executive compensation practices. It is also worth noting that such use of the SEC's disclosure regime has in other instances been struck down by the courts on First Amendment grounds.[1]

The pay ratio disclosure will in many instances provide a flawed and potentially misleading statistic to investors. Whether a CEO makes 15, 50, or 200 times the amount of the median employee provides no insight as to the CEO's performance or whether the median employee is fairly compensated. It will also be difficult-if not outright impossible-for investors to discern "fair" pay practices across different industries that have varying levels of compensation for rank and file employees. No matter how well the SEC may craft a rule under 953(b), we believe these issues with the mandate cannot be resolved.

[1] *Nat'l Ass'n of Mfrs. v. SEC*, 800 F.3d 518 (D.C. Cir. 2015).

The political agenda behind Section 953(b) has also led to a troubling development that may not have been considered by Congress or by the SEC when they promulgated the pay ratio rule. Several so-called "pay ratio tax" bills have been introduced in various state and municipal jurisdictions around the country. Indeed, the city council of Portland, Oregon recently voted to tax companies doing business in Portland that have a pay ratio the council decrees is too high.[2] These state and local efforts to penalize companies based on their pay ratios provide further evidence that the pay ratio rule has little to do with investor protection and thereby has no place within the federal securities laws.

Based on feedback that the Coalition has received from our member companies which are now actively engaged in the implementation of the pay ratio rule, we understand that many reporting companies have begun to encounter unanticipated compliance difficulties that may hinder their ability to meet the reporting deadline. As we discuss in greater detail below, the final rule suffers from a number of deficiencies, and we continue to believe that the best policy outcome is for Congress to repeal Section 953(b) in its entirety. We acknowledge, however, that the Commission is obligated under law to implement the rule, so the focus of our comments is improving the implementation of the current rule to the fullest extent possible.

- The pay ratio calculation includes part-time and seasonal workers while also permitting exclusion of up to five percent of a company's non-U.S. employees and non-U.S. employees in jurisdictions. Companies are also permitted to exclude employees where information is inaccessible due to data privacy laws, although the requirements for satisfying this exemption are so onerous few if any companies are likely to make use of this ability.

- Most companies that operate internationally face a substantially different labor market and tax regime than in the U.S., which distorts the data and median computations for reasons that reflect the disparity in wages between or among countries.

- Equalizing or harmonizing differences among countries in terms of living

[2] Gretchen Morgenson, Portland adopts surcharge on C.E.O. pay in move vs. income inequality, New York Times (December 7, 2016)

standards or job markets in a rule of this nature is a sheer impossibility.

- There is an underlying assumption in the rule that companies, particularly entities that operate globally, maintain harmonized compensation and payroll databases. This is simply untrue. For international companies, there is a legitimate and necessary business purpose for maintaining purposefully localized payroll systems to allow for distinct and local compensation and benefits customs. Despite this legitimate and necessary business purpose, pay ratio compliance will force companies without a unified database to design and implement an entirely manual data collection process which otherwise serves no legitimate business purpose.

- The conditions accompanying the exemption for companies seeking to exclude foreign employees based on the restrictions of privacy laws in foreign jurisdictions are simply too onerous and costly. First, an issuer must seek an exemption from the local data privacy regulator. We understand that no such process exists in many jurisdictions. Failing an exemption, the final rule requires a registrant to obtain and file with the Commission a legal opinion from counsel in the relevant jurisdiction (an opinion from U.S. counsel would not suffice) regarding the company's inability to comply with the rule without violating the data privacy laws, including the registrant's inability to obtain an exemption or other relief under any governing laws or provisions. The Coalition has been advised by several of its member companies that obtaining the written opinion of counsel in many foreign jurisdictions with respect to this issue will be extremely difficult, if not impossible, particularly in light of the requirement that the opinion be filed with the Commission.

- It is difficult to draw a direct comparison between executive pay and employee pay for a number of reasons. Most CEOs of public companies receive at least a portion (in many cases a majority) of their compensation in the form of equity, e.g., stocks and options, in an effort to align the performance of the company with the CEO's compensation. Equity pay accounted for 68 percent of the reported compensation for the CEOs included in a recent Equilar 200 study.[3]

- Thus, a significant percentage of CEO pay is contingent on the future

[3] See http://www.equilar.com/press-releases/47-200-highest-paid-ceo-rankings.html

performance of the company whereas many, if not most, non-executive employees may not receive company equity as part of their compensation.

Recommendations

In light of the rule's numerous shortcomings, set forth below are suggested modifications to the rule that, absent full repeal, may help reduce its burden on public companies and their investors.

Scope of Employees Included in the Rule

The Commission was granted fairly broad discretion by the statute to determine the employees that issuers would have to include as part of their median pay calculation. Despite the rulemaking flexibility afforded the SEC, the final rule reflects an overly rigid approach that has imposed unnecessary costs on issuers that must comply with the rule. We believe that exempting non-U.S. employees as well as part time and seasonal employees from the median employee calculation would be a useful step towards mitigating some of the negative impact of the final rule.

Additional guidance regarding independent contractors is one area the Commission should address, particularly the scope of their exclusion from the definition of "employee" for purposes of the rule. The definition of independent contractor used in the final rule differs from the definition of independent contractor that is commonly used in the employment law context (as well as IRS guidance). The SEC rule contemplates that most independent contractors' compensation is determined by unaffiliated third parties when, in fact, that only reflects one type of business model or arrangement. Under applicable IRS guidance, [4] for example, whether an individual is deemed an independent contractor for tax purpose should depend on a number of factors including, e.g., behavioral control, financial control, and relationship with other parties. Because more companies categorize employees based on tax status rather than an SEC rule, there would be administrative efficiency in relying on the prevailing standard adopted by the IRS.

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[4] See https://www.irs.gov/taxtopics/tc762.html

We also believe that seasonal/part-time employees and employees who are on a leave of absence or are furloughed should also be excluded from the calculation. To do otherwise will distort the pay ratio and cause companies to incur significant compliance costs. Inherent in the size and complexity of large multinational companies is the fact that at any point in time there are potentially thousands of individuals who are considered part-time/seasonal, on a leave of absence, or furloughed. In the case of employees on a leave of absence or furloughed, the facts and circumstances determination standard contemplated by the SEC may appear reasonable on its face, but companies will incur significant costs in evaluating each and every employee's human resource file to make such a determination.

Exemptions for Certain Non-US Employees

While the SEC recognizes that some countries' data privacy laws or regulations may prohibit the transfer of compensation data outside of a country's borders, the requirements that would have to be met in order for a public company to avail itself of the exemption are simply too burdensome and unrealistic. The rule should merely require that the company make reasonable efforts to obtain the necessary information, documenting such attempts and citing the applicable laws and regulations prohibiting access to such information. Requiring that the registrant seek an exemption from the country's data privacy laws and regulations or obtain a legal opinion from foreign counsel regarding its inability to obtain the necessary information to comply with the rule is costly and unreasonable.

An even more straightforward solution to the problem of including overseas employees would be to permit companies to exclude them from the median calculation altogether. The apparent thrust of Section 953(b) seems to be to spotlight the relationship between pay of American CEOs and pay of American workers. Thus, including non-U.S. workers in the underlying calculation serves no rationale purpose.

Better still, in lieu of requiring companies to engage in an expensive calculation exercise, the Commission should give registrants the option of using industry median compensation data as compiled by the Bureau of Labor Statistics. The Bureau tracks compensation data for over 800 occupations.[5] Doing so will still produce a pay ratio that approximates what would be required under the current system, without the need

[5] Relevant data is available at https://www.bls.gov/oes/.

for companies to engage in costly and unproductive computational exercises to arrive at their own median employee number. Companies that choose this option should be required to disclose that they selected this methodology and provide a brief explanation of why they chose to do so.

Conclusion

It is clear that the costs of complying with the rule far outweigh the alleged benefits. Nevertheless, there are a number of modifications that the Commission could make to the rule to lessen the burden on companies while still achieving its purported objective.

We again request that the Commission not stray from the guiding principle of providing investors with meaningful disclosures and not burden registrants with disclosure requirements that will require a massive undertaking both in terms of labor and system changes for what ultimately will provide no benefit to investors.

We thank you for your consideration of these comments and are available to discuss them further with the Commissioners or staff at your convenience.

Sincerely,

American Insurance Association
The Center On Executive Compensation
National Black Chamber of Commerce
National Association of Manufacturers
Securities Industry and Financial Markets Association
U.S. Chamber of Commerce

cc: The Honorable Michael S. Piwowar
The Honorable Kara M. Stein