Center On Executive Compensation

September 1, 2010

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

RE: Comments on Executive Compensation and Governance Provisions in Title IX, Subtitle E of the Dodd-Frank Wall Street Reform and Consumer Protection Act

Dear Ms. Murphy:

The Center On Executive Compensation is pleased to submit comments to the Securities and Exchange Commission ("Commission") providing its perspective on how the Commission should interpret the executive compensation and corporate governance provisions in Title IX, Subtitle E of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). For the most part, these provisions of the Dodd-Frank Act are unprecedented in their vagueness and breadth, and we urge the Commission to take a practical and Board-centric approach to implementation.

The Center On Executive Compensation is a research and advocacy organization that seeks to provide a principles-based approach to executive compensation policy from the perspective of the senior human resource officers of leading companies. The Center is a division of HR Policy Association, which represents the chief human resource officers of over 300 large companies, and the Center's more than 70 Subscribing Companies are HR Policy members that represent a broad cross-section of industries. Because senior human resource officers play a unique role in supporting the compensation committee chair, we believe our views can be particularly helpful in understanding the important role that carefully constructed executive compensation packages play in ensuring a strong link between pay and performance. Our comments are focused on a practical approach to ensuring that the Commission's implementation of Dodd-Frank Act does not impose significant unintended consequences.

I. Executive Summary

The executive compensation and corporate governance provisions of the Dodd-Frank Act are unprecedented in their breadth and vagueness. The Center believes that in its proposed release or releases implementing these sections, that the Commission should seek practical and workable approaches that reinforce a board-centric view of corporate governance and a company-specific approach to performance-based compensation. The following summarizes the Center's most important views on the issues under consideration in Dodd-Frank.

Say on Pay. The Center urges the Commission to develop guidance quickly so that issuers, particularly those with annual meetings in January and February can understand their obligations under the law. We suggest that the Commission give companies flexibility in structuring the resolutions implementing the periodic nonbinding vote on pay, as it did for TARP companies. More importantly, with respect to the advisory vote on whether say on pay votes should happen annually, biennially or triennially, boards should have the flexibility in whether to offer a vote on all three frequencies or an up-or-down vote on the alternative (e.g., one year) selected by management.

Disclosure and Vote on Change-in-Control Arrangements. The Center recommends that the Commission implement the disclosure requirements applicable to change-in-control arrangements by including in the proxy statement related to the merger, etc., the relevant information from the post-termination disclosures already required under section 402(j) of Regulation S-K in annual proxy statements. In addition, the Center believes the SEC should clarify that a separate shareholder vote is necessary only if the structure of the change-in-control arrangements have changed since the last periodic say on pay vote.

No-Fault Clawback Policy. The Center believes that clawback policies are an important corollary to pay for performance and to risk mitigation. We also believe that to be effective, the clawback policy articulated in Section 954 of the Dodd-Frank Act requires careful consideration of how incentive compensation arrangements are structured so that the proposed release reflects those practicalities. Specifically:

- The Center believes that the clawback policy articulated in the statute applies only to incentive compensation based on financial information required to be reported under the securities laws." Based on this definition, the Center urges the Commission to exclude time-vested stock options and restricted stock from this definition.
- The Center also recommends that the Commission explicitly recognize the role of Board discretion in executing clawbacks of incentive compensation covered by the mandate, especially: where discretion was used in making the award; where the cost of recoupment exceeds the amount to be clawed back; and in determining how to recoup the excess compensation over what would have been received.

Our comments include several examples of common incentive arrangements and address implementation issues, such as the need for the new standards to apply prospectively with sufficient transition.

Disclosure of Pay Versus Performance. The Center believes the Commission should provide flexibility in defining compensation "actually paid," consistent with principles-based disclosure, rather than taking a uniform approach. Companies that grant long-term incentives based on the prior year's performance may view the total annual planned compensation value as compensation "actually paid." By contrast, companies that do not believe that the accounting estimates in the Summary Compensation Table reflect the pay for performance linkages underlying the Board's decisions may disclose how compensation realized in the reporting year links to long-term performance. We also believe that companies should compare compensation "actually realized" to financial performance as determined by the financial metrics used in their incentive plans, but that companies should be allowed to include this in an overall assessment of pay and performance if they choose to do so.

Pay Ratio Disclosure. The Center believes that the pay ratio requirement in section 953(b) of the Dodd-Frank Act makes accurate compliance extremely difficult, if not impossible for global employers because it requires them to individually calculate the pay for "all employees," however defined, using the SEC's requirements for the named executive officers. Within the framework of the statute, we urge the Commission to limit the calculation to full-time U.S. employees and to simplify the calculation to the greatest extent possible. Because of the difficulty of calculating the median under the Commission's executive rules, we urge the Commission to make the ratio a furnished, rather than filed disclosure.

The Center's detailed comments on these issues follow.

II. Shareholder Vote on Executive Compensation Disclosures

Section 951(a) of the Dodd-Frank Act mandates that corporate issuers hold nonbinding shareholder votes on executive compensation once every three years and requires a separate shareholder vote to determine the frequency of such "say on pay" votes. In sum, the Center believes the Commission should interpret this requirement as follows:

- The Commission should be mindful of the influence of proxy advisory firms over shareholder votes such as say on pay and should ensure that advisory firms employ sound methodologies that result in accurate and unconflicted recommendations to institutional investors.
- Issuers should have flexibility in structuring the text of the nonbinding say on pay resolution, so long as the statutory requirements are met.
- Companies should have the flexibility in structuring the shareholder vote on the frequency of say on pay resolutions, either as an up-or-down nonbinding vote on a frequency (one, two or three years) chosen by management or as a vote allowing shareholders to choose whether votes should be held every one, two or three years.
- The statute should be read to prohibit shareholder resolutions seeking a different frequency of say on pay votes. The statute already requires a periodic shareholder vote on the frequency (at least every six years), and the rule of construction in new section 14A(c)(4) should not be read as allowing such resolutions.
- Companies should not be required to file preliminary proxy statements in 2011 merely because they have a say on pay resolution on the ballot.

These issues are discussed in detail in the following paragraphs.

A. Mandatory Say on Pay and the Expanded Influence of Proxy Advisory Firms

As the Commission begins to consider its approach to implementing Section 951 of the Dodd-Frank Act, the Center urges the Commission to be mindful of the impact of proxy advisory firms on the executive compensation process, and the need for these firms to transmit accurate, unconflicted analysis to institutional investors. Many commentators have expressed concern that advisory firm methodologies may cause investors to favor "cookie cutter" pay packages at the expense of company-specific performance-based compensation approaches.[1] Likewise, inaccurate analyses may impact investor proxy votes. For example, Center On Executive Compensation research among its subscribing companies suggests that as much as 10 percent of final reports from proxy advisory firms contain significant inaccuracies that were not corrected.

Because institutional investors can rely on the analysis of proxy advisory firms in making their voting determinations, the advisory firms wield considerable influence over their voting determinations. Although say on pay is an advisory vote, it will still have substantive implications because of the impact a substantial percentage of votes against a say on pay can have on compensation committees. For example:

- Academic research has shown that a negative recommendation on a management proposal can reduce the support of institutional investors by up to 20%;[2]
- Recent statistics from proxy solicitation firm Innisfree M&A found that clients of Institutional Shareholder Services, the largest proxy advisory firm, typically control 20-30% of outstanding shares of mid-cap or large-cap companies, and Glass-Lewis clients typically control 5 to 10%;[3] and,
- A 2010 survey of 251 companies by TowersWatson found that 59% of respondents believed that proxy advisors have significant influence over pay decision making processes at U.S. companies.[4]

If a proxy advisory firm recommendation is based on a flawed methodology or inaccurate information, executive compensation could be affected considerably at some companies. The purpose of a shareholder advisory vote should be to obtain the views of shareholders on executive compensation practices, not to further cement the influence of proxy advisory firms over executive compensation. We urge the Commission to take action, through its review of the proxy voting process, to more closely oversee and regulate the industry so that analyses are unbiased, reports are accurate, and votes are not improperly influenced.

B. Give Companies Flexibility in Structuring Say on Pay Resolutions

The Center believes that the Commission should provide companies with flexibility in how they structure the text of the nonbinding resolution on pay, so long as the statutory requirements are met. The statute requires the resolution be simply "to approve the compensation of executives" as disclosed in the Commission's executive compensation disclosure rules in Item 402 of Regulation S-K. The Center recommends that the SEC follow an approach similar to the one it adopted for companies subject to a say on pay vote under TARP, which allowed companies considerable flexibility to discuss why shareholders should approve the resolution.

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[1] *See, e.g.,* Jeffrey Gordon, "Say on Pay: Cautionary Notes on the UK Experience and the Case for Shareholder Opt-In," 46 Harvard J. on Leg., 323 (2009); Peter C. Clapman, "Next Steps? Be Careful What You Wish For," Directors and Boards, July 2008.
[2] *See, e.g.,* Jennifer E. Bethel and Stuart L. Gillan, "The Impact of the Institutional and Regulatory Environment on Shareholder Voting," Financial Management, Vol. 31, No. 4 (Winter 2002).
[3] Yin Wilczek, Bounty Program to Cramp Corporate Boards; ABA Speakers Discuss Governance Provisions, Daily Report for Executives (BNA), Aug. 10, 2010, at EE-4.
[4] Towers Watson Press Release, "Few U.S. Companies Well Prepared for Executive Say-on-Pay Legislation, Towers Watson Survey Finds," June 29, 2010.

C. The Frequency Vote Should Allow an Up or Down Vote, Not Merely A Multiple Choice Approach

New sections 14A(a)(2) and (3) require a separate management resolution allowing shareholders to vote to determine whether say on pay votes will be held every one, two or three years. The vote is to occur in the first year say on pay is applicable and at least every six years after that. The Center believes that Board flexibility in implementing the "frequency vote" is important to a board-centric approach to governance and is not inconsistent with the statute. We believe that the Commission should allow boards to decide whether there should be an up-or-down vote on a management recommended frequency (i.e., management could offer a resolution that recommends that the shareholder vote should occur every year, and shareholders would vote up or down on the resolution) or whether shareholders would be provided with a choice among having a say on pay vote every one, two or three years. For legal, practical and procedural reasons, we believe that allowing a choice is the preferable approach as opposed to mandating that shareholders be only allowed to choose among one, two or three years.

<u>The Frequency Vote Is Nonbinding</u>. One important reason the Commission should adopt flexibility on the frequency vote is that a plain reading of the statute indicates that the frequency vote is nonbinding, just as the actual say on pay vote is, and we recommend that the Commission confirm the plain language reading in its proposed rules. The rule of construction in new section 14A(c) states "The shareholder vote referred to in subsections (a) and (b) *shall not be binding* on the issuer or the board of directors of an issuer" and section 14A(c)(1) states that the vote "*may not be construed as overriding a decision by such issuer or Board of Directors.*" Because the frequency vote is advisory, management should be allowed to propose a selected frequency and have shareholders support, oppose or abstain from it, as well as provide for a choice among three alternatives.

The Center also believes that it is important that in its regulations implementing the mechanics of the say on pay and frequency votes, the Commission distinguish between the language of the statute in describing the votes and their actual impact. Section 14A(a)(1) states that the say on pay resolution is "to *approve* the compensation of executives," but read together with Section 14A(c),which states that the vote is nonbinding, it is clear that shareholders are not actually approving executive compensation but providing their general views on executive compensation. Similarly, with respect to the frequency vote, section 14A(a)(2) states that the proxy shall include a "separate resolution subject to shareholder vote to *determine*" whether say on pay votes will take place annually, biennially or triennially. Because the frequency vote is nonbinding, shareholders are not actually determining the frequency but providing their input on frequency, with a decision to be made by management, and this should be made clear in the implementing release.

<u>A Management-Determined Resolution Is Consistent With Existing Commission Rules</u>. The Commission's current rules provide that shareholders may not have a choice on a shareholder resolution other than to vote for, vote against, or abstain. The Center believes that new Section 14A(a)(2), should be read as being consistent with the rules and as giving management a choice between applying the existing rules, allowing companies to choose among one, two or three years or providing shareholders a choice from among the options. From a

practical perspective, allowing a "multiple choice" approach makes it possible, if not likely, that none of the three alternatives will win a majority of votes, leaving the direction to management uncertain. Even though it is possible shareholders will not support a management resolution seeking an up or down vote on frequency, a rejection would give management clear direction as to the will of the shareholders.

The Commission Should Ensure That the Proxy Voting Industry Can Handle a Three-Way Vote. In addition, the Commission should seek comment from the proxy distribution and tabulation firms in its proposed implementing release whether these firms will have their proxy cards and computer systems ready for the first shareholder meetings after say on pay takes effect on January 21, 2011.[5]

Management Should Be Allowed to Recommend a Vote Frequency. Regardless of how the say on pay resolution is framed, just as with any management resolution, management should be allowed to recommend the frequency of the say on pay vote it would prefer and provide its reasons for that choice. From a practical side, management is in the best position to recommend how frequently say on pay votes should occur based upon the nature of their business cycles, strategies and the related compensation program designs which reflect those considerations. For example, it may be that a company in an industry with long lead times may recommend a less frequent say on pay vote, but one with shorter cycles may propose a shorter frequency for the shareholder vote.

D. The Statute Should be Read to Prohibit Shareholder Resolutions Seeking Alternative Voting Frequencies

The Center believes that new section 14A should be read as preempting shareholder proposals seeking more or less frequent votes on say on pay than management has implemented. The statute has put in place a system for obtaining shareholder input on the frequency of the vote and specifies that shareholders be given the opportunity to vote on the frequency at least every six years. Thus, the Center believes that the combination of a mandated vote on pay and the mandate that shareholders be allowed to vote on the frequency of the vote fully occupies the space on this issue. Any subsequent shareholder resolutions in this area should be considered "substantially implemented" as a result of the statutory requirements.

Allowing for annual shareholder resolutions asking companies to change the frequency of the shareholder vote (either more or less frequently) is redundant and overly burdensome, given the cost of assessing the propriety of a resolution, engaging the proponent, fashioning a response and then publishing the resolution in the annual proxy. Moreover, because there is evidence that institutional investors disagree over the best frequency of a say on pay vote,[6] it is possible that in

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[5] An informal review of Center Subscribers showed that five out of 67 companies that are U.S. publicly traded companies have annual meetings scheduled between January 21, 2011 and March 15, 2011, or just over seven percent of total Subscribers. Extrapolating this figure to the roughly 1,600 corporations deemed large accelerated filers, there would be roughly 119 companies holding annual meetings during that period.

[6] *See, e.g., "Say on Pay" Rolls Forward, But Some Investors Wary*, Reuters, July 22, 2009, *last viewed at* http://www.reuters.com/article/idUSTRE56L52O20090722 (stating the United Brotherhood of Carpenters "has proposed holding say-on-pay votes every three years rather than annually, and only at the largest U.S. corporations. It says this would give investors more time to assess pay plans, which must be reviewed individually because

any given year, a company could receive two resolutions seeking alternative time frames (e.g., a company that has chosen to hold a say on pay vote every two years could receive resolutions seeking say on pay votes every year or every three years).

In addition, nothing in the statute prevents a company from proposing a resolution on the frequency of say on pay more often than every six years. If a company determines that there is a groundswell of support among shareholders for changing the frequency of the vote, it can choose to offer a resolution proposing a different frequency.

The Center believes that this interpretation is consistent with the rule of construction in section 14A(c)(4), which states that the shareholder vote "may not be construed to restrict or limit the ability of shareholders to make proposals for inclusion in proxy materials *related to executive compensation*." The Center believes that shareholder proposals seeking a more or less frequent vote on executive compensation are not "related to executive compensation" as contemplated by the statute because they do not seek to address a specific aspect of compensation. Instead the resolution is related to the process of the Board, specifically, how frequently the company will hold a statutorily mandated vote.

In addition, the SEC has long allowed exclusion of shareholder proposals under Rule 14a-8 that would conflict with a management proposal. The staff's analysis recognizes that the Board would not know how to respond if, for example, conflicting proposals each receive a majority vote.[7] Allowing shareholder proposals in this case would appear to create the potential for such conflicts.

In sum, the Center believes that the Commission should exclude shareholder proposals seeking a different frequency of the say on pay vote than that implemented by the company. The statute provides a clearly established process requiring the company to reevaluate the views of shareholders on the frequency of the say on pay vote every six years. In addition, the Center believes that the exclusion of such votes is permissible under the section 951 rule of construction.

E. The Commission Should Not Require Companies to File Preliminary Proxy Statements

The SEC should not require companies to file a preliminary proxy statement in 2011, merely because they have a say on pay resolution on the proxy. This is consistent with the interpretation the SEC took for TARP companies, and it should apply equally in this case. Because the say on pay requirement will apply to nearly all publicly held companies in 2011, the preliminary proxy filing requirement would shorten the amount of time companies have to tailor their disclosures in advance of the first say on pay vote. Moreover, as a practical matter, it is difficult to imagine that the staff would have the time or resources to review more than a very small percentage of preliminary statements filed.

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policies on calculating an executive's salary, bonus, stock options, perks and retirement benefits vary widely."); AFSCME and Walden Asset Management Press Release, "More Than 50 Companies Voluntarily Adopt "Say on Pay" as Institutional Investors Continue to Press for an Advisory Vote," March 2, 2010, *last viewed at* http://www.afscme.org/press/27802.cfm. ("Investors pushing for annual advisory shareholder votes on executive compensation today announced that more than 50 companies have now voluntarily adopted giving their shareholders *an annual advisory vote* on executive compensation, colloquially known as "Say on Pay.") *emphasis added*.

[7] Rule 14a-8(i)(9).

III. Disclosure and Shareholder Vote on Certain Golden Parachute Payments

Section 951(b) of the Dodd-Frank Act requires public companies who enter into a merger, change-in-control, purchase, etc., to provide additional disclosure “in a clear and simple form” of any agreements or understandings the company has with the NEOs of either company (whether present, deferred or contingent). It also requires a separate nonbinding shareholder vote on the change-in-control arrangements where the arrangements have not been previously included as part of a say on pay vote.

A. Additional Disclosure Requirement Should Incorporate Approach From Existing Post-Termination Payment Disclosure

The Center believes the Commission should address the additional disclosure requirement by simply incorporating the current disclosures for post-termination payments in Section 402(j) of Regulation S-K, which companies currently are required to include in their annual proxy statements, in proxy statements related to merger or change-in-control agreements. The current disclosures address the statutory requirements and provide for consistency in reporting annual compensation and compensation in the event of a merger/change-in-control. This approach also will make it clear to shareholders whether there have been material changes in the structure of change-in-control agreements, thus enabling them to determine whether a separate shareholder vote on the change-in-control payments is warranted.

B. Shareholder Vote Should Only Be Required If Structure of Payments Has Changed Since Last Say on Pay Vote

The Center believes the SEC should clarify that a separate shareholder vote is necessary only if the structure of the change-in-control arrangements have changed since the last periodic say on pay vote. There should not be a separate vote merely because the value of the change-in-control agreement changes due to stock price fluctuations or changes in performance levels affecting other metrics. Otherwise, the statute’s requirement that a separate vote be held only when there have been changes in the agreements or understandings related to the change-in-control arrangement would be meaningless. A contrary interpretation – i.e., that a say on pay vote be held any time the amounts of executive compensation payments that are projected to result from a change-in-control agreement differ from previously disclosed amounts require a separate shareholder vote each time there is a merger, acquisition, or combination.

Finally, in the event where only certain elements of a change-in-control agreement are added or changed, the shareholder vote should focus on the elements that have been changed.

IV. No-Fault Clawback Policy

Section 954 of the Dodd-Frank Act requires the SEC to promulgate rules directing the securities exchanges and securities associations to develop listing standards requiring companies to adopt and disclose a no-fault clawback policy. Specifically, the policy to be disclosed must provide, in the event of a material restatement, for the recoupment of incentive compensation that is “based on financial information required to be reported under the securities laws” from current and former executive officers of the company, if such compensation is in excess of that which would have been paid in view of the restatement. This mandate raises a number of issues, including:

- which compensation is "based on financial information required to be reported under the securities laws;"
- the mechanics of determining the amount to be recouped in the event of a material restatement;
- the role of board discretion in executing the recoupment policy, particularly where board discretion was applied in originally awarding the incentive compensation; and
- the need to provide companies with sufficient lead time to implement a policy before the clawback mandate takes effect.

Each of these examples is discussed below.

A. Clearly Delineate Compensation Subject to the No-Fault Clawback Policy

The linchpin of the requirement in section 954 of the Dodd-Frank Act is that companies are required to disclose and enforce a policy that provides for recoupment of incentive compensation that is "based on financial information that is required to be reported under the securities laws." Thus, if incentive compensation is "based on" financial results that are reported under the securities laws, it is potentially subject to recoupment. Consistent with principles-based disclosure and recognizing the complexity of issues that are created by the language of the statute, the Center believes that in its proposed release the Commission should differentiate incentive compensation that is subject to the recoupment requirement from compensation that is not subject to it. This will enable Boards of Directors and Compensation Committees charged with enforcing it to better understand their obligations.

Financial information that is required to be reported under the securities laws includes measures such as revenue, net income and earnings per share. It also may include non-GAAP measures such as earnings before interest, taxes, depreciation and amortization and return on net assets.

Incentive information that is not required to be disclosed under the securities laws includes stock price, total shareholder return (which is based on the change in share price plus dividends over a period of time) and operational performance measures specific to the business such as market share and customer satisfaction. Such measures are not financial information that is filed with the SEC and therefore would not be subject to clawback under section 954.

The Center believes that it is important for the Commission to understand how incentive plans are structured, so that it may factor this information into its proposed regulations. Although compensation arrangements vary widely, depending upon the company, industry, competitive condition and global focus, below we present five hypotheticals, illustrating four common types of compensation arrangements:

(1) Purely formulaic incentive plans, based on financial metrics, that pay out in cash;

(2) Formulaic incentive plans in which a pool is funded based on the achievement of objective financial measures, but the board has discretion whether to allocate the entire bonus pool toward incentives, where a recoupment would not be required;

(3) Identical to (2), except the facts change so that recoupment is required;

(4) Formulaic long-term incentive plans based upon financial performance with overlapping awards; and

(5) Nonqualified stock option grants, that are not granted or vested based upon performance.

Annual and Long-Term Cash Incentive Measures Based Upon Financial Metrics. The implementation of the recoupment policy is easiest when dealing with incentive plans that are purely formulaic, based exclusively on financial measures, and paid out in cash. In that situation, the clawback is the excess of what was actually received compared to the amount that would have been received under the formulaic plans had the financial statements been correct.

Example 1: Formulaic Incentive Plan With Incentives Based on Financial Metrics

- Annual bonus is based on achievement of targeted level of net income.
- The performance for 2009 equaled 105% of the targeted level of net income.
- The incentive formula increases payout by 3% for each 1% by which performance exceeds the target.
- The payout at 100% performance is 50% of salary.
- The payout based on the performance results would be 115% of the targeted payout.
- 115% of 50% of salary would produce an annual incentive payout of 57.5% of salary.
- Assume the performance results for 2009 had to be restated in 2011 and the impact was to reduce net income to 90% of the targeted level of performance.
- The incentive formula reduces payout by 3% for each 1% by which performance falls short of target.
- The incentive payout on the restated earnings would have been 70% of the targeted payout of 50% and would have produced an incentive payout of 35% of salary.
- The amount of annual incentive that would be clawed back would be the difference between what was paid (57.5% of salary) and that which would have been paid on the restated earnings (35%), which would equal 22.5% of salary.
- Assuming the executive had a salary of $500,000, the bonus amount to be clawed back would equal $112,500 (the difference between an incentive of $287,500 at 57.5% of salary and an incentive of $175,000 based on 35% of salary).

Formulaic Incentive Plans Where Financial Measures Fund a Bonus Pool. Where the financial measure funds a pool which is distributed based upon financial and non-financial measures, the application of the clawback policy will differ based upon whether the Board and/or the Compensation Committee had discretion in determining how much of the pool to allocate for incentives and whether the Board and/or the Compensation Committee has discretion in determining the individual awards.[8] Assuming the Board or Compensation Committee had discretion in determining the amount of the bonus pool to allocate to individual awards and the individual awards are determined based upon some measures that require the judgment of the board (rather than formulaic), a material restatement could require the Board to revisit its decisions. Examples 2 and 3 illustrate the pool concept and the role of Board discretion:

Example 2: Incentive Pool Approach With Restatement; Recoupment Not Required

- The annual incentive pool is generated based upon a percentage of net income, and at targeted level of net income for 2009 the pool would be sufficient to provide incentives equal to the sum of the incentive targets for the participating executives.
- The amount of incentive payout any individual would receive is based upon his or her individual performance against non-financial objectives in the areas of (1) talent development, (2) productivity and cost-savings, (3) operational performance measures and (4) modeling the desired company culture and promoting ethical behavior (weighted 25% each).
- In total the payouts to executives cannot exceed the incentive pool, but there is no requirement that the board allocate the entire pool to incentive payments.
- For 2009, the company hit 100% of the net earnings target, and the incentive pool was generated on that basis.
- The board allocated 95% of the pool for incentives.
- No executive received an incentive payment directly based upon the achievement of the net income target. Some executives received incentive payments above their targeted incentive; some received less than their targeted level of incentive and some received their targeted level of incentive. The amount received by an individual executive was based on the assessment of performance in the four areas listed above.
- Assume the performance results for 2009 had to be restated in 2011, and the impact was to reduce net income such that the incentive pool equaled 98% of the sum of the incentive targets for the participating executives.
- At this restated level of performance the bonus pool was sufficient to cover the actual amount of incentives paid (98% pool, 95% actually paid out).
- In this situation there does not appear to be a need to recoup any of the incentives paid unless the board determines it would have made different individual incentive decisions in view of the restated earnings.

[8] If the Board does not have discretion (i.e., the bonus pool and the individual awards are formulaic), the clawback would be applied similar to Example 1 for the portion of the award based on the restated financial performance.

Example 3: Incentive Pool Approach; Recoupment Required

- Same as Example 2 but the restated earnings would have produced an incentive pool equal to 90% of the sum of the incentive targets for the participating executives.
- The Board has three options regarding how to recoup the 5% that exceeded the amount allocated to the incentive pool.
  - Ratably reduce all executive incentives by 5% (non-discretionary recoupment although the incentive paid to each individual was based on board discretion);
  - Discretionary recoupment on an individual-by-individual basis (the same way the bonus amounts were awarded) such that the total amount recouped equaled the 5% overpayment (discretionary recoupment);
  - Recoupment is left to the discretion of the board, pursuant to the company's recoupment policy.

The Center believes that the Commission should recognize the need for Board discretion in such situations. Thus, the Board should have the ability to decide to use any of the three options, so long as its rationale is explained in the company's next proxy statement.

<u>Overlapping Long-Term Awards and the Impact of a Material Restatement on Target Setting</u>. Long-term incentives are often three-year awards granted annually so that the awards are overlapping. In this situation a material restatement, and any required recoupment could affect up to four cycles of long-term incentive grants (the three outstanding performance cycles, plus the basis for setting the next award depending on whether the financial measures included in the restatement affect the long-term incentive program and also serve as the base year for setting performance targets for the next award). Example 4 illustrates the mechanics of this model:

Example 4: Overlapping Long-Term Incentive Awards

- Assume that Performance Unit Awards are granted annually and have the following design:
  - Units are denominated as a dollar amount (e.g., $100,000 value for achieving targeted performance).
  - Performance in excess of the targeted level of performance increases the payout by 3% for each 1% by which targeted performance is exceeded.
  - Performance that falls short of target reduces the payout by 3% for each 1% shortfall in performance versus targeted level of performance.
  - The performance metric is cumulative earnings per share (EPS) over the three-year performance period.
- Since the awards are granted annually, and given that the performance period is three years, a participant will have 3 overlapping awards outstanding at any given time.
- Therefore, a given year will be included in three separate award cycles and, depending how performance targets are set, may serve as the base year upon which the performance targets for a 4th award cycle are set.

- Outlined below is an example of the outstanding awards under a performance unit program:

	2007	**2008**	**2009**	**2010**	**2011**	**2012**
2007 Award:	2007-------	2008------	2009			
2008 Award:		2008------	2009-----	2010		
2009 Award:			2009-----	2010---	2011	
2010 Award:				2010---	2011-------	2012

- Assume that in mid-2010 the company materially restates downward the earnings for 2009, thereby reducing 2009 EPS.
- The impact of the restatement would be to reduce the performance for the 2007, 2008 and 2009 award cycles.
- The restatement would also lower the base year upon which the board set the EPS targets for the three-year award cycle beginning in 2010.
- The 2007 awards would have been paid out to the participants and therefore the company would have to initiate recoupment for the excess payment that was based on the pre-restated 2009 EPS.
- The 2008 and 2009 award periods would not yet have been completed and therefore the potential payout of the performance units would be automatically reduced. No recoupment would be required.
- The board should also revisit the targeted cumulative EPS goals for the performance cycle beginning in 2010 to determine if the goals would have been set at a lower level had the board been aware of the restated EPS for 2009 at the time the goals were set.

Performance-Granted and Performance-Vested Equity Awards. Section 10D(b)(2) of the statute states that the clawback policy applies to "incentive-based compensation (including stock options awarded as compensation)." The Center believes this language should be read as requiring that the clawback policy applies to (1) incentive-based compensation as defined under the Commission's disclosure rules that is based upon information required to be reported under the securities laws; and (2) stock options that are awarded as compensation and that are incentive-based compensation as defined under the Commission's disclosure rules where the incentive is based on financial information required to be reported under the securities laws. This approach makes the clawback language in section (b)(2) consistent with the reporting language in (b)(1), which requires companies to disclose the policy of the company on recoupment of incentive-based compensation under the securities laws.

Applying this interpretation, the Center believes that performance-granted and performance-vested equity awards can be incentive compensation subject to the recoupment mandate, if the above definitions are met. Unlike nonqualified time-vested stock options, restricted stock or restricted stock units, which are not considered incentive compensation under the Commission's rules, performance-granted or performance-vested stock options, for example, are incentives that are often granted based on financial performance or other performance measures.

Time Vested Stock Options. Stock options generally take one of two forms: (1) performance-based stock options for which the granting or vesting of the award is based on the achievement of financial performance, as discussed above or, (2) time-vesting stock options for which the award is based on considerations other than financial performance and the vesting of such awards is based on the passage of time and is not contingent on achieving financial performance objectives. Stock options that vest merely on the basis of time are not considered incentive compensation under the SEC's disclosure rules and therefore should not be subject to a mandatory clawback. Many companies determine the level of stock options granted to an individual based on the executive's level, tenure and expected performance level, which are not linked to financial performance. In this case the following example should apply:

Example 5: Stock Option Awards

- Stock option awards are determined on an executive-by-executive basis.
- The actual award received is a function of salary grade, title, performance and potential.
- The determination of the performance of an individual executive for purposes of granting stock option awards is not tied directly to the financial results of the overall company.
- The option awards granted in 2006 have vested but the executives have not exercised the stock options.
- Assume the results for 2006 were restated in 2009 and the net income of the company was reduced by 1%.
- Correspondingly, the stock price dipped on the day of the restatement by 10% and has recovered over subsequent weeks but the recovery in stock price has trailed the overall movement of the market and the stock price appreciation of industry peers.
- In view of the fact that there has been no gain to the executives since the options have not been exercised, and in view of the fact that the size of the grant was not influenced by the net income of the company, no recoupment is warranted.
- An alternative stock option design would be a stock option that vests on the basis of achieving financial targets. In this case, the number of stock options that would not have vested based on the restated financial performance outlined above would be subjected to recoupment due to the material restatement.

In sum, the Center believes that the better way to interpret the clawback language in section 954(b)(2) is to consider any incentive compensation that is awarded, granted or vested based on financial measures required to be reported under the securities laws as subject to recoupment. Conversely, vehicles such as time vested stock options, restricted stock and restricted stock units should not be considered incentive compensation, and if the granting of such awards was not based on the restated financial performance, it is therefore not subject to the clawback requirement. However, if the granting of individual stock option awards is based on the restated financial performance, the number of shares awarded would be subject to the clawback based on the excess of the award over that which would have been awarded based on the restated financial performance.

B. The Commission Should Provide for Board Discretion in Executing the Recoupment Policy

In implementing the clawback requirement, the Commission should recognize the role that Board or Compensation Committee discretion plays in setting executive compensation, and explicitly provide for Board and Compensation Committee discretion in the determination of the amount to be recouped and how that recoupment is to be executed. This interpretation recognizes that Board discretion often plays a role in how incentive compensation is awarded and allows the Board to make determinations to ensure that the recoupment is in the best interests of shareholders.

<u>The Level of Discretion Used by the Board/Committee in Determining Amount to Be Clawed Back Should Be the Same as That Used in Making Original Grant</u>. Boards should be given the same level of discretion to determine the amount to be clawed back as was used in making the initial compensation decision. As illustrated in the examples above, this may involve discretion under section 162(m) incentive plans in which financial performance funds a pool to be used for the distribution of compensation to NEOs or other executive officers. Committee discretion may also be used in applying other financial criteria used to make individual awards.

Board or Committee discretion is also increasingly an element of a company's risk mitigation system. Affording the Compensation Committee discretion allows it to reduce (or add) incentive payouts, when the committee takes the entirety of the circumstances into account. In addition, long-term incentive grants, whether granted on a value or a number of shares basis, are often made based on a formula, to which Committee discretion is applied in determining the actual grant.

<u>Discretion Not to Claw Back Where the Cost of Executing the Clawback Would Outweigh the Benefits to Shareholders</u>. The Center believes that in addition to discretion as discussed above, the Commission should recognize that Boards should have discretion in determining not to execute a clawback against a current or former executive officer where, for example, the amount to be clawed back is de minimis or the Board believes that protracted litigation would be required to recoup the compensation. In cases such as this, the Center believes the Commission should explicitly recognize the Board's ability to decide not to claw back and to disclose that decision in the proxy. This is especially important with respect to executive officers in certain countries or other jurisdictions that are extremely protective of employees, where it may not be possible to recoup the entire amount. For similar reasons, in crafting its proposed release, the Commission should consider situations in which a Board would be permitted to settle a clawback for less than the full amount.

<u>Discretion in Determining How to Recoup Compensation From a Current Or Former Executive Officer</u>. The Center believes that since the statute is silent as to how clawbacks are to be executed, the Commission should explicitly recognize Board/Compensation Committee discretion in executing recoupment by any method the Board deems to be appropriate (and

discloses in the next proxy statement), including cancellation of unvested awards (equity and nonequity awards) and offsetting against amounts otherwise payable by the company to the executive (for example, deferred compensation) in place of having executives write a check, if the circumstances warrant. This flexibility helps to mitigate some of the procedural complexities involved in executing a clawback, including the need to file amended tax returns by both the company and the executives.

C. The Three-Year Recoupment Period Should Be Linked to the Restatement Filing Date

The Center also believes that the trigger for recoupment (i.e., when a company is "required to prepare an accounting restatement") should be when the company actually files an accounting restatement due to the material noncompliance of the company with a financial reporting requirement under the securities laws. This creates a verifiable date certain from which to determine the three-year period over which the recoupment applies. It also avoids speculation over when a company determined it should have known it was required to prepare a restatement.

The Center encourages the Commission to exclude restatements based on changes in Generally Accepted Accounting Principles from the types of restatements that trigger a recoupment. These restatements are not based on oversights or deliberate errors by the company, but rather a change in the framework for reporting. Mandating a recoupment in such circumstances does not fulfill the policy objective sought by the clawback mandate: namely, if an executive did not earn incentive compensation based on financial results, he or she should be required to return it.

D. Include Sufficient Lead Time to Implement the New Clawback Requirements

The Center urges the Commission to provide in its implementing release that the clawback policy will apply only to any new incentive compensation that is received after the effective date of the listing standards approved by the Commission. To apply the recoupment policy to compensation already granted would create excessive complexity in term of amendments required to outstanding compensation plans and executive contracts.

In addition, the Center believes that the Commission should give companies sufficient time to put such policies into place prior to the effective date of the listing standards incorporating the disclosure and recoupment obligation taking effect because of the considerable number of issues, such as plan amendments and contract renegotiation that must be addressed. We believe that a reasonable time is 12 months after the Commission approves the listing standards.

V. Disclosure of Pay Versus Performance

The Center believes that the Commission should interpret the additional disclosure required by new section 14(i)(a), entitled Disclosure of Pay Versus Performance, by taking an approach consistent with principles-based disclosure that recognizes the need for flexibility in properly portraying the unique aspects of individual company pay philosophies, programs and decisions. The statute requires companies to disclose "information that shows the relationship between compensation actually paid and the financial performance of the issuer, taking into account any change in the value of the shares of stock and dividends of the issuer and any distributions." We believe this disclosure should reinforce the purpose of the CD&A, namely to "put into context the compensation disclosure provided elsewhere."[9]

With this in mind, the Center believes this disclosure should reflect the Board's and Compensation Committee's perspectives on compensation and financial performance in making its compensation decisions. Rather than focus on uniform disclosure, the requirement in new section 10(i) should be interpreted to focus on explaining the link of compensation "actually paid" to performance, allowing companies the flexibility to explain the committee's decisions in the context of its overall pay philosophies.

Definition of Compensation "Actually Paid." We believe that the determination of "actually paid" will vary based on how the Compensation Committee and the Board structured the performance basis of incentive compensation granted to executives. This is consistent with the requirement that the CD&A "focus on the material principles underlying the registrant's executive compensation policies and decisions and the most important factors relevant to analysis of those policies and decisions."[10]

Because much of the CD&A focuses on the amounts in the Summary Compensation Table, the intended performance linkage between pay and performance may not be clear from the amounts in that Table, depending upon the philosophy of the company, especially with respect to long-term incentives. The linkage between pay and performance is fairly consistent as it relates to salary and annual incentive because the amounts realized are reported in the same year as the corresponding performance. However, the design of long-term incentive plans can vary considerably among companies depending on the basis upon which awards are granted, performance periods, performance objectives and incentive vehicles used.

Long-term Incentives as Awards for Past Performance. For example, a Compensation Committee may grant long-term incentives as a reward for past performance. In this case, the grant date fair value estimate for long-term equity-based incentives in the Summary Compensation Table more appropriately reflects the decisions made by the Compensation Committee and the Board and thus the linkage between compensation "actually paid" and performance.

Example 1: The Company has a tremendous year in terms of financial performance and the senior executive team is granted above guideline stock option awards to reflect the accomplishments of the prior year in the total planned annual compensation value. In this case, the Compensation Committee and the Board would discuss the relationship between the financial results and the date of grant value of the stock option awards, as reported in the Summary Compensation Table, when combined with other forms of incentive compensation reported in the Summary Compensation Table, as reflecting the relationship of pay and performance. If performance had been below expectations, a lower planned grant value could result. This pay for performance philosophy is in large part backward looking in that long-term incentive grants are the result of past performance.

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[9] U.S. Securities and Exchange Commission, Executive Compensation and Related Person Disclosure, Release Nos. 33-8732A, 34-54302A, 71 Fed. Reg. 53,157, 53,164 (September 8, 2006).
[10] *Id*. at 53,242.

Alternative: Realized Compensation as "Actually Paid." By contrast, some companies are concerned that the long-term incentive estimates disclosed in the Summary Compensation Table do not completely reflect the pay for performance linkage underlying the committee's decisions. As a result, they may choose to put those amounts into context by discussing how compensation actually realized -- the compensation actually received by the executive at the end of the performance period based on the degree of achievement of the underlying performance objectives -- is the proper reflection of pay for performance rather than grant date value of the award.[11] This approach requires an explanation of how pay and performance were linked over the period the awards were outstanding and gives shareholders a sense for how such forward-looking incentive programs operate in practice.[12]

Example 2: The Company is in a turnaround situation and the Compensation Committee believes that it is important to grant a market-competitive level of long-term awards to the executive team to motivate them to improve the performance of the company. In this case the philosophy of the company is that the link between pay and performance is best reflected based upon the pay that will be actually realized by the degree to which performance goals are achieved and the long-term awards create gains to the executives. This pay for performance philosophy is forward looking in that future performance will determine the pay received from the performance-contingent awards.

Some companies have begun disclosing the realized value of long-term incentive amounts in a table, similar to the following (which is separate from example 2):

Form of Compensation	**Total Received ($)**	**Annualized Amount**	**Performance Results Over Performance Period That Produced the Compensation**
• **2008-10 LTIP Payout**	$3,384,275	1,128,092	The total 2008-10 Long Term Incentive Plan award was $3,384,275. Performance criteria for this award were: (1) Total return to shareholders vs S&P Industrials Index companies, weighted 50%, for which the company ranked in the top 25 percent of companies, producing a near maximum payout for this component. (2) ROIC, weighted 25%, which exceeded the targeted level by 100%, resulting in maximum payout; and (3) Cash flow, weighted 25%, which exceeded the target by 15%, which resulted in a target payout. Overall the payout represented 150.25% of target.

[11] This approach is also reflective of the way the Commission has distinguished estimates of compensation included in the Summary Compensation Table and compensation earned and paid out in the preamble to its 2006 disclosure release. *See, e.g.,* U.S. Securities and Exchange Commission, Executive Compensation and Related Person Disclosure, Release Nos. 33-8732A, 34-54302A, 71 Fed. Reg. 53,157, 53,169 (September 8, 2006) ("This table, as amended, shows the named executive officers' compensation for each of the last three years, whether or not actually paid out.") *referring to the Summary Compensation Table*); *Id*. at 53,174("No further disclosure will be specifically required when payment is actually made to the named executive officer.") *discussing the treatment of equity awards on the Summary Compensation Table*.

[12] This approach may also be useful in turbulent economic times where the accounting estimate of long-term incentive awards included in the Summary Compensation Table may vary considerably from the amounts actually realized.

The appendix to these comments includes a more complete version of this disclosure. As the two examples above demonstrate, it is important that the Commission's regulations allow flexibility for the Compensation Committee and the Board to present the pay for performance relationship in a manner that is consistent with the company's pay philosophy.

Regardless of the approach used to describe the relationship between incentives and performance, the Center does not believe that the actuarial increase in defined benefit pension plans should be included in the calculation of compensation "actually paid" because the amounts are based on credited service, age, interest rates, and historical earnings, factors not generally related to financial performance, and given that pension estimates have not yet been received by the executive and thus should not be considered pay actually paid. The Center also believes that "other compensation," should be excluded as it is not related to financial performance.

<u>Definition of Financial Performance Should Be Company-Specific.</u> We believe that the definition of "financial performance" should link the compensation "actually paid" to the financial metrics the Compensation Committee and the Board have incorporated into the company's incentive plans. Companies choose these financial measures because they link to short-term and longer term financial objectives intended to drive long-term shareholder value that will ultimately be reflected in stock price. We suggest that a company be required to clearly state the extent to which financial performance measures are used in determining the incentive compensation "actually paid" to named executive officers and how those amounts relate to financial performance.

Example 3: For example, a company that links its long-term incentives to financial performance may state: "our company provides a long-term incentive program for senior executives that is paid out in shares of company stock at the end of the period, based on the achievement of certain financial results. A certain number of performance share units are granted at the beginning of the three-year performance period and adjusted based on performance at the end of the period. The financial performance on which the payout is based is:

- 60% Earnings per share;
- 20% Return on Invested capital; and
- 20% Cash flow."

The company would then provide the pay (either on an estimated basis or realized pay basis) that is linked to the financial performance.

We also encourage the Commission to permit companies to incorporate into this disclosure comparison of how other, nonfinancial measures compare with performance, consistent with the Commission's existing disclosure rules, so long as the link between financial performance and compensation actually paid is clear. This approach would allow companies to describe the link between pay and the performance on which it is based, whether financial, operational or strategic. Companies that base compensation decisions or measure performance based on financial and operational measures would report the compensation decisions or compare compensation received with the achievement of those objectives, while companies that base compensation actually paid on total shareholder return would measure performance on that basis.

Example 4: Company A determines a total long-term incentive value based on the committee's evaluation of the external market and allocates that total among two long-term incentive vehicles:

- 40% time-vested stock options, which vest after three years and provide value if the company's stock price exceeds the grant price and
- 60% performance shares, which are based equally upon the achievement of earnings per share and total shareholder return measures.

In this case, only the performance shares are related to financial performance. However, rather than requiring a separate disclosure in which the company shows the link between the portion of the long-term incentive that was based on financial performance and compensation, the company should be able to disclose how each element of the long-term incentive produced or is expected to produce compensation based on performance (depending on the committee's philosophy in granting compensation as discussed above), and to highlight the elements that are based on financial performance.

Of course, as is the case under current disclosure rules, companies would not be expected to disclose non-public performance metrics that would lead to competitive harm if disclosed to competitors.

In sum, compensation is not a one-size-fits-all exercise, and companies use different approaches that fit their size, industry, strategy, competitive outlook and talent retention and development needs. The Commission should help promote clearer shareholder understanding of the decisions made by a Compensation Committee and/or the Board by implementing a principles-based approach to disclosure of the relationship between pay and performance.

VI. Pay Ratio Disclosure

The new disclosure requirements created by section 953(b) of the Dodd-Frank Act, which requires companies to calculate the median pay for "all employees," would be extremely difficult, if not impossible for large companies, especially those with substantial global operations. While the Center opposes the ratio because it does not believe it will provide any meaningful or material information that will be used by investors, the Center recognizes that the Commission has obligation to implement the language. For this reason, the Center believes that the Commission should interpret the statutory language in a way that fulfills the statutory mandate while making it practicable for corporations to comply. In sum, the Center believes the following:

- The phrase "all employees" should be interpreted to mean all full-time U.S. employees because of difficulty in aggregating and calculating disparate pay data from dozens of locations and systems;
- Total compensation for non-NEO employees should exclude certain items, including pension values and other compensation; and
- Because of the difficulty in aggregating the information globally, companies should be able to present a reasonable, good faith estimate, and the amounts should be considered as "furnished" rather than "filed."

Our rationale for each of these recommendations is discussed below.

A. "All Employees" Should Be Interpreted as "All Full-Time U.S. Employees"

The Center believes that the SEC should propose reasonable and workable interpretation of section 953(b) that takes into consideration the practical ability of companies to calculate the "median of annual total compensation." The critical part of the section states that an issuer is required to disclose "the median of the annual total compensation of all employees of the issuer except the CEO," using the same calculations the company uses to determine total pay under the SEC's proxy disclosure rules. Because the definition of median means "midpoint," depending on how the phrase "all employees" is defined, companies could be required to calculate pay as specified by the proxy rules for each individual employee globally and then determine the median of those values. For large employers, this means they will have to accurately calculate pay for tens of thousands and in some cases, hundreds of thousands of employees to determine the median. For some companies it will be nearly impossible to develop this number with the same accuracy that applies to NEO pay disclosures.

For many global employers, compensation data is housed in dozens of computer systems, and the data may not be sufficiently accurate for SEC disclosure purposes. The following examples of the number of employees and systems affected illustrate why this is a difficult and costly challenge for global employers and why the Commission should adopt a narrow interpretation of the provision:

- Company A: over 200,000 employees operating in over 60 countries has data housed in over 100 different systems;
- Company B: 33,000 employees in 35 countries and had data in roughly 75 systems;
- Company C: 107,500 employees in 52 countries with 115 pay systems and over 100 vendors.

In each of these situations, the company would be required to develop and coordinate a consistent calculation for each employee in all countries and then ensure that the results were accurate. In addition to the challenges of computing employee compensation as required under the Commission's executive compensation disclosure rules, the global compensation data would need to be translated into U.S. dollars, and those amounts could fluctuate considerably based upon unpredictable exchange rates. Moreover, unless the Commission makes the ratio a "furnished number" the data disclosed will need to be sufficiently accurate that company CEOs and CFOs could sign off on the disclosures as required under section 302 of Sarbanes-Oxley.

Because of these difficulties, and recognizing that the phrase "all employees" is not defined in the legislation or the legislative history, the Center urges the Commission to use its interpretive discretion to define "all employees" as "all full-time U.S. employees." This approach provides greater consistency because the comparison is being made within one geographic market, and nearly all U.S. employers would be able to readily obtain basic compensation information, which would not be the case if the phrase were interpreted to include all global employees. Limiting the disclosure to full-time employees eliminates the need to determine which employees are eligible for the disclosure and simplifies data collection without substantially affecting the calculation.

B. The Commission Should Exclude Pension Values and All Other Compensation Amounts for Non-NEO Employees

Section 953(b) requires companies to calculate compensation as is required for the named executive officers. No public company currently calculates each employee's total compensation as it calculates total pay on the Summary Compensation Table for the named executive officers, because disclosure of executive pay has a different purpose than internal accounting. With this in mind, the Center urges the Commission to eliminate the calculation of the actuarial increase in pension benefits and all other compensation for the purposes of the pay ratio. As a practical matter, few rank-and-file employees are likely to have such amounts, but eliminating them from the calculation would avoid the requirement that employers have to check for them with respect to each employee.

C. The Pay Ratio Should Be Considered a Furnished, Rather Than Filed Number

Even if the scope of the disclosure is limited as discussed above, the Center believes that the Commission should make the total median pay of all employees and the pay ratio disclosure a furnished rather than filed number, due to the complexities in developing an accurate calculation. Making the ratio a furnished number would not affect any of the executive compensation disclosures, including the disclosure of CEO compensation under the Commission's executive compensation rules. This approach would, however, encourage employers to provide a reasonable good faith calculation of the ratio while recognizing the substantial resources required to develop the median total compensation for all employees that would be sufficiently accurate for CEO and CFO certifications. Because of the difficulties described above, many companies have stated anecdotally, that they may only be able to provide an estimate. Making the ratio "furnished" rather than filed is a reasonable solution that also satisfies the policy objectives of the legislation.

In sum, the Center opposes the pay ratio disclosure requirement. However, we understand that the Commission must implement the law as passed by Congress. We urge the Commission to adopt a narrow interpretation which would satisfy the intent of the provision while mitigating the extraordinary expense employers would be required to bear to create the information, which very few shareholders would find useful.

Conclusion

The Center On Executive Compensation appreciates this opportunity to provide comments on our suggested approaches to regulation under the pay and governance provisions of the Dodd-Frank Act. If you have any questions about these comments, please contact me at tbartl@execcomp.org.

Sincerely,

Timothy J. Bartl
Senior Vice President and General Counsel

Attachment: Pay for Performance at a Glance Disclosure

cc: Securities and Exchange Commission
Hon. Mary L. Schapiro, Chairman
Hon. Kathleen L. Casey, Commissioner
Hon. Commissioner Elisse B. Walter, Commissioner
Hon. Commissioner Luis A. Aguilar, Commissioner
Hon. Commissioner Troy A. Paredes, Commissioner

Securities and Exchange Commission -- Division of Corporation Finance
Ms. Meredith Cross
Ms. Paula Dubberly

Appendix: Example of Disclosure of Compensation Actually Paid to Financial Performance Using a Realized Pay Approach

(NOTE: For the sake of illustration, mock up assumes disclosure is made in 2009 and the reporting year is 2008)

Executive Summary

-for-performance philosophy that seeks to link the interests of the named executive officers with those of the shareholders and that guides the Committee's decisions regarding executive compensation. Despite an unfavorable economic environment in the second half of the year, in 2008, the company still generated positive earnings and posted an increase in cash flow. Long-term results were also positive and on par with peer companies.

To assist shareholders in assessing the extent of the pay for performance link, the company has a supplemental table that shows how realized pay compares with actual performance. This table differs from the Summary Compensation Table (page X) in that the Summary Compensation Table is a mixture of actual pay realized in 2008 and the accounting expense for long-term incentives that are contingent upon future performance. The Summary Compensation Table also includes elements considered compensation under SEC rules which are not directly related to performance, specifically items included in "All Other Compensation" and the actuarial increases in pension value and nonqualified deferred compensation earnings. The tables are not intended as a replacement for the Summary Compensation Table, and while no approach to explaining the link between compensation programs and performance is perfect, the company believes the following tables provide greater clarity into the relationship.

Table 1 provides information as to the actual levels of compensation realized during 2008 by Mr./Ms. (Name), the company's Chief Executive Officer, and a description of the performance results that generated the realized compensation. In the case of long-term incentive payouts, gains on stock options exercised and restricted shares that vested during the year, these awards were earned over multiple years but were realized in 2008. For this reason, Table 1 provides both the total compensation realized and the annualized amount of compensation ratably attributable to 2008 and the other years between the grant date and 2008. Because the ratable amount is not known until the year in which the award is realized, and this is the first year the company has used this format, the ratable portion for years before 2008 is not reflected in previous years' compensation. Going forward, the company intends to use this framework annually, which should enhance the comparability of realized pay year-to-year.

Table 1: Comparison of Actual Pay Received in 2008 to Actual Performance*

Form of Compensation	Period Covered	Total Received ($)	Annualized Amount ($)	Performance Results Over Performance Period That Produced the Compensation
Salary	2008	$1,000,000	$1,000,000	The company generally targets salary for all executives at the 50th percentile of peer group companies. Based on this analysis, no adjustment was necessary for 2008.
Annual Incentive	2008	$1,800,000	$1,800,000	The annual incentive paid to NEOs is based on EBITDA, which measures economic profit and is a good measure of short-term performance; free cash flow from continuing operations, which reflects the company's ability to generate cash; and other corporate objectives, which are not disclosed due to competitiveness concerns. 2008 EBITDA increased by 11.4% over the prior year and exceeded the targeted level of performance. Free cash flow from continuing operations increased by 7% over 2007, totaling $3.3 billion and exceeded target. The Compensation Committee determined that accomplishment of other targeted corporate objectives fell short of expectations and thus resulted in no payout.
Long-Term Incentive Payout	2006-2008	$6,450,000	$2,150,000	The Long Term Incentive award was earned over the three-year performance period, 2006-2008, and produced a total payout of $6,450,000, or $2,150,000 per year. Performance criteria for this award were: (1) EPS growth, weighted 50%, which exceeded the targeted level; EPS reflects the company's profit per share and is a measure of the after-tax returns generated by the company. (2) Opening new markets in key strategic regions, weighted 25%, which was not achieved at the targeted level, and (3) Total return to shareholders compared against peer group companies, weighted 25%, for which the company ranked 7th out of 15 peer companies, producing a payout at target. Overall the payout represented 105% of target.
Equity Compensation				
Stock Option Exercises	2000-2008	$8,000,000	$1,000,000	The gains upon exercise of stock options in 2008 were $8 million, based upon stock price appreciation between 2000 and 2008. During that time, the stock price appreciated from $15 to $35 per share, reflecting the company's strong growth and profitability. Because the $8 million was earned over the 8 years the award was outstanding, the annualized gain (i.e., the gain spread equally over the period the options were held), is $1 million for each year the options were outstanding, reflecting the amounts earned over the performance period.
Restricted Stock Vesting	2006-08	$4,500,000	$1,500,000	Similarly, the value of the restricted stock that vested in 2008 was $4.5 million, and was earned over the three-year period from 2006 and 2008. Because the total gain was earned based on stock over the three-year vesting period, the annualized gain (i.e., the gain spread equally over 2006, 2007 and 2008) is $1.5 million per year. The company uses restricted stock to retain our top talent and to further align their interests with those of shareholders.
Total Actual Compensation Earned in 2008	2000-2008	$21,750,000**	$7,450,000**	See explanations under the Salary, Annual Incentive and Long-term Incentive boxes above. For amounts earned over more than one year, the annualized amount represents the pro-rata portion attributable to 2008. It includes the annualized gain for LTIP payout, stock option exercises and restricted stock, as well as total annual salary and annual incentive.

Note: This Table differs substantially from the Summary Compensation Table required by the U.S. Securities and Exchange Commission and is not meant a substitute for that table.

* Sample disclosure for illustrative purposes only.