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National Investor Relations Institute

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October 17, 2013

Elizabeth M. Murphy, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Comment Letter on Pay Ratio Disclosure (File No. S7-07-13)

Dear Ms. Murphy:

This letter is submitted on behalf of the members of the National Investor Relations Institute (NIRI). Founded in 1969, NIRI is the professional association of corporate officers and investor relations consultants responsible for communication among corporate management, shareholders, securities analysts and other financial community constituents. NIRI is the largest professional investor relations (IR) association in the world with more than 3,300 members representing over 1,600 publicly held companies and $9 trillion in stock market capitalization.

NIRI appreciates the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed rule to implement Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). NIRI members play a key role in making sure that U.S. public companies understand and respond to investors' concerns about executive compensation. NIRI members also work with their companies to ensure investors receive accurate and understandable disclosures on compensation so they can make better investing and proxy voting decisions.

While NIRI understands that the SEC proposed this rule to carry out a congressional mandate, NIRI believes that the draft rule, as written, would provide no material benefit to most investors while imposing significant costs on more than 3,800 U.S. issuers and inhibiting efficiency, competition, and capital formation. This rule, as proposed, will result in disclosures by issuers that are likely to be misleading or inconsistent or both with a high probability that the disclosures would confuse most investors and not contribute to their understanding of corporate pay practices. While the Commission has taken steps to provide flexibility and address issuer concerns, NIRI still expects that compliance costs will be exorbitant, especially for those firms with overseas employees.[1] NIRI believes the Commission should use its rulemaking discretion to limit this disclosure to full-time U.S. employees, and permit issuers to rely on existing industry-

[1] NIRI supports the Commission's decision to exempt "smaller reporting" companies from the proposed rule and to limit this mandate to annual reports and other filings where companies have to provide executive compensation information pursuant to Item 402 of Regulation S-K.

specific employee compensation data, which would significantly reduce the burden of this mandate.

Relevant Background

Section 953(b) has prompted great concern among investor relations professionals and other corporate stakeholders ever since they learned in July 2010 that it had been inserted into the final Dodd-Frank Act legislation with minimal public debate or understanding about its potential ramifications. NIRI joined with 22 other organizations in a joint letter to the SEC on Section 953(b) on January 19, 2012.[2] At that time, the groups urged the Commission "to engage in expanded public outreach and consideration of alternatives before moving forward with a public release of proposed rules implementing Section 953(b)." Specifically, NIRI and the other groups asked the SEC to: 1) hold a roundtable discussion of experts and stakeholders to better understand the potential issues and unintended consequences that may flow from implementation; 2) consider engaging in negotiated rulemaking to ensure thorough and well-balanced input that minimizes unintended consequences; and 3) follow the requirements as outlined in Executive Orders 13563 and 13579 to identify alternative approaches and choose the least burdensome means of implementing the rule.

While the Commission decided to propose this rule before conducting such engagement, NIRI hopes that the SEC will move cautiously and fully consider the views of the many corporate stakeholders who would be greatly affected by this rule.

NIRI's Views on the Proposed Rule

Proposed Rule Would Result in Misleading Disclosures

As noted above, NIRI members play a key role in helping issuers communicate with their investors on executive compensation matters. Investor relations officers are typically a key part of the corporate management team -- together with the corporate secretary, the general counsel, human resources, and the compensation committee of the board of directors -- that anticipates and responds to the pay-related concerns of investors and proxy advisors. With the arrival of mandatory Say-on-Pay votes at many U.S. companies in 2011, these compensation-related responsibilities have increased, and many IR professionals have learned that they must engage with investors on executive compensation and other governance matters throughout the year to gain strong shareholder support at their annual meetings. While Say-on-Pay has increased the proxy season workloads of both issuers and investors, the rule has had the beneficial effect of encouraging greater dialogue and a better understanding of executive compensation decisions.

The same cannot be said of the misleading and confusing disclosures that would result from this proposed rule. The pay ratio rule would result in a single "headline" number that would grossly

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[2] This letter is available at: http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-84.pdf

oversimplify corporate compensation practices and not add to the understanding of most institutional and retail investors. As the Commission acknowledged in its rulemaking release, "the ratio may significantly depend on how a company structures its business."[3] As noted by commenters, there are various factors (such as the company's use of contract (or leased) workers, the employment of workers from lower-wage states or countries, or the increased use of lower-wage workers to address seasonal spikes in typically retail-centric businesses) that could cause the ratios to differ significantly. Accordingly, the release noted that "precise comparability across companies may not be relevant and could generate potentially misleading interpretations or conclusions."

The Commission's release gave this example that clearly illustrates how the pay ratio numbers could be distorted by business structure differences.

> *For example, one company might outsource the labor-related (manufacturing) aspects of its business to a third-party to focus on product innovation, while another company competing in the same industry might choose to retain the labor aspect of its business. To the extent that product innovation requires higher pay than manufacturing, the outsourcing company will have a lower pay ratio for the same PEO [Principal Executive Officer] pay. If pay ratio parity between these two companies were pursued, and a lower ratio sought, this could create incentive for the manufacturing company to outsource jobs.*[4]

The release also acknowledges that a company, under pressure to maintain a low pay ratio, could decide not to expand business operations in lower cost regions. "This could adversely affect states and municipalities in lower wage geographies seeking to generate jobs for their communities," the Commission noted.[5] Before adopting with a final rule, the Commission should fully consider these unintended consequences, including the potential economic impact on U.S. states and cities with lower labor costs.

<u>Lack of Defined Standards Will Result in Inconsistent Disclosures, and May Cause Investor Confusion and Increase Compliance Costs</u>

The disclosures under this proposed rule may further confuse investors because many companies likely will use different methodologies and statistical samplings to calculate their median employee compensation. While NIRI appreciates the SEC's intent to provide more flexibility to issuers, this approach -- and the lack of established private sector standards to make such calculations -- may encourage some issuers to take statistical shortcuts to save money. At the same time, more cautious companies would incur greater expenses to ensure that they produce a more accurate (and presumably higher) ratio number, a fact that won't be considered by most investors when the company is compared to its peers. Given the varying methodologies that companies could use, the resulting disclosures may be inconsistent and not useful for investors.

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[3] See SEC Rulemaking Release on Pay Ratio Disclosure (SEC Release), File No. S7-07-13, p. 93.

[4] See SEC Release, p. 93.

[5] See SEC Release, p. 105.

The lack of clearly defined calculation standards could lead to other unintended consequences and greater compliance costs. Given that the proposed rule would treat pay ratio numbers as a "filed" (rather than "furnished") disclosure and thus subject to greater liability, some companies may ask their auditors to review this data and verify that the company used appropriate calculation methods.[6] However, it will be costly for auditors to do this work, given the lack of clear-cut standards to guide these reviews. The absence of Commission-endorsed methodologies also will open the door for proxy advisory firms or activist investors to apply their own methodologies that further confuse other investors and/or propose more onerous methodologies that may become the default standard, and undercut the flexibility for issuers that the Commission intended. Instead, the Commission should delay this rulemaking until it can work collaboratively with corporate stakeholders, investor advocates, the audit industry, and other relevant third-party organizations to develop recommended calculation methods that would be reasonable for companies of all sizes.

Proposed Rule Likely Will Lead to Less Informed Proxy Voting

This proposed rule likely will lead to less informed investor voting decisions and further distort the proxy voting process. For example, many retail investors (and smaller institutions without in-house proxy voting teams) will be tempted to base their Say-on-Pay votes solely on pay ratio numbers (i.e., does the company's pay ratio exceed some arbitrary number? If so, then vote against management). To save time, many investors will rely on these pay ratio numbers without fully considering a company's detailed compensation disclosures, financial performance, and business structure differences that would explain why its pay ratio number is higher than other issuers. As noted earlier, it is also likely that this rule would subject companies to unfair comparisons with peer firms with different business structures and compensation programs, and lead to more debate over peer group selections, which already is a source of contention and confusion during Say-on-Pay votes. In addition, it is foreseeable that the proxy advisory firms will develop new voting policies based on pay ratios, and thus potentially increase the number of institutions that vote in lockstep with their recommendations.

The SEC should be cautious about adopting any final rule that would create such an incentive for uninformed proxy voting. In keeping with the Commission's ongoing focus on and commitment to investor education, the SEC should seek to implement programs that would help retail investors understand these pay ratio disclosures.

Companies Should Be Able to Use Existing BLS Data to Calculate Their Pay Ratios

As other comment letters have stated, the proposed rule would result in a costly compliance process for most companies that would shed little light on employee pay beyond that already illuminated by existing employee data. The release notes the existence of data from the U.S.

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[6] As the Center On Executive Compensation stated in its September 2010 comment letter, this pay ratio data (if it is deemed "filed" with the SEC) will have to be sufficiently accurate enough to enable a company's CEO and CFO sign off on the disclosures, as required by Section 302 of the Sarbanes-Oxley Act. This letter is available at: http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-8.pdf

Department of Labor's Bureau of Labor Statistics (BLS), and points out that "statistics on the average earnings of U.S. workers in various industries are already publicly available to investors."

In addition to this duplication, this release would result in disclosure that most investors haven't asked for and may never use.[7] As the experience of three years of Say-on-Pay votes have shown, most investors are more concerned about whether directors are acting responsibly to create meaningful performance-based pay hurdles that would incentivize senior management to create long-term shareholder value.

The only investors that have consistently advocated for pay ratio disclosure are union pension funds, which presumably would use these numbers to attract more news media attention to future "vote no" campaigns against a company's pay practices or compensation committee members. Interestingly, despite their relatively modest holdings, these labor funds already have proven that they can run effective proxy campaigns with data from existing sources, including BLS statistics.[8] At the same time, most of these union efforts have focused on pay-for-performance disconnects or egregious severance payouts, rather than employee pay, because those concerns resonate more prominently with other investors.[9]

Before proceeding with a final rule, the Commission should explore more fully whether investors' needs for pay ratio disclosure could be met by permitting issuers to use existing BLS industry data on employee compensation.[10] Such an approach would be faithful to the legislative intent of Section 953(b) and greatly reduce the compliance burdens for both large and small companies. Although the company-specific mean employee data required by the proposed rule would produce more precise ratios than BLS data, this greater degree of precision would not add more material value to most investors. Whether a firm's pay ratio is 230 or 235 simply won't matter much to most investors as they consider the totality of a company's compensation practices. As the Center On Executive Compensation asked in its November 2011 comment letter: "if the SEC is willing to use an estimate to approximate median employee compensation through statistical sampling, why require companies to divert valuable time and resources to collecting an estimate of median employee pay when similar estimates are currently available?"

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[7] Shareholder proposals seeking pay ratio disclosures have received minimal investor support, averaging just 7 percent support at 12 companies since 2010, according to the Center On Executive Compensation.

[8] To make its CEO pay ratio comparisons, the AFL-CIO's Executive PayWatch website (http://www.aflcio.org/Corporate-Watch/CEO-Pay-and-You) uses data on average U.S. worker pay from the 2012 BLS Current Employment Statistics Survey. This calculation method would be far simpler than the requirements of the proposed rule but still would meet the needs of investors and fulfill the intent of Section 953(b).

[9] See Letter from the Change to Win Investment Group (CtW) to McKesson Shareholders, July 1, 2013; CtW, "Compensation Concerns at Cigna," April 2012 (CtW cited performance metrics and other compensation concerns at both companies but did not mention employee pay).

[10] See Letter from the Center On Executive Compensation, November 11, 2011, available at: http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-79.pdf. The Center observed that companies "could customize the ratio to their primary industries or create a blended employee pay rate based on existing BLS data that comparatively would be far more cost effective than the global data gathering exercise explained above and would support efficiency and business growth."

Accordingly, the SEC should use its rulemaking discretion to allow companies to use existing data sources, which would not materially affect the quality of the disclosures provided to investors.

Pay Ratio Disclosure Should Be Limited to Full-Time, U.S.-Based Employees

The Commission missed an opportunity to provide more useful disclosure and reduce compliance costs when it concluded that the pay ratio calculation must include non-U.S. workers, part-time and seasonal employees, and workers at company subsidiaries. As many commenters have noted, the inclusion of these additional employees around the world will greatly increase issuers' data-gathering burdens and make the resulting pay ratio disclosure far less meaningful for U.S. investors.

The Commission adopted this expansive interpretation of Section 953(b)'s reference to "all employees," even though the law is silent on whether it applies to overseas workers.[11] In addition, there is no reliable legislative history that would support such a view. As the Commission observed, the requirements of Section 953(b) were not discussed during the joint House-Senate Conference Committee's deliberations on the Dodd-Frank legislation, and the Conference Committee's report does not mention the pay ratio requirements in its summary of the law's corporate governance provisions.[12] The only support that the SEC referenced for this interpretation is a January 2011 letter from Section 953(b)'s original sponsor, Senator Robert Menendez, but it's a well-established legal principle that such post-enactment pronouncements are not entitled to deference when determining legislative intent.[13] Given the absence of pre-enactment legislative history on this issue, the Commission should use its rulemaking authority to limit this disclosure mandate to full-time, U.S.-based employees.[14]

In addition, there is not a clear consensus among activist investors that including foreign workers in the pay ratio calculation would result in disclosures that would be most beneficial for shareholders. As the Commission noted in its release, the Social Investment Forum and Walden

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[11] In *Morrison v. National Australia Bank*, 130 S. Ct. 2869, 2878 (2010), the U.S. Supreme Court declined to extend the reach of Section 10(b) of the Securities Exchange Act to permit shareholder lawsuits by non-U.S. investors over allegedly fraudulent conduct outside the United States, since the statute was silent on whether it could be applied in an exterritorial manner. As the Court held, "When a statute gives no clear indication of an extraterritorial application, it has none." Likewise, the Commission should not interpret Section 953(b) to encompass overseas employees without explicit congressional authority to do so.

[12] See SEC Release, pp. 11-12 (citing the Conference Report on H.R. 4173, H. Rep. No. 111-517, at 872).

[13] See SEC Release, p. 25, fn. 50. See also *Sullivan v. Finkelstein*, 496 U.S. 617, 631 (1990) (Justice Scalia concurring in part) ("Arguments based on subsequent legislative history, like arguments based on antecedent futurity, should not be taken seriously, not even in a footnote.")

[14] The Commission reasonably used its rulemaking discretion to narrow the companies covered by this mandate, even though there is no explicit language in Section 953(b) or other legislation that exempts smaller reporting companies and foreign private issuers. The SEC should take a similar approach and limit this rule to full-time, U.S.-based employees.

Asset Management acknowledged in comment letters that a pay ratio based on U.S. employee compensation would be "most useful."[15]

NIRI also believes that the Commission has failed to fully consider the staggering costs of including foreign workers in the median employee compensation calculation. We believe that the Commission's estimate that this mandate would require an average of 340 hours of staff time in year one significantly understates the time that many companies (especially those with overseas workers) would need to comply.[16] For most multinational companies, this global data-gathering exercise will be far more complex than the disclosures required under the Commission's 2006 compensation disclosure rules, which related to readily available information on the pay and benefits of just five individuals (a company's top five executives).

As other commenters have noted, and the SEC has acknowledged, U.S. companies will have to contend with stricter data privacy laws in the European Union, Canada, Japan, and other countries; the varying pension rights and severance benefits received by foreign workers; and currency exchange fluctuations throughout the year. Many publicly traded, multi-national companies do not have globally integrated payroll systems that can analyze the pay data on thousands of employees across multiple business units and borders, and have never attempted the quixotic task of gathering such data. These structural impediments cannot be easily overcome by using statistical sampling or "reasonable" estimates, as the rulemaking release would suggest.[17] While NIRI appreciates the Commission's intent to allow for sampling, such an approach won't reduce compliance burdens of most issuers, as long as non-U.S. employees are included in the pay ratio calculation.

As the Center On Executive Compensation observed in its November 2011 comment letter:

> *Statistical sampling would not ease the core burdens associated with calculating the pay ratio for most global companies that stem from aggregating global employee data. Most companies, especially larger multinational companies, do not maintain a centralized list of employees that is linked to their compensation information. Instead, information about each individual employee, including payroll data, is typically maintained in each country, business unit or individual location where the company does business. Thus, to develop a representative sample, whether by targeting a certain percentage of all employees, seeking to achieve a certain confidence level, or using stratified sampling by country, region, location or division, companies would still need to develop a list that identified all employees and once the appropriate sample is selected, identify and calculate all the*

[15] See SEC Release, p. 25, fn. 51.

[16] See SEC Release, pp. 145-147.

[17] In a 2011 survey conducted by the HR Policy Association, which represents human resource officers at large companies, most of the 95 respondents said sampling would not eliminate the difficulty in determining median employee compensation. According to that survey, 76.1 percent of respondents said they would have to have a team manually calculate at least some of the data, while 47.8 percent said the calculation "would be predominantly manual based upon the sampling requirements." See Letter from the Center On Executive Compensation, November 11, 2011, p. 5.

elements of compensation to be used for sampling purposes. . . . In the end, sampling creates as many issues as it solves.[18]

Given that sampling won't provide any meaningful relief to address companies' overseas compliance costs, the Commission should consider additional ways to reduce these burdens. If the SEC decides not to exclude foreign and part-time employees from the pay ratio rule, it should at least provide a longer compliance period (such as two additional years after the rule's effective date) for the inclusion of these workers.[19] This extra time would allow companies to hone their sampling techniques and calculation methods on a smaller pool of full-time, U.S.-based workers and give the Commission an opportunity to refine this rule to better meet the concerns of investors and issuers. Section 953(b) has no statutory deadline, so the Commission is free to delay part of this mandate to help minimize this rule's cost to companies.

We believe that the Commission also should exclude part-time and seasonal employees from the pay ratio disclosure calculation. As currently drafted, the proposed rule would unfairly penalize companies, such as retailers, that traditional rely on seasonal employees during the final months of the year.[20] However, given that the proposed rule applies only to part-time workers that are employed at the end of a fiscal year, some issuers may try to depress their ratios by terminating their seasonal workers right before the end of the year. Such tactics would be unfair to those modestly compensated seasonal employees and generate less inaccurate pay ratios.

In addition, NIRI believes that companies should be permitted to annualize the compensation for part-time and seasonal workers, which would help issuers more easily analyze employee pay over the same time period. Such an approach also would provide investors a more accurate picture of a company's pay practices.

While the proposed rule would allow companies to use "reasonable estimates" to determine any element of employee compensation, the Commission should provide additional relief to reduce the burden of identifying the median employee. Specifically, the SEC should allow companies to exclude the value of pension accruals, 401(k) matches, and non-cash benefits when performing this initial determination. This change would spare issuers from the costly challenge of identifying all those employees who receive such benefits and then obtaining estimates of the value of those benefits.[21]

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[18] See Letter from the Center On Executive Compensation, November 11, 2011, pp. 2-6.

[19] The SEC took a similar approach to help reduce compliance costs when it adopted its "conflict minerals" rule. As part of that rule, the Commission provided a two-year transition period (with four years for smaller reporting issuers) under which companies may rely on a "conflict undeterminable" designation if they cannot reasonably determine the source of the minerals in their supply chains. See 17 CFR PARTS 240 and 249b, File No. S7-40-10.

[20] See Letter from the Retail Industry Leaders Association, Oct. 27, 2010, p. 2, available at: http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-43.pdf

[21] See Letter from the Center On Executive Compensation, September 10, 2010, p. 22; and Letter from NIRI and Business Groups, January 19, 2012, p. 3, n. 2. (One issuer has estimated that it would cost $2 million annually to determine the actuarial value of the various pension benefits received by employees.)

Finally, the SEC should consider the cumulative impact of other Dodd-Frank rulemakings on issuers as it prepares to finalize this pay ratio rule. In addition to the burdens of Say-on-Pay votes, many issuers now are struggling to gather data from hundreds of suppliers to comply with the Commission's "conflict minerals" disclosure rule. In recent years, U.S. companies have had to respond to new disclosure mandates (or SEC guidance) on mine safety, cyber-security incidents, and business operations in Iran. In addition, companies will have to prepare for the SEC's yet-to-be-proposed Dodd-Frank rules on pay-for-performance disclosure, "claw-back" policies, and hedging policies. Accordingly, the implementation of Section 953(b) should not be viewed in isolation, but should be part of a balanced Commission rulemaking approach that meets the information needs of most investors without unduly inhibiting U.S. efficiency, competition, and capital formation.

NIRI's Recommendations

In conclusion, NIRI makes the following recommendations to help reduce the cost of compliance while providing more useful data to investors:

- The SEC should design disclosure requirements that fulfill the general intent of Section 953(b) without imposing undue costs or complexity on issuers. The SEC should use its rulemaking discretion to interpret the statutory text so the final rule does not unfairly penalize companies based on their business structure or the location of their employees.
- Companies should be permitted to use BLS data on average employee compensation by industry to determine their pay ratios.
- Given the difficulty of gathering worldwide employee data and the reality that many companies will have to rely on estimates, the SEC should treat pay ratio disclosures as "furnished," rather than "filed."
- The rule's pay ratio calculation should be limited to full-time, U.S.-based employees.
- If the Commission decides to extend this mandate to non-U.S. employees, companies should receive at least two years to prepare before they have to include those overseas employees in their calculations.
- If part-time and seasonal employees are included, the Commission should permit companies to annualize the pay data of those employees to provide more meaningful comparisons.
- To help companies more easily identify their median employee, issuers should be allowed to exclude employee pension accruals and non-cash benefits from this initial determination.
- The Commission should extend the comment period on this release for another 60 days to allow issuers more time to prepare estimates of their potential compliance costs.
- The Commission should undertake an education effort to help retail investors understand the limits of pay ratio disclosure and remind them that they can find other information (such as an executive summary of the Compensation Discussion and Analysis section of a company's proxy statement) that can provide a more complete understanding of corporate pay practices.

NIRI appreciates this opportunity to comment about pay ratio disclosure.

Sincerely,

Jeffrey D. Morgan, CAE
President & CEO