



AMERICAN BENEFITS  
COUNCIL

March 23, 2017

*Filed Electronically*

Acting Chairman Michael S. Piwowar  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

**RE: CEO Pay Ratio Disclosure Rule**

Dear Acting Chairman Piwowar,

On behalf of the American Benefits Council (the “Council”), we are writing in response to your request for comments on the Securities and Exchange Commission’s (the “SEC’s” or the “Commission’s”) Pay Ratio Disclosure rule published in the Federal Register on August 18, 2015 (the “Pay Ratio Rule”).<sup>1</sup> Our discussion below responds to your request in the SEC’s Public Statement dated February 6, 2017 for public input concerning “unanticipated compliance difficulties” and “whether additional guidance or relief may be appropriate.”<sup>2</sup>

The Council is a public policy organization representing principally Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council’s members either sponsor directly or provide services to health and retirement plans that cover more than 100 million Americans. As the comments below indicate, the Council’s members strongly believe that the costs associated with the Pay Ratio Rule far exceed any benefits, and that additional guidance and relief are consequently appropriate in order to simplify compliance.

Against the backdrop of speculative benefits, our members want to reiterate that they do not support the pay ratio disclosure requirement in its current form. We

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<sup>1</sup> Pay Ratio Disclosure, 80 Fed. Reg. 50,104 (Aug. 18, 2015).

<sup>2</sup> “Reconsideration of Pay Ratio Rule Implementation,” available at: <https://www.sec.gov/news/statement/reconsideration-of-pay-ratio-rule-implementation.html>.

nevertheless realize that the Commission has acted under a statutory requirement to promulgate rules implementing Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”).

## COMPLIANCE DIFFICULTIES AND REQUESTS FOR ADDITIONAL GUIDANCE

Our comments below describe current compliance difficulties and additional guidance that our members believe could reduce the substantial compliance costs associated with making disclosures under the Pay Ratio Rule. We wish to emphasize, however, that our suggestions should not be taken as support for the Pay Ratio Rule or for the view that it can be implemented at a reasonable cost to shareholders.

*(a) Delay the Effective Date in order to Re-examine Cost-Saving Alternatives:* The Commission has already received numerous comment letters suggesting changes that would make compliance with the Pay Ratio Rule more economically workable. We will not reiterate the full range of reasonable suggestions here, but instead suggest that the effective date of the Pay Ratio Rule be delayed by at least one year in order to permit the Commission to re-examine and reconsider cost-reduction and other reasonable compliance alternatives. As we mentioned in our previous comments on the SEC’s 2013 proposed Pay Ratio Rule, there is no statutory deadline associated with Section 953(b) of the Dodd-Frank Act. Therefore, if the Commission determines that more time is necessary to avoid or ease implementation challenges, a one-year delay would be a sound and judicious exercise of the SEC’s authority under the relevant statutory directive.

*(b) Exclude All Independent Contractors:* The Pay Ratio Rule’s definition of “employee” excludes workers who provide services as an independent contractor or leased worker when such workers’ compensation is determined by an unaffiliated third party. Additionally, the Compliance and Disclosure Interpretations (“C&DIs”) released by the Commission in October 2016 indicate that, in certain circumstances, a worker could be considered an “employee” under the Pay Ratio Rule if the issuer company “determines” that worker’s compensation, regardless of whether the worker would be considered an employee for employment law or federal tax purposes. This additional guidance, which is not necessarily contemplated by the provisions of the Pay Ratio Rule itself, has increased uncertainty and added significant complexity and cost to our member companies’ compliance efforts. For example, our member companies cannot rely on straight salary data for independent contractors, and therefore have needed to come up with an appropriate methodology for determining these workers’ annual compensation, notwithstanding the fact that this information may not be readily tracked or documented.

The SEC’s interpretation of what constitutes an employee for purposes of the Pay Ratio Rule departs from the traditional common law employee/independent contractor test that is used for most employment law and federal tax purposes. Under that

common law test, the most important factor for determining employment status is control over the worker performing services, not who determines the worker's compensation. The common law test considers factors like operational control and the worker's contractual relationship with the hiring company. As previously mentioned, the Pay Ratio Rule standard has created uncertainty and unanticipated compliance burdens for a number of our member companies and relief is warranted. Accordingly, we urge the Commission to issue guidance that would allow issuers to exclude independent contractors from any pay ratio determination as long as the issuer reports the income of those workers on a Form 1099 because they are classified as independent contractors under applicable Internal Revenue Service ("IRS") guidance. SEC harmonization with the IRS would result in significant operational and administrative efficiencies because it would permit employers to design payroll and information technology systems based on a single standard for differentiating employees from non-employees. Moreover, most companies already organize their operations pursuant to the IRS standard, with the Pay Ratio Rule already recognizing W-2 status as a valid source for determining employee income.

*(c) Exclude Part-time, Temporary, and Seasonal Employees:* We recommend that the SEC issue additional guidance or relief in order to permit issuers to exclude from pay ratio determinations those employees who normally work less than six months per year, or 20 hours per week. Such employees' inclusion in the pay ratio determination adds an extra layer of cost and complexity to identification of the median employee, and has the effect of distorting a company's median employee compensation data. Our members see no compelling policy reason to include these employees, and believe that the SEC could reasonably provide flexibility that allows issuers to make their own determinations regarding excluded employees, provided they disclose needed information regarding any classes of excluded employees. Because CEOs work full-time, it is illogical to make pay ratio determinations by reference to an issuer's employees who are not also working full-time throughout the year. Likewise, our members see inclusion of seasonally-hired or temporary employee groups as an unnecessary distortion of the pay ratio disclosure.

In the preamble to the final Pay Ratio Rule, the SEC justified its inclusion of part-time, temporary, and seasonal employees in the determination of median employee compensation by emphasizing the fact that "Section 953(b)(1)(A) expressly directs disclosure of the median of the annual total compensation of 'all employees of the issuer, except the chief executive officer (or any other equivalent position) of the issuer'"<sup>3</sup> (emphasis added). However, this stated justification is inconsistent with other portions of the SEC's pay ratio determination rules, which provide for the reasonable exclusion of certain non-U.S. employees from the definition of "employee." We do not suggest that the SEC exceeded its interpretive authority by excluding certain non-U.S. employees. Rather, we recognize that the SEC's exclusion of those employees reflects a

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<sup>3</sup> 80 Fed. Reg. at 50,117.

reasonable interpretation of the statute based on the SEC's determination that the benefits of collecting such data do not outweigh their costs.<sup>4</sup> In a similar regard, we encourage the SEC to use its reasonable judgement to exclude part-time, temporary, and seasonal employees, as well as those individuals who are not considered employees for other employment law and federal tax purposes, from the determination of the median employee because the increased costs associated with collecting information on those employees outweigh the limited benefits of reporting such information.

*(d) Exclude Non-U.S. Employees:* The Council recommends that the Commission provide additional relief to permit issuers to focus only on their U.S. workforces in order to identify their median employee for pay ratio disclosure purposes. Specifically, we support additional guidance that would allow issuers to make their own determinations regarding the exclusion of non-U.S. employees, provided they disclose any classes of excluded employees. Such relief would significantly reduce compliance costs for most companies because U.S. payroll data is generally centralized, readily accessible, reconcilable, and consistently comparable.

Our member companies have indicated that the inclusion of non-U.S. employees in the pay ratio determination creates immense compliance complications. In fact, some of our member companies have indicated that the single biggest driver of costs under the Pay Ratio Rule will be the inclusion of non-U.S. employees in the pay ratio determination. Examples of these difficulties include:

- Foreign data privacy laws can change and complicate the process of obtaining compensation from non-U.S. jurisdictions.
- In some countries, it is not possible to get compensation data without explicit employee consent.
- In the non-U.S. employee context, our member companies cannot rely on straight salary data for identifying their median employees, due to, for example, currency exchange issues.
- Many of our members have multinational operations with multiple payroll systems in the various countries in which they operate. Some members without centralized payroll systems are having to request compensation figures from foreign subsidiaries and will have to rely on local staff in each foreign location to gather and transmit the data necessary to complete the disclosure required by the Pay Ratio Rule, an additional burdensome step.
- The inclusion of benefits as an integrated part of payroll complicates the median employee calculation.

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<sup>4</sup> "To help address concerns about compliance costs, and consistent with commenters' suggestions, the final rule provides two tailored exemptions from the definition of "employee," which otherwise includes all of a registrant's U.S. and non-U.S. employees in the median employee determination." 80 Fed. Reg. at 50,111.

Each of these issues will generate avoidable compliance costs and distort compensation data that is necessary to calculate the required pay ratio disclosure. In order to prevent these problems, the SEC should grant the relief we have requested and allow issuers to make their own determinations regarding the exclusion of non-U.S. employees, provided they disclose any classes of excluded employees.

*(e) Employees without Compensation:* Our member companies indicate that their efforts to comply with the Pay Ratio Rule have been unnecessarily complicated by the need to consider *all* employees when calculating the pay ratio disclosure, *even employees that have not received compensation during the relevant fiscal year*. The final Pay Ratio Rule defines an employee as “an individual employed by the registrant or any of its consolidated subsidiaries . . . as of a date chosen by the registrant within the last three months of the registrant’s last completed fiscal year.” Because this broad definition makes no express references to compensation, it presumably includes new employees who have not yet received their first paycheck and other employees that may not receive compensation during a given year. We encourage the Commission to issue guidance that would allow issuers to exclude any employee that does not receive compensation from its pay ratio determination. Otherwise, consideration of those employees will unreasonably affect the determination of an issuer’s median employee and unnecessarily distort an issuer’s pay ratio calculation.

*(f) Base Pay to Determine Median Employee:* Our member companies indicate that the use of base pay to identify their median employee can result in significant cost savings. Instruction 4 to Item 402(u) indicates that “[a] registrant may identify the median employee using annual total compensation or any other compensation measure that is consistently applied to all employees included in the calculation, such as information derived from the registrant’s tax and/or payroll records.” Although our members appreciate the instructions’ clarity on the permissible use of W-2 income when determining the median employee, in many cases, it is simpler and more efficient to use base pay to determine the median employee. Accordingly, we encourage the Commission to provide additional guidance, like a safe harbor, explicitly stating that issuers can use base pay as a measurement to determine the median employee as long as it is consistently applied to all employees. Such guidance would add clarity to the Pay Ratio Rule and result in significant cost savings.

*(g) Foreign Private Issuers:* The Council commends the Commission for expressly excluding foreign private issuers from the Pay Ratio Rule in its 2013 proposal and 2015 final rule. The Pay Ratio Rule’s application to foreign private issuers would have made it very difficult to gather an issuer’s total annual worldwide compensation data, while providing very little in terms of useful data for shareholders. As the Commission reconsiders the Pay Ratio Rule, we want to take this opportunity to express our continued support for the exclusion of foreign private issuers from the scope of the Pay Ratio Rule’s disclosure requirements.

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Thank you in advance for your consideration of our recommendations. Please let us know if further information or a meeting would be helpful.

Sincerely,

A handwritten signature in black ink that reads "Lynn D. Dudley". The signature is written in a cursive style with a large, prominent "L" and "D".

Lynn D. Dudley  
Senior Vice President,  
Global Retirement and Compensation Policy