

# American Federation of Labor and Congress of Industrial Organizations



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**Sent via electronic mail: [rule-comments@sec.gov](mailto:rule-comments@sec.gov)**

December 2, 2013

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

**Re: Pay Ratio Disclosure, File No. S7-07-13**

Dear Ms. Murphy:

On behalf of the American Federation of Labor and Congress of Industrial Organizations (the "AFL-CIO"), I am writing to provide comment to the Securities and Exchange Commission (the "SEC") on the proposed pay ratio disclosure rule. The proposed rule is required by Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The AFL-CIO strongly supports the SEC's proposed rulemaking in its current form, and we encourage the SEC to adopt a final rule as soon as possible to satisfy the requirements of Section 953(b) of the Dodd-Frank Act.

The AFL-CIO is the umbrella federation for U.S. labor unions, including 57 unions representing more than 12 million union members. Union-sponsored and Taft-Hartley pension plans hold more than \$540 billion in assets. Union members also participate directly in the capital markets as individual investors and as participants in pension plans sponsored by corporate and public-sector employers. The retirement savings of America's working families depend, in part, on public companies having responsible compensation practices for their chief executive officers and all other employees.

The SEC's proposed rule to implement Section 953(b) will provide investors with material information about the employee compensation practices of their companies, including the median of the annual total compensation of all employees excluding the

chief executive officer, the annual total compensation of the CEO, and the ratio of the two. Disclosure of this information will promote market efficiency and facilitate capital formation by making companies' employee compensation practices more transparent. Pay ratio disclosure will also help protect investors from excessive CEO pay.

A company's internal pay ratio is an important financial metric for investors to monitor and evaluate. High levels of CEO pay relative to other employees can reduce company performance.<sup>1</sup> Employee productivity, morale and loyalty suffer when workers see that the CEO is taking more while those same workers do more for less. In contrast, a reasonable pay ratio sends a positive message to the workforce that the contributions of all employees are valued. For these reasons, the proposed rule will help investors better understand the impact of internal pay disparities on company performance.

Pay ratio disclosure will also help investors evaluate CEO pay levels when voting on executive compensation matters such as "say-on-pay" resolutions. At present, CEO pay levels are set based on a peer group analysis of what other CEOs are paid. Over time, the use of peer group analysis leads to a ratcheting up of CEO pay levels.<sup>2</sup> Pay ratio disclosure will give investors an alternative metric to assess the reasonableness of CEO pay within each particular company.<sup>3</sup> This will encourage consideration of internal compensation practices rather than relying on peer group analysis alone.

The benefits of pay ratio disclosure will be substantial for investors because pay ratio disclosure will help moderate the overall level of CEO pay growth. Over the past two decades, average CEO pay at large U.S. corporations increased at an annually compounded rate of 6 percent from \$3.8 million in 1992 to \$12.3 million in 2012.<sup>4</sup> In comparison, average worker pay increased only 3 percent annually over the same period.<sup>5</sup> Had CEO pay grown at the same rate as average worker pay during this period, the average large company would have paid its CEO \$5 million less in 2012.

As the statutory language of Section 953(b) mandates, the SEC's proposed rule requires that companies calculate the median compensation for "all employees." Accordingly, the proposed rule appropriately includes employees of company subsidiaries, as well as international, part-time, temporary, and seasonal employees. If these classes of employees are excluded from disclosure, investors would receive an

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<sup>1</sup> For a discussion of various academic studies regarding the impact of pay disparities on organizational performance, see Appendix A to the AFL-CIO letter to the SEC dated August 11, 2011, available at <http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-78.pdf>.

<sup>2</sup> Elson, Charles and Craig Ferrere, "Executive Superstars, Peer Groups, and Overcompensation: Cause, Effect, and Solution," *Journal of Corporation Law*, Vol. 38, No. 3, Spring 2013.

<sup>3</sup> James Cotton, "Toward Fairness in Compensation of Management and Labor: Compensation Ratios, A Proposal for Disclosure," *Northern Illinois University Law Review*, 1997.

<sup>4</sup> "Executive Pay: The Party Ain't Over Yet," *Businessweek*, April 25, 1993, available at <http://www.businessweek.com/stories/1993-04-25/executive-pay-the-party-aint-over-yet> (1992 CEO pay); AFL-CIO Executive Paywatch website analysis of CEO pay data provided in 327 proxy statements of S&P 500 companies, available at <http://www.paywatch.org> (2012 CEO pay).

<sup>5</sup> Bureau of Labor Statistics' Current Employment Statistics Survey – Table B-2.

incomplete picture of their company's employee pay practices. For example, many companies employ a majority of their workers overseas, or as part-time employees.

We commend the SEC for drafting the proposed pay ratio disclosure rule in such a way that gives companies considerable flexibility in determining the median employee's pay for calculating the ratio, while not diminishing the value of these disclosures to investors. In particular, we approve of the SEC's permitting companies to use statistical sampling as well as payroll and tax records to determine the median employee for disclosure purposes. The AFL-CIO had previously suggested these methodologies to the SEC in our earlier comment letters regarding Section 953(b).<sup>6</sup>

The SEC's proposed rulemaking provides appropriate guidance for companies to comply with the pay ratio disclosure requirements. Because pay ratio data is relevant for CEO pay analysis, it should appear in company filings in which Item 402 disclosure is required. Estimates of annualized compensation should not be permitted for temporary or seasonal employees because such an estimate would distort pay levels. Companies should be required to provide a brief description of their methodology and material assumptions, and explain the reasons for any changes to their methodology.

As the SEC's proposed rulemaking notes, companies may also provide investors with supplemental disclosure of their employee compensation practices and additional pay ratios. If a company believes that the required disclosure of median employee compensation does not provide a sufficient picture of the company's overall workforce, the company should provide supplemental information to investors. For example, companies may provide supplemental disclosure of the median compensation and pay ratios for their U.S. based employees or their full-time employees.

We note that pay ratio disclosure will become more common in the near future by non-U.S. companies who are not subject to SEC disclosure requirements. For example, India recently enacted a pay ratio disclosure requirement by including a provision similar to Section 953(b) into its Companies Act.<sup>7</sup> Voluntary disclosure of pay ratio data will also become more frequent. In 2013, the Global Reporting Initiative approved new standards for sustainability reports that urge companies to voluntarily disclose the ratio CEO to median employee compensation.<sup>8</sup>

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<sup>6</sup> AFL-CIO letter to the SEC dated August 11, 2011, available at <http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-78.pdf>; AFL-CIO letter to the SEC dated December 13, 2010, available at: <http://www.sec.gov/comments/df-title-ix/executive-compensation/executivecompensation-54.pdf>.

<sup>7</sup> India Companies Act, 2013, Section 197(12) provides that "Every listed company shall disclose in the Board's report, the ratio of the remuneration of each director to the median employee's remuneration and such other details as may be prescribed."

<sup>8</sup> "G4 Sustainability Reporting Guidelines," Global Reporting Initiative, 2013, p. 41, available at: <https://www.globalreporting.org/resource/library/GRIG4-Part1-Reporting-Principles-and-Standard-Disclosures.pdf>.

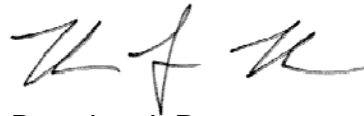
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In conclusion, we support the proposed pay ratio disclosure rule and urge the SEC to adopt a final rule as soon as possible to fulfill its legal obligations under Section 953(b) of the Dodd-Frank Act. Thank you for taking the AFL-CIO's views into consideration regarding this matter. If the AFL-CIO can be of further assistance, please contact me at (202) 637-5152 or [brees@aficio.org](mailto:brees@aficio.org).

Sincerely,

A handwritten signature in black ink, appearing to read 'B. J. Rees', written in a cursive style.

Brandon J. Rees  
Acting Director, Office of Investment

BJR/sdw  
opeiu #2 afl-cio