

Written Testimony

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Subcommittee on Capital Markets and Government Sponsored Enterprises
Committee on Financial Services
United States House of Representatives

Concerning Proposals to Alter or Repeal Section 953(b) of the Dodd-Frank
Act, on Disclosure of the Ratio of CEO Compensation to the Median
Worker Compensation

My name is Kenneth A. Bertsch. Since December 2010 I have served as President and CEO of the Society of Corporate Secretaries and Governance Professionals (the “Society”).

The Society is a professional association, founded in 1946, with more than 3,100 members who serve more than 2,000 companies. Our members are responsible for supporting the work of corporate boards of directors and their committees and the executive management of their companies regarding corporate governance and disclosure. Our members generally are responsible for their companies’ compliance with the securities laws and regulations, corporate law, and stock exchange listing requirements. The majority of Society members are attorneys, although our members also include other non-attorney governance professionals. More than half of our members are from small and mid-cap companies.

The Society supports development of corporate governance policies and practices that best serve the functioning of boards and the long-term interests of shareholders.

Until December 2010, I served as Executive Director for Corporate Governance at Morgan Stanley Investment Management. My previous employment entailed work in corporate governance research for investors at Moody’s Investors Service, TIAA-CREF and the Investor Responsibility Research Center.

I am honored to give testimony before this Subcommittee on behalf of the Society.

Background

The Committee has asked for our views on the “Pay Ratio” provision of Section 953(b) of the Dodd-Frank Act. This section requires companies to disclose the median of annual total compensation paid to all employees of the company (other than the CEO) as well as the annual total compensation paid to the CEO, and then provide a ratio comparing those two numbers (“Pay Ratio”).

Calculation of “annual total compensation” of an employee for purposes of this provision must be determined in accordance with the rules for named executive officers in Item 402 of Regulation S-K.

Summary Comments

We believe that it will be virtually impossible for large global companies to comply with Section 953(b) as now written, and that implementation will impose a substantial burden even on smaller non-global issuers. More importantly, while we acknowledge a public policy concern on pay gaps in the United States, we strongly believe the required ratio will not be material or meaningful to investors in company securities. Accordingly, we believe the provision should not be implemented at this time; rather this section should be repealed and, if it is determined to be appropriate, new more workable legislation should be enacted.

We note also that the SEC faces challenges in implementing the many Dodd-Frank reforms, and is otherwise resource-constrained, as indicated by the recently completed Boston Consulting Group study mandated by Section 967 of the Dodd-Frank Act. The SEC must prioritize and focus on the most important issues facing investors and the securities markets.

The Pay Ratio Would Not Provide Meaningful Information to Investors

We do not believe the Pay Ratio provides useful data for investors, who under existing SEC requirements have access to extensive disclosure on senior executive compensation. It is important to keep in mind that SEC disclosure documents are meant to contain information that a “reasonable investor” needs to make an investment decision. The “reasonable investor” standard for materiality is well-established under law. SEC disclosure documents are not meant to contain every item of information that any investor could possibly want to know. Proliferation of disclosure requirements not centered on a disciplined standard will make SEC disclosure documents unusable for the average investor, while adding costs that ultimately are borne by investors.

The Pay Ratio under Section 953(b) will not provide useful information to investors because it is not comparable in any way – across industries, companies, geographies, or employees. For example, companies located in certain areas of the country pay employees and executives more than others, given the cost of living in those areas. Some businesses have a large number of low-paid workers and some have a higher percentage of part-time employees or seasonal employees. These companies will likely have “worse” Pay Ratios. Some companies have outsourced jobs to locations with lower pay levels in an effort to save costs, and these companies may have “better” Pay Ratios than those that have chosen to maintain their operations (call centers for example) in the United States. In addition, companies with franchisees rather than company-staffed stores will also likely have a “better” Pay Ratio. The Pay Ratio will not be a meaningful measure to compare to the CEO’s compensation, or to compare the pay practices compared within a single industry. For this reason we do not believe that shareholders will find this disclosure relevant in deciding whether to invest in the company, or on how to vote in election of directors, or how to vote on a “say on pay” resolution.¹

¹ **Illustration of lack of comparability:** A major factor in lack of usefulness of the Pay Ratio is the widely varying practices even within industries on outsourcing of production. Employees of vendors would not be included in the pay ratio. A company that keeps relatively greater production in-house would tend to have a significantly lower median “annual total compensation” than one that outsources extensively.

Consider the following hypothetical, using median “company” salary as currently calculated by Payscale.com in the United States (about \$60,000), Poland (about \$20,500) and India (about \$10,500); other forms of compensation for non-CEO employees are excluded for purposes of this example.

Company A has 1,000 employees, including 100 U.S.-based executives and other employees, all but the CEO paid at the market median. The other 900 employees are all

We submit that the key data points for considering pay equity that investors could use would be (1) CEO pay, which already is subject to extensive disclosure rules, and (2) market-wide pay information, which is publicly available from various government and private sources. So even aside from the question on whether investors generally would find pay equity ratios useful, the particular ratio mandated under 953(b) would be of limited or no use.

More generally, we believe investors have indicated limited interest in obtaining such pay ratio information from companies. We are aware of votes in 2010 on 10 shareholder proposals requesting reports on pay disparity. On average, the proposals were supported by only 6.1% of the shares voted (and opposed by 93.9%), which is a markedly low level of support.

Finally, if investors are concerned that they need additional disclosure on pay equity from a particular company, they currently may submit shareholder proposals requesting such information, and/or use say-on-pay votes under Dodd-Frank to express their views.

Requirement is Burdensome Well Beyond its Benefit

The Pay Ratio disclosure requirement appears to some observers to be a trivial addition to existing disclosure requirements. However, developing the data to calculate the Pay Ratio would be highly burdensome. SEC Corporation Finance Director Meredith Cross recently testified that she has concerns on whether the SEC staff can make the Pay Ratio provision workable. Other SEC officials have noted that the calculations required by the provision would be extremely difficult, especially for large, multinational corporations that pay workers throughout the world in a variety of methods.

in Poland and assemble the company's products; assume all Poland employees are paid the same amount, at the market median.

Company B also has 100 U.S. based executive and other employees, with all but the CEO also paid at the market median. However, Company B outsources assembly of its products to another firm, which assembles the products in India. Company B has no other employees.

Assume each company's CEO is paid \$1 million. The Pay Ratio for Company A will be "49:1" (\$1 million/\$20,500 of the median employee at the company), while that for Company B will be "17:1" (\$1 million/\$60,000). Company A appears to have relatively poor pay equity, even though its assembly work is done in Poland, which has substantially higher median pay than India, and even though the two companies otherwise are similar.

While this hypothetical is but one simplified example of the problem, it shows the danger in disclosing a ratio that is not based on similarly situated employees.

Given the definition of “annual total compensation” as set forth in Section 953(b)(2), many companies, including most large worldwide U.S. companies, would not be able to calculate the “median of the annual total compensation of all employees of the issuer” with the degree of precision and certainty required for information filed under the U.S. securities laws. Payroll systems are not set up to gather the kind of information required under this provision. This is especially the case for companies organized into multiple operating business units. Those business units keep records and have internal controls over what each employee is paid, but they report aggregated figures to the parent company for inclusion in consolidated financial reports for public filings. Thus, the parent company that files SEC reports does not have direct access to the employee-by-employee data necessary to identify the median employee. This is complicated even further when operating business units are based outside the United States or employ people in multiple countries.

Moreover, Section 953(b) requires the issuer to disclose the median of all employees, using the same calculations as are used to determine total pay for named executive officers under the proxy rules. In other words, a company would have to convert the pay of each employee globally into the pay formula applicable to the named executive officers in the Summary Compensation Table. To our knowledge, no public company now calculates each employee’s total compensation in the way it is required to calculate total pay on the Summary Compensation Table for named executive officers (usually five individuals). Disclosure of executive pay has a different purpose than internal accounting.

For a company with tens or hundreds of thousands of employees, this would be a large and costly task. Note that many global corporations house compensation data in dozens of computer systems. It is not clear that companies could perform consistent calculation for each employee in all countries and ensure that the results are accurate, even with large expenditure on the data.

As we indicated in Society testimony in 2010, there are a number of questions that must be answered by corporate staff trying to compile data necessary to identify the median employee, including the following:

- How do you handle currency conversions for non-U.S. employees? What rate do you use and as of what date?
- In many parts of the world, compensation includes non-monetary components, such as transportation, housing, direct medical care, security, and sometimes even food. How do you treat these kinds of compensation?
- What if you have employees in countries where local privacy laws do not allow personal compensation information to be sent across borders without express employee consent?
- How do you treat company-matched contributions to 401(k) plans? And, what about company matched contributions to a 401(k) plan that is invested in

company stock or discounted employee stock purchase plans? Should we treat those as equity compensation?

- How do you treat employees brought in as part of a mid-year acquisition or new employees that started mid-year? Conversely, how do you treat employees that left as part of a mid-year disposition or were terminated mid-year?
- How do you treat severance paid to terminated employees?
- How do you treat special early retirement programs?
- How do you treat overtime and shift differential payments for hourly workers and non-exempt employees? Is that included in “All Other Compensation”?
- For those employees who have an eligibility waiting period how do you treat the waiting period?
- What about store discounts? Are they excludable?


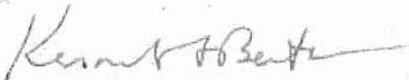
In summary, we believe that the provision is simply unworkable and would produce information that is not meaningful to investors.

I want to thank the Subcommittee again for the opportunity to provide testimony, and indicate the willingness of the Society to answer questions on this now or in the future, and to comment on the workability of any substitute provisions that Congress may wish to pursue.

United States House of Representatives
Committee on Financial Services

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Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name: KENNETH A. BERTSCH	2. Organization or organizations you are representing: SOCIETY OF CORPORATE SECRETARIES AND GOVERNANCE PROFESSIONALS
3. Business Address and telephone number: 	
4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
6. If you answered yes to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets. 	
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