HR POLICY ASSOCIATION
The Association of Senior Human Resource Executives

October 23, 2006

VIA ELECTRONIC MAIL

Ms. Nancy Morris
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-9303

RE: File Number S7-03-06
Executive Compensation Disclosure: Request for Additional Comment

Dear Ms. Morris:

HR Policy Association ("HR Policy") is pleased to submit these comments in response to the U.S. Securities and Exchange Commission's ("SEC" or "Commission) request for comments on its revised proposal to require compensation disclosure for up to three additional highly compensated employees.[1] We appreciate the Commission's willingness to consider eliminating the disclosure for employees who do not have responsibility for significant policy decisions within a company, such as sales employees or highly knowledgeable engineers. However, based on a survey on the effects of the revised proposal, the Association believes that the proposal will not provide information useful to investors and would impose an undue administrative burden on large issuers relative to the information generated. For these reasons, we recommend that the SEC not pursue the proposal further.

HR Policy Association is a public policy advocacy organization representing the chief human resource officers of over 250 leading employers doing business in the United States. Representing nearly every major industry sector, HR Policy members have a combined U.S. market capitalization of more than $7.5 trillion and employ more than 18 million employees world wide. Our members are particularly interested in executive compensation disclosure because they are responsible for assisting boards of directors and board compensation committees in developing compensation programs for executives in an effort to recruit and retain the best talent. We believe that executive compensation should be clearly and fully disclosed in a comprehensive and understandable manner to give investors an accurate basis for evaluating the effectiveness of a company's executive compensation program.

EXECUTIVE SUMMARY

HR Policy believes that, even with the suggested changes, the disclosure of the job description and total compensation of up to three additional employees as set forth in the revised proposal will neither provide context nor facilitate a better understanding of the compensation

[1]Securities and Exchange Commission, Executive Compensation Disclosure, Release Nos. 33-8735, 34-54380, 71 Fed. Reg. 53267 (Sept. 8, 2006) (proposed rule) [hereinafter "Revised Proposed Rule"].

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structure of the named executive officers (NEOs) and directors. On the contrary, HR Policy believes that the disclosures under the Commission's revised proxy disclosure rule is more than sufficient to accomplish those goals.

The Association believes that the Commission's attempt to limit disclosure under the revised proposal to employees who exert "significant policy influence" will create substantial confusion as to which employees are covered. Companies will spend substantial administrative time and resources to identify and calculate the total compensation for employees that may be covered. In addition, the revised proposal would encourage "poaching" of the employees' whose pay is disclosed by rival firms. It also would create employee relations problems, as similarly situated but lower paid employees are likely to question why they are not paid the same amount, as well as raise potential privacy concerns.

Professor Robert L. Clark of North Carolina State University has studied the impact of the proposal based on a survey of HR Policy Association and WorldatWork members.[2] The results are referred to throughout these comments. They confirm the Association's arguments that the revised proposals costs far outweigh any benefits:

- Only 20 percent of survey respondents keep the information necessary to calculate total compensation for highly paid employees in a single database;
- 70 percent of survey respondents indicated they do not currently have systems in place to determine total compensation, as defined by the SEC, for highly compensated employees;
- 70 percent of these companies said it would be difficult or very difficult, as well as costly, to develop and maintain such systems;
- 92 percent of respondents said that the information required by the revised proposal would be of limited value for shareholders at best, with the vast majority of these saying it would provide no value; and
- 62 percent of respondents said the proposal would make it easier or much easier for competitors to "poach" employees, and a total of 80 percent said poaching would be made at least a little easier.

For these reasons, and because the compliance costs would be at least three times the SEC's estimate, HR Policy respectfully requests that the Commission decide not to pursue any proposal to require the disclosure of three additional employees further.

[2] Robert L. Clark, "Impact of Proposed Disclosure Requirement for Total Compensation of Highly Compensated Employees (copy on file with HR Policy Association) [hereinafter "Clark Report"]. The web-based survey was conducted between September 29 and October 9 and was sent to 1,393 companies that were members of HR Policy Association, WorldatWork or both.

A. The Revised Proposal Will Not Provide Information That Is Useful to Investors

The Commission has revised its proposal to require disclosure of total compensation and a job description of an additional three employees whose total compensation exceeds that of any named executive officer (NEO). According to the Commission, it has done this in order to assist investors "in placing in context and permit[ting] a better understanding of the compensation structure of the named executive officers and directors."[3] In reality, however, the revised proposal would not enhance investors' understanding of the compensation for either group, particularly the NEOs.

1. The Revised Proposal Would Not Enhance Comparability of Named Executive Officer Compensation

The purpose of the pay disclosures for the named executive officers is to permit shareholders to compare executive compensation for the highest leadership positions in a corporation across companies and industries.[4] Although still imperfect, in its final rule revising these disclosure requirements, the SEC has arguably enhanced such comparisons across companies by explicitly including the principal financial officer as one of the named executive officers. The comparison of the other three most highly compensated named executive officers is less direct because the positions vary by company. However, it is still meaningful because the basis for comparison – the three most highly compensated executive officers – will be consistent.

By comparison, the SEC's proposal to disclose an additional three employees will not facilitate meaningful comparisons among the NEOs or the three additional employees. The positions potentially subject to disclosure under the revised proposal will vary substantially by company. Some will be executive officers, while others will be nonexecutives. In addition, unlike the NEOs, the composition of the other three most highly compensated employees is more likely to change annually, making comparisons among companies significantly less meaningful for shareholders. This will especially be the case where some companies have "other three" employees to report and others do not.

Employees that have responsibility for significant policy decisions may make as much as (if not more than) a named executive officer due to factors wholly unrelated to NEO compensation. For example, the head of a business unit could receive a retention award that has a significant grant date fair value under the SEC's rules. The grant may vest over three-to-five years. Likewise, a senior sales manager could receive a substantial incentive payment after the manager's team wins an important new account. These are one-time events that are unrelated to the company's executive compensation program. Sporadic payments such as these do not change that the applicable pay structures still vary with the employee's level in the company, his

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[3] Revised Proposed Rule, 71 Fed. Reg. at 53268.
[4] *See, e.g.*, Securities and Exchange Commission, Executive Compensation and Related Person Disclosure, Release Nos. 33-8732A;34-54302A, 71 Fed. Reg. 53157, 53160 (Sept. 8, 2006) (final rule) (Commission is building on the 1992 amendments intended to promote "comparability from year-to-year and company-to-company"),

or her job and talent level. Thus, at best, such payments relate indirectly to the NEO compensation structure and shed little light on it.

2. The Proposal Does Not Place Named Executive Officer Compensation in Perspective

Moreover, the additional disclosures required by the Commission's proposal would not provide information that assists in understanding the comprehensive explanations of the company's compensation program already required for the named executive officers. Under the SEC's new proxy disclosure rule, companies are required to provide an elaborate narrative description of the executive compensation programs and plans in the Compensation Discussion and Analysis,[5] six numerical tables with supplemental narratives and footnotes and additional narrative disclosure. These items present each element of a company's executive compensation program for NEOs and explain how they further a company's overall compensation objectives. No additional information is needed to fulfill this purpose.

This sentiment is clearly shared among the large companies that would be subject to the additional disclosure. According to the survey of HR Policy and WorldatWork members, when companies were asked whether the revised proposal would provide information useful to shareholders, analysts and the general public, two-thirds replied no and another 28 percent said any value would be extremely limited.[6]

3. The Revised Proposal Will Not Necessarily Enhance Understanding of Compensation Committee Approach to Senior Executive Compensation

Another reason the revised proposal would not result in the disclosure of more meaningful information to investors is that in many companies the Compensation Committee does not directly oversee all, and potentially even most, employees whose compensation that would be subject to disclosure. At many companies, the Compensation Committee is primarily focused on the senior management of the company. Often these individuals report directly to the CEO or are one step below the CEO's direct reports. Below this level, most compensation committees are responsible for ensuring the compensation plans are aligned with the company's business strategy. Typically, the Committee is briefed on outstanding performers and approves the incentive or equity plans in which they participate. However, the specific incentive levels and awards are typically left to the chief human resource officer and the managers directly overseeing that employee.

As discussed further below, the broad definition of those who exert "significant policy influence" is likely to sweep in employees who do not have any impact on the governance of the company and are not normally reviewed by the Committee. Disclosure of the total compensation of these individuals will not provide additional insight into the Committee's approach to setting senior executive compensation.

[5] The CD&A is the disclosure with the greatest impact because it adds texture to the required tabular information and enables investors to understand to the purposes and arguably evaluate the effectiveness of the programs.
[6] Clark Report, *supra* note 3, at 13.

B. Determining Employees Who "Exert Significant Policy Influence" Is Unworkable and Would Require Monitoring and Disclosure of Many Lower-Level Employees

In its revised proposal, the Commission has responded to criticisms by HR Policy Association and many others that the original proposal was overly broad by: (1) suggesting that it may consider expanding the group subject to disclosure to include all employees, including executive officers; and (2) excluding employees who have "no responsibility for significant policy decisions." Although HR Policy appreciates the Commission's willingness acknowledge the flaws in the original proposal, in practice, the revised proposal is still unworkable. It will continue to require disclosure of total compensation for some high-level nonexecutive employees, such as sales employees. More importantly, the vagueness of "significant responsibility for policy decisions" will make it difficult to determine which employees need to be monitored and disclosed and promote inconsistent application. The end product will only serve to confuse shareholders.

1. Most Highly Paid Employees Will Not Be Excluded by the "Significant Policy Decisions" Limitation as Defined by the Commission

The revised proposal excludes from disclosure employees that have "no responsibility for significant policy decisions" at the company, a principal business unit, division, or function of the company.[7] However, by definition, this means that employees with any responsibility for significant policy decisions are potentially subject to disclosure. As a practical matter, this does not eliminate many employees whose compensation could have been disclosed under the original proposal.

Within large companies, significant policy decisions are approved by an ultimate decision maker -- or a group of them -- but many individuals that report to the decision maker(s) also have responsibility for elements of the decision. For example, when a senior human resource executive approves a change in the company's retirement plan, the executive shares responsibility for the change with the Chief Financial Officer, the General Counsel and their staffs. Many others under each discipline have responsibility for aspects of the decision. For example, the vice president of compensation and benefits is responsible for heading up the change from the HR side, the chief investment officer has some responsibility for ensuring that the change is consistent with the company's principles, and the company's internal benefits attorney must also review and approve it. All of these individuals arguably would fit within the definition of "significant policy influence."

2. The Lack of Meaningful Direction on What Constitutes a "Significant Policy Decision" Will Lead to Inconsistent Application

The vagueness of the term "responsibility for significant policy decisions" will leave interpretation of the phrase to individual employers and result in inconsistent information for shareholders. The lack of clarity will drive many employers to interpret the phrase broadly, thus

[7] Revised Proposed Rule, 71 Fed. Reg. at 53268.

increasing the number of employees whose total compensation must be monitored for possible disclosure. However, others will interpret the phrase narrowly. This inconsistency will further dilute any helpful information that the proposed disclosure would provide.

In describing the revised proposal, the Commission notes that the phrase "responsibility for significant policy decisions could consist of … the exercise of strategic, technical, editorial, creative, managerial or similar responsibilities."[8] The revised proposal also provides several examples of positions that exercise such responsibility, such as the news director of a major network.[9] However, the information provided does not provide a clear line – or a framework for determining – when an individual has responsibility for significant policy decisions and when he or she does not. Defining where that line is will be a Herculean task involving fact-specific inquiries into the decisions on which the employee provides input.

For example, a highly compensated sales employee who also helps set sales strategy for the year would appear to be included under the revised proposal. This could result in the employer disclosing confidential information about its sales incentive structures. Likewise, a creative marketing employee who is responsible for one part of marketing policy would arguably be included. Even a news personality who had input on the production of his or her show could be considered covered. However, another employer with identical facts could make a different determination if it interpreted the standard narrowly. Regardless of the employer's interpretation, the amount of administrative work required to make these determinations cannot be justified given the small amount of useful information the disclosure would provide to investors.

C. The Additional Disclosure Would Impost Unacceptable Compliance Burdens on Large Issuers

By indicating that it may limit the revised proposal to large accelerated filers, the Commission is attempting to reduce the substantial compliance burdens and costs discussed by many who commented on the original proposal, including HR Policy Association. However, based upon the survey research by Professor Clark, HR Policy Association believes that large accelerated filers would shoulder unacceptable compliance burdens if it were implemented.

1. The Proposal Would Require Most Companies to Collect Substantial Data From Different Sources to Develop a Total Compensation Number

The survey summary shows that the Commissions revised proposal would create a substantial compliance burden. Over 70 percent of survey respondents indicated that they do not currently have systems in place to provide total compensation, as defined by the Commission's proxy disclosure rule, on highly paid employees throughout the company.[10] More specifically:

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[8] *Id*.
[9] *Id.*
[10] Clark Report, *supra* note 2, at 16, Appendix A, question 2.

- Only 20 percent of survey respondents indicated that they keep the information necessary to calculate total compensation in a single database;[11]
- 36 percent of companies responding reported that they keep compensation and benefits information in separate databases.[12] Consequently production of a total compensation figure would either require additional systems programming or manual calculations; and,
- 35 percent of respondents keep separate compensation and benefits databases for U.S. employees and employees of foreign subsidiaries.[13]

With respect to companies with a significant number of subsidiaries or divisions outside the U.S., different regulatory structures often require that they keep separate databases for each country in which they operate. Noting this, one survey respondent stated, “Our biggest concern would be in trying to identify and accurately value the total compensation package for a number of employees in foreign countries. In most years we would probably have no one to report but would need to spend a lot of time making sure.”[14]

The vast majority of large issuers, regardless of whether they have foreign operations, would incur substantial costs to develop the data necessary to comply. Over 70 percent of those firms stating that they did not maintain a total compensation number as defined by the Commission indicated that it would be difficult or very difficult and costly to develop and maintain such systems.[15]

In sum, the Commission’s revised proposal would require companies to develop a new infrastructure to calculate total compensation across more employees.

2. The Proposal Would Require Companies to Develop Total Compensation Information for a Significant Number of Additional Employees

In addition to developing new and more sophisticated systems for calculating total compensation as defined by the SEC, companies would effectively be required to develop the information for more employees to be sure that they are in compliance. One HR Policy Association member summarized the process of developing the information as follows: First, the company would have to develop a list of employees who would potentially be in the top three, and then calculate their total compensation to determine if total compensation disclosure is required.

When asked how many additional employees would have to be monitored to comply with the proposal, 67 percent of large companies surveyed indicated more than 10 employees,[16] 37 percent expected the number of employees to be between 10 and 25, and over 20 percent

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[11] *Id*. at 8.
[12] *Id*.
[13] Clark Report, *supra* note 2, at 9.
[14] *Id*. at 7.
[15] *Id*. at 9
[16] *Id*.

indicated between 26 and 100 employees.[17] Some respondents expressed concern that the pool of employees that would need to be monitored would change annually because of changes in compensation and responsibilities, further adding to the administrative burden.

3. The Cost of Compliance Far Outweighs the Benefit of the Proposal and Substantially Exceed the Commission's Estimate

Based on the survey results, HR Policy believes that the costs of the Commission's "other three" proposal would far exceed the benefits. Following the SEC's methodology, the survey asked participants to estimate the cost of compliance in the first year and in the second and subsequent years. Professor Clark found that the average annual cost for compliance over the first three years is expected to be $38 million or more than three times that of the SEC's estimate of $11 million.[18] This includes an average first year cost of $27,845, double the SEC's estimate, and an average cost in the second and subsequent years of $19,873, or eight times the SEC's estimate of $2,550.[19] From the responses, it is likely that companies believed there would be significant variability in collecting the data from year-to-year that would not be made significantly more efficient even after systems were in place.

Because we believe that the revised proposal would provide very little meaningful information to investors, the administrative cost and burdens of developing the information are excessive and unjustified.

D. The Revised Proposal Would Make It Easier for Competitors to Hire Away Talented, Highly Compensated Employees

We believe that the revised proposal would make it much easier for competitors to hire talented employees away from a company because the employee's total compensation information would be publicly available. The changes to the revised proposal that scale back the pool of employees subject to disclosure do not eliminate this concern. In fact, the changes may increase it.

Based on the survey, Professor Clark's research shows that over 85 percent of the survey respondents said the revised proposal would make it at least "a little easier" to hire away talented employees, with a third of the respondents indicating it would make such poaching "much easier" than under the current disclosure rules.[20]

The Commission has ostensibly aided such recruitment efforts by focusing on executive officers and, arguably, others in higher policymaking roles. This increases the chances that

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[17] *Id*. at 9-10.
[18] *Id*. at 14.
[19] *Id*.
[20] *Id*. at 12.

talented top managers, rather than lower level individuals such as sales employees, would be lured away by a competitor willing to top their compensation packages.[21]

Because of the poaching effect, the proposal would likely ratchet up pay for the additional employees whose pay is disclosed. In general, when a company looks seeks to recruit talent from outside, it often must pay a premium to persuade the individual to leave their current position. On average, this premium runs around 30 percent of pay. By making the pay information readily available, companies will need to be prepared to pre-empt the poachers, and this will cause total compensation to spiral upward.

E. The Proposal Would Disrupt Employee Relations

In addition to the administrative and cost burdens, increasing the chances of external recruitment and generating little useful information for investors, the revised proposal would create internal disruptions and employer morale issues by disclosing the pay of three additional employees. Even though the revised disclosure proposal requires only a job description, employees will be able to determine the identity of the individuals whose pay is disclosed. As one company noted, the disclosure will cause similarly situated employees throughout the company to make comparisons to the employees whose pay was disclosed. This will lead to low morale and additional unproductive time as employees seek to understand why they are not similarly compensated.

As with the original proposal, the revised disclosure requirements will raise privacy concerns for the individuals whose pay is disclosed. While senior officers of the company understand that disclosure is required when leading a publicly-traded company, lower-level executives and employees have no similar frame of reference. Mid-level executives may have confidentiality provisions as part of their employment agreements. As one survey respondent noted:

> Total rewards is a complex and confidential matter. To expose the value that we place on our most highly paid non-executive employees would be embarrassing for these individuals and demotivating for their peers.

Employees who are not executive officers who are paid well due to their performance level need to be respected by their peers, subordinates and managers, all of whose pay may be less than their own. One HR Policy member indicated that it would be concerned that an enterprising reporter would seek to develop a story around the disclosure of the other three employees, exacerbating the potential embarrassment and morale issues.

Thus, aside from providing little helpful information to shareholders and imposing substantial administrative burdens on employers, the proposal also is likely to be disruptive to the workforce. For these reasons the Commission should eliminate it from further consideration

[21] The proposal also would be a bonanza for headhunters because the information needed to do their job – a job description and total compensation -- would be provided in the proxy statement. From there, a headhunter could fairly easily identify the individual and seek to recruit him or her to a competitor.

CONCLUSION

We urge the Commission to eliminate any further consideration of its proposal to disclose the compensation of an additional three highly paid employees. We appreciate the opportunity to comment on the proposals, and would be pleased to discuss any questions the Commission may have with respect to this letter. Any questions about this letter may be directed to Timothy J. Bartl, Assistant General Counsel and Vice President, Corporate Relations at (202) 789-8692.

Respectfully submitted,

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Jeffrey C. McGuiness
President