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AMERICAN BAR ASSOCIATION

November 3, 2006

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Secretary, American Bar Association
Division for Policy Administration
American Bar Association
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Robert D. Evans
Director, Governmental Affairs Office
American Bar Association
740 15th Street, NW
Washington, D.C. 20005

Dear Sirs:

At its June 2005 meeting, the ABA Board of Governors approved the request of the Section of Business Law to submit technical comments to certain governmental executive branch agencies under Part D of the Association's Blanket Authority Procedure.

Pursuant to this authorization, the Section will submit the attached technical comments to the U.S. Securities and Exchange Commission. These technical comments are within the Section's primary and special expertise, and were approved by the Section Officers on October 31, 2006.

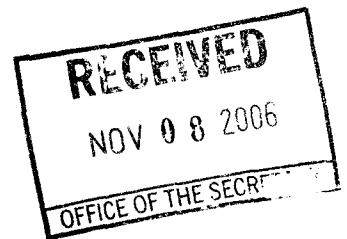
These comments were submitted to International Law and Practice Section on October 19, 2006. The comment period set forth by the SEC was 60 days. The Section of International Law has not expressed any objection to the attached.

Sincerely,

Linda Hayman
Chair

Section of Business Law

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By Electronic and United States Mail

October 31, 2006

Nancy M. Morris

Secretary

Securities and Exchange Commission

100 F Street NE

Washington, D.C. 20549-9303

Re: File No. S7-03-06

Release No. 33-8735; 34-54380

Executive Compensation Disclosure; Disclosure of Non-Executives' Compensation

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Federal Regulation of Securities of the American Bar Association, Section of Business Law (the "Committee") in response to the request by the Securities and Exchange Commission (the "Commission") for additional comments on a proposal to require narrative disclosure of total compensation for up to three additional highly compensated employees (the "Proposal") as set forth in the release described above dated August 29, 2006 (the "Release"). The Proposal refines a concept initially proposed in Release No. 33-8655 (January 27, 2006) (the "Initial Proposal").

The comments expressed in this letter represent the views of the Committee only and have not been approved by the American Bar Association's House of Delegates or Board of Governors and therefore do not represent the official position of the ABA. In addition, this letter does not represent the official position of the ABA Section of Business Law, nor does it necessarily reflect the views of all members of the Committee.

Overview

We appreciate the opportunity to comment further on the Proposal. When the Commission proposed in January 2006 to adopt new rules on disclosure of executive and director compensation, related party transactions, corporate governance matters and executive and director security ownership, we generally supported the Commission's proposals but opposed the proposal to require disclosure of compensation paid to non-executives. In light of the Commission's adoption of rules

that greatly expand on the scope of executive compensation disclosure and that broadly embrace a principles-based philosophy in calling for disclosures that will be meaningful to investors, we continue to believe that the Proposal does not advance appropriate policy objectives. In addition, we believe the Proposal is cast too broadly, creating a number of implementation issues. We address each of these below.

A. The Proposal does not further appropriate policy objectives

In response to the Initial Proposal, many commenters questioned whether the proposed disclosures constitute material information, given that the covered employees would not be in a policy-making position as executive officers. The Release suggests that if highly paid employees exert significant policy influence at the company,¹ at a significant subsidiary of the company or at a principal business unit, division or function of the company, “then investors seeking a fuller understanding of a company’s compensation program may believe that disclosure of these employees’ total compensation is important information.” The Release also suggests that disclosure of the proposed information “should assist in placing in context and permit a better understanding of the compensation structure of the named executive officers and directors.”

We respectfully suggest that disclosure of the amount of compensation paid three employees does not provide any context for a company’s general compensation program and does not further an understanding of a company’s compensation programs. Companies typically have a wide range of compensation arrangements applicable to various portions of their employee population. There is no evidence that we are aware of, and the Commission has not pointed to any, suggesting that disclosure of three employees’ compensation provides a basis for understanding the myriad arrangements that companies have in place for compensating all of their employees.

We also question the underlying premise that there is sufficiently broad investor interest in companies’ general compensation programs as to single this area out for a new “line item” disclosure requirement. As we stated in our comments on the Initial Proposal, the Commission has not provided an explanation of why this compensation information is any more deserving of disclosure than any other expenditure that a

¹ As discussed in further detail below, to the extent that the Proposal addresses compensation of persons who have significant policy-making authority at a company level or otherwise covers persons who are executive officers of the registrant, the Proposal runs counter to the Commission’s determination to limit the number of “named executive officers” for whom disclosure is required under the Commission’s recently adopted executive compensation and related party transaction disclosure rules. We believe that those recently adopted rules are designed to adequately provide investors with sufficient information regarding executive compensation without adoption of the Proposal.

company incurs in the course of business (such as amounts paid to an individual to purchase a business, the amount paid to a third party service provider or the amount paid to license intellectual property from an individual). The Commission and investors have not sought line item disclosure of the greatest amount spent by a registrant on a building, a patent license or a single research and development project; we do not believe that general employee compensation programs should be singled out for different treatment.

We also question the assertion that the Proposal “should assist in placing in context and permit a better understanding of the compensation structure of the named executive officers and directors.” The request for comment in the Release identifies a number of reasons why the Proposal would not further this objective. For example, the covered employees may not participate in the same compensation programs as the executive officers, and decisions regarding covered employees’ compensation may not be made by the board compensation committee or the other persons who set executive officers’ compensation. Most significantly, as we and others noted with respect to the Initial Proposal, there is no corporate governance nexus to the proposed disclosure. Because the covered employees may not have significant policy-making responsibility at the corporate level, their compensation does not implicate the related-party nature of directors’ and executives’ compensation and may not reflect on how the registrant is being governed. In addition, the Proposal would have a disparate impact from company to company based on factors such as the extent to which a particular company determines to hire and retain employees to handle certain tasks versus the extent to which a company may contract tasks out to non-employees.

In this respect, the Proposal represents a stark contrast to the disclosure regime established under the Commission’s recently adopted Compensation Discussion and Analysis (“CD&A”) requirements. As described by the Commission, the CD&A “is to provide material information about the compensation objectives and policies for named executive officers” and “is intended to put into perspective for investors the numbers and narrative that follow it.” The fact that the disclosure called for by the Proposal would not typically otherwise be addressed in the CD&A demonstrates that the Proposal does not serve the objective of “placing in context and permit[ing] a better understanding of the compensation structure of the named executive officers and directors.”² Moreover, mandating disclosure of the information called for under

² We recognize that the Commission has stated that in particular circumstances it may be appropriate for a company to address in its CD&A how any program, plan or practice to time option grants to executives fits in the context of the company’s program, plan or practice with regard to option grants to employees more generally. Similarly, we recognize that under a principles-based disclosure regime, in particular circumstances it may be appropriate for the CD&A to address how a named executive officer’s total compensation fits into the compensation program applicable to employees generally. For example, some companies have disclosed compensation policies based upon “internal pay equity,” where executive officer compensation levels are compared to the historic trend in the aggregate level

the Proposal when it would not otherwise be required under the CD&A is an unexplained divergence from the principles-based disclosure regime that the Commission determined to implement through the recently adopted executive compensation disclosure rules. Thus, we do not believe that the proposed rule, even with the modifications set forth in the Proposal, provides investors with material information necessary to understand the company's compensation policies and structure or executive compensation programs. We believe that this goal instead should and will be fulfilled by the CD&A.

Finally, in assessing whether there are policy considerations that support the Proposal, we believe that it is important for the Commission to recognize the significant costs that will be incurred by companies due to the disruption to internal employee relations that could result from the Proposal.³ We concur with other commenters who have noted that employees who are not executive officers have justifiable expectations of privacy that would be disrupted by the Proposal. More significantly, because the Proposal would apply to persons below the executive officer level within a company who may have many "peers" across the corporate structure, we believe that adoption of the Proposal could cause significant internal disruptions and internal "politics" since it would result in employees who believe their responsibility within a particular subsidiary, business unit, division or function to be comparable to that of others learning that some of the others are paid more than they are.⁴ This could lead to employee dissatisfaction, a general increase in the level of compensation within companies and/or increased employment turnover. While difficult to quantify, these potential costs could far exceed the Commission's cost estimates for the Proposal, and are reason enough to reassess whether implementation of the Proposal would materially benefit investors.

of non-executives' compensation levels. However, we believe the CD&A requirements already sufficiently accommodate such disclosure in those cases, which we expect will be rare, when such information would "place in context and permit a better understanding of the compensation structure of the named executive officers." Thus, we believe it could be consistent with the Commission's existing CD&A disclosure regime to amend Item 402(b)(2) to add "the extent to which non-executives receive greater compensation" as a sixteenth example of the type of information that could, depending on the facts and circumstances, be material to an understanding of executive officer compensation.

³ We note that the Commission has requested comments on whether implementation of the Proposal would result in disclosure of information that would be material to investors. We are not aware of any basis to conclude that the Proposal would provide material information and, as we discuss, believe that any assertion of possible benefits from the Proposal need to be weighed with the costs and other impact on companies' management of their non-executive talent.

⁴ Whether or not a company would be required to name the persons whose compensation is disclosed, it should be expected that within many companies other employees would be able to identify covered employees based on the disclosure and description of the employees' job position.

B. The text of the Proposal raises significant problems in implementation

The text of the Proposal set forth in the Release is cast overly broadly and gives rise to significant interpretive issues that we address below. Attachment A to this letter suggests revised language to address these concerns.

- The standard for determining which employees are covered by the disclosure requirement should be measured with respect only to persons who are “named executive officers” on account of the amount of their compensation. The goal of the Proposal presumably is to report information on compensation that is relatively high within a company. It seeks to achieve this goal by comparing the compensation of policy-making employees to compensation paid to the named executive officers. Under the Commission’s rules, certain persons are “named executive officers” on account of their status, regardless of the level of their compensation. In particular, persons who served as principal executive officer (PEO) or as principal financial officer (PFO) during the year will be a named executive officer even if their total compensation is relatively low.⁵ Requiring disclosure of employees who earn more than one of these named executive officers could result in disclosure of relatively low paid employees. Accordingly, if adopted, the language of the Proposal should be revised to operate in a manner similar to the existing standard for determining when an individual who ceased to serve as an executive during the year is a “named executive officer,” by requiring disclosure only if compensation is higher than that paid to the persons who are named executive officers on account of the level of their total compensation.
- The policy-making standard reflected in the Proposal does not do much to narrow the scope of covered employees because there is no standard for determining the significance of an employee’s responsibility. The significance standard applied under the existing definition of “executive officer” in Rule 3b-7 is useful because “significance” is measured with respect to the company as a whole. In contrast, the Proposal covers any employee who has a policy-making position that is significant “within the company, a significant subsidiary or a principal business unit, division or function.” This variable standard for measuring significance within and among variously sized operations and departments within a company will be difficult to apply and could result in widely disparate interpretations of

⁵ A PEO or PFO’s compensation could be low because they are a founder of the company and therefore receive relatively low levels of compensation (for example, Pixar’s 2005 proxy statement reports compensation of \$52 for its PEO, Steve Jobs, who owned a majority of the company’s stock) or because the person may have been employed for only a short period during the year (for example, a PEO or PFO who retires one month after the beginning of the year or who is hired one month before the end of the year will nevertheless be a named executive officer on account of status).

who is a covered employee. Likewise, it is impossible to gauge what constitutes “responsibility for significant policy-making decision within the company, a significant subsidiary or a principal business unit, division or function” when there is no standard for measuring significance. The Release itself demonstrates that any type of decision-making role by an employee might be encompassed by the rule, as it states that “Responsibility for significant policy decisions could consist of, for example, the exercise of strategic, technical, editorial, creative, managerial, or similar responsibilities.” Moreover, the proposed standard could result in the anomalous situation of providing compensation information for an employee who functions at a level within the company for which no other financial information is provided; investors would have more financial information on a single employee than on the subsidiary, business unit, division or function within which the employee exercises decision-making authority. We believe that a more appropriate standard for measuring significance below the corporate level would be to address only employees who have significant policy-making responsibilities for a reportable business segment.⁶ Under this approach, investors would have financial information on the business where the employee works, enabling them to put the compensation information in context. We do not believe that naming the covered employees provides any further context to the information; describing their position within the reportable business segment alone would provide sufficient context to the information.

- The Proposal should only apply to persons who demonstrably perform significant policy-making functions, instead of being drafted to apply to highly compensated employees absent a demonstration that an individual “has no responsibility for significant policy-making decisions.” As drafted, the Proposal would require a company to prove a negative; that the employee had not at any time been responsible for a significant policy-making decision. The proposed language heightens the vagueness of the Proposal and thereby would increase companies’ compliance costs.
- The Proposal should not expand the class of executive officers for whom compensation disclosure is required. The Initial Proposal would have required disclosure with respect to “up to three employees who were not executive officers during the last completed fiscal year.” Without any explanation for the change, the Proposal has been expanded to cover highly compensated employees “whether or not they were executive officers during the last completed fiscal year.” For companies where persons who served during the year as PEO and PFO are not among the highest paid executives, the standard will result in additional disclosure on executive compensation. This aspect of the Proposal

⁶ See Exchange Act Rule 3b-7, defining “executive officer” as, among other things, one “who performs similar policy making functions for the registrant.”

increases the lack of focus, and thus the lack of utility, of the proposed disclosure. Limiting disclosure to those who earned more than persons who are "named executive officers" on account of the amount of their compensation, as we suggest above, eliminates this disparity from the operation of the provision.

- We agree that the determination of whether an employee is "highly compensated" under the Proposal should be measured in the same manner as for named executive officers under the Commission's executive compensation rules, in order to reduce the number of interpretive questions that would arise.
- In order to allow companies sufficient time and experience in identifying the most highly compensated executive officers for purposes of Item 402(a)(3) and for establishing systems for identifying employees who are more highly compensated than such executive officers, if the Commission adopts the Proposal it should be applicable only for disclosures in fiscal years ending on or after December 15, 2007.

We believe that the foregoing revisions are necessary to make the Proposal workable. However, even with these revisions, we believe the Proposal does not advance investors' understanding and could cause significant internal disruptions, and therefore we continue to oppose the Proposal.

The Committee appreciates the opportunity to comment on the Proposal and respectfully requests that the Commission consider the recommendations set forth above. We are prepared to meet and discuss these matters with the Commission and the Staff and to respond to any questions.

Respectfully submitted,

/s/ Keith F. Higgins

Keith F. Higgins
Chair, Committee on Federal Regulation of Securities

cc: Christopher Cox, Chairman
Paul S. Atkins, Commissioner
Roel C. Campos, Commissioner
Annette L. Nazareth, Commissioner
Kathleen L. Casey, Commissioner
John W. White, Director, Division of Corporation Finance

Nancy M. Morris, Secretary
Securities and Exchange Commission
October 31, 2006
Page 8

Drafting Committee:

Ronald O. Mueller, Drafting Chair

Anne Plimpton

George R. Ince, Jr.

Christine M. Daly

W. Alan Kailer

Ann Yvonne Walker

Scott Spector

Attachment A
Suggested Language Revisions

For each of the company's three most highly compensated employees employed at the end of the fiscal year who perform significant policy-making functions for a reportable segment of the registrant and, whether or not they were executive officers during the last completed fiscal year, whose total compensation (as calculated pursuant to paragraph (c)(2)(x) of this Item, reduced by any amounts described in paragraph (c)(2)(viii) of this Item) for the last completed fiscal year was greater than that of any of the named executive officers described in paragraph (a)(3)(iii) of this Item, disclose each such employee's total compensation for that year and describe the employee's job position, without naming the employee; ~~provided, however, that employees with no responsibility for significant policy decisions within the company, a significant subsidiary of the company, or a principal business unit, division, or function of the company are not included when determining who are each of the three most highly compensated employees for the purposes of this requirement, and therefore no disclosure is required under this requirement for any employee with no responsibility for significant policy decisions within the company, a significant subsidiary of the company, or a principal business unit, division, or function of the company.~~