October 23, 2006

Re: Re-Proposed Requirement to Disclose Compensation Of Up to Three Non-Executive Officers (File No. S7-03-06)

Dear Ms. Morris:

The Securities and Exchange Commission (the "Commission") has requested additional comments on the Commission's modified proposal that large accelerated filers be required to disclose the job descriptions of and amount of total compensation paid to up to three highly compensated employees who are not executive officers but who earn more than the registrant's named executive officers (the "Proposal").[1] We welcome the opportunity to comment on the Proposal.

The undersigned are writing on behalf of seven of the leading U.S. financial services institutions. Our companies are engaged in providing a broad range of financial services in the domestic and global markets, including consumer, corporate and investment banking; insurance; asset management; and prime brokerage services. Together, our companies play an important role in the successful functioning of the capital markets and contribute to the health of the U.S. and global economies.

We share a commitment to striving to maintain the highest standards of corporate governance and we commend the steps the Commission has taken towards improving the transparency to investors of registrants' executive compensation and related party transaction policies and practices. However, we believe that the Proposal would not further these goals, for the following reasons:

- The Proposal would not contribute to the Commission's ongoing efforts to enhance the material information available to investors in the area of compensation.
    - The disclosure that would be elicited by the Proposal is not material to understanding the compensation of the named executive officers and directors.

[1] The concept of compensation disclosure for up to an additional three employees (the "Original Proposal") was originally set forth as part of the Commission's proposed rules regarding executive compensation and related party transaction disclosure in Release Nos. 33-8655; 34-53815 (the "Proposing Release"). The Original Proposal was not included in the final rules adopted in Release Nos. 33-8732A; 34-54302A (the "Adopting Release"); rather, the Commission requested further comments on the proposed new disclosure requirement respecting the additional three employees and on whether it should be modified as discussed below.

- The compensation paid to the additional employees who would be covered by the Proposal is not material to registrants.

- The Proposal would not enhance corporate governance because the self-dealing, conflict and related risks that exist with executive officers do not exist with the additional employees who would be covered.

- The Proposal would result in competitive harm to U.S. financial institutions vis-à-vis our foreign competitors (whether or not registered with the Commission) and private entities such as hedge funds and private equity firms, and would have a disproportionate and adverse effect on the U.S. financial services industry.

- In addition to such competitive harm, the Proposal would raise privacy and security concerns and would impose significant administrative burdens on affected registrants.

- The Proposal, as modified to cover only large accelerated filers, has no basis in disclosure principles and raises disclosure issues that may not be fully and appropriately addressed through the current comment process.

We strongly urge the Commission not to discount the potentially serious competitive harm particularly affecting the U.S. financial services industry (and other industries whose success is similarly dependent on human capital) that would result from adoption of the Proposal. We also believe that the negative consequences associated with the Proposal outweigh any potential corresponding benefit of providing the contemplated information to investors.

I. Summary of the Proposal

The Original Proposal, as set forth in the Adopting Release, would have required the following disclosure:

> For up to three employees who were not executive officers during the last completed fiscal year and whose total compensation for the last completed fiscal year was greater than that of any of the named executive officers, disclose each of such employee's total compensation for that year and describe their job positions.

The Commission requested further comments on this disclosure requirement, and specifically on the following modifications to the Original Proposal:

> For each of the company's three most highly compensated employees, whether or not they were executive officers during the last completed fiscal year, whose total compensation for the last completed fiscal year was greater than that of any of the named executive officers, 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.

As examples of employees who would not be subject to this disclosure requirement, as modified, the Commission cited sales persons, entertainment personalities, actors, singers and professional athletes. As examples of employees who do have responsibility for significant policy decisions, the Commission cited the director of the news division of a major network; the principal creative leader of the entertainment function of a media conglomerate; or the head of a principal business unit developing a significant technological innovation. The Commission also stated that as a general matter "investment professionals (such as a trader, or a portfolio manager for an investment adviser who is responsible for one or more mutual funds or other clients)" would not be deemed to have responsibility for significant policy decisions, but "an investment professional, such as a trader or portfolio manager, who does have broader duties within a firm (such as, for example, oversight of all equity funds for an investment adviser) may be considered to have responsibility for significant policy decisions." In addition, the Commission has proposed that this disclosure requirement as modified would apply only to large accelerated filers.

II. The Proposal Would Not Contribute to the Commission's Ongoing Efforts to Enhance The Material Information Available to Investors in the Area of Compensation.

The Proposal would not further the policy goals underlying the Commission's approach to pay disclosure generally, and there is no demonstration in the Proposing Release, the Adopting Release or the comments to date that it would further any policy goals. As discussed below, proposals to require similar disclosure, and previously existing requirements covering similar subject matter, have been rejected after consideration by the Commission in the past because the Commission has concluded, correctly, that the information elicited is not material to investors.

(a) The Disclosure Is Not Material to Understanding the Compensation of the Named Executive Officers and Directors.

Contrary to the Commission's assertion in the Adopting Release, the Proposal would *not* "assist in placing in context" or "permit a better understanding of the compensation structure of the named executive officers and directors." It is hard for us to understand how the disclosure of the compensation paid to up to three additional employees who have *any* responsibility for significant policy decisions within the company, a significant subsidiary, or a principal business unit, division or function of the company, and who earn more than the lowest paid named executive officer could possibly assist in understanding the structure of the compensation of the named executive officers (and still less of the directors). This is particularly true given the fact that the employees included in the additional three are highly likely to change from year to year based on short-term or even fortuitous events with no disclosure significance.[2]

[2] For example, the inclusion of a non-executive officer employee who, in a given year, might be more highly compensated than the named executive officers as a result of a one-time, extraordinary payment such as a severance payment or a signing bonus designed to make that employee whole for compensation forgone at a previous

Investors should look to the Compensation Discussion and Analysis section (which will be a filed, not furnished, document) for a principles-based explanation of the material factors relating to compensation objectives and decisions relating to named executive officers, rather than to disclosure of compensation of these three other highly compensated employees.[3]

(b) The Compensation Paid to the Additional Employees Who Would Be Covered by the Proposal Is Not Material to Registrants.

There is no reason to think that the compensation of employees who have no policy-making function at the registrant level, even if they are highly paid, would be material to the registrant as a whole. If this information were material in connection with the company's use of corporate assets it would, in any event, be subject to separate disclosure requirements. There is no reason to single out this particular cost of doing business from any other and treat it as presumptively material.

(c) The Proposal Would Not Enhance Corporate Governance Because the Self-Dealing, Conflict and Related Risks That Exist With Executive Officers Do Not Exist with The Additional Employees Who Would Be Covered.

In earlier guidance concerning the disclosure of management compensation, the Commission has noted that the materiality of the information in question arises, at least in part, from the fact that executive officers of the company may have a role in or some influence over the setting of their own pay. For example, in Release No. 33-5856 (August 18, 1977) the Commission noted that "[f]ull disclosure of remuneration is necessary to informed voting and investment decisions regardless of whether the company's board of directors or its security holders have approved the remuneration package received by management, **because of the substantial influence of management in determining its remuneration**."[4] This rationale does not extend to the compensation of employees who have no authority to make policy decisions for the registrant and who have no opportunity for "self-dealing" in the determination of their compensation. As Institutional Shareholder Services argued in its comment letter in response to the Proposing Release, the disclosure required by the Proposal would "provide little value to shareholders" because "[u]nlike the named executive officers, the three non-officer employees are generally not individuals who have the ultimate authority over the company's strategic imperatives or broad business activities."[5] The additional employees who would be covered by

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employer would do nothing to inform investors' understanding of the registrant's executive compensation framework.

3 The Commission has expressed some concern that companies have avoided disclosure of the compensation of certain employees who have policy-making authority at the registrant level. Such an employee should be deemed to be an "executive officer" of the registrant and his or her compensation would (if the employee is so highly compensated as to be among the named executive officers) be required to be disclosed under the existing rules. The Commission has further "clarified this point" by calling attention in the Adopting Release to Instruction 2 to Item 402(a)(3), which remains unchanged following the recent amendments. This instruction emphasizes that it may be appropriate for the registrant to include as named executive officers one or more executive officers or other employees of subsidiaries in the disclosure required by Item 402. As a result, the concern has been addressed.

4 Emphasis added.

5 Prior to the 1992 amendments of management remuneration disclosure, registrants were required under Item 4(a) of Regulation S-K (and previously under Item 7(a) of Schedule 14A) to disclose aggregate management remuneration of "officers" of the company as a group. The Commission noted in an interpretive release that the

the Proposal are by definition not executive officers who perform policy-making functions for the registrant (if they were, they would be named executive officers). In addition, in most companies, the compensation of employees in this category is set with processes and dynamics different from those for executive officers.[6]

II. <u>The Proposal Would Result in Competitive Harm to U.S. Financial Institutions Vis-À-Vis Foreign and Privately Held Competitors and Would Have a Disproportionate and Adverse Effect on the U.S. Financial Services Industry</u>.

Disclosure of information about the compensation of highly paid financial professionals would place the affected registrants at a competitive disadvantage vis-à-vis competitors who are not required to disclose equivalent information. In particular, many peers of major U.S. financial institutions are foreign-based financial conglomerates that compete for intellectual capital with our companies in the same markets. Such peer entities may or may not be registered with the Commission as foreign private issuers; whether or not they are so registered, they are not subject to the executive compensation disclosure regime that applies to U.S. issuers. The Commission must understand that the firms signing this letter compete for talented human capital with foreign competitors all over the world. We will be placed at a significant competitive disadvantage in every financial center, within and outside the United States, if the Proposal is adopted.

The required disclosure would amount to providing competitors and headhunters with a shopping list of some of the registrant's key employees with price tags attached. (While the Proposal would not require the names of the employees to be provided, there is no doubt that competitors, headhunters and the media would be able to identify them almost immediately.) Not only would foreign-based competitors be in a position to "poach" the best financial professionals from registrants subject to the Proposal, but they would also be more attractive as employers because they would not be required to invade the privacy of employees by publicly

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covered officers "should have policy and decision-making responsibilities with respect to activities of the registrant [or] a significant subsidiary, division or function" – a group almost identical to the employees potentially covered by the Proposal (Release Nos. 33-6166; 34-16419 (December 12, 1979)). The requirement to disclose *even the aggregate compensation of these employees as a group* was dropped in connection with the 1992 amendments, reflecting broad commenter support for abandoning this requirement, presumably due to the lack of materiality to investors of the information elicited (Release Nos. 33-6962; 34-31327 (October 16, 1992)). It would be ironic indeed for the Commission to return to a variant of a concept that it rejected in 1992 after several decades' experience, especially when the disclosure required under the Proposal would be more arbitrary and less informative in operation than it was under the rule that was superseded fourteen years ago.

[6] In 1978, the Commission proposed a rule requiring disclosure of the remuneration of "the next five most highly compensated officers or directors of the registrant, or executive officers or directors of wholly owned subsidiaries, other than those individuals named in response to item 4(a)(i)" (the precursor to Item 402 of Regulation S-K) (the "1978 Proposal") Release Nos. 33-5940; 34-14904 (June 29, 1978). The 1978 Proposal elicited a large number of negative comments, which were summarized by the Commission in a subsequent release announcing that this aspect of its proposals was being abandoned. In the Commission's words, commenters pointed out *inter alia* that the required disclosure would not result in "any materially important new information becoming available to shareholders and investors" because, "since the heads of subsidiaries are generally not in a position to determine their own salary levels, the possibility of conflict or abuse in connection with establishing their levels of compensation is reduced." Release Nos. 33-6003; 34-15280 (December 4, 1978). (The heads of subsidiaries who perform policy-making functions for the registrant are, of course, deemed to be executive officers of the registrant under Rule 3b-7 and are within the scope of the existing executive compensation disclosure rules.)

disclosing what may to them be sensitive private compensation information. Furthermore, as noted above, this significant competitive harm would not be offset by the provision of any material information to investors. In addition to competition from foreign firms, publicly held financial institutions face stiff competition for talented employees from private entities such as hedge funds and private equity firms, which would also enjoy the advantages described above in being able to identify and hire away especially productive employees. The Commission should not discount the potential talent drain away from U.S. publicly traded financial institutions to non-U.S. and privately held competitor entities.

Disclosure of compensation information regarding employees who are not executive officers could also lead to significant problems inside the company. As the Commission noted in deciding not to adopt the 1978 Proposal, such information generally "is considered very confidential within the corporation," and pay levels may vary greatly due to "a number of factors which may have no disclosure significance, such as seniority, pay scales in the industry, special arrangements to induce employment, employment contracts entered into at the time the subsidiary was acquired, and foreign cost-of-living allowances." The Commission noted that various adverse consequences could result from the disclosure of this sensitive information, including "a loss of morale, a trend toward standardization of salaries at higher levels without regard to individual factors and a danger of pirating of employees by competitors willing to pay a higher salary."[7] Individual compensation information is a sensitive matter that is usually kept highly confidential within a company for good reasons. Revealing the compensation of the company's most highly paid employees would invite other senior employees working in what might be considered similar positions to compare the disclosed amounts to their own compensation. This would cause internal dissension and would exert upward pressure on compensation, as other employees would tend to look to the compensation of the most highly paid as a benchmark. Other perverse and surely unintended consequences of adopting the Proposal could include causing talented employees to avoid providing their expertise to their employers beyond management of portfolios, trading or similar responsibilities in order to avoid the risk of having policy-making responsibilities that would bring them within its scope, and encouraging registrants to increase the compensation of the named executive officers so that no non-executive officer employees would receive more than the lowest paid named executive officer.

The Original Proposal would have captured any employee, regardless of his or her position or responsibilities with the company, who earned more than any of the named executive officers. This proposed requirement raised concerns regarding a broad range of industries, including the entertainment, apparel, financial and sports industries, where it is not necessarily uncommon for individual non-executive employees such as performers, designers, traders and athletes to be paid more than the most highly compensated members of management.

If adopted with the modifications suggested by the Commission, the Proposal would not appear to apply to many of the employees described above. The Proposal would continue to risk application in any industry where talented, highly paid human capital is at the

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[7] Release Nos. 33-6003; 34-15280 (December 4, 1978). The Commission's comments referred specifically to disclosure of the pay of heads of subsidiaries. As noted above, heads of subsidiaries are deemed under the current rules to be executive officers of the registrant if appropriate in light of their responsibilities, and the compensation of heads of subsidiaries who are in this position is already potentially subject to disclosure.

core of success, including in particular the financial services industry. An exceptionally productive investment banker, trader or portfolio manager who is more highly compensated than the lowest paid named executive officer might well have some responsibility for significant policy decisions at the level of a significant subsidiary or business unit, division or function of the company but no such responsibility at the registrant level. For example, the Proposal cites as an example of an individual who would come within its scope a trader or portfolio manager who has broader duties within a firm, such as oversight of all equity funds for an investment adviser. Significant policy decisions could, depending on the facts, also include other areas, such as portfolio selection, portfolio guidelines, position limits, trading models and the like, where highly compensated employees could have *some* responsibility. It is by no means unusual for the most talented and productive (and correspondingly highly paid) investment professionals to have some managerial responsibilities of the kind described, whereas in industries such as entertainment and sports this would presumably be more rare. As a result, the Proposal, apparently unintentionally, effectively targets industries such as our own whose success is highly dependent on human capital. We believe that this outcome is inconsistent as a policy matter with the Commission's goal of providing uniform disclosure that lends itself to comparability between companies and across industries.

III. The Proposal Would Impose Significant Additional Burdens on Affected Registrants, Including Privacy and Security Concerns and Administrative Costs.

In addition to the competitive costs, which would be paramount, the disclosure required by the Proposal would result in additional costs and risks to affected registrants. First, the Proposal would raise severe privacy and security concerns. Although the Proposal does not require identification of the relevant individuals by name, the disclosure that would be required (total compensation and job description) is such that, as noted above, anyone familiar with the registrant's business – including competitors, customers and the media – would be able to determine quickly who the individuals were. In some cases, highly compensated financial professionals could be based at a subsidiary or business unit in a foreign country where personal security is a significant concern, and disclosure of their compensation information will increase the costs to the company of protecting the security of such employees and decrease the company's ability to retain them.

More importantly, whatever the Commission's objective judgments may be as to the legitimate privacy concerns involved, we can each assure the Commission that highly compensated employees make their own subjective judgments as to their own legitimate privacy interests, and that those subjective judgments will drive the behavior of the employees affected to the detriment of our firms' competitive position. In short, some highly compensated employees are likely to go to work for a non-U.S. or private competitor if the consequences of working for us involve disclosure of their compensation. Obviously, in the case of named executive officers, privacy concerns have been considered by the Commission and viewed as outweighed by the legitimate interest of investors in understanding the company's compensation policies and practices with respect to these individuals. However, as discussed above, there is no material interest favoring disclosure with respect to non-executive officer employees of a company that would outweigh these significant privacy concerns.

In addition, the Proposal would impose considerable administrative and information-gathering burdens on the affected registrants. It will not always be clear, even with careful analysis, which non-executive officer employees have "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," and the distinction between those employees and employees who do not have such responsibility is not a bright line. In addition, it is unclear what level of responsibility for policy decisions – beyond no responsibility at all – is sufficient to bring an employee within the scope of the Proposal. On its face, the Proposal captures all employees who have *any* responsibility for the covered "significant policy decisions," without any qualification as to the extent or materiality of the employee's involvement in the decision. This literal interpretation, which as a practical matter seems implausible, would greatly increase the broad sweep of the Proposal and the difficulty of administering it; however, if the Proposal is in fact intended to capture only employees with something more than no responsibility or a *de minimis* level of responsibility for policy decisions, registrants would be required to make difficult judgment calls about where that line should be drawn. In addition, we question the need for yet another definition delineating a category of employees for disclosure purposes, in addition to the numerous existing categories that are based on a more solid rationale than the Proposal.[8]

The Commission has specifically requested comments on its estimate regarding the costs of determining which employees meet the standards for disclosure and on monitoring and collecting compensation information with respect to potentially covered employees. The Commission has estimated that the average annual cost would be approximately $11 million, based on an assumption that companies will on average retain outside counsel to advise them regarding which employees meet the disclosure standard for eight hours in the first year and two hours in each of two succeeding years, at $400 per hour. While the costs associated with the Proposal would vary widely depending on the particular facts and circumstances of each registrant, we have no doubt that the Commission's estimate is far lower than the actual costs that would be incurred by companies with potentially covered employees. As noted above, the analysis of which employees could be covered is a complex one, and we expect that considerable resources would be devoted to developing a fully reasoned position on these questions. These would include substantial internal resources, as well as time billed by outside counsel which we anticipate will be well in excess of eight hours and well in excess of $400 per hour.[9] Furthermore, the interpretive questions that arise would not be settled once and for all in the first year; both the questions and the information-gathering and verification processes would continue

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[8] See, e.g., the definition of "executive officer" under Rule 3b-7; the definition of "officer" under Rule 16a-1(f); the category of named executive officers described in Item 402(a)(3) of Regulation S-K; and the category of employees with respect to whom disclosure is required under Item 5.02 of Form 8-K (all of which categories are slightly different).

[9] For example, if a trader sits on a credit committee along with six other members, would that individual be considered to have *any* responsibility for the "significant policy decisions" made by the committee, such that he or she could potentially be covered by the Proposal? Would the answer change if the individual were one of only three members of the committee? Would it change if the individual were the chair, or the co-chair, of the committee? We expect that questions of this nature would arise frequently throughout the first and subsequent years, and for any registrant aspiring to adopt best practices in disclosure would necessitate extensive discussions with internal and external counsel.

from year to year with changes in the registrant's factual situation. The ongoing cost burden would therefore continue to be significant, and is wholly underestimated by the Commission.

Having reached a determination as to which employees are potentially covered, registrants would have to track all components of compensation for those employees, who may be spread out among numerous subsidiaries and business units and/or located in foreign countries, throughout the year in order to determine whether any of them is more highly compensated than the named executive officers and, if so, for which employees disclosure is required. In an industry such as ours where pay can vary radically from year to year based on full year performance, the compensation of numerous individuals will need to be tracked and only at year-end will the registrant be able to determine whose compensation has to be publicly disclosed. Even if the registrant anticipates that only a few employees are likely to receive compensation exceeding that of the lowest paid named executive officer, extraordinary and unpredictable payments, such as signing bonuses and other inducement grants, could cause an employee to be included in the group unexpectedly; accordingly, in order to ensure that all the information potentially required to be disclosed will be available as needed, registrants would have to monitor the compensation of *all* employees with the relevant policy-making authority. Furthermore, registrants would have to calculate the relevant amounts following the methods required under the executive compensation disclosure rules, including items such as the aggregate incremental cost of perquisites and the actuarial value of defined benefit pension plans, which are complex calculations not performed in the ordinary course with respect to employees other than the named executive officers. We believe that the Commission's estimate may not reflect a full appreciation of the administrative costs of monitoring and compiling this information, which (while, again, they will vary from case to case) will be considerable and will also be ongoing.

Finally, the Proposal would drive additional expenditure of corporate resources because, as noted above, it would create inflationary pressure on compensation and would result in loss of key employees to competitors with concomitant costs of searching for and hiring replacement employees.

IV. <u>The Proposal As Modified to Cover Only Large Accelerated Filers Has No Basis in Disclosure Principles and Raises Disclosure Issues That May Not Be Fully and Appropriately Addressed Through the Current Comment Process</u>.

The Commission has proposed limiting the application of the Proposal to large accelerated filers. However, the Commission has not to date drawn lines regarding disclosure requirements at the large accelerated filer point and, indeed, has to a great extent resisted distinctions in disclosure requirements (as opposed to materiality determinations) based on issuer size. (Slightly different requirements for small business issuers under Regulation SB are not relevant to the issue of whether accelerated filers or large accelerated filers should operate under different disclosure rules.) Thus, such a limitation would be a significant departure for the Commission, and it would be a first-time departure in a circumstance where the rationale for the departure is not clear. Modifying the Proposal to apply only to large accelerated filers would not "focus this disclosure obligation on companies that are more likely to have these additional highly compensated employees." Indeed, it may be the case that such employees are more prevalent, or disclosure of such information might provide more information regarding corporate governance, in smaller companies. Furthermore, the proposed distinction would put large firms at a competitive disadvantage to smaller or so-called "boutique" investment firms. The limitation to large accelerated filers has no basis in disclosure principles, but rather is an arbitrary threshold.

V. Conclusion

For the reasons set forth above, we urge the Commission not to adopt the Proposal. We thank the Commission for the opportunity to submit the foregoing comments. We would be very happy to discuss our comments with you and to respond to any questions you may have. Please feel contact any of the undersigned through the contact information below if you wish to discuss these matters further.

Sincerely,

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