GovernanceMetrics

Howard Sherman
President and CEO
Direct Line 212 949 1313 Ext. 301
hsherman@gmiratings.com

August 19, 2009

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

VIA E-MAIL

Re: Proxy Disclosure and Solicitation Enhancements (File No. S7-13-09)

Dear Ms. Murphy:

I am writing on behalf of GovernanceMetrics International (GMI), the corporate governance research and ratings firm.

The SEC proposal concerning proxy disclosure and solicitation enhancements includes a wide range of thought-provoking recommendations and questions concerning enhanced compensation disclosure (section A), enhanced director and nominee disclosure (section B), new disclosure concerning compensation consultants (Section D), reporting of voting results on form 8-K (section E) and the proxy solicitation process (section F).

Given the nature of our business and our client base we have a strong interest in each of these areas. But we think we can be most helpful by focusing on one area in particular, new disclosure about company leadership structure and the board's role in the risk management process (section C).

Board Leadership GMI supports the Commission's proposed new requirement to Item 407 of Regulation S-K and a corresponding amendment to Item 7 of Schedule 14A that would require disclosure of the company's leadership structure and why the company believes it is the best structure for it at the time of the filing.

GMI does not think there can ever be a single litmus test of good or bad corporate governance. The governance process is far too complex, which is why our database includes more than 400 indicators (metrics) per company. These cover the gambit from structural checks and balances to a wide range of behavioral issues. When these hundreds of metrics are compiled, given that we evaluate companies on a relative basis, we are confident there is a significant variation in the quality of corporate governance and the risk associated with governance weaknesses when you compare a company rated at the very low end of our scale to one rated at the very high end.

But even within our own system some criteria are given more emphasis than others. To wit, the first set of metrics in our company database concern Board Leadership.

We are aware that many in the governance community think the time has come to separate the chairman and CEO positions through legislation or regulation. We prefer the Commission's proposed disclosure route and note that there has been an evolution, albeit a very gradual evolution, in board leadership among US companies even without enhanced disclosure requirements.

For example:

- 62% of the S&P 500 Index companies had a combined chair / CEO as of June 2009, compared to 66% three years earlier

- 53% of the 1,748 US companies covered by GMI had a combined chair / CEO as of June 2009, compared to 57% three years earlier

We agree with the Commission that disclosure of board leadership structure and why the company believes this is the best structure will increase the transparency for investors into how boards function.

The Board's Role in the Risk Management Process We agree in principle with the Commission that "disclosures of the board's role in the risk management process may also benefit investors. Expanded disclosure of the board's role in risk management may enable investors to better evaluate whether the board is exercising appropriate oversight of risk management. Investors would be able to adjust their holdings, allocating more capital to companies in which they believe the board is adequately focused on risks."

We think the latter is a critical point. Some recent studies in fact have found a statistically significant, inverse relationship between governance quality and cost of capital – the market rewards companies perceived to have better governance practices, in other words.[1]

We would however suggest that as the Commission moves ahead with this topic it considers disclosures concerning the board's role in the risk oversight process as opposed to risk management. It's a subtle but important point as questions about separation of responsibilities between the board and management are at the heart of effective governance. In our view the board's role is to oversee; the management has to manage on a daily basis.

We also suggest the Commission focus its disclosure efforts in a few areas:

Structure – How is the board structured to oversee risk? For example, is there an independent risk committee or subcommittee or is the risk oversight process handled in different way? Similarly, how is risk management structured at the company level? Does the company employ a chief risk officer or risk management group? Does the company make use of enterprise risk management (ERM) and if so how rigorous is its ERM program? How does the nature of the business (e.g., financial v non-financial) affect how the board and management structure risk oversight and risk management?

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[1] See for example, Jeroen Derwall and Patrick Verwijmeren, "Corporate Governance and the Cost of Equity Capital," European Centre for Corporate Engagement, ECCE Research Note 06-01, January 2007, and Hollis Ashbaugh-Skaife, University of Wisconsin-Madison and Ryan LaFond, Sloan School of Management –MIT, "Firms' Corporate Governance and the Cost of Debt", January 2006.

GovernanceMetrics International One Exchange Plaza, 55 Broadway, 11th Floor, New York, NY 10006 **T** 212 949 1313 **F** 212 599 0274 **W** www.gmiratings.com

Process – Just as our database includes both structural and behavioral items, we think enhanced disclosure concerning the process of risk oversight and risk management, including lines of reporting and communication is critical. We recommend that any new disclosure requirements should address questions "such as whether the persons who oversee risk management report directly to the board as whole, to a committee, such as the audit committee, or to one of the other standing committees of the board; and whether and how the board, or board committee, monitors risk."

To assist the Commission in its deliberations GMI would like to submit two related documents along with this comment letter.

"The Importance of ERM during Economic Upheaval" is a white paper jointly published in February 2009 by our firm and Marsh Inc., the world's largest insurance broker and strategic risk advisor. Among other things, our survey found while companies were in the process of adopting risk oversight and risk management processes and policies at an accelerated rate, standard disclosure about the governance of risk oversight was still clearly lagging.

The second document is a GMI news released dated June 29, 2009, "GMI Looks at Corporate Boards and Risk Oversight." This release announced the introduction of new metrics concerning risk oversight at the board level along with an increased emphasis on the experience of directors responsible for oversight of financial reporting or risk oversight in our rating.

Based on the favorable reaction from both rated companies and our institutional and advisory clients, we believe the Commission is absolutely right to push for improved disclosure in the area of risk management and board level oversight, and commend you for starting the process.

Thank you for the opportunity to comment. We would be happy to answer any questions.

Sincerely yours,

Howard Sherman
Chief Executive

GovernanceMetrics International One Exchange Plaza, 55 Broadway, 11th Floor, New York, NY 10006 **T** 212 949 1313 **F** 212 599 0274 **W** www.gmiratings.com

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February 2009

The Importance of ERM During Economic Upheaval

Compiled by:

Christy Kaufman, Marsh Inc.

Julie Oh, Marsh Inc.

Howard Sherman, GovernanceMetrics International

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Introduction

In response to the recent economic challenges, it has become increasingly important for organizations to solidify their approach to risk management as part of sound corporate governance. Enterprise Risk Management (ERM) is a disciplined and integrated approach that supports the alignment of strategy, process, governance, people, and technology, and allows organizations to identify, prioritize, and effectively manage their critical risks. A robust ERM program provides management a portfolio view of risks affecting the organization.

With a successful ERM approach, organizations can learn to anticipate and successfully manage critical risks. By recognizing and responding to uncertainties before they erupt, organizations can help to avoid losses, improve allocation of resources, and stay ahead of competitors. In these uncertain economic times, it can mean the difference between staying in business and starting over.

Adding fuel to the economic fire, several market analysts, including Standard and Poor's, recently announced their intent to include an evaluation of non-financial firms' risk management practices within their global credit ratings process. Moody's is adopting a similar, though less formal, focus. Regulators are also increasingly interested in promoting predictable, transparent, and sustainable risk management practices. As a result, even the most financially sound companies may experience increased regulatory oversight during this tumultuous time.

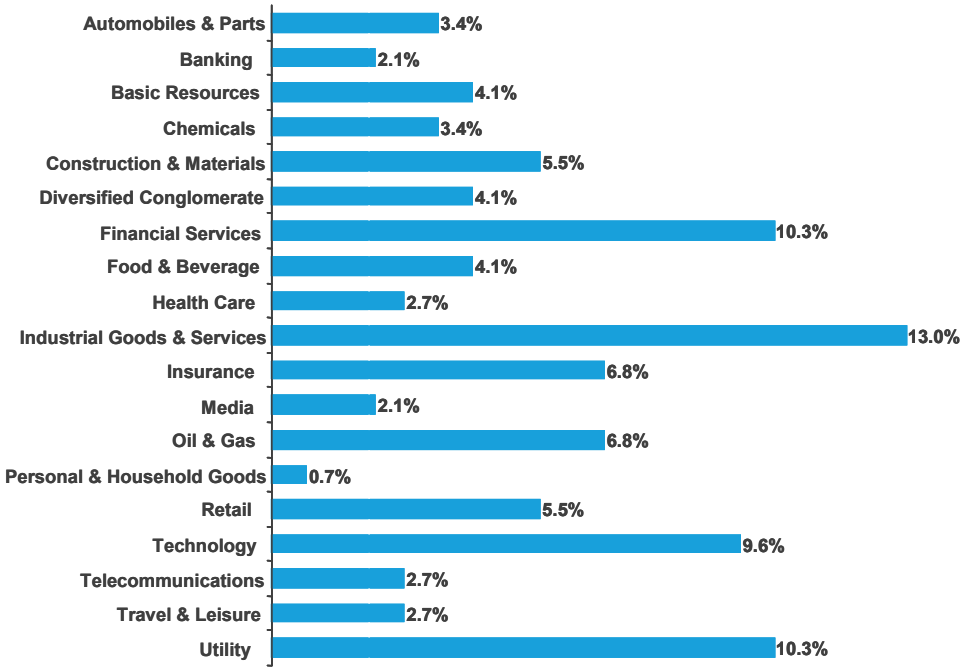
In light of these developments, GovernanceMetrics International (GMI), the corporate governance research and ratings firm, and Marsh, Inc., the world's leading insurance broker and strategic risk advisor, recently conducted a joint survey to assess how public companies worldwide are organizing their approach to identify, prioritize, and manage the various business risks they face. One of the goals of the survey was to help GMI develop a baseline for the addition of ERM metrics into its rating model in 2009.

Survey Results

A total of 149 companies from Australia, Eurozone, Japan, Norway, Singapore, South Africa, Sweden, Switzerland, Taiwan, the United Kingdom, and the United States responded to the survey. Their average revenue was US$4.74 billion in the last fiscal year.

> "The average revenue for companies that responded to the survey was US$4.74 billion in the last fiscal year."

Snapshot of Respondents by Market Sector



The good news is that while companies are in the process of adopting ERM processes and policies at an accelerated rate, governance issues, especially clear disclosure of ERM processes and policies, are still lagging. This could prove challenging for companies in the future as independent analysts (e.g., the credit rating agencies and corporate governance analysts) will consider giving better credit ratings to those companies adopting advanced ERM processes and policies and clearly disclosing them to the market. In today's market environment, such clear disclosure presents an opportunity for companies with advanced ERM processes and transparent company leadership, as they could be expected to be rewarded with lower stock price volatility, lower cost of capital, and higher valuations.[1]

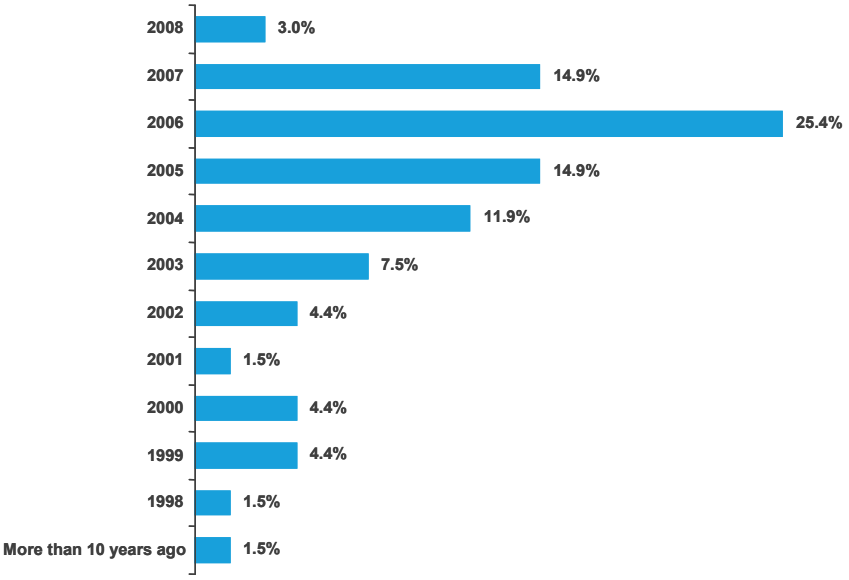
1 See, for example, Derwall, J. and P. Verwijmeren (2006), "Corporate Governance and the Cost of Equity Capital", ECCE Research Note 06- 01, European Centre for Corporate Engagement.

Some key observations are as follows:

Enterprise Risk Management (ERM) has gained wide acceptance as a method for assessing and responding to key exposures. 79% of the respondents indicated their companies employ a formal ERM program. Most of the companies that currently employ an ERM program are either in the infancy of formal development (28%) or mature with opportunities for improvement (48%). Of the companies that currently do not have a formal ERM program, approximately 40% intend to employ a formal ERM program in the next 12 months.

67% of companies that have a formal ERM program in place initiated the process between 2004 and 2007. ERM gained significant traction between 2004 and 2007, perhaps in response to well-publicized corporate failures and the release of the Committee of Sponsoring Organizations of the Treadway Commission's (COSO) ERM Framework, which helped bring attention and standardization to the methodology. 2006 experienced the biggest growth with 25% of companies first employing ERM that year.

Growth in Companies Employing ERM for the First Time by Year



No single ERM standard prevails. Over half (54%) of the respondents indicated their ERM program does not adhere to any particular external standard. For those whose program does follow a standard, 67% said their ERM program adheres to COSO, and 16.2% indicated they have adopted AS/NZS 4360, commonly referred to as "the Australian/New Zealand standard." Both COSO and AS/NZS 4360 attempt to provide a best practice framework for establishing the context, identification, analysis, evaluation, treatment, monitoring, and communication of risk. Neither standard is mandatory.

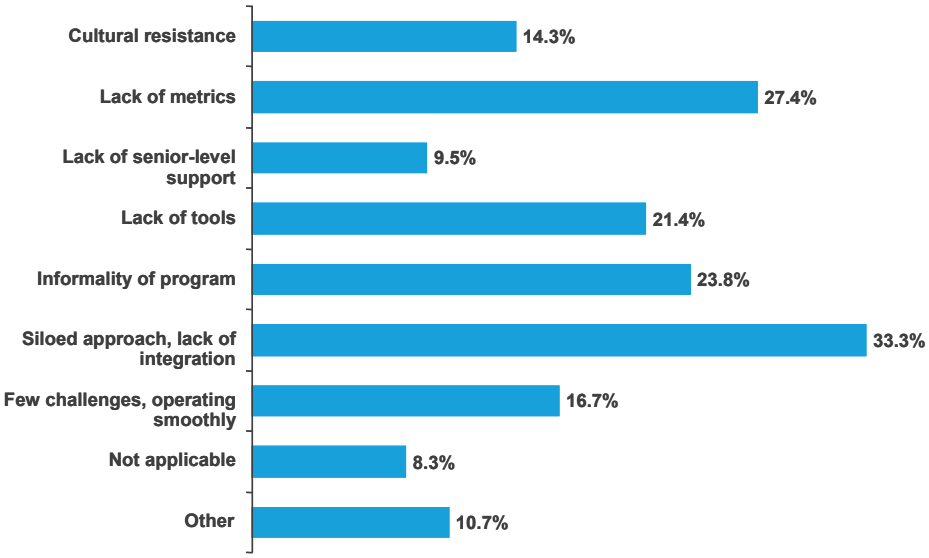
Corporate governance and best practice are two primary drivers in the adoption of ERM. 74% and 64% of companies indicated that corporate governance and best practice are the primary drivers for their organization's ERM program, respectively. Pressure from regulators and rating analysts were also noted, but of lesser importance.

Non-hazard risks receive the most emphasis in companies' ERM programs. The five risk areas receiving the most emphasis in companies' ERM programs are:

- Internal controls/Financial reporting (44%)
- Strategic planning/Competitive risks (43%)
- Legal/Compliance risk (36%)
- Credit/Liquidity risk (30%)
- IT systems/Data security (28%)

Lack of integration and siloed approaches are the biggest challenges confronting 33% of ERM programs. 46% of respondent companies indicated that their ERM program is only partially integrated into the company's routine business processes. This lack of integration is perhaps due to insufficient or ineffective communication between companies' risk function and the rest of the business, a relative lack of influence exerted by the risk function, or a potential lack of risk expertise at the Board level. Some other key challenges are lack of metrics (27%), program informality (23%), and lack of tools (21%).

The Biggest Challenges Facing ERM Programs Today



ERM is typically sponsored by a senior executive. Primary ERM champions are Chief Risk Officers (36%), Chief Financial Officers (23%), and Chief Executive Officers (11%). Further evidencing the importance of the effort, 40% of ERM champions report directly to the Chief Executive Officer.

The Audit Committee of the Board has primary oversight responsibility for ERM in over 50% of companies. The link between ERM and audit is intuitive given the governance nature of the two disciplines. For 65% of respondents, at least one Audit Committee member has a background in risk management. 37% of companies surveyed have their ERM program reviewed by the full Board annually and 32% of them semi-annually. An opportunity exists at 52% of companies to define and obtain board approval of the organization's overall level of risk tolerance.

> "37% of companies surveyed have their ERM program reviewed by the full Board annually and 32% of them semi-annually."

External disclosure is an opportunity for improvement. Although ERM continues to gain momentum in companies across the world, it is not regularly communicated to investors. 75% of companies surveyed said that they currently do not provide information to investors on their approach to ERM, and, of these, 73% have no plans to increase the amount of information they provide within the next 12 months. Companies communicating to their investors on ERM utilize their annual report and investor presentations to provide the information.

Case Study

Tyco International - Enhancing Corporate Governance Through ERM

Tyco International ("Tyco") is a diversified industrial company, with $20 billion in annual revenue and 118,000 employees. The company provides security products and services, fire protection and detection products and services, valves and controls, and electrical and metal products to customers across the globe.

> "Tyco established an Enterprise Risk Assessment program that included visits by the Board to key business sites and dialogue with business management teams to assess risk and mitigation plans."

During the past five years, Tyco has been recognized by its peers for excellence in ethical standards and corporate governance. Tyco currently holds a GMI rating of 9.0, well ahead of the industry average of 6.0[2]. Tyco's Board and CEO are committed to assuring investors and employees that strong ethics, good corporate behavior, and sound risk management practices are top priorities for the company. Responsibility for ERM currently resides with Tyco's Nominating and Governance Committee of the Board.

Several years ago, Jack Krol, former Chairman and CEO of DuPont and Tyco's Lead Director at the time, recognized the need to evaluate the company's global operational risks and identify any risks that required immediate mitigating action. In order to assess the risks, Tyco established an Enterprise Risk Assessment program that included visits by the Board to key business sites and dialogue with business management teams to assess risk and mitigation plans. Tyco continues to conduct a risk assessment at each of its business segments annually.

In January 2008, the Board asked management to better integrate the Enterprise Risk Assessment process with the company's annual strategic and operational planning cycles. Tyco engaged Marsh Risk Consulting to help standardize risk assessment and mitigation practices across the company, measure relative risk across the business and functional areas, provide the Board and business leadership with a portfolio view of inherent risks, and encourage assimilation with strategic and operational planning.

Features of Tyco's current ERM program include:

- On-site board member risk reviews of each major business segment, chaired by Bruce Gordon, Tyco's Lead Director
- Oversight through a newly established ERM Steering Committee with cross-functional representation

2 GMI ratings are scaled 1.0 to 10.0, with 10.0 the highest.

- Use of risk assessment "tools" and scenario models to give the Board and management a number of views on risk
- Bi-annual risk self assessments of each business segment and corporate function
- Provision of a forum to review previously identified risks and measure the success of mitigating actions executed by the business or core function
- Designation of risk owners, responsible for managing each segment/ corporate function's significant exposures
- Utilization of risk reviews in the company's annual strategic planning process

A primary consideration in the design of Tyco's ERM program was the autonomous and decentralized nature of each of its business segments. Given that the businesses are closest to their key risks, they are better positioned than a centralized corporate function to assess and manage them. As a result, the role of Tyco's ERM Steering Committee is to provide oversight, guidance, and tools to each of the designated business risk liaisons. The Committee meets quarterly to discuss emerging risks, review risk management performance, and develop updates for the Board.

When designated Board members conduct the annual risk reviews at each business segment, they focus only on the major issues and key activities to manage them. Furthermore, Tyco's Board now receives one consolidated, holistic risk update, as opposed to numerous separate updates from each of the corporate functions. "The process is far more efficient and frees up time on the Board's calendar to discuss additional priority topics," according to John Jenkins, Tyco's Corporate Secretary.

Tyco's approach aligns ERM with liquidity and performance management, two tenants of Standard and Poor's ERM evaluation criteria when assigning businesses a credit rating. The Board and management recognize that assessing business risk is a "living process" and cannot be completely framed in a static process. A robust ERM process should have a sustained and positive impact on the company.

While GMI does not currently employ ERM metrics in its rating model—as noted, one of the purposes of the joint survey was to help GMI develop a baseline for new ERM metrics—Tyco's efforts already have been rewarded through steadily improving corporate governance ratings. Once GMI introduces new ERM metrics into its model, companies practicing and disclosing best practice in this area may well see an upgrade in their overall governance assessment.

"The Board and management recognize that assessing business risk is a "living process" and cannot be completely framed in a static process."

About the Authors

Christy Kaufman is a Vice President with Marsh Inc.'s Enterprise Risk Management practice. Christy has experience aiding a variety of clients in the identification, analysis, and mitigation of enterprise risks, as well as business continuity planning, crisis response, and risk financing. Before joining Marsh, Christy worked in the risk management consulting practices of both a global accounting firm and another global insurance brokerage firm. Christy has both undergraduate and graduate degrees in Risk Management from the University of Wisconsin and also serves as a part-time instructor for the university. She holds the Chartered Property and Casualty Underwriter designation and is a frequent speaker and author on risk management topics. Please see www.marsh.com for additional information.

Julie Oh is an Assistant Vice President with Marsh Inc.'s Enterprise Risk Management practice. Julie has experience in assisting clients from various industries in their risk identification, assessment and mitigation efforts as well as the development of strategic risk management policies and procedures. Julie has an undergraduate degree in Business Administration from the University of California, Berkeley and is currently pursuing a Master of Business Administration from the University of California, Berkeley. She holds the Associate in Risk Management designation. Please see www.marsh.com for additional information.

Howard Sherman is President and CEO of GovernanceMetrics International (GMI), the corporate governance research and ratings firm. He is the former chief executive of Institutional Shareholder Services (ISS) and Thomson Financial Investor Relations. He is a founding member of the International Corporate Governance Network and the Network for Sustainable Financial Markets and a member of the board of directors of the IRRC Institute for Corporate Responsibility. Howard has worked in the corporate governance field since 1986, when he joined the Investor Responsibility Research Center as senior analyst. He is a frequent speaker before both institutional investor and corporate audiences and the author of numerous articles and op-ed pieces in publications such as the Wall Street Journal, Pensions and Investments, and Directors and Boards. He is the co-author of several major reports on corporate governance, including Structural Imbalances in Japanese Corporate Governance with Bruce Babcock, Conflicts of Interest in the Proxy Voting System with Jamie Heard, and The Market Impact of Corporate Governance Ratings with John Bodt. Please see www.gmiratings.com for additional information.

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Contact: Howard Sherman, GMI
+ 1 212-949-1313 ext. 301

GMI Looks at Corporate Boards and Risk Oversight
Investors Need Greater Transparency

New York, June 29, 2009 - **G**overnance**M**etrics **I**nternational (GMI), the corporate governance research and ratings firm, announced today new findings concerning enterprise risk management and risk oversight at the board level, noting standardized disclosure is lacking at most companies.

GMI's most recent rating release, made available to clients last week, includes a number of new metrics concerning risk oversight. These had been under consideration for a while but were made paramount by ongoing turmoil in the financial and credit markets. The new metrics are now factored into the GMI rating model. Some highlights follow:

Standardized disclosure of company-wide risk management is lacking

- Only 33.1% of the 4,162 companies covered by GMI worldwide provide comprehensive disclosure on their enterprise risk management policies (ERM) in the annual report or other publicly available source
- Only 8.4% disclose they have implemented a nationally or internationally recognized risk management charter or standard such as COSO's Integrated Framework for Enterprise Risk Management

Risk committees of the board are even less common and are sector-specific

- 27.6% of companies covered by GMI disclose having a combined audit and risk committees
- 5.9% of companies covered by GMI disclose a stand-alone board level risk committee or subcommittee
- These were most often found among Banks (35.1%), followed by Life Insurers (21.3%) and Non-life Insurers (17.6%)
- There were no stand-alone board level risk committees or subcommittees in 11 of the 41 sectors covered by GMI

There is a huge disparity between directors with risk management experience and those with general accounting or financial expertise

- Only 1% of the companies covered by GMI globally have at least one non-executive board member who has general expertise in risk management

- By contrast, 77.1% of companies covered by GMI have at least one non-executive member of the board audit committee who has general expertise in accounting or financial management

This pattern is not likely to change any time soon

- Of the 1,659 new board members tracked by GMI so far in 2009, 35% had general accounting or financial expertise, compared to 1.4% with risk management expertise

The Banking sector in particular is racing to raise oversight standards

- Of the 227 new board members tracked by GMI at Banks so far in 2009, 55.5% had general accounting or financial expertise and 3.5% had risk management expertise

The Australia-New Zealand region looks relatively progressive overall

- The Australia - New Zealand region disclosed the widest use of stand-alone board level risk committee or subcommittees (12.1% v. 5.9% worldwide)
- 75.8% of companies in Australia and New Zealand have at least two non-executive directors with substantial industry knowledge, compared to 56.8% worldwide

According to GMI President and CEO Howard Sherman, "Events of the last year have made it clear there is a need for heightened risk oversight at the board level. As companies start to come to grips with the challenge, we thought now would be the right time to start to develop a baseline. Our expectation going forward is that companies seen to be taking serious steps to augment risk oversight, especially in the financial sector, will be rewarded by the market."

GMI's new metrics focus on four areas:

- Company disclosures concerning enterprise risk management (ERM)
- A determination as to whether members of the board involved in risk oversight and / or those serving on the audit committee have relevant industry experience
- The prevalence of risk oversight experience among members of the board
- Qualifications of members of the audit committee of the board

The new ERM metrics were based in part on a survey and paper GMI prepared jointly with the Risk Consulting Practice of Marsh Inc. (*The Importance of ERM during Economic Upheaval*, February 2009). Sherman observed that the disparity between directors with risk management experience and financial or accounting backgrounds was not a surprise given the former has not been a typical career path for board members.

"Ideally, the full board should be involved in risk oversight," said Sherman. "To that end, we expect to see companies employing a variety of approaches. Whatever path they choose to take, there clearly is a need for increased transparency concerning companies' overall approach to risk management. At the end of the day, our job is to help our clients identify companies adopting best practices and those where progress may be lacking."

In keeping with the increasing demands on directors' time, with its latest release GMI also announced it had tightened the standards by which it treats "over-boarded" directors. GMI's new guidance is that the CEO should serve on no more than two public company boards (with the board where he or she serves as CEO counting as one of the two), down from three. For non-executive directors our new guidance is that the upper limit is no more than three public company boards, down from four.

About GMI: GMI ratings, research reports and e-Alerts are used by a wide array of global financial institutions. Depending on the organization, clients use GMI as part of their overall investment research strategy, to support corporate engagement programs and ESG-specific research and investment products, and to help assist with portfolio risk analysis. GMI is often combined with traditional analytical tools such as discounted cash flow or financial ratio analysis to create more robust valuation models. GMI publishes new research reports for all companies covered on a quarterly basis and conducts interim re-ratings when events so warrant. Additional information can be found at www.gmiratings.com.

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