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August 3, 2010

U.S. Securities and Exchange Commission
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Washington, DC 20549

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DODD-FRANK ACT
Title IX Investor Protections
Subtitle E—Accountability and Executive Compensation
SEC. 956. ENHANCED COMPENSATION STRUCTURE REPORTING

Inclusion of a standard measure for corporate culture when determining what behavior encourages inappropriate risks that could lead to material financial loss to covered financial institutions

I am writing on behalf of zEthics, Inc. and the Business Integrity Alliance. The Business Integrity Alliance is one of eleven (11) firms selected to participate in the California Public Employees' Retirement System (CalPERS) Corporate Governance Research Spring-Fed Pool.

The zEthics technology platform provides a structured process for employees to anonymously disclose comprehensive and timely information about the impact on soft controls that are essential to manage the corporate culture. In addition, the zEthics technology platform provides the corporate entity an opportunity to take corrective actions and implement preventative measures to remedy non-conformances with the company's mission, goals, strategies, and objectives.

The Corporate Culture Index is an innovative new tool that measures the integrity of the corporate culture, verifies the tone-at-the-top, and protects shareholders and stakeholders by providing an early warning against corruption, fraud and management misconduct. The Corporate Culture Index provides a quantitative tool to measure the tone of the corporate culture at the Company level, Business Unit level, and Management level.

The zEthics corporate culture surveys and reports provide the organization the knowledge and power to validate and continually improve the integrity of the most important part of the internal control system – the people.

PROPOSED RULE/REGULATION:

The appropriate Federal regulators are requested, by jointly prescribed regulations or guidelines that are intended to prohibit any types of incentive-based payment arrangement, to include a standard measure of an issuer's corporate culture when determining what behavior encourages inappropriate risks that could lead to material financial loss to covered financial institutions.

SUPPORTING ARGUMENT

The financial crisis has demonstrated with certainty that financial institutions with aggressive corporate cultures that discount risk provide executive officers, employees, directors, and principal shareholders of the covered financial institution with excessive compensation, fees, or benefits.

Senior executives often wield risk management to quantitative analysts (mathematicians) whose methods they don't understand – a recipe for disaster and detrimental to the interests of shareholders and for the protection of investors and the public. Baron Rothschild's old dogma "I don't take a risk that I don't understand" has been long forgotten.

Corporate culture is a profound driver of any business. Leadership and corporate culture excellence are essential to company performance and organizational well being. The "tone at the top" shapes corporate culture and pervades a company's internal and external relationships.

All the soft controls in an organization together constitute its corporate culture. The corporate culture will drive the success or failure of financial institutions as the corporate culture is the most powerful control in any organization. It influences every employee's behavior.

Evaluating soft controls — tone at the top, the organization's ethical climate, and management's philosophy and operating style — and reporting weaknesses to those accountable is perhaps the greatest challenge faced by financial institutions.

Including a standard measure of the issuer's corporate culture in proxy solicitation materials makes it possible for shareholders to better understand risks specific to the company and its operations, as evaluating the soft controls makes it possible for representatives from the legal, finance, and investor-relations departments to specifically quantify the various risks affecting their company, their potential impact, and whether that impact warrants disclosure.

Jonathan F. Foster, managing director of Current Capital, explains that while splitting the leadership of a company and its board generally improves governance, the quality of the people is the key factor for success. "The reality is that even the worthiest regulatory fixes and policy enhancements are not nearly as significant as the quality of the people involved."

Monitoring the soft controls is necessary to provide 1) an early warning of problems; 2) extended visibility into the organization to correct problems; and, 3) serve as a check and balance to ensure that the organization is optimized to drive business returns with integrity, transparency, accountability and comprehensive risk oversight.

Shareholders and investors want to know where the high risks are. All stakeholders want assurance that the financial institution will not be the next highly publicized failure. To give them that assurance, the financial institution must identify the potential causes of such failures: weaknesses in the corporate culture.

In a recent study, Sean Griffith and Tom Baker examined how liability insurers transmit and transform the content of corporate and securities law. The findings suggest that what matters in corporate governance are deep governance variables such as culture and character, rather than the formal governance structures that are typically studied.

Adopting a standard measure for corporate culture addresses current shortcomings in the marketplace for stakeholder due diligence, including:

1) Credit rating agencies that evaluate a company's creditworthiness
    a. Ratings have proven to be unreliable
    b. Ratings are impossible to measure
2) Outside auditors who provide independent assurance that the company’s financial condition is portrayed fairly
    a. The audit report — which is the sole communication between auditors and investors on a particular company — explain the auditors' role and their limitations in finding fraud
    b. The disclosure of financial problems tends to come after the fact
    c. Auditors don’t examine every transaction and event, so there is no guarantee that all material misstatements, whether caused by error or fraud, will be detected
3) Securities analysts who assess the company’s business prospects are not independent
    a. Loyal to investment banks that are allowed to trade ahead of the rest of the market
    b. Have proven to be biased and sometimes misleading
4) According to Chairman Mary Schapiro, “Both companies and investors have raised concerns that proxy advisory firms may be subject to undisclosed conflicts of interest, may fail to conduct adequate research or may base recommendations on erroneous or incomplete facts.”

It is apparent to most experts that the internal audit method of managing risk failed on a colossal scale. The rating agencies are amending their processes to ensure that risk management is being practiced enterprise wide, and that boards have a fiduciary responsibility to ensure that the issuer has a risk management identification and mitigation program in place.

The board has a responsibility to serve as “keeper” of the corporate culture — which is increasingly critical as a board duty — and it must ensure the right culture for its management to operate in. A lax culture permits employees to take myriad shortcuts and unacceptable risks. In practically any corporate scandal that allows malfeasance or misguided judgments to happen, the question arises, "Where was the board?"

The most crucial item for boards to keep in mind is to recognize that there are risks outside the processes, procedures and guidelines that are part of an organizations structure, and it is incumbent upon the board to try to identify and manage those risks. The only practical way to accomplish this is to provide the board access to a standard measure for corporate culture through an independent evaluation of the financial institution's soft controls.

The Corporate Library is putting together a report on stock options granted to executives during the market lows in 2008 and early 2009. In some cases, these options have already resulted in hefty paper profits for executives as stocks recovered. According to senior research associate Paul Hodgson, "It's not incentive pay. It's money for nothing."

COST

The cost of acquiring a standard measure of the corporate culture through an independent evaluation of the financial institution's soft controls is not considered burdensome. The cost is estimated to be between $50,000 and $100,000 annually for the majority of financial institutions, with an estimated rate of return between two (2x) to ten (10x) times through improved economic performance.

CONCLUSION

A standard measure for corporate culture is the single most effective performance measure for incentive-based payment arrangements. Independent monitoring of the soft controls makes it possible to readily identify inappropriate risks that can lead to material financial loss to covered financial institutions.

The issuer's boards of directors need to trust but verify what the executive leadership team is doing. Trust is a soft control that constitutes the issuer's corporate culture, along with competence, shared values, leadership, expectations, openness and high ethical standards. The compensation committee and outside compensation consultants must have a clear understanding of the financial institutions' corporate culture in order to establish incentive-based payment arrangements that prevent inappropriate risks that could lead to material financial loss.

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Thank you for considering our comments and your robust, dynamic and transparent approach to regulation. If you would like to discuss any of the following points, please do not hesitate to contact me directly at (602) 358-9586 or Michael Brozzetti at (215)-687-7376.

Yours sincerely,

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Attachments:

A) Dodd Frank Act, Title IX, Subtitle E, Section 956

B) References

ATTACHMENT A
DODD-FRANK ACT

Subtitle E—Accountability and Executive Compensation
SEC. 956. ENHANCED COMPENSATION STRUCTURE REPORTING.
(a) ENHANCED DISCLOSURE AND REPORTING OF COMPENSATION ARRANGEMENTS.—
(1) IN GENERAL.—Not later than 9 months after the date of enactment of this title, the appropriate Federal regulators jointly shall prescribe regulations or guidelines to require each covered financial institution to disclose to the appropriate Federal regulator the structures of all incentive-based compensation arrangements offered by such covered financial institutions sufficient to determine whether the compensation structure—
(A) provides an executive officer, employee, director, or principal shareholder of the covered financial institution with excessive compensation, fees, or benefits; or
(B) could lead to material financial loss to the covered financial institution.
(2) RULES OF CONSTRUCTION.—Nothing in this section shall be construed as requiring the reporting of the actual compensation of particular individuals. Nothing in this section shall be construed to require a covered financial institution that does not have an incentive-based payment arrangement to make the disclosures required under this subsection.
(b) PROHIBITION ON CERTAIN COMPENSATION ARRANGEMENTS.—
Not later than 9 months after the date of enactment of this title, the appropriate Federal regulators shall jointly prescribe regulations or guidelines that prohibit any types of incentive-based payment arrangement, or any feature of any such arrangement, that the regulators determine encourages inappropriate risks by covered financial institutions—
(1) by providing an executive officer, employee, director, or principal shareholder of the covered financial institution with excessive compensation, fees, or benefits; or
(2) that could lead to material financial loss to the covered financial institution.
(c) STANDARDS.—The appropriate Federal regulators shall—
(1) ensure that any standards for compensation established under subsections (a) or (b) are comparable to the standards established under section of the Federal Deposit Insurance Act (12 U.S.C. 2 1831p–1) for insured depository institutions; and
(2) in establishing such standards under such subsections, take into consideration the compensation standards described in section 39(c) of the Federal Deposit Insurance Act (12 U.S.C. 1831p– 9 1(c)).
(d) ENFORCEMENT.—The provisions of this section and the regulations issued under this section shall be enforced under section H. R. 4173—531 505 of the Gramm-Leach-Bliley Act and, for purposes of such section, a violation of this section or such regulations shall be treated as a violation of subtitle A of title V of such Act.
(e) DEFINITIONS.—As used in this section—
(1) the term ''appropriate Federal regulator'' means the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Board of Directors of the Federal Deposit Insurance Corporation, the Director of the Office of Thrift Supervision, the

National Credit Union Administration Board, the Securities and Exchange Commission, the Federal Housing Finance Agency; and
(2) the term ‘‘covered financial institution’’ means—
(A) a depository institution or depository institution holding company, as such terms are defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813);
(B) a broker-dealer registered under section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o);
(C) a credit union, as described in section 19(b)(1)(A)(iv) of the Federal Reserve Act;
(D) an investment advisor, as such term is defined in section 202(a)(11) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(11));
(E) the Federal National Mortgage Association;
(F) the Federal Home Loan Mortgage Corporation; and
(G) any other financial institution that the appropriate Federal regulators, jointly, by rule, determine should be treated as a covered financial institution for purposes of this section.
(f) EXEMPTION FOR CERTAIN FINANCIAL INSTITUTIONS.—The requirements of this section shall not apply to covered financial institutions with assets of less than $1,000,000,000.

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ATTACHMENT B

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