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David E. Gordon
Managing Director

Re: Comments on Section 952 of Subtitle E of Title IX—Accountability and Executive Compensation under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

December 21, 2010

VIA E-MAIL: rule-comments@sec.gov

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

Dear Ms. Murphy:

I am submitting this letter in response to the solicitation by the Securities and Exchange Commission (the "Commission") for preliminary comments on Subtitle E of Title IX-Accountability and Executive Compensation of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act"). These comments are limited to section 952 of the Act, which amends the Securities Exchange Act of 1934 (the "Exchange Act") to add new section 10C(a) ("Independence of Compensation Committees").

I am a Managing Director of Frederic W. Cook & Co., Inc., a national consulting firm that specializes in providing executive compensation advice primarily as consultants to compensation committees of large public companies. In connection with advising clients regarding the implications of the Act, I have consulted with numerous clients on the new rules regarding director independence. In that connection, one client (MGM Resorts International—"MGM") has expressed particular concern regarding the potential application of the director independence rules in situations where a controlling shareholder owns 50% or less of the issuer and directors who represent that shareholder serve on the compensation committee. I am writing this letter to express both the client's views and my views as to how the Act should be applied in this situation.

Specifically, it is important that the Commission's rules under 10C(a) not disable directors that represent large shareholders from serving on the compensation committees of companies that are considered affiliated with the large shareholder. This issue is of direct concern to MGM since two members of its compensation committee are executives of Tracinda Corp., which owned 37% of MGM as of April 1, 2010.

1. Section 10C(a)

This subsection directs the Commission to publish a rule directing the national securities exchanges and national securities associations (the "exchanges") to prohibit the listing of an issuer (subject to certain exceptions) unless the rules of section 10C(a)(2) are met. Section 10C(a)(2) requires that each member of the compensation committee be "independent." Section 10C(a)(3) states that the Commission's rules shall require that the exchanges' rules consider several factors in determining independence. Of significance to this letter is section 10C(a)(3)(B), which states that relevant factors include:

> "whether a member of the board of directors of an issuer is affiliated with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer."

The provision resembles section 10A(m)(3) of the Exchange Act, which provides that each member of the audit committee shall be independent. Section 10A(m)(3)(B) elaborates on the criteria for audit committee independence by providing that a member of an audit committee "may not" be "an affiliated person of the issuer or any subsidiary thereof." Rule 10A-3(e) defines "affiliate" to include both a person controlling the registrant and any executive officer or employee of an affiliate. As a result, employees of controlling shareholders cannot serve on the audit committee of a controlled corporation.

The audit committee independence rules have raised a concern among some that directors that represent controlling shareholders may also be prevented from serving on compensation committees of controlled corporations. For the reasons set forth in the next section, we believe that neither the language of Section 10C(a) nor the policies behind the enactment of the Act should lead to this result.

2. Directors Who Represent Controlling Shareholders Are As Vigilant in Monitoring Executive Compensation as Other Independent Directors, If Not More Vigilant

Based on my experience, which is shared by many, there is no general reason to think that a director representing a large shareholder would act less independently with respect to compensation than other independent compensation committee members. In fact, the tendency is exactly the opposite—a large shareholder is, obviously, more directly harmed or benefited in absolute dollar terms by a registrant's performance than other shareholders.

The obvious purpose of section 10C(a) is to attempt to ensure that compensation committee members do not have relationships with a registrant's management that would compromise their objectivity in deciding the compensation of executive officers. Representing a large shareholder is an obvious positive factor in achieving this objectivity since poor corporate performance financially harms the large shareholder more than anyone else. Many large shareholders are, of course, venture capital and private equity firms. Their own financial success, including the ability to raise capital, hinges on the financial success of their portfolio companies. These types of investors will often have a more demanding pay-for-performance orientation than any other category of investor.

Stock exchange rules reinforce the conclusion that independence is not compromised by representing large shareholders. Section 303A.02 of the NYSE Listed Company Manual contains the independence tests for corporate directors. The commentary to Section 303A.02 contains the NYSE's explanation of why it does not consider share ownership a bar to an independence finding: "However, as the concern is independence from management, the Exchange does not view ownership of even a significant amount of stock, by itself, as a bar to an independence finding."

Finally, it should be noted that a determination that representatives of large shareholders are barred from compensation committee service would lead to an extremely bizarre result since section 10C(g) explicitly provides that all the rules in section 10C do not apply in the case of a "controlled company," which is defined as a company more than 50% owned by one person.[1] Unless section 10C(a)(2) is interpreted in a manner that allows representatives of large shareholders to be considered independent, the following would occur:

- Directors representing significant shareholders could be represented on the compensation committee up until the time that the significant shareholder was considered an affiliate. So, for example, if 20% marked the dividing line in a particular situation, the shareholder could be represented until the ownership interest reached 20%.[2]
- From 20% through 50% the shareholder could not be represented on the compensation committee.
- Above 50%, the shareholder could again be represented on the compensation committee.

We are unable to ascertain any statutory purpose that would be served by this interpretation of section 10C(a).

3. Unlike the Language of Section 10A(m), the Language of Section 10C(a) Does Not Bar Affiliate Shareholders From Being Represented on Compensation Committees

As previously noted, the language of section 10C(a)(3)(B) only requires that the Commission issue rules under 10C(a)(3) that require the exchanges, in determining their definition of the term "independence," to take into consideration various factors, including whether a member of the board is "affiliated with the issuer, a subsidiary of the issuer, or an affiliate of a subsidiary of the issuer." We do not disagree that some of the relationships mentioned in this clause could clearly be relevant to independence—for example, relationships with subsidiaries of the registrant can raise significant independence issues.

Section 10C(a) does not, however, require the Commission to define "independence," but only to issue rules to be used by the exchanges in promulgating their own definitions of "independence." We request that the Commission's rules not limit the freedom of the exchanges

[1] This exception does not exist in section 10A of the Exchange Act, reinforcing the conclusion that different policy concerns exist with respect to audit committees and compensation committees.

[2] Of course, there is no clear dividing line between "affiliate" and "nonaffiliated" status, so an additional problem will be determining when stock ownership has become too high.

to promulgate a definition of "independence" that allows directors of controlling shareholders to be considered "independent." In particular, in light of some of the confusion that has been raised by the statutory language, it would be helpful if the Commission's rules or the accompanying commentary clarify that 10C(a)(3) does not prohibit a finding that directors of controlling shareholders can be considered independent.

We thank the Commission for the opportunity to comment on its rulemaking initiatives. I would be happy to discuss our comments or to answer any questions about them. I can be reached at 310-734-0111.

David E. Gordon
Managing Director
Frederic W. Cook & Co., Inc.