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October 16, 2009

Via e-mail to: **rule-comments@sec.gov**

U.S. Securities and Exchange Commission
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Attn: Elizabeth M. Murphy, Secretary

RE: File No. S7-13-09
Release Nos. 33-9052; 34-60280**;** IC-28817
Proxy Disclosure and Solicitation Enhancements

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Federal Regulation of Securities (the "Committee" or "we") of the Section of Business Law (the "Section") of the American Bar Association (the "ABA") in response to the request by the Securities and Exchange Commission (the "Commission") for comments on its July 10, 2009 proposing release referenced above (the "Proposing Release").

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 Section, nor does it necessarily reflect the views of all members of the Committee.

## I. Overview

We are pleased to have the opportunity to comment on the proposals set forth in the Proposing Release. Although we support the concept of enhanced proxy statement disclosure regarding compensation and corporate governance, we do not support the adoption of certain of the Commission's proposals, and we suggest that the Commission consider revisions to certain other proposals. At the outset, we believe that any rules adopted by the Commission should adhere to three broad themes:

- The rules should encourage clear, concise and meaningful disclosure. Any enhanced disclosure should be required only to the extent such disclosure will materially assist the ability of shareholders to make informed voting decisions relating to the matters to be voted on pursuant to the proxy statement.

- The rules relating to corporate governance and compensation should be neutral, and should not implicitly or otherwise suggest that any one form of governance structure or form or amount of compensation is inherently preferable to any other, or more appropriate in the context of any particular company.

- The rules should require disclosure based on objective disclosure standards, in order to avoid the investor confusion and anomalies that could arise as a result of different companies basing their disclosure on a range of various and perhaps inconsistent subjective criteria.

We are also concerned about "disclosure creep" in proxy statements. In our view, the optimal form of proxy statement is one that presents meaningful information to a company's shareholders in a clear and concise format that encourages shareholders to review and thoughtfully consider the matters on which they will vote at shareholder meetings. By increasing the length and complexity of proxy statements, we are concerned that the Commission may be reducing the likelihood that shareholders will be willing to invest the time and effort necessary to review and consider the information presented, thereby undermining the very purpose of the disclosures. We therefore encourage the Commission to weigh carefully the relative benefits of each of the additional items of disclosure it is proposing and to satisfy itself that the proxy statement disclosures that will result from this rulemaking will, in fact, represent the most clear, concise and meaningful disclosure the Commission believes to be possible.

We have addressed our comments below in the order presented in the discussion of the proposed rules in the Proposing Release.

## II. Enhanced Compensation Disclosure

### A. Compensation Discussion and Analysis Disclosure

The proposed rule amendments would expand the scope of the Compensation Discussion and Analysis ("CD&A") portion of a proxy statement to include a discussion of a company's broader compensation policies and overall actual compensation practices for employees generally, if risks arising from those compensation policies or practices may have a material effect on the company. We suggest, for the reasons set forth below, that the Commission not adopt the rule amendments as proposed. In the event, however, that the Commission believes that disclosures relating to the risk implications of general compensation practices are appropriate corporate disclosures, we recommend that such disclosures be integrated with a company's risk factor disclosure in its Forms 10-K and 10-Q, and not be presented in CD&A, and that the rule more precisely identify the situations that are intended to be addressed.

Because there are no well-defined standards or commonly accepted means by which companies are able to evaluate the relationship between compensation policies and risk, we are concerned that the proposed amendments would be susceptible to widely varying interpretations and could result in disclosures that do not contribute meaningfully to investors' understanding of a company. Unlike assessments of internal control over financial reporting, where

management's evaluation is based on a standardized and identified framework[1], the evaluation of the association between compensation and risk would be, in the absence of such a framework, largely subjective and likely to vary widely from one company to another. Given the absence of a framework for analyzing whether and the extent to which there is a relationship between compensation and business risks, the ambiguities in the nature and scope of risks that are intended to be addressed by the proposed rule amendments and the broad "may have a material effect" standard, companies may be induced to provide generalized "cover the waterfront" disclosures that would provide little meaningful insight to shareholders. In the absence of clearly defined standards by which the relationship between compensation and risk is to be evaluated, we respectfully suggest that the Commission not adopt this disclosure proposal. If the compensation-specific risk disclosure amendments nevertheless are adopted, the Commission should focus those disclosures on specific types of compensation applicable to specific contexts, as discussed below.

**1. Disclosure of compensation-related risk in the CD&A artificially removes the discussion of such risk from a company's other risk disclosures; if such disclosures are to be required, they should be integrated with other such risk disclosures in a company's Form 10-K and 10-Q.**

We believe that the proposed amendment's attempt to address only the compensation-related aspect of risk and to place those disclosures in the CD&A presents such information outside the context of the company's business and other risk management efforts, and thus likely will not provide investors an understanding of a company's overall risk profile. We also believe that the proposed disclosure will not align with many companies' governance and operational structures for addressing risk management. For these and other reasons addressed below, we believe that the Commission should not amend the CD&A requirements as proposed, but instead should address risk disclosures through Form 10-K and Form 10-Q disclosures[2]. We believe that any disclosure of the relationship between general employee compensation policies and business risks should arise in the context of a company's disclosures regarding its business, operations and competitive environment. In this regard, we believe that it would not be helpful to investors, and often will not be practicable, to attempt to isolate compensation as a special aspect of a company's risk profile.

The difficulty in isolating and discussing a relationship between business risks and compensation is reflected in the variety of ways that the proposed amendment's text can be interpreted. When discussing the proposed compensation-specific CD&A risk disclosure rule, the Proposing Release in many instances suggests that compensation practices are a discrete element of a company's risk profile and refers, for example, to compensation practices that

[1] See Item 308(a)(2) of Regulation S-K.

[2] Our references to risk factor disclosure in Form 10-Q refer to the requirement in Item 1A of Form 10-Q that only material changes from the risk factors previously disclosed in the registrant's Form 10-K be disclosed. As discussed elsewhere in this letter, we believe that smaller reporting companies, that are not required to provide risk factor information in Forms 10-K or 10-Q should not be subject to any compensation-based risk factor disclosure.

"create risk," to "risks arising from compensation policies or practices," and to "compensation programs [that] may have the potential to raise material risks to the company." However, there is a public debate as to whether such a causal relationship exists,[3] and no clearly defined standards for companies to apply in assessing whether disclosure would be required. Compensation policies may be designed to align with or otherwise relate to particular business risks, but it is rare for compensation policies in and of themselves to create a business risk.[4] For example, a financial services firm that has determined to expand its lending business with the expectation that it can securitize and thus reduce its exposure to certain loans, as well as a firm that engages in the business of serving as a counterparty in derivative contracts, will both be faced with risks from those businesses, regardless of whether the firm pays employees engaged in those operations fixed salaries or performance-based compensation. Compensation policies at those types of firms may relate to and even exacerbate their business risks, but it would seem inappropriate for the firms to state that their compensation policies, as opposed to a variety of other factors, create the business risk. Thus, we believe that if one is to begin trying to disclose and assess relationships between compensation and business risks, those disclosures need to be placed in the context of disclosures regarding a company's business, operations and competitive environment.

Moreover, because of the systemic and interrelated nature of business risks, risk assessment and oversight matters are typically addressed by management and boards on an integrated, enterprise-wide basis, and not solely with a focus on compensation policies. As noted by the Commission in the proposing release[5], "the persons in management that oversee risk management [may] report directly to the board as a whole, to a committee, such as the audit committee, or to one of the other standing committees of the other standing committees of the board."[6] Thus, assessments of any relationship between general compensation policies and business risks might be addressed by the full board, by an audit committee or by a risk

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[3] Jeffrey Friedman, "Bank Pay and the Financial Crisis: G-20 Accounting Rules, Not Bank Bonuses, Put the System at Risk," *Wall Street Journal* (Sept. 25, 2009); Mark Hulbert, "Did Bankers' Pay Add to This Mess?" *The New York Times* (Sept. 27, 2009); Rene Stulz and Andrea Beltratti, "*Why did some banks perform better during the crisis? A cross-country study of the impact of governance and regulation*," Ohio State University, *Fisher College of Business Working Paper No. 2009-03-012* (finding no evidence that banks with better governance performed better during the recent financial crisis).

[4] One example of a compensation policy that itself may create a long-term business risk is the adoption of a defined benefit pension plan. As companies in the steel and automobile industry have learned, those plans are premised on numerous assumptions regarding matters such as life expectancy and returns on investment. A company's need in future years to fund benefits for employees' past service can jeopardize a company's long-term business prospects if those assumptions are inaccurate or if the company does not continue to grow and maintain its profit margins. However, this type of risk is already extensively disclosed in companies' financial statements and other disclosures, and we would be surprised if this is the type of disclosure the Commission is seeking to address in its proposed rule.

5 Proposing Release, text following footnote 75.

[6] NYSE rules require audit committees to discuss policies with respect to risk assessment and risk management. The commentary to the rules states that the audit committee "is not required to be the sole body responsible for risk assessment and management, but . . . must discuss guidelines and policies to govern the process by which risk assessment and management is undertaken." Further, the commentary acknowledges that "many companies, particularly financial companies, manage and assess their risk through mechanisms other than the audit committee."

management committee. In contrast, we believe that it is rare for a board compensation committee's charter to assign to the compensation committee responsibility for compensation-related aspects of risk management policies, other than in the context of its authority over, and responsibility for, setting executive compensation. The proposed disclosures are therefore not consistent with the manner in which most companies assess and address their risk exposures.

The significance of an appropriate context for the proposed disclosures is reflected in the existing CD&A disclosure requirement. The current CD&A requirement is designed to elicit disclosures about the material elements of a company's compensation policies and to put into perspective the tabular compensation data contained in the tables and otherwise disclosed pursuant to Item 402 of Regulation S-K.[7] The proposed new compensation-specific CD&A risk disclosures, however, would not provide context to any other information in the proxy statement and thus would be isolated from any discussion of the matters to which it relates. Thus, if the proposed amendments are adopted, companies will either struggle to provide meaningful disclosures relating only to general compensation policies or, to place the disclosures in context, may be compelled to significantly expand the length of their proxy statements to provide extensive additional contextual information that is not currently required to be set forth in their proxy statements (but which is addressed in the companies' annual reports on Form 10-K and quarterly reports on Form 10-Q) regarding business lines, scope of operations, strategy, and the competitive environment.

For the foregoing reasons, we do not believe that the Commission should adopt the proposed compensation-specific CD&A risk disclosure rule. We believe instead that the Commission should address risk-related compensation disclosure rules in the context of its evaluation of existing disclosure rules relating to a company's business, operations and competitive environment.[8] We further believe that such disclosures should not appear as part of the proxy statement CD&A but should appear in the Form 10-K and Form 10-Q.[9] This approach to disclosure is further supported by the following two considerations.

First, as reflected in the Proposing Release, information on business risks is primarily relevant to shareholders in their roles as investors. That type of information has historically been set forth in the disclosures set forth in Form 10-K and Form 10-Q, whereas the proxy statement is traditionally the forum for presenting information relevant to shareholders in their role in evaluating the performance of management and directors. Thus, while we believe that the

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[7] See Note 2 to Item 402(b).

[8] The Director of the Division of Corporation Finance stated to the Federal Regulation of Securities Committee at the American Bar Association's Annual Meeting in August 2009 that the Commission is undertaking a comprehensive review of whether the periodic disclosures required in Forms 10-K and 10-Q need to be updated to address more relevant information. We would expect any such review to consider disclosures relating to enterprise risk management.

[9] For example, the Commission could amend its rules requiring a narrative disclosure of a company's business and competitive environment to require that such disclosures include a discussion of any compensation program or arrangement for non-executives that is a material aspect of its business or competitive strategy, or upon which its business is materially dependent.

Commission's proposal to require additional disclosure about the board's role in a company's risk management process is appropriate for proxy and information statements,[10] we believe that disclosures regarding those business risks and elements that affect a company's approach to business risks, including non-executive compensation-related policies, should be set forth in the Form 10-K and Form 10-Q.

Second, it is significant in this regard that the Commission's rules already require the Form 10-K to contain a discussion of the company's business and many other risk-oriented disclosures, including disclosure of risk factors, disclosures regarding market risks and the Management's Discussion and Analysis, which is required to address known trends and uncertainties that are material to the business. To the extent that the purpose of the proposed rule is to encourage disclosure of any relationship between risk-taking activities and general compensation policies or practices that may have a material effect on the company, we believe such disclosures are more appropriately made in conjunction with other disclosures that currently appear in the Form 10-K[11]. In addition, by providing for disclosure in the Form 10-K, the disclosures can be updated each quarter in the Form 10-Q if there is a material change from the previously disclosed information.

Even if the Commission does not concur with our view that, if the proposed disclosures were to be adopted at all, they should appear in companies' Forms 10-K and 10-Q, we urge the Commission to place the proposed disclosures in a separate and new section of the proxy statement and not in the CD&A for the following two reasons.

First, because board compensation committees typically are not charged with oversight responsibilities for companies' general employee compensation-related risk policies (with that function instead being performed by the full board or another board committee as part of the company's general enterprise risk management oversight), the board compensation committee often will not be able to make the disclosures required in the Compensation Committee Report under Item 407(e)(5) of Regulation S-K with respect to general employee compensation-related aspects of a company's risk management practices.

Second, we are also concerned that placing information regarding compensation practices and policies that are not applicable to executive officers in the CD&A will create confusion over the significance and scope of advisory votes on executive compensation. For example, Section 111(e) of the Emergency Economic Stabilization Act of 2008 requires that companies that have accepted certain federal assistance provide an advisory vote on "the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Commission (which disclosure shall include the <u>compensation</u> <u>discussion</u> <u>and</u> <u>analysis</u>, the compensation tables, and any related material)." (emphasis added). Including discussions in the CD&A of compensation matters not

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10 See our comments on this proposal at part IV of this letter.

[11] The relocation of the proposed disclosure is even more important when the interests of security holders who may not receive proxy statements, such as holders of nonvoting debt, are considered. Although such holders would, of course, be able to access a company's proxy statement on EDGAR, they (as well as all other holders of a company's securities) would be deprived of the ability to view the disclosure on one unified format.

involving executive officers may create uncertainty over which information in the CD&A shareholders are voting on, thus interfering with the objective of advisory votes on executive compensation.

**2. Because there are no well defined standards to evaluate relationships between compensation policies and risk, companies may be forced to speculate as to these links, undermining disclosure consistency between companies and leading to investor confusion.**

The Commission recognizes in the Proposing Release that in light of the complexity of the issue and compensation programs generally, it may be difficult to identify and describe which compensation structures may expose a company to material risks. In our view, if the Commission were to adopt a general compensation-specific risk disclosure requirement, then in light of the number and variety of risks faced by companies and the complexity of compensation programs generally, the Commission should revise the language of proposed Item 402(b)(2) to address more specifically the situations in which disclosure is to be required. We believe that a number of aspects of the proposed language may not be as clearly stated as possible, and therefore we recommend specific language changes in the paragraphs that follow.

There are a wide variety of material short and long-term strategic and operational issues and decisions that businesses face on an on-going basis, and thus a wide variety of risks that each company encounters, many of which are inherent in and integrally related to a company's business. Risks to which a company is or may be subject include risks relating to competitive factors, legal and policy compliance risks, changes of demand for products or services, availability of raw materials or suppliers of specified services, market acceptance of new goods and services, customer preferences and changes to the customer base, availability of financing, customer credit risks, protection of patent or other intellectual property rights, domestic and worldwide market conditions and a host of other considerations. We believe that requiring companies to assess and disclose relationships between these types of risks and company compensation programs will not significantly enhance investors' understanding of a company. For example, we believe that little will be achieved if any new rule calls for disclosures that read, "Our base salaries and overall compensation levels may not be sufficient to attract or retain a sufficient number of employees with appropriate skills in order to enable us to maintain or expand our operations, which may cause us not to succeed."

It also frequently will be difficult for companies to assess, other than on an after-the-fact basis, whether a particular compensation policy exacerbates a risk. For example, if a company's business prospects are dependent on it developing, testing and bringing to market a specific product before its competitors do, it is not clear whether it is riskier for that company to pay its product development team bonuses for achieving certain milestones on or before certain target dates, or whether it is riskier to pay them only a fixed salary regardless of whether the product development occurs on schedule. Even a compensation program composed of both base and incentive compensation may not adequately incentivize the product development team to timely and successfully develop the specific produce and may not be sufficient to prevent other companies from recruiting and hiring key personnel away from the company, thereby materially

undermining its future prospects. Likewise, if such a company awards a significant bonus for the product development team upon its achieving a particular product development milestone, but only pays that bonus after the product is introduced and achieves a specified sales goal (or subjects the bonus to a recoupment feature if a sales milestone is not achieved), the company may risk losing its product development talent to a competitor for not properly incentivizing that talent by making those employees' bonus contingent upon the success of a different team of employees. Even if a compensation program is designed to motivate and incentivize the product development team, it may be difficult to determine whether the compensation program was in fact the reason why the team successfully and timely developed the specific product. There may be motivational factors, such as desire of team members for esteem within the organization; structural factors, such as the assignment of appropriate personnel who work well together under a competent leadership structure with appropriate funding support; and other factors, such as sheer luck, which have as much, if not significantly more, relationship to the successful result.

Assessing a relationship between compensation and risk is even more problematic when dealing with matters whose success may be determined only on a long-term basis. The further removed a particular effort is from the ability to assess its success or failure, the more likely it is that other factors will also affect that assessment. For example, if a product development team creates a product within its allotted time and cost parameters, but the product turns out to be unsuccessful and the entire effort is viewed as having been a failure, the fault would lie not necessarily with the product development team, but could also have resulted from poor performance by the manufacturing team, the marketing department and sales team, by a poor management business plan, or by reason of external factors that arose from the passage of time, such as regulatory changes, changes to consumer preferences or the introduction of competing products. It may therefore be exceedingly difficult to determine the effect compensation policies had on the risk-taking aspects of the venture, or on the overall result.

In attempting to set forth rules on when disclosure is required in this context, we do not view it as helpful or appropriate for the regulatory text or explanations of it to refer to "excessive" or "inappropriate" risks. Although those terms may apply in the context of entities that are subject to substantive regulation designed to protect the nation's economic system (such as those administered by federal banking agencies and the Commission's regulation of certain financial services firms), the difficulty of objectively determining whether a risk is appropriate or excessive suggests to us that the Commission refrain from referring to these terms in its rules. For example, if a number of companies in the same industry are engaging in the same risk-related activity, it may be difficult to conclude that a risk is excessive. Moreover, if risk is evaluated based upon the perceived likelihood of an event occurring, the absence of prior occurrences may give rise to a view that a risk is not excessive. Moreover, a company's business may be highly risky, without being considered excessively risky, provided that investors are aware of those risks. Investors may view highly risky enterprises to be entirely appropriate investments as long as the investor has received adequate disclosure that allows the investor to assess the entity's risks. Thus, for example, it may be highly risky to invest in the common stock of either a single-branch savings and loan holding company that primarily extends mortgage loans for vacation properties in a single region of the country or a biotech company that is in the

research and development stage of developing only a single drug designed to combat a particular illness. But if an investor is informed of and fully assesses those risks and determines to make the investments, then that investor must have concluded that the risks were not excessive or inappropriate.

With the foregoing in mind, were the Commission to adopt a general compensation-specific risk disclosure requirement, we believe that revisions to and/or greater clarity relating to each of the following four aspects of the disclosure standard will help lead to more responsive disclosures that are informative to investors:

*The types of risks to be addressed*. The rules should specify the types of business risks that are to be assessed. The more numerous and generalized the types of risks that are to be assessed, the more likely that a company will be inclined to provide generalized, boilerplate disclosure, which would not add to investors' understanding of a company's risks beyond those already addressed in a company's risk factor disclosures in its Forms 10-K and 10-Q. We therefore suggest that any compensation-specific risk disclosure standard should be focused on material short-term financial risks that materially imperil a company's financial viability.

*The types of compensation to be addressed*. There are risks that any compensation programs may not achieve their desired objectives and may not be sufficient (or may be richer than necessary) to attract or retain employees. We believe the principal thrust of any compensation-specific risk disclosure rules should be limited to contingent performance-based or incentive-based compensation arrangements that are specifically tied to achieving one or a few specific goals.

*The relationship between the compensation arrangement and the risk*. As noted above, a standard that requires disclosure of compensation arrangements that create risks (that is, give rise to the existence of a risk that would not otherwise exist) will result in a significantly different scope of disclosures than a standard that requires disclosure of compensation policies that encourage employees to take material risks. In addition, any compensation arrangement that is tied to achieving a certain objective may have the unintended effect of motivating employees to obtain the objective by illegal or fraudulent conduct. Because this risk is inherent in any such compensation program, and more importantly because companies typically have other, non-compensation related, controls in place to guard against such conduct, we do not believe that it will meaningfully add to investors' understanding of a business to require disclosure of this type of potential consequence from a performance-based compensation arrangement. Finally, because there are so many factors that affect long-term risks, we believe that it is not practical for companies to isolate particular compensation programs as potentially impacting long-term risks. We believe instead that the rule should be focused on compensation practices that reward or encourage employees to take actions that produce or contribute to material short-term financial risks.

*The materiality standard*. The rule should apply a traditional materiality standard for when disclosure is required and should expressly take into account other factors that are designed to mitigate or control risks. Disclosure of any possible implication from a compensation

arrangement that "may" have a material effect, without regard to controls and other steps taken to mitigate the possibility or likelihood of that effect, will impose a burdensome responsibility on companies to speculate and describe all sorts of unlikely scenarios and will diminish the utility of disclosures to investors. In addition, the rule should confirm that the presence of controls and other policies that mitigate the effects of a particular compensation arrangement on risk-taking activities can and should be taken into account in determining whether disclosure of the compensation policy is required and that no disclosure is required if mitigating factors (whether implemented through other compensation structures or through other procedures) reduce risk to an immaterial level.

With respect to the specific regulatory text proposed, we have the following comments:

The first sentence of proposed text of Item 402(b)(2) states that the disclosure is required "to the extent that risks arising from the registrant's compensation policies and <u>overall</u> <u>actual</u> <u>compensation</u> <u>practices</u> for employees <u>generally</u>" may have a material adverse effect on a company (emphasis added). However, the examples provided for when disclosure may be required suggest that the Commission may be seeking disclosure in situations that do not involve "overall actual compensation practices for employees generally." If the Commission intends to require disclosure with respect to specific compensation practices that are not broadly applicable to employees generally at a company, the language quoted in the preceding sentence should be revised or deleted.

The first sentence of the proposed text also states that the disclosure should address compensation policies "as they relate to risk management practices and/or risk-taking incentives." This and other references to risk management practices could be read to mean that companies are required to discuss compensation policies that help to mitigate risk, while other language in the proposed rule and the Proposing Release indicates that the disclosure is designed to provide investors information on how compensation practices may create or magnify risk. As such, the proposed rule could require extensive discussions of a wide variety of compensation arrangements at companies, involving both those that may enhance or promote risk-taking and those that help to mitigate risk-taking incentives. While companies may wish to address how they manage or mitigate compensation practices that otherwise may create or promote risk-taking, we believe that compensation practices that mitigate risks should not of themselves trigger disclosure under the proposed rule.

Taking into account the foregoing points, the first sentence of the proposed text could be revised to read, "A registrant shall discuss any compensation arrangement or program maintained by the registrant providing for compensation that is contingent or otherwise based on achievement of a specified task or goal that promotes taking covered risks in order to achieve the task or goal that are material to the registrant or that contributes significantly to material covered risks faced by the registrant," with "covered risks" being defined as material short-term financial risks.

With respect to the listed examples of situations that may require disclosure under proposed Item 402(b)(2), we believe that the list of situations where compensation policies may

induce risk-taking behavior can and should be appropriately narrowed in order to avoid imposing costs on companies by requiring extensive analyses of situations or compensation arrangements that are less likely to materially impact a company's risk profile. Accordingly, the Commission should adopt an exclusive list of situations requiring disclosure that is limited to (i) compensation policies at business units of a company that carry a significant portion of the registrant's material risk profile, and (ii) compensation policies applicable to groups of employees where at least a majority of the employee compensation is tied to achievement of only one or a few goals. Absent these situations, the other examples listed in the proposed rule do not indicate a significant likelihood that compensation policies will induce unacceptable risk-taking behavior. For example, situations where bonuses are awarded upon accomplishment of a task, while the income and risk to the company from the task extend over a significantly longer period of time, tend to indicate that there are many other factors and individuals affecting the return realized by the company from the effort (such as successfully manufacturing, pricing and marketing a product once it has been developed) and not that the compensation policy or achievement of the task itself created risks to the company.

Proposed Instruction 1 to Item 402(b) seems appropriate only with respect to Item 402(b)(1), as proposed to be renumbered, and therefore should be moved to appear as Instruction 3 to that item. This is because the first sentence of the instruction states that the focus of CD&A should be the principles underlying and analysis of compensation policies and decisions, whereas proposed Item 402(b)(2) appears to be focused on disclosure of the existence of particular compensation policies. The second sentence of the instruction refers to "the more detailed information set forth in the tables and narrative disclosures that follow," but as noted above Item 402(b)(2) does not relate to information otherwise set forth in the disclosures called for under Item 402 or that otherwise appears in a proxy statement.

**3. Responses to Certain of the Commission's Inquiries**

**(a) Would expanding the scope of the CD&A to require disclosure concerning a company's overall compensation program as it relates to risk management and or risk-taking incentives provide meaningful disclosures to investors?**

We believe the CD&A should be limited to its current scope, subject to the comments set forth in this letter. We are concerned that expansion of the scope of CD&A to refer to a company's overall compensation program would not be relevant to an investor's voting decision at the shareholder meeting to which the proxy statement relates. We also believe that, in the absence of generally accepted criteria for evaluating the relationship of compensation to risk taking, generalized statements by different companies may be based on different standards, and therefore be inconsistent.

**(b) Should the scope of the amendments be limited in application to specific groups of employees, such as executive officers, or to companies of a particular size, like large accelerated filers, or**

**to particular industries like financial services, including companies that have segments in such industries?**

We note and concur with the Commission's statement in the Proposing Release that, to the extent risk considerations are a material aspect of a company's compensation policies or decisions for named executive officers ("NEOs"), a company is required to discuss such matters as part of its CD&A under the current rules.[12] Thus, while it is possible that some executive officers who are not NEOs participate in relevant compensation arrangements that are not already required to be discussed in the CD&A, we believe that such situations are the exception, and thus that additional rulemaking is not necessary to elicit disclosure of elements of executive officer compensation that relate to material risks.

Were the Commission to adopt a general employee compensation-specific risk disclosure requirement, we believe that the scope of any such requirement should be more focused than the proposed disclosure. There are a wide variety of material short- and long-term strategic and operational issues and decisions that businesses face on an on-going basis, and thus a wide variety of risks that companies encounter. In many cases, these risks will be inherent in and integrally related to the business. For example, a company that competes for contracts may not win a bid; and a technology company may not efficiently, timely or successfully develop technology that is embraced by the marketplace. We do not believe that investors' understanding of these types of risks typically will be enhanced by disclosures of the compensation structures applicable to non-executive employees. Instead, as reflected in the situations cited in the Proposing Release, the recent economic tumult has highlighted the possibility that significant financial risks undertaken by a company may undermine the long-term growth and success of a company. Thus, we believe that any compensation-specific risk disclosure rule adopted by the Commission should address disclosure of compensation policies that encourage activities that contribute to the taking of material short-term financial risks. We expect that these types of risks may arise at companies with large financial services or trading operations, and thus that limiting the rules' applicability to financial services firms and firms that have material segments in that industry may be appropriate.

**(c) Is the cost of tracking and disclosing the nature of the risk different at different types of companies or company segments and if so, should that be reflected in our rules?**

The factor that will most significantly affect the cost of complying with any new general compensation-specific risk disclosure requirements will be the scope of any such rule. As noted above, companies in their ordinary business operations are subject to a wide variety of risks. In our view, and in the absence of any established standards to gauge the relationship of compensation to risk-taking, the costs and burdens of the proposed disclosure requirement of creating and then implementing such a system would not be justified unless the scope of the disclosure requirement are focused on a specific set of financial risks, as discussed above, and

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[12] Proposing Release at note 31.

unless the Commission raises the materiality standard applied for determining when disclosure is appropriate.

Companies typically utilize a wide variety of compensation arrangements. Even smaller companies that are engaged in a single business line may have many different categories of employees, each of whom may be covered by a variety of compensation arrangements covering basic compensation, one or more bonus arrangements, and various incentive plans, each with its own minimum conditions, performance target criteria, vesting, and contractual or discretionary elements, and payable in cash, equity or some combination. These arrangements may be changed with some frequency (including changes in design and changes in relative weighting compared to an employee's overall compensation package) as companies adapt compensation programs to different economic and competitive environments and constantly changing business objectives. It may not be clear to companies how any particular element of the compensatory system, let alone all of the elements combined, relate to risk-taking behavior. If companies must review, assess and potentially discuss each of these situations in connection with risk elements that may have a material effect on the company, even if those risk elements are aligned with the long-term operational and competitive risks that the company faces in the ordinary course of its business, then the burden of the new disclosure rules would be great.

The cost of assessing and disclosing arrangements will particularly be magnified if the Commission adopts disclosure standards with the low materiality threshold that the Commission has proposed. A disclosure standard based on a criterion that the matter disclosed "may" have a material effect on a company is well below the standard applied currently for disclosure of known trends and uncertainties in Management's Discussion and Analysis and appears to be below even the standard applied for risk factor disclosure.[13] With little or no probability standard for assessing when disclosure would be appropriate, companies would be required to speculate as to the linkage between compensation and risk and, having engaged in that first speculation, to speculate further as to whether any one of a potentially wide range of conceivable circumstances "may" materially affect the company. The resulting disclosures, which could resemble (but be more extensive than) risk factor statements, would be so broad and encompass so many conceivable scenarios that any benefit investors might glean from such disclosures would be far outweighed by the costs to companies of monitoring, assessing and preparing such disclosures. However, should the Commission determine to require this disclosure, to avoid overly generalized disclosures and unnecessary costs of compliance, the Commission should apply a traditional materiality standard and only require disclosure based on known risks that are "reasonably likely" to have a material effect on the company.

[13] Item 1A of Form 10-K refers to Item 503(c) of Regulation S-K, which provides for disclosure of significant factors that make [a company] speculative or risky. The disclosure does not appear to require a company to speculate as to factors that "might" present risks, but instead appears to require disclosure of known risks.

**(d) Should other elements of compensation that may encourage excessive risk taking be highlighted in the CD&A?**

For the reasons discussed above, the Commission should focus any compensation-oriented risk disclosure requirements on contingent performance-based or incentive-based compensation arrangements that are specifically tied to achieving one or a few specific goals.

**(e) We have included a list of examples of the types of issues that would be appropriate for a company to discuss and analyze. Is that list appropriate?**

As discussed above, we agree that a company may wish to discuss risk management techniques in order to place into appropriate context any discussion of compensation arrangements that promote risk-taking or contribute to material risks faced by the company, such as those included in the list of issues that may be appropriate to discuss and analyze. However, we also believe that controls (including controls not tied to compensation structures, such as quality review committees and audit procedures) or mitigating compensation arrangements (such as claw backs, holding periods and deferral arrangements) should be taken into account in determining whether an arrangement is material enough to warrant any disclosure under the proposed rule, and that this should be expressly stated in the rule.

**(f) Rather than treat the list as examples, should we require discussion of each item?**

We do not believe that prescriptive, item-by-item disclosures are appropriate in light of the wide variety of business risks faced by companies, and the wide range of compensation programs adopted by companies. We agree that any disclosure requirement should be principles-based and thus allow companies to address only those issues that they have identified as being material in their specific circumstances.

**(g) Are there other disclosure requirements that would provide more meaningful information about the effect of the registrant's compensation policies on its risk profile or risk management?**

We believe that compensation-related risk disclosures would be better addressed in Forms 10-K and 10-Q, in the context of discussions regarding a company's business lines, scope of operations, strategy and competitive environment.

**(h) Are there certain risks that are more clearly aligned with compensation practices the disclosure of which would be important to investors?**

We believe that the disclosures should be limited to practices that relate to material short-term financial risks that may be faced by a company and not the general business and

competitive risks that companies face, which are much more appropriately addressed in the "Risk Factors" Item in Forms 10-K and 10-Q.

**(i) If a company determines that disclosure under the proposed amendments is not required, should we require the company to affirmatively state in its CD&A that it has determined that the risks arising from its broader compensation policies are not reasonably expected to have a material effect on the company?**

The Commission's disclosure rules, including other rules specifically addressed to risk disclosures, have not traditionally required companies to address affirmatively matters that the company has determined are not applicable to it, and we do not believe that this context calls for any different treatment.

**(j) Should smaller reporting companies, who are currently not required to provide CD&A disclosure, be required to provide disclosure about their overall compensation policies as they relate to risk management?**

Smaller reporting companies are not currently required to provide an annual CD&A in their proxy statements or risk factor disclosure in their periodic reports. We do not believe it would be appropriate to subject smaller reporting companies to any compensation-specific risk disclosure requirement adopted by the Commission.

**B. Revisions to Summary Compensation Table**

We support the Commission's decision to revise the reporting of equity awards in the Summary Compensation Table ("SCT") and the Director Compensation Table ("DCT"). Experiences over the past three fiscal years with the existing rules have demonstrated that the rules' reliance on FAS 123R as the basis for determining the presentation of equity compensation information is inconsistent with the way that equity awards are viewed by board compensation committees and by investors, resulting in companies and investors largely ignoring the values reported in the SCT and DCT and instead presenting alternative calculations. We believe that reporting grant date fair value of equity awards in the SCT and DCT, rather than reporting the financial statement recognition amount for all awards outstanding during the year, more accurately presents the compensation committee's recent actions and intentions and facilitates a company's ability to provide a CD&A that clearly and concisely explains and analyzes material compensation policies and decisions that are relevant for the most recent fiscal year.

We believe, however, that the Commission's proposed standard for reporting equity awards that are subject to performance conditions (referred to under the rules as equity incentive plan awards) would continue to fail to reflect the way that compensation committees and investors view such awards. This is because FAS 123R does not take into account the effect of performance-contingent conditions when determining the grant date fair value of an award, instead treating performance conditions as affecting whether and when the grant date fair value is

actually expensed.[14] In contrast, in our experience compensation committees almost universally take performance-contingent vesting conditions into account when granting such arrangements. In order to provide more meaningful information in the SCT and DCT, therefore, performance-contingent equity awards should be reported based on their grant date fair value taking into account the grant date assessment of the probable number of options or shares that will vest (typically, the target value).[15] Phrased more technically, the value reported in the SCT and DCT should take into account both the measurement and recognition criteria of FAS 123R other than with respect to purely time-based vesting. If performance-contingent equity awards are reported in the SCT and DCT at full grant-date fair value, as is proposed, thereby effectively ignoring the impact of performance conditions on the value of awards, we believe that companies and investors will continue to disregard the values reported for equity awards in the SCT and DCT and instead continue to present alternative summary compensation tables that present equity award values based on more realistic assumptions. In addition, by valuing performance-contingent equity awards at their maximum, instead of expected, fair value, the Commission's proposed rule could discourage companies and executives from embracing performance-contingent equity awards, since they would be viewed as artificially inflating compensation amounts.[16]

The Commission asks whether the proposed SCT reporting of equity awards is a better approach for providing investors clear, meaningful, and comparable executive compensation disclosure consistent with the objectives of providing concise analysis in the CD&A and a clear understanding of total compensation for the year. We view the proposed SCT reporting as a better approach for providing investors clear, meaningful, and comparable executive compensation disclosure and believe that it will allow companies to more clearly analyze and explain their equity compensation programs in the CD&A. Experience over the past three years has shown that the current rules do not reflect the manner in which executive compensation decisions are made, create investor confusion and can distort the total compensation numbers and the determination of NEOs. This has particularly been the case with respect to performance-contingent equity awards, which as a result of the current rules' reliance on financial statement reporting standards, has resulted in negative amounts being reported, and we believe that the proposed rules would continue to distort the presentation of performance-contingent equity awards. We believe instead that the grant date value reported for such awards should take into account the expected (i.e., probable) extent of vesting of such awards, and not report the maximum potential fair value of such awards. We do not believe that this modification will result in abuse, as companies are required under accounting rules to assess the probable extent of

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[14] "In determining the amount recognized, FAS 123R requires a company to estimate at the grant date the number of awards that ultimately will be earned." Executive Compensation Disclosure, Exchange Act Release No. 34-55009, at part II.A, p. 13 (December 22, 2006).

[15] If the Commission determines that it disclosure of the maximum potential fair value of equity incentive awards also would be useful to investors, the Commission could provide for that amount to be reported in the Grants of Plans-Based Awards Table.

[16] Ironically, the Commission's proposal also could have the effect of increasing executive compensation levels, as the overstated values for performance-based equity awards might be taken into account in compensation surveys that are used for benchmarking purposes.

vesting in order to be able to account for performance-contingent equity awards in the period in which they are granted. Because the Grants of Plan-Based Awards Table ("GPBAT") shows the target and maximum size of equity incentive awards and because, as discussed in response to Comment 3 below, we endorse the GPBAT continuing to report grant date fair values on a grant-by-grant basis, investors will be able to easily determine the maximum grant date fair value of multiple equity incentive plan awards from the information provided in that table. However, if the Commission determines that it is also helpful to require disclosure of the maximum potential fair value of equity incentive awards granted in a year, the Commission could provide for that amount to be reported in the GPBAT or in a footnote to that table.

1. **The proposal contemplates that the Summary Compensation Table would report the aggregate grant date fair value of stock awards and option awards granted <u>during</u> the relevant fiscal year, just as the Grants of Plan-Based Awards Table reports each grant of an award made to a named executive officer in the last completed fiscal year. Should the Summary Compensation Table instead report the aggregate grant date fair value of equity awards granted for services in the relevant fiscal year, even if the awards were granted <u>after</u> fiscal year end? Explain why or why not. For example, could such an approach be applied in a manner inconsistent with the purposes of our compensation disclosure rules, for example by distorting the determination of named executive officers? If we change our approach with respect to the Summary Compensation Table, should the Grants of Plan-Based Awards Table be amended correspondingly to conform to the scope of awards reported in that table?**

While many compensation committees evaluate and grant equity awards as a component of compensation for the year in which the awards are granted, some companies grant such awards in advance of the fiscal year for which they are awarded, while others grant them after the fiscal year for which they are awarded. Although compelling arguments can be made for reporting awards based only on the year of grant, allowing equity awards to be reported for the year with respect to which they are awarded may allow companies to more effectively present compensation arrangements in the manner in which they are viewed by compensation committees and thereby promote more effective explanations in CD&As.[17] We note that this approach appears to be consistent with equity award reporting that will result from the Commission's proposed amendment to Instruction 2 to the salary and bonus columns of the SCT. While we do not believe that companies would seek to manipulate or abuse reporting on this basis, to enhance the presentation of equity awards the Commission could require the GPBAT to report any equity award that is included in the SCT as well as any other equity award made during the fiscal year, with footnote explanations describing the year for which such awards are reported in the SCT.

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[17] The Commission's rules could state that equity awards are to be reported in the year in which they are granted, unless the registrant's CD&A addresses such compensation arrangements as being an element of compensation for the preceding or following year, in which case they may be reported in such fiscal year.

**2. If the Summary Compensation Table is amended as proposed, should the Grants of Plan-Based Awards Table disclosure of the full grant date fair value of each individual award be retained, rather than rescinded as proposed? Should the Grants of Plan-Based Awards Table continue to disclose the incremental fair value with respect to individual awards that were repriced or otherwise materially modified during the last completed fiscal year? If so, why? If disclosure of grant date fair value of individual awards is retained, should it also be made applicable to smaller reporting companies?**

Because the SCT would report an aggregate value for all awards granted during (or for) the fiscal year, grant-by-grant reporting of grant date fair values in the GPBAT would continue to provide helpful information, and thus should be retained, both for new grants and for repriced awards.[18] If the Commission adopts our recommendation to report performance-contingent equity awards based upon their expected grant date fair value in the SCT, the Commission could specify that full (maximum) grant date fair value be reported in the GPBAT.

If the Commission retains grant-by-grant fair value reporting in the GPBAT, then the footnote requiring disclosure of the assumptions used in determining grant date fair value should be tied to the GPBAT disclosures, and not to the SCT disclosures. In other words, proposed Instruction 1 to Item 402(c)(2)(v) and (vi) should instead be adopted as an instruction to Item 402(d). We note that this instruction states that assumptions shall be disclosed by reference to a discussion in the registrant's financial statements. However, because many companies prefer to state the assumptions in the GPBAT footnote itself, the Commission should explicitly accommodate this practice by revising the text of the Instruction to state that the assumptions shall be either set forth in a footnote to the table or disclosed by reference to a discussion of those assumptions in the registrant's financial statements. Existing disclosure rules do not require smaller reporting companies to provide a GPBAT. We believe that this continues to be appropriate and would not suggest adding a requirement that smaller reporting companies provide grant date fair values for each equity award granted during the year.

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[18] Thus, current Instruction 7 to 402(d) should be retained.

**3. As described above, one reason for adopting the financial statement recognition model was the potential for distortion in identifying named executive officers when a single large grant, to be earned by services to be performed over multiple years, affects the list of named executive officers in the Summary Compensation Table, even though the executive earns a consistent level of compensation over the award's term. Are multi-year grants a common practice, so that they would introduce significant year-to-year variability in the list of named executive officers if the proposed amendments are adopted relative to the variability under the current rules? If so, how should our rules address this variability?**

While the proposed amendments create the potential for distortion in identifying named executive officers from large grants that are made in a single year but intended to represent compensation for multiple years, the current reporting regime creates a similar issue when, for example, compensation expense is recognized in a single year for retirement eligible executives. As discussed above, the current reporting regime also presents other distortions, such as a potential for negative numbers to appear in the SCT. Moreover, the proposed amendments, unlike the current reporting regime, will more closely reflect the compensation committee's recent compensation decisions and will more closely align with how investors view equity awards. Thus, we believe that the proposals present a better reporting regime than the existing rules. Companies that utilize multi-year grants will be able to provide appropriate explanatory disclosure in the CD&A and the narrative disclosure following the SCT and, if they determine that it is appropriate, can voluntarily include additional executives in the SCT even if a multi-year award to another executive prevents the additional executives from being among the three next most highly compensated executives for a particular year.

**4. Under the proposal, all stock and option awards would be reported in the Summary Compensation Table at full grant date fair value, including awards with performance conditions. Would the proposal discourage companies from tying stock awards to performance conditions, since the full grant date fair value would be reported without regard to the likelihood of achieving the performance objective? If the proposal is adopted, is any disclosure other than that already currently required (e.g., in the Compensation Discussion and Analysis, the Grants of Plan-Based Awards Table, and the Outstanding Equity Awards at Fiscal Year-End Table) needed to clarify that the amount of compensation ultimately realized under a performance-based equity award may be different?**

Yes, we believe that the proposed reporting standard for equity awards that are subject to performance conditions presents another situation, similar to that which exists under the existing rules, where accounting conventions would result in a presentation that differs significantly from the way that performance-contingent equity awards are viewed by compensation committees and

investors. Because the full grant date fair value calculation determined under FAS 123R ignores the effect of performance conditions on the likelihood that an award will be earned, it overstates the expected value of performance-contingent awards. FAS 123R prevents this overstatement from affecting financial statements by taking into account the probable outcome of the performance condition when determining the amount that is actually expensed during a reporting period.[19] We believe that utilizing full grant date fair value for SCT and DCT reporting (i.e., taking into account only the measurement criteria of FAS 123R and not both the measurement and recognition criteria) will discourage compensation committees from awarding performance-contingent equity awards and result in their being disfavored among executives. Thus, we strongly oppose ignoring the probable effect of performance conditions when determining amounts that are to be reported in the SCT and DCT.

We note that even accounting standards do not require the full grant date fair value determined under FAS 123R for performance-based awards to be reported anywhere for accounting purposes if performance is not actually achieved and instead take expected performance into account for recognition purposes. In this regard, we believe that the treatment of performance conditions should be distinguished from the treatment of service conditions, which currently and as proposed are not taken into account when determining grant date values. This is because compensation committees typically assume, and we believe it is reasonable for investors to expect, that executives will satisfy the service conditions for equity awards. In contrast, it is not reasonable to assume that performance conditions will be fully satisfied when for accounting purposes that outcome is not considered probable. Thus, performance-contingent awards should be valued based instead on their expected fair value.

5. **As proposed, Instruction 2 to the salary and bonus columns would be revised to provide that any amount of salary or bonus forgone at the election of a named executive officer pursuant to a program under which a different, non-cash form of compensation may be received need not be included in the salary or bonus column, but instead would need to be reported in the appropriate other column of the Summary Compensation Table. Should this approach cover elections to receive salary or bonus in the form of equity compensation only if the opportunity to elect equity settlement is within the terms of the original compensatory arrangement, so that the original arrangement is within the scope of FAS 123R? Why or why not?**

If the original arrangement is within the scope of FAS 123R, the current rules appear to require that the arrangement be reported in the equity compensation columns. We note that, if the proposed instruction is adopted, then an issue will arise as to whether the equity awards should be reported in the year granted or in the year for which the salary or bonus was earned. As noted above, we believe that there are merits to allowing reporting in the year **for** which an

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[19] "In determining the amount recognized, FAS 123R requires a company to estimate at the grant date the number of awards that ultimately will be earned." Release No. 34-55009, Executive Compensation Disclosure, at part II.A. (Dec. 22, 2006).

equity award is granted, even if different than the year in which it is granted, provided that the company's CD&A discusses the compensation in a manner that is consistent with the SCT presentation.

**6. The Commission also has received a rulemaking petition requesting that we revise Summary Compensation Table disclosure of stock and option awards a different way. Instead of reporting the aggregate grant date fair value of awards granted during the year, as we propose, the petition's suggested approach would report the annual change in value of awards, which could be a negative number if market values decline. For restricted stock, restricted stock units and performance shares, the reported amount would be the change in stock price from year-end to year-end. For stock options, it would be the change in the in-the-money value over the same period. Would the approach suggested by the rulemaking petition be easy to understand or difficult to understand? Would the information provided under the suggested approach be useful to investors? In particular, would investors be able to evaluate the decision making of directors with respect to executive compensation if the value of equity compensation on the date of the compensation decision is not disclosed, but instead investors are provided information regarding changes in value of the compensation, which changes occur after the compensation decision is made? Would it enhance or diminish the ability of companies to explain in CD&A the relationship between pay and company performance? Would it be more or less informative to voting and investment decisions than the aggregate grant date fair value approach we propose? Would it be a better measure for computing total compensation, including for purposes of identifying named executive officers? Are there any other ways of reporting stock and option awards that would better reflect their compensatory value? If so, please explain. For example, are there any potential amendments to the Grants of Plan-Based Awards Table or the Outstanding Equity Awards at Fiscal Year-End Table that we should consider to better illustrate the relationship between pay and company performance?**

We recognize that there are many different ways to analyze executive compensation, especially arrangements under which equity compensation is earned and realized over time. While the information that would be provided under the rulemaking petition could be helpful to investors, the presentation reflected in the Commission's proposal will more clearly present the decisions made by the board compensation committee for the current year, and thus will help inform investors as they evaluate management and the board in the context of making proxy voting decisions.

The Commission should, however, consider changes to the Outstanding Equity Awards at Fiscal Year-End Table ("Outstanding Equity Awards Table") and the Option Exercises and Stock Vested Table that may enhance investors ability to evaluate equity-based awards that are held by NEOs. In particular, we believe that the Outstanding Equity Awards Table should be presented on an aggregate, not grant-by-grant basis for each NEO, and should present both the number and year-end in-the-money value of each NEO's vested and unvested options. This presentation would not only significantly reduce the length of the table, but would also allow investors to quickly assess the value of executives' equity-based compensation holdings and, by looking at prior year proxy statements, changes in that value. Although this information can be calculated from the information currently disclosed in the Outstanding Equity Awards Table, it is not clear that many investors make the effort to do so. If the Commission determines that grant-by-grant information of the type currently included in the Outstanding Equity Awards Table has some utility, companies should have the option of providing that information on their websites or in a Form 10-K or Form 10-Q exhibit.

The Commission may also wish to consider having the Option Exercises and Stock Vested Table instead report the intrinsic value of options that first became exercisable during the year, regardless of whether exercised, both because the vesting event is the point at which the executive has earned the award (with a decision on whether or not to exercise being more akin to a decision on whether or not to defer compensation that has been earned) and because this would more closely align the information with that presented in the table for stock awards.[20] In this regard, we note that information on the value realized from exercising stock options is readily available through Form 4 filings.

**7. The Summary Compensation Table requires disclosure for each of the registrant's last three completed fiscal years, and with respect to smaller reporting companies, for each of the registrant's last two completed fiscal years. Regarding transition, our goal is to facilitate year-to-year comparisons in a cost-effective way. To this end, we are considering whether to require companies providing Item 402 disclosure for a fiscal year ending on or after December 15, 2009 to present recomputed disclosure for each preceding fiscal year required to be included in the Summary Compensation Table, so that the Stock Awards and Option Awards columns would present the applicable full grant date fair values, and Total Compensation would be recomputed correspondingly. If a person who would be a named executive officer for the most recent fiscal year (2009) also was disclosed as a named executive officer for 2007, but not for 2008, we expect to require the named executive officer's compensation for each of those three fiscal years to be reported pursuant to the proposed amendments. However, we would not require companies to include different named executive officers for any preceding fiscal year based**

[20] The Commission also should explicitly confirm that neither the vesting nor the exercise of options is reported in the SCT.

**on recomputing total compensation for those years pursuant to the proposed amendments or to amend prior years' Item 402 disclosure in previously filed Forms 10-K or other filings. Would recomputation of prior years included in the 2009 Summary Compensation Table to substitute aggregate grant date fair value numbers for the financial statement recognition numbers previously reported for those years cause companies practical difficulties? Is there a better approach that would preserve the objective of year-to-year comparability on a cost-effective basis as a transitional matter?**

We believe that the Commission's proposed approach for transitioning to the proposed grant date reporting standard is reasonable. We do not expect that presenting prior years' grant date fair values will create any difficulties for most issuers. However, in case of unexpected circumstances, the Commission may wish to grant the Division of Corporation Finance authority to waive the requirement to recompute prior year grant date fair values in cases of hardship. We expect that in any such cases the Division would require appropriate disclosure of the lack of year-to-year comparability.

## III. Enhanced Director and Nominee Disclosure

### A. General Comments

We do not support the adoption of enhanced director and nominee disclosure as proposed by the Commission, for the reasons discussed below. Although we agree that a proxy statement should include information material to an investor's voting decision, we are concerned that the Commission's proposal would require companies to provide disclosure on the basis of a number of subjective, rather than objective, factors. The Commission's proposal, in our view, also suggests, erroneously we believe, that there is an articulable set of factors underlying a person's nomination when, in many cases, the list of factors which underlie a person's nomination may be considerable, and the interplay among these factors may be impossible to encapsulate in a brief summary. Not only are the factors affecting one person difficult to describe, but the characterization of the strengths and weaknesses of the members of the board as a whole are even more complicated.

We believe it is important that proxy statements be sufficiently concise to encourage a substantial portion of a company's shareholders to read, and make voting judgments based on, the proxy statement. As the requirements for proxy disclosure expand beyond strictly factual information to more subjective topics, we are concerned that such disclosures will not be particularly meaningful to shareholders, and will carry the risk of being misleading in a number of respects. For example, each of the members of a company's nominating committee may have a variety of reasons why he or she believes a particular person should be nominated as a director, which may differ from the views of other members. Such members may also be aware of the limits of the scope of a candidate's professional experience, or other factors that may represent weaknesses rather than strengths. Against this backdrop are subjective and personal considerations, such as whether the proposed nominee would work cooperatively with the other

members of the Board of Directors in the best interests of shareholders, and considerations relating to the other persons who the committee has considered, or might want to consider, for nomination. The communications among members of the nominating committee may articulate certain of these considerations, but not necessarily all of them. The burden of disclosing the congeries of factors entering into consideration by each member of the nominating committee may be extensive. Expanding the disclosure to reasons underlying the collective decision by the members of the nominating committee may be impossible. Our fear is that if disclosure is mandated, it will either be so generalized as to be meaningless to investors, or will be inaccurate because of the difficulty of reflecting accurately the views, expressed and unexpressed, of the members of the nominating committee.

**B. Responses to Certain of the Commission's Inquiries**

**1. Would the proposed amendments provide investors with important information regarding directors and nominees for director? Are there any additional changes that we should make to further improve the disclosures about director and nominee qualifications?**

We do not believe that the new rules should refer to characteristics that "qualify" a person to serve as director, except to the extent that the company's governing instruments actually create minimum director qualifications, such as a requirement to be a shareholder or to own a specified minimum number of shares. Requiring disclosure about how individuals are "qualified" to serve as a member of the board of directors may:

- suggest that as a result of meeting such qualifications, the directors have various levels of expertise that would hold them to new and higher standards, and as a result unintentionally and inappropriately expose those directors to increased risk of liability; and

- in the context of committee service, create an inappropriate and incorrect impression that only persons with certain backgrounds are "qualified" to serve on certain committees (for example, only persons with human resources or compensation backgrounds should serve on the compensation committee, or only persons with accounting or finance backgrounds can be productive members of audit committees). Our experience indicates that persons from a wide variety of backgrounds can be effective members of these committees, and that committees overall often benefit from a diversity of backgrounds, experiences and skill sets among their members. Creating the impression that only persons with certain backgrounds are qualified to serve on specific committees may unintentionally result in a narrowing of the diversity of skills and perspectives that exist on committees, which may not be in the best interests of shareholders.

Unlike the rule relating to an audit committee financial expert, which does not require a company to designate such an expert, but only to disclose whether or not such an expert has been

designated, the proposed rule would require that a company make an affirmative statement regarding the qualifications of each director. Unlike the audit committee financial expert, for which the general qualifications are set forth in the Commission's rule, there are no standards by which qualification to serve as a director are determined. Indeed, we are of the view that there should not be any mandated standards, because service as a director involves many qualities, many of which are subjective. We believe that the absence of specified standards in this context makes the risk of investor confusion even greater than in the case of the audit committee financial expert. Should, however, the Commission determine to require statements with respect to the qualification of a director, we suggest that the final rule provide, as in the context of the audit committee financial expert, that any disclosure with respect to a person's experience, qualifications and skills is not intended to result in that person being deemed to be an expert for any purpose, does not impose any additional duty, obligation or liability on that person, and does not affect the duties, obligations or liabilities of other directors.

We believe the Commission can achieve its objective of enhancing investor understanding of the qualifications of director candidates without requiring the disclosure of subjective and potentially misleading information. In lieu of the Commission's proposal, we recommend that the Commission consider expanding the objective information currently required by Item 401(e) of Regulation S-K, such as the Commission is proposing to do by expanding the requirement for information about other directorships of public companies to cover a five-year period. This alternative approach could, for example, require disclosure of the person's business experience over a ten-year period rather than a five-year period. We note that, under existing Commission rules, a company remains free to provide in its proxy statement additional information relating to a director's professional, business or other background if the company believes such information would be meaningful to shareholders. This type of expanded objective disclosure, together with disclosure mandated by other existing Commission rules and stock exchange rules, would enhance the information made available to enable investors to assess the suitability of nominees.

**2. If Item 401 is amended as proposed, should the disclosure currently required by Item 407(c)(2)(v) of Regulation S-K regarding disclosure of any minimum qualifications that a nominating committee believes must be met by someone nominated by the committee for a position on the board, be retained? Does the disclosure by Item 407(c)(2)(v) provide useful information that would supplement the information provided pursuant to the proposed amendment to Item 401?**

We believe that the disclosure elicited by Item 407(c)(2)(v) continues to be meaningful and appropriate, even under the Commission's proposed revision of Item 401. We believe, however, that a significant portion of the new proposed disclosure (specifically, any disclosure as to why a particular person has been nominated for election) would be more appropriately addressed under Item 407 rather than under Item 401. The final rules or adopting release should also acknowledge that, in the case of controlled companies or nominees selected pursuant to contract rights, disclosure of the existence of that status or those rights satisfies this requirement.

**3. Should we amend Item 407(c)(2)(v) to require disclosure of any additional factors that a nominating committee considers when selecting someone for a position on the board, such as diversity? Should we amend our rules to require additional or different disclosure related to board diversity?**

We believe that the language of Item 407(c)(2)(v) already encompasses diversity to the extent a committee considers diversity in selecting nominees and that no additional disclosure requirement is necessary. In our experience, many companies that affirmatively consider issues of diversity in selecting nominees already disclose that fact.

**4. Would director qualification disclosure for all of a company's board committees be useful to investors, or should the disclosures be focused on membership of certain key committees, such as the audit, compensation and nominating/governance committees?**

We believe that any new required disclosure should be focused on the reasons a candidate was selected for nomination to serve as a member of the board of directors. In the specific context of committees, we believe that:

- it is important to keep in mind that shareholders do not elect directors to specific committee assignments, but rather to membership on the board as a whole, and that boards generally retain their ability to change committee assignments at any time;

- committee assignment decisions are often not determined until after the annual meeting at which directors have been elected, and we would not want to see a disclosure requirement create an incentive for companies to defer decisions regarding committee composition;

- as noted above, requiring disclosure of all the “qualifications” for committee service that a nominee might have could lead to unwieldy, lengthy and overwhelming disclosure that is not useful to investors; and

- to the extent any additional disclosure is nevertheless required in the Commission’s final rules, it should be limited to committees that are required by applicable rules (currently audit, compensation and nominating committees).

**5. Should we require the proposed director qualification disclosure less frequently than annually? Even though the overall composition of a board may change, is it sufficient to require this disclosure only when a director is first nominated or periodically, such as every three years? Should the disclosure be required only when the director is standing for election, or should it be required each year, as proposed,**

**in order to facilitate shareholders' assessments of the quality of the board as a whole?**

Were the Commission to adopt the proposed director qualification disclosure, we believe it should only be required with respect to a nominee in a year in which the nominee is standing for election or re-election. Information regarding directors not standing for election would be available on EDGAR with respect to the year in which the director was last elected. We also note that, in the case of a company with a classified board:

- the "specific experience, qualifications, attributes or skills that qualify that person to serve as a director for the registrant at the time that the disclosure is made" -- which is the information called for by the Commission's proposal -- is simply that the person is an existing director whose term continues in effect. This disclosure, while fully accurate, is not helpful to investors; and

- it seems unlikely that the disclosure relating to director qualifications for individuals whose terms have not expired at the time of the annual meeting would become stale from the time it was last provided.

**6. Would it be helpful to investors if we required companies to list and describe all committees of the board similar to the current disclosure requirements for audit, compensation and nominating/governance? Would it also be helpful if we required disclosure of whether the board (or a committee) periodically conducts an evaluation of the performance of the board as a whole, the committees of the board and/or each individual director?**

We do not believe companies should be required to list and describe all board committees. Boards often create *ad hoc* committees to undertake specific tasks, or assign additional temporary duties to standing committees. We do not believe that this information is necessarily of any importance to shareholders and are concerned that, in some situations, this disclosure could harm the company. For example, premature disclosure of the formation of a special committee to explore a proposed significant transaction could force premature disclosure of information that is generally not viewed as material and that the Commission has historically protected from disclosure and such premature disclosure could be very harmful to the company. Similar concerns may exist with the formation of special litigation committees or special investigative committees. Disclosure of the creation of certain special committee may also provide competitors with valuable information, to the detriment of a company's shareholders. Companies are, of course, free to disclose more information about their committee structure than is required under current Commission rules, and many companies make such disclosures. We believe, however, that mandating such disclosures would be inappropriate.

We do not believe the Commission should require disclosure as to whether companies conduct board, committee and/or individual director evaluations. We note that many companies currently make such disclosure either voluntarily in their proxy statements or as part of their

publicly available corporate governance guidelines. We believe voluntary reporting is preferable to any prescriptive mandate and that mandatory disclosure is not necessary in light of current practices of many companies.

**7. Should we require disclosure of other directorships for more than the past five years? If so, for how long?**

We believe that a five year look-back with respect to disclosures about past directorships generally provides sufficient information, and that disclosures going back further are not likely to be material. We note that Exchange Act Rules 12b-20 and 14a-9 require disclosure of, in addition to the information expressly required to be included in a report or proxy statement, such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.

**8. Could requiring more director and nominee qualification disclosure in any way hinder a company's ability to find potential candidates for the board? If so, explain how.**

We are concerned that a requirement could have such an effect. Among other things, statements that a particular candidate possessed certain qualities (for example, leadership skills) would suggest that a candidate who is not identified as having been selected on the basis of such skills lacks them. The result may be personally embarrassing, create resentment on the Board against those directors responsible for articulating the qualities of individual directors, and weigh adversely on a person’s consideration as to whether to seek election as a director. As discussed above, we believe that, if the proposed rule is adopted, the Commission should make clear that any additional disclosure is not intended to result in such person being deemed an expert for any purposes, does not impose any additional duties, obligations or liability on such person and does not affect the duties, obligations or liabilities of other directors.

**9. Should the current five-year disclosure period for legal proceedings be maintained? Should it be longer than proposed, for example for fifteen or twenty years? Should there be no time limit? Would it be more appropriate to require disclosure of legal proceedings for longer periods with respect to certain types of legal proceedings - for example, criminal fraud convictions, civil or administrative actions based on fraud involving securities, commodities, financial institutions, insurance companies or other businesses? If so, for what period or periods and why?**

We believe that a ten year look-back with respect to disclosures regarding involvement in legal proceedings would, in general, provide adequate information to investors. We note that Exchange Act Rules 12b-20 and 14a-9 require disclosure of, in addition to the information expressly required to be included in a report or proxy statement, such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.

**10. Are there any additional legal proceedings disclosures that reflect on a director's, executive officer's or nominee's character and fitness to serve as a public company official that should be required to be disclosed? For example, should we expand the current requirements to require disclosure of:**

- Any civil or administrative proceedings resulting from involvement in mail fraud, or wire fraud;
- Any judicial or administrative findings, orders or sanctions based on violations of Federal or State securities, commodities, banking or insurance laws and regulations or any settlement to such actions;
- Any disciplinary sanctions imposed by a stock, commodities or derivatives exchange or other self-regulatory organization; or
- Situations where the director, nominee, or executive officer was a general partner of any partnership or served as a director or executive officer of any corporation subject to any Federal or State agency receivership?

We note that the California Corporate Disclosure Act currently requires disclosure regarding any conviction for fraud in the past ten years that has not been overturned or expunged. We believe that this would also be appropriate disclosure for all public companies.

**11. Should we continue, as proposed, to permit companies to exclude disclosure of director, director nominee or executive officer legal proceedings, when the registrant concludes that the information would not be material to an evaluation of the ability or integrity of the director, nominee or executive officer, or should this disclosure be required in all cases?**

We believe that the current instruction allowing a company to exclude disclosure if it is not material to an evaluation of the director or director nominee should be retained. In our experience, this exception has not been the subject of abuse and is appropriate.

**12. Should we make any special accommodations in the proposed amendments to Item 401 for smaller reporting companies? If so, what accommodations should be made and why?**

Because of the generally smaller board size of many smaller reporting companies and the resulting practical constraints on the possible configurations of board committees (i.e., given the smaller number of independent directors, many directors must be appointed to serve on multiple committees simply to meet the membership requirements of these committees and enable them to perform their functions rather than based on any special expertise, skill set or qualifications of the director), we believe that smaller reporting companies should not be required to provide any

additional disclosure regarding director and nominee qualifications on a committee-level basis as in many cases such disclosure would not provide meaningful new information to shareholders.

As we discussed above, we also believe that it would not be appropriate to require disclosure of director qualifications and reasons for their selection at the board of directors level. In today's environment, it is extremely difficult to find persons who are willing to serve as directors of a public company. This is true in spades for smaller reporting companies, for whom serving as a director is typically not seen as a "prestigious" position and who nearly always compensate their directors at a much lower level than larger companies. Smaller public companies do not have the luxury of choosing among a long list of qualified candidates who would be willing to serve as a director of such small company. In fact, smaller public companies often consider themselves lucky to be able to attract outside directors at all.

Given these realities of director service on a the board of a smaller reporting company, we do not believe that disclosure of any kind of subjective factors relating to the nominee's selection, such as director "qualifications," should be required.

**13. Should the proposed amendments regarding director and nominee qualifications, past directorships held by directors and nominees, and the time frame for disclosure of legal proceedings apply to registered management investment companies? If so, where should each of the disclosures be required (e.g., proxy statements, statements of additional information, and/or shareholder reports)? Does the disclosure requirement need to be modified in any way to make it more appropriate for registered management companies?**

As indicated elsewhere in this letter, we do not support extending the proposed disclosure obligations to investment companies.

## IV. New Disclosure about Company Leadership Structure and the Board's Role in the Risk Management Process

### A. General Comments

The Commission is proposing a new disclosure requirement to Rule 407 of Regulation S-K and a corresponding amendment to Item 7 of Schedule 14A to describe the company's leadership structure and to disclose (i) whether the company has a combined principal executive officer and board chair, or whether those positions are filled by two different people, (ii) if one person serves in both roles, whether the company has a lead independent director, as well as the specific role the lead independent director plays in the leadership of the company, and (iii) why the company has determined that its leadership structure is appropriate given the specific characteristics or circumstances of the registrant. Finally, the Commission is proposing to require additional disclosure in proxy and information statements about the board's role in the company's risk management process.

We support the disclosure of the company's leadership structure, and agree with the Commission that such information is important to investors. While we believe it may be evident from existing disclosure, a specific statement as to whether or not a company has a combined principal executive officer and chair, or a lead independent director, may assist investors' understanding of the checks and balances inherent in any governance system. In this regard, we also support a requirement to describe in general the role that a lead director plays in the leadership of the company.

We do not, however, believe that a company should be required to state why it has determined that its leadership structure is appropriate, for the following reasons. First, the disclosure assumes that a company has made a specific determination as to the appropriateness of its leadership structure. In many situations, this may not be the case. Instead, a company may simply not have determined that any alternative leadership structure is more appropriate. Such a failure to make an affirmative determination regarding leadership structure does not necessarily represent, in our view, any failure by a board to discharge its responsibilities. It may instead mean that the board, through its ongoing reviews and assessment processes, believes that the board functions effectively and that there is no reason at the time to review and assess alternative leadership structures. Second, even if a board had determined to implement a particular leadership structure, that determination may have occurred five, ten or even more years ago. It would, in our view, be inappropriate (and most likely meaningless to investors) for a company to be obligated to disclose the historical reasons that the members of a prior board of directors made any specific determination. Third, we are concerned that a change of leadership structure could call into question the accuracy of a company's prior statement that the leadership structure was appropriate . We believe that any disclosure obligation that may inhibit a company's willingness to review and change its leadership structure is ultimately adverse to investors. We suggest that, instead of requiring the affirmative statements set forth in the Proposing Release, the Commission require a company that has changed its leadership structure in a material respect during the prior fiscal year, or has plans to implement such a change, to describe such change and why the company believes such a change is appropriate for the company. By tying the disclosure to a current or planned change of management structures, in which an evaluation of a current (or prior) structure with a new structure is an active part of the board dialogue, the Commission would effectively bring shareholders into the boardroom by illuminating the basis for the changes, and perhaps give shareholders an opportunity to evaluate the benefits of the proposed new structure.

We support the Commission's suggestion that a company disclose the extent of the board's role in the company's risk management, provided that such disclosure is brief and factually based rather than speculative. Specifically, we believe that it would be helpful for investors to know whether a board has a risk management committee, the composition of such committee the primary scope of that committee's responsibilities. We would not support a requirement, if a company does not have a risk management committee, for a company to state why it does not have one. In our view, companies should not be required to provide a granular discussion regarding the management of various specific categories of risk, but may choose to do so depending upon the structures they have implemented. We do not support disclosure of the

effect that risk management has on a company's leadership structure, because this information is likely to be speculative.

It is important to us that no investor is led to believe that "risk management" necessarily means "risk control." Any risk management system is based on an identification of particular risks, an assessment of the various components of such risks, an evaluation of the likelihood of occurrence of each such component, the interplay between and among such components and the economic and other consequences of such occurrences, a review of the ways in which such risks can be mitigated and the costs of such mitigation, and other systemic questions, such as how variations from an anticipated risk profile are identified, whether the identification and response system is effective, and extent to which, in a dynamic environment, each of the foregoing factors requires continuing review and re-evaluation. As good as a company's risk management system may be at providing some assurance that a company's risk profile is not inconsistent with what it intends it to be, many factors relating to risk are beyond a company's control. Just as it would be deceptive to investors to suggest that a company's prior financial performance is indicative of future performance, it would be equally deceptive to suggest that the existence of any particular risk management system, and the allocation of risk management responsibility to the board or other members of a company's leadership structure, in some way insulates a company from various forms of risk or even assures that, in a given situation, the risk management system will be effective. For these reasons, we believe that a brief statement with respect to the extent of the board's role in the company's risk management and the effect, if any, this has on the company's leadership structure, would be preferable to any more prescriptive disclosure.

We also want to note certain differences between the proposed amendments regarding leadership structure and the Commission's description of them in the Proposing Release. In the Proposing Release, the Commission characterizes the new rule as requiring disclosure of "why the company believes it is the best structure for it at the time of the filing." The proposed amendment does not refer to a "best" structure, but instead to why a particular leadership structure "is appropriate" given the specific characteristics or circumstances of the registrant. We believe the differences between the Proposing Release and the proposed amendment are more consequential than just word choice. A statement as to "best" structure suggests that a board has undertaken a conscientious review of structures, and in some form of vote or equivalent determination has concluded that its current structure is the "best". We read the language of the proposed amendment as merely requiring a conclusion that a structure is "appropriate. " In this regard, we believe that a company may conclude that there are a range of "appropriate" leadership structures, and that its current leadership structure falls within that range. Although the language of the amendments should be determinative, we are concerned that, were the amendments to be adopted, the Commission and its staff should not take the position that a determination that a structure is "appropriate" means that it is the "best" structure. We encourage the Commission to clarify this in any adopting release.

As an overall comment, we believe that, aside from a general description of the leadership structure, more extensive disclosure should not be required for controlled companies. To the extent that a single shareholder, or a group of shareholders, has the ability to adopt and

amend bylaws, and to elect the entire board, we believe the fact of such control subsumes the need for more detailed leadership structure disclosure. In these instances, it may be the parent, rather than the board, that has effectively determined whether to create a particular leadership structure. For example, an executive officer of a subsidiary may have been assigned to such position pursuant to a parent's overall allocation of responsibilities within a consolidated group. While the disclosure of the structure may be important, disclosure of the parent's rationale would in our view go beyond what should appropriately be required, and may lead to generic disclosure that would not be meaningful to investors. Similarly risk management at a subsidiary may be within the scope of the overall risk management function of a parent entity, rather than a stand-alone set of standards at the subsidiary level. Indeed, it may be appropriate to advise investors that any leadership structure or risk management structure of the subsidiary may be subject to change at the sole discretion of the parent.

**B. Responses to Certain of the Commission's Inquiries**

In response to the Commission's request for comment regarding specific questions, please see our responses below:

**1. Are the proposed amendments to Item 407 appropriate? Are there additional disclosure requirements that should also be included in these proposed requirements?**

As discussed above, we support a provision that would require brief disclosure about a company's leadership structure. On the other hand, and for the reasons set forth above, we believe that a company should not be required to state why it has determined that its leadership structure is appropriate. Instead, we suggest that the Commission adopt an amendment requiring a company that has changed its leadership structure in a material respect during the prior fiscal year, or plans to implement such a change, to describe such change and why the company made the change. We support the Commission's suggestion that a company disclose the extent of the board's role in the company's risk management, provided that such disclosure is brief and factually based rather than speculative. Specifically, we believe that it would be helpful for investors to know whether a board has a risk management committee (or a committee performing those functions), the composition of such committee is and the primary scope of that committee's responsibilities. We would encourage the Commission not to require companies to disclose any more specific information. We also do not believe that disclosure of the effect that risk management has on a company's leadership structure, because this information is likely to be speculative.

Also, we note that many companies have executive committees of their boards, which are empowered to act with respect to all matters as to which the board is authorized to act, except as may otherwise be provided by law. We suggest that the Commission consider requiring disclosure of existence of the executive committee in this situation, as well as an identification of its members and its chair.

Also as discussed above, we recommend that the Commission consider excluding controlled companies from the scope of disclosures other than the basic disclosure of the leadership structure.

**2. Are there certain considerations that would affect the company's leadership structure that should be highlighted in the proposed amendment? If so, explain.**

We are not aware of any such considerations, except to the extent that a company may be mandated by contract or otherwise to maintain in effect any particular leadership structure, or may be prevented from changing its leadership structure without the consent of certain third parties, such as an investor group or financial institution.

**3. Are there any additional disclosures about a company's leadership that would be helpful to investors?**

As discussed above, it may be helpful to investors for a company to disclose if it has an executive committee authorized to perform any or all of the functions of the board, and certain details with respect to such a committee.

**4. Should we require disclosure of the specific duties performed by the board's chair or independent lead director?**

Although we support a requirement to describe in general the role that a lead director plays in the leadership of the company, we do not believe that a disclosure of the specific duties performed by the chair or independent lead director should be required. We are not convinced that the incremental benefit of the disclosure would be meaningful to investors.

**5. Should we require disclosure of other board structure matters, such as how a company determines the number of independent directors to have on its board, and/or how a company determines the size of the board?**

We do not believe such additional information should be required. Except in the case of controlled companies, stock exchange rules already require that companies have a majority of independent directors. Why a company may choose to have a greater number of independent directors is, we believe, immaterial to investors, as is disclosure regarding board size. Companies should be encouraged to consider a variety of different leadership and board structures, and mandating disclosures regarding these structures may inhibit such experimentation.

**6. Are there competitive or proprietary concerns about the level of detail about the company's risk management structure and function that the proposed rule should account for? If so, please identify these concerns and explain how they should be accounted for.**

Within the scope of certain businesses and industries competitive or proprietary concerns may arise, and these problems may be exacerbated by adding detail. As a very general example, knowing that a bank has a security system in place to guard its assets may be important to investors; knowing more details of how the system operates and is administered may be more of interest to a felon. The Commission should be sensitive to the extent to which the information it requires a company to disclose is of value to competitors and others, to the detriment of the company's investors. Because of the high barriers to confidential treatment imposed by the Commission (which we believe are higher than those imposed by many other governmental agencies), we are concerned that too detailed disclosure requirements will in fact harm shareholders of certain companies.

**7. Should we make any special accommodations in these proposed amendments for smaller reporting companies? If so, what accommodations should be made and why?**

So long as the required disclosures regarding leadership structure and risk management are limited in the manner suggested by our comments above, we do not believe that compliance would be overly burdensome for smaller reporting companies.

**8. The proposals address risk management oversight by the board of directors as a part of the corporate governance disclosures required in proxy and information statements. We are considering whether we should revise our existing disclosure requirements, such as in Items 303 and 305 of Regulation S-K, to require additional disclosure regarding a registrant's risk management practices in other registrant filings, such as annual and quarterly reports? Should we consider proposing additional requirements? If so, what additional or different disclosure requirements should we consider proposing?**

Except as provided elsewhere in this letter, we would not encourage the Commission to propose additional disclosure requirements.

**9. Should we, as proposed, require a registered management investment company to provide disclosure about its leadership structure and the board's role in the risk management process? Are there alternative disclosures relating to a fund's leadership structure and board involvement in the risk management process that would be more helpful to investors? If we require each of the disclosures, where should such disclosures appear (e.g., proxy statements, statements of additional information, and/or shareholder reports)?**

The Commission also plans to enhance disclosure for investment company ("fund") directors and director nominees. In the Proposing Release, the Commission states that "investors in funds would, for the same reasons as investors in operating companies, find this information useful." In explaining the proposal for operating companies, the Commission discussed the relationship of a company's overall compensation policies to corporate risk, director and nominee qualifications, and the company's leadership structure. The Commission's focus on corporate risk profiles related to the extreme market turmoil during the past 18 months.

Following its operating company rationale, the Commission's proposal for fund proxy statements would require each director or nominee to discuss "specific experience qualifications, attributes or skills that qualify that person" to serve as a director and/or committee member. "If material, this disclosure should… include *information about the person's risk assessment skills*, particular areas of expertise, or other relevant qualifications." In a fund's statement of additional information (SAI), the Commission is proposing that a fund "disclose the extent of *the board's role in the Fund's risk management ….*"

The premise of the Commission's proposals for funds in the areas previously noted does not translate well from the operating company context. The Commission has not cited any evidence that funds experienced the same type or level of risk taking as corporate institutions. At this point, the Commission's proposal for funds seem to be an afterthought, which we believe should be reconsidered. In the fund context, risk assessment should focus on a fund's staying true to its disclosed investment objective, investment strategies, and risk disclosures.

Regarding a person's risk assessment abilities, typical skills, such as education, business experience and good judgment, that make someone an able fund director would be the same skills that would enable a director to provide appropriate risk oversight in the fund context. If the Commission is looking for another type of skill set for fund directors, it should provide additional guidance.

In considering a board's role in risk management, we do not believe that Commission should impose any disclosure requirements that suggest that a director should micro-manage a fund's day-to-day operations. This would be counter to the proper role a board, as well as other fund incentives that the Commission and its staff are pursuing. For example, the Director of Investment Management stated, in a speech last March, that his "staff is [working on] possible rule modifications and other guidance that may enable directors to focus their time more

efficiently overseeing conflicts of interest rather than engaging in day-to-day management of the fund." In the present rule-making, the Commission seems to be suggesting more than an oversight role for fund boards. We request that the Commission clarify that this is not the case.

**10. As proposed, funds would be required to include the proposed disclosure in registration statements filed on Forms N-1A, N-2, and N-3. Should we differentiate between open-end and closed-end funds? For example, should we omit this requirement from Form N-2 because closed-end funds generally hold annual shareholder meetings pursuant to exchange requirements and their shareholders will receive this disclosure in annual proxy or information statements?**

As stated above, we would not support additional disclosures by funds.

## V. New Disclosure Regarding Compensation Consultants

### A. General Comments

In our view, the disclosure triggers in the proposed amendments should be refined, and any resulting disclosure should focus on the matters the compensation committee considered in determining to hire the consultant rather than simply on fees.

The Commission's proposed amendments would require disclosure about the fees paid to compensation consultants and their affiliates when they play any role in determining or recommending the amount or form of executive and director compensation, if they also provide other services to the company. The proposed amendments also would require disclosure of whether the decision to engage the consultant or its affiliates for other services was made, subject to screening, or recommended, by management, and whether the compensation committee or the board approved such other services. The Commission states that the basis for the proposed disclosures is that the provision of additional services by compensation consultants or their affiliates may create the appearance, or risk, of a conflict of interest that may call into question the objectivity of the consultants' executive pay recommendations, and that the proposed disclosures are intended to enable investors to assess any incentives a compensation consultant may have in recommending executive compensation and better assess the compensation decisions made by the board.

We believe that there are more effective and direct means to address the objectives stated by the Commission. The standard currently applied under the Commission's rules for determining when compensation consultant disclosure is required, which focuses on whether a consultant has "any role … in determining or recommending the amount or form of executive or director compensation," is subject to nuance and can lead to difficult line-drawing, which will be problematic when a burdensome disclosure obligation is triggered. Therefore, we believe that the circumstances triggering heightened disclosure obligations regarding compensation consultant objectivity should be more clearly defined. Specifically, we recommend that disclosure regarding potential conflicts of interest apply to any compensation consultant that is

retained by the board compensation committee or that is described as being "independent." In order to place shareholders in a position to better assess for themselves factors that may affect the objectivity of a compensation consulting firm that serves the board compensation committee, we believe that any required disclosures should include the matters that the compensation committee considered in determining whether the firm is able to provide objective and professional advice.[21] We are concerned that disclosures focusing on fees will not be as effective in helping shareholders to assess the significance of any factors affecting the consultant's objectivity and yet may become viewed by shareholders as a standard of independence. We also are concerned with practical difficulties in providing the proposed fee disclosures, and question whether the costs of gathering such information justify its limited utility.

### B. Responses to Certain of the Commission's Inquiries

#### 1. Will this disclosure help investors better assess the role of compensation consultants and potential conflicts of interest, and thereby better assess the compensation decisions made by the board?

We respectfully do not believe that the proposed disclosures will help investors better assess consultants' potential conflicts of interests. As noted by the Commission, "the provision of additional services by compensation consultants or their affiliates <u>*may*</u> create the <u>*appearance*</u>, or risk, of a conflict of interest." (emphasis supplied). Thus, the proposed disclosures would do little more than highlight the possible appearance of a conflict of interest without mandating disclosure of information that would enable shareholders to assess whether fees or other circumstances actually create a conflict of interest. We note that concerns over conflicts of interests from fee arrangements arise in many contexts, and we understand that a number of compensation consulting firms have implemented procedures, similar to those used by other companies ranging from investment banking firms to proxy advisory firms, to avoid potential conflicts that may arise in the course of their business.[22] Focusing the disclosure on the compensation consulting firm retained by the board compensation committee (or on any other compensation consulting firm that is described as "independent") and addressing the actual factors considered by a compensation committee in evaluating the objectivity of the compensation committee's consultant will more directly address the issue identified by the Commission as the objective of this rule initiative and provide information that is more useful for investors seeking to assess the firm's objectivity.

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[21] The disclosure thus would be similar to the existing requirement that companies disclose the factors considered by a board of directors when determining that a director is independent. See Item 407(a)(3) of Regulation S-K.

[22] For example, in response to concerns over whether a proxy advisory firm's practice of consulting with corporations regarding its voting positions presented a conflict of interest, the Government Accounting Office recently concluded that the proxy advisory firm had taken sufficient steps through disclosures (short of actual fee disclosures) and "firewalls" to mitigate any potential conflicts of interest. Corporate Shareholder Meetings: Issues Relating to Firms that Advise Institutional Investors on Proxy Voting," U.S. Government Accounting Office (June 2007).

**2. Would the disclosure of additional consulting services and any related fees adversely affect the ability of a company to receive executive compensation consulting or non-executive compensation related services? If so, how might we achieve our goal while minimizing that impact?**

We do not believe that the proposal will affect a compensation committee's or company's ability to receive executive compensation or non-executive compensation-related services. Our experience is that consultants from both "multi-service" compensation advisory firms and from "boutique" compensation advisory firms take steps to avoid conflicts of interest and to preserve their objectivity. However, we are concerned that the proposed disclosures could result in compensation committees selecting one consulting firm for executive compensation advice and companies selecting a different consulting firm for non-executive compensation work based solely on a desire to avoid a possible appearance of conflicts, as opposed to basing such decisions on actual objectivity and other merits.

**(a) Are there competitive or proprietary concerns that the proposed disclosure requirements should account for? If so, how should the amendments account for them if the compensation consultant provides additional services?**

We expect that the proposed disclosures could affect compensation committees' and companies' decisions on which firms are retained, both for executive compensation matters and on other matters, in order to avoid disclosure of potentially competitive or proprietary information regarding the nature or cost of other projects for which they may engage a consulting firm or its affiliates. For example, if a company is exploring certain strategic alternatives for its business that could affect a significant number of employees, it might avoid selecting a firm for that work if the nature of the work and the magnitude of the project (as revealed through fee amounts) would be subject to disclosure.

**(b) Are there additional disclosures regarding the potential conflicts of interest of compensation consultants that should be required? For example, would requiring disclosure of any ownership interest that an individual consultant may have in the compensation consultant or any affiliates of the compensation consultant that are providing the additional services to the company help provide information about potential conflicts? If so, why?**

Because there are many different aspects to assessing a consultant's objectivity, we believe that more useful and effective disclosure would be obtained if the Commission required a discussion of the actual factors considered by a compensation committee in assessing its consultant's objectivity, regardless of whether the firm provides other services to the company. We believe that this will be more effective in highlighting potential conflicts of interest than

attempting to identify in advance and prescribe by rule the situations in which such conflicts may arise.

**(c) The proposed disclosure requirement calls for disclosure of services during the prior year. Should we also require disclosure of any currently contemplated services in order to capture a situation where the compensation consultant provides services related to executive pay in one year and in the next year receives fees for other services? If so, should we require that fees for the currently contemplated services be estimated? Is there a better way to require that information, for instance through the date of the filing? Should we require disclosure for the prior three years?**

We expect that the proposed fee disclosures will be difficult and expensive for companies to provide, and that those difficulties will be exacerbated if disclosure is required for contemplated services, services during the current year or past services. We believe that it is inaccurate to analogize disclosure of fees paid to consultants and their advisors to the fee disclosures that companies are required to make in relation to fees paid to their independent audit firms. Audit firm fee disclosure has developed in a highly regulated environment, where governmental, PCAOB and self-regulatory initiatives have provided an extensive set of standards that, among other things, delineate certain services as audit services or audit-related services, other services as neither audit or audit-related, and still other services as impermissible for an independent auditor to provide, and where companies and registered public accounting firms are required to monitor the services provided by the independent auditor and its associated entities. In contrast, there currently is no requirement that companies track or even identify fees paid to compensation consultants or to their affiliates, which may be involved in businesses that have no connection to compensation-related matters. Nor are there established professional standards for determining whether services are related solely to executive and director compensation.[23] The absence of existing professional standards for identifying services that constitute "executive and director compensation services" and those that constitute "additional services," and the absence of standards requiring consulting firms to separately identify or separately charge for "additional services," means that companies will encounter many practical difficulties in trying to provide the proposed fee disclosures.

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[23] It is common for executive compensation consultants to advise compensation committees on arrangements that are not limited exclusively to executives (as defined under the securities rules) and directors. Thus, for example, if a consultant advises on the terms of a stock option plan and officers or other employees who are not executives or directors are granted awards under the plan, the company will have to determine whether the consultant's advice constituted "additional services" that would trigger segregated fee disclosure for executive and non-executive compensation services. Factors that could complicate that determination include situations where non-executives are eligible to participate under the plan but are not in fact granted awards under the plan, or are granted awards under the plan only after the consultant has ceased to be involved with the design of the plan, and whether the consultant has been informed that non-executives might be allowed to participate in the plan.

Thus, we believe that many practical difficulties will arise if companies are required to identify and report segregated fee information, and that it will be expensive and time-consuming for companies to do so, both when upon initial adoption of the proposed rules and whenever a compensation committee determines to change consultants. In addition, companies may be required to seek interpretive advice from the Commission and its staff regarding the characterization of services and fee disclosures under the regime that the Commission is proposing to now create, such as when the consultant's fees involve a fixed element or the consultant advises on arrangements that affect both executives and non-executive employees.[24] Thus, we believe that fee disclosure, if required, should address only services provided during the last fiscal year, in order to limit the complexity and expense of gathering the required information.

**(d) Is the proposed exclusion for consulting services that are limited to broad-based, non-discriminatory plans appropriate? Should we consider any other exclusions for services that do not give rise to potential conflicts of interest? If so, describe them.**

The standard for determining whether information on the objectivity of compensation consultants is required should not be based upon the factual inquiry of whether the compensation consultant's advice in fact played any role in determining or recommending the amount or form of executive compensation. Instead, if this item is to present information on the objectivity of compensation consultants utilized by a compensation committee, and not just the structure of the compensation committee's processes, we believe that shareholders should be provided the opportunity to assess the independence of a compensation consultant's objectivity when the compensation consultant is retained by the board compensation committee or is described as being "independent." We believe that the "any role" standard in some respects is too broad. For example, it could encompass a consultant that was retained by management and whose work was incorporated into recommendations presented by management to the compensation committee, without the consultant knowing how its work product would be utilized, and as well could encompass a compensation consultant that is utilized by, but whose work is vetted and validated by, the compensation committee's own consultant (for example, we understand that some consulting firms utilize survey data developed by other consulting firms).[25] In other respects, the

[24] As another example, if a consultant assists a company in designing a 401(k) plan and an "excess benefit plan" (as defined under Rule 16b-3(b)(2)) that provides highly compensated employees (including but not limited to executives) benefits that would be provided under the 401(k) plan but for the Tax Code limitations on the 401(k) plan, would all of the consultant's work constitute "additional services," or would only all or a portion of the work on the excess benefit plan constitute "additional services," and if the consultant's fees include a fixed component that covers both plans, how would that part of the fee be allocated if only a portion of the fee is disclosable. Also, companies with international affiliates often permit their non-U.S. affiliates to design and implement local non-U.S. compensation structures independently from the board compensation committee. The U.S. entity may not, as a practical matter, be aware of what consultant the non-U.S. entity chooses.

[25] We recognize that this ambiguity exists under the current rules, but believe that when an extensive and burdensome disclosure obligation is triggered, it is more important to enunciate precise standards. For example, the proposed text states that disclosure is triggered only if a consultant played a role in determining or recommending

standard may be too narrow, as it could involve an inquiry into whether a compensation consultant that was retained by and presents information to a compensation committee "plays a role" in the actual determination of executives' or directors' compensation or actually makes a recommendation, as opposed to only presenting alternatives or commenting on recommendations made by management.

If however the Commission adopts a standard that looks at the nature or effect of the consultant's advice or recommendations, instead of examining who a consultant is retained by and reports to, then we believe the proposed exclusion for consulting services that are limited to broad-based, non-discriminatory plans is appropriate. However, unless this exemption is also expanded to cover "excess plans" that provide the same level of benefits that would be provided under a broad-based plan, but for Tax Code limitations, the exemption may be of limited utility. In addition, to clarify that the "played a role" standard does not encompass services that are limited to data gathering or "number crunching," the Commission should exempt compensation consultant services that involve performing only actuarial or other calculations (that is, performing calculations to value benefits when the consultant has no role in structuring or recommending the form or amount of benefits) and compensation consultant services that involve producing survey data that either is not customized for a particular company or that is customized based on parameters that are not developed by the consultant (such as when a compensation committee or its consultant asks a third party consulting firm to provide information from its survey database for companies whose revenues or operations meet criteria specified by the compensation committee or its consultant).

**(e) Should we establish a disclosure threshold based on the amount of the fees for the non-executive compensation related services, such as above a certain dollar amount or a percentage of income or revenues? If so, how should the threshold be computed?**

While we have concerns regarding the cost and ability of implementing a fee disclosure standard, as addressed above, we agree that those issues may be mitigated, although not eliminated, if there is a disclosure threshold. An appropriate design for such a threshold should involve a *de minimis* dollar amount, such as $120,000, and a percentage threshold set at a level where the effect of such fees diminishes the possible appearance of a conflict of interests. Similar to standards for director independence, such a percentage test could be tied either to the amount of business the compensation consulting firm does with the company or the revenues of the compensation consulting firm.

**(f) Would disclosure of the individual fees paid for non-executive compensation related services provided by the compensation**

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the amount or form of executive **and** director compensation, but expect that the Commission does not intend to limit the required disclosure to consultants that only provide both types of services. On the other hand, we do not understand the circumstances referenced in the proposed regulatory text when it refers to situations in which a compensation consultant **or** its affiliate plays this role.

**consultants be more useful to investors than disclosure of the aggregate fees paid for non-compensation related service provided as proposed?**

As noted above, we do not believe that disclosure of fee data is as effective as other means at addressing whether there is more than an appearance of a conflict of interest, and we do not believe that more detailed fee data provides any greater insight into that issue. A requirement for more detailed fee data will exacerbate the questions and concerns we address above regarding when and how fees would be reported for services that touch upon, but are not limited to, the compensation of executive officers and/or directors.

**(g) Would disclosure about the fees paid to compensation consultants and their affiliates help highlight potential conflicts of interest on the part of these compensation consultants and their affiliates? Is fee disclosure necessary to achieve this goal, or would it be sufficient to require disclosure of the nature and extent of additional services provided by the compensation consultant and its affiliates? Should disclosure only be required for fees paid in connection with executive compensation related services?**

We believe that disclosure addressing the factors considered by a board compensation committee in evaluating its compensation consultant's objectivity will enable shareholders to assess the committee's basis for selecting its compensation consultant.

**(h) Should we make any special accommodations in the proposed amendments to Item 407(h) for smaller reporting companies? If so, what accommodations should be made and why?**

While we believe that the burden and expense of identifying, categorizing, tracking and disclosing fees paid to a compensation consulting firm and its affiliates will be significantly greater for larger companies, smaller reporting companies may particularly be unable to bear such additional costs and thus should be relieved from any fee-oriented disclosure rule adopted by the Commission. In our experience, many smaller reporting companies do not use outside compensation consulting firms because they can't afford it. They may use publicly available surveys, but in many cases they will, of necessity, rely primarily on data gathered by the management team. If a smaller reporting company does use an outside compensation consultant, it would rarely engage more than one firm. And that one firm may be performing a variety of tasks for a negotiated price, making it difficult, if not impossible, to allocate the cost among the tasks.

For these reasons, we do not think that smaller reporting companies should be subject to any additional disclosure regarding the use of and payments to compensation consultants.

**(i) Are there other categories of consultants or advisors whose activities on behalf of companies should be disclosed to shareholders? If so, what kind of disclosure would be appropriate?**

We believe that compensation committees should not be discouraged from utilizing other advisers through burdensome fee disclosure rules. While we believe that many compensation consultants take steps to avoid conflicts of interest and to preserve their objectivity, the professional and ethical standards to which attorneys are subject reduce the utility of any fee disclosures with respect to firms that serve as counsel to compensation committees.

## VI. Reporting Voting Results on Form 8-K

### A. General Comments

In general, we support the Commission's proposal to provide for more timely disclosure of the outcome of votes at shareholder meetings. The principal changes we suggest, as elaborated below, are to:

- clarify that the new disclosure requirement does not create a presumption that the disclosed information is material, in order to avoid unintended consequences under Regulation FD;
- modify the situations in which preliminary results must be reported, and in certain circumstances allow a company to instead disclose why it is not providing preliminary results;
- address the fact that there are situations other than contested elections where additional time may be needed before definitive results can be reported;
- permit companies to provide the new required disclosure by press release or website posting;
- simplify the wording of the disclosure requirement currently contained in Item 4 of Form 10-Q and Form 10-K; and
- extend the safe harbor provisions currently provided to certain Form 8-K items to cover the new required disclosure.

## B. Responses to Certain of the Commission's Inquiries.

### 1. To what extent would requiring the reporting of voting results on Form 8-K provide more timely information to investors and the markets?

Subject to the modifications we suggest below, we support the Commission's proposal to provide for more timely disclosure of the outcome of votes at shareholder meetings. We agree that shareholders and investors have a legitimate interest in knowing the final outcome of matters voted on at shareholder meetings in advance of when disclosure is currently required to be made.

We are concerned, however, that adding proposed Item 5.07 to Form 8-K may have unintended consequences under Regulation FD for companies that do not webcast their shareholder meetings, which includes a large number of smaller companies. Items required to be reported on Form 8-K are often viewed as being "presumptively material". If new Item 5.07 to Form 8-K were interpreted to mean that the results of every vote at every shareholder meeting are presumptively material, then companies that do not webcast their meetings in a manner compliant with Regulation FD might feel unable to announce the results of voting at their shareholder meetings (since those meetings do not constitute a broad, non-exclusionary distribution of the information to the public) unless making a simultaneous press release or filing a Form 8-K prior to the announcement. We do not believe this is an intended result of the proposal, or that it is desirable to put all public companies into the position where they must webcast their shareholder meetings (or simultaneously issue a press release or file a Form 8-K reporting the vote results at their shareholder meetings) in order to eliminate the possibility of violating Regulation FD.

Moreover, we do not believe the matters voted on at every meeting of shareholders are in fact "presumptively material." For example, a ratification of the selection of auditors already designated by an audit committee would, in the absence of any significant opposition, not be considered material. In addition, we believe that there continue to be situations where the outcome of an uncontested election of directors would not be considered material (including in the case of a controlled company where the majority shareholder's vote in favor of the management slate would be presumed).

Companies should continue to be free to assess whether they believe the outcome of votes at their shareholder meetings constitutes material nonpublic information for purposes of Regulation FD (and for other purposes). Any new requirement to make more timely disclosure of the outcome of votes should clearly state that the new requirement does not create a presumption that the information is material.

**2. Are there any possible adverse consequences to requiring the disclosure of preliminary voting results in a contested election when the outcome is not final? For example, could the preliminary disclosure affect the final outcome?**

We believe there could be adverse consequences of requiring the disclosure of preliminary voting results if:

- Disclosure is required to be made at a time when the opportunity remains open for additional votes to be cast, because the reporting of preliminary results could influence later voting. To minimize this risk, we recommend that the term "end of the meeting" be explicitly defined and that such definition provide that a meeting has not ended until the voting process has ended and no additional votes will be accepted. If a legal challenge has been asserted to the voting process or the closing of the vote prior to when the new required disclosure is provided, the "end of the meeting" should not be deemed to have occurred until such matter is finally resolved, either by court order, settlement or withdrawal of the challenge.

- Disclosure is required to be made even though the preliminary numbers are so inconclusive that disclosure of the information could be misleading to investors. This would be the case if the company has a reasonable basis for believing that there is a more than remote chance the final results will differ from the reported preliminary results. To minimize this risk, we believe that, where definitive numbers are not available, companies should only be obligated to report (within a specified number of days after the end of the meeting) either the preliminary numbers or an explanation of why preliminary numbers are not being reported.

**3. Should the filing period under Form 8-K for the reporting of voting results be longer than four business days?**

We believe that, in general, a four business-day reporting period would be workable, so long as the term "end of the meeting" is defined as we suggest above and companies have the ability, as we suggest above, to omit preliminary results in situations where there is a more than remote chance the final results will differ from the reported preliminary results. In addition, as we note below, certain circumstances may arise that would result in a delay with respect to the filing and, in these cases, we believe that companies should be afforded the opportunity to defer the filing until the circumstances are resolved.

**4. Should we require the reporting of preliminary voting results?**

We believe that any requirement to report preliminary results needs to address the concerns we identify above.

**5. Are there unique difficulties or significant costs in finalizing voting results at smaller reporting companies that would warrant a longer filing period for those companies?**

Many smaller reporting companies do not request that a representative from their transfer agent attend their annual meetings of shareholders to serve as Inspector of Elections and help tally votes at the meeting in order to cut costs. Such companies typically appoint a non-director officer (often the chief financial officer) to serve as the Inspector of Elections for the meeting. Although the transfer agent can provide the Inspector of Elections with the status of the voting tallies immediately prior to the actual meeting, any votes that are cast in person by shareholders or proxy holders at the meeting must be factored into the count. It may take a number of days, or even a week or more, for the Inspector of Elections to coordinate with transfer agent after the meeting to determine whether shareholders who voted at the meeting in person or through a proxy holder were, in fact, shareholders entitled to vote at the meeting, how many shares were held of record on the record date by shareholders who voted at the meeting in person or through a proxy holder, and whether shares voted at the meeting were being voted for the first time or represented a revocation of a previously submitted proxy and change in vote. Except in highly unusual cases, it would be counter-productive for the officer who is serving as Inspector of Elections to ignore his or her normal day-to-day duties at the company in order to complete the final vote tally and file a Form 8-K within four business days.

For these reasons, we suggest that smaller reporting companies either be exempted from reporting voting results on a Form 8-K (and continue to report them on the Form 10-Q for the quarter during which the meeting was held) or that the time within which they must file a Form 8-K be lengthened to at least ten business days.

**6. What factors should we consider in deciding whether to make the filing period longer? Are there situations other than contested elections that might warrant a longer filing period?**

We believe that, in some instances, companies may experience difficulties in determining final vote counts. For example, there may be technical difficulties (including computer or communications outages) that prevent the prompt tabulation of results, or review of voting results may disclose inconsistencies or irregularities calling into question the integrity of information reported earlier. Questions with respect to the entitlement of particular shareholders to vote in an election may also arise, which could call into question the final voting results. Included in this category are situations involving over-voting, where more than one shareholder may have cast votes with respect to certain shares. Issues of this sort are also possible because of the extent to which shares are held in street name, and the determination as to proper voting may require not just inquiry of a company’s transfer agent, but also inquiry to, and coordination with, The Depository Trust Company. As a result of these potential issues, we believe that any final rule should permit companies to determine to defer the disclosure of final results with respect to any matter being voted on, as these issues may affect matters other than a contested election of directors.

**7. Are there alternative methods to disseminate this information to investors sooner or within a similar time frame that would be more effective or appropriate?**

In our view, it would be appropriate for the Commission to permit companies, in lieu of filing a Form 8-K to announce voting results, to announce such results by issuing a press release or by a website posting. Similar to the approach taken for reporting waivers and amendments of its code of conduct/ethics, any company that wishes to use an alternative to Form 8-K should state in its proxy statement how it intends to provide the results of shareholder votes. Nothing, of course, would prevent a company that elects to do so from filing a Form 8-K.

**8. We are moving and accelerating the disclosure requirement but not proposing any other revisions to the disclosures that are currently required by Item 4 of Form 10-Q and Form 10-K. Are there any changes to the requirements as to what should be disclosed that we should consider? For instance, since disclosure must be provided for all matters voted on, including a separate tabulation for the election of each director, should we eliminate the portion of Instruction 4 that provides when paragraph (b) need not be answered?**

In our view, the existing Form 10-Q and Form 10-K disclosure items can, and should, be significantly simplified. In particular:

- Existing Instruction 3 can be deleted if Item (a) is modified to itself provide that it only applies when a meeting is involved.
- Items (b) and (c) can be collapsed into a single item that simply calls for quantitative disclosure of the results of each item voted on. We believe the current requirement in (b) to name each director whose term of office as a director continued after the meeting is unnecessary. The consolidation of Items (b) and (c) would make it possible to delete the first sentence of Instruction 4 and all of Instruction 5.
- In light of the short period of time between the end of the meeting and the Form 8-K filing deadline, Instruction 7 is probably of limited practical significance and could be deleted for the sake of simplification.

We also believe that companies should be required to clearly indicate which matters were approved by shareholders and which were not. The Commission may also want to consider whether to require voting results to be presented in a tabular format.

**9. Would the proposal impose any significant costs or difficulties on companies? If so, what type and amount of costs? Are these short-term or one-time costs to adjust a company's reporting procedures, or long-term ongoing costs?**

Except as described above, we are not aware of any significant costs or difficulties that would be imposed on companies if the proposal is adopted.

**10. Would the proposal create any special burdens for smaller reporting companies? If so, would scaled disclosure be appropriate for these companies and how should it be accomplished? Alternatively, should these requirements be phased in for smaller reporting companies?**

As discussed above, we believe that the proposed Form 8-K disclosure of voting results may be more burdensome for smaller reporting companies than for a larger company that arranges for its transfer agent to attend its shareholder meetings and to serve as its inspector of elections. We believe that the best way to ease this burden would be either to exempt smaller reporting companies from proposed Item 5.07 of Form 8-K or to lengthen the filing deadline to at least ten business days after the meeting.

**11. Would the accuracy of disclosure of voting results be affected as a result of a Form 8-K filing requirement?**

Please see our response to question 2 above.

**12. Should we amend Section 13a-11(c) to include proposed Item 5.07 in the list of Items with respect to which the failure to file a report on Form 8-K will not be deemed to be a violation of Section 10(b) or Rule 10b-5? Similarly, should we amend General Instruction I.A.3(b) of Form S-3 to add proposed Item 5.07 to the corresponding list of Items on Form 8-K with respect to which a company's failure timely to file the Form 8-K will not result in the loss of S-3 eligibility? Why or why not?**

We believe it would be appropriate to include Item 5.07 in the safe harbor provided to other specified items of Form 8-K. We view the Commission's effort to accelerate the disclosure of voting results as being very helpful to investors. However, we are mindful that the proposal does not impose a new requirement; it merely accelerates an existing requirement. In addition, the nature of the required disclosure is different from other Form 8-K items because there are situations where the required information will not be material. We believe that the failure of a company to timely file an Item 5.07 Form 8-K should not be deemed to be a *per se* antifraud violation, nor should it disqualify a company from the ability to use Form S-3. In our view, the Commission has adequate enforcement tools available to remedy breaches of the securities laws without recourse to remedies that may have a draconian effect and harm the very shareholders the Commission is committed to protect.

## VII. Proxy Solicitation Process

### A. Exchange Act Rule 14a-2(b)(1) -- Introductory Text

We respectfully urge the Commission not to amend the introductory text of Rule 14a-2(b)(1) to codify the Staff's informal position that a "form of revocation" does not include an unmarked copy of management's proxy card that a soliciting shareholder asks be returned directly to management. In our view, providing a form of proxy in this context is the functional equivalent of a proxy solicitation – that of a "form of revocation." Accordingly, such activities should be regulated as a proxy solicitation under the federal proxy rules. This is true because in most situations the intent of the soliciting party is to induce shareholders who have previously submitted a proxy in favor of management, to revoke such proxy and to vote against management. In "just vote no" solicitations, buttressed by an unmarked copy of management's card, "it is possible that these non-management persons will succeed more often in defeating management proposals."[26]

We concur with the view of the U.S. Court of Appeals for the Second Circuit in its 2004 MONY decision, that "[t]he plain text of [current] Rule 14a-2(b)(1) shows that the easy revocation of proxies was [a] … potential abuse" of the liberalized proxy regulatory scheme adopted by the Commission in 1992.[27] Before opening the door to such "potential abuse", we respectfully submit that the Commission should give careful consideration to whether the proposed amendment might have the unintended effect of altering -- or even conflicting with -- the plain meaning of "form of revocation" under governing state laws relating to proxies. In this regard we note that the Commission appears tacitly to recognize this possibility, in seeking comment on whether the proposed amendment would "raise concerns under applicable state law."[28] For example, in MONY, the Second Circuit observed, in considering applicable state law, that in Delaware a solicitation in opposition to a merger involving dissemination of a duplicate copy of management's proxy card is really nothing more than a solicitation of revocations of previously cast proxy votes -- rejecting the District Court's acceptance that in these circumstances there might be other purposes for disseminating management's card without management's proxy statement.[29]

At a minimum, the Commission should evaluate the costs and benefits of the proposal within the broader framework of the comprehensive reassessment of the federal proxy rules now underway at the Commission.[30] Shareholders and companies alike would be much better served, in the final analysis, by a more holistic examination by the Commission of the use of the Rule 14a-2(b)(1) exemption over the past five years in light of developments such as the proliferation of share borrowing, equity-based, cash-settled derivatives and other synthetic

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[26] See the Proposing Release at footnote 144.

[27] See *MONY Group v. Highfields Capital Mgmt.*, 368 F.3d 138 at 146 (2d Cir. 2004)

[28] See the Proposing Release at page 51.

[29] See *MONY Group*, 368 F.3d 138, at 140.

[30] See Commissioner Elisse B. Walter, *"SEC Rulemaking—'Advancing the Law' to Protect Investors"*, delivered to the 48th Annual Corporate Counsel Institute, Northwestern University School of Law (Chicago, Ill, Oct. 2, 2009) available at http://www.sec.gov/news/speech/2009/spch100209ebw.htm

financial instruments that have arguably given rise to "empty voting" and other practices now under Commission scrutiny with a view toward possible rulemaking under the beneficial ownership reporting requirements of Exchange Act Sections 13(d) and (g) and Regulation 13D/G thereunder,[31] the imminent changes to the broker-dealer discretionary voting standard in NYSE Rule 452 and the evolution of state corporate law reforms fostering, through private ordering, enhanced shareholder power within the corporation via majority voting in director elections and proxy access for shareholder nominations of directors.

If the Commission nevertheless decides to proceed with the proposed amendment, we recommend that any soliciting person who intends to rely on the Rule 14a-2(b)(1) exemption to circulate copies of management's unmarked proxy card be required to file a written notice with the Commission that identifies the person or persons relying on the exemption, discloses any relationships with the company and its affiliates, or with any other person engaged or intending to engage in an exempt or non-exempt solicitation of the company's shareholders under the federal proxy rules, and indicates how much stock the soliciting person owns and whether such person(s) intends to hold its stock through the date of the meeting (or effective date of action by consent). This exemptive treatment should not be available unless the card is returned to management; in other words, it should not be used to invite shareholders to return management's card to the soliciting person invoking Rule 14a-2(b)(1). Nor should its use be permitted in a contested setting to circulate a dissident's unmarked proxy card.

### B. Exchange Act Rule 14a-2(b)(1)(ix)

We fully support the Commission's proposal to clarify the circumstances under which a shareholder would be deemed to hold a "substantial interest" in the matter and thus precluded from relying on the Rule 14a-2(b)(1) exemption. We agree that the "substantial interest" as currently referenced in the rule should not be limited to security holdings. Rather, a person could very well have an interest that would give rise to a benefit from the solicitation that is not shared pro rata with all other holders of the same class of securities. We do not believe it should make any difference whether the person is or is not currently a security holder of the class being solicited. In light the complexity of today's financial markets where parties are able to structure derivative transactions in such a way that they can lock-in a specific economic interest in a company's securities without the attendant beneficial ownership interests, we believe the test should not turn on whether the person is or is not a holder of shares in the subject company.[32]

### C. Exchange Act Rule 14a-4(d)(4)

While we generally support the Commission's proposal (in concept) that would allow shareholders to "round out" their short slates with nominees from either the company or another shareholder – we believe the ability to do so should be subject to certain limited conditions. In short, we are concerned – as the Commission has correctly acknowledged -- that ""[i]t is possible

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[31] See *CSX Corporation ("CSX") v. The Children's Investment Fund Management (UK) LLP ("TCI"), et al.* (08 Civ. 2764 (LAK) (SDNY June 11, 2008).
[32] See *In the Matter of Perry Corp.*, Release No. 34-60351, IA-2907 (July 21, 2009).

that permitting a soliciting person to round out its short slate with other persons' nominees instead of or in addition to a registrant's nominees … could lead to a change in the majority of the board" – thus triggering "poison pill" rights plans and other change in control provisions (including those commonly found in loan and employment agreements). In addition, it is highly likely that allowing shareholders to round out their short slates with nominees of other shareholders will only encourage shareholders to run more short slates – thereby creating a potential "pile-on" effect that will only "increase[s] the likelihood of displacing company nominees and potentially increasing each shareholder's negotiating power with management." Furthermore, we don't believe the prohibitions against Section 13(d) "group" activity contained in the proposal will be sufficient to prevent situations where the truth is not known until months or years after a shareholder meeting is held and directors are elected. One need look no further than the recent litigation surrounding the recent election contest at CSX to know that the issue of whether a 13(d) group has or has not been formed can take months if not years to litigate.

As such, we believe it is critical for the Commission to impose clear and objective conditions to reliance on the proposed rule to minimize the inherent risks associated with potential Section 13(d) groups forming and tacitly agreeing to team up against issuers thereby giving rise to protracted litigation and triggering change of control provisions along the way. In this regard, we believe the Commission should limit the availability of a soliciting person to "mix-and-match" nominees in a short slate situation so that:

- a soliciting party may only round out its short slate with nominees (up to the total number of director positions that are up for a vote) if both the company's and the other soliciting party's nominees are included in this "remainder."[33]

- the other soliciting party or parties must only be seeking a minority representation on the board – *i.e.,* not running a complete competing slate – and any other person soliciting in support of a short slate should be required to use its proxy authority to vote for at least the number of management nominees that would constitute a majority.

- any person seeking to rely on the rule should certify that they are not acting as a member of a group or otherwise acting in concert with any other party to engage in a solicitation of proxies – *i.e.* no Section 13(d) "group" activity and no soliciting activity that would make one a "participant" in the competing short slate (or slates) solicitation.[34]

Lastly, we do not believe the Commission should "amend Rule 14a-4(d)(4) so the exception it provides … extends to non-management persons who do not have their own nominees for whom to solicit support but seek authority to vote for nominees named in the registrant's or other persons' proxy statement." Any person seeking to rely on the rule should

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[33] This specific condition was set forth in the no-action letter to Eastbourne Capital, L.L.C. (March 30, 2009).
[34] Such representations, if required, would make it much easier for the Commission and the private sector to enforce compliance with the new rule.

have a real stake in the solicitation, or at least one that shareholders can appreciate and understand – *i.e.*, a competing set of nominees for less than a full majority of the board.

**D. Exchange Act Rule 14a-4(e)**

The Commission proposes to amend this rule to clarify that when a proxy statement or form of proxy provides that shares represented by proxy will be voted "subject to reasonable specified conditions," such conditions must be "objectively determinable" in order to enable a shareholder to make an informed decision with respect to granting proxy authority. We agree that any such conditions should be objectively determinable. However, we believe the Commission should outline some examples of what would not be objectively determinable, or provide examples of the types of conditions that would not satisfy this condition.

**E. Exchange Act Rule 14a-12(a)(1)(i)**

Lastly, the Commission proposes to clarify that a person who engages in soliciting activity *before* security holders are furnished with a proxy statement must disclose certain specified participant information in a filing no later than the time the first soliciting communication is made. We agree with the Commission that it should not be sufficient for a soliciting person to provide the participant information in a document that is filed at a later time, but instead that information should be filed when the first soliciting communication occurs.

## VIII. Other Requests for Comment

At this time, we have no specific further comments regarding proxy disclosures, other than to suggest that in proposing any new disclosure obligations the Commission consider the themes referred to in the "Overview" section of this letter.

## IX. Impact on Small Business Issuers

Our views with respect to the impact of the proposals on small business issuers are set forth in the foregoing sections of this letter.

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The Committee appreciates the opportunity to comment on the Proposals 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/ Jeffrey W. Rubin
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