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September 14, 2009

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

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

Dear Ms. Murphy:

We are submitting this letter in response to the solicitation by the Securities and Exchange Commission (the “Commission”) for comments on the proposed amendments to the compensation and corporate governance disclosure and proxy rules under the Exchange Act. We appreciate the opportunity to comment on the Proposal and support the Commission’s efforts to improve compensation and corporate governance disclosure. We provide below comments to the proposed disclosure relating to compensation programs and risk, equity awards, compensation consultants and director and nominee qualifications and the proposed exemption from the proxy rules of solicitations that include a proxy card.

1. The discussion and analysis of the registrant’s overall compensation policies and practices as they relate to risk and risk management should be required only if the risks arising from those policies and practices are reasonably likely to have a material effect on the registrant.

The Proposal would amend Item 402 of Regulation S-K to add a new requirement to the Compensation Discussion and Analysis (the “CD&A”) to discuss and analyze situations in which a registrant’s overall compensation policies and practices may “create incentives that can affect the company’s risk and management of that risk.” This requirement would apply “[t]o the extent that risks arising from the registrant’s compensation policies and overall actual compensation practices for employees generally may have a material effect on the registrant” (emphasis added). We believe that the final rule should require such discussion and analysis only if such risks are reasonably likely to have a material effect on the registrant. Basing the disclosure standard on whether the risks are “reasonably likely” would give registrants more certainty and provide investors with a meaningful discussion and
analysis, whereas the proposed “may” standard is vague and could be interpreted to capture much more
than the material information that the Commission is seeking.

When the Commission previously considered proposed disclosure in Management’s Discussion and Analysis (“MD&A”) of off-balance sheet arrangements and aggregate contractual limitations, it initially proposed a disclosure standard based on whether the information “may” be material but ultimately adopted a “reasonably likely” disclosure threshold for the final rule under Item 303(a)(4) of Regulation S-K. As the Commission explained in the preamble to the final rule:

[W]e are adopting the “reasonably likely” disclosure threshold that we currently apply to other portions of MD&A disclosure. We believe that the “reasonably likely” threshold best promotes the utility of the disclosure requirements by reducing the possibility that investors will be overwhelmed by voluminous disclosure of insignificant and possibly unnecessarily speculative information . . . . [W]e conclude that the “reasonably likely” standard focuses on the information most important to an understanding of a registrant’s off-balance sheet arrangements and their material effects on the registrant’s financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources. In addition, we are mindful of the potential difficulty that registrants would have faced in attempting to comply with the “remote” disclosure threshold set forth in the [proposed rule under Item 303(a)(4) of Regulation S-K]. We also believe that our use of a consistent disclosure threshold throughout MD&A will preclude the potential confusion that could result from disparate thresholds.¹

As the Commission noted above, the “reasonably likely” disclosure threshold is applied also to other key aspects of MD&A disclosure.² Adopting a “reasonably likely” disclosure threshold for the new CD&A requirement to discuss and analyze a registrant’s overall compensation policies and practices that give rise to risks that materially effect the registrant also would be consistent with the Commission’s stated view that the disclosure that registrants provide in their CD&As should parallel the disclosure that they provide in their MD&As: “the primary focus of the Compensation Discussion and Analysis should be ‘[m]uch like the overview that [the Commission has] encouraged companies to provide with their Management’s Discussion and Analysis of Financial Condition and Results of Operations.”³

Although the development of the CD&A is more recent, registrants have a long history of understanding and complying with MD&A requirements. The Proposal is analogous to MD&A in its intent that registrants disclose material and not all, or even most, information and recognizes that the disclosure will vary depending on the particular registrant and its compensation programs. Establishing a disclosure threshold already familiar to registrants in other contexts, including in analyzing and disclosing financial, liquidity and other risks, will better fulfill the Proposal’s objectives.

2. The aggregate grant date fair value of equity awards that are granted for services rendered in the prior year should be reported for such prior year.

The Proposal would amend Item 402 of Regulation S-K to require reporting in the Summary Compensation Table and Director Compensation Table the aggregate grant date fair value of equity

² For example, Item 303(a)(1) of Regulation S-K requires a registrant to “[i]dentify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant’s liquidity increasing or decreasing in any material way.” (emphasis added)
³ Staff Observations in the Review of Executive Compensation Disclosure (October 9, 2007), quoting the preamble to the final rule under Item 303(a)(4) of Regulation S-K.
awards for the year of grant, rather than the amount recognized each year for financial statement reporting purposes for any outstanding awards. We agree with the Commission that this change will result in more meaningful disclosure than the current rule because, in making voting and investment decisions, investors will be able to consider compensation decisions made during the year, which are reflected in the aggregate grant date fair value, and not the amount recognized for financial statement purposes.

Consistent with the concept of evaluating compensation that is related to the performance year being disclosed, the final rule should provide that the Summary Compensation Table report the aggregate grant date fair value of equity awards granted for services in the relevant fiscal year, even if the awards are granted after fiscal year-end. Many companies in a diverse range of industries, including insurance, healthcare, financial services and energy, currently grant equity awards for services rendered in the prior year. Such companies may wait until the following year to grant equity awards because compensation committees, in evaluating executive performance, wish to have the full information that is available only after the year ends, including whether relevant performance criteria have been attained. This change in the final rule would result in greater comparability and improved disclosure because the value of the awards would be reported for the year with respect to which the compensation decision was made.

Moreover, reporting in the year of grant the grant date fair value of an equity award granted for services rendered in the prior year may be misleading. For example, a registrant that performs well in 2009 could grant an equity award to a named executive officer in early 2010 as a bonus for performance rendered in 2009. Under the Proposal, the grant would not be disclosed until 2011. If the registrant’s performance declined in 2010, stockholders may believe that the award was intended to reward the officer for poor performance in 2010, rather than for good performance in 2009. The tendency of this disclosure to confuse is evidenced by media reports that often inaccurately state that such awards are granted for the year of poor performance, further increasing stockholder misunderstanding. Because stockholders may not understand the existing rule, many companies that grant equity awards for services rendered in the prior year provide a supplemental table that reports these equity awards for the prior year. Our recommendation would eliminate the need for such a supplemental table, making the CD&A shorter and clearer.

The existing rule appropriately requires that the amount of a cash bonus be reported for the year with respect to which the bonus was earned, even if paid in the following year. Requiring the grant date fair value of an equity award granted for services rendered in the relevant year to be reported for such year would treat similarly all annual bonuses, regardless of whether they are paid in the form of cash or equity and regardless of whether they are paid in the year with respect to which the performance was rendered or in the following year.

Instruction 1 to Items 402(c)(2)(iii) and (iv) of Regulation S-K provides that if a registrant omits from the Summary Compensation Table the amount of a cash bonus because it is not calculable through the latest practicable date prior to the proxy filing, the registrant must include a footnote to the table disclosing this and providing the date that the amount of the bonus is expected to be determined. The registrant then must disclose a recalculated total compensation amount (i.e., revised to reflect the amount of the cash bonus) in a filing under Item 5.02(f) of Form 8-K when the amount of the bonus becomes calculable. An analogous approach could also be used to disclose an equity award that is to be granted for services rendered in the prior year but that has not yet been granted as of the most recent practicable date prior to the proxy filing. That is, the registrant would be required to include a footnote to the Summary Compensation Table disclosing that the equity award has not yet been granted and providing the date that the award is expected to be granted and, when the award is granted, disclose in a filing under Item 5.02(f) of Form 8-K a recalculated total compensation amount (i.e., revised to reflect the grant date fair value of the award).
3. **The FAS 123R values of performance-based equity awards should be reported in the Summary Compensation Table.**

The Commission asks whether disregarding the likelihood of achieving performance conditions in reporting performance-based equity awards would discourage registrants from granting such awards. We believe that it would and suggest, therefore, that registrants instead be required to report the FAS 123R values of the awards, which would reflect the likelihood of achieving the relevant performance goals.

4. **Compensation consultant disclosure.**

   a. **The requirement to provide disclosure of non-compensation-related services provided by compensation consultants should not be effective until the 2011 proxy season.**

The Proposal would amend Item 407(e) of Regulation S-K to require a registrant to provide specified disclosure if a consultant is engaged to provide services that are used to determine or recommend the amount or form of compensation paid to executives and directors and such consultant or its affiliates also provide other services to the registrant or its affiliates. The Commission states in the preamble to the Proposal that the Proposal’s amendments, including this amendment, would be effective for the 2010 proxy season.

To meet the requirements of this amendment, a registrant must complete a number of tasks prior to filing its 2010 proxy materials. First, the registrant must identify:

- each consultant engaged by the registrant to provide services that are used to determine or recommend the amount or form of compensation paid to the registrant’s executives and directors;
- each affiliate of such consultant and of the registrant; and
- any additional services provided by such consultant or any of its affiliates to the registrant or any of its affiliates.

If the registrant determines that any such additional services have been provided, it must determine and prepare disclosure regarding the following:

- the nature and extent of such additional services;
- the aggregate fees paid for such additional services;
- the aggregate fees paid for services used to determine or recommend the amount or form of executive and director compensation;
- whether management decided, or otherwise participated in the decision, to engage such consultant and its affiliates for such additional services; and
- whether the registrant’s board of directors or compensation committee approved such additional services.

Registrants with December fiscal year-ends in particular may not be able to complete these tasks in a thorough and thoughtful manner in time to provide such additional disclosure in their 2010 proxy materials.
We therefore believe that the Proposal’s requirement to provide such disclosure should not be effective until the 2011 proxy season.

b. The additional disclosure relating to compensation consultant services should be required only if the aggregate fees for such services exceed $120,000.

The Commission requests comment as to whether the Proposal’s requirement to provide disclosure with respect to services unrelated to executive compensation should be subject to a threshold based on the aggregate amount of fees for such unrelated services. We believe that it should.

In the preamble to the Proposal, the Commission explains that the additional disclosure is intended to illuminate for investors potential conflicts of interest that may arise from a compensation consultant’s desire to retain revenue streams unrelated to executive compensation services. That is, a consultant may feel pressure to recommend an executive compensation package that does not alienate the executives and directors who will decide whether to continue to engage the consultant and its affiliates to provide such additional services.

We believe that if the aggregate fees for such additional services are insignificant, the conflict is diminished significantly and that therefore disclosure with respect to such additional services should be subject to a threshold. Item 404(a) of Regulation S-K currently requires disclosure regarding certain transactions between a registrant and a related person (e.g., a director or executive officer of the registrant) if the amount involved exceeds $120,000. The Proposal’s requirement to provide additional compensation consultant disclosure should also be subject to a $120,000 threshold, applied in the aggregate with respect to all additional services provided by the consultant and its affiliates.

c. The requirement to provide additional disclosure relating to services provided by compensation consultants should exclude industry benchmarking surveys.

A registrant may elect to purchase from a consultant a compensation benchmarking survey that provides general information regarding the forms and amounts of compensation typically paid to executive officers and directors within a particular industry. The compensation committee may find such information useful in determining the forms and amounts of compensation to pay to its executive officers and directors.

Because consultants do not tailor their industry benchmarking surveys to particular clients, such surveys do not raise the potential conflicts of interest that the Proposal’s additional disclosure are intended to address. The final rule therefore should not require disclosure regarding the use of such surveys. For the same reason, the proceeds from the sales of such surveys should not be aggregated with the fees for services unrelated to executive compensation for purposes of determining whether the $120,000 disclosure threshold that we recommend above is met.

5. The requirement to provide disclosure regarding the qualifications of directors and nominees should not require a discussion as to service on board committees.

We recommend that the proposed amendments to Item 401 of Regulation S-K regarding disclosure as to the qualifications of directors and nominees not require a discussion as to service on board committees. Directors are not recruited to serve on specific committees but rather to enhance the overall composition of the board. The proposed requirement to provide a description about the specific experience, qualifications, attributes and skills that make the individual qualified to serve as a director, including information about the individual’s risk assessment skills, particular areas of expertise or other relevant qualifications, is already sufficient to balance the Commission’s objectives of providing
stockholders with more meaningful disclosure to make informed voting decisions and companies sufficient flexibility to disclose material information about the individual.

Other than financial literacy or expertise for audit committee members that already will be disclosed as part of a director’s general qualifications, neither the Commission nor any listing exchange has indicated that directors must have any special expertise to serve on board committees, and we do not believe that the Commission now intends to suggest otherwise. Boards recruit and evaluate members who complement and strengthen the skills of their existing members, rather than selecting for particular skill sets or subject matter expertise. It is unclear in fact what particular background or expertise makes a director more suitable for the nominating and governance committee, for example, rather than the compensation committee. The proposed disclosure requirement also could discourage the preference of some boards to rotate directors among different committee positions, which they believe allows directors to gain a thorough perspective of the company.

6. Solicitations that include a proxy card should not be exempt from the proxy rules.

Exchange Act Rule 14a-2(b)(1) exempts from most proxy rule requirements solicitations by disinterested shareholders and non-management parties who do not seek proxy authority and who do not furnish, among other things, a “form of revocation.” The Proposal would amend the introductory text of Rule 14a-2(b)(1) to clarify that providing an unmarked copy of management’s proxy card to be returned directly to management would not constitute a “form of revocation” rendering the exemption unavailable even though the return of the card would revoke the shareholder’s prior vote. We believe this change would result in potential abuse of the exemption by enabling an insurgent to effectively conduct a proxy contest (in the form of a “vote no” campaign) without complying with the disclosure and other requirements set forth in the proxy rules — in direct contravention of the Commission’s stated objectives when it first adopted the rule in 1992.

When the Commission adopted the exemption, its stated objective was to foster “free discussion, debate and learning among shareholders” by deregulating constraints on certain communications by disinterested persons. At the same time, the Commission recognized the “potential for abuse both by insurgents and by management” and thus limited the exemption to solicitations by persons who (1) do not seek proxy authority and (2) would not be receiving a non-pro rata benefit (compared to other shareholders) from a successful solicitation.

Since the adoption of the exemption, shareholders have employed the rule to conduct sophisticated “vote no” campaigns involving press releases, public speeches, newspaper ads, meetings with ISS and investors and the dissemination of targeted letters to shareholders through Broadridge (formerly ADP) without complying with the Commission’s filing and other proxy solicitation requirements. These solicitations arguably were permissible as they met the rule’s requirements and did not, among other things, include a proxy card or otherwise seek proxy authority.

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5 Id. at p. 27.

6 Specifically, Rule 14a-2(b)(1) limits the exemption to a person who does not “seek directly or indirectly, either on its own or another’s behalf, the power to act as proxy for a security holder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization . . . .”

7 One such solicitation that attempted to include an unmarked copy of management’s proxy card was enjoined by the Second Circuit in Mony Group, Inc. v. Highfields Capital Mgmt. L.P., 368 F.3d 138 (May 13, 2004). Reversing a lower court decision, the Second Circuit recognized that the “easy revocation of proxies” was one potential form of abuse that the Commission attempted to prevent by adopting the rule’s specific language and held that in the context of a merger vote — which required the approval of a majority of all of the company’s shareholders — the duplicate proxy operated as a “form of
A solicitation that includes a duplicate of management’s unmarked proxy card, in the context of a "vote no" campaign, would, in effect, be seeking proxy authority. While the insurgent would not actually be soliciting votes through its own separate proxy cards, it would be furnishing the shareholder with a ready means to cast an effective vote against management’s proposal without complying with the SEC’s proxy solicitation rules. Meanwhile, solicitations made by persons conducting a traditional proxy contest (and additional solicitations made by the targeted company to counteract the campaign) would have to be filed.  

It is this type of abuse that we believe the Commission intended to prevent when it originally adopted the exempt solicitation rules in 1992. We therefore recommend that the Commission not adopt the proposed change to the introductory text of Rule 14a-2(b)(1).

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We appreciate the opportunity to participate in this process and would be pleased to discuss our comments or any questions the Commission may have with respect to this letter. Any questions about this letter may be directed to David Caplan, Ning Chiu or Kyoko Takahashi Lin at 212-450-4000.

Very truly yours,

DAVIS POLK & WARDWELL LLP

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8 We disagree with the Commission’s statement in footnote 144 of the proposing release that “it seems unlikely that many solicited shareholders would vote differently merely because they have more opportunities to vote as a non-management soliciting person suggests.” On the contrary, we believe that a shareholder would be more likely to vote on a proposal if given the means to do so. Currently, a shareholder receiving soliciting materials from an insurgent waging a “vote no” campaign must first locate the management proxy or wait for the management proxy to be delivered by the company in order to cast a vote. The proxy would be accompanied by required disclosures, giving the shareholder the ability to cast an informed vote. Under the Proposal, a shareholder that receives an insurgent’s soliciting materials could easily be persuaded to return a ballot based on extremely limited information regarding the proponent and without the proxy disclosure and other recommendations of management.