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Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Subpart 400 of Regulation S-K Disclosure requirements relating to management, certain security holder and corporate governance matters (File No. S7-18-16)

CFA Institute[1] appreciates the opportunity to offer comments to the U.S. Securities and Exchange Commission ("SEC" or the "Commission") on certain disclosure requirements in Regulation S-K relating to management, certain security holders, and corporate governance matters contained in Subpart 400. CFA Institute represents the views of those investment professionals who are its members before standard setters, regulatory authorities, and legislative bodies worldwide about issues affecting the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues affecting the efficiency, integrity and accountability of global financial markets.

We believe strong corporate governance is key to the successful functioning of any corporation as corporate governance is the system of internal controls and procedures by which individual companies are managed. Corporate governance provides a framework that defines the rights, roles, and responsibilities of various groups—management, board, controlling shareowners, and minority or non-controlling shareowners—within an organization.

At its core, corporate governance is the arrangement of checks, balances, and incentives a company uses to minimize and manage the conflicting interests between insiders and external shareowners. Its purpose is to prevent insiders such as management and significant owners, from expropriating the cash flows and assets of one or more other groups. It is therefore important that investors have all of the information they need about the corporate governance policies and systems of the companies in which they invest.

Summary

The Commission is requesting public comment on certain disclosure requirements in Regulation S-K relating to management, certain security holders, and corporate governance matters

[1] CFA Institute is a global, not-for-profit professional association of more than 141,000 investment analysts, advisers, portfolio managers, and other investment professionals in 157 countries, of whom nearly 135,500 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 147 member societies in 73 countries and territories.

contained in Subpart 400. This request is part of an initiative by the Division of Corporation Finance to review the disclosure requirements in Regulation S-K to consider ways to improve them for the benefit of investors and registrants. Comments received in response to this request for comment will also inform the Commission's study on Regulation S-K, which is required by Section 72003 of the Fixing America's Surface Transportation Act ("FAST Act"). We submitted our comments related to the broader Regulation S-K study on 5 October 2016.

Subpart 400 of Regulation S-K requires certain disclosures about a registrant's management, certain security holders, and corporate governance matters. The items covered are as follows.

- Item 401 requires certain disclosures about a registrant's directors, executive officers, promoters and control persons.
- Item 402 requires disclosure of all plan and non-plan compensation awarded to, earned by, or paid to a registrant's named executive officers and directors.
- Item 403 requires a description of the security ownership of certain beneficial owners and management.
- Item 404 requires a description of certain transactions with related persons, promoters and certain control persons.
- Item 405 requires a registrant to identify certain persons who, as disclosed in certain forms, failed to file reports required by Section 16(a) of the Securities Exchange Act on a timely basis during the most recent fiscal year or prior fiscal years.
- Item 406 requires disclosures about whether the registrant has adopted a code of ethics that applies to certain of its executive officers, or persons performing similar functions, and, if it has not adopted such a code of ethics, an explanation why it has not done so.
- Item 407 requires certain corporate governance disclosures about director independence, board meetings, various board committees (e.g., nominating, audit and compensation committees) and any process for shareholder communications.

We will address each of these items in our comments below

Item 401 - Registrant's directors, executive officers, promoters and control persons

Among its many roles, a board of directors is responsible for establishing accountability for company management and assuring reasonable internal controls through independent third-party reviews of the company.

Shareowners need to understand the experience and expertise of board members and the systems the board has adopted to adequately oversee management, and issuers should provide essential data to enable them to do so. This information should be disclosed prominently in an issuer's proxy statement and elsewhere. We encourage companies to avoid boilerplate language and tell their stories in a brief but still-thorough narrative that communicates all of the information that investors need.

We do not believe that the current amount of data investors receive from boards is a problem. At the same time, we want to ensure that the quality of the information issuers provide is of the highest quality and that investors get the information they need in a timely manner. It is difficult for the SEC (or any regulatory body) to prescribe all of the information investors need across industry, sector, company size and company lifecycle.

We therefore ask that the SEC encourage companies to move away from boilerplate language by offering less-prescriptive guidelines around these disclosures. Likewise, it should require that information be disclosed without prescribing the type of language through which it must be disclosed.

Item 402 – Executive Compensation plans.

Investors are well served when they know about the methods and rationale for executive and director compensation. Compensation provides powerful incentives to management, staff and directors, and certain perquisites may dilute shareowners' holdings or have other direct and substantial effects on their interests.

The increase in absolute levels of executive compensation in recent decades has focused investors on the strategies used to pay senior executives. Companies need to supply understandable disclosures relating to the level and structure of executive pay to help investors understand the connections between performance and pay. Creating a link between executive compensation and fundamental performance will better align executive and shareowner interests.

We believe that compensation for senior company executives should be explicitly linked to long-term financial and operating performance. Creating a link between compensation and fundamental performance will better serve investors' interests.

Non-binding votes on executive compensation packages, or "say-on-pay" votes, give shareowners opportunities to send messages to their boards about the compensation awarded. Where implemented, such policies have led to more communication between shareowners and companies' boards about appropriate compensation strategies and the amounts paid to senior executives.

The Compensation Discussion & Analysis ("CD&A") is a company's primary engagement tool with investors and, therefore, needs to tell a company's compensation story in a concise manner that investors will understand. The CD&A is also used to comply with US SEC requirements, but thinking of it first and foremost as a compliance document misses the opportunity to communicate effectively with investors. For a more thorough review of best practices in compensation design and disclosure, we invite the SEC to review the CD&A Template[2] recently published by CFA Institute with the help of issuers, investors and others with expertise in executive compensation.

The template was designed to improve understanding, serve as a global model for improved investor communications about this important issue, and elevate compensation disclosure beyond an exercise in legal compliance. The CD&A has been used more successfully as a communications tool in recent years due to increased engagement between issuers and investors around executive compensation issues. More companies are now telling their compensation

[2] http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2015.n4.1

stories in non-boilerplate language that are appreciated by investors as best practices have begun to emerge that are being copied by more and more issuers.

We caution the SEC to not make the CD&A and executive compensation any more burdensome, as issuers and shareowners in recent years have worked together to greatly improve the process. In fact, we encourage a much more focused and concise disclosure of compensation as outlined in our template. This will both improve and significantly reduce the amount of disclosure required.

Item 403 - Description of the security ownership of certain beneficial owners and management

Investors benefit from the information currently disclosed concerning beneficial ownership of management, board members and other insiders. Investors and issuers both find information about investors' ownership in a company informative, though there is an ongoing debate as to whether the current reporting framework is adequate and of best service to investors.

Currently any investor or group that acquires 5% of a company's shares must report such an ownership stake within ten days. Some recommended changing the standard from the current 10 days to one or two days. Those who would like to shorten the time period for such reporting argue for a required disclosure the day following an investor reaching the 5% threshold, in addition to a "cooling off" period of two days in which the investor could not acquire additional ownership of a company's shares. These parties assert that hedge funds or other activist investors will pass the 5% threshold and continue accumulating shares through actual buying of shares or derivative positions for up to 10 days before they have to make any disclosure. This 10-day disclosure window, therefore, allows corporate raiders with a short-termist mindset to accumulate outsized positions for 10 days before anyone knows what is going on.

Those in favor of shortening the reporting period make the following points:

- The current definition of beneficial ownership and the 10-day reporting lag after the Schedule 13D ownership threshold is crossed facilitates market manipulation and abusive tactics.
- There is no good reason that purchasers of significant ownership stakes in public companies should be permitted to hide their actions.
- Transparency, fairness, and equality of information in our financial markets have never been higher.
- Since its adoption as part of the Williams Act in 1968, the purpose of beneficial ownership has been to alert the markets to potential changes in corporate control.
- Impediments to immediate reporting no longer exist, and the 10-day window is an anachronism.

Those in favor of keeping the reporting period as it is ask the SEC to provide evidence of abuse of the system before changing such a rule. They argue that shortening of the disclosure window is designed as a corporate entrenchment mechanism, noting that many issuers would quickly adopt or activate already-existing poison pills once the 5% threshold were breeched in order to head off more meaningful accumulation of shares by activist investors. Such action could effectively allow issuers to set ceilings to the number of shares activists may acquire.

Those in favor of the status quo make the following points:

- Current disclosure requirements should be tightened only if the SEC reaches a policy conclusion, after weighting relevant costs and benefits, that doing so would benefit investors.
- Given existing impediments to the market for corporate control, outside blockholder activities, are especially important for reducing agency costs and managerial slack in public companies.
- The drafters of the Williams Act recognized that outside blockholders "should not be discouraged, since they often serve a useful purpose by providing a check on entrenched but inefficient management."
- Having a blockholder representative on the compensation committee is correlated with a stronger CEO pay-performance links, stronger links between performance and CEO turnover, and lower CEO pay.
- State rules now permit the adoption of low-trigger poison pills that prevent blockholders from acquiring even blocks that are widely recognized not to convey control.

We are wary of adopting a rule change that may be used to further entrench management, and would need to see concrete evidence from multiple independent sources that the current reporting structure is being abused before it is changed. We recommend the that the SEC conduct a comprehensive study of the implications of any changes to this rule before proposing such a change.

If the 10-day rule were to be shortened, we could see more instances like we saw in the Sotheby's case a few years ago where corporate defenses were targeted at one type of investor. We feel that it is better for companies to build relationships with investors through engagement, so when an unwanted raider comes calling a company will have investors willing to take its side in the contest of ideas put forth by said raider.

Item 404 – Related-Party Transactions

A related-party transaction takes place when a deal is arranged among at least two entities, and where one has control over the other or where the parties come under the same control of another. The nature and prevalence of such transactions generally vary according to different ownership structures and the investor protection mechanisms which govern them vary by jurisdiction.

We encourage the SEC to set appropriate thresholds for determining when related-party transactions require board and/or shareowner approval. Such thresholds should not merely be a dollar amount, but should be made with the consideration of whether a "*quid pro quo*" relationship has been established. Such related-party transactions need not be monetary in nature (a favor done, a promise for future consideration,) but would nonetheless be necessary to disclose to investors.

Investors need assurances that there are systems in place that monitor the legitimacy of major transactions pursued by company management. We encourage the SEC to ensure that such disclosures are thorough enough that approval of independent parties on the board are required of such transactions. Board approval makes management more accountable, and shareowner approval makes management, as well as the board, accountable.

Item 405 – Identify certain persons who failed to file on a timely basis.

CFA Institute has not comments on this section at this time.

Item 406 – Disclosure about a code of ethics.

Most every public registrant now has a code of ethics prominently displayed on its website or in its corporate governance documents. However, most of these documents contain similar boilerplate language and do not make much of a difference when employees or management of some issuers have engaged in questionable behavior. That said, investors do find such documents useful when they speak to investors about the policies and procedures a company has in place to promote an ethical corporate environment.

Item 407 – Certain corporate governance disclosures.

Corporate governance disclosures about boards, their independence and committees in US listed companies are usually of good quality as the standards set by the SEC and the exchanges require significant disclosures about boards, their committees and governance policies. We therefore do not believe that any new corporate governance disclosures are needed. We only ask that the nature of these disclosures is high-quality in terms of clarity and transparency without the use of non-boiler language.

There are certain other issues however where we think SEC rules or guidance would be helpful to investors.

Proxy Access

In addition to disclosures under 407 (c)(2)(ix), we believe it could be beneficial to add a provision 407(c) (2)(x) requiring more detailed disclosures on the registrant's policy regarding proxy access. This could include whether they have a policy for considering director candidates recommended by shareowners and, if so, describe the material elements of the policy.

Separately, as we first stated in our recent paper, "Proxy Access in the United States: Revisiting the Proposed SEC Rule[3]," we encourage the SEC to revisit the proxy access rule. The last few years have shown that more issuers and investors are reaching accommodation on proxy access

[3] http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2014.n9.1

that closely follows the SEC's proposed rule that allows shareholders who have held 3 percent of a company's shares for 3 years.

Communication with shareholders - engagement

One of the biggest corporate governance adjustments in the past five years has been the increase in engagement between the issuer's Board of Directors and investors. We'd encourage consideration of a new section 407(c) (2) (xi) that describes the registrant's view and approach to such interactions.

Conclusion

Given the importance of corporate governance to a company's ethical and operational structure, we believe it is important that investors have the information they need about the corporate governance policies and systems of the companies in which they invest. The items within Subpart 400 of Regulation S-K do a good job of providing the relevant governance information that investors need to make informed decisions. Should you have any questions about our positions, please do not hesitate to contact James Allen, CFA at [redacted] or [redacted] or Matt Orsagh at [redacted] or [redacted]

Sincerely,

/s/ James Allen, CFA

Head, Capital Markets Policy
CFA Institute

/s/ Matt Orsagh, CFA

Director, Capital Markets Policy
CFA Institute