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October 30, 2012

Sent Electronically

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

Re: SR-NYSE-2012-49; Exchange Act
Release No. 68011 (Oct. 9, 2012)

Dear Ms. Murphy:

Please accept this comment on the proposed rule change submitted by New York Stock Exchange LLC that would modify the listing rules for compensation committees in order to bring them into compliance with Rule 10C-1 under the Securities Exchange Act of 1934 ("NYSE Proposal").

The Proposal falls short of the requirements imposed under Section 10C of the Exchange Act and Rule 10C-1 in two significant respects. First, the Proposal does not, as the statute mandates, require boards to consider as a relevant factor the compensation paid to the directors for their service on the board. Second, the Proposal does not adequately require boards to take into account personal or business relationships between directors and executive officers in determining director independence.

I. Compensation for Service on the Board

Section 10C mandates that the listing rules of the exchanges specify the "relevant factors" that must be considered in determining the independence of directors serving on the compensation committee. The factors must include "the source of compensation of a member of the board of directors of an issuer, including any consulting, advisory, or other compensatory fee paid by the issuer to such member of the board of directors".[1]

[1] 15 U.S.C. § 78j-3(a)(3)(A).

Fees paid for service on the board are a form of compensation. *See* Item 402 of Regulation S-K, 17 CFR § 229.402 (providing for disclosure of fees in a table labeled "director compensation). As a result, the broad language of Section 10C requires that compensation paid to directors for service on the board be treated as a relevant factor in determining director independence.

The NYSE Proposal, however, specifically rejected consideration of these payments. In doing so, the Proposal did not rely on the language of Section 10C or the legislative history. Instead, the NYSE Proposal asserted that "[n]on-executive directors devote considerable time to the affairs of the companies on whose boards they sit and eligible candidates would be difficult to find if board and committee service were unpaid in nature." In addition, the Proposal reasoned that "the Exchange does not believe that an analysis of the board compensation of individual directors is a meaningful consideration in determining their independence for purposes of compensation committee service." Neither rational, however, justifies the failure to include director compensation as a relevant factor.

The NYSE Proposal apparently reads the language in Section 10C and Section 10A, the provision dealing with audit committees, as identical. The two provisions are, however, very different. Section 10A *prohibits* a director from serving on the audit committee if he or she accepts "any consulting, advisory, or other compensatory fee from the issuer."[2] Expressed as a prohibition, the "compensatory fee" language did not extend to compensation paid for service on the board. To have done so would have limited membership on the audit committee to unpaid directors.

Early versions of Dodd-Frank sought to use the same approach with respect to the compensation committee. The House version proposed to *prohibit* directors who received "any consulting, advisory, or other compensatory fee from the issuer."[3] As in Section 10A, the language was not intended to extend to compensation paid for service on the board.[4]

The final legislation, however, rejected the House approach. Rather than *prohibit* directors from serving on the compensation committee, Section 10C merely required the board to consider "relevant factors" in determining independence. The weight and significance of each factor was left to the discretion of the board.

This broader, more flexible approach allowed Congress to expand the types of compensation that had to be considered in determining director independence. Rather than limit consideration to "any consulting, advisory, or other compensatory fee," the approach taken in Section 10A and proposed in the House, Congress broadened the language to include consideration of "the source of compensation of a member of the board of directors of an issuer".

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[2] 15 U.S.C. § 78j-1.

[3] *See* 156 Cong. Rec. H9214 (July 31, 2009).

[4] *See* 156 Cong. Rec. H9214 (July 31, 2009) ("In order to be considered to be independent for purposes of this subsection, a member of a compensation committee of an issuer may not, *other than in his or her capacity as a member of the compensation committee, the board of directors, or any other board committee* accept any consulting, advisory, or other compensatory fee from the issuer.") (emphasis added).

The NYSE Proposal largely reads the phrase out of the statute. The phrase, however, has obvious and significant meaning. The language on its face ("source of compensation") applies to all types of compensation, including compensation paid by any person (including non-issuers) and compensation paid to directors for service on the board.[5] Thus, the NYSE's view on the importance of the information is irrelevant. The explicit mandate of the statute is that boards consider all compensation, including fees paid for service on the board.

Nor is the NYSE's reasoning for excluding director compensation convincing. Requiring consideration of fees does not mean that directors on the compensation committee will need to go "unpaid," as the NYSE Proposal claims. The particular weight given fees is a matter for the board. In most cases, fees will not impair independence. To the extent that they do, however, the board can alter the compensation amount or formula in a manner that alleviates any concerns. In no case must directors be "unpaid" for their service on the compensation committee.

The NYSE's belief that board compensation is not a "meaningful consideration" in determining independence is likewise mistaken. Independence can be lost as a result of excessive fees[6] or fees paid as a *quid pro quo*.[7] Likewise the method used to determine fees can impair independence. Compensation committee members with excessive discretion over the terms of director compensation may lose their independence.[8] Indeed, the NYSE itself has noted that the payment of non-customary fees can raise concerns about director independence.[9]

The Commission should require that the NYSE Proposal give Section 10C its plain meaning and specify that boards must, in determining director independence, consider as a relevant factor the amount paid to directors for service on the board.

II. Personal or Business Relationships

Section 10C specifies two relevant factors that must be considered in determining director independence. Congress, however, also provided that the exchanges "shall consider" other relevant factors. In promulgating Rule 10C-1, the Commission "emphasize[d] that it is important for exchanges to consider other ties between a listed issuer and a director" and suggested that they "might conclude that personal or business relationships between members of

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[5] The proposing release arguably recognizes that the provision applied to non-issuer compensation. *See* Exchange Act Release No. 68011 (Oct. 9, 2012) ("When considering the sources of a director's compensation in determining his independence for purposes of compensation committee service, commentary to proposed Section 303A.02(a)(ii) provides that the board should consider whether the director receives compensation *from any person or entity* that would impair his ability to make independent judgments about the listed company's executive compensation.") (emphasis added).

[6] *See Orman v. Cullman*, 794 A.2d 5, 29 n. 62 (Del. Ch. 2002) (leaving open the possibility that independence can be lost where "the fees were shown to exceed materially what is commonly understood and accepted to be a usual and customary director's fee.").

[7] *See In re Nat'l Auto Credit S'Holders Litig.*, 2003 Del. Ch. LEXIS 5 (Del. Ch. Jan. 10, 2003).

[8] *See Seinfeld v. Slager*, 2012 Del. Ch. LEXIS 139 (Del. Ch. June 29, 2012).

[9] The impairment of independence as a result of excessive fees has been recognized by the NYSE, *see* 303A.09 Corporate Governance Guidelines ("The board should be aware that questions as to directors' independence may be raised when directors' fees and emoluments exceed what is customary.").

the compensation committee and the listed issuer's executive officers should be addressed in the definition of independence."[10]

The NYSE Proposal would require consideration of "all factors specifically relevant to determining whether a director has a relationship to the listed company which is material to that director's ability to be independent from management in connection with the duties of a compensation committee member . . ." The NYSE has vaguely noted that this language includes consideration of relationships between management and directors.[11] The Proposal, however, is not sufficient to ensure that boards weigh personal or business relationships between executive officers and directors in determining director independence.

First, as with the current version of Section 303A.02(a), the proposed listing rule only references relationships with "the listed company." This language can be read to suggest that the board need only consider relationships between directors and the issuer and not between directors and senior management. This is not an academic matter. Confusion on this matter has existed within the issuer community.[12]

Second, the omission of any explicit reference to business or personal relationships with management is inconsistent with the approach otherwise taken in the Proposal. With respect to the consideration of affiliate status, boards would be required to consider whether a relationship placed directors under the "control of the listed company or its senior management" or "create[d] a direct relationship between the director and members of senior management." With respect to compensation consultants, compensation committees would be required to consider "[a]ny business or personal relationship of the compensation consultant, legal counsel, other adviser or the person employing the adviser with an executive officer of the issuer."[13] The explicit reference to relationships with management creates a negative inference, that in circumstances where there is no explicit reference, these relationships need not be considered.

Finally, the legislative history makes it absolutely clear that Congress, in adopting Section 10C, expected personal or business relationships to be explicitly considered in determining director independence. Section 10C was designed to "strengthen" the independence of compensation committees "from the executives they are rewarding or punishing."[14] Said another way, Congress expected the board to exclude from the committee the "pals and golfing

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[10] Exchange Act Release No. 67220 (June 20, 2012).

[11] *See* Exchange Act Release No. 68011 (Oct. 9, 2012) ("The Exchange's existing director independence requirements require the board to consider relationships between the director and any member of management in making its affirmative independence determinations.").

[12] At least one NYSE traded company interpreted similar language to mean that relationships between directors and officers "generally are not relevant to the independence tests under the New York Stock Exchange rules because they do not create a material relationship between a director and the company." *See* http://www.theracetothebottom.org/independent-directors/2010/6/1/the-nyse-and-the-problems-of-director-independence-the-plain.html

[13] Rule 10C-1(b)(4)(vi), 17 CFR 240.10C-1(b)(4)(vi).

[14] Summary, Restoring American Financial Stability Act of 2010, 156 Cong. Rec. 4329 (May 28, 2010), *available at* http://banking.senate.gov/public/_files/RAFSASummary_UpdateMay28revised.pdf ("Standards for listing on an exchange will require that compensation committees include only independent directors and have authority to hire compensation consultants in order to strengthen their independence from the executives they are rewarding or punishing.").

buddies" of management.[15]

The SEC should, therefore, compel changes in the NYSE Proposal to resolve the ambiguities in the existing language and expressly require that boards must consider "business or personal relationships" between directors and executive officers (or senior management) in determining the independence of those serving on the compensation committee.

III. Conclusion

The Commission should require changes to the NYSE Proposal to meet these requirements. Alternatively, the Commission should immediately initiate rulemaking procedures and alter the NYSE listing rules to bring them into conformity with Section 10C.

With regards,

Yours truly,

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[15] *See* 156 Cong. Rec. S2705-06 (April 27, 2010) (statement by Senator Whitehouse) (noting that requirement for independent directors was designed to "make sure, in particular, that the compensation committees of the board that sets executive pay aren't just the pals and the golfing buddies of the people whose multimillion-dollar pay and bonuses they are approving; to make sure it is independent directors who are on the compensation committee and making those decisions."); *see also* 156 Cong Rec S 2611 (April 26, 2010) (Statement by Senator Whitehouse) (legislation "would ensure that the compensation committees of boards of directors, the ones who are figuring out what the CEOs should be paid, are composed of directors who are independent, who are not tied to the management: No more having your pals and golfing buddies decide how much you should be paid.").