PM&P | Pearl Meyer & Partners
Comprehensive Compensation®

September 15, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 20549-1090

Dear Ms. Murphy,

Pearl Meyer & Partners (PM&P) is pleased to submit comments to the Securities Exchange Commission on its proposed release seeking to amend rules concerning disclosure of executive and director pay and governance. At the outset, we once again commend the Commission in its efforts toward greater transparency with regard to executive and director pay, as well as its willingness to revisit essential issues that have emerged since the inception of the enhanced rules several years ago. While we acknowledge the need for updates in light of changing economic times, we urge the Commission to consider balancing its goals of transparency and accountability with practical implications to public filers and the potential benefits to investors.

This letter is intended to provide feedback that represents our views, as well as those expressed by many of our clients, with respect to the proposed rules. We also take into consideration the practical implications and potential burdens that would be placed on public filers by certain requirements.

By way of background, Pearl Meyer & Partners is one of the nation's leading compensation consulting firms, serving Board Compensation Committees as independent advisors and assisting companies in the creation and implementation of innovative, performance-oriented compensation programs to attract, retain, motivate and appropriately reward executives, employees and Board Directors. As independent advisors, we help Boards and Committees establish and maintain sound governance practices, particularly as this relates to executive and director pay decision-making. Since its founding in 1989, PM&P's compensation professionals have advised hundreds of organizations in virtually every industry, ranging from Fortune 500 companies to smaller private firms and not-for-profit organizations.

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We appreciate the opportunity to comment and share our views. We note that PM&P is submitting this commentary on its own behalf, and not on behalf of any specific client. Please contact us at 212-407-9517 if you have any questions regarding our comments.

Sincerely,

David N. Swinford
President and CEO
Pearl Meyer & Partners
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Attachment

Pearl Meyer & Partners
Comprehensive Compensation®

Additional Proposed Risk Disclosure

The Commission's proposal expands disclosure of compensation in the proxy to cover "how the company's overall compensation policies for employees create incentives that can affect the company's risk and management of that risk." This expansion was prompted, at least in part, by the current market turmoil at a number of large financial institutions. At the outset, we want to be clear that compensation plans–and resulting executive compensation payouts–were not the primary cause of the collapse of the financial markets, though clearly, compensation plans can contribute to excessive and/or unnecessary risk-taking, particularly among financial institutions. Rather, company business strategies–particularly those related to the mortgage derivative markets–were the impetus for the risk-taking that jeopardized the financial health of many companies. Therefore, we believe the significance of analyzing risks inherent in core business strategies far exceeds analysis of risk inherent in compensation plans in and of themselves. At the opposite extreme, we believe that pushing companies toward compensation programs with zero risk, e.g., 100% base salary and/or defined benefit pensions, runs counter to the pay-for-performance linkage that investors seek. Thus, we accept that some level of risk tied to performance is quite appropriate for compensation programs, even if investors cannot be assured that there will not be a negative outcome.

Conceptually, we agree that expanded disclosure regarding risk and compensation plans should benefit shareholders and investors by increasing the transparency of a company's risk management practices, thereby potentially leading to more widespread and effective risk oversight. However, as proposed, the rule lacks specificity and fails to provide sufficient guidance as to what must be disclosed for most companies (particularly non-financial institutions). The Compensation Discussion and Analysis (CD&A) in many proxy statements is already lengthy and, in many cases, so voluminous that important disclosures are even less transparent than prior to the rule changes. We believe that in an attempt to meet the expanded requirements about risk, CD&As will become even longer without necessarily providing additional useful information to investors. We believe proxy statements can provide investors with more useful and less voluminous disclosures if the rules: (i) provide an additional threshold for "materiality;" (ii) provide a different set of examples as to what could be disclosed if the materiality threshold is met; and (iii) narrow the scope of disclosure to executive levels only.

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Provide Additional Threshold for "Materiality"

The Commission's proposal would require companies to disclose compensation policies or actual compensation practices that may have a "material effect" on the company, stating that materiality is a facts and circumstances test. While the Commission does provide examples of what may rise to the level of material, these scenarios focus on situations that are largely specific to the financial services industry. Without further guidance about what constitutes "materiality" (particularly for those companies outside of the financial services sector), CD&As will become even more voluminous with unnecessary verbiage as companies exercise good faith to ensure compliance with the requirement. As a threshold matter, we believe that "materiality" can only exist where the compensation plan is ***likely*** to promote executive behavior that could have a significant and damaging impact on the overall operations and financial footing of the company as a whole.

Provide Different Illustrative Examples of How Risk Could be Disclosed

The Commission has offered a set of illustrative examples of items that may be discussed if the materiality threshold is met. We believe that the examples are not specific enough to help companies draft succinct and transparent disclosure. In our practice, we have suggested a methodology for companies to follow in assessing risk in their compensation programs. Of course, analysis of risk is unique to each company–the size of the company, the industry, etc. will cause the analysis to vary widely. However, we believe that the following questions would better serve as appropriate examples of items that might be discussed if the materiality threshold is met:

- What risks can threaten the company's value?
- How do incentive plan metrics reflect the company's business strategy?
- Are the leverage and mix of incentive compensation elements appropriate?
- Is the full range of potential upside/downside payouts under the company's incentive plans appropriate?
- Do plans have protections/controls to avoid excessive risk-taking and excessive payouts? If not, are there sufficient protections/controls external to the incentive plans (e.g., stringent investment guidelines/processes)?
- Do plans focus executives on long-term performance that aligns with shareholder interests? In particular:
  - Are there stock ownership and retention requirements?
  - Are there instances in which the company would be obligated to pay excessive severance (e.g., significantly in excess of 3x base plus bonus) if the executive is terminated for poor performance?
  - Are there sufficient controls to ensure that payouts are aligned with risk horizons? For example:

- Are incentive awards above a certain level paid in restricted stock or unvested deferred compensation?
- Does the company require a hold back of a portion of annual incentive awards pending sustained performance results?

- How does performance compare to industry/peers, and do the payouts align with market practice for the level of performance achieved?
- How does the company address payments of awards based on performance that is later materially restated negatively?
- Do the plans allow the Committee to exercise discretion?

Our methodology and supporting information are summarized in a recent webinar we conducted in association with the National Association of Corporate Directors. The presentation is attached as **Exhibit A**.

Limit Risk Disclosure Requirements to Executive Population

We believe the proposed risk disclosure should only apply to executives whose actions could have a significant negative effect on a company. Employees below the executive level (particularly outside of the financial services sector), generally have a limited impact on risk and company viability unless they have clear authority to make significant decisions on behalf of the company. Requiring disclosure of lower level employee plans will lead to longer CD&As that contain information not helpful to investors. As an alternative, a disclosure that the company has a process in place to review material risks presented by compensation plans covering the non-executive population, and that such process has been reviewed by the Committee, should be sufficient to encourage companies and Boards to establish processes to evaluate and control for risk in non-executive compensation plans.

Other Elements that Should Be Considered

We believe a thorough risk assessment should apply to all compensation components as well as the program as a whole–not just annual incentives. While pay elements like base salary do not pose risk, they are important in balancing incentive pay elements that carry more risk by definition. Thus, the mix of at-risk vs. non-risk pay elements should be considered. Quite a few companies have included a supplemental table demonstrating the target (if applicable) and/or actual pay mix between pay elements with different levels of risk. We have found such charts to be extremely helpful in laying out compensation programs for investor review.

Affirmative Statement if No Risk Disclosure Presented

If no risk disclosure related to compensation plans is presented in the proxy, companies should be required to affirmatively state in their CD&A that a determination has been made that the risks arising from broader compensation

policies are not reasonably expected to have a material negative effect on the company.

Risk Disclosure for Smaller Reporting Companies Should be Required

We believe that smaller reporting companies may carry greater business risk, including risk that executive actions could have a significant negative effect on the company's survival. In our experience with initial public offerings, the compensation programs and related governance processes for nascent companies tend to be less well defined than at larger, more established companies. Simpler or more discretionary incentive plans do not necessarily involve less compensation risk. As such, we believe that investors would benefit from risk disclosure from smaller reporting companies.

Reporting Equity Awards at Fair Value in the Summary Compensation Table (SCT) and Director Compensation Table (DCT)

The FAS 123R values now required in the SCT and DCT are largely ignored by compensation consultants, our clients and investors when they are seeking to understand total annual pay for named executive officers (NEOs). To understand annual compensation on a comparable basis, most practitioners instead turn to the last column of the Grants of Plan-Based Awards Table (GPBAT), which currently contains grant date fair values. Thus, the Commission's proposed change makes sense from a compensation analysis standpoint. However, such a change does not come without its own set of complexities. Reporting FAS 123R accruals for equity-based compensation grants is a clear and defined process, as rules exist and are maintained by a regulatory body. While reporting grant date fair values per FAS 123R (rather than FAS 123R accruals) would be more meaningful for investors, a different set of ambiguities would need to be addressed. Our comments below address some of these vagaries.

SCT Should Include Only Equity Grants Made During the Current Year

We believe the Commission should maintain its current rule that provides for reporting of equity grants in the year in which the grant is made (rather than the year to which the associated performance may relate). Equity grants should be consistent with the FAS 123R determination of grant date. To do otherwise would result in inconsistent and possibly manipulated reporting. Companies that regularly make equity grants in the current year based on prior year performance may still clarify that timing difference in the CD&A and in footnotes to the SCT.

Maintain Disclosure of Individual Grant Date Values in the GPBAT

Maintaining disclosure of individual grants in the GPBAT would further the Commission's objectives to promote transparency and accountability. Aggregating

the grants in the SCT, without grant-by-grant breakouts, would impede investor ability to track awards and their impact on compensation levels over time. Grant-by-grant disclosure enables investors to determine whether pay and performance are actually linked, allowing a clearer picture of pay-for-performance.

Multi-Year Grants

The Commission has requested comment as to prevalence and treatment of multi-year (or "mega") grants. In our experience as compensation consultants, multi-year grants are not a typical practice. When they do occur, the disclosure surrounding the grant generally clarifies that it was intended to cover more than a single year. As such, we do not believe that adjustments should be made in the SCT to account for, or discount, multi-year grants. Footnote disclosure, along with discussion in the CD&A, should be adequate to explain why the grant date fair value of the award is more than expected for an annual grant. Alternatively, any special multi-year grants could be reported in a separate column (similar to the 'Bonus' column), but still included in the Total Compensation figure. We do not believe exceptions should be made if the multi-year grant results in variability in the determination of NEOs. If the grant-date value is large enough that it results in unwanted variability in NEOs, the company can remedy the situation by not making the multi-year grant. If the company makes the grant, it may voluntarily disclose the compensation information for the "sixth NEO" who would otherwise have been included in the SCT to alleviate some of the year-over-year variability of NEOs. Providing too many exceptions to the grant date value methodology will eviscerate consistency and standardization of the rule.

Valuation of Performance-Based Awards in SCT Should Be at Target, Not Maximum

We believe that requiring reporting at maximum will have the unintended consequence of discouraging Compensation Committees from adopting performance-based programs. The Commission's current position on reporting of fair value in column (l) of the GPBAT requires that such awards be reported at maximum–a position consistent with FAS 123R. However, CD&I 120.05 has the effect of overstating fair values of performance-based equity programs. This was clearly problematic in the GPBAT, but becomes exponentially troubling when it is factored into the SCT and used to determine NEOs and Total Compensation.

Performance-based equity plans are intended to incentivize executives to achieve the goals of the program, which are typically expected to be at "target." Grantees of such awards are not expected to achieve maximum levels, except in the case of exceptional and unusual performance levels. The degree of difficulty in achieving target is already a required disclosure in the CD&A. Requiring reporting at maximum would overstate the company's original intentions with respect to the expected level of compensation payouts.

Even if reporting of equity of awards is at target in the SCT, investors will still have access to the value of potential maximum awards in the GPBAT, so shareholders will not lose any information. Investors can still see the number of shares or dollar awards authorized under threshold, target and maximum levels and compute the total value at maximum.

Do Not Use Multiple Tables to Report Summary Compensation

We agree with the Commission's message that there is no perfect way to disclose compensation in the tables. While the Commission and many practitioners have suggested that perhaps multiple tables can display compensation in a variety of ways, we believe that simpler is better. All of the information needed to assess annual compensation is already required by the current rules, as well as the proposed rules (assuming column (l) of the GPBAT is not eliminated). So long as the CD&A and accompanying narratives explain the vehicles and potential and actual payouts, investors should be able to piece together, without undue effort, an accurate picture of compensation plans for executives. Companies concerned with the clarity of their required disclosures can always provide supplemental tables or narrative to explain their intent or result.

We do not support revising the SCT to report the annual change in the value of awards, as per a rulemaking petition received by the Commission. We believe that such a table would be confusing and not consistent with the manner in which Compensation Committees make the decision to grant equity awards. Those companies wishing to provide such information may include a supplemental table.

The Outstanding Equity Awards at Fiscal Year End Table would, however, benefit from a column showing the intrinsic value of outstanding stock options. While the intrinsic value can be calculated from the information already included in the table, it is not convenient and quite a few filers have added a supplemental column or table to show the intrinsic option values, particularly as many grants are deeply underwater at this time.

Continue to Report Salary and Annual Incentives in the "Salary" and "NEIP" (or "Bonus") Columns, Regardless of their Form of Payment

There are many forms of 'hybrid' compensation that are both annual and long-term in nature. However, if the Compensation Committee originally considered the compensation to be Salary or Bonus or "Annual NEIP" (annual incentive), then it would be clearer to report it as such. If the form of payment would otherwise qualify as equity compensation, explanation of the form of payment should be provided in the CD&A and the Footnotes to the tables.

Require Re-Computation of Prior Years during a Two-Year Transitional Reporting Period

We agree that companies should provide re-computation of prior years in the 2009 SCT and in the 2010 SCT (the 2011 SCT would have three years under the new rules). Since the grant date fair values of equity awards were provided in the GPBAT in prior years, it would not be difficult for registrants to provide this re-computation and allow investors to easily consider year-over-year changes in compensation. We also agree that companies should not be required to include different NEOs for any preceding years based on the recomputed figures.

Additional Compensation Consultant Disclosure

The Commission's proposal would require additional disclosure in cases in which the Board's compensation consultant advises on executive/director compensation and has also provided "Additional" services. We agree that additional disclosure that promotes consultant independence and freedom from conflicts is a good policy. However, further specificity is needed to define "Additional" services so as not to impede the Committee's ability to use its compensation consultant for matters clearly ancillary to and directly related to executive or director compensation services.

We believe that the objective should be to highlight situations where the management could influence the Compensation Committee's compensation advisor because that advisor is being retained directly by management to provide significant "Additional" services. There would not be any potential for conflict, and therefore no need for additional disclosures, if the Compensation Committee's compensation advisor were to provide:

- "Additional" services to the Board or another Committee (e.g., governance advice, director education, evaluation of Committee or director effectiveness, etc.); or
- "Additional" services at the request and direction of the Compensation Committee (e.g., design of equity and annual bonus plans where executives and non-executives are participants, executive compensation surveys, compensation risk assessments, etc.); or
- An insignificant level of "Additional" services to management, with the knowledge and approval of the Compensation Committee.

Since these types of services do not represent conflicts of interest, we believe that the Commission should not consider them as "Additional" services in determining whether heightened disclosures, including disclosure of fees, are warranted. At the end of the day, the critical issue is whether the compensation consultant's ethics might be compromised by performing these activities. We believe many ancillary services do not compromise ethics and therefore should not trigger additional disclosure requirements.

The Commission specifically notes that services such as benefits administration, human resources consulting and actuarial services would fall in the "Additional" service bucket and trigger additional disclosures. It also points out that fees generated by these services may be more significant than fees earned by the consultants for their executive services–a fact that clearly signals either a real or perceived conflict. However, we posit that there are certain services (other than administration, human resources consulting and actuarial services) that are routinely performed by independent compensation consultants at the request of the Compensation Committee as part of the overall executive or director compensation review. We also think in certain scenarios (other than administration, human resources consulting and actuarial services), the chances of a real or perceived conflict are minimal. We address these issues and others by answering the questions posed by the Commission with respect to this element of enhanced disclosure, as follows:

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 (or the Compensation Committee)?

Yes. The disclosure of "Additional" services provided by the consultant, and the relationship between the fees earned by these firms for executive and director compensation services relative to "Additional" non-executive and director compensation services, will help investors assess potential conflicts of interest. However, we do not believe it would help investors better understand the role of the compensation consultant or the decisions made by the Board. Nonetheless, investors should be aware of the total financial arrangement between the company and the consultant; and Compensation Committees should mitigate the risk of potential conflict by either minimizing "Additional" services or selecting an equally capable, independent consulting firm for their executive and director compensation needs.

We see this as analogous to the current disclosure of fees paid to the company's external auditor for audit and non-audit services, which seems to have worked well. As in the case of auditor fees, there are unique and unusual circumstances where it would be economical and more effective to have a single advisor working with the Board, the Compensation Committee, and the company's management on executive and non-executive matters, such as advisory services related to mergers and acquisitions activity or initial public offerings. In these instances, the timeframe for such blended services is limited and it is important to have continuity between executive and non-executive compensation actions or programs.

Would the disclosure of additional consulting services and related fees adversely affect the ability of a company to receive executive and director compensation consulting or non-executive and director compensation consulting related services?

No. There is no shortage of consulting firms with highly capable individuals providing compensation advisory services. This provides companies with a relatively easy solution of selecting one firm for its executive and director compensation consulting needs and another firm for its broader human resources consulting needs (while still allowing for competition on both relationships). Furthermore, the focus on independence over the last five years has resulted in many senior practitioners joining or forming single line-of-business compensation consulting organizations specifically to provide Compensation Committees with a truly independent choice for their executive and director compensation needs.

Are there additional disclosures regarding potential conflicts of interest of compensation consultants that should be required?

Yes. Given the need and desire for independence, there has been a proliferation of sole proprietorship and/or consulting firms with a very small number of senior advisors and clients. Another potential source of conflict may arise when a single client represents a significant portion of a firm's total revenue. Additional disclosure of such information would help investors assess potential conflicts of interests. For example, a disclosure such as the following could be required if a client represents more than 10% of a firm's annual revenue: *"The fees paid to the company's executive and director compensation consultant represented more than 10% of the compensation consulting firm's total revenue for the year."*

Should we also require disclosure of currently contemplated services? Should we require disclosure for the prior three years?

No and Yes. We do not believe disclosure of currently contemplated services should be required, because these services may not occur and would not likely have materially affected the decisions being reported in the current CD&A and proxy filing, nor will it give investors useful information. However, we do believe that the time period for disclosing "Additional" services should be extended to the prior three years (with the first year of required disclosure under this rule looking back three years). Many consulting assignments occur once every few years as opposed to annually. Simply because a particular service was not provided in the most recent year should not preclude it being reported as an additional financial arrangement with the Compensation Committee's compensation consulting firm. This additional disclosure would help investors assess potential conflicts of interest.

Is the proposed exclusion for consulting services that are limited to broad-based, non-discriminatory plans appropriate? Should we consider any other exclusions?

Yes and Yes. The fees associated with consulting services for other broad-based, non-discriminatory plans should only be considered as "Additional" services for purposes of the enhanced disclosure if the consultant also provides executive and director consulting services.

In addition, there are often ancillary services provided by the Compensation Committee's independent compensation consulting firm that should be excluded from the definition of "Additional" services. For example, the Compensation Committee's independent compensation consulting firm may be asked to provide assistance obtaining approval of a new share request that applies to all employees or to provide guidance with respect to severance and change-in-control agreements that may cover a broader group of key employees. In addition, many executive compensation consulting firms also market pay surveys that are often executive-oriented, but which generally cover executives and management below those reported as NEOs in the proxy statement. As long as these services are requested and/or approved by the Compensation Committee, we believe they should not be considered "Additional" services.

In an effort to obtain statistical affirmation of this position, we conducted a review of Compensation Committee Charters of the Fortune 50 companies. Attached as **Exhibit B** is a graph which highlights the most prevalent duties prescribed in the charters, grouped specifically by "CEO," "Other Executives," "Plans" (non-executive specific) and "Other" (non-executive specific). The study reveals that there are many services performed by compensation consultants on behalf of the Compensation Committee and the Board that are typically not considered in conflict with executive and director compensation services. We would urge the Commission to consider some of these items as specific exceptions from the rule that would trigger additional disclosure. When the Compensation Committee's executive and director compensation consultant is asked by a Board or Compensation Committee to perform services that are reasonably and appropriately within and related to the Compensation Committee's purview, such services do not constitute "Additional" services that should trigger heightened disclosure. They are considered by the Board or the Committee to be within the scope of the executive compensation relationship and therefore do not compromise the consultant's independence.

Should we establish a disclosure threshold based on the amount of the fees for non-executive and director compensation consulting services?

Yes. As noted by the Commission, conflicts, or at least perceived conflicts, typically occur where fees generated from "Additional" services far exceed those from executive and director compensation services. We posit that where the fees generated from "Additional" services do not approach the majority, or are a small proportion, of all services performed by the Compensation Committee's independent compensation consultant, additional disclosure would not be warranted. For example, if fees for "Additional" services during the most recent year do not exceed more than 10% of total compensation consultant fees for all services during the most recent year, we believe conflict, or perceived conflict, is effectively eliminated.

Would disclosure of the individual fees paid for non-executive and director compensation related services be more useful to investors than disclosure of the aggregate fees paid for non-executive and director compensation services?

No. The potential for conflict arises more from the totality of the relationship than from its components.

Would disclosure of the fees paid to compensation consultants and their affiliates help highlight potential conflicts of interest? Should disclosure of fees only be required in connection with providing executive and director compensation services?

We agree with the Commission's position that the enhanced disclosure of fees for executive and director compensation consulting services and for "Additional" services should only be triggered when the consulting firm is providing both types of services to the Company. The disclosure of fees is not necessary and does not help investors assess conflict where the nature of the services provided, and the financial relationship, does not include "Additional" services. We also agree with the Commission's position that the disclosure of all fees where the compensation consultant is receiving fees for both types of services is helpful for investors to assess the magnitude of potential conflicts and for Compensation Committees to ensure appropriate risk management.

Should we make any special accommodations for smaller reporting companies?

No. The potential for conflict exists at all companies and the enhanced disclosure does not increase the cost of disclosure for the registrant.

Are there other categories of consultants or advisors whose activities on behalf of companies should be disclosed to shareholders?

Yes. With the increasing influence of proxy advisory firms on shareholder voting, many companies feel compelled to hire such firms to assist them with various shareholder proposals. We believe it would be appropriate for companies to disclose any fees paid to proxy advisory firms for such guidance. We also believe that law firms often experience similar potential conflicts of interest when advising Compensation Committees where a larger relationship already exists advising management as outside counsel. Similar disclosure of law firm fees for executive and director compensation consulting services and "Additional" services may be helpful for investors in understanding potential conflicts of interest.

Director Qualification Disclosure

The proposed rules would require expanded disclosure of Board qualifications for all publicly-traded companies. However, we are opposed to either requiring, or requiring disclosure of, a specific checklist of qualifications for any particular committee, and particularly for the Compensation Committee. We believe this may the have a chilling effect on Board diversity and could shrink the pool of qualified Board nominees. As discussed below, we have found the most effective Compensation Committees to be engaged and diverse, possessing the skills necessary to understand compensation issues. The enhanced disclosure requirements should help investors determine whether directors, and particularly the Compensation Committee, acting together, have the skills necessary to effectively guide the organization. Furthermore, if the Committee has the authority and funding to hire compensation advisors, it is not critical that there be a 'compensation expert' designation on the Committee. In general, the composition of the Board need not include an expert in each important discipline; rather the Board or the relevant Committee should have the ability to retain experts and advisors as needed.

Other Requests for Comment

Specific Compensation Disclosure Should Not Be Required Below the NEO Level

We have noted that many companies' good faith efforts to fully respond to all of the Commission's disclosure requirements have resulted in CD&As of up to 40 pages for the five most senior executives. Requiring disclosure below this level for employees with limited scope of responsibility and ability to influence the performance of the company as a whole could further significantly increase the volume of disclosure. We do not think such extended disclosure would aid the Commission's goals of transparency and accountability to shareholders or that such disclosure would be helpful in assisting investors to understand compensation programs for individuals that have a significant impact on company performance. Moreover, companies would likely resist disclosure of performance

targets for these lower level employees (particularly heads of business units), if competitive harm is likely and the goals have not already been made public through company reports or earnings statements.

Current Rules for Mandatory Disclosure of Performance Targets Should Not Be Expanded

As independent compensation consultants, we have directly witnessed the unintended consequences of the Commission's current requirements to disclose performance targets. On one hand, we saw many companies move away from discretionary plans where pay was clearly linked with performance, albeit not in a formulaic manner. The current disclosure framework discriminates against such discretionary plans. We continue to believe that information about performance targets may be helpful for investors, but should not discourage Compensation Committees from doing their jobs–that is, limit their flexibility to make discretionary judgments about executive performance in the context of the organization's performance and that of its peers. In many scenarios, particularly a volatile environment that makes goal setting nearly impossible, a discretionary evaluation system is more appropriate than trying to lock in precise compensation formulas at the beginning of the year for the sake of optics.

In addition, many companies have performance targets that, while not rising to the level of the Commission's definition of confidential, are still deemed by the company to be proprietary. For example, some companies regularly set "stretch" goals that are ahead of investment analyst estimates. Disclosing such practices, even "after the fact," could tip the competitive scale and/or result in diminished employee motivation. In seeking to satisfy shareholder optics as well as minimize disclosure of such proprietary goals, many companies tended to homogenize performance targets. These targets were used for compensation purposes, as opposed to company specific measures (either concrete or as determined by the Committee at the end of the year), that may have been more appropriate. Therefore, we strongly disagree with any expansion of the performance target disclosure requirement–whether by eliminating the confidential information exception or creating a three-year look-back.

We do think, however, that a clear statement regarding the percentage of target awards actually earned would be helpful to investors and shareholders.

CD&A and CCR Reporting Technicalities Should Not Be Amended

While there was initial uncertainty whether the CD&A was a document of the Compensation Committee or management, we believe that after three seasons of reporting, the system is working and should not be altered. Some suggest the difference between a "filed" and "furnished" document may lead to better or worse disclosure, or more or less accountability. However, we have observed that in either case, both the Compensation Committee and management are fully engaged in the content of the CD&A and seek to provide a document that is as clear, concise and as accurate as possible.

Mandatory Disclosure about Compensation Committee Expertise Is Unnecessary; Discussion About Resources Should be Required

While it is easy to define experience with respect to financial or accounting functions, compensation expertise is a less specific qualification. In our experience working with Compensation Committees, we have found the most effective members do not necessarily have specific human resources, financial or accounting backgrounds. Rather, they are engaged Board members who utilize their general business experience, taking a common sense approach to compensation and working as a team with outside advisors. The Commission also requested comment as to whether the disclosure should state if sufficient resources are being provided to the Committee to hire outside counsel. We believe such discussion should not only be required for counsel, but also for resources for compensation consultants.

Mandatory Disclosure about Specific "Hold to Retirement" and Clawback Policies Is Unnecessary

While all compensation programs should encourage executives to act in the best interests of the company and its shareholders on a long-term basis, all companies do not and should not follow the same route to achieve this goal. If the Commission were to require disclosure about whether or not a company maintains hold-to-retirement programs, it might signal that this is a compensation "best practice." While a hold-to-retirement policy may be one ingredient in the mix of better long-term practices, it is not right for every company or every executive. At the extreme, if one company required all executives to hold all of their equity compensation to retirement, that company would be at a significant disadvantage in hiring relative to its competitors, as executives naturally prefer some diversification in their investment portfolios. In addition, we do not believe additional disclosures are needed with regard to clawback policies–Item 402(b)(viii) of the existing rules gives companies the opportunity to discuss such policies.

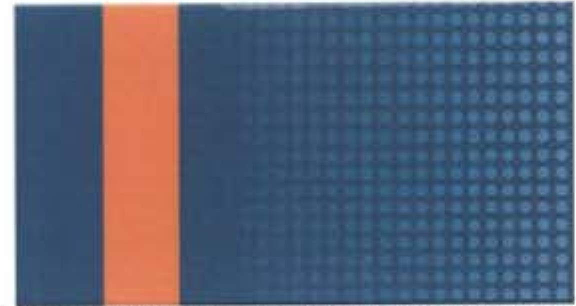
Mandatory Disclosure about Internal Pay Equity Is Unnecessary and Could Result in Competitive Harm

As compensation consultants, we often conduct an internal equity analysis for our clients. However, it is one piece in the mix of analysis for most companies, and decisions are never made exclusively with respect to internal pay equity. We do not believe internal equity should be the primary driver of compensation decisions for executive compensation practices. Again, if the Commission were to require a specific pay ratio disclosure, we are concerned that it may unintentionally prescribe a "best practice." It should be noted that there are also situations (e.g., preparing for CEO succession) where a company's disclosure of the rationale for specific changes in internal pay ratios could result in competitive harm.

More Disclosure about "Other" Compensation Plans is Unnecessary

Again, proxy statements are already overwhelmingly voluminous. Additional requirements about the total number of compensation plans and total number of variables below the executive level will add even more complexities to the disclosure. More importantly, they will not benefit an investor's understanding of the main drivers of compensation for policy making functions–and in fact are more likely to obfuscate such important disclosure.

Exhibit A



ENGAGED DIRECTORS. EFFECTIVE BOARDS.®

Responsible Risk: Effective Incentive Rewards in Turbulent Times

Today's Speakers

Yvonne Chen, a Managing Director in PM&P's New York office, has more than 25 years of experience consulting with companies, subsidiaries and joint ventures in the development of compensation objectives, value-based performance measurement and incentive plan design.

Susan O'Donnell, a Managing Director in PM&P's Boston office, has consulted for over 22 years on issues related to executive and director compensation and governance, with significant experience in the banking/financial services industry.

Suzanne Hopgood is Director of the NACD's Board Advisory Services; Director of Newport Harbor Corporation and Acadia Realty Trust; and President and CEO of The Hopgood Group, LLC.

Risk Assessment – What We Will Cover

NACD Guidance on Risk

- Key Agreed Principles for Boards
- NACD White Papers on priority matters
- Recommendations for executive compensation

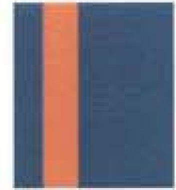
Framework for Risk Assessment

- Process for conducting a risk assessment
- Who should (and shouldn't) be involved in the assessment
- The link between business risks and compensation programs
- Acceptable risk-reward relationships

Compensation Risk Assessment Scorecard

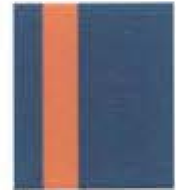
- Key questions to ask when reviewing incentive plans
- Plan design changes to mitigate risk
- 2009 disclosures - where do we go from here?

NACD Leading the Charge



- Directors, investors, and lawmakers are all focused on restoring confidence in Corporate America
- In 2008, NACD took the lead by convening directors, the business community and investor groups to codify a set of principles to guide boards of directors
- NACD's Key Agreed Principles enable directors to test their current practices without being prescriptive and avoid a "check the box" approach to good governance
- The goal is to enable boards to make governance decisions in the context of their own corporate strategy

NACD Leading the Charge



- **NACD's Key Agreed Principles**
  - Provide a blueprint for action for boards to discuss and debate governance issues and practices
- **White Papers: Series I**
  - Dive deeper into priority matters, identifying emerging concerns and guidance in four specific areas:
    - Risk Oversight
    - Corporate Strategy
    - **Executive Compensation**
    - Transparency

Principle 6: Integrity, Ethics, & Responsibility:

Governance ... should promote an appropriate corporate culture of integrity, ethics, and corporate social responsibility

Key Recommendations:

- Rewards should reflect success in reaching both long- and short-term milestones
- Develop internal executive talent
- Foster independence and courage on the compensation committee
- Remain diligent in making decisions based on independent compensation consultants

Source: NACD's Key Agreed Principles to Strengthen Corporate Governance, 2008

Executive Compensation

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"The Buck truly does stop" in the boardroom – 88% of directors surveyed say pay is too high – 54% say it's due to inadequate performance metrics

What do we need?

Executive Compensation

NACD
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Better Performance Metrics

- Reward long-term, sustainable performance
- Consider bonus banks that allow bonuses to be paid out over a period of time to executives who meet predetermined benchmarks

Stronger human capital development

- Avoid exorbitant costs by grooming internal talent to replace upper management. Studies show that internal candidates perform better and at equitable prices.
- Include executive talent management as a component of the evaluation of the CEO's performance

Executive Compensation

Composition of the Compensation Committee

- Use directors who are not only independent by definition, but who are independent minded as well.

Independent consultants

- Advice from consultants is just one tool in creating a pay package.
- Boards should remain diligent in making decisions based on the company and its performance.

Transparency

- Disclosure of board processes
  - Share information regarding in-boardroom processes and decision-making procedures to shed light on the work
  - Key committees could insert letters into the 10-Ks and 10-Qs to alert shareholders to major decisions and the decision-making processes.

The Process – Charting New Ground

Who Should Conduct an Assessment?	Team Structure
• Objective parties • Small group of experts • Individuals with a company-wide view • Advisors with an external market view	• Senior Risk Officer (SRO) • Support from HR, Internal Audit, Legal, Advisors • Report to Compensation Committee • Coordinate with Audit/Risk/Investment Committees
Who Should Not Be Involved?	**Considerations**
• Interested parties • Large management team • Individuals with a narrow focus • External regulators/authorities	• CEO & CFO may lead compliance, but should not review their own compensation and performance • Specialist may provide insights on key risks, but may not have the depth to recognize risk interactions • External parties may govern compliance (for TARP participants) and reporting/proxy disclosure (SEC)
Frequency/Timeframe	**Scope**
• First time process • Annual reviews thereafter • Semiannual reviews for TARP participants • Follow-up on specific items during the year	• Review of business risk • Review of incentive/compensation risk • Stress test based on positive and negative outliers • Identify areas for change and follow-up

A Framework for Assessing Risk

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- An understanding of the business strategy and risks should be the starting point for assessment
- Knowledge of compensation plans is also needed to evaluate the risk-reward interaction

Business Strategy → **Compensation Philosophy**

Business Risks

Operating Risks
Financial Risks
Competitive Risks
Regulatory Risks, etc.

Compensation Plans

Fixed Pay Elements
Short-Term Incentives
Long-Term Incentives
Special Incentives

Risk Assessment

Risk Time Horizon
Management Profile
Corporate Governance
Shareholder Alignment

Upside/Downside Leverage
Positioning vs. Market
Mix of Pay Elements
Balance of Performance Metrics

Changes to Compensation Plans may result from the Risk Assessment

Business Risks

- Companies are in business to take risks, and executives need to be encouraged to take *appropriate* risks.
- But not all risks are acceptable; some risks should not be unduly rewarded.
- Appropriate protections and controls are needed, both within the compensation program and throughout business processes (investment criteria, risk oversight, etc.)
- Business risks may be evaluated using several factors:
  - Type of risk: strategic, operational, financial, competitive, regulatory, etc.
  - Nature of risk: ongoing vs. event-driven; internally vs. externally driven; etc.
  - Potential exposure/impact if the business risk occurs
  - Time horizon for impact
  - Quality of the existing controls and whether it is possible to implement additional controls
- Compensation Committees should take care that compensation plans:
  - Are designed with an understanding of key business risks
  - Do not have design flaws that motivate unnecessary and excessive risk-taking
- There is growing support for linking rewards with "risk-adjusted" returns and capital costs, especially in financial services

Business Risks – Key Questions to Ask

- What are the company's business risks?
- Which risks could most threaten the company's value?
- What is the probability that the business risk will occur?
- Over what time horizon should business risk be measured?
- What controls are currently in place to mitigate risk? What controls should be put in place to better protect the company from excessive risk taking?
- Which risks are connected (directly or indirectly) to incentive compensation?

Risk Matrix –
Linking Business Risks with Compensation Programs

- Business risks would typically be prioritized by the Senior Risk Officer (SRO)
- Examples from various industries are shown below

Industry/ Risk Factor	Type of Risk	Time Horizon	Potential Impact	Level of Controls	Action Steps	Link with Incentive Plans
Investment Banking Derivatives Losses	Ongoing; Systemic	Medium	High	Medium; governed by investment policies	Risk is retained by the company or transferred Portfolio diversification and tighter monitoring	Direct: derivatives traders were paid based on current results
Homebuilder Credit Freeze	Event-Driven; Financial	Medium	High	Medium	Risk is retained by the company Manage D/E ratio; review banking relationships	None
Manufacturer Raw Materials Shortage	Ongoing; Operating	Medium	High	Medium	Risk is retained by the company; some hedging may be possible Monitor inventory; improve supply chain reliability & diversity	Inverse & Indirect: 50% wt. on EPS in STIP tends toward low cost supplier & minimal inventory
Utility Employee Safety	Ongoing; Operating & Regulatory	Long	Moderate	High	Risk may be reduced & insured Improve safety standards and "safety first" culture	Direct: 5% wt. on safety in STIP
Retailer Employee Pilferage	Ongoing; Operating	Short	Low	High	Risk may be reduced & insured Maintain security systems, new employee screening and insurance coverage	Indirect: 50% wt. on EPS in STIP

STIP = short-term incentive plan.

Examples of "High Risk" vs. "Low Risk" Compensation Strategies

- "Low Risk" and "High Risk" are not necessarily good and bad
- Despite risk assessment and controls, any system can fail when people fail

"High Risk" Compensation Strategies	"Low Risk" Compensation Strategies
Investment Banking Industry • Salary is less than 10% of total compensation • Heavy reliance on annual performance measures, even if a portion is paid in deferred shares • Uncapped upside opportunity • Multi-year guarantees as part of recruitment	***Traditional Utility Industry*** • Salary and pension benefits are more than 30% of total compensation • Narrow payout range from 80% to 120% of target for threshold-max; balanced scorecard approach to metrics • Greater reliance on restricted shares with dividends • Little or modest use of stock options
Homebuilding Industry • Total compensation equals a % of annual pre-tax profits • Uncapped upside opportunity • Formula-driven incentive plans do not allow negative discretion for "worst of the best" performance • Entrepreneurial culture favors use of stock options	***Not-for-Profit Sector*** • Compensation levels restricted to a fraction of total compensation for executives at public for-profit • Emphasis on base salary • Little or no bonus opportunity • Ongoing use of benefits and perquisites

Acceptable Risk-Reward Relationships

Typically Acceptable:

- Defined range of incentive awards (e.g. 50% - 200% of target)
- Majority of incentive compensation weighted toward long-term, equity-based incentives
- Long-term incentive/equity vesting schedules that are three years or more
- Meaningful stock ownership and retention guidelines

May Be Questionable:

- Small variations in performance that result in large variations in pay
- Heavily lopsided reward opportunity, e.g., uncapped upside or guaranteed minimum payouts
- Quarterly bonus payments without "true-up" if full year results fall short
- Immediate (or quick) vesting of equity-based incentives
- Overloading on stock options through mega grants

Compensation Program Risk – Key Questions

- Do incentive plan metrics reflect the company's business strategy?
- Is there an appropriate balance and mix of performance metrics?
- Is the leverage (upside and downside) appropriate?
- Is there appropriate focus on long-term performance?
- Are there protections/controls in place to avoid excessive payouts?
- Do the payouts align with shareholder interests?
- Do the payouts align with market practice?

Compensation Risk Scorecard (partial example)

Risk Factor	Specific Parameters	Effectiveness Rating				
		1	2	3	4	5
Performance Metrics	Incentive plan metrics are selected in the context of the Company's business strategy, goals and key risks					
	There is a balanced "portfolio" of performance measures across short- and long-term incentive plans					
	No one performance measure receives too much weight/impact toward incentive payout					
	...					
Quality of Goal Setting	Target performance levels represent reasonable variation relative to historical performance and investment analyst forecasts					
	The probability of payout at threshold, target and stretch is understood and reasonable					
	Over time, historical payouts track with stock price					
	...					
Pay Mix and Balance	The overall pay mix reflects desired philosophy and objectives					
	There is appropriate balance between short- and long-term performance					
	There is appropriate balance between cash and equity compensation					
	....					

Compensation Risk Scorecard (partial example)

Risk Factor	Specific Parameters	Effectiveness Rating				
		1	2	3	4	5
Leverage	The full range of total compensation opportunity for low and high performance is known and appropriate (Dynamic Pay Modeling)					
	Incentive plans do not provide for uncapped upside (or controls are in place to manage extraordinary windfalls)					
	Changes in performance result in appropriate changes in payout (i.e. curve)					
	...					
External Reference	The compensation peer group is based on companies similar in size and other key parameters					
	Compensation practices are in line with industry/peer practice					
	Company performance explains any pay variation from market practice					
	...					
Checks and Balances	The company has an audit process for determining incentive plan payouts					
	The company has a defined clawback policy					
	The company has stock ownership/retention guidelines					
	....					
Other	The Company has formal governance practices related to CEO performance					
	....					

Example of Incentive Plan Design Changes Resulting from the Compensation Risk Scorecard Assessment

- **Adjust the mix of performance measures**
  - Company had too much weight on one measure (revenues), which was rewarded in both the short- and long-term incentive plans
  - Introduced a return measure to the short-term incentive plan to balance the mix
  - Refocused the long-term incentive plan on sustained long-term performance and stock value
  - Considered both absolute and relative performance measures
- **Shift toward a longer-term performance horizon in the pay mix**
  - Reduced weight on annual incentive plan; increased weight on long-term incentives
  - Introduced a performance share plan based on 3-year TSR relative to peers
- **Implement design features that reward sustainability of performance**
  - Introduced overlapping performance cycles for long-term performance share plan
  - Lengthened the stock holding requirements
- **Implemented protections for "swing for the fences" behavior**
  - Capped upside opportunity to 300% of target
- **Incorporate Committee discretion** to adjust awards based on "how" results were achieved and "quality" of earnings; at end of day, business judgment should rule

- However, beware that mitigating risk could dampen the pay-for-performance linkage
  - Multiple performance measures, with little weight on each
  - Bonus deferral tends to result in "smoothing" of awards
  - Committee discretion may be applied inconsistently

2009 Proxy Disclosure – Where Do We Go From Here?

- Limited details provided in 2009 proxies
  - Initial focus on TARP participants only
  - New process and rules with little time to execute
  - In a PM&P review of 2009 proxy filings for 50 large companies:
    - 7 of 9 TARP companies discussed "excessive risk"
    - However, only 8 of 41 non-TARP companies discussed "excessive risk"
- Disclosure tended to focus on:
  - Summary of process and who was involved
  - Identification of business risks
  - Examples of plan design features that mitigate risk
  - Overall finding that incentive plans do not motivate excessive risk taking
  - Several non-TARP companies only provided an overall statement with limited reference to plan design features
- A call to action for improvements in 2010:
  - More expectation for all companies to assess risk as part of their compensation review process
  - More rigorous analysis in general
  - Better integration with general business risk analysis
  - Greater investment of time to conduct the assessment and hold discussions
  - Identification of plan design features/changes

CDE Credit Information

Holders of the NACD Certificate of Director Education will receive 2 CDE Credits.

More than 1100 directors and executives have obtained the NACD Certificate designation and maintain it annually through continuing director education. If you would like to know more about the Certificate of Director Education, please visit our website at www.nacdonline.org.

If you have any CDE questions, contact

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To learn more about the National Association of Corporate Directors, visit www.nacdonline.org.

NACD Corporate Governance Conference

October 18-20, 2009
Omni Shoreham Hotel, Washington, DC

This year's conference will provide directors with a unique forum for thinking through and tailoring their own governance structures and practices to create a new blueprint for action in the boardroom. Please visit http://www.nacdonline.org/conference/2009default.asp for program details and registration.

Our Next Webcast:

Thursday, June 18, 2009, 2pm ET

The Future of Options

Deborah Lifshey, Managing Director, Pearl Meyer & Partners
Ed McGaughey, Managing Director, Pearl Meyer & Partners

For more information, visit nacdonline.org

NACD Resources

Educational Resources

1. **Additional NACD Board Advisory Services** - In-Boardroom Programs and Evaluations - ***http://www.nacdonline.org/services***

2. **NACD Education** – *Director Professionalism®* Course, Committee Seminars, & Annual Governance Conference ***http://www.nacdonline.org/dp***

3. **NACD Chapters** - ***https://secure.nacdonline.org/source/meetings/chapter_Page.cfm***

4. **NACD Publications** - Blue Ribbon Commission Reports, Surveys, and Handbooks - ***http://www.nacdonline.org/publications***

5. **NACD Directors Registry™** – Qualified Candidates for Effective Boards - ***http://www.nacdonline.org/registry/default.asp***

Thank You!

- A copy of these slides will available by tomorrow at pearlmeyer.com/responsiblerisk.
- Both the replay and the presentation will be available at nacdonline.org or pearlmeyer.com next week.

Thought of a Question After the Presentation?

Please feel free to direct additional questions regarding this presentation to:

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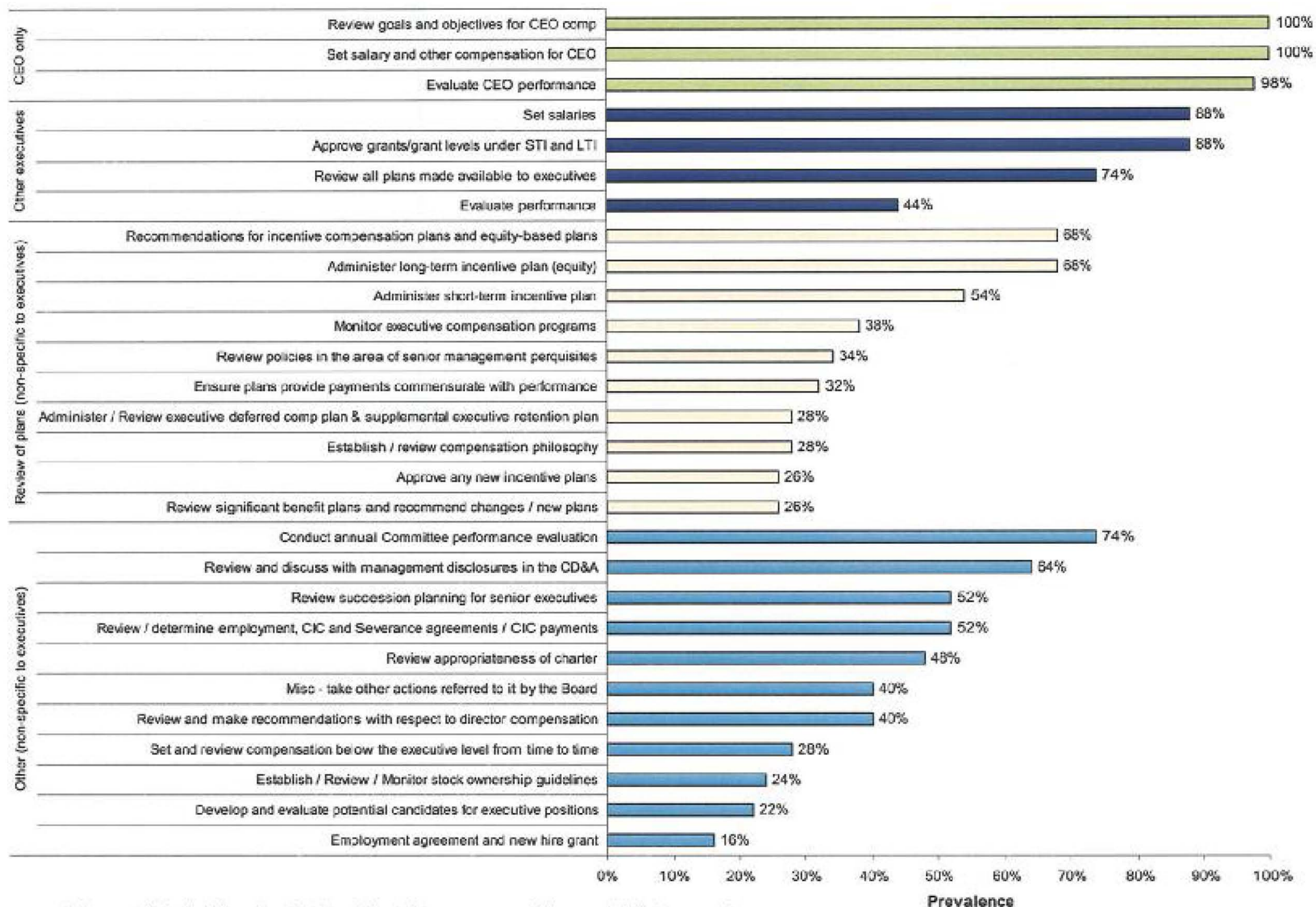
Exhibit B

Fortune 50 Companies - Most Prevalent Compensation Committee Duties per Charter*



** Does not include risk-review that is anticipated to commence with amended disclosure rules*