United States Proxy Exchange

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VIA UPLOAD: http://www.sec.gov/rules/proposed.shtml

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609

Re: File No. S7-13-09
Proxy Disclosure and Solicitation Enhancements

Dear Ms. Murphy:

The United States Proxy Exchange (USPX) and co-signers of this letter are delighted to submit comments on Proxy Disclosure and Solicitation Enhancements: SR 07-10-09. We are a non-government organization, incorporated in the Commonwealth of Massachusetts, that is dedicated to facilitating shareowner rights, primarily through the proxy process. We support some but not all of what has been proposed. We have a number of specific suggestions for how the proposals might be improved.

A1. Enhanced Compensation Disclosures Related to Risk

The Commission has proposed to amend existing Compensation Discussion and Analysis (CD&A) disclosure requirements to "include a new section that will provide information about how the company's overall compensation policies for employees create incentives that can affect the company's risk and management of that risk,"[1] *The Commission indicates "In preparing this disclosure, we believe that companies will need to consider the level of risk that employees might be encouraged to take to meet their incentive compensation elements. We believe that disclosure of a company's overall compensation policies in certain circumstances can help investors identify whether the company has*

[1] Proposal, p. 8.

established a system of incentives that can lead to excessive or inappropriate risk taking by employees."[2]

Our organization has considerable expertise related to these specific matters. Many of our volunteers are finance professionals, and several have experience with risk management. In particular, our executive director, Mr. Glyn A. Holton, is a noted expert on financial risk management. Our chairman, Mr. Vincent Cirulli, is the head of market risk management at MetLife. Our treasurer, Ms. Kitti Barker, CPA, CVA, has conducted internal risk assessments, audits and SEC filing restatements for companies including MCI, Freddie Mac and Fannie Mae. Before we address the Commission's specific proposal, let's present some context.

We believe that, over the past two decades, the financial services industry has discovered "risk" to be a convenient scapegoat in instances where financial institutions or their clients suffer staggering losses due to fraud or other forms of abuse.

If a man jumps out of an airplane without a parachute, is he taking risk? If he is certain to die, the answer is "no." Risk is not about consequences. It is about *uncertain* consequences. If there is no uncertainty, there is no risk. Similarly, there was no risk in many of the securitizations that crippled our economy in 2008. These were bundles of mortgages underwritten as if home prices would rise forever, creating a giant pyramid scheme. They were guaranteed to fail. Mortgage originators, investment bankers and credit rating analysts knew, or should have known, the instruments were unsound. Yet, the entire industry aggressively pushed the instruments because they had incentive compensation that promoted such abuse.

In the midst of the ensuing crisis, Congress and other branches of our government did not wait for hearings before they embraced Wall Street's excuse that "excessive risk" was to blame. We believe this shifting of blame from abuse, where the blame correctly belongs, to excessive risk, where it is largely misplaced, is forestalling appropriate legislative and regulatory initiatives that might prevent future market panics. We believe the current administration's proposal to form a systemic-risk regulator, regretfully, falls short of what is needed. What our economy needs is a systemic-*abuse* regulator.

Excessive risk taking is one form of abuse, and it may be motivated by perverse incentive compensation schemes, but it is not the only one:

- Putting low-income families into mortgages they cannot afford is "predatory lending." It is a form of abuse unrelated to "excessive risk taking."

- Routinely falsifying those families' mortgage applications to ensure they are approved is "fraud." It too is a form of abuse unrelated to "excessive risk taking."

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[2] Proposal, p. 9.

- Bundling those structured-to-fail mortgages into CDO's and giving them investment grade ratings is "deception." It too is a form of abuse unrelated to "excessive risk taking."

- Parking the toxic CDO's in affiliated hedge funds and providing those hedge funds inflated valuations to hide the losses is "collusion." It too is a form of abuse unrelated to "excessive risk taking."

- Foisting those hedge funds on unsuspecting institutional investors and charging them "2 and 20" for the privilege is "manipulative sales practices." It too is a form of abuse unrelated to "excessive risk taking."

None of these abuses relates to "excessive risk taking." All are, or can be, motivated by perverse incentive compensation schemes.

It is in this context that we respectfully suggest that amending existing CD&A disclosure requirements to include information about how compensation policies create incentives affecting a company's risk falls short of the real need. We have three reasons.

1. Focusing on risk treats "excessive risk taking" as the sole form of abuse that incentive compensation might motivate. This misses—and will likely distract people from—the important point that perverse incentive compensation has caused, and likely will continue to cause, a wide variety of abuses.

2. Risk is a subjective notion.[3] This makes assessing any link between risk and incentive compensation problematic. Furthermore, that link will be impacted by a myriad of other factors, including corporate controls, any risk management function, corporate culture and the involvement of senior management. Corporations will have broad latitude in how they choose to perceive, and hence present, any possible relationship between risk and incentive compensation. We expect that disclosures on this matter will be unenlightening "boilerplate" statements drafted by lawyers.

3. We believe that standardized disclosures to shareholders about any relationship between risk and incentive compensation is inconsistent with a suitable distinction between the roles of a company's management, board and shareholders. The matter of non-executive employee compensation should be addressed by management with close supervision by the board. When things get so bad that shareholders have to be drawn in, that is a clear indication that boards are failing to perform their oversight function. The fundamental problem is that entrenched boards, largely unanswerable to shareholders, lack necessary incentives to protect shareholder interests. Disclosures

[3] See Glyn A. Holton (2004). Defining risk, *Financial Analysts Journal*, 60 (6), 19–25, available on-line at http://www.riskexpertise.com/papers/risk.pdf.

about possible relationships between risk and incentive compensation will do nothing to address this problem.

Our answers to specific Commission questions follow.

A1.1 Would expanding the scope of the CD&A to require disclosure concerning a company's overall compensation program as it relates to risk management and or risk-taking incentives provide meaningful disclosures to investors? Should the scope of the amendments be limited in application to specific groups of employees, such as executive officers? Should it be limited to companies of a particular size, like large accelerated filers? Should it be limited to particular industries like financial services, including companies that have segments in such industries? Is the cost of tracking and disclosing the nature of the risk different at different types of companies or company segments and if so, should that be reflected in our rules?

While we believe there is a need for corporate disclosures relating to risk and risk management, we do not believe these disclosures, at least as currently proposed, will be useful. They will address subjective matters without any objective criteria for assessing the veracity, quality or completeness of whatever disclosures a company chooses to make. Other than ensuring that companies make a disclosure statement—any disclosure statement—no enforcement will be possible. Philosophically, a purportedly factual statement that is impossible to confirm or reject based on empirical evidence is meaningless. But that is exactly what these subjective disclosures will be.

We anticipate corporate lawyers will draft boilerplate responses to these items that will be recycled year after year.

A1.2 In light of the complexity of the issue and compensation programs generally, we recognize that it may be difficult to identify and describe which compensation structures may expose a company to material risks. We believe the listed examples are situations where compensation policies may induce risk taking behavior, and therefore, potentially have a material impact on the company. Are the listed examples appropriate issues for companies to consider discussing and analyzing? Are there any other specific items we should list as possibly material information? Are there any items that are listed that should not be? If so, why?

We emphasize that it is not compensation structures that are the problem. It is abusive practices that exploit compensation structures—only some of which entail excessive risk. We believe that disclosures that focus exclusively on compensation practices will fail to isolate situations where abuse is possible or actually taking place. Furthermore, we believe that identifying the sorts of compensation situations that the Commission highlighted is likely to be an expensive and largely arbitrary process.

Here are the specific examples of situations the Commission identified in the proposal that might trigger discussion.

1. A business unit of the company that carries a significant portion of the company's risk profile;

2. A business unit with compensation structured significantly differently than other units within the company;

3. Business units that are significantly more profitable than others within the company;

4. Business units where the compensation expense is a significant percentage of the unit's revenues; or

5. That vary significantly from the overall risk and reward structure of the company, such as when bonuses are awarded upon accomplishment of a task, while the income and risk to the company from the task extend over a significantly longer period of time.

To our knowledge, "business unit" is not a well defined notion. For internal reporting purposes, a company might segment its operations into business units, but where such practice exists, it is likely to be inconsistent from one company to another. People might use the term "business unit" to refer to anything from a three-person team to a 20,000 person division.

Companies may formally allocate revenue or profits to "business units" for internal reporting purposes, but the manner in which they do so may not be relevant for risk assessment. For example, an insurance company may earn revenue from annuity sales, but which business unit should take credit for those revenues: the sales department that sells the annuities; the underwriting department that underwrites them; the actuarial department that prices them; the investment department that hedges them, or the asset-liability department that monitors how they are hedged? All these business units impact the company's risk, and all facilitate the revenue in some capacity. Whichever department the company chooses to allocate the revenue to, the decision will be somewhat arbitrary.

Because revenue, and hence profits, allocated to individual business units are such arbitrary notions, the third and fourth of the Commission's above example situations are not particularly meaningful.

Trying to allocate risk to specific business units is even more problematic than trying to allocate revenues. At least revenues sum across business units. Risks, which can hedge or diversify one another in complex ways, generally do not. Consider the same insurance company. If the annuities ultimately cause the company to lose money, which business unit was responsible for the risk—sales, underwriting, actuarial, investments or asset-liability management?

Because risk allocated to individual business units can be a largely arbitrary notion, the first of the Commission's above example situations also may not be particularly meaningful.

We note that the Commission's second example situation—"A business unit with compensation structured significantly differently than other units within the company"—is so broad as to require numerous disclosures. Any sales department that pays salespeople on commission would meet the criteria.

The Commission's fifth example situation identifies a significant problem. For example, such poorly-designed compensation practices caused Enron staggering losses in their international operations, and it was attempts to cover up those losses that eventually mushroomed into the vast fraud that doomed the company. However, compensation practices that technically meet the indicated criteria are widespread, especially in how the financial services industry compensates brokers, traders and salespeople. If the Commission is concerned about abuses that arise from those compensation practices—we certainly are—we recommend direct regulation of those compensation practices as more effective than disclosures that the practices exist. *We all know they exist.* Even laymen have a pretty good understanding of how insurance salesmen, stock brokers, traders and derivatives salesmen are compensated. Requiring that we all be reminded in the 10-K each year seems unnecessary.

Overall, we believe that these proposed disclosures are flawed for focusing on compensation rather than abuse. We also believe they fail to recognize that efforts to "allocate" revenues, profits or risks among business units can be arbitrary or otherwise not useful for risk assessment purposes.

A1.3 Should other elements of compensation that may encourage excessive risk taking be highlighted in the CD&A?

As we have indicated, we believe disclosures should focus more directly on potential or actual abuses, only some of which entail "excessive risk taking."

A1.4 We have included a list of examples of the types of issues that would be appropriate for a company to discuss and analyze. Is that list appropriate?

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

As we indicated in our response to Question A1.2, we believe the examples the Commission presented pose interpretive or other challenges, and that similar examples would likely also be problematic.

A1.5 Are there other disclosure requirements that would provide more meaningful information about the effect of the registrant's compensation policies on its risk profile or risk management?

We believe there is a need for enhanced disclosures related to possibly excessive risk taking or other abuses. We do not feel much will be gained by narrowly focusing such disclosures on compensation practices that might be associated with these, at least not in the manners currently proposed.

The accounting profession in the United States has discovered, over some hundred years, that meaningful disclosures require that some individual certify those disclosures and be personally liable for their veracity. This was first done with auditors certifying companies' financial statements and more recently under Sarbanes-Oxley with CEOs and CFOs making similar certifications—and facing possible criminal penalties for misstatements. In the realm of accounting, "I didn't know" is no longer an acceptable excuse.

In the realm of risk and abuses, "I didn't know" is still accepted. So long as this remains the case, any disclosures related to risk or abuses that the Commission requires will be meaningless, as in ... "Yes, we disclosed that our company was taking little or no risk when in fact our traders were betting the house, but 'I didn't know.'"

This is an enormous problem that won't be resolved with a few minor additional disclosures. We encourage the Commission to take on the task of drafting a new rule dedicated entirely to corporate risk, abuse and the management of these. This could consolidate and dramatically expand on existing disclosures under Regulation S-K items 303 and 305. The centerpiece of this new rule should be a comprehensive, open-ended report signed by the principal executive officer and CFO for inclusion in the 10-K, with both individuals held personally liable for omissions in that report that come to light as a result of subsequent unanticipated losses.

It is certainly reasonable for businesses to give some latitude to employees to take risks or trust them to follow their professional judgment. We do not want to stifle that. However, the CEO and the CFO must each take personal responsibility for ensuring individual employee judgments are not turned into a systemic risk or pattern of abuse for the company.

A1.6 Are there certain risks that are more clearly aligned with compensation practices the disclosure of which would be important to investors?

While certain forms of incentive compensation may be associated with risk taking or abuse, we do not believe it is desirable or appropriate to disclose these to shareholders, for reasons we presented above.

A2. Disclosure of Executive Stock Option Grants

In 2006, the Commission enacted broad executive compensation disclosure amendments. One objective was to provide shareowners with a single dollar figure that includes all compensation—including equity grants and equity option grants—that is comparable across fiscal years and companies. For that purpose, the Commission required that equity options be valued at the cost recognized for financial reporting purposes in that fiscal year. This had the effect of spreading out the cost of option grants over multiple years and making the reported value of those grants reflect factors out of the compensation committee's control—the performance of the company's stock price, in particular. Based on feedback from shareowners, the Commission is now proposing that option grants be valued at full fair value as of the grant date.

We support this minor amendment for the reasons the Commission cites. It should be emphasized that this is an amendment to enhance disclosure of a form of executive compensation that is routinely abused. It would be unfortunate if the Commission's disclosure requirements were seen as somehow legitimizing executive stock options.

As we have already discussed in this letter, the Commission is concerned about forms of incentive compensation that motivate excessive risk taking. The quintessential such form of incentive compensation is stock options. Because options allow recipients to participate in the rewards of risk taking but not the adverse consequences, they provide a strong incentive for the taking of ever more risk.

Abusive executive compensation practices are one of the most alarming consequences of today's broken down proxy process. We are mindful of the Commission's efforts to repair the proxy process, especially through proposed Rule 14a-11. While that work progresses, we encourage the Commission to do everything in its power to go beyond disclosures and directly address abusive executive compensation.

B. Enhanced Director and Nominee Disclosure

Items 401 of Regulation S-K requires certain disclosures regarding directors or nominees for director positions. The Commission has proposed enhancements to these disclosures as well as certain additional disclosures.

Currently, the following information about individual directors can be gleaned from disclosures required under items 401 and 407 of Regulation S-K:

1. Name and age.

2. All positions and offices held with the company, including any periods of service as a director.

3. Any arrangement or understanding between her and any other person(s) pursuant to which she was selected as a director or nominee.

4. The nature of any family relationship with any other (existing or nominated) director or executive officer of the company.

5. A brief description of any business experience during the past five years, including principal occupation and employment. Employers during that period should be listed along with an indication of whether these are affiliated with the company.

6. Other directorships held at any company with securities registered under section 12 or subject to section 15(d) of the Exchange Act, or any company registered as an investment company under the Investment Company Act of 1940.

7. Within the past five years, bankruptcy proceedings or receiverships, either personal or relating to any partnership, corporation or business association of which she was a general partner or executive officer within two years prior to the event. (Unless deemed not material to an evaluation of her integrity or ability to serve as a director.)

8. Within the past five years, any criminal convictions or pending criminal proceeding in which she is a named subject (excluding traffic violations and other minor offenses as well as any items deemed not material to an evaluation of her integrity or ability to serve as a director).

9. Within the past five years, any instances in which she has been barred by a court or other authority from engaging in certain financial or business activities, and the order was not subsequently vacated. (Unless deemed not material to an evaluation of her integrity or ability to serve as a director.) See Regulation S-K, item 401 for details.

10. Within the past five years, she was found by a court in a civil action, or by the SEC or CFTC, as applicable, to have violated federal or state securities laws or to have violated federal commodities laws, and such finding was not subsequently vacated. (Unless deemed not material to an evaluation of her integrity or ability to serve as a director.)

11. Whether she serves on the audit, compensation or nominations committees and, if she serves on the audit committee, whether she does so as an audit committee financial expert (Regulation S-K, item 401(h)).

12. Whether she attended fewer than 75% of board meetings or meetings or committees on which she sits over the past year.

13. Whether she satisfies some applicable criteria for independence.

14. If she is not currently a director, whether her nomination was first proposed by a security holder, a non-management director, the chief executive officer, some other executive officer, a third-party search firm, or some other specified source (different categories apply for investment company director nominees).

While the list may appear lengthy, most of it relates to "red flags" which might raise questions about an individual's suitability to sit on a board. Items 3 and 14 are easily circumvented, and items relating to legal proceedings offer companies a broad exception for legal proceedings they deem not relevant. For the vast majority of board members, substantive disclosures comprise merely: work history for the past five years, the committees she sits on, and directorships at other companies. Recognizing that this is hardly a basis for shareholders "to determine whether and why a director or nominee is a good fit for a particular company,"[4] the Commission is proposing:

1. An additional disclosure for each director or nominee comprising a narrative description of "the specific experience, qualifications or skills that qualify that person to serve as a director and committee member."[5] The company will have broad latitude to decide what specifically to cover in this narrative.

2. Extension of the existing disclosure of a director or nominee's other directorships to include any directorships held *during the past five years*.

3. Lengthening of the time during which disclosure of legal proceedings is required from five to ten years.

We believe these additional disclosures fall short of the Commission's goal of providing a basis for shareholders "to determine whether and why a director or nominee is a good

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[4] Proposal, p. 27.
[5] Proposal, p. 27.

fit for a particular company." We explain why in answers to the Commissions specific questions below.

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

No. Some of the enhanced disclosures may be helpful, but they fall short of being "important information." They will do little to enhance shareowners' understanding of who is representing them on the board or running for the board.

The proposed narrative description is entirely open-ended, which will make it little more than an advertisement for the particular director or nominee. The Commission has separately proposed (Facilitating Shareholder Nominations, File No. S7-10-09) that companies be required to include in their proxy statements supporting statement for board nominees. These too will serve as advertisements for director nominees. To avoid redundancy, we recommend that the Commission combine the two proposed statements/disclosures into one.

We endorse disclosure of past directorships but believe all past directorships should be disclosed, not just those over the past five years. We elaborate in our response to Question B.7, below.

With regard to lengthening time during which disclosure of legal proceedings is required from five to ten years, we generally support the view that more disclosure is better than less. However, these are arbitrary numbers. Will the Commission come back in a few years, following the next financial crisis, and propose extending the period from ten years to fifteen?

We generally believe that disclosure periods should be set based on the nature of the legal proceedings to be disclosed. Certain of these, including criminal convictions, should have no time limit for disclosure. We elaborate in our response to Question B.9 below.

As we have indicated, we believe existing disclosures about individual board members or nominees are inadequate for shareowners to make informed decisions about whom they want representing them on the board. We do not believe the proposed additional disclosures address this problem. Below, we recommend additional disclosures.

It is incomprehensible that people can take seats on boards of multibillion dollar corporations in this country without ever producing a resume. Anyone else in this country who applies for pretty much any other position must produce one. What sort of elitist thinking has lead us to a situation where director nominees are exempt?

We encourage the Commission to require all directors or nominees to produce a standardized resume documenting:

1. Undergraduate colleges or universities attended, including fields of study ("majors"), degrees earned, grade point average (on a four-point scale), years of enrollment and dates on which degrees were granted.

2. Graduate programs attended, including university, fields of study, degrees earned, years of enrollment, and dates on which degrees were granted. In the case of a Ph.D., the thesis title should be provided with a link to the thesis held in pdf format on EDGAR.

3. An indication of whether the individual is an MD, CPA, lawyer, or other licensed professional, as well as the date on which that status was achieved.

4. Complete employment history, including employers, dates, titles, and job descriptions. Gaps in the employment history must be accounted for.

5. Full citations for the individual's publications broken down as most recent twenty books (first editions only), most recent twenty peer-reviewed journal articles, and the most recent twenty newspaper or magazine articles or editorials. In the case of co-authored publications, all authors names should be provided *in the order in which they appear* in the original publication. If the individual has a blog or opinion oriented website, the URL should be provided.

6. Particular expertise the individual has which would be valuable to the board, with an indication of when the expertise was acquired and when in the past it has been used (indentifying specific education or work history items in the resume).

Another thing that we find incomprehensible is that people can take seats on boards of multibillion dollar corporations in this country without having anyone vouch for their character or qualifications. Anyone else in this country who applies for pretty much any other position must produce references.

Accordingly, we recommend that all directors or nominees be required to produce three reference letters from individuals who have no association with the company. Letters should be required to open with one of the following three lines:

1. I have known [name] personally for [number] of years. I wholeheartedly endorse [him/her] for a directorship at [company name] without reservation.

2. I have known [name] personally for [number] of years. I strongly endorse [him/her] for a directorship at [company name] with the following caveats.

3. I have known [name] personally for [number] of years. I endorse [him/her] for a directorship at [company name] with the following reservations.

While we anticipate nominees will shop around to find people willing to write letters with the first opening line, shareholders will take note of what caliber people are willing to put their reputations on the line by so vouching for the nominee.

When letters are informative, they could provide valuable anecdotes or insights related to the individual. When they are bland and tentative, that fact alone could be informative.

Reference letters would serve another valuable purpose. While directors or nominees may delegate preparation of their other disclosures to lawyers, accountants or secretaries, most will decide to personally approach friends to ask "will you please write a letter for me." This personal, vulnerable act will impress on directors—in a way no other duty or prerogative of the director role does—that *they work for the shareowners*.

Letters could be used for five years. After that, new letters *by new authors* would have to be obtained.

Another profoundly important disclosure that should be required of current directors is information on their track records. How did they vote at board meetings? What motions did they make? What initiatives did they pursue? Due to the wall of silence entrenched boards maintain around their actions, shareowners never know any of this. This absurd situation has two consequences:

1. Even after a director has served on the board for years, shareowners have no basis for assessing whether she has represented them in a manner of which they approve.

2. Knowing shareowners will never be aware of their actions, directors are under no pressure to personally act in the best interests of shareowners.

The Commission desperately needs to break through the wall of silence around entrenched boards. We believe an entire new rule should be dedicated to this topic. One particular suggestion is to require the disclosure of the minutes from all board meetings, including:

- All motions, who made them, and who seconded them.
- Who voted for, against or abstained for each motion.
- All committee or other reports, transcribed with supporting documents.
- All consent decrees as well as who voted for, against or abstained fro each.

The CEO could apply minimal redaction to these materials for the sole purpose of protecting business secrets. However, shareowners would need to see where material had been redacted as actual text blacked out. They could then draw inferences from the volume of redactions. Also, the complete materials, without any redactions, would have to be disclosed three years later. At that point, material could only be redacted with the Commission's consent, and that consent would have to be given again every three years until the redacted material was finally disclosed.

One of the remarkable accomplishments of the US Government in the 20th century was FOIA—the Freedom of Information Act. We need a FOIA for corporate boards.

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

We believe this specific disclosure should not be retained. Shareowners can and should determine for themselves what qualifications they feel are appropriate or necessary for board members.

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

We do not believe disclosure of any factors that a nominating committee considers is desirable or appropriate.

The USPX does not have a position on whether or not diversity is an appropriate consideration when forming a board. We believe it is entirely up to shareowners to decide for themselves if they will take diversity into account when making nominating or voting decisions.

So shareowners may consider diversity, if they so choose, additional disclosures related to diversity are appropriate. We recommend the following disclosures for each director or nominee:

- gender,
- self-described ethnicity,
- a color photo of the director or nominee.

The photo will serve to keep self-described ethnicity "honest." If a director describes himself as "Hispanic" but his photo looks "White Anglo-Saxon Protestant," shareowners will draw appropriate conclusions.

Photos should be standardized as follows. They should be submitted and made available on EDGAR as 768 pixel wide by 1024 pixel high color JPG files. They should be passport-style headshots cropped closely to the head. They should be sharp photos taken within the last five years. They should be placed in the public domain, so shareowners, proxy advises or publishers may freely use them.

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

Even if they don't change from one year to the next, qualification disclosures should appear annually. This would be convenient for shareowners, saving them from having to rummage through past 10-K's. It would also prevent confusion among shareowners who were unaware of the rule for when qualification disclosures for given directors should or should not be made.

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

We believe all past directorships should be disclosed, not just those over the past five years. Past directorships, and especially directorships held early in one's career, could provide valuable insights into an individual's formative experiences serving on boards. Knowing, for example, that someone's first board position was with Citizen's Energy might distinguish that person from someone whose first board position was with ExxonMobil. This sort of texture, which can provide insights into an individual's character, priorities, social circles and worldview is missing from existing director disclosures.

The currently proposed wording for this amendment[6] would require disclosure of "directorships ... in any company with a class of securities registered pursuant to section 12 of the Exchange Act (15 U.S.C. 78l) or subject to the requirements of section 15(d) of the Exchange Act (15 U.S.C. 78o(d)) or any company registered as an investment company under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.) ..." We are aware that the unfortunate National Securities Markets Improvement Act of 1996 created an enormous loophole in the 1940 act, which has facilitated massive growth in the so-called hedge fund industry. We believe that, for the same reasons shareowners would desire disclosure that a director or nominee holds or has held directorships at investment companies, they would also want disclosure that a director or nominee holds or has held a general partner or other principal position in a large hedge fund or other such exempt pooled investment vehicle.

We note that, for this purpose, a convenient definition of "large" would be any such fund that is exempt under the 1940 Act but that would not have been exempt prior to the National Securities Markets Improvement Act of 1996.

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

No. Director positions are extremely attractive part-time employment. They offer prestige, social access and compensation that vastly exceeds that paid for most full-time jobs. Companies will have no difficulty attracting exceptional candidates. A bigger question is whether they are willing to do so. The community of entrenched board members is rife with cronyism. If enhanced qualification disclosures embarrass some of the cronies into not running, that might *force* entrenched boards into looking outside their insular circle.

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

[6] Proposal, pp. 128-129.

We believe there should be no time limit on disclosures of serious crimes or the sorts of fraud mentioned. These are serious matters that speak volumes about the perpetrator's character.

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

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

All of these should be disclosed. It is unimaginable that they currently are not.

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

No. Any legal proceeding could be critical to shareowners' understanding of a director's, nominee's or executive's "ability or integrity." It should be left to shareowners to decide what they consider material. If a director has three arrests for drunk driving, that is a clear indication of recklessness and disregard for human life. Most shareowners would want to know, but we expect corporate lawyers would exclude it as "immaterial." Shareholders would want to know if a director has battered his wife, but we expect corporate lawyers would exclude this too as "immaterial." Shareowners would want to know of *any* instance in which a director violated securities laws, but we expect corporate lawyers will concoct reasons to exclude instances as "immaterial."

Furthermore, we believe the existing waiver for disclosing traffic violations should be clarified so as to not exclude serious crimes such as driving under the influence or vehicular homicide.

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

Director qualification disclosures should apply to investment companies.

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

The Commission is proposing a new disclosure requirement that would have companies indicate whether and why they separate or combine the principal executive officer and board chair positions. If a company has a lead director position, this will need to be indicated with an explanation of why and a description of the specific role of that lead director. The role the company's board plays in risk management would also need to be disclosed.

We believe that, for publicly traded companies, having a single person hold both the positions of principal executive officer and board chair violates an essential separation of power. An important purpose of the board is to hire, fire and otherwise oversee the executive officers, and especially the principal executive officer. Having the principal executive officer hold the board chair undermines this purpose. It is abusive.

While we support disclosure of instances where companies violate this important separation of powers, we believe the amendment, as drafted, will have the unfortunate consequence of legitimizing such instances. It implicitly treats the separation of the two roles as just one of several legitimate arrangements. Indeed, the Commission endorses this view in the proposal:

> " ... we note that different leadership structures may be suitable for different companies depending on factors such as the size of a company, the nature of a company's business, or internal control considerations, among other things."[7]

No examples or theories or empirical evidence is offered in support of this claim. We believe that, for publicly traded companies, having a single person hold both the positions of principal executive officer and board chair violates an essential separation of power

[7] Proposal, p. 34.

and creates an unnecessary conflict of interest—where one individual chairs a group charged with supervising, setting the compensation for, and possibly firing that same individual.

To set a suitable tone, and to avoid legitimizing conflicted leadership structures, the Commission should waive the disclosure requirement for corporations that separate the two roles. That is the appropriate leadership structure, and it needs no justification. In this way, the proposed amendment would be a vehicle for companies with conflicted leadership structures to acknowledge the fact and provide an explanation for shareowners.

We do not believe the proposed disclosures regarding the board's role in risk management are appropriate or useful. By focusing exclusively on risk taking, the proposed disclosure is likely to distract attention from other potentially abusive practices within the company—many of which contributed more to the recent market crisis than did "excessive risk taking." Furthermore, in our experience, lines on an organizational chart have little or no bearing on the effectiveness of an organization in taking or otherwise managing risk. As most any business consultant will acknowledge, there are official organization charts, which are lines on a sheet of paper, and there are effective organizational charts, typically unacknowledged, that reflect how reporting actually works within an organization. Disclosures about official organization charts will tell shareowners little or nothing about a board's involvement in risk management.

What our experience indicates is that personal commitment on the part of individual board members to manage risk is essential to any risk management process. Any board can go through the motions of managing risk. Only some actually roll up their sleeves and do a meaningful job at it. The proposed disclosure will provide shareowners no means of distinguishing the former from the latter.

We do believe that alternative forms of reporting on a company's risk or risk management practice could be valuable. However, reporting on these matters without some form of personal accountability will likely be useless. As indicated in our response to Question A1.5, a comprehensive report signed by the principal executive officer and CFO for inclusion in the 10-K could be highly informative, if the principal executive officer and CFO were held personally liable for omissions in that report that come to light as a result of subsequent unanticipated losses.

In our experience, such individual accountability is extremely important for risk management. Where there is "group accountability," organizations often just go through the motions.

D. New Disclosure Regarding Compensation Consultants

In 2006, the Commission amended Regulation S-K item 407 to require companies to describe, among other things, any role played by compensation consultants in determining or recommending the amount or form of executive and director compensation. Many compensation consultants, or their affiliates, offer additional services, such as benefits administration, human resources consulting and actuarial services. The provision of such additional services may create a conflict of interest, which calls into question the objectivity of the consultants' executive pay recommendations. For this reason, the Commission is proposing amending item 407 to require that, if a company employs a compensation consultant to advise on executive or board compensation, it must disclose if that consultant or its affiliates provide additional services. If it or its affiliates do, all fees paid to it and the affiliates would have to be disclosed.

In drafting this letter, no other item generated the controversy or debate among our co-signers that this one did. We will not attempt to present a unified response to this item. Instead, we will provide statements by four of our co-signers that illustrate the breadth of opinion on this matter. One thing that should be eminently clear is that compensation consultants are controversial.

We will start with a statement generally supporting the Commission's proposal. It was submitted by Jim McRitchie of corpgov.net:

> We support the Commission's proposal to require more disclosure of fees paid to compensation consultants that also provide additional services to management. Although potential conflicts of interest occur not only at firms with existing overlapping contracts but also at any firm that offers services to both companies and boards. Any such consultants have an incentive to recommend overpayment of executives in order to be favored with future contracts from management. Disclosure should include the nature of all services provided to the board or management and fees paid (including type: i.e., cash, stock, or stock options), and whether the board or compensation committee approved the provision of the services.
>
> We do not recommend a "threshold" for fee disclosure, since that encourages artificial manipulation of fee levels. The time period covered by the disclosure should include the preceding five actuals, as well as coming five years estimated, if any services are contemplated, in order to capture situations where services are not provided in the same fiscal year but could still raise conflicts of interest. This at least would begin to address the situation where contracts by both boards and management are not yet in effect but are contemplated. While banning consultants from providing services to both the board and management may be impractical, at least more complete disclosure may help curb abuse.

Alexander Krakovsky of lemonjuice.biz is generally supportive of Jim McRitchie's position, but he recommends stronger disclosures:

> Boards engage compensation consultants mostly to provide comparisons with other companies' compensation practices. The "thinking" behind this comparison is that the company needs to be competitive in compensating the executive. However, this is silly because most top executives are promoted from within and the competition for the positions is limited. **What compensation consultants do not really do well or at all is the analysis of what is the appropriate incentive structure for the company that will maximize shareholder value.** While insiders scream that "one size does not fit all," they do exactly that with compensation consultants. Keeping up with the Joneses is the name of the game, regardless of how thoughtless or irrelevant compensation structures in other firms are. And this is why everyone jumps off the cliff at the same time.
>
> For the above reason, I believe that compensation consultancy disclosure needs to be expanded to include:
>
> 1. Information about all compensation consultants retained, and not just the one upon whose analysis they finally relied upon.
>
> 2. All CC engagement letters and final recommendations should be made public. (Yes, that means no limited use or confidentiality provisions in CC engagements, thought the part of the actual analysis that deals with company's confidential information should be left out).
> 3. There should be specific disclosure regarding what recommendation compensation consultants made regarding the company's appropriate incentive structure. Certainly, the answer can be "none." However, this answer would be just as informative as any.
>
> I feel that compensation consultants need to be put on trial. As much as we like to just ignore them, the only way to expose this practice is through more disclosure.

Our executive director Glyn Holton believes the Commission should not require any disclosures related to compensation consultants because doing so only legitemizes them:

> We believe that compensation consultants who advise boards on executive and director compensation are inherently conflicted. While we might hope that they make recommendations that are in the best interests of shareholders, they are hired by and are answerable to boards. If a board's intentions for executive or director compensation are at odds with the best interests of shareowners, compensation consultants have little choice but to fall in line. Otherwise, they are soon *out-of-work* compensation consultants.

> In setting executive or director compensation, boards want to know how other companies similar to their own compensate executives and directors. They turn to compensation consultants to conduct compensation surveys. Armed with the results, boards routinely decide that, to remain "competitive," they should compensate their executives and directors more highly than do most of the companies in their survey. With most companies going through this process annually, companies continually leapfrog one another, granting their executives and directors ever more lavish compensation.
>
> Compromised as they are, compensation consultants are powerless to halt this abuse. They are incapable of playing a legitimate role in corporate governance. Boards may hire them for whatever purposes they choose, but shareowners can never trust their recommendations.
>
> In this light, we think it unfortunate that the Commission acknowledged a corporate governance role for compensation consultants in the 2006 amendments to Regulation S-K. It would be unfortunate for the Commission to do so again with these latest proposed amendments. By requiring disclosures related to compensation consultants, the Commission implies that these consultants have a legitimate role to play, and that—with suitable disclosures and monitoring—they can play it honestly, without bias, and in the best interests of shareowners. This is patently false.
>
> To avoid inappropriately legitimizing a role for compensation consultants in corporate governance, we recommend that the Commission not implement the proposed disclosures related to compensation consultants and remove all mention of compensation consultants from existing rules.

Finally, Steve Nieman, president of the Ownership Union, supports Glyn Holton's position, but with insights of his own:

> Just as important as what goes in is what's left out.
>
> The problems these days are people and institutions seem to think that everything should be included — more disclosure — and the economic world will right itself.
>
> I disagree.
>
> Management paid consultants will NEVER disclose what they do no matter if the SEC or any power thinks they can force them. They and their attorneys will find ways around any regulations (laws are made to be broken, right?)

The other important point is that we have to find simple solutions to problems without holding a gun to somebody's head, because in America, we don't do things that way. (Plus, it's acutely non-productive over the long term).

There are already numerous disclosure requirements for management pay. Through 10Qs, 8Ks — and shareholder activists — the word will get out about how ridiculous management over-compensation has become. In fact, it is bankrupting companies. Through stock options and stock grants, many management teams are stealing 10% of a company's wealth every year. After ten years, that's 100% of the company's worth.

This is NOT lost on people representing "old money" or savvy pension investors. This new breed of Chairman/CEO, COO, CFO, senior VP, etc. is a new elite class of businessmen who are literally robbing the planet's economic future.

But let them. It won't get better until it probably gets a lot worse.

If the SEC Commissioners could see how intelligent it would be to remove any reference to a "governance role for compensation consultants," this would be an important signal that the basic "rules of engagement" are changing, IMO. Government can't fix this problem; only people working in the field can.

The root cause of excessive management compensation is that there are no accountable representatives of stakeholders on the boards of most large stock companies. These stakeholder reps, if they could gain governance seats on board compensation committees, would NEVER agree to this insane process. This is where I'm spending more of my time.

So I agree with Glyn's position.

This is an important topic, and I'm glad it's addressed again in this most recent letter.

As we all know, Life and its spontaneous way of intelligently working can be relied upon as a wise guide to help organize human affairs. Unfortunately, there appear to be legions of arrogant humans who think Mother Nature must conform to human behavior, and not the other way around.

You can't force someone to love you. You can't force someone in power to "get religion," or NOT take advantage of those numerous levers they can pull and push to commit almost invisible fraud. What you can do is empower common stakeholders so that they can erect simple infrastructure changes as well as broaden communication channels to help prevent unaccountable concentrations of power, which breeds unacceptable deterioration of the commonwealth.

E. Reporting of Voting Results on Form 8-K

Currently, results of shareholder votes are reported in the 10-K or 10-Q. This means that, depending on when a shareholder meeting takes place, several months could transpire before a vote's results are reported. Accordingly, the Commission is proposing that vote results be reported instead in an 8-K within four business days of a vote. If vote results cannot be finalized within four business days, companies would disclose on Form 8-K the preliminary voting results within four business days after the preliminary voting results are determined, and file an amended report on Form 8-K within four business days after the final voting results are certified.

We strongly support this proposal. As one example of how it might benefit shareowners, we can cite FirstEnergy. Shareowners of that firm have been conducting withhold vote campaigns against its directors. At firms that don't have majority voting, such as FirstEnergy, withhold vote campaigns can only embarrass directors. Without publicity, they are ineffective (even with publicity, they are largely "pushing on a string." But that is a different matter.). At this year's FirstEnergy meeting, several directors received majority withhold votes. There were a number of news organizations at the meeting, but the director vote counts were not reported at the meeting. Three months passed before the company reported its full vote totals. By that time, the media had lost interest, so the successful withhold vote campaign did not attract media attention.

We are concerned that companies will be allowed to wait until four days after preliminary results are prepared to report those preliminary results. If this is how the final rule reads, we anticipate companies will take a fine long time preparing those preliminary results. At the end of a shareowners meeting, a company will have *some* preliminary results. We recommend that they be required to disclosure *those preliminary* results within four days of the shareowners meeting.

We appreciate this opportunity to comment. We hope our feedback is helpful, and we welcome an opportunity for further dialogue on these important issues. Our executive director, Glyn Holton, can be reached at (617) 945-2484 or mail@glynholton.com.

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