Marc Hodak

May 18, 2011

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F. Street, NE
Washington, DC 20149-1090

Re: File Number S7-13-11, Listing Standards for Compensation Committees

Dear Ms. Murphy,

I am writing on behalf of Hodak Value Advisors, LLC. We advise investors and boards on performance measurement, incentive compensation, and related governance issues. I personally have been working with client firms on these matters for eighteen years, and have been teaching corporate governance at the New York University's Leonard N. Stern School of Business for the past six years. In addition to our work advising companies, we conduct and review research to better understand the relationship between various compensation structures and total shareholder returns. This research both supports our work with clients and is used by securities analysts and asset managers to determine the quality of management alignment at firms in which they invest. We provide independent advice to our clients, and approach our compensation governance responsibilities holistically with regards to owners' interests. In this context, we respectfully offer our views on the proposed changes to Section 10C to the Securities and Exchange Act of 1934 mandated by Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. We address your specific requests for comments as follows:

Section 10C(b) specifies that the independence factors identified by the Commission must be competitively neutral, but does not state how we should determine whether a factor is competitively neutral. Are there any issues that should be considered to determine or assess whether a factor is competitively neutral?

Are the five factors identified in Section 10C(b) of the Exchange Act competitively neutral among different types of compensation advisers? If not, what modifications or adjustments should be made in order to make these factors competitively neutral? Are there specific categories of compensation advisers that would be adversely affected by the compensation committee's use of these factors to assess independence?

The law, in effect, forces the Commission to trade off the goal of greater adviser independence against a goal of protecting a particular class of incumbent advisors against competitors (e.g., multi-line firms vs. boutique firms), new entrants and other competitive threats. Since there is no way to rationally reconcile or balance these goals when they come into conflict, we suggest that the Commission generally recommend factors that, when applied equally across the full spectrum of existing firms, help in achieving the goal of advisor independence, which is the ultimate intent of the law, i.e., factor-by-factor neutrality. In any case, the full effects of these or any factors upon competition in the rapidly evolving advisory industry are not entirely knowable, and therefore shouldn't drive attempts by the Commission to anticipate or resolve them all, nor should the Commission allow itself to be used as an instrument to either endanger or protect any particular industry structure in a way that does not serve the interests of shareholders.

The only alternative to factor-by-factor neutrality would be either to compromise on the goal of adviser independence, or to adopt some individual factors irrelevant to adviser independence, but that help preserve the existing structure of the advisory industry. We suggest that "percentage of fees-to-firm-revenue" falls in the latter camp. In our experience, adviser independence is far more a function of revenue concentration at the firm *partner or manager* level than at the *employer/firm* level. We note that Arthur Anderson wasn't saved because Enron was a relatively minor part of their overall firm revenues; they were doomed because Enron was such a large portion of one Houston partner's revenues.

Are there any factors affecting independence that we should add to the list of factors identified in proposed Rule 10C-1(b)(4)? If so, what are they and why should they be included?

If the Commission must retain the fees-to-firm-revenue factor, it should consider allowing boards to alternatively consider a partner-level percentage of fees-to-revenues-managed. Furthermore, it should preserve compensation committee discretion to determine the independence of their adviser without numerical thresholds or limits that might deprive shareholders of the best available advice.

Would the existence of a business or personal relationship between a compensation adviser and an executive officer of the issuer be relevant in considering whether to engage the compensation adviser? If so, why? Should we add this to the required list of factors that must be considered?

Based on the language in Section 10C(b)(2), which distinguishes between the adviser and the person that employs the adviser, a personal or business relationship between the person employing the adviser and a member of the compensation committee would not be covered by the proposed rule (which, like Section 10C(b)(2)(D), only refers to relationships between the adviser and the compensation committee). Should the required list of factors also include a business or personal relationship between the person employing the compensation adviser and a member of the compensation committee? Along those lines, should it also cover a business or personal relationship between the person employing the adviser and an executive officer of the issuer?

A relationship between an adviser and an executive officer may be relevant, and ought to be considered by the compensation committee. However, mandating that such a factor be considered, especially if there were any bright line standards associated with such consideration, could penalize experience and competence. The most experienced advisers in a given industry are more likely to have developed extensive relationships over the course of their careers. The most competent are more likely to have their services referred among executives and directors, including those holding each role in different companies. This is especially true in sectors where executives easily move between private equity, as investor representatives or operating partners working alongside advisers, and public companies, as senior executives whose compensation committees might hire those same advisers. Furthermore, positions and relationships are not static. What would a company do if it hired an executive that had previously worked with its current adviser?

These caveats are especially important with respect to employer-level relationships; any firm populated with reasonably experienced and competent advisers will have a network of relationships that, if made an explicit independence factor, could seriously impair their ability to work with a significant number of clients in a given sector.

Should we provide materiality, numerical or other thresholds that would apply to whether or when the independence factors must be considered by a compensation committee? If so, what should they be? For example, should we require consideration of stock ownership only if the amount of stock owned constitutes a significant portion of an adviser's net worth, such as 10%?

We strongly agree that the Commission should avoid specifying bright-line numerical thresholds—or limits—for any factors that the compensation committee must consider. Such numbers will be inherently arbitrary compared to the judgment of independent directors conscientiously weighing all of the considerations that apply to their situations. We do, however, suggest a qualitative threshold with regards to revenue concentration (percentage of fees-to-revenue), i.e., that this factor need not be considered *at all* in the case of advisers *not* making recommendations with regards to director pay.

Logic would suggest that *independent directors* have no reason to seek or accept biased advice with regards to *executive pay* regardless of their adviser's concentration of fees from a particular client. Indeed, the more dependent an advisor is upon a particular committee's business, the more responsive they are likely to be to that committee in their best efforts to fulfill their fiduciary duties. Even in the extreme case of an adviser with 100 percent revenue concentration, i.e., a full-time adviser on the committee's payroll and serving at the committee's pleasure, one would have no reason to expect that such an adviser would provide compromised advice with regards to *executive pay*. The only potential source of bias of an adviser serving an *independent* compensation committee would be with regards to *director pay*. Thus, the requirement that a fee-to-revenue percentage be considered by the compensation committee should apply only with respect to advisers that are providing or have provided recommendations on *director pay*.

Should we clarify what is covered by "provision of other services" in proposed Rule 10C-1(b)(4)(i)?

The Commission should clarify that additional work on organizational incentives consistent with executive incentives should not count toward "other services," even if they are nominally paid for outside of the compensation committee's 'budget.' Shareholders benefit from a consistent set of incentives up and down the organization, even if somewhat different metrics or compensation structures may apply to employees below the senior executive level. The creator of senior executive incentives is likely to be in the best position to implement such a consistency across the organization, which implementation may cost as much as, or more, than the original executive incentive plan implementation. All costs of incentive plan implementation should be considered as executive compensation for these purposes, as long as the compensation committee is involved in the decision to hire the adviser for overall incentive plan implementation.

We interpret "any stock of the issuer owned by the compensation consultant, independent legal counsel or other adviser" in proposed Rule 10C-1(b)(4)(v) to include shares owned by the individuals providing services to the compensation committee and their immediate family members. We do not believe this factor is intended to extend to the person that employs the adviser since Section 10C(b) is specific when factors extend to the employer and that language is not included for stock ownership. Is this an appropriate interpretation of this factor? If not, why and how should this phrase be interpreted? Should it also cover the person that employs the adviser?

This provision should cover the adviser employer only if its holdings are significant enough to enable the employer to influence a board of directors in their selection of advisers.

Should we define or clarify the meaning of the phrase "business or personal relationship," as used in proposed Rule 10C-1(b)(4)(iv), and if so, how?

The Commission should clarify that the business or personal relationship to be considered are those relationships *outside* of compensation advisory work. Shareholders benefit from quality of advisory work judged by many factors besides independence. The best way for directors to know the quality of an adviser is from personal knowledge of their work and effectiveness.

Would the proposed requirements have any unintended effects on the compensation committee or its process to select a compensation adviser? If so, please explain.

Based on the history of compensation regulation, these rules will likely have myriad unintended effects, many of which may not be known at this time.

- A significant application of the fee-to-firm-revenues factor would likely force a consolidation of smaller compensation advisory firms, without adding anything to the independence of advice to compensation committees, as discussed earlier.
- Any bureaucratic hurdles associated with these factors will also raise the fixed costs of supplying advisory services, favoring larger firms, and creating a greater urgency to retain individual clients in order to cover those fixed costs, potentially hurting their independence.
- An aggressive application of the "personal or business relationship" standard would penalize advisers known from the experience of directors to provide superior service, which could hurt the company and its owners. This could be especially detrimental to shareholders since any executive compensation costs saved as a result of a more independent adviser could easily be lost many times over as a result of poor incentives designed by an otherwise less capable adviser.
- Aggressive application, or misapplication, of the stock ownership factor could preclude cash-starved companies from paying good advisers in stock, or from hiring advisers who are otherwise personally aligned with the interests of the shareholders.
- The overwhelming unintended effect will be to raise the costs of providing and obtaining compensation advisory services to public corporations, costs that will ultimately be borne by shareholders, as a result of increased bureaucratization of adviser selection, the need to document and possibly disclose the selection process, and the decision to avoid certain advisers with valuable competencies due to factors that may not be relevant to a particular issuer at a particular time.

The clearest evidence for the latter result is the already large and growing difference in costs for given compensation advisory services between public and private companies.

Should we adopt rule amendments to Regulation S-K to require listed issuers to describe the compensation committee's process for selecting compensation advisers pursuant to the new listing standards? Would information about the compensation committee's selection process – how it works, what it requires, who is involved, when it takes place, whether it is followed – provide transparency to the compensation adviser selection process and provide investors with information that may be useful to them as they consider the effectiveness of the selection process? Or, would such a requirement result in too much detail about this process in the context of disclosure regarding executive compensation?

In light of rules requiring the independence of compensation committee members, it's difficult to see what such additional disclosure would provide to the shareholders, other than lengthen an already dense disclosure—with the effect of reducing transparency—and further bureaucratizing the selection of every adviser. If the compensation committee is truly independent, then investors should trust that the committee would choose a good adviser. If the committee's independence is suspect, there will be nothing discernable in disclosure of a selection process that would indicate a poor choice.

We close our comments by suggesting that some of the problems that we are trying to avoid would actually help our firm. Since we have relatively fewer connections across larger companies in the public universe, we would benefit from discouragement of compensation committees hiring advisers with whom they have a personal or business relationship. Although we are open to receiving stock in lieu of cash for our services, we don't tend to own the stock of our clients except through index funds. Although as a boutique firm we sensitive to revenue concentration as a factor, we have been around for nine years, and are reasonably diversified among clients. Instead, our comments are driven by our conviction that an adviser to boards is best able to grow by serving their clients well in fulfilling their fiduciary responsibilities, and that no firm should be penalized for being successful in this endeavor.

I would be pleased to discuss or explain any of these comments, if the Commission wishes, at the contact information provided below.

Sincerely,

Marc Hodak
Hodak Value Advisors
212-877-1297
mhodak@hodakvalue.com