



December 7, 2012

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

[Via e-mail: rule-comment@sec.gov](mailto:rule-comment@sec.gov)

**Re: Proposed Rule Change by the NASDAQ Stock Market LLC to Modify the Listing Rules for Compensation Committees to Comply with Rule 10C-1 under the Exchange Act and Make Other Related Changes (Release No. 34-68013; File No. SR-NASDAQ-2012-109)**

Ladies and Gentlemen:

The Society of Corporate Secretaries & Governance Professionals (the “Society”) appreciates the opportunity to provide comments to the Securities and Exchange Commission (the “Commission” or “SEC”) on the above-referenced rule proposal (the “Proposal”) by the NASDAQ Stock Market LLC ( “NASDAQ”). The Proposal has been proposed in order to comply with Section 10C of the Securities Exchange Act of 1934 (“Exchange Act”) and Rule 10C-1 thereunder, adopted to implement Section 952 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”).

Founded in 1946, the Society is a professional membership association of more than 3,000 corporate secretaries, legal counsel and other governance professionals who serve approximately 2,000 companies of almost every size and industry. Society members are responsible for supporting the work of corporate boards of directors and their committees and the executive managements of their companies regarding corporate governance and disclosure. Our members generally are responsible for their companies’ compliance with the securities laws and regulations, corporate law, and stock exchange listing requirements.

The Society generally supports the Proposal and appreciates NASDAQ’s efforts in this regard. However, we believe that certain aspects of the Proposal are unnecessarily burdensome or are not sufficiently clear, and therefore will likely result in practical issues and/or inconsistent administration that may fail to fulfill the objectives of Section 952 of the Dodd-Frank Act. Accordingly, we believe that the Proposal should be amended to address these matters before being approved by the Commission. Our detailed comments follow.

## **I. Compensation Committee Director Independence Requirement**

*The Proposed Independence Standard for Compensation Committee Members Is Overly Prescriptive and Should Be Revised.*

The Proposal provides that compensation committee members must not accept directly or indirectly *any* consulting, advisory or other compensatory fee, other than for board service, from a company or any subsidiary thereof. NASDAQ states that this is the same as its rule for audit committee members. We see no reason why the bright-line test for audit committee members should be applied to determining the independence of compensation committee members. The independence requirements of Rule 10A-3 under the Exchange Act, “Listing standards relating to audit committees,” differ from the independence requirements of Rule 10C-1 with respect to fees paid by the company to a director for consulting or advisory work. Specifically, Congress expressly imposed a strict prohibition against audit committee members accepting such fees under the Sarbanes-Oxley Act of 2002; therefore, the Commission had no choice but to impose this bright-line test in Rule 10A-3. In contrast, Congress did not impose any such blanket prohibition in the Dodd-Frank Act, and the Commission opted not to do so in Rule 10C-1. Rather, Rule 10C-1 merely deems such source of compensation a “relevant factor” to be considered in determining independence. We believe this distinction is important and should be reflected in NASDAQ’s rules.

We believe that the approaches taken by Congress and the SEC under the Dodd-Frank Act on this issue are appropriate and that compensation committee members who accept consulting, advisory or other compensatory fees from a company that are not in excess of \$120,000 during any period of twelve consecutive months within the three years preceding the determination of independence should not automatically be prohibited from serving on such compensation committees. Accordingly, we believe a blanket prohibition is inappropriate and that a better approach is to have a company’s board of directors consider such consulting or advisory fees in making its determination as to whether the member’s receipt of such compensation would, in the opinion of the board, interfere with the member’s exercise of independent judgment in carrying out the director’s responsibilities as a member of the compensation committee.

This is important to companies that seek to maximize the contributions of their directors, in general, and compensation committee members, in particular. For example, a board member may have a particular expertise in an area that the company needs. That expertise may even have been considered by the company’s corporate governance and nominating committee, for example, in reaching its decision to nominate the director in the first instance. As long as the compensation is properly limited, as determined by the board, the company should be able to engage a director in a consulting or advisory capacity without suffering automatic disqualification of that independent director from serving on the company’s compensation committee.

We are particularly concerned that this absolute prohibition would disproportionately impact small- and mid-cap companies, whose boards tend to be smaller and who have fewer resources to engage non-employee advisors and consultants.

## II. Compensation Committee Advisors

### *The Proposed Independence Assessment for Compensation Committee Advisors Is Vague and Should Be Clarified.*

Exchange Act Rule 10C-1(b)(4) provides that “The compensation committee of a listed issuer may select a compensation consultant, legal counsel or other adviser to the compensation committee only after taking into consideration the following factors, as well as any other factors identified by the relevant national securities exchange or national securities association in its listing standards.” This provision reflects the Commission’s determination that information gathered from an independence assessment of these categories of advisers will be useful to the compensation committee as it considers any advice that may be provided by these advisers. While we recognize this objective, we note that the required independence assessment will be time-consuming and burdensome due to the scope of information that will need to be gathered in order to conduct the required independence assessment. Uncertainty over the scope of the requirement could have a counterproductive effect of discouraging compensation committees from obtaining the advice of advisers subject to the rule, particularly in situations where quick action is required of the compensation committee. Accordingly, we believe that there should be greater clarity around this new standard.<sup>1</sup> We identify below certain fundamental issues that we believe the Exchange should address so that companies, their compensation committees and advisers can know how to satisfy the listing requirement.

- NASDAQ should confirm and clarify that the independence assessment is required only with respect to advisers who are providing advice on executive compensation.<sup>2</sup> In this respect, the linchpin of the Commission’s definition of “compensation committee” is the committee whose members “oversee executive compensation matters.” If a company determines to assign other responsibilities to its compensation committee, such as the determination of director compensation or oversight of broad-based retirement plans, persons who provide advice to the committee on such additional matters should not be subject to the required independence assessments. Otherwise, boards will be forced to pursue form over substance

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<sup>1</sup> Our members have observed that the stock exchanges appear to be reluctant to issue interpretive advice regarding listing standards that are mandated by SEC rules. For example, the Exchange has not published any interpretations regarding the listing standard for the independence of audit committee members mandated under Exchange Act Rule 10A3-(b). We believe that the stock exchanges are well positioned to interpret how these standards should be applied in the context of companies whose securities they list, particularly in the context of standards adopted under Exchange Act Section 10C, where Congress provided for flexibility in the implementation of the new listing standards, and therefore that the SEC should encourage the stock exchanges to provide interpretive guidance regarding these listing standards, both at the time of adoption and thereafter.

<sup>2</sup> For example, the Exchange could revise proposed Rule 5605(d)(3)(iii) to read, “responsibility to consider certain independence factors before selecting such advisers, other than in-house legal counsel, to provide advice to the compensation committee on executive compensation.”

by moving those additional responsibilities to other board committees in order to avoid the burden of conducting an independence assessment as to advisers addressing matters that do not relate primarily to the compensation of the company's executives.

- NASDAQ also should confirm, either in the text of its rules or in commentary or interpretive guidance, that not all persons who provide services to a board compensation committee are deemed to be providing executive compensation advice. For example, we understand that a consultant whose services for a compensation committee are limited to providing information, such as surveys, that either is not customized for a particular company, or that is customized based on parameters that are not developed by the compensation consultant, should not be considered as providing advice to the compensation committee merely as a result of providing such survey data.<sup>3</sup> Similarly, actuaries, in-house human resources staff and others who provide information or make recommendations to a compensation committee, even if relating to executive compensation, should not as a result of such actions alone be deemed persons who "provide advice" to the compensation committee.
- Because Section 10C and the rules adopted pursuant to it create a distinction between the "compensation consultant, legal counsel or other adviser to the compensation committee" and the "the person that employs the compensation consultant, legal counsel or other adviser," the Exchange should clarify that references to the "compensation consultant, legal counsel or other adviser to the compensation committee" refer only to the individual person(s) who are responsible for providing the advice to the compensation committee (for example, an engagement partner) and not to all other persons who may work under the supervision of or provide input to that person. Typically, a consultant or other adviser will consult numerous sources and obtain the views and input of numerous other individuals in developing the advice that is provided to a compensation committee. Nevertheless, the compensation committee looks to and relies upon the judgment and experience of the person actually providing advice to it when evaluating executive compensation decisions. Accordingly, the Exchange should confirm, either in the text of its rules or in commentary or interpretive guidance, that the independence assessment need only address that individual when assessing whether the compensation adviser can provide independent advice to the compensation committee.
- Finally, the Exchange should address and provide guidance on how often the required independence assessment must occur. Many compensation committee consultants and other advisers attend and provide advice at each meeting of the compensation committee, including the many telephonic committee meetings that in our experience typically occur during the year. It will be extremely burdensome and disruptive if prior to each such meeting, the

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<sup>3</sup> See, for example, the SEC's statement in Exchange Act Rel. No. 61175 (Dec. 16, 2009), noting the distinction between providing services and providing advice when the SEC stated that the compensation committee fee disclosure rule for consultants who supply survey data "would not be available if the compensation consultant provides advice or recommendations in connection with the information provided in the survey."

committee had to conduct a new assessment. NASDAQ should confirm, either in the text of its rules or in commentary or interpretive guidance, that an annual assessment of independence is sufficient, and that thereafter during the following year a new assessment is necessary only if the adviser or the company learns of a material change in circumstances that is reasonably likely to affect the adviser's independence.

We expect that additional interpretive questions will arise under the listing standard requiring the compensation committee to assess the independence of each compensation consultant and other adviser that provides advice to the committee. Because Section 10C and Rule 10C-1 recognize that the exchanges are in the best position to assess how the statutory mandates should apply to their listed companies and provide the exchanges discretion in how the statutory mandates are implemented, we request that the SEC encourage the exchanges to provide appropriate on-going interpretive advice on the application of the adviser independence assessment rules.

### **III. Cure Periods**

*The Cure Provision Should Address Compliance with Each Requirement under the Listing Standard as Required under Section 952 of the Dodd-Frank Act.*

As required by Exchange Act Section 10C(f)(2), Rule 10C-1(a)(3) provides that the listing rules adopted by the exchanges "must provide for appropriate procedures for a listed issuer to have a reasonable opportunity to cure any defects" in compliance with the rules (emphasis added). We support the rule proposed by the Exchange to permit issuers a period of time to cure failures to comply with the requirements as a result of a vacancy or if one member of the compensation committee ceases to be independent for reasons outside the member's reasonable control. However, to fulfill the statute, NASDAQ also should provide an opportunity to cure any other form of non-compliance with these new rules. This is particularly true in the context of the requirement that the committee may obtain advice from a consultant or adviser only after assessing that individual's independence. Inadvertent violations of this requirement could arise, for example, if a person is appearing before a compensation committee solely to provide information or other services, and the individual then on a solicited or unsolicited basis makes a statement that could be viewed as providing advice on executive compensation. In the absence of a cure mechanism, the company would be in violation of the listing standard and have no recourse.

Accordingly, in addition to addressing situations where a compensation committee member fails to comply with the independence requirements, we believe NASDAQ should permit a cure period for any other form of non-compliance with the listing standards mandated by Rule 10C-1(a)(3). Thus, a company should be allowed to take corrective action within a reasonable time after the company's senior executives learn of the non-compliance. In the case of the requirement to conduct independence assessments of compensation committee advisers, a reasonable time for curing a violation should be review of the adviser's independence no later than three months after the company learns of the non-compliance. This cure period will allow sufficient time to conduct an appropriate inquiry and due diligence into the required independence factors, and for the committee to review and consider the information identified as a result of that inquiry.

Additionally, we believe that a company relying on the opportunity-to-cure provision regarding defects in the composition of compensation committees should be required to provide notice to NASDAQ “promptly” rather than “immediately” upon learning of the event or circumstance that caused the noncompliance. This subtle distinction would give companies ample time to analyze the situation presented and report it accurately.

#### **IV. Date of Effectiveness**

##### *More Time Should Be Provided to Comply with the New Listing Standard.*

NASDAQ proposes that its Listing Rule 5605(d)(3), which would require compensation committees to have the specific responsibilities and authority necessary to comply with Rule 10C-1(b)(2), (3) and (4)(i) – (vi) under the Exchange Act, be effective immediately. NASDAQ has also proposed that companies must comply with the remaining provisions of the amended listing rules by the earlier of: (1) their second annual meeting held after the date of approval of this proposal; or (2) December 31, 2014.

We support the transition period for compliance with the new compensation committee independence standards but believe that the Exchange should provide a longer period for companies to satisfy proposed Listing Rule 5605(d)(3). These provisions are not required to be adopted in a homogenous fashion by all companies; rather, each company is free to develop its own specific guidelines and language on the responsibilities and authority of its compensation committee. This process should receive the proper attention of the boards of directors that are tasked with the responsibilities of formulating the guidelines and charters. Consequently, the Society requests that companies have until the first fiscal year beginning on or after December 27, 2013 in order to comply with the new listing rules. We expect that during this transition period most companies will hold at least two board meetings, which would provide an adequate opportunity for companies’ boards to consider and approve any changes necessary to satisfy the new standards. We believe that such time would tend to encourage best practices to develop for the individual companies.

**Summary**

Again, we appreciate the time and effort put into the proposed rules by the Staff of the Division of Corporation Finance of the Securities and Exchange Commission and the rulemaking staff the Office of the General Counsel of NASDAQ. We support the rules as proposed, subject to the suggestions made in this letter.

Respectfully submitted,

A handwritten signature in black ink, appearing to be 'R. Lamm', with a stylized loop at the end.

Robert B. Lamm,  
Chair, Securities Law Committee  
The Society of Corporate Secretaries & Governance Professionals

cc: Mary L. Schapiro, Chairman  
Luis A. Aguilar, Commissioner  
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