Davis Polk

ADDITIONAL COMPENSATION AND CORPORATE GOVERNANCE DISCLOSURE REQUIREMENTS FOR 2010 PROXY SEASON

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On July 10, 2009, the Securities and Exchange Commission (SEC) issued a proposed rule that would amend the compensation disclosure requirements in Regulation S-K. The SEC anticipates that the following changes would become effective for the 2010 proxy season:[1]

- Reporting in the Summary Compensation Table and Director Compensation Table the aggregate grant date fair value of equity awards for the year of grant, rather than the amount recognized each year for financial statement reporting purposes, which generally allocates the value of equity awards over several years according to their vesting schedules.
- A new section in the Compensation Discussion and Analysis (CD&A) discussing and analyzing if and how risks arising from a company's employee compensation programs could have a material effect on the company.
- Disclosure of services unrelated to executive or director compensation provided by compensation consultants and their affiliates and fees paid for such services.

The more significant implications of these new compensation requirements are the following:

- Reporting the aggregate grant date fair value of equity awards could change the identities of a company's named executive officers in the 2010 proxy. For companies that have received TARP assistance, this could also change the identities of the individuals subject to the TARP compensation restrictions that apply to their named executive officers (*e.g.*, bonus restrictions, prohibition on golden parachute payments).[2]

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[1] On July 1, 2009, the SEC held an open meeting at which it voted unanimously to adopt the proposed rule. For a summary of the actions taken by the SEC at the meeting, see our client newsflash entitled SEC Eliminates Broker Discretionary Vote for Director Elections in 2010, Proposes "Better" Proxy Disclosures and Codifies TARP Recipients "Say on Pay", dated July 1, 2009.

[2] For a summary of the compensation requirements applicable to TARP participants, see our client memorandum entitled Treasury Regulations Governing Compensation for TARP Participants, dated June 17, 2009.

- The new CD&A compensation risk section would apply to programs covering any employees, not just executive officers. Many compensation committees may be required to expand their focus beyond what, for most committees, has traditionally been limited to executive compensation, and beyond what is required of committees under the NYSE and Nasdaq rules.

- The expanded disclosure relating to compensation consultants, which is intended to address such consultants' perceived conflicts of interest, may lead more companies to engage different compensation consultants to provide executive and director compensation services and broader benefits services.

In the preamble to the proposed rule, the SEC poses a series of questions relating to each of the new compensation requirements and compensation generally (see Appendix A for these questions). The SEC invites comments on these questions and the proposed rule generally. The comment period will remain open through September 15, 2009.

The proposed rule also would amend several requirements relating to corporate governance disclosure and the proxy solicitation rules. For a brief summary of these requirements, see page 6.

Equity Awards

Current Rule

In 2006, the SEC amended Item 402 to require companies to disclose in the Summary Compensation Table and Director Compensation Table the dollar amount of equity awards recognized for financial reporting purposes for each fiscal year in accordance with FAS 123R. For example, if on January 1, 2008 a named executive officer was granted a stock option that vested over three years and had an aggregate grant date fair value of $300,000, the company was required to disclose in the Option Awards column of the Summary Compensation Table for 2008 the amount expensed with respect to the award for 2008, generally $100,000 (*i.e.*, $300,000 ÷ 3 years = $100,000), plus the aggregate amount expensed in 2008 with respect to each option or similar award granted to the officer in previous years.

Companies and investors have criticized the current rule for creating confusing disclosure having odd results. If, for example, the named executive officer described in the previous paragraph was retirement-eligible on the grant date and the grant became fully vested upon eligibility for retirement, the award would be treated as vested for accounting purposes on the grant date and the entire $300,000 expense would be disclosed for 2008. As a result, the executive would appear to have received an award having three times the value of an otherwise identical award received by a non-retirement-eligible colleague.

Another odd result of the current rule is that certain awards could result in the disclosure of a negative number in the applicable column—for example, due to the reversal of charges upon the forfeiture of a service vesting award on termination of employment. Moreover, the current rule could result in the disclosure of a positive number in the applicable equity award column even if the named executive officer did not receive any equity awards in that year—*i.e.*, with respect to an award granted in a prior year that continued to vest in the year for which the disclosure was made.

Proposed Rule

The proposed rule would amend Item 402 to provide that, under the example above, the company would report in the Summary Compensation Table for 2008 the $300,000 aggregate grant date fair value of the option award and would not report any amount with respect to grants made in prior years. The SEC explains that it has proposed the change because, in making voting and investment decisions, shareholders generally consider compensation decisions made during the fiscal year, which are generally reflected in the full grant date fair value, and not the amount recognized for financial statement purposes.

Because the amount of total compensation is used to determine which three executive officers—in addition to the chief executive officer and chief financial officer—are included in the Item 402 tables, the full grant date fair value is more likely to lead to the inclusion in the tables of the executive officers that the company intends to compensate most highly. For example, under the current rule, if in 2008 executive officer A was granted an option with an aggregate grant date fair value of $600,000 that vests over four years, and retirement-eligible executive officer B was granted an option with an aggregate grant date fair value of $300,000 that by its terms vests over four years but is treated as vested at grant for accounting purposes, executive officer B could supplant executive officer A in the table for 2008, even if executive officer A's compensation otherwise exceeds that of executive officer B.

The SEC also explains that the proposed rule makes more transparent the effect of stock option repricings on total compensation (*i.e.*, because the Options Awards column of the Summary Compensation Table relating to the year in which a repricing occurs would be required to include the incremental fair value of any options repriced during the year).

We agree that the proposed rule's equity award disclosure requirement represents a positive change that will generally lead to more meaningful disclosure than under the current rule.

Elimination of Current Requirements

The proposed rule would eliminate the current requirement to disclose the full grant date fair value of individual equity awards in the Grants of Plan-Based Awards Table and in a footnote to the Director Compensation Table. The SEC maintains that these disclosures are largely duplicative of the proposed rule's requirement to disclose the aggregate grant date fair value of equity awards granted in a fiscal year in the Summary Compensation Table and Director Compensation Table.

The proposed rule also would amend Instruction 2 to the Salary and Bonus columns of the Summary Compensation Table to eliminate the requirement that companies report in those columns the amount of salary or bonus that a named executive officer elected to forgo pursuant to a program under which the officer may receive equity or other non-cash compensation instead of such salary or bonus. The equity and other non-cash compensation actually received would instead, depending on the form of award, be reported in the applicable column of the Summary Compensation Table (*i.e.*, Stock Awards, Option Awards, All Other Compensation) or in a footnote to the Salary or Bonus column, with a reference to the Grants of Plan-Based Awards Table. The SEC asserts that this change would provide more meaningful disclosure because it would reflect the form of compensation ultimately received. That said, if a named executive officer elects to forgo cash in exchange for equity, the company may wish to disclose voluntarily, in a footnote or the narrative accompanying the table, the amount of compensation that the named executive officer elected to forgo to indicate the officer's willingness to accept exposure to the value of the company's equity.

Transition Issues

The SEC states that it will not require companies to change the named executive officers for 2007 and 2008 if recomputing the values of their equity awards would result in different executive officers having greater total compensation than the named executive officers for those years, as determined under the current rule. The SEC apparently has not yet determined whether, under the final rule, companies will be required to recompute the amounts disclosed in the Stock Awards and Option Awards columns in the Summary Compensation Table for 2007 and 2008 for executive officers included in the Summary Compensation Table for 2009. In noting that such recomputation would meet its objective of year-to-year comparability, the SEC hints that the final rule may require this.

Companies should consider performing calculations of the amounts that would have been disclosable in the Stock Awards and Option Awards columns for 2008 for each of its executive officers had the proposed rule been in effect for the 2009 proxy season. This will reveal whether different executive officers would have appeared in the tables in the 2009 proxy, which will help companies ensure that they are collecting compensation data for the appropriate executive officers for the 2010 proxy.

Bonuses Paid in Equity

The proposed rule, like the current rule, would require that the amount of a cash bonus be disclosed for the year with respect to which the bonus was earned, even if paid in the following year, but that the aggregate grant date fair value of an equity award for services rendered in the prior year but granted in the following year be disclosed in the following year. However, the SEC requests comments regarding whether the disclosure of a bonus paid in equity should be made for the year with respect to which the bonus was earned, thereby suggesting that it is aware of the potential for confusion. For example, if a company that performs well in 2009 grants to a named executive officer in early 2010 a stock option having an aggregate grant date fair value of $500,000 as a bonus for performance rendered in 2009 and the company then performs poorly in 2010, under the current rule the option grant would be disclosed in 2011 as a 2010 amount, potentially giving shareholders the mistaken impression that the officer was rewarded for the poor performance in 2010.

Compensation Programs and Risk

The proposed rule would amend Item 402 to add a new requirement to the CD&A to discuss and analyze situations in which a company's compensation programs may "create incentives that can affect the company's risk and management of that risk." The requirement would apply to all employee compensation programs and not merely to those in which executives participate. However, this discussion would be required only if the risks arising from such programs may have a material effect on the company. The materiality qualification appears to be intended to allow companies to focus their analyses; however, the use of the word "may" (rather than, for example, "would" or "are likely to") seems to undercut that focus.

The proposed rule details examples of situations that could trigger the need to provide such discussion. These examples include compensation programs:

- at a business unit that carries a significant portion of a company's risk profile;
- at a business unit with compensation that is structured significantly differently from that of other units;
- at a business unit that is significantly more profitable than other units;
- at a business unit whose compensation expense constitutes a significant percentage of the unit's revenues; and
- that vary from the company's overall risk and reward structure (*e.g.*, if bonuses are awarded for accomplishing short-term tasks, whereas the income and risk to the company from the tasks extends over longer periods).

The proposed rule also enumerates issues that a company may need to address if it determines that its compensation programs may create incentives that can affect the company's risk and risk management. These include, for example:

- how the design and implementation of its compensation programs incentivize employees to take risks;
- whether its compensation programs encourage short-term or long-term risk taking (*e.g.*, through clawbacks or holding periods);[3]
- whether the company adjusts its compensation programs to respond to changes in its risk profile; and
- the extent to which the company monitors its compensation programs to ensure that they are not incentivizing employees to respond in ways that conflict with the company's risk management objectives.

The SEC emphasizes that these situations and issues are merely examples and that a company's decision as to whether this discussion is necessary and, if so, what to discuss will depend on the company's particular circumstances.

Companies should advise their compensation committees now of the proposed rule's compensation risk disclosure requirements so that the committees may begin to consider whether this discussion will need to be included in the companies' 2010 proxies.

For a brief summary of the proposed rule's required disclosure regarding the board's role in the management of non-compensation-related risk (*e.g.*, credit risk, liquidity risk, operational risk), see page 6.

Compensation Consultants

Current Rule

Item 407(e) currently requires a company to describe the following with respect to any compensation consultant that it engages:

- any role that such consultant plays in determining the amount or form of executive and director compensation;
- the nature and scope of such consultant's assignment;
- whether such consultant is engaged directly by the compensation committee or any other person; and
- the material elements of instructions or directions given to such consultant with respect to the performance of its duties.

[3] In making the point that some incentive compensation arrangements may misalign the interests of executive and other employees from the long-term well-being of a company, the SEC cites to a report prepared by the Financial Stability Board, a group based in Basel, Switzerland and comprising senior representatives of national financial authorities, international financial institutions, standard-setting bodies and committees of central bank experts. This appears to evidence the SEC's willingness to look to non-U.S. sources for input on reforming compensation and corporate governance disclosure. The report is available at http://www.financialstabilityboard.org/publications/r_0904b.pdf.

The current rule does not require a company to describe additional services provided by a compensation consultant or its affiliates unrelated to executive or director compensation.

Proposed Rule

The SEC states that shareholders are concerned about the potential conflicts of interest that may arise when compensation consultants provide additional services, in particular because the fees earned for such services may be greater than the fees earned for executive compensation services. The SEC presumably believes that if a consultant is concerned about being retained to provide additional services, it may fear alienating the executives and directors who will decide whether to continue to engage the consultant to provide such additional services. As a result, the consultant may provide compensation advice designed to curry favor with management, rather than present an unbiased analysis of the company's compensation alternatives and make recommendations that will best suit corporate and shareholder interests.[4]

The proposed rule would amend Item 407(e) to require a company to disclose the following if a consultant is engaged to provide services that are used to determine or recommend the amount or form of compensation paid to executives and directors and such consultant or its affiliates also provide other services to the company or its affiliates:

- the nature and extent of all additional services provided to the company and its affiliates by such consultant and its affiliates;
- the aggregate fees paid for all such additional services;
- the aggregate fees paid for services used to determine or recommend the amount or form of executive and director compensation;
- whether management decided, or otherwise participated in the decision, to engage such consultant and its affiliates for such additional services; and
- whether the board of directors or compensation committee approved such additional services.

Because broad-based non-discriminatory plans, such as 401(k) savings and medical plans, do not favor executives over other employees, the proposed rule would not require disclosure if the only executive and director compensation services provided by a consultant related to executive and director participation in such non-discriminatory plans.

Companies should review the nature and extent of the work performed by their consultants to understand how the proposed rule's required disclosure will appear in their proxies beginning in 2010.

Corporate Governance Disclosure

In addition to amending the requirements governing compensation disclosure discussed above, the proposed rule would amend certain requirements related to corporate governance, including:

[4] The SEC cites to a 2007 report released by the U.S. House of Representatives Committee on Oversight and Government Reform, chaired by Representative Henry Waxman. The Waxman report concluded that compensation consultants' provision of other services results in a conflict and may contribute to higher levels of executive pay. The report is available at http://oversight.house.gov/documents/20071205100928.pdf. A 2008 study by the Wharton School, however, was "unable to find widespread evidence of more lucrative CEO pay packages for clients of conflicted consultants . . . ." A summary of the Wharton School report is available at http://knowledge.wharton.upenn.edu/article.cfm?articleid=1941.

- **Enhanced Background Disclosure**. Item 401(e) would be amended to require disclosure for each director or nominee regarding the specific experiences, skills, qualifications and attributes of that individual to serve as a director and committee member in light of the company's business and structure. If material, the disclosure could cover more than five years and include information about the individual's risk assessment skills and particular areas of expertise. In addition, the information for directors and nominees must include any public company directorships held at any time during the past five years instead of only current directorships. The proposed rule would also lengthen the time period for which disclosure of legal proceedings involving directors or executive officers is required from five to ten years. These new disclosures would also apply to registered investment companies. Since the proposed rule could become effective in time for the 2010 proxy season, companies should be aware of the possible need to revise their D&O questionnaires.

- **Board Leadership Structure Including CEO/Chair Position**. A new Item 407(h) would require disclosure of a company's leadership structure, such as whether the same person or different individuals serve as CEO and chairman of the board, and why the leadership structure is appropriate given the company's specific characteristics or circumstances. If one person serves as both CEO and chair, the company must state whether it has a lead independent director and such director's role.[5] The proposed rule would also require disclosures regarding the board's role in the company's risk management process. Similar new disclosures would also apply to registered investment companies.

- **Vote Result Reporting**. Companies would be required to disclose shareholder voting results on a new Item 5.07 to Form 8-K within four business days after the end of the meeting instead of the current requirement to report the results in the next quarterly or annual report. In a contested director election, companies would be permitted to disclose preliminary voting results within four business days after the preliminary results are determined and to file an amended 8-K reporting the final voting results after the final results are certified.

Proxy Solicitation Clarifications

The proposed rule also contains technical amendments to the proxy rules to clarify and codify several SEC staff interpretative positions:

- **Exempt Solicitations**. Exchange Act Rule 14a-2(b)(1) exempts from most proxy rule requirements solicitations by disinterested shareholders and non-management parties who do not seek proxy authority and who do not furnish, among other things, a "form of revocation."

  The proposed rule would clarify that providing an unmarked copy of management's proxy card to be returned directly to management (for example, in connection with a "withhold vote" campaign), would NOT constitute a "form of revocation" rendering the exemption unavailable, even though

[5] As part of its voting recommendation for shareholder proposals seeking to separate the chair and CEO positions, RiskMetrics Group evaluates as one element whether a company has a designated lead director, elected by and from the independent board members, with clearly delineated and comprehensive duties. These duties include: presiding at all meetings of the board at which the chairman is not present, including executive sessions of the independent directors; serving as liaison between the chairman and the independent directors; approving information sent to the board; approving meeting agendas for the board; approving meeting schedules to assure that there is sufficient time for discussion of all agenda items; having the authority to call meetings of the independent directors; and, if requested by major shareholders, ensuring that he or she is available for consultation and direct communication.

the return of the card would revoke the shareholder's prior vote. This change would clarify that persons running a "just vote no" campaign may do so without incurring the costs of conducting a full proxy solicitation.

The exemption is not available to any "person who, because of a substantial interest in the subject matter of the solicitation, is likely to receive a benefit from a successful solicitation that would not be shared pro rata by all other holders of the same class of securities, other than a benefit arising from the person's employment with the registrant." In a number of cases, insurgents have argued that they did not have a disqualifying interest under the rule because they were not shareholders of the company. The proposed rule clarifies that a person need not be a security holder of the class of securities being solicited and a benefit need not be related to or derived from any security holdings in the class being solicited for a person to be disqualified from relying on the exemption.

- **Short Slates**. The proposed rule would allow an insurgent to "round out" its short slate with another dissident's nominees, in addition to the registrant's nominees, so long as the soliciting person does not actively recommend their election or form a "group" or become a "participant" in the other dissident's solicitation and otherwise complies with Rule 14a-4(d)(4). This amendment would codify a recent no-action letter issued in connection with the recent Amylin Pharmaceuticals proxy contest.

- **Conditionality of Proxies**. The proposed rule would codify the SEC staff's long-standing position that any conditions to a proxy recipient's obligation to vote as specified in the proxy must be "objectively determinable" (*i.e.*, not overly vague or otherwise within the control of the proxy recipient).

- **Information Regarding Interests of the Participants in a Proxy Solicitation**. Some soliciting persons had argued that Rule 14a-12 allowed information regarding the interests of the participants in a solicitation to be omitted from the soliciting person's first SEC filing of solicitation materials and filed at a later date. The proposed rule would clarify that this information needs to be filed by the time of the first SEC filing.

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This is a summary that we believe may be of interest to you for general information. It is not a full analysis of the matters presented and should not be relied upon as legal advice.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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Appendix A

Compensation Disclosure Questions Posed by SEC in Proposed Rule

The SEC requests comments in response to the following questions relating to the new compensation requirements and to compensation disclosure more generally.

Equity Awards

- Is the proposed Summary Compensation Table reporting of equity awards a better approach for providing investors clear, meaningful, and comparable executive compensation disclosure consistent with the objectives of providing concise analysis in CD&A and a clear understanding of total compensation for the year? Would the proposals facilitate better informed investment and voting decisions?

- The proposal contemplates that the Summary Compensation Table would report the aggregate grant date fair value of stock awards and option awards granted <u>during</u> the relevant fiscal year, just as the Grants of Plan-Based Awards Table reports each grant of an award made to a named executive officer in the last completed fiscal year. Should the Summary Compensation Table instead report the aggregate grant date fair value of equity awards granted for services in the relevant fiscal year, even if the awards were granted <u>after</u> fiscal year end? Explain why or why not. For example, could such an approach be applied in a manner inconsistent with the purposes of our compensation disclosure rules, for example by distorting the determination of named executive officers? If we change our approach with respect to the Summary Compensation Table, should the Grants of Plan-Based Awards Table be amended correspondingly to conform to the scope of awards reported in that table?

- If the Summary Compensation Table is amended as proposed, should the Grants of Plan-Based Awards Table disclosure of the full grant date fair value of each individual award be retained, rather than rescinded as proposed? Should the Grants of Plan Based Awards Table continue to disclose the incremental fair value with respect to individual awards that were repriced or otherwise materially modified during the last completed fiscal year? If so, why? If disclosure of grant date fair value of individual awards is retained, should it also be made applicable to smaller reporting companies?

- As described above, one reason for adopting the financial statement recognition model was the potential for distortion in identifying named executive officers when a single large grant, to be earned by services to be performed over multiple years, affects the list of named executive officers in the Summary Compensation Table, even though the executive earns a consistent level of compensation over the award's term. Are multi-year grants a common practice, so that they would introduce significant year-to-year variability in the list of named executive officers if the proposed amendments are adopted relative to the variability under the current rules? If so, how should our rules address this variability?

- Under the proposal, all stock and option awards would be reported in the Summary Compensation Table at full grant date fair value, including awards with performance conditions. Would the proposal discourage companies from tying stock awards to performance conditions, since the full grant date fair value would be reported without regard to the likelihood of achieving the performance objective? If the proposal is adopted, is any disclosure other than that already currently required (*e.g.*, in the Compensation Discussion and Analysis, the Grants of Plan-Based Awards Table, and the Outstanding Equity Awards at Fiscal Year-End Table) needed to clarify that the amount of compensation ultimately realized under a performance-based equity award may be different?

- As proposed, Instruction 2 to the salary and bonus columns would be revised to provide that any amount of salary or bonus forgone at the election of a named executive officer pursuant to a program under which a different, non-cash form of compensation may be received need not be included in the salary or bonus column, but instead would need to be reported in the appropriate other column of the Summary Compensation Table. Should this approach cover elections to receive salary or bonus in the form of equity compensation only if the opportunity to elect equity settlement is within the terms of the original compensatory arrangement, so that the original arrangement is within the scope of FAS 123R? Why or why not?

- The Commission also has received a rulemaking petition requesting that we revise Summary Compensation Table disclosure of stock and option awards a different way. Instead of reporting the aggregate grant date fair value of awards granted during the year, as we propose, the petition's suggested approach would report the annual change in value of awards, which could be a negative number if market values decline. For restricted stock, restricted stock units and performance shares, the reported amount would be the change in stock price from year-end to year-end. For stock options, it would be the change in the in-the-money value over the same period. Would the approach suggested by the rulemaking petition be easy to understand or difficult to understand? Would the information provided under the suggested approach be useful to investors? In particular, would investors be able to evaluate the decision making of directors with respect to executive compensation if the value of equity compensation on the date of the compensation decision is not disclosed, but instead investors are provided information regarding changes in value of the compensation, which changes occur after the compensation decision is made? Would it enhance or diminish the ability of companies to explain in CD&A the relationship between pay and company performance? Would it be more or less informative to voting and investment decisions than the aggregate grant date fair value approach we propose? Would it be a better measure for computing total compensation, including for purposes of identifying named executive officers? Are there any other ways of reporting stock and option awards that would better reflect their compensatory value? If so, please explain. For example, are there any potential amendments to the Grants of Plan-Based Awards Table or the Outstanding Equity Awards at Fiscal Year-End Table that we should consider to better illustrate the relationship between pay and company performance?

- The Summary Compensation Table requires disclosure for each of the registrant's last three completed fiscal years, and with respect to smaller reporting companies, for each of the registrant's last two completed fiscal years. Regarding transition, our goal is to facilitate year-to-year comparisons in a cost-effective way. To this end, we are considering whether to require companies providing Item 402 disclosure for a fiscal year ending on or after December 15, 2009 to present recomputed disclosure for each preceding fiscal year required to be included in the Summary Compensation Table, so that the Stock Awards and Option Awards columns would present the applicable full grant date fair values, and Total Compensation would be recomputed correspondingly. If a person who would be a named executive officer for the most recent fiscal year (2009) also was disclosed as a named executive officer for 2007, but not for 2008, we expect to require the named executive officer's compensation for each of those three fiscal years to be reported pursuant to the proposed amendments. However, we would not require companies to include different named executive officers for any preceding fiscal year based on recomputing total compensation for those years pursuant to the proposed amendments or to amend prior years' Item 402 disclosure in previously filed Forms 10-K or other filings. Would recomputation of prior years included in the 2009 Summary Compensation Table to substitute aggregate grant date fair value numbers for the financial statement recognition numbers previously reported for those years cause companies practical difficulties? Is there a better approach that would preserve the objective of year-to-year comparability on a cost-effective basis as a transitional matter?

Compensation Programs and Risk

- 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?

- 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?

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

- We have included a list of examples of the types of issues that would be appropriate for a company to discuss and analyze. Is this list appropriate? Rather than treat the list as examples, should we require discussion of each item?

- 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?

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

- If a company determines that disclosure under the proposed amendments is not required, should we require the company to affirmatively state in its CD&A that it has determined that the risks arising from its broader compensation policies are not reasonably expected to have a material effect on the company?

- Should smaller reporting companies, who are currently not required to provide CD&A disclosure, be required to provide disclosure about their overall compensation policies as they relate to risk management?

Compensation Consultants

- Will this disclosure help investors better assess the role of compensation consultants and potential conflicts of interest, and thereby better assess the compensation decisions made by the board?
- Would the disclosure of additional consulting services and any related fees adversely affect the ability of a company to receive executive compensation consulting or non-executive compensation related services? If so, how might we achieve our goal while minimizing that impact?
- Are there competitive or proprietary concerns that the proposed disclosure requirements should account for? If so, how should the amendments account for them if the compensation consultant provides additional services?
- Are there additional disclosures regarding the potential conflicts of interest of compensation consultants that should be required? For example, would requiring disclosure of any ownership interest that an individual consultant may have in the compensation consultant or any affiliates of the compensation consultant that are providing the additional services to the company help provide information about potential conflicts? If so, why?
- The proposed disclosure requirement calls for disclosure of services during the prior year. Should we also require disclosure of any currently contemplated services in order to capture a situation where the compensation consultant provides services related to executive pay in one year and in the next year receives fees for other services? If so, should we require that fees for the currently contemplated services be estimated? Is there a better way to require that information, for instance through the date of the filing? Should we require disclosure for the prior three years?
- Is the proposed exclusion for consulting services that are limited to broad-based, nondiscriminatory plans appropriate? Should we consider any other exclusions for services that do not give rise to potential conflicts of interest? If so, describe them.
- Should we establish a disclosure threshold based on the amount of the fees for the non-executive compensation related services, such as above a certain dollar amount or a percentage of income or revenues? If so, how should the threshold be computed?
- Would disclosure of the individual fees paid for non-executive compensation related services provided by the compensation consultants be more useful to investors than disclosure of the aggregate fees paid for non-compensation related service provided as proposed?
- Would disclosure about the fees paid to compensation consultants and their affiliates help highlight potential conflicts of interest on the part of these compensation consultants and their affiliates? Is fee disclosure necessary to achieve this goal, or would it be sufficient to require disclosure of the nature and extent of additional services provided by the compensation consultant and its affiliates? Should disclosure only be required for fees paid in connection with executive compensation related services?
- Should we make any special accommodations in the proposed amendments to Item 407(h) for smaller reporting companies? If so, what accommodations should be made and why?

- Are there other categories of consultants or advisors whose activities on behalf of companies should be disclosed to shareholders? If so, what kind of disclosure would be appropriate?

Other Compensation-Related Questions

- Are there any disclosures required in the proxy statement that we should consider proposing to eliminate in light of the proposed amendments?
- Are there other initiatives we should consider in order to improve the disclosure in proxy statements, particularly with regard to disclosure regarding executive compensation? For instance should we propose requiring disclosure of the compensation paid to each executive officer, not just the named executive officers? Should we consider proposing to eliminate the instruction that provides that performance targets can be excluded based on the potential adverse competitive effect on the company of their disclosure? Alternatively, should we consider proposing to revise the CD&A to require disclosure of performance targets on an after-the-fact basis, after the performance related to the award is measured, such as three or more fiscal years later, whether or not the disclosure may result in competitive harm?
- Under current Item 407(e)(5) of Regulation S-K, the Compensation Committee Report must state whether the committee: (1) has reviewed and discussed the CD&A with management; and (2) recommended to the board of directors that the CD&A be included in the company's annual report and the proxy or information statement. Although the CD&A is considered "filed", the Compensation Committee Report is "furnished." Because it is furnished, the Compensation Committee Report does not have the same liability as the CD&A and other information that is "filed." For example, it is not incorporated by reference or otherwise considered a part of the company's Form 10-K, registration statements and other filings, and is not covered by the principal executive officer and principal financial officer certifications required under Exchange Act Rules 13a-14 and 15d-14. Should we consider proposing to amend this rule to make the CD&A be a part of the Compensation Committee Report? Why or why not? If we make the CD&A part of the Compensation Committee Report, should the Compensation Committee Report be "filed"? If we were to make the CD&A part of the Compensation Committee Report, are there any requirements to the CD&A that we should change?
- Should we consider requiring disclosure regarding whether a member of the compensation committee has expertise in compensation matters and whether the committee has the resources to hire its own independent legal counsel?
- Some investors may want more information regarding whether compensation arrangements are reasonably designed to create incentives among executives to increase long-term enterprise value. Should we consider supplementing any of the tabular and narrative disclosure requirements to require additional disclosure about whether or not a company has "hold to retirement" and/or claw back provisions and if not, why not?
- Are investors interested in disclosure of whether the amounts of executive compensation reflect any considerations of internal pay equity? For example, would investors find such disclosure relevant in considering the motivation and effectiveness of broad based compensation plans? Should we consider proposing additional requirements to address this? For instance, should we consider proposing required disclosure regarding internal pay ratios of a company, such as disclosure of the ratio of the total compensation of the named executive officers, or total

compensation of each individual named executive officer, to the total compensation of the average non-executive employee of the company?

- In order to give investors a better understanding of the breadth and depth of a company's focus on compensation, should we require disclosure regarding the total number of compensation plans a company has and the total number of variables in all of its compensation plans? Are there other ways to convey the complexity and significance of all of a company's plans?
- Should we consider proposing to supplement the required disclosure of tax gross-up arrangements that the company has for the named executive officers to include a requirement to disclose and quantify the savings to each executive?