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Via e-mail: rule-comments@sec.gov

Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090
Attention: Nancy M. Morris,
Secretary, Securities and Exchange Commission

Re: File No. S7-03-06; Release Nos. 33-8655; 34-53185; IC-27218
Executive Compensation and Related Party Disclosure

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Securities Regulation of the New York City Bar in response to Release Nos. 33-8655, 34-53185, IC-27218, dated January 27, 2006, in which the Securities and Exchange Commission solicited comments on proposed amendments to the disclosure requirements for executive and director compensation, related party transactions, director independence and other corporate governance matters and security ownership of officers and directors.

Our Committee is composed of lawyers with diverse perspectives on securities issues, including members of law firms, counsel to corporations, investment banks and investors, and academics. Please note that Mr. David Rosenfeld, a member of the Staff of the Commission and a member of our Committee, did not participate in the preparation of this letter or the decision by our Committee to submit this letter to the Commission.

Introduction

Our Committee expresses its appreciation for the substantial efforts of the Commission and its Staff to update and upgrade the rules governing executive compensation and related issues addressed in the Release, in response to the evolving concerns of the securities markets and the contemporary needs of investors, government officials and the general public relating to public company disclosures. Our comments below do not relate to the details of the proposed revisions to compensation disclosure. Rather, the comments focus on specific modifications that we suggest will remove certain unintended inconsistencies or defects, conform certain of the rules to accepted norms and practices, preserve certain existing provisions whose proposed deletion we believe would be ill-advised and, in one case, obviate a practice difficulty under existing rules not addressed in the Release.

1. CD&A (S-K[1] Item 404(b)). We appreciate that the CD&A, to achieve its goal of improving disclosure regarding the executive compensation decision process, requires some level of prescription. On the other hand, the rules must necessarily accommodate a range of compensation programs, from the simple to the highly complex. We believe therefore that certain of the items in the list of required CD&A disclosures (subsection (b)(1)) should be shifted to the menu of suggested disclosures that will vary depending on facts and circumstance (subsection (b)(2)). In particular, we recommend eliminating from the roster of mandatory disclosures—

> disclosure on what the registrant's program is designed *not* to reward (clause (ii)), since in many or even most cases this is unlikely to enter into the calculus performed by a compensation committee. Those circumstances in which a committee has specifically determined not to reward certain achievements could be picked up in subsection (b)(2) of the proposed rule;
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> disclosure on how each compensation element affects decisions regarding other elements (clause (vi)), which is likely in cases of a relatively simple compensatory scheme to be inapplicable and to spawn uninformative boilerplate.

2. The CD&A and Proposed S-K Item 407(e). It would appear that the CD&A is intended to address specific elements of a registrant's compensation program, while S-K Item 407(e) is meant to cover the processes and procedures by which compensation decisions are made. The role of executive officers in determining executive compensation appears both under the CD&A rules (Item 404(b)(2)(xiii)) and in a somewhat different formulation in proposed Item 407(e)(3)(ii). This disclosure is more consistent with the disclosure framework of Item 407(e) and should be eliminated from the CD&A.

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[1] We reference in text Regulation S-K, although our comments apply to Regulation S-B as well, to the extent relevant.

3. The Performance Graph (Existing Item S-K 402(l). We join with other commentators in recommending that the performance graph be retained. While we recognize that the graph has its limitations and can be very sensitive to values in the base year, we believe investors have come to rely upon the graph for a quick side-by-side of executive compensation versus issuer performance. Rather than eliminate the graph, the Commission might explore ways in which a superior nexus could be created between the graph and the compensation disclosure that it accompanies.

4. Related Party Transaction Threshold (S-K Item 404(a). The proposed rules would raise the threshold for related party transaction disclosure from $60,000 to $120,000 to adjust for inflation. We suggest that the Commission consider indexing this amount to an appropriate pricing index, as is done for example under the Hart-Scott-Rodino Act 15 U.S.C. §18a and Section 8 of the Clayton Act, 15 U.S.C. §19. Through indexing, the threshold would adjust on a regular basis and would not again become so out-of-sync with economic realities that it would need to be doubled in order to restore it to a sensibly informative level.

5. Related Person (Instruction 1 to S-K Item 404(a)). The Commission is proposing to modify the definition of "immediate family member" for purposes of related party disclosure. (Instruction 1.b.ii to S-K Item 404(a)) The modification would add "any person (other than a tenant or employee) sharing the household of a related person." We assume that the change is intended to address contemporary relationships that in many ways are the functional equivalent of the traditional family unit. (We note that a similar concept appears in New York Stock Exchange Corporate Responsibility Rule 303A.02, General Commentary.) If this is indeed the rationale behind the rule change, we suggest that the Commission consider a corresponding modification to the definition of "immediate family" in Rule 16a-1(e). While the purposes of related party disclosure under S-K Item 404(a) and the insider transaction disclosure under Section 16 differ, there would appear to be no basis for applying different concepts of family in the two regimes.

6. Employment Compensation as a Related Party Transaction (Instruction 5 to S-K Item 404(a)). The proposed rules would exempt executive compensation from related party transaction disclosure if certain criteria are satisfied. (Instruction 5.b to S-K Item 404(a)) In the case of an executive officer whose compensation is not required to be disclosed under S-K Item 402, these criteria include that such executive officer is not an immediate family member of a related person, that the compensation would have been disclosable under S-K Item 402 and that the compensation had been approved by the compensation committee of the board or another group of independent directors. We note that the compensation committees of many public companies recommend to the board, but do not themselves approve, the compensation of executive officers (other than the CEO). The NYSE Corporate Responsibility Rules so provide explicitly. ("The compensation committee must have a written charter that addresses: the committee's purpose and responsibilities – which, at minimum, must be to have direct responsibility to: . . . make recommendations to the board with respect to non-CEO executive officer compensation"; Corporate Responsibility Rule 303A.05(b)(i)(A)) We believe that the

recommendation of an independent compensation committee provides sufficient assurance that payments are being made for bona fide compensatory purposes and that the rules of the Commission in this regard should not effectively compel registrants to abandon the accepted practice of committee recommendation and board approval for non-CEO compensation. We therefore suggest that proposed Instruction 5 be modified so that a recommendation by a board compensation committee or similar independent body of directors will be sufficient to satisfy the criteria of Instruction 5.

7. Existing Instructions 1 and 9 to S-K Item 404(a). We note that Instruction 1 to Rule 404(a), discussing the concept of a materiality, appears to have been dropped from the proposed rules and that the Commission is proposing to eliminate existing Instruction 9 to Item 404(a), which indicates that the related party transaction threshold is not a bright line materiality standard, because of the view that the instruction is repetitive of general principles. We would urge the Commission to retain an instruction on materiality, even if the Commission believes that it is appropriate to replace the current formulation. As a general principle, we believe that it is advisable for core concepts of a disclosure rule to be evident on the face of the rule, and readers should not be required to reference case law or adopting releases to tease out their meaning. We note in this regard that the standard of materiality in current Instruction 1 and recited in Section V.A.1. of the proposing release ("The materiality of any interest would continue to be determined on the basis of the significance of the information to investors in light of all the circumstances and the significance of the interest to the person having the interest") is decidedly not the same as the definition of materiality under Rule 12b-2. We therefore recommend that the Commission retain materiality instruction in suitable form. A formulation along the following lines might be appropriate:

> The $120,000 is not a bright line materiality standard. The determination of whether a related person has a direct or indirect material interest in a transaction should be determined on the basis of the significance of the information to investors in light of all the circumstances and the significance of the interest to the person having the interest.

8. Review of Related Party Transactions (S-K Item 404(b)). The proposed rules would require disclosure of a registrant's policies and procedures for review, approval or ratification of related party transactions required to be reported under S-K Item 404(a). Related parties include generally directors and nominees, executive officers, 5% shareholders and their immediate family members. There are two modifications to this requirement that the Commission may wish to consider. The disclosure requirement of proposed Item 404(b)(1) ties to "any transaction required to be reported under paragraph (a) of this Item." Item 404(a) requires disclosure of any transaction since the beginning of the prior fiscal year in which a related person has or has had a material interest, including a director or executive officer who only became a related person subsequent to the transaction. See Section V.A.1.b of the Release. While we understand the rationale for disclosure of a related party transaction involving an officer or director occurring before the person assumed office, we do not believe it is reasonable or customary for a company's related party transactions policy to extend to transactions

occurring before an individual has become affiliated with the company. Also, while the 5% share ownership threshold is appropriate for related party transaction disclosure, a registrant could reasonably determine that it is too low a threshold for invoking the registrant's review and approval procedures. Similar concerns attach to proposed Item 404(b)(2), which would require identification of any transactions reported under Item 404(a) that did not require review under the registrant's related party transaction policy and procedures. We therefore recommend that proposed Item 404(b) be modified to eliminate its applicability to transactions occurring before a director or executive officer became such and to raise the threshold of related party share ownership for this Item only to 10%.

9. Director Independence (S-K Item 407(a)(1)(i)). We point out a minor defect in proposed Item 407(a)(1)(i). Item 407(a)(1) specifies the applicable definition of independence that a registrant must use in determining whether or not a director or nominee is independent. Subsection (i) states,

> If the registrant is a listed issuer whose securities are listed on a national securities exchange or in an inter-dealer quotation system which has requirements that a majority of the board of directors be independent, the registrant's definition of independence that it uses for determining if a majority of the board of directors is independent in compliance with the listing standards applicable to the registrant.

As the Commission is aware, the rules of the NYSE (Corporate Responsibility Rule 303A.01), The Nasdaq Stock Market (Market Place Rule 4350(c)) and the American Stock Exchange (Corporate Governance Requirements Section 802) provide that controlled companies, defined generally as issuers more than 50% of whose voting stock is controlled by a single person or group of persons, are not required to have a board consisting of a majority of independent directors. Read literally, the proposed rule would not apply to such issuers. The rule can be readily modified, however by the appropriate inclusion of a qualifier to the effect of "or would be required to make such determination if it were not a controlled company, as defined under the applicable listing standards."

10. Independence Standards (S-K Item 407(a)(2), (3)). Proposed Item 407(a)(2) provides that if a registrant uses its own definitions for determining whether its directors, nominees and committee members are independent, the registrant must disclose whether the definitions are available on the registrant's website. If the definitions are not posted, they must be periodically appended to the registrant's proxy statement. As contemplated by the Corporate Responsibility Rules of the NYSE (Commentary to Rule 303A.02(a)), issuers have adopted categorical standards of independence such that transactions falling within these standards are per se deemed immaterial. We assume that the Commission intends to require disclosure of such standards under proposed Item 407(a)(2). There is some ambiguity on this point, however, because standards of this sort complement, but do not supplant, the definitions of the applicable exchange. We suggest that the Commission modify proposed Item 407(a)(2) to clarify this ambiguity and require disclosure of such categorical standards. We note that the cited Corporate Responsibility Rule of the NYSE itself requires disclosure of these standards.

In a similar vein, proposed Item 407(a)(3) would require disclosure of any transaction, relationship or arrangement not disclosed pursuant to Item 404(a) considered by the board under applicable standards of independence in determining that a director or nominee is independent. We suggest that the proposed rule be modified to clarify that no such transaction, relationship or arrangement need be separately disclosed if it is captured by categorical standards disclosed pursuant to Item 407(a)(2).

11. Compensation Disclosure in Exchange Offers (Items 18 and 19 of Form S-4). While not addressed in the Release, there is a matter relevant to executive compensation disclosure that has been a source of concern for practitioners and that the Commission might address in its current review of the executive compensation rules.

Item 18 of Form S-4 prescribes certain disclosures for business combination transactions in which proxies or consents are being solicited. Item 19 of the Form requires similar information for exchange offers or transactions in which no proxies or consents are to be solicited. In both cases, the Form calls for the disclosure mandated by Items 401, 402 and 404 of Regulation S-K with respect to each person who will serve as a director or an executive officer of the surviving or acquiring person. Registrants that satisfy the requirements for use of Form S-3 may incorporate this information by reference from their latest Form 10-K.

From time to time, a stock-for-stock acquisition is scheduled to occur during an acquiror's first fiscal quarter. The acquiror's executive compensation disclosure for the immediately concluded fiscal year that is called for by Item 402 may either not yet be available or might only be obtained through great effort and expense. We suggest that in the limited circumstances of (i) an S-3 eligible acquiring issuer, (ii) soliciting proxies or consents for a stock-for-stock transaction in its first fiscal quarter, and (iii) where the Item 402 executive compensation information for the immediately preceding fiscal year is unavailable or cannot be obtained without undue effort or expense, the Commission amend its rules to allow the acquiror to continue to incorporate by reference the Item 402 information for the next preceding fiscal year from its most recently filed Form 10-K (although we believe, at a minimum, that the Commission should make such an amendment, we would also support an amendment that would more broadly extend the relief to permit Item 402 information for the next preceding fiscal year to be used in other filings (for example, filings on Form S-1) at times when the financial statements for such next preceding fiscal year are not yet stale or the registrant's Form 10-K is not otherwise due). In support for this exception, we note that business combination transactions are often driven by dynamics wholly unrelated to an issuer's cycle of public disclosure. Holding a transaction hostage to executive compensation disclosure at a time early in the fiscal year when such disclosure is not expected by the markets to be available would not appear to be in the best interests of either the target or the acquiror's stockholders. Limiting the exception to S-3 eligible issuers provides assurance that the acquiror is timely in its recent filings with the Commission and, through the minimum float requirements, attracts a certain level of market interest.

Conclusion

Our Committee applauds the Commission for undertaking a thoughtful and comprehensive revision to the disclosure scheme for executive compensation and related matters addressed in the Release. We believe that attention to the matters in this letter will enhance the work of the Commission in this regard.

Please note that this letter does not necessarily reflect the individual views of members of our Committee.

Members of our Committee would be pleased to answer any questions you may have regarding our comments, and to meet with the Staff if that would be of assistance.

Respectfully Submitted,

/s/ Matthew J. Mallow

Committee on Securities Regulation

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