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September 15, 2009

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street N.E.
Washington, DC 20549-1090

Re: File Number S7-13-09

Dear Ms. Murphy,
Thank you for the opportunity to provide comments to the Commission related to File Number S7-13-09; they are attached. If you have any questions, I would be happy to respond further.

With best regards,
Eleanor Bloxham
CEO, The Value Alliance and Corporate Governance Alliance
614-571-7020
ebloxham@thevaluealliance.com

Below are my specific comments related to File Number S7-13-09.

A.1 Disclosure with respect to Compensation and Risk

In April, 2006, I wrote to the Commission in response to requests for comments on compensation disclosure.

In that letter, I recommended that the Commission's proposals include disclosure with respect to compensation and risk. http://www.sec.gov/rules/proposed/s70306/ebloxham041006.pdf

I do believe that if the Commission had enacted these suggestions, positive benefits would have ensued. Going forward, I believe such requirements would help to positively shape board decision making with respect to the relationship between compensation and risk -- and would create a deeper understanding of the use of compensation as a motivational tool. This would be accomplished, as outlined in my original letter, by asking the company to disclose the way in which compensation relates to the risks in the business, as well as to address compensation itself as a risk.

Clearly, therefore, I have been on the record for over three years in support of disclosure with respect to compensation and risk.

That said, I do not favor meaningless disclosure. The primary reason for this is that meaningless disclosure will likely provide false comfort by serving to confuse respondents themselves into believing that they have achieved a level of understanding with respect to compensation and risk which, in fact, has not been realized. Such false comfort can only engender harm to investors and companies over the long run.

As noted above, and in my 2006 letter, there are two major areas of disclosure that should be addressed with respect to compensation and risk.

One major area of disclosure relates to the material risks in the business. The CD&A should disclose how the compensation programs, policies, practices, structures, and philosophies relate to and address those material risks i.e. how the material risks are taken into account in pay practices. (Material risks are already required to be outlined in the MD&A.)

The second major area of disclosure relates to the risks of the compensation program more specifically. Since compensation programs, policies, practices, structures and philosophies create risks themselves (which heretofore may not have been delineated in the MD&A -- for example, programs that create a risk of earnings manipulation), disclosure with respect to the risks created by the compensation program itself, and how the company seeks to address them, if at all, should be disclosed.

The link between compensation and the material risks in the business

Regarding the first issue, on the material risks in the business and how compensation relates to those risks, in my April, 2006 letter, I made the following recommendations with respect to the CD&A disclosure which I still believe to be a good approach to this disclosure. This recommendation regarding disclosure was built on the SEC's requirements in the MD&A. The requirements of the MD&A serve to provide investors with meaningful information in evaluating the company's performance and outlook. Building on the SEC's requirements in the MD&A, specifically, my recommendations included that the CD&A should:

- *"Explicitly address "the key performance indicators" outlined in the MD&A -"both financial and non financial" - that "management uses to manage the business and that would be material to investors" -- and how the compensation programs provide appropriate incentives to management with respect to these key performance indicators. This discussion [should] include why certain indicators are used in compensation, which are not used, and why."*
- *"Explicitly address "the known trends, events, demands, commitments and uncertainties" outlined in the MD&A "that are reasonably likely to have a material impact on financial condition or operating performance" and how the compensation program addresses these issues. Which of these issues is management held accountable for under the compensation plan, if any, and why? Which not and why?"*
- *"Explicitly address "the quality and potential variability of earnings and cash flow" outlined in the MD&A and how the compensation program addresses this variability and its impact on management -- or, if it doesn't, why it doesn't."*
- *"Explicitly address the "economic and industry wide factors relevant to the company" outlined in the MD&A and how the compensation program addresses these trends in terms of its incentives of management. What is considered and how?"*
- *"Explicitly address "the material opportunities, challenges and risks such as those presented by known material trends and uncertainties on which the company's executives are most focused for both the short and long term as well as the actions they are taking to address these opportunities, challenges and risks" as outlined in the MD&A. The compensation discussion should address these areas of focus and whether and how the compensation program addresses each of them."*

Since incentive compensation should relate to the nature of the business and what it is boards wish to reward, it seems perfectly reasonable to simply ask the CD&A to address the way in which compensation relates to the MD&A discussion of the business and its risks.

From an ease of implementation standpoint, managements are already familiar with the MD&A and its requirements. Similarly, investors are familiar with the MD&A and its content. Finally, SEC reviewers are or should be familiar with the MD&A and what it contains. The MD&A is thus a good platform for designing the appropriate CD&A disclosures.

The MD&A requirements recognize rightly that all businesses have certain performance metrics which are used to run the business. The MD&A requirements also recognize that all businesses have uncertainties and risks which should be disclosed. Similarly, compensation operates within the business context of metrics, uncertainties and risk. Just as disclosures in the MD&A are not subject to arbitrary trigger mechanisms, neither should the CD&A disclosure be. (In fact, establishing trigger mechanisms for the MD&A and CD&A disclosures would so weaken the disclosure process, I believe, that more harm than good would be created.)

Amplifying further on disclosure, in my April, 2006 letter, I recommended that the CD&A:

- *"Be reflective of and responsive to a company's statements about vision, mission, ethics and values as outlined in its annual report, website and other publicly available communications - as well as its regulatory obligations …[and] explicitly address how the compensation program addresses these issues. Are ethical lapses or breaches and regulatory enforcement actions factored into compensation decision making? Are issues related to corporate culture? To values*

associated with behavior to stakeholders? To the company's enterprise risk management system and system of internal controls? etc... How is this done?"

- *Cover [not] only the link between the business realities [and] how the compensation strategy supports them, but also … [how the compensation strategy] explicitly links each of the elements of compensation (salary, bonus etc) to its purpose in supporting corporate objectives.*

Clearly, any changes from the prior period in the ways in which compensation relates to the MD&A and the other items above should also be disclosed.

Risks created by the Compensation program itself

Regarding the second major issue, all compensation programs create risk (and to not have incentive compensation programs creates risk). It's unavoidable.

Enron, WorldCom, Tyco and other corporate scandals are dramatic examples. However, in addition there is ample academic research that points to the material risks created by compensation programs.

For example, Floyd Norris in the NY Times, High and Low Finance, July 31, 2009, reported that according to a study by René Stulz, and Rüdiger Fahlenbrach "banks run by chief executives with a lot of stock were, if anything, likely to do worse than other banks in the crisis... the one with the most valuable holdings of stock and options in his company at the end of 2006 was Richard Fuld of Lehman Brothers". This kind of finding is not new from an academic literature standpoint.

However, in light of the financial crisis, it makes a point. Clearly, one of the reasons traders and executives weren't looking at the risks in the business were because the compensation programs were tied to metrics unrelated to the intrinsic risk in the business.

So again, for emphasis, all compensation programs create certain risks. The risk of de-motivation, the risk of excessive risk taking, retention risk, etc. -- all these risks a board and company must weigh in setting out its compensation programs.

From a disclosure standpoint, what is important, then, is to outline the risks created by the programs and in their design how the board and/or management, as appropriate, seek to mitigate them.

Perhaps some would argue that because all compensation programs create risks, no risks need be mentioned. I would disagree. In fact, although, heretofore, the SEC has not required that the material risks created by compensation programs be set out in the MD&A, hindsight is 20-20 and perhaps such a requirement would have been beneficial in the run up to the crisis. Going forward, the SEC should require filed disclosures outlining the risks created by each of the corporation's compensation programs, policies, practices, procedures and philosophies.

As stated in my April, 2006 letter:

"Compensation represents a component of corporate strategy in the retention and motivation of employees and management."

The CD&A should:

The Value Alliance. 6834 Willoughby Ct. Westerville, OH 43082 USA www.thevaluealliance.com
Eleanor Bloxham. 614-571-7020. ebloxham@thevaluealliance.com

- "D*iscuss the risks associated with the compensation strategy employed and how the board intends to mitigate those risks".*

"All compensation programs have risks of incenting behavior in a certain direction. Some empirical studies have demonstrated these risks. For example, the risk of earnings manipulation. In other instances, there are other risks: for example multiple measures that generate confusion as to direction represent a risk. Other risks might include a tendency to focus short vs. long term, etc."

The CD&A should include:

- *"An assessment of the risks by the compensation committee for whatever compensation strategy is chosen and an outline of what they have done to strategically mitigate those risks so that the strategy employed does not have material adverse unintended consequences."*

Expanding beyond the plans under the board's direct oversight, the SEC should require an outline of the risks created by each of the corporation's compensation programs, policies, practices, procedures and philosophies and how the board and/or management have sought to mitigate them.

It is important to realize that in making determinations regarding the level and extent of disclosure required what is critical and often misunderstood is the influence that compensation has on strategy and execution, not just "excessive risk-taking" as it has generally been termed since the financial crisis hit.

The metrics used in compensation (and the form of compensation given i.e. stock versus cash as well as other compensation practices) influence the metrics used to make strategic decisions -- and influence execution choices. Thus what may seem to be small compensation choices have a large impact in driving corporate decision making, capital allocation choices, etc. This means that what may not seem material with respect to compensation itself, can and is ultimately material, with respect to corporate results. (Corporations themselves often fail to fully recognize these impacts because long-standing choices in compensation and strategic practices have remained unchallenged for so long.)

Footnote number 74 should be applied to the Commission's thinking with respect to compensation disclosure. Because compensation choices with respect to policy, procedure, programs, philosophies and practices are always material, the SEC should err on the side of greater disclosure with respect to compensation in both major areas:

- the risks of the business and how compensation is structured related to that
- compensation itself as a risk.

All the firms' compensation programs should be included in this analysis.

A.2. Presentations in the Summary Table

The SEC should make changes that investors believe would be helpful to them. It would be useful to also include the information which is not included in the table in footnote form. Tables recast with prior year amounts on the same basis should also be required.

B. Enhanced Director and Nominee Disclosure

I believe that the recommendations for expansion of director and nominee disclosure proposed by the SEC are worthwhile. I believe the biographical history should include more than five years and represent

at least two decades of the nominee's history along with full disclosure of the nominee's risk assessment skills. All directorships held at public, private and non-profit companies, through their history, disposition of those seats (retired, resigned, etc), and shareholder votes for and against them on those various boards during their term of office, should be disclosed. In addition to other legal proceedings, their history with respect to civil actions by investors and disposition of those actions including awards and judgments in the matter should be disclosed.

In addition, disclosures should include additional information on how the board nomination process works, including how members are refreshed and changed and the extent to which board evaluations are used in this process. If the company has changed strategy or its risk factors have changed, the disclosure should include how board membership has changed to effectively oversee the new environment, or if not, why not i.e. the expertise on the board with respect to those new strategies and risks.

I do believe that diversity in the boardroom is a significant issue and the board disclosure should discuss how the board ensures diversity of thought, gender, and race in the boardroom. Included in the disclosure should be specific disclosure regarding the make-up by gender and race of the workforce, entry level college workforce, management, top executive team, and board. Data with respect to customers and suppliers should also be provided if the company tracks the data.

C. Company Leadership and the Board's Role in the Risk Management Process

I agree with the suggestions for disclosure.

Disclosure should include how the leadership positions of the board (the chair of the board, lead director, if any, and chairs of the committees) are appointed, nominated and selected and how those positions are refreshed or changed i.e. what are the processes and procedures, who manages them, etc.

The MD&A should include how the board seeks to oversee risks and how it seeks to mitigate risks in its compensation and other oversight practices.

Here it should be recognized that not only does the company have risks, but the oversight practices of the board contain certain risks as well. The board should include statements on how it seeks to mitigate risks in its oversight practices, if at all, and if not, why not. Risk management practices, in general, and these in particular should be included in quarterly and annual reporting statements.

D. Disclosure regarding Compensation Consultants

I actually believe that some of this proposal is not useful and is like putting a band aid on a gaping wound. Large firms providing multiple services are no more prone to conflicts, in my opinion, based on my experience, than small ones. While large firms may be doing other corporate business, small ones may be anxious to do whatever it takes to get and maintain the business.

What would be more useful is to understand in the disclosure the areas of expertise of the particular consultant and why the consultant was chosen. For example, what skills and expertise did the consultant fill in that the board itself was lacking. Also useful would be what services they have performed in some detail. For example, did they benchmark pay, choose the benchmark firms, etc.

The Value Alliance. 6834 Willoughby Ct. Westerville, OH 43082 USA www.thevaluealliance.com
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In addition, disclosure with respect to how they were chosen is relevant as well, including the exact process used. For example, knowing whether management pre-screened down to a list of three to five candidates would be helpful.

E. Reporting of Voting Results and F. Proxy Solicitation Process

I believe insights from the SEC's newly formed *Investor as Shareholder Subcommittee* could be useful.

Other Requests for Comment

The proposals regarding expansion of compensation disclosure are worthwhile.

Internal pay equity is an important consideration for boards and investors and can have a significant impact on motivational risk. The ratios suggested seem reasonable. Discussion of the board's and management's philosophy with respect to pay equity would be useful.

Descriptions of hold-back and claw-back mechanisms, including how they work and how they benefit long term shareholders, would be highly beneficial.

Disclosure of the full range of the compensation programs is also helpful for a number of purposes. This disclosure should include the risks of simplicity versus the complexity of different compensation programs and structures, and how the board and management seek to address the issues of alignment (i.e. alignment risk) in complex systems.

One of the trigger mechanisms for disclosure suggested by the SEC proposals in A.1. above was a business unit with a different compensation structure. I have already expressed why I think trigger mechanisms send the exactly wrong message with respect to these important disclosures. I also believe that such mechanisms would do more harm than good.

It could be the case that one business unit with a different compensation structure could be the only unit with a structure that takes into account risk and therefore has a less risky compensation structure than all the other units. The unit could also, however, be subjected to external risk from other units who are not on similar plans.

Regarding filing and furnishing, I think the CD&A should have two sections: that filed by the board and that filed by management, based on the duties and responsibilities that have been separately undertaken by each with respect to oversight of the company's compensation processes.

With respect to the SEC's own oversight of these matters, notwithstanding the establishment of the *Investor as Shareholder Subcommittee*, I would recommend that the SEC reach out more broadly to resources that can provide them with background in the areas of risk analyses and how they impact company behavior, areas and issues associated with the current state of risk oversight, as well as the areas of compensation program implementation which takes into account risk.

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