

EXEQUITY

February 2, 2007

VIA E-MAIL to rule-comments@sec.gov

Nancy M. Morris, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-03-06; *Executive Compensation Disclosure*, SEC Release Nos. 33-8765; 34-55009 (December 22, 2006) and published in the Federal Register, 17 CFR Parts 228, and 229 (December 29, 2006) [71 FR 78338] (the “Amending Release”)

Dear Ms. Morris:

We are independent board and management advisors on executive compensation and mergers and acquisitions. Additionally, we develop web-based tools for public companies to handle some of the technical aspects of their compensation programs, including our ProxEASE™ 280G Parachute Modeler™, which assists companies in determining and quantifying their post-termination payments and benefits to their named executive officers (NEOs) for proxy disclosure purposes.

We have been assisting our clients in preparing their proxies in accordance with the new proxy disclosure rules, including the Amending Release. In doing so, we have gained some insight into potential practical issues with the way the rules operate and have had a chance to think through some of the more substantive issues confronting companies as they comply with these disclosure rules. The comments we raise are not an exhaustive list of issues, but rather represent the major issues we have come across to date. Given the deadline for comments to the Amending Release (which has already passed), we wanted to get the comments we had to you rather than wait any longer to see what other issues we confront this proxy season.

Overall, the timing of the issuance of the Amending Release has caused some of our clients problems given the short time period they have to understand and comply with the rules prior to the filing of their proxy statements. We are aware of many companies whose NEOs changed after the Amending Release’s rule changes were taken into account, which has touched off a mad dash to try and incorporate new individuals into the tabular and narrative disclosures.

Our Comments

We have arranged our comments to the Amending Release according to their impact on the required tabular disclosures.

Summary Compensation Table

The Amending Release made several changes to the Summary Compensation Table and its related instructions:

- The reporting of equity awards in the Summary Compensation Table was changed to follow the expense recognition methodology under Statement of Financial Accounting Standards No. 123, *Share Based Payment* (revised 2004) (FAS 123R);
 - **Comment:** *If the rules now require companies to follow the accounting rules' expense recognition methodology for purposes of equity compensation disclosures in the proxy, why not also require the same method of reporting for long-term cash awards, i.e., non-equity incentive plan compensation, to achieve greater consistency across all incentive vehicles? Performance-based equity awards that do not have a market condition now require performance estimates to be conducted, i.e., such awards are included in the proxy tables only if it is probable that the performance condition will be achieved, which can result in reversals of previously disclosed amounts or adjustments of compensation throughout the award's performance period. This type of analysis is very similar to the one that would be conducted for the expensing of long-term cash awards, where the payout depends on the performance achieved during a stated period.*
- Companies are now required to include any amounts of salary or bonus elected to be taken as non-cash compensation (stock, equity-based or other forms of non-cash compensation) in the Salary or Bonus columns and requires a footnote that indicates the receipt of such non-cash compensation and, where applicable, refer to the Grants of Plan-Based Awards Table where the stock, option or non-equity incentive plan award elected is reported;
 - **Comment:** *On this issue the Amending Release seemed "pretty clear¹." However, when we reviewed the guidance which was issued on January 24, 2007 by Corporation Finance regarding the Item 402 disclosures², we began to wonder about that conclusion. The Guidance indicates in Question 4.03 that "if the agreement pursuant to which the named executive officer had the option to elect settlement in stock or equity-based compensation was within the scope of FAS 123R ... the award would be reported in the Stock Awards or Option Awards column." We cannot easily conceive of a plan or arrangement that would permit an executive to elect to take cash or equity that would not fall within the scope of FAS 123R. While there may be \$0 fair-value expense from a FAS 123R perspective, the equity awards elected to be taken by an executive in lieu of cash compensation would still fall within the*

¹ Comments of David Lynn during CompensationStandards.com's webcast, *The SEC's December Rule Changes: How They Impact You* (January 11, 2007), archive and transcript available at www.CompensationStandards.com.

² *Item 402 of Regulation S-K – Executive Compensation*, Last Update: January 24, 2007, <http://www.sec.gov/divisions/corpfin/guidance/execcomp402interp.pdf> (the "Guidance").

scope of FAS 123R when determining grant date fair value versus price paid. As a result, if the Guidance trumps the plain language of the instruction set forth in the Amending Release, then anytime an executive elected to take stock, options or another equity-based incentive in lieu of salary or bonus, it would always be reported in the Stock Awards or Option Awards column. At the very least, the apparent discrepancy between the plain language of the instruction from the Amending Release and Question 4.03 of the Guidance should be resolved, and/or the instruction should be revised to reflect the intent of the drafters.

- The amounts in the Stock Awards and Option Awards columns must reflect “the dollar amount recognized for financial statement reporting purposes with respect to the fiscal year in accordance with FAS 123R;”
 - **Comment:** *Again, this instruction appears self evident on its face, and also appears to support comparability of compensation disclosures across companies. However, by abandoning the originally announced use of full grant date fair value, the Amending Release adopts a standard that will cause comparability to be lost until all outstanding equity awards, as normally granted and vested, across all public companies are accounted for in accordance with FAS 123R. This is because some 800 companies accelerated the vesting of their equity awards prior to adopting FAS 123R³. In doing so, they ensured they would not have to recognize an expense under FAS 123R for such awards during the awards’ remaining terms (unless materially modified). But, this also means that two executives at similar companies and holding a similar amount of outstanding equity awards, albeit that one has more equity awards that are vested than the other, would show up with potentially very different amounts and totals in the Summary Compensation Table. Thus, until the equity awards that were accelerated flush through the entire proxy reporting system and all companies have outstanding awards that are vesting based on their normal vesting schedules, comparability is lost. Comparability is also lost for retirement-eligible executives whose awards would have their vesting accelerated upon retirement.*
- Requires that a footnote be included for awards whose financial statement expense is included in the Stock or Option Awards column that discloses all the forfeitures during the year as well as all assumptions made in the valuation.
 - **Comment:** *The footnote to indicate the forfeitures during the most recent fiscal year will make it easier for investors to understand the impact of forfeitures on the expense amounts shown in the Stock Awards and Option Awards columns. However, the requirement to detail all the assumptions used in the valuation will cause confusion. It was not immediately clear to us whether this portion of the instruction applies to all equity awards for which expense was recognized under FAS 123R (which is what we presumed) or to*

³ Jack T. Ciesielski, *The Analyst’s Accounting Observer*, August 15, 2006, at 2.

only those granted during the last fiscal year. However, Question 4.04 of the Guidance clarifies this issue and states that the grant date fair value must be reported for all awards whose expense is included in the Summary Compensation Table. This is redundant as these assumptions would be repeated year after year.

Suggestions

- Synchronize the disclosure of all compensation (cash, equity and non-equity incentives) with the accounting rules to increase consistency of the disclosures and better reflect the amounts attributed to each period covered by a proxy or information statement.
- Clarify the proxy disclosure if an executive (or director) elects to take salary or bonus in equity (even if covered by FAS 123R).
- Move the required footnote disclosure of the material assumptions underlying valuations to the Grants of Plan-Based Awards Table (to join the newly added grant date fair value column), and only require such footnote for the awards required to be included in the Grants of Plan-Based Awards Table, *i.e.*, those granted during the applicable fiscal year, those that are repriced or materially modified, and, in keeping with the suggestion above, those taken in lieu of salary or bonus even if paid (granted) in the subsequent fiscal year.

Grants of Plan-Based Awards Table

The Amending Release also made several changes to the Grants of Plan-Based Awards Table:

- A new column was added that details the grant date fair value of each equity award reported as computed in accordance with FAS 123R;
 - *Comment: This seems straight-forward enough, except that it does not require the footnote disclosure of the material assumptions that went into the development of the valuations used to come up with the grant date fair values of the equity awards that are disclosed in the new column.*
- For options, SARs and similar option-like instruments that have their exercise or base price adjusted, the incremental fair value will be reported in the newly-added grant date fair value column;
 - *Comment: Again this disclosure appears fairly straight-forward. This instruction also does not require the material assumptions with respect to the determination of the incremental fair value to be set out in a footnote, which information could help investors gain a better understanding of what was done.*

- Instructions have been added that indicate that options, SARs and similar option-like instruments that are granted in connection with a repricing transaction or other material modification must be reported in this Table.
 - *Comment: This instruction is good clarification of what is required. Again, a footnote disclosing the material assumptions underlying the incremental fair value determination may prove useful to investors.*

Suggestions

- Move the currently required footnote disclosure of material assumptions underlying valuations from the Summary Compensation Table to the Grants of Plan-Based Awards Table.
- Require footnote disclosure of the material assumptions underlying any incremental fair values disclosed in the Grants of Plan-Based Awards Table.
- Clarify the reporting of equity awards that are taken in lieu of salary or bonus, and require them to be included in the Grants of Plan-Based Awards Table in the proxy in which the salary or bonus would otherwise have been reported, if the equity is granted in the subsequent fiscal year prior to the filing of the applicable proxy statement.

Additional Comments

We also wanted to share with you some additional comments on the Adopting Release⁴ and the Additional Comment Release⁵.

Summary Compensation Table and Change in Pension Value

The Adopting Release included an instruction to the Summary Compensation Table that indicates that if the aggregate change in pension value is negative, it cannot be included in the Summary Compensation Table but only in a footnote to the table⁶.

- *Comment: Given that the Amending Release permits forfeitures and other adjustments to equity awards' expense recognition for accounting purposes to be reflected in the Summary Compensation Table, not permitting negative changes in pension values to be shown in the Summary Compensation Table would cause an avoidable inconsistency in the compensation disclosures.*

⁴ *Executive Compensation and Related Party Disclosure*, Release No. 33-8732A (Aug. 29, 2006) (the "Adopting Release").

⁵ *Executive Compensation Disclosure*, Release No. 33-8735 (Aug. 29, 2006) (the "Additional Comment Release").

⁶ Instruction 3 to Instructions to Item 402(c)(2)(viii).

Suggestion

- Revise the Instructions to the Summary Compensation Table to permit negative changes in pension value to be reflected in the Summary Compensation Table to increase the consistency of the reporting methodology across the different forms of compensation.

Equity Awards and NQDC

In working with the rules from the Adopting Release and the Amending Release, one question we have confronted is how to report restricted stock units (RSUs) after the year in which they have vested but remain unpaid. Based on the rules for the named executive officers, it appears that such RSUs would need to be disclosed in the Nonqualified Deferred Compensation Table through the year they are paid out (assuming an executive remains a named executive officer for such period). Also, for directors, because the rules generally applicable to the named executive officers' compensation apply to them⁷, it appears that such RSUs held by directors would or should be disclosed in a footnote as deferred compensation, and, at the very least, as outstanding stock awards at fiscal year end.

- *Comment: While RSUs would be classified as deferred compensation for purposes of Section 409A of the Internal Revenue Code of 1986, as amended, tax code classifications have generally not controlled the compensation disclosures in the proxy. Extensive disclosure requirements applicable to equity awards (i.e., disclosure in the Summary Compensation Table, the Grants of Plan-Based Awards Table, the Outstanding Equity Awards at Fiscal Year-End Table, and the Option Exercises and Stock Vested Table) and the disclosure of vested but unpaid stock can be done in a clearer fashion.*

Suggestion

- We encourage the Commission to issue guidance that would permit RSUs and other equity-based awards to not be disclosable as deferred compensation in the Nonqualified Deferred Compensation Table for executives or by footnote to the Director Compensation Table for directors. The new disclosure rules already provide more than adequate disclosure of such awards, so also having to disclose them as deferred compensation adds an additional and unnecessary burden, which may not be entirely clear to investors.
- Require RSUs that have vested but that have not yet been paid out to be reported in the Outstanding Equity Awards Table at Fiscal Year-End in a new column titled, "Vested But Unpaid Stock Awards."

⁷ See Instruction to Item 402(k) which causes certain Item 402 provisions applicable to executives, including Instruction 4 to Item 402(c), to apply to directors.

Disclosure of Compensation of up to Three Non-executives

The Commission asked for additional comments on its proposal to require compensation disclosure for up to three additional employees. Specifically, the proposal would require companies to disclose the total compensation and job descriptions of up to an additional three most highly compensated employees who are not executive officers or directors but who earn more than any of the named executive officers. The proposed rule was modified in the Additional Comment Release to require such disclosure only for employees who have responsibility for significant policy decisions within either the company, a significant subsidiary or a principal business unit, division, or function. The Commission requested specific feedback on a series of possible modifications of this proposed rule to address comments it had received.

- ***Comment:** With all the changes that have been wrought by the Adopting Release, the Amending Release and the Guidance, we believe it would be prudent to wait to see how disclosures look after at least one proxy season under the new rules before implementing this proposed rule. It may be, as we believe, that the new rules will improve compensation disclosures and make this proposed rule unnecessary. Additionally, given that most companies are still grappling with the changes wrought by the Amending Release and trying to ensure their proxy tables and related disclosures reflect those changes before their proxies are filed this year, asking them to also try and grapple with figuring out their three highest paid non-executives with significant policy decision making authority would be unduly burdensome, particularly after the Amending Release's reclassification of equity compensation for the prior fiscal year.*

Suggestion

- Do not implement this proposed rule.
- If this proposed rule is to be implemented, then delay its effective date until at least next proxy season (during 2008) so that companies are not overly burdened by trying to comply with the rule in 2007.

Ms. Nancy M. Morris, Secretary
Securities and Exchange Commission
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Conclusion

We hope this letter explains our comments on the Amending Release. If you have any questions about our comments or suggestions, we would be happy to discuss these with you. Please call us at (847) 996-3960 or e-mail us at edward.hauder@exqty.com or mike.sorensen@exqty.com at your convenience.

Best Regards,

Exequity LLP



Edward A. Hauder



Michael Sorensen

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