

April 22, 2010

Senator Christopher Dodd, Chair
Senate Committee on Banking, Housing and Urban Affairs
448 Russell Senate Office Building
Washington DC 20510-0702
Fax: 202-224-1083

**Re: Global Institutional Investor Support for Corporate Governance Provisions
in Financial Reform Legislation**

Dear Senator Dodd:

We write as global asset managers/owners of over \$1.6 trillion to express our strong support for legislation to create the Restoring American Financial Stability Act of 2010 (the "Act"), which was favorably reported out of the Senate Committee on Banking, Housing and Urban Affairs.

Among the primary causes of the economic crisis were massive failures of oversight on both the regulatory and corporate governance levels. The damage that was done to the real economy, and to the participants in our funds, was staggering. Much of that damage can never be repaired. All eyes are now on Congress. Only Congress has the power to address many of the underlying causes of this global economic catastrophe.

As institutional investors that act on behalf of millions of individual beneficiaries, we have billions of dollars invested in United States companies and have a keen interest in both the integrity and success of United States markets. As corporate governance rights have improved in other developed markets, the United States has been falling behind. Governance Metrics International currently ranks the United States behind Australia, Canada, Britain and Ireland on quality of corporate governance. Investors in many emerging markets even have fundamental corporate governance rights that are not available in the United States. It is critical that Congress and the President act promptly to reverse this trend before additional damage is done to the United States investment climate.

Some of us have previously written to President Obama and Congressional leaders in support of financial and corporate governance reform. A letter from 2009, which describes our concerns on corporate governance issues, is attached for your reference.

The Act contains corporate governance reforms that have been sought by investors for years. We urge the Senate to pass the Act, without dilutive amendments. Although there are many important reforms in the legislation which merit enactment, we would like to highlight the following provisions which we strongly support:

- **Majority Voting:** The plurality vote standard, which is still used for election of unopposed director candidates at 75 percent of companies in the Russell 3000, is widely viewed as one of the most undemocratic electoral processes ever used. During the 2009 proxy season, 91 director candidates at 49 United States public companies failed to receive a majority of shareholder votes. Nonetheless, all of those directors retained their seats, including two who submitted resignations but were reappointed by the board. The Act would restore accountability to directors and rationality to the electoral process.
- **Proxy Access:** Shareowners at United States public companies rarely have the right to call a shareholder meeting to remove ineffective directors. Consequently, the only practical way for them to put forth alternate director candidates when a board has become ineffective is through an expensive proxy fight. This is both inefficient and serves to insulate incompetent boards and management from accountability. From our experience in Britain, Australia, the Netherlands, Italy and other markets where directors may be removed or alternative candidates put on the proxy by shareowners, we have found that proxy access improves the quality of dialogue between shareholders and directors, without being disruptive to companies or broadly generating election contests. It has also resulted in boards putting forth higher quality and less conflicted candidates.
- **Say on Pay:** Misaligned executive remuneration practices and excessive pay awards encouraged inordinate risk-taking that was one of the primary causes of the economic disaster. United States pay practices also influence executive remuneration structures and amounts in other markets. In order to encourage better alignment of compensation practices with performance, Britain, Australia, Germany, Sweden, Spain and France, as well as companies in Canada and Switzerland, now require advisory shareholder votes on executive compensation. The Netherlands and Norway use binding shareholder approval votes on executive compensation policies. Nearly 60 non-TARP companies in the United States have voluntarily adopted say on pay to obtain shareowner input on their compensation practices. We believe it is time to level the playing field for these progressive companies by requiring all public companies to adopt say on pay as a means of providing boards with shareowner responses to their pay practices – without removing any board authority on pay decisions.
- **Golden Parachute Approvals:** In addition to say on pay, we would like to see the legislation strengthened by incorporating provisions from legislation passed in the House of Representatives to require shareholder approval of golden parachutes (payments made to executives when their company is acquired). Australia recently adopted a shareholder approval requirement for golden parachute payments in excess of one year's salary. Use of a similar provision here would help to change the 'pay for failure' culture that has become such a problem in the United States.
- **Executive Compensation Practices:** From hearings held in 2007 by the House Committee on Oversight and Government Reform, it is clear that much of the

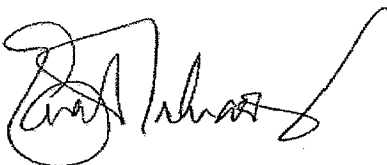
misalignment in executive compensation incentive structures has been encouraged by lack of independence on the part of compensation advisors and compensation committee members. The Act would mandate development of independence criteria for compensation committee consideration when retaining advisors. It would also require that all members of compensation committees be independent directors, mandate the clawback of incentive compensation inappropriately paid based on results that are later restated, and require that companies report the relationship between executive compensation and company performance. We see these provisions as critical to restoring investor trust in integrity of the executive compensation process.

- **Independent Board Chair:** The Act would direct the SEC to develop rules requiring that companies disclose why they have adopted their board leadership structure. While this is a move in the right direction, we note that use of an independent board chair is a firmly established practice in Britain, Canada and Europe. The absence of a strong independent board chair is viewed by most investors as a structural impediment to effective board oversight of management that presents unnecessary shareholder risk. We urge Congress to strengthen this provision by adopting a presumption that boards have an independent chair, with ability to depart from this governance structure if a full explanation is provided.

We hope these comments will be helpful during Congressional deliberations. These are critically important reforms, both for future stability of the global economy and the ability of United States companies to attract capital from investors at favorable rates.

Please contact us if you have any questions or would like additional information.

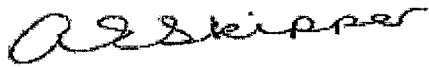
Respectfully submitted,



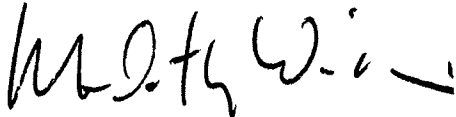
Eva Halvarsson
CEO
Second Swedish National Pension Fund – AP2 (Sweden)



Paul Frentrop
Head of Corporate Governance
APG Asset Management (The Netherlands)



Anita Skipper
Corporate Governance Director
Aviva Investors (UK)




Meredith Williams
Chief Executive Director
Colorado PERA (USA)



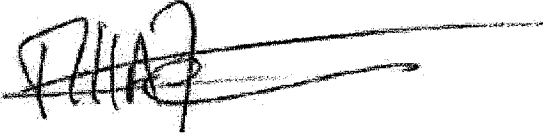
Abigail Herron
Corporate Governance Manager
The Co-operative Asset Management (UK)



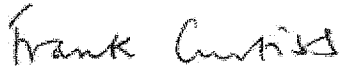
Mike McCauley
Senior Officer, Investment Programs & Governance
Florida State Board of Administration (USA)



Bess Joffe
Associate Director
Hermes Equity Ownership Services Ltd. (UK)



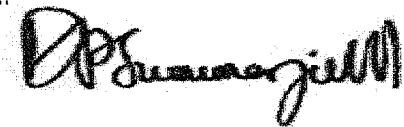
Marcel Jeucken
Head of Responsible Investment
PGGM Investments (The Netherlands)



Frank Curtiss
Head of Corporate Governance
Railpen Investments (UK)



Alison Kennedy
Head of Governance Engagement
Standard Life Investments (UK)



Dr. Daniel Summerfield
Co-Head of Responsible Investment
Universities Superannuation Scheme (UK)

cc: President Barack Obama
Senate Banking Committee Members
Senator Harry Reid, Senate Majority Leader
Senator Mitch McConnell, Senate Minority Leader
Representative Barney Frank, Chair, House Committee on Financial Services

13 February 2009

The Honorable Barack Obama
President of the United States
The White House
1600 Pennsylvania Avenue NW
Washington, DC 20500

The Honorable Nancy Pelosi
Speaker of the House
United States House of Representatives
235 Cannon House Office Building
Washington, DC 20515-0508

The Honorable Harry Reid
Senate Majority Leader
522 Hart Senate Office Building
Washington, DC 20510

Re: United States Financial Market and Corporate Governance Reforms

Dear Mr. President, Madam Speaker and Senator Reid:

We write as global investment managers with more than \$1.3 trillion of assets under management, representing the savings and pension assets of 15 million individuals, to express our strong support for critical legal reforms to the United States financial markets and corporate governance practices.

Mr. President, in your inaugural address you highlighted the need for change in the financial markets, "The state of the economy calls for action, bold and swift, and we will act - not only to create new jobs, but to lay a new foundation for growth." We wholeheartedly agree. The time to restore investor trust in the integrity of America's capital markets and public corporations is long overdue.

We believe that fundamental reforms are needed to build the foundation of which you spoke. In particular, we see the United States markets as desperately needing:

- Collaborative development of best corporate governance practices, with a flexible 'comply or explain' company reporting approach; and
- Enactment of reforms described in the attached December 2, 2008 letter to Speaker Pelosi from the Council of Institutional Investors, namely:
 - Shareowner access to the proxy;
 - A majority vote standard for election of corporate directors;
 - Transition to independent board leadership with a split chair/CEO;

- An advisory shareholder vote on executive compensation;
- Repeal of the authority for brokers to vote uninstructed shares;
- Stronger provisions for clawing back illicitly-paid executive compensation;
- Limits on the use of conflicted executive compensation consultants; and
- Restrictions on executive severance payments that reward poor performance.

Over the last decade, foreign ownership of United States corporate securities has more than tripled.¹ Although many of the undersigned investors are located outside of the United States, we have collectively invested billions of dollars in United States companies. Accordingly, we have a keen interest in both the integrity and success of the United States market.

As global investors, we also recognize that practices in the United States and other major markets influence each other. Because practices in other markets have been improving, investors have begun to re-evaluate the relative investment risks presented by corporate governance practices in the United States.² To remain competitive in this environment, we believe the United States must promptly embrace the reforms we identified above and which are further discussed below.

Executive compensation practices

Executive pay at United States companies has too often been unrelated to company performance. As each of you has observed, executive compensation in the United States has reached outlandishly unnecessary levels compared to every other world market. Yet, despite these extravagant compensation practices, United States companies have not effectively managed risk exposures or produced outsized returns for shareholders.

From Congressional hearings held in 2007, we are aware that executive compensation plans at United States companies are often developed by consultants that have conflicts of interest due to lucrative contracts awarded them by the same executives covered by the plans.³ Far too often, we have seen executives receive huge severance and change-in-control payments that effectively function as a reward for their prior poor performance. Improperly-paid incentive compensation based on fraudulently manipulated results has rarely been recovered, even though clawback provisions could be used to avoid illicit windfalls. These practices have undermined investor confidence in the market and should be prohibited where they have not been approved by a vote of shareholders.

Shareholder advisory vote on executive compensation

In many other developed markets, shareholders and directors regularly interact on issues relating to executive compensation. This communication often occurs in the context of shareholder votes on company pay practices. For example, Britain implemented advisory

¹ Congressional Research Service Report for Congress, *Foreign Ownership of US Financial Assets: Implications of a Withdrawal*, January 14, 2008.

² For example, Governance Metrics International currently rates Ireland, Canada, Britain and Australia above the United States in quality of corporate governance.

³ House Committee on Oversight and Government Reform, *Executive Pay: Conflicts of Interest Among Compensation Consultants*, December 2007.

votes in 2003. They have been credited there with moderating the rate of increase in executive compensation, dramatically increasing the use of incentive pay and reducing executive pay levels at companies with negative operating performance.⁴ Both companies and shareholders have seen this vote process as beneficial.⁵

Some countries, including the Netherlands, use binding shareholder votes, where general principles underlying compensation plans must be approved by shareholders. However, shareholder votes on executive compensation are advisory in most other markets. We see adoption of such an advisory shareholder vote as a critical first step toward addressing the executive compensation problems that permeate the United States market.

Independent Board Chair Separate from the CEO

Board leadership is another area where the United States is falling behind. Appointment of an independent board chair is the predominant practice in Britain, Europe and Canada. However, barely more than one in five United States companies in the S&P 500 has an independent board chair.⁶ Even the National Association of Corporate Directors recently issued a report which emphasizes the importance of independent board leadership and says that boards without an independent chair should explain why they have adopted such an approach.⁷

We see the absence of a strong, independent chair as a structural impediment to effective board oversight of management and a factor that presents increased risk to shareholders. A split CEO/Chair structure for independent board leadership should be made standard practice at public companies in the United States.

Shareholder Access to the Proxy

Many shareholders view the United States director election process as being amongst the most undemocratic in the developed markets. Company owners rarely have the right to call a shareholder meeting to remove ineffective directors, and they have no practical way of putting forth director candidates at uncooperative companies without mounting an expensive proxy fight.

We all invest in markets that allow shareholders to remove ineffective directors and/or more easily put candidates up for election at the annual meeting. Our experience in Britain, Australia and the Netherlands, for example, is that boards whose members may be removed and replaced by shareholders are more attuned to investor opinion and much more likely to engage in meaningful dialogue with their shareholders. Moreover, we have found that availability of these rights has not proved to be disruptive to companies

⁴ Keith L. Johnson and Daniel Summerfield, *Shareholder Say on Pay*, International Corporate Governance, November 2008.

⁵ Stephen Davis and Stephen Alogna, *Policy Briefing No. 2: Talking Governance, Board-Shareowner Communications on Executive Compensation*, The Millstein Center for Corporate Governance and Performance, Yale School of Management (2008).

⁶ RiskMetrics Group, *Board Practices: Trends in Board Structure at S&P 1,500 Companies*, December 17, 2008.

⁷ National Association of Corporate Directors, *Key Agreed Principles to Strengthen Corporate Governance for U.S. Publicly Traded Companies*, October 2008.

or encouraged election contests. Instead, boards in those markets are incentivized to put forth higher quality independent director candidates that will be approved by shareholders. We believe that companies in the United States would benefit from creation of shareholder rights to place board candidates on the proxy.

Majority Vote Standard for Election of Directors

We applaud the recent movement in the United States toward adoption of a majority shareholder vote requirement for election of director candidates. However, the majority vote process that has been adopted by most companies still allows boards to override a shareholder vote and keep the rejected director in place.⁸

Our experience in other developed markets that use a true majority vote standard for election of corporate directors, including Britain, the Netherlands, Australia, New Zealand, Germany and France, has been positive. We find that it encourages better communications between shareholders and directors and strengthens alignment of interests between the board and company owners. The majority vote standard should be applied to all United States public companies.

Broker votes

Shares that are not voted in advance of an annual meeting typically end up being voted by brokers (who hold them in brokerage accounts) in favor of the company director slate. This amounts to legalized ballot stuffing and has changed the vote results in a number of elections. For example, uninstructed broker votes changed the outcome of director elections at the Washington Mutual 2008 annual meeting and the 2007 CVS annual meeting.

Since 2006, the NYSE has twice proposed abolishing the ability of brokers to vote uninstructed shares in director elections, but the SEC has failed to approve the change. It is time for the SEC to take action.

Corporate governance best practices

Finally, we believe the United States market would benefit from an interactive process involving companies, investors, regulators and other stakeholders (such as accounting, compensation design, proxy voting and consumer representatives) to develop and regularly review corporate governance best practices. When combined with a comprehensive disclosure regime using a 'comply or explain' approach similar to what is already in place in many other developed markets, this would encourage improved governance practices and promote ongoing communication between companies and their owners about best practices, while ensuring that individual companies retain the flexibility to adopt practices that meet their needs.

For example, a 'comply or explain' approach might identify annual board member elections as a best practice. Boards that decided to depart from that practice would be

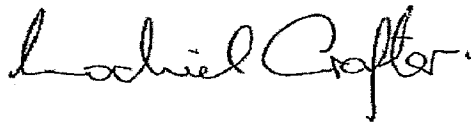
⁸ For example, three directors at Axcelis Technologies received more than 57 percent votes against their election at the 2008 shareholder meeting, but the board refused to accept their resignations. RiskMetrics, *Postseason Review: Withheld Votes*, October 17, 2008.

obligated to provide an explanation in the annual report to shareholders. Similarly, standards for disclosure of material extra-financial factors (such as the business ramifications of a company's carbon emissions, reputation risks, product obsolescence, etc.) might also be addressed through a 'comply or explain' process.⁹ Of course, effectiveness of this approach would require adoption of the other reforms outlined in this letter to ensure an appropriate balance between management, the board and shareholders.

We would like to see this process led in the United States by an appropriate government entity, with a goal for implementation of a best practices 'comply or explain' disclosure requirement in 2010. Other markets, including Britain, the Netherlands and Australia, have gone through similar processes and might be evaluated as models. We would be happy to assist with that process and believe that participation from outside of the United States would help to ensure broad support by investors that provide the necessary capital to United States companies.

We look forward to working with you in the near future on these important issues and hope you will contact any of us if we can be of further assistance.

Very truly yours,



Lochiel Crafter
Chief Executive Officer
ARIA - Australia



Vidette Bullock Nixon
Director Corporate Relations
General Board of Pension and Health
Benefits – The Methodist Church - US



Anita Skipper
Corporate Governance Director
Aviva Investors - UK



Lance E. Lindblom
President and Chief Executive Office
The Nathan Cummings Foundation - US

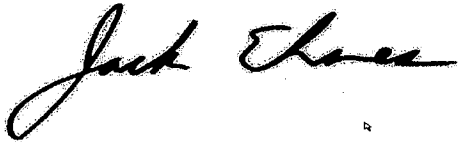
⁹ For additional information on extra-financial disclosure, see the International Corporate Governance Network Statement and Guidance on Non-Financial Business Reporting at the following website address: http://www.icgn.org/news/releases/ICGN_Statement_NFBR.pdf. Additional information about developing a comply or explain reporting approach to corporate governance best practices is available from the International Finance Corporation Global Corporate Governance Forum website at: [http://www.gcgf.org/ifcext/cgf.nsf/AttachmentsByTitle/PSO10/\\$FILE/GCGF+PSO+issue+10+12-8-08.pdf](http://www.gcgf.org/ifcext/cgf.nsf/AttachmentsByTitle/PSO10/$FILE/GCGF+PSO+issue+10+12-8-08.pdf).



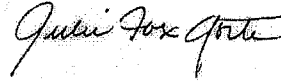
Doug Pearce
Chief Executive Officer
Chief Investment Officer
BC Investment Management Corporation -
Canada



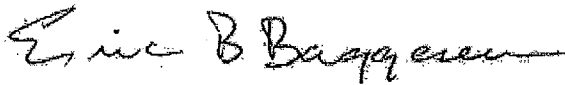
Robert Walker
Vice President, Sustainability
Northwest & Ethical Investments, L.P. -
Canada



Jack Ehnes
Chief Executive Officer
California State Teachers' Retirement
System - US



Julie Fox Gorte
Senior Vice President for
Sustainable Investing
Pax World Management Corporation - US



Eric Baggesen
Senior Investment Officer Global Equity
California Public Employees' Retirement
System - US



Johan van der Ende
CIO
PGGM Investments - Netherlands



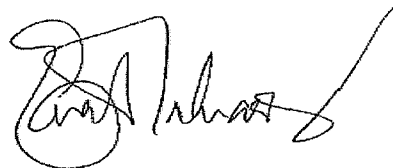
Shireen Muhiudeen
Managing Director
Corston-Smith Asset Management -
Singapore



Frank Curtiss
Head of Corporate Governance
Railpen Investments - UK



Dr. Dominique Biedermann
Executive Director
Ethos - Switzerland

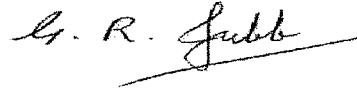


Eva Halvarsson
CEO
Second Swedish National Pension Fund -

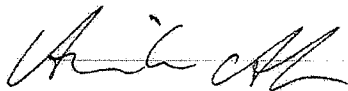
AP2 – Sweden



Elizabeth E. McGeveran
Senior Vice President
Governance & Sustainable Investment
F&C Management Ltd. – Boston, MA



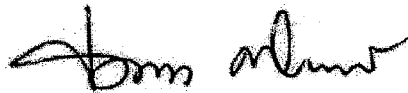
Guy Jubb
Investment Director
Head of Corporate Governance
Standard Life Investments Ltd. - UK



Annika Andersson,
Head of Corporate Governance
Fourth Swedish National Pension Fund -
Sweden



Frances Magill
Chief Executive Officer
Statewide Superannuation Trust - Australia



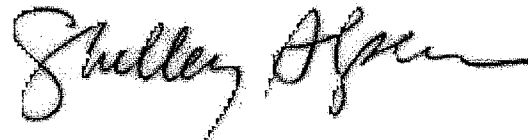
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Government Pension Fund - Thailand



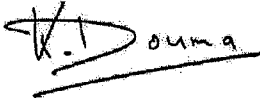
Christina Kusoffsky Hillesöy
Communication Manager and Head of SRI
Third Swedish National Pension Fund -
Sweden




Ian Greenwood
Chairman
Local Authority Pension Fund Forum - UK
(On Behalf of 48 Local Funds)



Shelley Alpern
Vice President & Director of Social
Research & Advocacy
Trillium Asset Management Corporation -
US



Kris Douma
Head of Responsible Investment & Active
Ownership
MN Services N.V. - Netherlands

Authorized 12 Feb 2009 

Terry McCredden
Chief Executive Officer
UniSuper - Australia



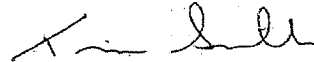
Gary Hawton
Chief Executive Officer
Meritas Financial Inc. - Canada



Peter Moon
Chief Investment Officer
Universities Superannuation Scheme - UK



Chief Investment Officer
The Central Finance Board of the Methodist
Church - US



Timothy Smith
Senior Vice President
Walden Asset Management - US

Attachment: Council of Institutional Investors Letter to Speaker Pelosi

cc: Senator Christopher Dodd, Chair
Senate Committee on Banking, Housing and Urban Affairs

Congressman Barney Frank, Chair
House Committee on Financial Services

Mary Schapiro, Chair
Securities & Exchange Commission

Senator Jack Reed, Chair
Senate Subcommittee on Securities, Insurance and Investment

Representative John Boehner
House Republican Leader

Senator Mitch McConnell
Senate Minority Leader

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