

COUNCIL OF INSTITUTIONAL INVESTORS

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January 12, 2009

The Honorable Christopher Dodd
Chairman
Committee on Banking, Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

Re: Nomination of Mary Schapiro to be chair of the Securities and Exchange Commission

Dear Mr. Chairman:

On behalf of the Council of Institutional Investors, I am writing to suggest several key issues for the Senate Banking Committee to consider exploring during the confirmation hearing for Mary Schapiro to be chair of the Securities and Exchange Commission.

The Council is a nonprofit association of more than 140 public, union and corporate pension funds with combined assets exceeding \$3 trillion. Council members have a significant and long-term commitment to the global capital markets, particularly the U.S. markets. They have lost billions in assets as a result of the global financial crisis.

Council members look to the SEC—the self-professed “investor’s advocate”—to protect investors through robust market oversight of market participants, vigorous enforcement of marketplace rules and regulations and reliable and timely disclosures.

With half of all households and one out of three individuals in the U.S. owning stock, the SEC’s work has never been more important. Unfortunately, the agency’s effectiveness and relevance has been questioned in the wake of the financial crisis and most recently, the Madoff scandal.

The Council strongly supports the existence of an independent, reliable regulator with a mandate of investor protection. The Council believes the SEC, now more than ever, needs a strong leader who can advocate for the agency and its vital role of safeguarding investors. As a result, any candidate for SEC chair must be committed to the commission’s primary mission of protecting investors. And in order to restore trust in U.S. markets, the SEC chair also must be committed to vigorous oversight and enforcement.

The financial crisis has brought the very role of the SEC itself into question. In light of the ongoing debate about the structure of the U.S. financial regulatory system, the Senate Banking Committee should seek Ms. Schapiro’s views on the fundamental issue of the appropriate role for the commission in any regulatory framework.

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Strong regulation alone cannot solve some of the problems that fueled the financial crisis. Effective rules must be buttressed by shareowner-driven market discipline. But investors need stronger tools to hold management and boards accountable. The Council believes that key corporate governance reforms are essential to providing meaningful investor oversight. These measures, which are discussed in the accompanying attachment, would empower shareowners to address some of the problems that contributed to the financial cataclysm and guard against excessively risky corporate behavior in the future.

As the SEC's chief executive, the chair sets the agenda for the commission. The Council thus believes it is important that the Senate Banking Committee ask any candidate for SEC chair for a commitment to support efforts to strengthen corporate governance.

The attachment summarizes several key commission-related issues of interest to Council members, with suggested questions for Ms. Schapiro. The Council respectfully requests that the Senate Banking Committee consider including these topics on its list of issues to be raised during her confirmation hearing.

Please feel free to contact me with any comments or questions. Thank you very much.

Sincerely,



Ann Yerger
Executive Director
Council of Institutional Investors

**SEC Chair Candidate Issues
January 12, 2009**

Proxy Access

Proxy access allows shareowners to place their nominees for director on the company's proxy card. In the United States, unlike most of Europe, public companies are not required to provide shareowners with access to the proxy to nominate directors. The only way that shareowners can present alternative director candidates at a U.S. public company is by waging a full-blown election contest. For most investors, that is onerous and prohibitively expensive.

On November 28, 2007, the SEC voted 3-1 to let companies reject shareowner proposals that relate to board nominations or elections. Despite a pledge by SEC Chair Christopher Cox to reconsider the adoption of some form of proxy access for shareowners, the commission has yet to revisit the issue. Commissioners Elisse Walter, Luis Aguilar and Troy Paredes have all expressed support for reconsidering the idea.

The Council believes that a right of access would invigorate board elections and would make boards more responsive to shareowners, more thoughtful about whom they nominate to serve as directors and more vigilant in their oversight of companies.

- ? *If confirmed, would you direct the commission to reconsider the issue of proxy access, and, if so, on what timeline?*
- ? *Do you believe that a right of access is in the interest of investors?*

Broker Voting

Adopted in 1937, New York Stock Exchange Rule 452 allows brokers to vote on certain “routine” proxy proposals if the beneficial owner has not provided voting instructions at least 10 days before a scheduled meeting. The uncontested election of directors is among the proposals the NYSE has considered to be routine. The Council has long argued that director elections are not routine. Also, since broker votes are virtually always cast for management, the Council believes that that the rule taints the integrity of proxy voting by effectively stuffing the ballot box for management. Despite repeated efforts by the NYSE to amend Rule 452 the SEC has taken no action.

In April 2005, the NYSE created a Proxy Working Group to review the exchange’s regulation of proxy voting. The Council testified before the group and urged the NYSE to abolish the broker voting rule or at least bar broker votes in director elections. In October 2006, the NYSE submitted for SEC approval a plan to redefine director elections as “non-routine,” in effect eliminating uninstructed broker votes from director elections. The SEC responded to the proposal with comments. On May 23, 2007, the NYSE board resubmitted the original proposal with an amendment to exclude board elections at investment companies (mutual funds).

The SEC took no action. In a September 24, 2007 letter to its listed companies, the NYSE reported that its plans to eliminate uninstructed broker votes from director elections had been sidelined by the commission. The Council sent a letter to the SEC criticizing the agency's failure to act on the NYSE proposal. The SEC said in its reply that it was still studying the issue.

- ? *If confirmed, would you revisit the issue of broker voting, and, if so, on what timeline?*
- ? *Do you believe that uninstructed broker votes should not be counted in director elections?*

International Accounting and Auditing Standards

Globalization of world markets is driving demand for uniform high quality financial reporting standards. The most widely used set of accounting standards currently are the International Financial Reporting Standards (IFRS) issued by the independent London-based International Accounting Standards Board (IASB). To date, more than 100 countries, including the European Union member states, either use or plan to adopt some version of IFRS rules.

Allowing IFRS to be used in the United States is controversial. Proponents argue that it would allow investors to compare financial statements of companies worldwide seamlessly, at a lower cost and with less risk of error. Opponents believe IFRS are not as high-quality as GAAP and that permitting their use would entail costly retraining by U.S. accountants and auditors as well as an overhaul of university curricula. Critics also contend that there would continue to be a severe lack of consistency in the implementation, interpretation and enforcement of IFRS standards worldwide.

The SEC voted unanimously on August 27, 2008, to submit for public comment a plan to potentially transition U.S. public companies to IFRS beginning in 2014. According to the proposed roadmap, the SEC intends to vote on the potential adoption of international accounting standards in 2011 after a period of voluntary use of the standards by certain large U.S. companies beginning in 2010.

The Council shares the SEC's goal of a single set of globally recognized high quality financial reporting standards that meet the needs of all investors. But it is unlikely that the SEC's proposal to switch from U.S. accounting standards to international standards starting in 2014 will achieve that goal. As recognized in the Council's policies, many complex issues must be carefully evaluated and resolved prior to the SEC mandating this momentous change in U.S. financial accounting and reporting.

- ? *What are your thoughts on the SEC's recently proposed roadmap for the U.S. adoption of IFRS?*
- ? *Do you agree with the views of many investors that substantive changes to the SEC's proposed roadmap are necessary to ensure that the roadmap results in high quality financial accounting and reporting?*
- ? *Would you consider restoring the requirement that foreign issuers using IFRS publicly provide a reconciliation of their financial statements to U.S. GAAP?*

Credit Rating Agencies

Credit rating agencies issue ratings on certain securities such as corporate bonds and collateralized debt obligations (CDOs). A rating serves as an indicator of the issuer's ability to meet scheduled interest and principal repayments. Investors often rely on ratings when deciding whether to buy or sell securities, especially highly complex products like CDOs. Various statutes and policies require certain institutional investors to hold only securities with investment grade ratings from rating agencies designated by the SEC as Nationally Recognized Statistical Rating Organizations (NRSROs).

The credit rating industry came under heavy fire in 2001 after NRSROs downgraded securities issued by Enron just days before the company filed for bankruptcy. Critics complained that the ratings process lacked transparency and that the ratings business was a cozy club, with high barriers to entry and poorly managed conflicts of interest that contributed to inaccurate ratings.

The Credit Rating Agency Reform Act of 2006 and the subsequent adoption of new SEC regulations for NRSROs sought to remedy these issues. The law granted the SEC the power to establish a new registration system for agencies seeking NRSRO status. Although the law explicitly denies the SEC the power to regulate the ratings methodologies used by the agencies, the commission has the authority to supervise and sanction agencies that engage in anti-competitive behavior or fail to address conflicts of interest. Despite these reforms, critics contend that the rating agencies played a large role in the recent subprime mortgage meltdown.

In an attempt to address these issues, the SEC proposed in June 2008 a new set of reforms, some of which were recently adopted. Still, investors remain wary of the soundness and independence of credit ratings.

- ? *What if any action do you believe the SEC should take regarding NRSROs?*
- ? *Do you believe NRSROs should be held responsible for consistently issuing inaccurate credit ratings, and, if so, how?*

Enforcement

A robust, empowered SEC enforcement division is critical to restoring investor confidence in U.S. capital markets. But the financial crisis and the Madoff scandal have cast a harsh light on the SEC's enforcement efforts. Morale has sunk at the once-proud division. Critics believe a January 2006 change in SEC enforcement policy is partly to blame. The new protocol requires enforcement staff attorneys to seek commission approval of a dollar range for corporate penalties before negotiating settlements. Previously, staff lawyers negotiated settlements first, then brought them to the commission for final approval. The shift has compromised the staff's negotiating clout, resulting in smaller penalties and ultimately weaker enforcement, many believe. Others cite a swing away from strong enforcement action against big public companies and Wall Street firms to an emphasis on petty-fraud cases.

- ? *What are your thoughts on the SEC's existing enforcement policy?*
- ? *Would you consider returning the commission to its prior enforcement process in which preapprovals of settlement ranges are not required?*
- ? *As SEC chair, what will you do to ensure vigorous enforcement to restore investor confidence and trust?*