



**Securities Industry Association**

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May 2, 2006

VIA EMAIL

Nancy M. Morris, Secretary  
U.S. Securities and Exchange Commission  
100 F. Street, NE  
Washington, D.C. 20549-9303

Re: Proposed NASD Rule 2290 Regarding Fairness Opinions  
File Number SR-NASD-2005-080; Release No. 34-53598

Dear Ms. Morris:

The Fairness Opinion Task Force of the Capital Markets Committee of the Securities Industry Association (“SIA”)<sup>1</sup> welcomes the opportunity to respond to the request of the Securities and Exchange Commission (the “Commission”) for comments dated April 4, 2006 in response to the proposal of the National Association of Securities Dealers, Inc. (“NASD”) to establish new Rule 2290 (the “Proposal”) regarding fairness opinion disclosures and procedures applicable to NASD member firms. Many members of SIA are regularly engaged in the process of rendering fairness opinions as part of the financial advisory services they provide in mergers, acquisitions and other similar transactions, and therefore have a significant interest in the development of disclosure and procedural requirements for issuing fairness opinions that will help to maintain public trust and confidence in the M&A process.

**Introduction**

SIA commends NASD and the Commission for undertaking a review of fairness opinion processes and the related disclosures made by member firms to the companies who retain them. SIA is generally supportive of the Proposal and believes that many aspects of the Proposal reflect current practice of most member firms. However, SIA believes that the Proposal

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<sup>1</sup> The Securities Industry Association brings together the shared interests of more than 600 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals, and its personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2005, the industry generated an estimated \$322.4 billion in domestic revenue and an estimated \$474 billion in global revenues. (More information about SIA is available at: [www.sia.com](http://www.sia.com).)

contains a number of overbroad provisions that should be more carefully tailored or otherwise revised in order to achieve the stated objectives for the Proposal. Accordingly, SIA respectfully submits the following comments, which first discuss the purpose and role of fairness opinions in the M&A process, and then address in turn each disclosure and procedural provision of the Proposal.

### **Purpose and Role of Fairness Opinions in the M&A Process**

Financial advisors typically provide fairness opinions in corporate control transactions, including mergers and acquisitions, as well as purchases or dispositions of material assets, divisions or subsidiaries. Fairness opinions are prepared for and delivered to a company's board of directors (or committee of the board of directors, as applicable), and express a view as to the fairness, from a financial point of view, to the company or its shareholders, as applicable, of the consideration to be paid or received in the proposed transaction, or of the exchange ratio in the case of stock-for-stock transactions. As such, the scope of fairness opinions is limited to the financial terms of the transaction, and, as noted by NASD, the concept of fairness does not indicate whether the consideration to be paid or received (or the exchange ratio, as applicable) in a proposed transaction is the best that could be attained, nor does a fairness opinion evaluate whether the amount and nature of the compensation from the transaction underlying the opinion benefits any individual officers, directors or employees, or class of such persons, relative to the benefits to shareholders of the company. Fairness opinions are prepared for the use and benefit of boards of directors (or committees thereof) as part of their exercise of due care in evaluating a potential transaction, and customarily indicate that they do not constitute recommendations to shareholders as to how shareholders should vote on a proposed transaction, or whether they should take any other action (such as tendering shares into a tender or exchange offer). Fairness opinions are based upon market, economic and other conditions as they exist on the dates the opinions are delivered, and are further based on the information that has been made available to the opinion provider as of such dates. In this regard, financial advisors analyze the information that is provided to them and other publicly available information that they deem relevant, but they rely on the accuracy and completeness of all such information, and in giving fairness opinions, financial advisors almost always do not assume any responsibility for independently verifying such information. The terms relating to the scope and use of fairness opinions and the ability of financial advisors to rely without independent investigation upon the information provided to them are generally embodied in the engagement letters that are entered into by financial advisors and companies and, in our experience, are almost always reiterated in the opinions themselves.

While fairness opinions are of limited scope and purpose, SIA believes that the meaning and purpose of such opinions is well understood within the M&A community, including boards of directors, transaction counsel, both federal and state courts, and the Commission, and that practice with regard to fairness opinions has evolved over time and continues to evolve with input from those participants. Although not required by statute or regulation, in the past twenty years fairness opinions have become a regular feature of corporate control transactions and play an important role in helping directors to satisfy their fiduciary duties under state corporate law to

act with due care and in an informed manner.<sup>2</sup> In many states, directors are entitled to rely in the performance of their duties upon the advice they receive from professional advisors, including financial advisors.<sup>3</sup> When fairness opinions are delivered to the boards of directors of publicly-traded companies, they are frequently disclosed (depending upon the form of transaction) in filings made by the parties to such transaction with the Commission.

## **Proposed Disclosure Requirements**

**Scope of Proposed Rule 2290.** The disclosure requirements under proposed Rule 2290 would apply to any member firm issuing a fairness opinion “that may be provided, or described, or otherwise referenced to public shareholders . . .” SIA is concerned that this phrase is overbroad and vague, and thereby fails to provide member firms with adequate guidance as to which fairness opinions they deliver will be subject to the disclosure requirements of the Proposal. For example, a fairness opinion that a member firm believed would not be subject to the Proposal at the time the opinion was delivered because no disclosure to shareholders was required or contemplated could thereafter become subject to the Proposal—at a time when it is too late to include the required disclosures in the opinion letter—if the company receiving the opinion included a casual reference in a press release or other disclosure that it had received a fairness opinion from a member firm in connection with the transaction. While member firms can attempt through the terms of their engagement letters to restrict or limit public references to their fairness opinions by clients, member firms ultimately do not have the ability to prevent disclosures by their clients in press releases, in filings with the Commission or in other settings. As a result, SIA believes that the phrase “provided, or described, or otherwise referenced” should be modified to provide member firms with a more precise standard for determining when the disclosure requirements under the Proposal will apply. Accordingly, SIA would support the scope of Proposed Rule 2290 if it were clarified to apply to a member firm issuing a fairness opinion that is reasonably likely to be included or summarized or referred to in disclosure documents required to be filed with the Commission by clients with a class of equity securities registered under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and disseminated to holders of such equity securities in connection with a vote or other investment decision relating to a change of control transaction that is the subject of the fairness opinion.<sup>4</sup>

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<sup>2</sup> See, e.g., Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).

<sup>3</sup> See, e.g., 8 Del. C. § 141(e) (“A member of the board of directors . . . shall, in the performance of such member’s duties, be fully protected in relying in good faith . . . upon such information, opinions, reports or statements presented to the corporation by . . . any other person as to matters the member reasonably believes are within such other person’s professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation”); N.Y. Bus. Corp. Law § 715 (McKinney 2005); and Cal. Corp. Code § 5231 (West 2005).

<sup>4</sup> Fairness opinions are routinely disclosed in connection with certain filings with the Commission. See, for example, Schedule 14A, Item 14(b)(6) (Proxy Statement pursuant to Section 14(a) of the Exchange Act); Schedule 14C, Item 1 (Information Statement pursuant to Section 14(c) of the Exchange Act); Form S-4, Item 4(b) (Registration Statement under the Securities Act of 1933, as amended); Rule 13e-3 Transaction Statement on Schedule 13E-3, Item 9 (for “going-private” transactions pursuant to Section 13(e) of the Exchange Act); and Solicitation/Recommendation Statement on Schedule 14D-9 under the Exchange Act.

**Proposed Rule 2290(a)(1).** Proposed Rule 2290(a)(1) would generally require a member firm issuing fairness opinions to disclose whether such member has acted as a financial advisor to any transaction that is the subject of the fairness opinion, and, if applicable, that it will receive compensation for (A) rendering the fairness opinion that is contingent upon the successful completion of the transaction, or (B) serving as an advisor that is contingent upon the successful completion of the transaction. As a drafting matter, SIA notes that member firms act as financial advisors to companies that are party to a transaction, rather than as advisors to the transactions themselves, and would respectfully suggest that the phrase “financial advisor to any transaction” be modified to refer to “financial advisor to any company that is a party to the transaction.” Subject to this modification, SIA supports this provision of the Proposal and believes that it is consistent with the current disclosure practices of most member firms.

**Proposed Rule 2290(a)(2).** Proposed Rule 2290(a)(2) would generally require a member firm issuing fairness opinions to disclose whether such member will receive any “other payment or compensation contingent upon the successful completion of the transaction.”

SIA is generally supportive of the disclosure of contingent payments or compensation but believes that, as currently drafted, this provision is overbroad and that member firms would not be able to comply with the literal terms of this disclosure requirement. SIA believes that member firms do not have the ability to track whether they would receive any payment or compensation, no matter how small or remotely related to the transaction, from any client of that firm contingent upon the successful completion of a transaction. For clarity’s sake, SIA believes that it would be more appropriate to require disclosure as to whether member firms will receive any other payment or compensation contingent upon the successful completion of the transaction from the member firm’s client receiving the fairness opinion or the counterparty to the transaction. For example, members of the Fairness Opinion Task Force believe that when a member firm is issuing a fairness opinion subject to the Proposal in a sell-side transaction, and the purchaser has agreed, at or prior to the time the fairness opinion is delivered, to use financing offered by the member firm or to have the member firm participate in the financing for the transaction, the member firm should disclose that contingent fee arrangement in the fairness opinion. Conversely, SIA believes that no such disclosure should be required for contingent payments or compensation to be received from customers that are not a party to the transaction underlying the fairness opinion.<sup>5</sup> SIA also believes, however, that the disclosure requirement under this provision of the Proposal should not require member firms to collect information over internal walls or other information barriers, which have often been established by member firms with the encouragement of regulators to protect the confidentiality of non-public information.

In response to the Commission’s request for comment regarding the quantification of contingent fees, SIA believes that any rule adopted should not require quantification of the amount of compensation. SIA agrees with NASD that it would be sufficient to disclose that contingent compensation relationships exist with descriptive rather than quantitative disclosures.

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<sup>5</sup> For example, a member firm could receive such unrelated payments or compensation from ordinary course trading activities, or if it had a customer with an investment or financial instrument whose value to the customer, and to the member firm, fluctuated dependent upon completion of the transaction, with the result that the cash proceeds would be swept into a cash account resulting in small incremental fees to the member firm.

SIA further notes that, in many cases, it would be difficult for a member firm to calculate the amount of the contingent consideration at the time a fairness opinion is delivered. Such contingent consideration is often dependent on information that is not available until the transaction is ready to close, such as stock price and balance sheet information, and therefore cannot be calculated at the time the fairness opinion is rendered.

In response to the Commission's request for comment as to whether it would be more informative for firms to specifically state that a "conflict" may exist because of a contingent fee arrangement and to describe the impact of such conflict, SIA believes that fee arrangements with a member firm in connection with the delivery of a fairness opinion should not be characterized as "conflicts" merely because a member firm would stand to receive payment or compensation contingent upon consummation of the transaction, as that form of contingent compensation does not in and of itself represent a conflict.<sup>6</sup> Fee arrangements in M&A transactions are heavily negotiated by the companies who retain financial advisors, and in the experience of the members of SIA's Fairness Opinion Task Force, in most transactions it is companies—and not the financial advisors—that structure the fee arrangement to make all or a substantial portion of the fee contingent upon the closing of the transaction because the companies believe there are benefits to such contingent fee arrangements.<sup>7</sup> SIA respectfully urges the Commission to refrain from suggesting that fee arrangements that are dependent on the success of the underlying transaction represent conflicts of interest or are otherwise per se problematic. SIA believes that any fee arrangement compensating a professional advisor for advice is potentially subject to criticism that there is an incentive to provide the advice that the client wants to receive, whether the fee is payable upon completion of services (or in the case of an M&A transaction, upon closing of the transaction) or at some earlier point in the engagement.

Currently, when companies are seeking to retain advisors to assist them in providing financial and other advice in connection with structuring and negotiating change of control or other M&A transactions, they frequently retain financial advisors that have provided services to them in the past because companies see many benefits in retaining firms (and indirectly the professionals employed there) that already have experience in the relevant industry and are familiar with the company and its business, operation and financial position, and possibly the other party to the transaction. SIA also respectfully submits that there is no per se or presumptive "conflict" in hiring a member firm merely because that firm has existing or prior relationships with a particular company or another party to the transaction, and the Commission

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<sup>6</sup> SIA believes that it is more appropriate to consider fee arrangements within the rubric of "material relationships," as that is the terminology that already applies to the disclosures required by registrants with respect to such arrangements under Item 1015(b) of Regulation M-A (17 CFR § 229.1015), and is also the terminology included in Proposed Rule 2290(a)(3).

<sup>7</sup> Courts have approvingly noted that contingent fee arrangements act as incentives for the financial advisors to seek the best available price in the transaction. See In re The MONY Group Inc. Shareholder Litigation, 852 A.2d 9 at 16 (Del. Ch. 2004) (MONY Group Inc. received a fairness opinion from a financial advisor, which was "incentivized to obtain the best available price due to a fee that was set at 1% of transaction value"); In re Vitalink Communications Corp. Shareholders Litig., 1991 WL 238816, at \*10 (Del. Ch. Nov. 8, 1991), *aff'd sub nom*, Grimes v. John P. McCarthy Profit Sharing Plan, 610 A.2d 725 (Del. 1992) (highlighting a fee agreement as an incentive to seek the best available price).

should not adopt any rule that might have the effect of discouraging companies from retaining financial advisors whom they believe are best qualified and whose judgments they most highly value to advise them with regard to a particular transaction by labeling those existing or prior relationships as “conflicts”.

In addition, a company involved in a change of control or other significant M&A transaction often believes it important to receive a fairness opinion from the financial advisor that has advised it on the relevant transaction because that advisor is most familiar with the process that has led to the transaction, the terms of the transaction, and the valuation issues that may be unique to that particular situation. Companies generally want the financial advisor that has provided on-going valuation advice to them and that has assisted them in negotiating the financial terms of the transaction to provide a fairness opinion in order to demonstrate to the board of directors that the institution that participated in the negotiations is prepared to express its view that the final negotiated price or exchange ratio (in the case of stock-for-stock transactions) is fair from a financial point of view. Indeed, in many circumstances board members would be concerned if the financial advisor that advised the company on the transaction did not also provide a fairness opinion.

**Proposed Rule 2290(a)(3).** Proposed Rule 2290(a)(3) would generally require a member firm issuing fairness opinions to disclose information regarding material relationships between the member and the companies that are involved in the transaction that is the subject of the fairness opinion.

SIA believes this provision as currently drafted is overbroad and respectfully suggests that this disclosure requirement should apply solely to corporate and investment banking services or relationships by or between the member firm and its client or the counterparty to the transaction in the following areas: financial advisory services, underwritings and capital markets services, lending and financing arrangements, and merchant banking or private equity relationships involving direct equity interests by the member firm in either the firm’s client or the counterparty to the transaction.

SIA believes that any rule adopted by the Commission should recognize that numerous groups within member firms (such as asset management groups) and affiliated entities operate independently from other groups within such firms or affiliated entities behind internal walls and information barriers. SIA is concerned that member firms would not be able to collect information regarding material relationships for purposes of making disclosure in a fairness opinion without improperly signaling that a transaction is contemplated, or otherwise violating such established internal walls and information barriers. SIA is also concerned that member firms do not have operating or information systems in place that would allow them to collect information regarding material relationships across all business lines or from affiliated entities on a timely or efficient basis. Finally, SIA believes that, as a drafting matter, the phrase “companies that are involved in the transaction” is unclear and respectfully suggests that it be modified to refer to “companies that are a party to the transaction.”

NASD has proposed that this disclosure would not extend to relationships with affiliates of the member firm. In response to the Commission’s request for comment regarding

whether the proposed disclosure should cover material relationships between the parties to the transaction and affiliates of the member firm providing the fairness opinion, SIA believes that such information would be difficult to obtain unless the scope of such disclosures were properly limited. In order to make this disclosure meaningful, SIA would respectfully suggest that, if the Commission determined to expand the disclosure to include relationships with affiliates of the member firm, this disclosure should be limited to affiliates that are either consolidated subsidiaries of the member firm, or consolidated subsidiaries of the holding company of the member firm. SIA notes that member firms with private equity or merchant banking affiliates may themselves be affiliated (through equity ownership or board representation) with literally hundreds of companies that could have a material commercial relationship with a company involved in the transaction, but these relationships are so indirect and remote from the fairness opinion process that it would be difficult to identify all of these relationships at the time a fairness opinion is delivered without risk of delay or breaches of confidentiality.

Finally, in considering the types of relationships between member firms and their clients that would constitute material relationships, SIA respectfully disagrees with NASD's suggestion that such material relationships would include a member firm's service as market maker or asset manager, or the member firm's provision of research coverage. SIA generally believes that these types of service are not material within the context of a relationship between a member firm and a client. Moreover, information pertaining to asset management and other similar functions would be both difficult to obtain for purposes of fairness opinion disclosures due to internal walls and information barriers, and also inappropriate to disclose in a fairness opinion due to confidentiality and privacy considerations.

**Proposed Rule 2290(a)(4).** Proposed Rule 2290(a)(4) would generally require a member firm issuing fairness opinions to disclose the categories of information that formed a substantial basis for the fairness opinion that was supplied to the member by the company requesting the opinion concerning the companies involved in the transaction, and whether any such information in each such category has been independently verified by the member.

In arriving at fairness opinions, financial advisors rely upon the information that is provided to them during the course of a transaction, as well as upon publicly available information. The members of SIA's Fairness Opinion Task Force are not aware of any member firms who currently assume responsibility for independently verifying information that they receive from companies or the counterparties to the transaction, and the fact that they do not assume such responsibility for independently verifying such information is typically a term of the engagement letters and also disclosed in fairness opinions.<sup>8</sup>

NASD notes that the Proposal would not require a member to independently verify data provided by the issuer, which SIA believes is the correct approach. In response to

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<sup>8</sup> Significantly, many courts have accepted that financial advisors can disclaim responsibility for independently verifying information they receive from companies. See, e.g., In re AOL Time Warner, Inc. Sec. & "ERISA" Litg., No. 1500, 02 CIV 5575 (S.D.N.Y. May 5, 2004); In re Reliance Sec. Litig., 135 F.Supp.2d 480 (Del. Ch. 2001); In re Global Crossing, Ltd. Sec. Litig., 313 F.Supp.2d 189 (S.D.N.Y. 2003); Goodwin v. Live Entertainment, Inc., Del. Ch., 1999 WL Del. Ch. LEXIS 5 (Jan. 22, 1999).

the Commission's request for comment on whether member firms should be required to obtain independent verification of information supplied by the company requesting the opinion, SIA is deeply concerned that imposing a duty of verification on member firms would dramatically change the role of fairness opinion providers in the M&A process, and the requirement for independent verification (whether imposed on member firms or others) would intrude upon corporate decision-making of boards of directors by dictating what services must be obtained from outside service providers. SIA believes that mandating independent verification would harm companies and the M&A process by causing significant delays, increasing risks of leaks of confidential and sensitive transaction information, and significantly increasing costs. SIA believes that much of the information provided to financial advisors by companies in the transaction (such as projected earnings and revenues, expected cost-savings and synergies, industry trends and growth rates, to use the examples of categories of information cited by NASD in the Proposal), and other information that financial advisors rely upon in the preparation of fairness opinions, such as information about other companies and transactions that are used in comparable company and comparable transaction analyses, is simply not susceptible to independent verification, or at least not in the context of a financial advisory or fairness opinion assignment. SIA respectfully notes that it does not believe that it would be appropriate for the Commission to adopt a rule requiring member firms to verify information provided by companies and other parties to the transaction, as SIA believes that companies retain financial advisors to provide financial advisory services, such as financial analysis and strategic advice, and not to undertake independent verification of the information provided to them. SIA suggests that it is the responsibility of a company's management and board of directors to insure that the information provided to member firms as part of the fairness opinion process is accurate in all material respects.

In light of the fact that most of the information forming a substantial basis for the opinion cannot be independently verified, SIA is uncertain what disclosure purpose would be served by requiring member firms to identify what categories of information formed a substantial basis for the opinion if the disclosure will go on to state that such information was not independently verified. As a result, SIA does not believe that disclosure of the categories of information that formed a substantial basis for the opinion will ultimately provide meaningful information to the reader of the fairness opinion. Should the Commission decide, notwithstanding the foregoing considerations, to include a disclosure requirement as to categories of information that formed a substantial basis for the fairness opinion, as a drafting matter SIA believes that the phrase "companies involved in the transaction" is unclear, as there may be numerous companies that are involved in a transaction at various stages in one form or another that are ultimately not relevant to the transaction that is the subject of the fairness opinion. As an alternative, SIA respectfully suggests that this phrase be modified to refer to "companies that are a party to the transaction."

**Proposed Rule 2290(a)(5).** Proposed Rule 2290(a)(5) would generally require a member firm issuing fairness opinions to disclose whether the opinion was approved or issued by a fairness committee. SIA supports this provision of the Proposal, and the members of SIA's Fairness Opinion Task Force believe that most member firms already require that fairness committees approve a fairness opinion before it may be rendered.

## Procedural Requirements

**Proposed Rule 2290(b)(1).** Proposed Rule 2290(b)(1) would generally require any member firm issuing a fairness opinion have procedures that address the process by which a fairness opinion is approved by a firm, including the types of transactions and the circumstances in which the member will use a fairness committee to approve or issue a fairness opinion. Subsection (C) of Proposed Rule 2290(b)(1) would further require that such procedures address “the process to promote a balanced review by the fairness committee, including review and approval by persons who do not serve on or advise the ‘deal team’ to the transaction.” SIA notes that in the course of discussing transactions or reviewing proposed fairness opinions, the fairness committees at many member firms regularly do provide advice to the ‘deal teams’ with regard to the terms of the proposed transaction, negotiating strategies for the client, and other matters, as do senior M&A bankers outside of the fairness opinion committee process.<sup>9</sup> So as not to impair these important functions or preclude individuals from serving on a fairness committee who give advice on a transaction but who are not members of the ‘deal team,’ SIA would support this provision of the Proposal if it were revised to provide that the process would include “review and approval by persons who do not serve on or advise (other than in their capacities as committee members or in the ordinary course as senior bankers) the ‘deal team’ to the transaction” (emphasis added).

**Proposed Rule 2290(b)(2).** Proposed Rule 2290(b)(2) would generally require any member firm issuing a fairness opinion have procedures that address the process by which a fairness opinion is approved by a firm, including the process to determine whether the valuation analyses used in the fairness opinion are appropriate. SIA supports this provision of the Proposal.

**Proposed Rule 2290(b)(3).** Proposed Rule 2290(b)(3) would generally require any member firm issuing a fairness opinion have procedures that address the process by which a fairness opinion is approved by a firm, including the process to evaluate whether the amount and nature of the compensation from the transaction underlying the fairness opinion benefiting any individual officers, directors or employees relative to the benefits to shareholders of the company, is a factor in reaching a fairness determination.

SIA generally believes that the amount and nature of compensation payable to officers, directors and employees relative to that payable to public shareholders is almost never a factor in the financial analysis underlying a fairness opinion. Consequently, SIA believes that requiring member firms have a process that would require them to evaluate whether those relative benefits are a factor in reaching a fairness determination does not make sense in terms of how member firms arrive at fairness determinations, nor does it provide meaningful guidance as to what procedures would be required under this provision of the Proposal.

Of the many professional advisors and other parties who are involved in the M&A process, SIA believes that member firms are not best situated to evaluate the amount and nature

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<sup>9</sup> Some member firms have separate M&A groups with senior leadership and management roles, while these consulting functions occur on a more informal basis at other firms.

of compensation that individual officers, directors or employees will receive from the underlying transaction relative to other parties, and SIA notes that not all member firms have the requisite knowledge or expertise to do so. SIA respectfully submits that any rule adopted by the Commission should not mandate procedures requiring financial advisors to evaluate compensation arrangements, or to compare the relative benefits to be received by one group of corporate constituents versus another. It would not ultimately enhance the M&A process to require member firms to second guess decisions and judgments previously made by companies' boards of directors, or to require member firms to take actions extending beyond their advisory role in M&A transactions.<sup>10</sup>

SIA is also concerned that a procedural regulation of this type would require member firms to take actions that extend beyond their advisory role in M&A transactions, resulting in significant delay and the imposition of significant additional expense in the negotiation of mergers and acquisitions and other transactions. Boards of directors (or committees of the board) are already responsible for executive compensation decisions, including change of control payments,<sup>11</sup> and boards of directors already have the ability to confer with numerous consultants regarding executive compensation arrangements, in general, and with regard to the compensation arrangements in a potential change of control transaction, in particular. Notably, the Commission's recent proposed amendments to the tender offer best-price rule highlight the central role that compensation committees play in reviewing and approving employment compensation, severance and other employee benefit arrangements in acquisition transactions.

The Proposal states NASD's belief that this provision is driven by the goal of "ameliorating [the potential conflict between corporate insiders versus other shareholders] through procedures reasonably designed to consider whether in fact such conflict exists and to what extent it may bear on the determination that a transaction is fair," by requiring that member firms "consider the extent to which the differential in remuneration between management and other shareholders accruing from the deal proceeds, for which there was no prior contractual commitment, is a factor in determining the fairness of the transaction to shareholders." SIA believes that current Securities Act and Exchange Act rules already require extensive disclosure of the interests of specified executives and other persons in a proposed transaction.<sup>12</sup> To the extent it is perceived that executive compensation poses conflict issues for shareholders, SIA believes that other disclosure requirements, such as the Commission's recent proposed initiatives on executive compensation, are much better suited to addressing those concerns.

In light of the limited ability of the financial advisors to evaluate these arrangements and the fact that differential remuneration between different constituencies is

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<sup>10</sup> SIA is not aware of any judicial decision holding as a matter of state law that a fairness opinion must include this type of analysis, or holding that a board of directors could not properly rely on a fairness opinion that did not include this analysis.

<sup>11</sup> See Release Nos. 34-52968; IC-27193; File No. S7-11-05.

<sup>12</sup> For example, Schedule 14A, Item 5, and Form S-4, Item 18(a)(5)(i), each require disclosure of the interests of certain persons in matters to be acted upon, including "any substantial interest, direct or indirect, by security holdings or otherwise" of directors and executive officers.

simply not a factor considered by fairness opinion providers in the fairness analysis, SIA believes that it would be inappropriate to require member firms to adopt fairness opinion policies with regard to this type of analysis.

In response to the Commission's request for comment regarding whether member firms should disclose fairness opinion procedures in the fairness opinion or elsewhere, SIA does not believe such disclosure is warranted. In general, SIA believes that disclosure of these procedures elsewhere is unnecessary, and notes that NASD has many other effective rules requiring member firms to adopt and maintain policies and procedures without requiring public disclosure of those policies and procedures.<sup>13</sup> Indeed, given that member firms include all types of institutions, ranging from boutique firms to international investment banks, SIA believes that each member firm should have the ability to adopt and implement policies and procedures best suited for that member firm; public disclosure of these policies and procedures may detract from the ability of the member firms to adopt the most effective and efficient procedures, and could discourage firms from updating or revising these procedures as they would otherwise deem appropriate. Accordingly, SIA believes that public disclosure of internal fairness committee policies would not enhance the overall fairness opinion process and could instead harm that process.

## Conclusion

We thank the Commission for the opportunity to present our views. If you have any questions or would like to discuss these issues further, please contact the undersigned, Eileen Ryan, Vice President and Associate General Counsel of SIA, at 212-618-0508 or [eryan@sia.com](mailto:eryan@sia.com), or counsel to SIA's Fairness Opinions Task Force for this letter, David Schwartzbaum of Latham & Watkins LLP, at 212-906-1215 or [david.schwartzbaum@lw.com](mailto:david.schwartzbaum@lw.com).

Very truly yours,

*/s/John Faulkner*  
John Faulkner  
Chair, Capital Markets Committee

cc: The Hon. Christopher Cox, Chairman  
The Hon. Cynthia Glassman, Commissioner  
The Hon. Paul Atkins, Commissioner  
The Hon. Roel Campos, Commissioner  
The Hon. Annette Nazareth, Commissioner  
John W. White, Director, Division of Corporation Finance  
Robert Colby, Acting Director, Division of Market Regulation  
Gary L. Goldsholle, Vice President and Associate General Counsel, NASD

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<sup>13</sup> NASD Rules 3010-3013, for example, govern general supervisory obligations of member firms, but there is no requirement for member firms to publicly disclose their supervisory policies and procedures under those rules.

Joseph E. Price, Vice President Corporate Finance  
Eileen Ryan, Securities Industry Association  
David Schwartzbaum, Latham & Watkins LLP

Fairness Opinion Task Force:

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Bear, Stearns & Co. Inc.  
Canadian Imperial Bank of Commerce  
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