

# COMMITTEE OF CONCERNED SHAREHOLDERS

10732 Farragut Drive  
Culver City, CA 90230  
<http://www.ConcernedShareholders.com>  
[Information@ConcernedShareholders.com](mailto:Information@ConcernedShareholders.com)

June 11, 2009

VIA EMAIL: Rule-Comments@SEC.gov

Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

**Re: Facilitating Shareholder Nominations**  
**File No. S7-10-09**

Dear Ms. Murphy:

The Committee of Concerned Shareholders ("Committee") submits its comments on Facilitating Shareholder Nominations --- SR 07-10-09 ("Proposed Rule") as follows:

- I. Introduction
- II. Been There, Done That!
- III. Institutional Investors Do Not Need the Alleged Benefits of the Proposed Rule
  - A. Mutual Funds Won't Participate Due to Conflicts of Interest
  - B. Pension Funds Already Have the Ability to Engage In Proxy Contests
- IV. The Opposition Represents Entrenched Entitlement
- V. Proposed Rule – A Sham upon the Investing Public
  - A. Arbitrary Percentage Ownership and an Effective Alternative
  - B. Basic Inequity
  - C. Ineffective Short Slates of BOD Candidates
  - D. Issues Not Addressed
- VI. Petition for Rulemaking (SEC File No. 4-461)
- VII. Conclusion – A Political Kabuki Dance

## **I. Introduction**

In order for American capitalism to function properly, the Board of Directors ("BOD") of corporations with publicly traded securities must become more accountable to Shareholders, the true owners of corporate America. However, at best, the Proposed

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Rule is a misguided attempt to avoid the accountability and competence problems that faced Enron, Worldcom and others. At worst, it is a sham upon the investing public.

Public and investor confidence in supervision of corporate activities by BODs and government regulators is at an all time low. The Proposed Rule is supposed to restore accountability by assuring "equal access" to the corporate ballot, but only for a small number of Institutional Investors. The Proposed Rule promotes UNequal "equal access." The Proposed Rule should guarantee "equal access" to ALL Shareholders, so that they could become effective watchdogs of corporate America.

Very few Institutional Investors have engaged in a proxy contest, but it is incorrect to assume that current rules have prevented them from waging low cost/effective proxy contests. Institutional Investors would not avail themselves of any purported benefits of the Proposed Rule. Even if they were to do so, studies demonstrate that minority representation on a BOD, as prescribed by the Proposed Rule, is ineffective.

Other than the Committee, no group of Individual Shareholders has engaged in a proxy contest to save a company that was drifting toward bankruptcy due an incompetent Management and/or BOD. The Committee feels that public confidence in the securities markets would be restored only by empowering Individual Shareholders to protect their own financial interests --- by functioning as their own watchdogs and acting, when necessary, to seek accountability at the 9,000+ corporations that have publicly traded securities.

## **II. Been There, Done That!**

The Committee, formerly known as the Committee of Concerned Luby's Shareholders, consisting of shareholders of Luby's, Inc. ("Luby's") who met on a Yahoo! Finance Message Board in 2000, is the first grass-roots shareholder group to conduct a formal proxy fight. Luby's, headquartered in San Antonio, Texas, was then a near 230-unit cafeteria chain with annual sales of approximately \$500 million. Its shares are listed for trading on the New York Stock Exchange.

The Committee's Director-nominees received 24% of the votes cast. Two (2) of the Shareholder Proposals that it supported, *i.e.*, removal of all anti-takeover defenses, annual election of all Directors, received approximately 60% of the votes cast. Luby's acceded to the Committee's demand that any board member be allowed to place an item on a board meeting agenda. Previously, only the Chairman or CEO could set agenda items.

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The Committee's out-of-pocket expenses were less than \$15,000. (A member of the Committee, with a legal and computer background, provided services without charge.) The Committee was able to solicit approximately 80% of the potential votes. Luby's expended more than \$250,000 of corporate assets to oppose the Committee's efforts.

Some have said that the Committee's efforts with Luby's caused the departure of its former Chief Executive Officer and President, the nomination of a Director-candidate with hands-on restaurant experience, the entry of a restaurant experienced white-knight/investor and the relinquishment of position by the former Chairman of the Board.

The Committee's proxy contest efforts revealed substantial difficulties that Individual Shareholders face in an attempt to hold Directors accountable. Further, it showed that the extent of Shareholder dissatisfaction might not be proportional to the size of stock holdings of Director-candidate nominators. In our proxy contest at Luby's, even though our Director-candidate nominators held about 1/4% of the outstanding stock (more than that owned by the incumbent Directors), our candidates garnered 24% of the votes cast.

On August 2, 2002, the Committee and James McRitchie, Editor of CorpGov.net, filed Petition for Rulemaking (SEC File No. 4-461)("Petition") with the Securities and Exchange Commission ("SEC"). The Petition seeks, in substance, to eliminate SEC Rule 14a-8(i)(8), which forbids the use of Shareholder Proposals to elect Directors. Hundreds of investors have formally registered their comments with the SEC in support of the Petition. They express the view that it is time that true proxy access for nomination of Director-candidates comes to the corporate ballot.

On March 10, 2004, the Committee was a panelist at the Security Holder Director Nominations Roundtable, sponsored by the SEC, in Washington, D.C.

### **III. Institutional Investors Do Not Need the Alleged Benefits Of The Proposed Rule**

The Proposed Rule, with its Director-nominator percentage ownership requirement, is available only to Institutional Investors. Mutual Funds are so severely conflicted that they will not avail themselves of the alleged benefits of the Proposed Rule. Pension Funds have had and have the ability to seek BOD and Management accountability through inexpensive proxy contests, but, if the past is prologue, do not have the will to exercise their power.

**A. Mutual Funds Won't Participate Due to Conflicts of Interest**

Mutual Funds will not actively participate in proxy contests even if the Proposed Rule is enacted. It would be detrimental to their financial interests vis-à-vis the financial interests of their public investors.

On December 12, 2002, John J. Sweeny, President of the American Federation of Labor and Congress of Industrial Organizations (the "AFL-CIO"), stated:

[A]nother conflict of interest in our financial markets—the conflict that encourages mutual fund companies to use our money to be ‘yes-men’ for corporate management in proxy votes. Using our money, mutual funds have bought up more than one-fifth of U.S. corporate stocks. Their sheer size makes mutual funds one of the most powerful forces in deciding who sits on corporate boards.... [W]e suspect that mutual funds vote with management at the expense of our jobs and savings to win profitable deals on retirement accounts and selling other services. ... Take Fidelity Investments, for example, the world's largest mutual fund company and one of the most influential investors in the global capital markets. Fidelity earned \$2 million in 401(k) management fees in 1999 from Tyco. ... [W]ill Fidelity or any other mutual fund company, ever vote against management and risk a contract worth millions?

In the 2003 AFL-CIO Proxy Voting Guidelines, Mr. Sweeney further stated, "[C]onflicted mutual fund companies use their tremendous proxy voting power as rubberstamps for corporate management rather than to promote their investors' best interests."

With current Mutual Fund proxy voting disclosures in place, Mutual Funds may be embarrassed into voting for dissident Director-candidates. However, it is highly unlikely that Mutual Funds would nominate a Director-candidate and, thus, jeopardize their actual or potential incomes.

**B. The Pension Funds Already Have the Ability to Engage In Proxy Contests**

Pension Funds vaguely allege that they need "equal access" to the corporate ballot in order to seek BOD and Management accountability. Few question the allegation. The truth is that Pension Funds have not needed and do not need the alleged benefits of the

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Proposed Rule to engage in low cost proxy contests. Further, they have presented no evidence that they will employ any new rule or the extent of any intended employment.

Some Pension Funds claim that an "equal access" rule would alleviate the high costs of running an effective proxy contest. That is false. Corporate ownership is concentrated with Institutional Investors. Usually, the votes of less than 30 Institutional Investors with the largest stock holdings in a particular corporation would be sufficient to elect Director-candidates. By filing a bare-bones proxy statement with the SEC and securing the votes of, at most, 30 Shareholders does not present a large financial burden. The Committee, inexperienced, but determined, did that, and much more, with an out-of-pocket expenditure of less than \$15,000.

Pension Funds have had the ability to seek BOD and Management accountability through the existing proxy process, but have not availed themselves of it. Even with enactment of the Proposed Rule, there is no assurance that they will proceed. Further, there are questions as to their resources to mount even a few such contests with respect to the 9,000+ corporations with publicly traded securities.

#### **IV. The Opposition Represents Entrenched Entitlement**

The Business Round Table and others (collectively "BRT") oppose "equal access" to the proxy statement. Their objections are based upon factually unsupportable and speculative forecasts of doom and gloom.

It took the sarcasm/wisdom of Molly Ivins to summarize the situation. "If you look around on almost any level, you'll notice that people who have special advantages almost always manage to convince themselves that they are entitled to those advantages. ... [P]eople will just get outraged if you try to correct even the most glaring inequities -- that sense of entitlement to special privilege is really tricky. Almost everyone who has previously enjoyed an advantage and is suddenly forced onto a level playing field will feel cheated, treated unfairly, singled out for undeserved punishment."

#### **V. Proposed Rule – A Sham upon the Investing Public**

##### **A. Arbitrary Percentage Ownership and an Effective Alternative**

The percentage ownership requirement is arbitrary. On the other hand, the Shareholder Proposal criteria (continuously owned at least \$2,000 of the corporation's stock for at least one year) have been tested for many years and proved to be effective.

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For the most part, it will be necessary for Pension Funds to form groups to meet the percentage nominator criteria. The Committee has had experience in forming and attempting to maintain an investor group for the purpose of nominating Director-candidates. We found that, even if such a group could be formed, it is very difficult to maintain when the targeted corporation causes desertions by partially satisfying the particular interest(s) of some members. We faced issues similar to the dissidents with Disney. "New York's state pension officials ... withheld support from Eisner.... This, week Democratic State Comptroller Alan Hevesi said he was no loner calling for Eisner's immediate ouster. ... [H]e was contacted by new Disney Chairman George J. Mitchell. The two had worked on a Northern Ireland peace initiative. Mitchell ... had persuaded Hevesi to alter course...." (LAT, 3/24/04, "Running Disney's Word Machine")

A relatively recent example involving ten (10) major pension funds demonstrates the difficulty of forming an investor group to attain a stock ownership threshold. They formed an investor group to sign a letter dealing with one policy issue, a much simpler task than forming a group to nominate Director-candidates.

A group of major pension funds Monday called on Unocal to reconsider its role ... in Myanmar... The group, led by New York State Comptroller Alan G. Hevesi and joined by California's treasurer and the state's two largest pension funds... In all, representatives from 10 investment funds owning more than 4.5 million Unocal shares, or 1.6% of the stock, signed the letter and requested a meeting on the matter.... The 10 funds include the California Public Employees' Retirement System and the California State Teachers' Retirement System. (5/20/03, Los Angeles Times, "Shareholders Press Unocal on Myanmar")

If a major investor group with ten (10) members, formed to pursue an issue that is much less complex than Director-candidate nominations, can, at best, muster 1.6% of the stock, it is unlikely that many investor groups could be formed with the percentage stock ownership to pursue the complex issue of Director-candidate nominations.

To enact rules with Director-nominating criteria that are unlikely to meet, except in extremely rare circumstances, would be a travesty on the investing public. On the other hand, our Petition recommends the same reasonable and well-tested nominator threshold criteria used for Shareholder Proposals. That threshold would allow Shareholders to have an active voice in nominating Directors at a large number of corporations. It would restore investor confidence because investors would know that they have the tools necessary to look after their own interests.

**B. Basic Inequity**

There is no suggestion that members of a corporation's Nominating Committee, also, need meet the percentage ownership criteria. Our studies have shown that members of Nominating Committees own (not counting recently granted unexecuted stock options) less than 2/100ths of 1% of the outstanding stock. Some members own no stock whatsoever. In our campaign with Luby's, our Director-candidates owned or controlled more stock than substantially all of the Directors.

Some might argue that the negligible stock ownership of members of the corporation's Nominating Committee should be excused, as each owes a "fiduciary duty" to the corporation and/or Shareholders that outsiders do not owe. However, members are NOT truly independent as they are beholden to their fellow Directors and/or the CEO for their positions and longevity and, thus, have a conflict of interest in the nominating process. Self-preservation will prevail. Nominating Committees will substantially always find potential Director-candidates that have been nominated by outsiders to be "unqualified" and/or will decline to "consider" them.

**C. Ineffective Short Slates of BOD Candidates**

Dissident Shareholders should be permitted to nominate more than a minority of the BOD. A relatively recent study has demonstrated that permitting the nomination of only a few truly independent Directors would be ineffective in causing real reform. If elected, their fellow board members will isolate those truly independent Directors.

"[T]he corporate director who asks management the tough questions often gets a cold shoulder from the 'in' crowd or shunned by the ruling clique. ... 'These processes are to some extent under the radar screen of institutional investors.' ... The research and resulting 65-page paper, 'Social Distancing as a Control Mechanism in the Corporate Elite' by Westphal and Poonam Khanna, confirms what critics have long argued -- country-club cronyism bogs down efforts to rein in CEO power and advance shareholder rights. ... [T]he corporate board rocker's views will not be solicited, his advice will be shunned, and his contact with fellow directors will wane. ... '[Y]ou should be relatively pessimistic about the chances for voluntary board reform, unless there is a significant turnover in board membership...' (Reuters, 8/3/03, "Reformist directors get the big chill, study finds")

The publicly reported experiences of Guy Adams, who unseated the Chairman of the Board of Directors of Lone Star Steakhouse & Saloon (STAR) in a bitterly fought proxy contest, vividly demonstrate the impracticality of one dissent serving on a BOD. "Teams often work better when they have at least some conflict, particularly if there is

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more than one dissenter, says Michael Useem, a professor at the University of Pennsylvania's Wharton School. 'A single devil's advocate or whistleblower faces a really uphill struggle,' he says. 'But if you have one ally, that is enormously strengthening.'" (WSJ, 9/29/04, "Some Ideas Are So Bad That Only Team Efforts Can Account for Them")

"After two years of debate about independent directors and auditing standards, the Disney takeover drama reminds us that the best guarantee of good 'corporate governance' is an open market for corporate control." (WSJ, 2/17/04, Editorial: "Of Mouse and Management") Opponents to change might argue that "equal access" to the Company ballot "might be abused by dissidents to mount a no-premium corporate takeover disguised as a boardroom coup." (Staff Report to Trustees of CalPERS.) One should not assume that Shareholders have little or no intelligence. The Director-candidates can set forth their respective positions and the Shareholders can vote. If the "dissidents" prevail, it would be because Shareholders, casting at least 50% of the votes, desired that result. "Though never popular with the Business Roundtable, the takeover threat was a remarkably effective way of enforcing corporate accountability in the 1980s." (WSJ, 6/19/03, Editorial: "A Welcome Brawl")

#### **D. Issues Not Addressed**

The Proposed Rule does not deal with Management's unlimited use of corporate funds for advertising and other potential costs. It does not deal with reimbursement of costs should a dissident nominee be elected. It does not deal with reasonable and easily enforceable access to the email and other lists of Shareholders maintained by the Management and/or its agents.

#### **VI. Petition for Rulemaking (SEC File No. 4-461)**

A background paper, prepared by the Council of Institutional Investors, stated that the Petition for Rulemaking (SEC File No. 4-461), filed on August 1, 2002 with the SEC by the Committee and James McRitchie, Editor of CorpGov.Net, has "re-energized" the "debate over shareholder access to management proxy cards to nominate directors and raise other issues."

The Petition seeks "equal access" to the corporate ballot for ALL Shareholders by using the Shareholder Proposal procedure. The SEC has received hundreds of positive comments from investors and posted them on its website.



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The BRT fears that, without a percentage stock ownership threshold, Director-candidates would storm the corporate gates. There is an excellent solution to cure that concern. It is similar to the concept of selecting a "lead plaintiff" in a class action lawsuit --- "lead nominator." With a "lead nominator" provision, there is absolutely no need for a percentage stock ownership threshold. The "lead nominator" solution would allow Individual Shareholders to act as watchdogs of their investments at 9,000+ corporations that have publicly traded securities. Institutional Investors do not have the interest, desire and/or resources to seek Director accountability on such a scale.

Further, it is human nature that Individual Shareholders will not field Director-candidates because they enjoy engaging in what generally evolves into a bitter proxy fight. However, Individual Shareholders should have an effective means to attempt to secure BOD and Management accountability if the need arises.

## **VII. Conclusion – A Political Kabuki Dance**

The Proposed Rule, allegedly intended to promote BOD and Management accountability, would limit "equal access" to the corporate ballot to only Institutional Shareholders. There are 9,000+ corporations with publicly traded securities where the legitimate corporate governance needs of all investors should be protected. Institutional Investors, alone, will not have the interest or the resources to nominate Director-candidates at many of those corporations. Director accountability should be promoted at more than a few corporations. Individual Shareholders should be able to act as their own watchdogs in protecting their investments.

The SEC, Institutional Investors and the BRT are engaged in a political kabuki dance to the detriment of the investing public. An ineffective proxy access reform rule will probably be implemented. The SEC and Institutional Investors will probably claim "victory" on the part of Shareholders. The BRT will publicly moan and groan and, privately, claim "victory" for the proponents of business as usual. The media will inform the investing public that it has been handed a great "victory." However, BODs will remain just as unaccountable to Individual Shareholders as before the strange dance began.

Failing to provide Individual Shareholders with an effective means to hold BODs accountable will assure that the children of Enron, Worldcom and others will eventually take their places in the hall of sham. The choice is clear: true corporate democracy or continued paternalism by the corporate aristocracy.

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It would be my pleasure to discuss the foregoing issues with the SEC and/or its Staff.

Very truly yours,

Les Greenberg, Chairman

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