PITTSBURGH POST-GAZETTE

Heard Off the Street: SEC dabbles in democracy with changes in elections of directors

Monday, October 13, 2003

By Len Boselovic, Post-Gazette Staff Writer

Simultaneous with the democratic spectacle of California voters ensconcing Herr Gropenfuhrer in the governor's mansion, the Securities and Exchange Commission is proceeding with the liberalization of rules for electing boards of directors -- the corporate elite who govern publicly held companies.

Depending on which end of the spectrum of opinion on this issue you consult, the SEC is either inviting the corporate version of the French Revolution or minimally advancing the cause of corporate democracy.

"The proposals present the possibility of special interest groups hijacking the director election process," warns Pfizer Chairman Henry A. McKinnell.

McKinnell is keenly aware of the power of special interest groups. He co-chairs one called the Business Roundtable, whose constituency sits squarely in the bull's-eye of the regulatory initiative. McKinnell believes the SEC's proposals "may stifle business innovation, decrease productivity and stall economic growth."

Then there's Les Greenberg, the leader of the Committee of Concerned Shareholders, a group of shareholder activists that traces its roots to Yahoo! message boards.

"At best, the proposed 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," Greenberg says in a letter he's sending to the SEC.

Just what is the protector of public markets proposing that can elicit such disparate opinions?

The SEC wants to give shareholders more of an opportunity to nominate board candidates. In certain circumstances, companies would be required to place the name or names of shareholder-nominated candidates on the ballot sent to shareholders. Currently, the only names on the ballot are those of candidates nominated by the board, which prompts critics such as Greenberg to compare the process to elections in a communist country: everyone can vote, but there's only one candidate on the ballot.

While the SEC has not yet detailed the mechanics involved, putting shareholder nominees on the official ballot would be triggered by two events.

First, shareholders who have owned at least 1 percent of a company's stock for one year or more could sponsor a resolution seeking shareholder access to the ballot. If the proposal won a majority at a stockholder meeting, a shareholder-nominee would be placed on the ballot at the following annual meeting.

Alternately, if shareholders withheld at least 35 percent of their votes from company-sponsored nominees, a shareholder nominee could appear on the ballot the following year.

In either case, the number of shareholder-nominees placed on the ballot would depend on the size of the board. One nominee would appear if the board has eight or fewer members, two for boards with nine to 19 members and three for larger boards.

The California Public Employees Retirement System, the nation's largest public pension fund, welcomes the SEC's action as "a good first step." But CalPERS and other institutional investors have reservations about using "triggers" to grant what many perceive should be a shareholder right.

"We are concerned about triggering events," says Joe Keefe, senior strategic advisor on social policy for Calvert Group, a Baltimore mutual fund operator. He says shareholders "shouldn't have to prove ... that something went wrong in the past to have that access."

There are also concerns about the two years it would take to get an insurgent's name on the ballot.

"It's a significant impediment to a shareholder right," says Tim Smith, president of the Social Investment Forum, a coalition of investors who build their portfolios based on companies' policies on social and ethical issues.

Much of the interest in the proposal centers on who could be nominated. In order to prevent corporate raiders and the other ogres McKinnell envisions from using the process to hijack a company, the SEC will place limits on who could be nominated. Candidates would have to promise they don't intend to use the election as part of a takeover and that they will hold the stock for a certain length of time.

Greenberg has two beefs with the proposal: it doesn't address the rights of small shareholders and provides no additional rights to large investors. Not your run-of-the-mill Yahooligan (he's a semi-retired securities lawyer), Greenberg says institutional investors don't exert the full influence they already have. For example, mutual funds, which own about 20 percent of shares available to investors, don't want to take on companies for fear of losing such business as providing 401(k) plans.

"If they elected to become more aggressive, they could do it now without the rule," Greenberg says. "It should be for the benefit of individual shareholders. The others don't need this. We do."

The SEC is expected to detail the proposal in the Federal Register in the next few days and provide interested parties 60 days to comment before it takes final action. If the response is comparable to the SEC's previous solicitations of opinion on the issue, expect an outpouring of commentary.

Given the often cozy relations between boards and management and the well documented failure of some directors to protect shareholder interests, it's pretty clear the SEC wants to -- and must -- do something to strengthen the voting rights shareholders only theoretically possess when it comes to electing directors. The tough task it faces is how to give shareholders the access to the proxy they deserve in a forum more constructive than the Worldwide Wrestling Federation strain of democracy California voters appear to prefer.