

Governance & Proxy Review

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As We See It - Commentary from The Altman Group

Review of Letters Submitted to the SEC on “Proxy Access” (Dec. 19-Jan. 19 Comment Period)

Kenneth L. Altman, President

James F. Burke, Director, Special Research

Executive Summary

The Altman Group has just published a Research Note containing a detailed review of letters submitted during the reopened comment period for the SEC’s proposed rules on “Facilitating Shareholder Director Nomination.” The comment period on the proposed rule was reopened for 30 days (through January 19, 2010), during which the Commission received some 46 letters (as posted on the SEC’s web site). The largest number of letters came from pension funds (10 in all, from CalPERS to OPERS), professional associations, academics (from Harvard’s Lucian Bebchuk to Stanford’s Joseph A. Grundfest), and various other proxy and corporate governance experts. A large minority of the comments that were submitted focused on a broader range of issues than the specific topics raised by four studies cited in the SEC’s release. Among the responses that did address specific topics mentioned in the four reports, more comments were received on the subject of “private ordering” than on any other topic.

The most significant response to the SEC’s request came in the form of a new study from Prof. David F. Larcker (Stanford University, Rock Center on Corporate Governance), who submitted the results of an analysis examining general stock market reactions to “proxy access events” triggered by headlines regarding regulatory and legislative developments. What Larcker and his co-authors found was that “the evidence suggests shareholders react negatively to regulation of proxy access...the market perceives that shareholders of firms with many large blockholders are harmed by proxy access and is consistent with critics’ claims that large blockholders will use the privileges afforded them by proxy access regulation to manipulate the governance process to make themselves better off at the expense of other shareholders. Interestingly, the results also suggest that shareholders of firms with many small institutional

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January 25th, Goldman Caps U.K. Pay at £1 Million

Aaron Lucchetti and Sara Schaefer Muñoz discuss the investment bank’s imposition of a salary cap in the U.K.

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guardian.co.uk

January 24th, “You are Right to be Angry. The Banks Should Have to Pay for State Backing”

In a column this past Sunday, Paul Myners, the U.K. Financial Services Secretary, calls for an independent review into the British investment banking industry.

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January 23rd, Wall Street's Pay Shift Augurs Ill for Stockholders

Susanne Craig reports on what the shift from cash to stock, at the largest banks, means for shareholders.

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investors are harmed less, either because the market perceives proxy access as less likely to occur at such firms, or because smaller institutional investors are perceived as less likely to promote agendas that are deleterious to value.” (See <http://www.sec.gov/comments/s7-10-09/s71009-598.pdf>) Prof. Joseph A. Grundfest also brought to the attention of the Commission a second new study documenting negative reactions to the prospect of proxy access regulation: Ali C. Akyol, Wei Fen Lim and Patrick Verwijmeren, “Shareholders in the Boardroom: Wealth Effects of the SEC’s Rule to Facilitate Director Nominations,” Department of Finance, University of Melbourne, Dec. 14, 2009.

In our view, this latest group of letters to the SEC has, on balance, strengthened the case for a “private ordering” regime for proxy access. The Commission has been informed of new studies documenting negative reactions in equity markets to headlines signaling increased risk of regulation of proxy access. In addition, the only thing that has been conclusively demonstrated through all of the performance statistics submitted is a short-run “contest effect” driving up stock prices in the months preceding a vote that results in the creation of a hybrid board (IRRC/“The Effectiveness of Hybrid Boards”). That same IRRC study found companies underperforming over a 3-year period following the creation of a hybrid board – a result that is consistent with earlier comparable studies cited by opponents of the proposed rule. All told, it is still not clear why shareholder dissatisfaction with corporate directors, which is, as described by Dr. Elaine Buckberg and Prof. Jonathan Macey, an issue that is “rare” among thousands of public companies, requires such a sweeping, and problematic, “solution.” It will be up to the Commission to decide if the gains from a direct proxy access rule will outweigh all of the costs, including (among many) the burden the rule will create for hundreds of companies each year and the rule’s impact on the competitiveness of U.S. equity markets.

After reviewing all of the arguments made by advocates of PR14a-11, it is also apparent that some of their conclusions are based on flawed assumptions -- the most significant of which is that once the rules of the game are changed companies will keep playing by the old rules instead of adapting. If PR14a-11 is adopted, companies will, in our opinion, be more likely to adjust poison pill provisions, move to other jurisdictions, and pursue other options to marginalize the impact of PR14a-11.

Moreover, if PR14a-11 is adopted, the rule might ultimately prove to be a “high-water mark” for shareholder activism. Some of the most significant gains by activists over recent years, most notably the widespread adoption of a majority vote standard, have come as a result of cooperation and accommodation by corporate boards. The proposed rule will drive both companies and supporters of activist agendas into more confrontational postures, and marginalize opportunities

January 22nd, Barclays To Defer Bonuses

Patrick Jenkins, David Oakley and Tom Braithwaite report on the global bank’s effort to tamp down anger over executive compensation and bonuses.

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January 24th, Infineon Seeks to Quell Shareholder Fight

Daniel Schäfer and Richard Milne discuss the battle between Infineon’s investors and its Chairman-designate.

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for cooperation and consensus. In other words, the total “influence” of shareholders on boards may actually be reduced as a result of the sharp escalation in the number of confrontations that PR14a-11 will unleash.

Over recent years, the pendulum has certainly swung sharply in favor of shareholder activists and proxy advisory firms, but we wonder if the SEC’s rule-making with regard to proxy access might actually trigger a reversal of that trend. Many companies are already facing serious challenges in director elections this year as a result of Amended NYSE Rule 452, which will sharply reduce total votes in such elections by eliminating uninstructed voting by brokers of shares held in Street name. Now, if PR14a-11 is adopted without a “private ordering” provision, companies facing potential PR14a-11 contests will be literally driven into taking decisive counter-measures.

In the final analysis, one can’t help but get the sense that 2-3 years after a rule on direct proxy access is adopted the Commission could end up being compelled to revise the rule as a result of unintended and unexpected consequences.

[To see the full analysis, please follow this link.](#)



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