

Governance & Proxy Review

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Edited by Francis H. Byrd

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As We See It – Commentary from The Altman Group

Storm Clouds Gather Over Director Elections-- Buckle-Up! The Trip is Likely to Get Bumpy – Part II

Domenick de Robertis, Senior Managing Director, and Reid Pearson, Managing Director and Corporate Governance Practice Co-Leader

In last week's Commentary, we discussed the amendment to Rule 452 which will eliminate the broker voting on director elections. As promised, we are following up this week with some statistics we compiled from our research on the voting impact that the change will have, and some additional issues to consider.

Impact Projection Statistics

Based on an analysis of 32 companies we have completed to date since the rule change was formally adopted, we estimate the following averages:

FOR Companies mailing proxy material using the traditional full-set method will experience a drop of 20.6% of shares outstanding.

FOR Companies that adopt a full Notice & Access mailing approach will see their director vote drop by 25.9% of shares outstanding.

These averages were derived from a widely dispersed data set, as the companies we looked at had varying market capitalizations, stock prices and shareholder profiles (e.g. levels of institutional vs. retail ownership). So while the numbers are interesting to note, they cannot be generally applied to a particular company without looking at the specific criteria for each issuer.

We thought it would be helpful, therefore, to present a sample cross-section of various shareholder profiles split between institutional and retail ownership (the names have been changed to protect the innocent) that issuers could use as a closer match:

FOR Alpha Company: 81% institutionally owned (% of FOR votes lost)

- Traditional Mailing: 10.3% drop
- Notice and Access: 13.8% drop

Governance News & Views from across the spectrum

>> **Executive Compensation**

THE WALL STREET JOURNAL

September 21st, Firms Back Plan to Change Pay Policies

Deborah Solomon reports on an effort, sponsored by the Conference Board, CalSTRS, and a number of top U.S. corporations to get out ahead of government regulation on executive compensation.

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Lex: Finance & Governance, September 21st, Executive Pay

A discussion of executive compensation in Europe, the UK and the U.S.


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DealBook


September 18th, Fed Considers Sweeping Rules on Bank Pay

Edmund L. Andrews and Louise Story discuss sweeping changes proposed by the Federal Reserve and the Treasury to limit bank executive pay and incentives.


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 Bravo Company: 65% institutionally owned (% of FOR votes lost)

- Traditional Mailing: 20.1% drop
- Notice and Access: 24.9% drop

 Charlie Company: 41% institutionally owned (% of FOR votes lost)

- Traditional Mailing: 35.5% drop
- Notice and Access: 44.0% drop


 Delta Company: 28% institutionally owned (% of FOR votes lost)


- Traditional Mailing: 31.1% drop
- Notice and Access: 40.4% drop


Percentages are based on shares outstanding


Assessing the Risk


The loss of the broker vote will present each company with unique challenges. Here are some issues we believe that company management should consider:

 Management has an obligation to notify its board of the changes and the new voting risks now, so that the board's expectations can be set accordingly, and they can have time to consider all options rather than having to make tough decisions under the gun on the eve of a proxy mailing.

 What is the breakdown of a Company's shareholder base, and the balance of voting power among institutional holders, retail holders, and other voting constituencies? The results from the data above is clear, companies with higher retail shareholder ownership will be impacted with a greater drop in support votes due to the amended Rule 452, as opposed to companies having higher institutional ownership.

 Company officers need to assess the voting profiles of shareholders targeted in new stock issuances and investor relations. For example, we have spoken to companies who have recently been trying to attract retail holders, who tend to be very loyal and stable. Significant alterations to the shareholder makeup may be beneficial in many aspects, but issuers now need to account for the risk of diminished vote returns from a more retail-dominated shareholder base.

 Are there any individual nominees or entire key committees at risk of receiving withhold/against votes due to corporate governance or compensation-related issues that violate the policies of the largest institutional holders or proxy advisory firms? Some of these problems result from a checklist approach that these firms use and consistently follow, but which, if spotted in time, can potentially be rectified.

 How influential will the recommendations of the proxy advisory firms be on the voting decisions of institutional investors? Companies should seriously

DealBook

September 18th, Blackstone Co-Founder Criticizes Bonus System

Cyrus Sanati speaks to Peter G. Peterson on executive compensation at U.S. financial firms.

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September 18th, Citigroup CEO Says \$100 Million Annual Pay Is Too Much

Dan Wilchins reports on comments by Citigroup CEO Vikram Pandit on executive pay and bonus compensation.

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September 18th, Bankers Face Sweeping Curbs on Pay

Damian Paletta and Jon Hilsenrath discuss a Federal Reserve Bank proposal to restrict risk and limit compensation.

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September 17th, EU Calls on G20 to Rule on Bankers' Bonuses

Tony Barber reports on a call by European Union leaders for binding rules and sanctions on bankers' pay.


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September 22nd, RBC Changes Traders' Pay Schemes

consider having an analysis prepared as to the level of influence each independent advisory firm has on the institutional investor base. It is likely that RiskMetrics Group (formerly ISS) will wield the most influence, possibly upon as much as 25% or more of the shares outstanding. Depending on who the largest holders are, however, Glass Lewis and PROXY Governance could also have a noteworthy impact.

 The decision as to whether to use Notice and Access for the proxy mailing should no longer be based on cost savings alone. As noted above, the percentage of votes lost due to the amended rule 452 is greater when a company uses Notice and Access than a traditional full-set mailing. There are alternate options for issuers to consider. A hybrid version of mailing instructions may be prepared by a solicitation advisor on mailing strategies to a select range of shareholders, for example:

- Holders of 1,000 shares & up – Traditional Mailing
- Holders of 999 shares & below – Notice & Access

Overall, companies will need to thoughtfully analyze the impact of this change well in advance of their 2010 annual meetings and have a plan in place to ensure a successful re-election process.

Bad news from our friends at PROXY Governance

Francis H. Byrd, Managing Director and Corporate Governance Practice Co-Leader

This past weekend, the proxy advisory firm PROXY Governance sent out a [news release](#) on an analysis they conducted on shareholder votes opposing director nominees in uncontested elections during the 2009 proxy season. The firm examined voting results for the first eight months of 2009 and found a sharp increase in the percentage of director nominees receiving a high level of opposition votes. They documented a year-over-year growth in opposition votes (“no” votes) against directors. This might be an expected development given the affect of the financial crisis on stock and company performance, except for the fact that the increase in opposition votes took place despite the fact that there were fewer organized vote “no” campaigns in 2009 than in either the 2007 or 2008 proxy seasons.

The good folks at PROXY Governance drew some conclusions from this data. Namely, activist institutional investors (public pension, union and CSR funds) were taking a harder, more detailed look at individual directors, and that many investors were voting against directors as a means to protest executive compensation practices. According to the analysis at least 60 percent of those directors suffering through withhold votes were members of their company’s compensation committee.

Tara Perkins discusses RBC’s decision to change trader pay.

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September 21st, Put the Ball Into ITV Shareholders’ Court

Neil Collins has commentary on Tony Ball and the board of ITV.

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September 21st, ITV On Brink Of Signing Former BSkyB Boss Tony Ball

Rupert Neate reports on the state of negotiations between Tony Ball and the board of ITV.

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September 18th, Half of Germany's Top Managers Given the Boot

Discusses a story on the difficulties facing German executives and directors of DAX traded companies.

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>>Proxy Contests/Battles for Control



September 22nd, Cadbury Tries To Force Kraft’s Hand

Jenny Wiggins in London and Julie MacIntosh in New York report on an effort by Cadbury to push Kraft on its takeover bid.

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PROXY Governance also stated that they expect a continued increase in opposition to directors as a result of the existing and proposed regulatory changes from the SEC to the proxy voting system for the 2010 proxy season – notably the elimination of the broker vote thru amendment of NYSE Rule 452. A more problematic point raised in the analysis was that a review of the PROXY Governance coverage universe showed 284 director nominees elected with less than 60 percent of the shares cast in support and 473 director nominees elected with less than 65 percent of the shares cast. PROXY Governance concludes that many of these directors would not have received a majority of the votes cast were it not for the broker discretionary vote.

One point of conjecture not discussed in their analysis is what the effect of all this will have on the majority vote movement. The companies who have adopted majority vote protocols have tended to be the larger Fortune 500 and S&P 500 corporations. Some of those companies may now have regrets. Yet the activist institutions are quite keen on seeing a wider adoption of majority vote, extending throughout Corporate America to small and mid-sized companies. A wider distribution of the PROXY Governance analysis may result in increased resistance to adoption of majority voting among the remaining large companies who have not adopted it, and a more fierce resistance among mid-size and smaller firms, especially those with a large percentage of retail owners for whom it would be much more problematic, as pointed out in the above commentary.

Ultimately, adoption of the majority vote standard may actually require federal legislation to become a system-wide reality. This means the PROXY Governance analysis is also bad news for the proponents of the majority vote as well.



September 22nd, Cadbury Boss Sees 'Sense' In Kraft Deal

Amy Wilson discusses remarks by Cadbury's chief executive Todd Stitzer admitting there may be "some strategic sense" in a tie-up with Kraft.

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>>Investor Action



September 22nd, What the SEC Might Look Like If It Did Its Job

Susan Antilla has commentary on the role and power of the Securities and Exchange Commission.

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September 22nd, Sustainable Investment Seen Gaining Momentum

Natsuko Waki discusses the rise of sustainable investment funds.

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September 16th, Companies Urged to Court Long-term Investors

David Oakley discusses changes in asset allocation among European institutional investors and concerns from Eurozone companies.

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September 18th, Activists Use Tools of Capitalism to Fight Darfur Genocide

Henryk M. Broder reports on efforts by U.S. shareholders in Fidelity Investments to convince the fund to divest from Sudan.

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[>>The Boardroom](#)



September 23rd, The Demise of the-lawyers-did-it Defense

Senior Editor Roger Parloff discusses legal tactics in the BofA versus SEC versus Judge Rakoff battle.

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AGENDA

September 21st Directors Seek to Combat Misperception of Board Role

Josh Martin reports on director concern over investor and stakeholder misunderstanding regarding the role and duties of the board of directors.

(please note that a free trial is available by going to the subscription page)

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AGENDA

September 21st, Directors Identify What's Wrong With Governance, Get Support

Kristin Gribben discusses an analysis of Agenda magazine's survey of independent directors.

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September 21st, Excessive Executive Pay: What's the Solution?

Roger Thompson examines ideas from faculty members of the Harvard Business School on what ails U.S. corporate governance.

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THE WALL STREET JOURNAL

September 21st, Boards Face Expanded Responsibilities

Joann Lublin explores responsibilities for directors of banks and financial services firms under the proposed Federal Reserve review of compensation practices.

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September 21st, No. 2 Jobs Dwindle Amid Cost Cutting

Cari Tuna discusses a new trend in the elimination of the chief operating officer position and the implications for CEO succession planning.

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September 20th, Business Coalition Urges Pay Overhaul

Francesco Guerrera reports on efforts of a coalition of corporate leaders and institutional investors calling for Corporate America to self-regulate on executive compensation to preempt proposals from U.S. Congress.

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The New York Times

September 19th, Too Many 'No' Votes to Be Ignored

Gretchen Morgenson discusses a report from proxy advisory firm Proxy Governance.

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