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August 17, 2009

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F. Street. NE
Washington. DC 20549-1090
Via Email: rule-comments@sec.gov

Re: Facilitating Shareholder Director Nominations
Release Nos. 33-9046; 34-60089; IC-28765;
File No. S7-10-09

Dear Ms. Murphy:

I appreciate the opportunity to comment on the Securities and Exchange Commission's (the "Commission") proposed rules on shareholder director nominations described in Release Nos. 33-9046; 34-60089 and IC-28675 (collectively, the "Release").

3M Company ("3M") was incorporated in 1929 under the laws of the State of Delaware to continue operations begun in 1902. 3M is a $25 billion diversified technology company with a global presence in the following businesses: Industrial and Transportation; Health Care; Safety, Security and Protection Services; Consumer and Office; Display and Graphics; and Electro and Communications. With products ranging from well-known consumer products such as Scotch® magic tape and Post-it® notes to advanced high-capacity electrical transmission cables, 3M serves customers in more than 60 countries and employs 75,000 people worldwide. 3M has approximately 700 million shares outstanding with about 875,000 stockholders. 3M has been listed on the New York Stock Exchange since 1945 and has been part of the Dow Jones Industrial Index since 1976.

3M's Board of Directors has taken numerous actions (including those proposed by stockholders) to promote effective corporate governance and accountability to stockholders, including declassifying the board and electing all directors annually, amending our bylaws to provide for majority voting in uncontested director elections, stockholder approval of poison pills and the right of stockholders to call special meetings, and eliminating supermajority voting provisions in our governing documents. Nine of the ten members of 3M's Board are independent directors.

We have carefully reviewed the Release and strongly urge the Commission not to adopt proposed Rule 14a-11. We believe, for the reasons that follow, that an unproven and untested federal rule mandating proxy access for all public companies is unnecessary in light of widespread governance changes over the last several years and ill-advised given the numerous workability and other issues surrounding Rule 14a-11. Instead, we believe the Commission should focus its efforts on appropriate amendments to Rule 14a-8(i)(8) to allow proxy access stockholder proposals. This approach would allow stockholders to choose the proxy access system, if any, they determine is appropriate for their individual company.

I. **An unproven and untested federal rule mandating proxy access for <u>all</u> public companies is <u>unnecessary</u> in light of widespread governance changes over the last several years**. -- During the past six years, widespread governance changes have occurred to significantly improve the director nomination and election process, including the following:

a. The Commission approved listing standards in 2003 prescribing rules for director independence. These rules established standards for independence of directors and required the board to be comprised of a majority of independent directors and allowed only independent directors to serve on the audit, compensation and nominating and governance committees; required the board to disclose its determination regarding each member's independence; and required independent directors to select the board's nominees for director.

b. The Commission also approved rules in 2003 requiring a public company to disclose information about its policies and procedures for nominating directors, including whether the Nominating and Governance committee considers stockholder-recommended and the procedures for submitting such nominees.

c. The Commission adopted the e-proxy rules in 2007 that have significantly reduced the stockholders' cost to engage in proxy solicitation. New Section 113 of the Delaware General Corporation Law, effective August 1, 2009, permits stockholders to adopt bylaws that require the corporation to reimburse a stockholder's expenses incurred in soliciting proxies for the election of directors.

d. In 2008, the Delaware Supreme Court, in response to the Commission's request for guidance, confirmed that stockholders, as well as directors, have broad statutory power under state law to adopt bylaws that promote and define procedural rights for electing directors.

e. The Commission approved an amendment to New York Stock Exchange Rule 452 on July 1 of this year that prohibits brokers from voting in uncontested director elections without specific instructions from beneficial owners. This amendment increases the influence of stockholders who affirmatively vote their shares.

f. The Commission, on July 10 of this year, proposed new disclosures regarding the particular skills, attributes and qualifications that qualify a nominee to serve on the board.

g. New Section 112 of the Delaware General Corporation Law, effective August 1, 2009, explicitly permits stockholders or companies to adopt proxy access bylaws that outline the process to include stockholder nominees for director in the company's proxy statement. This amendment allows for flexibility and enables stockholders and the boards of directors of individual corporations to establish (or reject) a proxy access system that reflects investor preferences rather than a federally mandated rule that does not.

h. Many governance reforms occur through existing stockholder communication processes, including the stockholder proposal process. Notable examples of such reforms include the widespread elimination of classified boards, supermajority voting

requirements, and poison pills and the adoption of majority voting in uncontested director elections. Today, about 75% of the S&P 500 companies, including 3M, have adopted majority voting in uncontested director elections through constructive dialogue with stockholders -- not through regulatory mandates.

i. The voice of stockholders in director elections is further amplified by "Just Vote No" and "Withhold Vote" campaigns, used effectively by both small retail and large institutional investors, and by proxy advisory services with significant market share and influence recommending "Withhold" or "Against" votes against unresponsive directors.

These developments, which improve the director nomination and election process, and the continuing constructive dialogue with stockholders through a "private ordering" process are the most effective way for companies and their stockholders to devise proxy access solutions best suited for each individual company.

II. **An unproven and untested federal rule mandating proxy access for <u>all</u> public companies is <u>ill-advised</u> given the numerous workability and other issues surrounding Rule 14a-11.** The Release is terrible public policy because it risks imparing the continued functioning of effective boards while failing to improve the operation of deficient boards. The Release also fails to address the current realities of lock-step institutional voting. As a result, the Release will serve principally to permit groups with a narrow, specific focus to achieve board representation (with the attendant adverse consequences for the vast majority of stockholders described below), or to disrupt the company in the process of trying. Since we urge the Commission to abandon proposed Rule 14a-11, we will not comment on the many workability and other issues surrounding the proposed rule. Instead, we wish to point out some significant issues and unintended consequences with a federally mandated proxy access rule.

a. *Increased proxy contests*. A federally mandated proxy access right could have serious unintended consequences of increased, but unproductive proxy contests which are costly to companies and disruptive to boards and management – taking precious time and resources away from the critical role of management and oversight of strategy that helps ensure the creation of long-term stockholder value. A board of directors must be able to represent the long-term interests of a company and all of its stockholders. Annual proxy contests also pose threats of divided boards and narrow or single-interest directors. Some stockholders could misuse proxy contests to seek corporate action with a short-term focus not in the interest of a majority of stockholders.

b. *Conflicts of Interest*. Each director has a fiduciary duty to represent all stockholders. By way of contrast, stockholders do not have any fiduciary obligations to the company or other stockholders. Stockholders can be self-interested in ways that directors, bound by the duties of care and loyalty, cannot be. Some stockholders favor the return of gains to investors through dividends and stock repurchases while others favor stock price appreciation that results from the development of innovative new products through long-term R&D investments in the company. Other stockholders seek to achieve goals other than financial ones, such as sustainability of operations, supply chain codes of conduct and labor codes. Each such investor will pursue different ways to encourage a

company's board to meet its investment goals. Certain investors may seek to exploit proxy access to further their own financial, political or social agenda. In addition to the potential conflict of interest with a director's fiduciary duty, the election of stockholder nominees with narrow special interests could lead to divisive boards that have difficulty functioning as a team.

c. *Negative Impact on Board Dynamics*. The absence of a role for the board's nominating and governance committee presents significant concerns. The Proposed Rule 14a-11 increases the election of stockholder-sponsored directors who have not been endorsed by a Board's nominating committee. As noted by the New York Stock Exchange listing standards, "[a] nominating/corporate governance committee is central to the effective functioning of the board. New director and board committee nominations are among the board's most important functions. Placing this responsibility in the hands of an independent nominating/corporate governance committee can enhance the independence and quality of nominees." The question is whether the resulting Board functions more effectively than a Board whose members are all approved by the Board's nominating and governance committee. The potential for adversely impacting the Board is significant, and is not addressed by the Release.

Dean Sonnenfeld's seminal study of effective Board dynamics (Harvard Business Review, *What Makes Great Boards Great,* September 2002) correctly points out that:

> *What distinguishes exemplary boards is that they are robust, effective social systems. ... Team members develop mutual respect; because they respect one another, they develop trust; because they trust one another, they share difficult information; because they all have the same, reasonably complete information,* they can challenge one another's conclusions coherently; because a spirited give-*and-take becomes the norm, they learn to adjust their own interpretations in response to intelligent questions.*

In discharging its oversight and supervisory functions, the Board acts best when it uses its collective insight and experience to test, question, and challenge the plans of the CEO and senior management. It is important that Board dynamics promote a spirit of constructive challenge, which occurs when board members respect one another and are committed to working together. Introducing one or more directors who may lack the respect of other board members, or who consider themselves only accountable to the stockholder subgroup that nominated them, risks developing political factions within the board and disrupting the critically important goal of developing and sustaining effective board dynamics.

An effective board must also serve as a sounding board for and give trustworthy advice to the CEO. The position of CEO in a modern major publicly held American corporation is very demanding, and the dynamics of corporate management makes the CEO's position a lonely one. CEOs must have confidence in the wisdom of the board so that they can confide in and seek guidance from the group responsible for the direction of the business. Including a director not approved by other board members will risk

constricting communication between board and CEO that is critical to effective oversight and management.

No director selection mechanism can absolutely guarantee a thoughtful, responsible group of directors who feel empowered and obligated to perform the key Board tasks – asking hard questions of senior management, providing support where senior management is pursuing a correct but challenging or uncertain path, and advising the CEO on the myriad issues that must be resolved if the corporation is to prosper. The most effective selection process needs independent directors on the board's nominating and governance committee who take their selection responsibility seriously, approach the task of director nominations with the same sense of fiduciary duty they apply to other significant board decisions, and devote the time necessary to assure that the new director(s) meet the board's current needs and enhance the diverse qualities that a board collectively requires.

It is equally appropriate for the nominating and governance committee to consider nominees proposed by stockholders, as it is for the committee to consider nominees proposed by the independent directors, search firms or others. A rule that overrides the role of the independent nominating and governance committee in favor of proxy access for stockholder-nominated director candidates increases the chance for a dysfunctional board, and reduces the chance for a collegial board of thoughtful and challenging directors from whom the CEO seeks guidance.

d. *The Release impermissibly interferes with the Director Selection Process.* A basic tenet of Delaware corporate law is that the board of directors is ultimately responsible for managing the business and affairs of a corporation. Directors, as fiduciaries to the corporation and its stockholders, must diligently exercise their responsibilities as managers of the corporation, and must not delegate their responsibilities to stockholders. The process for selecting directors is one of the most important tasks a board performs. At 3M, the Nominating and Governance Committee and 3M's Board devote substantial efforts to ensure that the Board is comprised of individuals with distinguished records of leadership and success who will contribute substantially to Board operations.

The 3M Board's Governance Guidelines address this important responsibility as follows:

> *The Nominating and Governance Committee periodically reviews with the Board the appropriate skills and characteristics required of Board members given the current Board composition. It is the intent of the Board that the Board, itself, will be a high performance organization creating competitive advantage for the Company. To perform as such, the Board will be comprised of individuals who have distinguished records of leadership and success in their arena of activity and who will make substantial contributions to Board operations. The Board's assessment of Board candidates includes, but is not limited to, consideration of:*
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> *(i) Roles and contributions valuable to the business community,*

(ii) Personal qualities of leadership, character, judgment and whether the candidate possesses and maintains throughout service on the Board a reputation in the community at large of integrity, trust, respect, competence and adherence to the highest ethical standards,

(iii) Relevant knowledge and diversity of background and experience in such things as business, manufacturing, technology, finance and accounting, marketing, international business, government and the like; or

(iv) Whether the candidate is free of conflicts and has the time required for preparation, participation and attendance at all meetings.

A Director's qualifications in light of these criteria is considered at least each time the Director is re-nominated for Board membership.

The proposed Rule 14a-11 is inadvisable because it (i) impermissibly delegates the board's responsibilities for director selection to certain stockholders for stockholder-nominated candidates, (ii) excludes consideration of the board's membership criteria for such candidates, and (iii) completely removes the Nominating and Governance committee and the full board from the process of ensuring "the Board will be comprised of individuals who have distinguished records of leadership and success in their arena of activity and who will make substantial contributions to Board operations."

e. *Availability of Superb Director Candidates*. Also undesirable is the disincentive the Release creates for encouraging qualified director candidates to stand for election to corporate boards. Government policies ought to actively encourage eminently qualified candidates to serve on publicly held corporate boards. Instead, the Release is a disincentive for that service at a critical time in the nation's business history. There are already too few attractive candidates for board service. This is due not so much to a fear of serving in the current climate, but to the added time board duties now plainly require. The added demands of time and attention limit the number of boards on which qualified people may serve. The proposals are another disincentive because qualified candidates are unlikely to agree to be nominated if they will risk becoming subject to a proxy contest that focuses on them personally. Many attractive candidates already facing many complicated demands will not participate in a process burdened by a significant risk of a contested election. As a result, adopting the Release can be expected to deter the willingness of qualified directors to serve.

f. *Ineffectiveness of the Release*. Risks to the functioning of currently successful, responsible boards might be worthwhile if the Release clearly promised to enhance oversight and effectiveness of deficient boards. But it is hard to see how adding one or two stockholder-nominated directors is highly likely to make a positive material difference. Can the SEC identify the person who, if selected by stockholders to the Lehman Brothers board, would have altered the course of the risks undertaken and Lehman's ultimate bankruptcy? Without engaging in hindsight, does the Commission believe a single director who perceives ambiguous corporate risk-taking can persuade other directors to act on that perception?

On page 7 of the Release, the Commission states that it is revisiting proxy access "[i]n light of the current economic crisis" which "has led to concerns about the accountability and responsiveness of *some* (emphasis added) companies and boards of directors to the interests of shareholders." While the premise is raised, there is no further discussion as to whether a casual link actually exists or as to whether a prescriptive proxy access right would have prevented or mitigated the economic crisis. Even if one assumes the validity of the premise, it does not warrant requiring a uniform, inflexible approach at all public companies, regardless of their individual risk profile, responsiveness to stockholders, and governance practices.

Without a significant basis to conclude that the pending Release, had it been adopted several years ago, would have prevented the current financial crisis, the potential benefits of the Release as outlined by the Commission do not outweigh its clear risks and significant burdens and costs.

III. **Instead of a federal rule mandating proxy access for <u>all</u> public companies, we support appropriate amendments to Rule 14a-8(i)(8) to remove federal impediments to the rights of stockholders created under state law**.

a. We encourage the Commission to abandon proposed Rule 14a-11 and, instead, to amend Rule 14a-8(i)(8) by removing the director election exclusion and allow stockholders to propose proxy access bylaw amendments, consistent with state law. As previously discussed, the stockholder proposal process under Rule 14a-8 has proven effective in bringing about improvements in corporate governance, including majority voting in uncontested director elections and the elimination of certain takeover defenses. The flexibility of this approach enables stockholders and boards of directors of individual corporations to establish (or reject) a proxy access system that reflects investor preferences, which a federally mandated rule does not.

b. We also urge the Commission to revisit the current eligibility requirements to submit stockholder proposals under Rule 14a-8(b) (i.e., $2,000 in company stock held for one year) and establish higher thresholds for proxy access stockholder proposals. The ownership thresholds for proxy access proposals under Rule 14a-8 should be at least 1% of the company's outstanding voting stock that has been held for three years. This enhanced eligibility requirement would help ensure proxy access stockholder proponents have both a significant stake and a long-term interest in the company.

c. A proxy access bylaw, as permitted under Delaware law, could address a number of important issues that proposed Rule 14a-11 does not, including:

    i. Appropriate stock ownership thresholds and pre- and post-election holding periods to ensure that a nominating stockholder has both a significant stake and a long-term interest in the company. Significant long-term investors are more likely to have interests aligned with all stockholders and less likely to exploit proxy access bylaws to further their own financial, political or social agenda or for other short term benefits.

ii. Disclosure of uniform information about all nominees, including a nominating stockholder's total ownership position. As the Commission's recent action against Perry Corp. (*In the Matter of Perry Corp., Securities Exchange Act of 1934 Release 60351 (July 21, 2009)*) illustrates, stockholders can and do amass significant voting stakes in companies while simultaneously hedging the financial exposure from their ownership in order to influence specific stockholder votes. Nominating stockholders' hedged positions would be material information to other stockholders and should be disclosed so that stockholders can make informed decisions based on a clear understanding of the proponent's true interest in the company.

iii. Disclosure of relationships between the nominating stockholder and the nominee to ensure stockholders have information relevant to their voting decisions.

iv. Director eligibility standards applicable to all director nominees, such as retirement age, limits on the number of boards on which nominees serve, advance resignation requirements, and other legal restrictions on board membership.

v. The governance, insider trading and confidentiality policies applicable to all nominees.

vi. Procedures to withdraw and replace or disqualify a proxy access nominee and appropriate restrictions on resubmission of any proxy access nominee who fails to receive a specified percentage of votes cast.

IV. **The Commission Should Address Significant Problems with the Current System to Elect Directors Before Consideration of Proxy Access.** Currently, proxy advisory firms have too much control over the voting decisions of institutional stockholders. Theses firms remain largely unregulated, and the influence of these firms continues to grow.

Currently a large majority of stockholders are institutional investors that typically cast their stockholder ballots in lock-step with the recommendation of a tiny number of proxy advisory firms, such as Risk Metrics Group (RMG) (formerly known as Institutional Shareholder Services (ISS)). Approximately 55% of our top 50 institutional stockholders (representing about 50% of shares outstanding) follow RMG's proxy voting guidelines. Neither the investors nor RMG or other such entities have the staff or resources to evaluate board-nominated director candidates on their individual merits. Instead they rely on a handful of litmus tests reflecting the policy decisions of RMG that are divorced from any one company's particular circumstances.

Conferring such power on a small group of proxy advisory firms is unwarranted. An experience at 3M provides a case in point: Prior to the 2004 Annual Meeting of Stockholders, ISS informed the Company that they would recommend a "withhold vote" for that year's nominees, including the CEO. They did not base this recommendation on any problem they had with 3M's performance, the conduct of the CEO, or on the performance of the other nominees. Instead, they based this recommendation solely on their claim that, in

the words of their policy, "the board ignored a stockholder proposal [concerning poison pills] that was approved by a majority of the votes cast for two consecutive years." In fact, not only is the ISS claim untrue, but the ISS position was at odds with the staff of the SEC who explicitly concurred with our position. Here are the facts:

- In 2002 and again in 2003, a stockholder submitted similar proposals relating to rights plans, or "poison pills," notwithstanding the fact that 3M does not have and has never adopted a rights plan. The proposal submitted at the 2003 Annual Meeting of Stockholders requested that the Board of Directors "redeem any poison pill previously issued (if applicable) and not adopt or extend any poison pill unless such adoption or extension has been submitted to a shareholder vote."
- Following the majority vote on that proposal, 3M's Board of Directors adopted and reaffirmed the policy originally adopted in 2002 in a Board resolution. Under our policy, 3M will submit any poison pill to a stockholder vote unless the Board, exercising its fiduciary duties under Delaware law, determines that such a submission would not be in the interests of stockholders under the circumstances.
- 3M received an opinion from its Delaware counsel that this policy implemented the stockholder proposal to the furthest extent permitted under Delaware law.
- Based on our adoption of this policy, the SEC staff allowed 3M to exclude a similar proposal on poison pills from the 2004 proxy statement on the grounds that 3M had "substantially implemented" the stockholder proposal.

Beyond the fact that ISS was both mistaken and at odds with the SEC staff, their proposed remedy – to withhold authority from directors who had done an excellent job – made no sense in the context of our Company and our Board. Many of the top 30 institutional stockholders we contacted in 2002, 2003 and 2004 to discuss our position would not engage in any meaningful discussions, often citing adherence to ISS proxy voting guidelines that called for support of the stockholder proposals in 2002 and 2003 and for the withhold vote in 2004.

Given the tremendous influence that proxy advisory firms hold over director elections and the problems such as the one we encountered with their inaccurate analysis of our governance practices, the SEC should consider reforming this system (including reforms of the NOBO/OBO system and the issues of borrowed shares) before creating a mandated federal rule on proxy access that will serve only to increase the power and improper influence of proxy advisory firms over director elections.

V. **Conclusion**. For the reasons outlined above, we believe an unproven and untested federal rule mandating proxy access for all public companies is unnecessary given the widespread improvements in the director nomination and election process and ill-advised given the numerous problems with the proposed Rule 14a-11. Accordingly, we urge the Commission to abandon proposed Rule 14a-11. Instead, we support appropriate amendments to Rule 14a8-(i)(8) to remove the director election exclusion so as to allow stockholders to propose proxy access bylaw amendments consistent with state law. We also urge the Commission to revisit the current eligibility requirements to submit stockholder proposals under Rule 14a-

8(b) (i.e., $2,000 in company stock held for one year) and establish higher thresholds for proxy access stockholder proposals. The ownership thresholds for proxy access proposals under Rule 14a-8 should be at least 1% of the company's outstanding voting stock that has been held for three years to ensure proxy access stockholder proponents have both a significant stake and a long-term interest in the company.

We thank the Commission for the opportunity to contribute to the dialog on these important issues and hope our comments are helpful to your deliberations.

Sincerely,

Gregg M. Larson
Deputy General Counsel and Secretary

cc: Hon. Mary L. Schapiro, Chairman
Hon. Luis A. Aguilar, Commissioner
Hon. Kathleen L. Casey, Commissioner
Hon. Troy A. Paredes, Commissioner
Hon. Elisse B. Walter, Commissioner
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