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Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F St. NE
Washington DC 20549-1090

Re: Facilitating Shareholder Director Nominations
(File No. S7-10-09)

Dear Ms. Murphy:

On behalf of the corporate law blog, The Race to the Bottom, I write to support the proposal by the Securities and Exchange Commission to provide shareholders with access to the company's proxy statement. The necessary amendments to the proxy rules are long overdue.[1] There are any number of judgments imbedded in the rules that could be changed at the margins and, one suspects, with experience, will eventually be altered.[2] On the whole, however, the rule proposals are good ones and ought to be adopted.

I write to address one significant point. In opposing access, a number of commentators have contended that the Commission ought not to adopt the rule and instead rely on a system of private ordering. Under this view, bylaws would be left to the discretion of each company, thereby avoiding a one size fits all approach.[3] These commentators often point to the very recent enactment of Sections 112 and 113[4] of the Delaware Code which expressly authorize the adoption of bylaws that provide access and allow for the reimbursement of proxy fees. As the Delaware Bar Association explained:

- Thus, the substantive state law policy reflected in Sections 112 and 113 is to promote the flexibility to adopt electoral arrangements (including proxy access) best suited to the corporation as determined by its stockholders and directors. By setting forth a non-exclusive list of conditions that bylaws governing proxy access may contain, Section 112 clarifies the extent of stockholder choice in regard to proxy access, through their power (concurrent with that of the board of directors) to adopt bylaws governing the process by

[1] For a history of the Commission's efforts with respect to access, see J. Robert Brown, Jr., *The SEC, Corporate Governance, and Shareholder Access to the Board Room*, 2008 Utah 1339, *reprinted at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1095032

[2] The most problematic provisions are the 5% threshold for small companies and the first come first served system of nominations.

[3] Of course, proposed rule 14a-11 does not embrace a "one size fits all" approach, as the different ownership thresholds demonstrate.

[4] http://legis.delaware.gov/LIS/lis145.nsf/vwLegislation/HB+19/$file/legis.html?open

> which directors are elected. Thus, the new provisions recognize that stockholders (or directors) may determine that a proxy access system may indeed be beneficial, and expressly authorize them to adopt such a system; at the same time, the statute gives stockholders the flexibility to determine that, with respect to any particular corporation, such a system would not be beneficial, or that a reimbursement system might provide a better alternative.[5]

Those relying on the adoption of these provisions imply that the authority will in fact be used to grant shareholders access to the proxy statement.

The argument is misguided and almost certainly wrong. The evidence in fact suggests that in the absence of a federal requirement, companies will opt for a categorical rule denying access. They will do so either by not adopting access bylaws (and vigorously opposing shareholder proposals to institute access) or by adopting access bylaws with restrictions that largely render access meaningless.

First, the whole concept of private ordering in the corporate law environment is flawed. It presupposes that directors and shareholders will somehow negotiate and adopt the most efficient set of provisions. The theory does not coincide with the practice. Evidence suggests that management's control over the drafting process and its ability to rely on the corporate treasury eliminate any real prospect of private ordering. Instead, when matters are made discretionary, they result in a categorical rule that favors management. This has been the case with respect to waiver of liability provisions and likely to be the case with respect to access proposals.[6]

Second, the empirical evidence so far shows that boards have strenuously opposed any effort by shareholders to obtain access. Even before the adoption of Section 112, boards had the authority to adopt access bylaws.[7] In fact, they almost never did. In the new millennium, only three companies voluntarily put access bylaws in place.[8] Another three access bylaws were submitted to shareholders, with only one passing.[9] Management

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[5] Letter from the Delaware State Bar Association, July 24, 2009, http://www.sec.gov/comments/s7-10-09/s71009-65.pdf

[6] *See* Brown & Gopalan, Opting Only in: Contractarians, Waiver of Liability Provisions, and the Race to the Bottom, 42 Indiana L. Rev. (2009), *reprinted at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1087404

[7] Access bylaws were permitted before the adoption of Section 112. What was unclear was the extent of the restrictions that companies could impose. The adoption of Section 112 has clarified that almost all tenure and ownership restrictions are permitted.

[8] Comverse, Apria Healthcare, see http://www.theracetothebottom.org/shareholder-rights/shareholder-access-the-sec-and-corporate-governance-the-5-th-1.html, and Riskmetrics.

[9] The bylaw failed at Hewlett Packard and UnitedHealth. See http://www.theracetothebottom.org/shareholder-rights/shareholder-non-access-corporate-governance-and-the-sec-the--1.html At least two other companies provided access like rights as a result of litigation. *See* Lawsuits Expand Access, http://www.corpgov.net/news/archives2005/Jan-Feb.html

opposed the proposals in each instance.[10] Nothing in the current environment suggests that this opposition has abated to any significant degree.

The only real response has been to point to the adoption of majority vote provisions, implicitly suggesting that access bylaws will undergo similar level of acceptance. This is, however, an inapt comparison. For one thing, majority voting bylaws are not as common as proponents often make them out to be. While they have been broadly implemented among the largest companies, they are far less common among smaller public companies. According to Directorship, for example, around 75% of the companies in the Russell 3000 still use straight plurality voting.[11]

For another, the popularity of these bylaws is no doubt due in large part to the lack of any meaningful authority extended to shareholders.[12] The most common models of majority voting merely require that nominees not receiving a majority of votes submit a letter of resignation. Boards may reject the letter and, in fact, have done so on a number of occasions, effectively overturning the decision of shareholders.[13]

Even if a bylaw were to require resignation, with no residual discretion given to the board, shareholders still have no real authority. Any vacancy that results from the defeat of a director will be filled by the board. The board can, if it wants, fill the position with the very director who did not receive a majority of the votes cast.[14]

Because of this lack of real authority for shareholders, majority vote provisions have been labeled on this Blog as a "myth."[15] Other commentators have described them

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[10] In some cases, this entailed the distribution of follow up communications to shareholders highlighting the management's opposition to the proposals. *See* For UnitedHealth: http://www.sec.gov/Archives/edgar/data/731766/000119312507120727/ddefa14a.htm; For HP: http://www.sec.gov/Archives/edgar/data/47217/000110465907017087/a07-7438_1defa14a.htm

[11] A link to this data can be found in http://www.theracetothebottom.org/shareholder-rights/the-myth-of-majority-vote-provisions.html

[12] Many in fact are not bylaws at all but policies or guidelines. As such, they are subject to fewer regulatory requirements. *See* Item 5.02 of Form 8-K (requiring companies to disclose amendments to articles and bylaws), *reprinted at* http://www.sec.gov/about/forms/form8-k.pdf

[13] *See* Claudia H. Allen, Study of Majority Voting in Director Elections, http://www.ngelaw.com/files/upload/majoritystudy111207.pdf (noting that in 2007 only one director "received a majority against vote at a company with majority voting" and "the board declined to accept her resignation"). More recently, companies such as Axcelis Technology and Pulte Homes have seen boards reject resignation letters from directors who received less than a majority. *See* http://www.theracetothebottom.org/preemption-of-delaware-law/city-of-westland-v-axcelis-technologies-majority-voting-and-5.html; http://blog.riskmetrics.com/2009/06/labor_investors_protest_pultes.html. In the case of Axcelis Technology, shareholders seeking to learn more details about the reasons why the board declined to accept letters of resignation have invoked their inspection rights, something that has resulted in litigation in Delaware. See http://www.theracetothebottom.org/preemption-of-delaware-law/city-of-westland-v-axcelis-technologies-majority-voting-and-1.html

[14] *See* commentary to Section 10.22 of the Model Business Corporation Act ("In the exercise of its power under section 10.22(a)(2), a board can select as a director any qualified person, which could include a director who received more against than for votes."), http://www.abanet.org/buslaw/committees/CL270000pub/nosearch/mbca/amendments/200606104.pdf

[15] See http://www.theracetothebottom.org/shareholder-rights/the-myth-of-majority-vote-provisions.html

as "smoke and mirrors." William K. Sjostrom, Jr. & Young Sang Kim, *Majority Voting for the Election of Directors*, 40 Conn. L. Rev. 459, 487 (2007).

Access proposals, in contrast, are not illusory. They provide shareholders with meaningful and substantive rights. They allow shareholders to insert nominees in the company's proxy statement, increasing the likelihood that the candidates will be elected. Management has no discretion to ignore the results or otherwise fill the board position. Boards can, therefore, be expected to vigorously oppose these bylaws, as has been the case so far.

The anticipated level of opposition can be gleaned from the response to say-on-pay bylaws. The bylaws have received considerable support from shareholders (averaging over 40% of the vote in each of the last four years, according to data provided by Walden Asset Management). There were over 100 shareholder proposals calling for say on pay in 2009, an increase from 79 in 2008 and 51 in 2007. The popularity among owners, however, has not translated into widespread popularity among managers. Data from Walden Asset Management indicate that only 24 companies have actually implemented the proposals and provided shareholders with a say on pay.[16] Access bylaws will likely engender even greater opposition.

The failure of the Commission to adopt the access proposal will not result in a thousand flowers blooming and private ordering running rampant. It will result in a universal rule of denial, the same one that is currently in place. Nothing in the enactment of Sections 112 and 113 require boards to put in place access bylaws and the evidence to date suggests that they will not. The only way to ensure meaningful access to the proxy statement is to adopt a federal rule that institutes the requirement.

With regards.

Yours truly,

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[16] See http://www.theracetothebottom.org/shareholder-rights/the-inevitability-of-say-on-pay.html