THE BOARD INSTITUTE

4350 East Camelback Road, Phoenix, Arizona 85018 | 480-998-1081 | fax: 480-998-1082
www.theboardinstitute.com | The Board Book | Director Executive Search www.morgansamuels.com

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COMMENTS RELATIVE TO SEC Proposed Rule S7-10-09 Release No.33-9046
Facilitating Shareholder Director Nominations

By Susan F. Shultz, President
The Board Institute, Inc.
Board Practice Lead, Morgan Samuels
[redacted]

Now is the time to restore trust in the integrity of boards of directors–strategic independent boards that add real value to the corporations they serve and help avoid the fatal mistakes Boards of directors are the core of the free enterprise system. Rather than subvert them, we must improve them.

We hear about the failed, passive boards. The untold stories are the 1000s of companies, public and private, that have avoided crises; that have succeeded, because of the advice and counsel of diligent, strategic boards of directors.

The right board members with the right mix of background, expertise, experience and perspective are the fundamental prerequisite for a good board. Transparency and accountability can counter the cacophony of negativity.

Just as Congress represents our national interests, so boards of directors safeguard our investments – and thus our nation's financial health. Over half of America's adult population owns stock in a publicly traded company; Thousands of entrepreneurs are invested in private companies. Boards are critical success factors for all of these companies.

I emphatically oppose SEC Proposed Rule S7-10-09 *Release No.33-9046*
Facilitating Shareholder Director Nominations

If shareholders can bypass the Governance Committee's objective selection procedure, both the recruitment process and the operation of corporate boards of directors would be politicized. The effectiveness of boards of directors would be diluted and marginalized.

1. *The process of filling Board seats could be subject to campaigning, special interest pressures, sizable expenditures to lobby other shareholders, horse trading for seats, etc.*

Allegiances would typically be to narrow interests. Shareholders are often not representative of the broad interests of a company. They are not monolithic and frequently represent short term financial interests, special interests or narrow agendas and constituencies that may be in direct conflict with the long term interests of the corporation.

Allegiances may sharply diverge and discourage deliberative, thoughtful, and strategic corporate governance.

2. *Balanced, independent boards would be a rarity.*

a. The best process by which to recruit effective directors is independent and objective, managed by the board's Governance and Nominating Committee. The steps are ideally as follows:
    i. Clarify the future objectives, opportunities and challenges of the company.
    ii. List and prioritize key criteria going forward.
    iii. Matrix the existing board, highlighting existing attributes, backgrounds and expertise.
    iv. Create director profiles responsive to needed expertise, background and attributes that complement any existing board members and that can be most beneficial to the company.
    v. Proactively recruit candidates who best meet that profile.
    vi. Present a choice of potential directors to the board of directors.

b. Independence has too often been a technicality, conveniently concealing a web of interrelationships and interdependencies where the allegiance is to management and board colleagues, rather than the combined shareholder interests.

c. Directors nominated by shareholders typically have a financial orientation as opposed to business development, marketing, research and development, business innovation, etc.

d. Shareholders should be included in an objective, recruitment process. They could advise on director candidate criteria and receive director position profiles. Shareholders could then be solicited for candidates who fulfill the criteria outlined in the profiles. Candidates recommended by shareholders would be folded into the independent selection process.

3. *The proposal that an open board seat for which there are multiple shareholder nominees be awarded to the first nominee received would further dilute the promise of a well rounded board and should be eliminated.* The nominees should be evaluated by an objective standard, not by a race to the finish.

4. *The ability of shareholders to bypass a thoughtful process would encourage a professional director class – closing the door to diversity* in age, experience, gender, ethnicity, geography, functional expertise, vision.

Further, this would create a barrier to those who currently do not hold board seats and thus perpetuate the failed practice of recycled directors.

5. *This process could lead to conflict, disruptive board members, warring factions and stalemates, as narrowly focused, diverging interests compete for power.* Boards could readily become dysfunctional.

Board Make-Up

Directors should be recruited proactively, objectively and independently. This would go a long way to break the web of conflict, misplaced loyalties, interlocking directorships and passivity that prevails at so many boards today. The New York Stock Exchange requires companies to disclose the method of recruiting. Last year, 51% of companies disclosed the source of their new directors. As more companies reveal not only who, but also how directors are recruited, objectivity and thus independence will be the norm.

Too often recruitment has more to do with relationships or celebrity, rather than strategic value. Too often, recruitment starts with the person, not the need, and thus allegiances to shareholders are compromised from the outset.

When board development begins with director assessment and focuses on the future—a matrix of talent, attributes and objectives; when each director position is profiled to complement existing strengths and fill in weaknesses; when the board has a choice of excellent candidates, great boards are the result. When such a process is in place, it validates the board, ensures integrity and helps to avoid the fatal mistakes

Independence has too often been a technicality, conveniently concealing a web of interrelationships and interdependencies where the allegiance has been to management and board colleagues, rather than the shareholder.

We are attacking the system instead of abuse of the system.

Government should regulate, not operate.

We can't legislate morality. We can regulate abuse. We can require accountability and transparency.

Just as boards must focus on policy and oversight and not stray into operations, so must government. Removing corporate leadership, dictating pay terms, legislating the role of stakeholders, all cross the line into operations and undermine the role, the autonomy and the capacity of boards of directors.

We should focus on aligning incentives and appropriately measuring risk.

There is danger in reducing governance to a formula.

Process and compliance is overtaking the business of the business in the boardroom. Governance is about strategy and culture and oversight, areas that cannot be precisely prescribed according to a national formula.

We can and must regulate broadly and respond to the new global economic reality. We must uncover the inevitable abuses of the system and focus resources on prosecution of those abuses. We have tolerated, and, in some cases, fueled, systemic abuses and conflicts for too long.

Director Certification

Centralized certification mandates should not be implemented, because certification deters diversity, tends to block first time directors and breeds homogeneity. Today only 15% of public company directors are women and 3% are minorities. There is even less diversity at smaller and private companies. And, the trend is flat.

There is an increasingly demonstrable link between good boards and successful companies

As a rule, we find out governance counts when something really bad happens. **How do you know if you have a good board? You measure it**–independently, confidentially and professionally. Last year, 88% of boards conducted evaluations, and 79% of directors say an effective board evaluation is the most important technique for ensuring that directors continue to perform at peak levels.

If there is no assessment, no accountability, how can shareholders know the board is effectively representing them and doing its job? Objective evaluations allow the board members to be confident that they are effective and allow directors to focus on their higher purpose, which is enhancing the business of the business and avoiding the fatal mistakes.

Accountability will come through meaningful evaluation, transparency through clear communication and disclosure, and independence through awareness and more objective and proactive recruiting to strengthen boards of directors.

Constructive, independent boards are responsible for untold millions going to the bottom line. The value of a single idea, of enhanced strategies, of strategic succession planning, of risk avoidance, the value of one mistake prevented, is incalculable. These are the stories that rarely get told. Or measured.

High integrity, strategic, independent boards of directors are critical to the success of our free enterprise system and to restoring consumer confidence in that system. Good boards do mean good companies. I hope we can embrace and enhance this mainstay of our economy and defeat S7-10-09.

QUESTIONS:

- Who is deciding how government intervenes?
- Is there any body advising on corporate governance?
- How are directors representing the government identified and appointed?

Susan Shultz is President of The Board Institute, Inc. (TBI)–with a suite of independent, web based, accredited tools to enhance boards by helping directors evaluate, educate (accredited by RiskMetrics), and benchmark their boards and committees. She leads the board of director practice at Morgan Samuels/SSA Executive Search. She authored *The Board Book*, *Making Your Corporate Board a Strategic Force* in Your Company's Success (AMACOM), speaks at major governance forums internationally, and has been featured in the major business media. [redacted]