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January 19, 2010

Dear Sir/Madam:

Please accept this e-mail as a comment on File Number S7-10-09, "Facilitating Shareholder Director Nominations." I write specifically to respond to a few points made in the Business Roundtable's August 17, 2009 submission.

According to its cover letter, the Business Roundtable ("Roundtable") is an "association of chief executive officers of leading U.S. companies with more than $5 trillion in annual revenues and nearly 10 million employees."[1] As such, the Roundtable represents a group whose interests are necessarily adverse to shareholders' interests, and its comments should be read in that light.

CEOs' interests are adverse to shareholders' interests to the extent that any cash compensation would otherwise belong to shareholders. This situation is ameliorated somewhat in firms where the CEO owns a large percentage of the firm's stock, such as Berkshire Hathaway and Oracle. But most firms are not Berkshire Hathaway or Oracle. And in most American public firms, the CEO's cash compensation dwarfs any stock compensation, meaning that on the margin the CEO would do better trying to increase his cash compensation than trying to increase his company's stock price. In addition, most CEOs, including without question the CEOs on the Roundtable's letterhead, are personally immune from their respective firms' failure. If the CEOs' stock holdings in their own companies instantly became worthless, their cumulative pre-crash cash compensation virtually guarantees that they would remain among the wealthiest people in the world.

I do not mean to say that CEOs deliberately milk their firms at the expense of their shareholders (although a small few do). I merely point out that the disconnect between the CEO's and the shareholders' interests is a fact of life in any public firm; and that this disconnect has the potential for mischief in direct proportion to the CEO's personal wealth.

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[1] Letter from Alexander M. Cutler, Chairman and Chief Executive Officer of Eaton Corporation and Chair, Corporate Leadership Initiative, Business Roundtable, to Ms. Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission 1 (August 17, 2009) ("Letter").

Boards Work for Management

The remedy for this disconnect is supposed to be a vigilant board of directors, but boards are not up to the task. Why? "Boards are really working for management rather than shareholders. Until that changes, not much will get done," said Professor Espen Eckbo of the Tuck School of Business at Dartmouth College.[2]

What accounts for the phenomenon of boards working for shareholders de jure but for management de facto? The only possible explanation is that CEOs, rather than the shareholders, choose the board. The directors know who butters their bread. Independent nominating committees do not change this. The requirement for independence prevents CEOs from choosing subordinates who determine their pay, but it does not eliminate the informal network that serves as the pool for potential board talent. Members of that network who become directors usually have some relationship with the CEO or an existing director and are not likely to cross management. (Professor Eckbo's remarks were made in 2009, after the advent of independent nominating committees.) So the Roundtable's 154 page submission can be boiled down to "don't mess with my board."

The Roundtable's Evidence is Scanty

One might think that the Letter's focus on the *expense* of proxy contests would be supported with empirical examples.[3] But nowhere in the Roundtable's 114-page Detailed Comments is there any report of the actual costs to firms of proxy contests, despite the fact that the subject of expense is covered generally.[4] Instead of surveying its members on what a proxy fight *might* cost, the Roundtable could have asked its members who had experience with proxy fights what they actually *did* cost. Is its omission of relevant data because none of its members have ever had a proxy contest? Or is it because the Roundtable chose not to include data that would have shed light on its assertion? And one wonders whether such contests would truly be expensive, given that the Roundtable's consultants found that "many contests" have "low cost" for shareholder activists.[5] If they are low cost for activists, why wouldn't they be low cost for firms?

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[2] As quoted in Yahoo! Finance News, "Annual Meetings Turning Ugly, But Change Remains Elusive," at http://finance.yahoo.com/news/Annual-Meetings-Turning-Ugly-cnbc-5014909.html?.v=2?sec=topStories&pos=8&asset=&ccode=.

[3] See Letter, p. 3.

[4] Detailed Comments of Business Roundtable on the Proposed Election Contest Rules and the Proposed Amendment to the Shareholder Proposal Rules of the U.S. Securities and Exchange Commission ("Detailed Comments"). The subject of expense is addressed in pp. 107-11.

[5] Buckberg and Macey, Report on Effects of Proposed SEC Rule 14a-11 on Efficiency, Competitiveness and Capital Formation In Support of Comments by Business Roundtable 6 (August 17, 2009).

A recent example may provide insight. Tier Technologies, Inc. (NASDAQ: TIER) experienced a contested election[6] in which a shareholder nominated two directors, both of whom were elected over management's candidates.[7] The contest happened during the two quarters after the fiscal year ending on September 30, 2008. The 10-Q for the first quarter in which Tier incurred expenses relating to the contest does not mention proxies at all.[8] The 10-Q for the second quarter includes the following statement in MD&A: "Contributing to the net loss were (i) restructuring and severance payments as we continue to implement our strategic initiative to focus on EPS [Electronic Payment Systems] Operations and streamline our general and administrative expenses and (ii) an increase in legal fees associated with the filing of our proxy."[9] Tier's General and Administrative Expenses were $14.142 million in the two quarters during which the proxy fight occurred and $13.982 million in the comparable year-earlier period.[10] Even attributing all the increase in General and Administrative Expenses to the proxy contest, it cost Tier $160,000 ($14,142,000 - $13,982,000 = $160,000).

Another assertion without empirical support is the claim that "The Proposed Election Contest Rules Will Promote Short Termism."[11] The Roundtable lacks evidence to back up that assertion, and consequently switches to softer language, like "the Proposed Election Contest Rules *may* exacerbate short-termism," and "we are concerned that the threat of a director election contest *could* place unnecessary pressure on a company to improve short-term financial performance."[12] If the proposals *may* encourage short-termism, they also *may* not, or they *may* encourage long-term thinking. The latter is more probable: a minority shareholder whose position is large, and therefore illiquid, may view itself as a long-term shareholder by necessity and not by choice. That is precisely the kind of shareholder who will be likely to take advantage of the proposed rules by nominating directors who take a long-term view that will benefit the

[6] See, e.g., Schedule 14A, March 3, 2009 filed by Discovery Equity Partners, L.P. et al. with respect to Tier Technologies, Inc., attaching letter to shareholders soliciting votes for Discovery's nominees, Daniel Donoghue and Michael Murphy, available at http://www.sec.gov/Archives/edgar/data/1045150/000110465909013893/a09-6799_1dfan14a.htm.

[7] Tier Technologies, Inc. 8-K, March 19, 2009 (reporting election of Donoghue and Murphy), available at http://www.sec.gov/Archives/edgar/data/1045150/000104515009000027/form8k.htm.

[8] Tier Technologies, Inc. 10-Q, Feb. 9, 2009, available at http://www.sec.gov/Archives/edgar/data/1045150/000104515009000019/form10-q.htm.

[9] Tier Technologies, Inc. 10-Q, May 11, 2009, p. 25, available at http://www.sec.gov/Archives/edgar/data/1045150/000104515009000039/for10q.htm.

[10] Tier Technologies, Inc. 10-Q, May 11, 2009, p. 2.

[11] Detailed Comments, p. 14.

[12] Detailed Comments, p. 15 (emphasis added).

shareholder. Shareholders interested in the short term are more likely to "vote with their feet" by selling their shares, rather than to spend time and money to influence the behavior of a firm in which they expect to have no long term interest.

The Current Rules Are Not Sufficient

The Roundtable downplays the potential efficacy of the proposals by pointing out that shareholders already have various means of influencing corporate behavior.[13] But none of those mentioned by the Roundtable give shareholders what they need: a choice in the form of contested director elections. And while many firms have adopted laudable best practices such as the requirement of a majority vote for election,[14] others can and will stifle shareholder concerns at every step. We need to enact the proposals for the shareholders of the latter firms; just because most people are law-abiding doesn't mean we don't need laws.

The Roundtable says that shareholders' ability to wage a proxy contest is "sufficient."[15] Sufficient for what? Current rules may be sufficient to achieve a contested election for smaller firms like Tier Technologies, in which it is possible for an activist shareholder and others to acquire significant stakes.[16] The current rules are not sufficient for larger firms. An activist shareholder can't acquire enough shares to make a difference by voting for its own nominees (try buying 10% of GE). By contrast, a shareholder who can acquire 10% of a small firm only has to persuade 44% of the remaining 90% of shareholders (i.e., 40% overall) to get its nominee(s) elected. Furthermore, the dispersion of shares in large firms creates inertia that works to management's advantage. The 10% shareholder of a small firm not only needs to convince fewer *shares*, but also fewer share*holders*, than even a 10% shareholder of a large firm.

And who said elections were not supposed to be contentious and distracting?[17] All elections, including those for town councils and executives of non-profits, can be contentious and distracting. This was surely understood by the elected legislators who voted state corporation laws into being. They made director elections part of basic corporate law, so the

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[13] Detailed Comments, pp. 5 – 13.

[14] <u>See</u> Detailed Comments, pp. 5 – 6.

[15] Detailed Comments, p. 10.

[16] The 10-K filed before the proxy contest disclosed that the activist shareholder, Discovery Group, owned 9.9 % of Tier, and four other shareholders owned at least 8.9 % each. Tier Technologies, Inc. 10-K/A, Jan. 28, 2009, p. 30, available at http://www.sec.gov/Archives/edgar/data/1045150/000104515009000027/ form8k.htm. The same 10-K (p. 2) indicates that the pre-contest market value of Tier's non-affiliate held common stock (i.e., market capitalization) was $156,044,551 on March 31, 2008. According to Standard & Poor's, the smallest firm in the S&P 500 as of September 30, 2009 had a market cap of $81,000,000; the median market cap was $7.98 billion, roughly fifty times Tier's size. <u>See</u> http://www2.standardandpoors.com/spf/pdf/index/SP_500_Factsheet.pdf.

[17] <u>See</u> Letter, p. 3.

"distraction" of an election is built in to the form. The fact that we haven't had frequent contested director elections is not an advantage inherent in the modern corporation, but rather an artifact of CEOs' control over nominations.

Finally, the Roundtable congratulates its firm members by announcing that 100 % of its member companies who responded to a survey "considered" candidates for the board recommended by shareholders.[18] Of those "considered," how many were chosen by management to replace an incumbent director? 5 %? 1 %? 0 %? The Roundtable doesn't tell us.

The SEC should enact the proposed rules regarding shareholder director nominations as drafted and published for comment. Thank you for this opportunity to comment.

Sincerely,

/s/

David Romine

[18] Detailed Comments, p. 10 n.43.