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Gille Law
3443 St. Louis Avenue
Minneapolis, Minnesota 55416-4396
Telephone: 612-925-2650
Facsimile: 612-915-1451
e-mail: info@gillelaw.com
<http://www.gillelaw.com>

Lori-jean Gille, Esq.
e-mail: lgille@gillelaw.com

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Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549-0609

Re: Comments to Proposed Security Holder Director Nominations
Release Nos. 34-48626, IC-26206; File No. S7-19-03

Dear Mr. Katz:

I am submitting these comments on behalf of one of my firm's reporting company clients in response to the publication by the Securities and Exchange Commission (the "Commission"), in Commission Release Nos. 34-48626, IC-26206 (the "Proposing Release"), of the proposed rules regarding security holder nominations for the Board of Directors of publicly-held companies (the "Proposed Rules").

As a general matter, my client does not support finalizing or adopting the Proposed Rules. First, it is too soon: with the many changes to the Commission's rules and the self-regulatory organizations' rules in the past 18 months, there has been no opportunity to implement those rules and determine the impact of those changes on the functioning of the Board of Directors, public companies or the capital markets, as a whole. Second, my client does not see the need for this type of "access", nor as many commentators have already suggested, does it believe that the rule changes proposed in the Proposing Release will accomplish their stated purpose—to "improve disclosure to security holders to enhance their ability to participate meaningfully in the proxy process for the nomination and election of directors." Many commentators have already voiced these opinions very ably. Therefore, this letter will simply raise some of the questions and issues that *weren't raised* in the over 300 questions the Commission itself raised in the Proposing Release.

1. *Consequences of a Triggering Event*
 - (a) My client has staggered terms for its Board of Directors, with each director being elected for a three year period. If there are three Board

positions up for election and the company is subject to the Proposed Rules due to the occurrence of a triggering event, is the largest security holder entitled to nominate candidates for more than one opening in the year in question? Must a company with staggered or multi-year Board terms have a Board member elected under this rule on its Board for a full three year term, whereas a company with one year terms is only required to have the security holder nominated Board member for a one year term?

- (b) If a triggering event occurs in year one and the company is required to include security holder nominations in its proxy materials, must it also then include a security holder proposal to opt into the rules in year two? Or in year three?
- (c) If a security holder nominated director is elected to the Board in year one and does not leave the Board in year two, is the largest security holder still entitled to propose a new nominee, as the company will still be subject to the Proposed Rules?
- (d) If a security holder nominee is defeated in year one, must the company still include the security holder nominee slate in year two?

2. *Voting Percentages*

- (a) The Commission has proposed that all voting percentages utilized under the new rules be based on actual votes cast, not on the number of votes that *could* be cast based on outstanding shares. Doesn't this treat non-voting security holders' votes as "no" votes? (For example, if a broker decides not to vote certain shares on behalf of a beneficial owner in absence of a direction from such beneficial owner, those broker non-votes effectively become "no" votes)¹.

One commentator has referred to the "rational apathy" of the small security holder—or, in lay terms, that the small security holder does not expect to have a direct impact on the functioning of the company and according to the rational market theory, will sell his shares if he isn't happy. This is my client's view as well. The Proposing Release itself suggests that in over 2,227 director elections in the past two years only

¹ The impact of treating non-votes as "no" votes is significant. If a company has 10,000,000 shares outstanding and 6,000,000 are voted, 35% of the shares votes is equal to 2,100,000 shares. Yet, that is only 21% of the total shares outstanding, a far smaller percentage of allegedly unhappy or dissatisfied security holders. Even if one assumed that half of those security holders who didn't vote were dissatisfied, which seems like an unlikely conclusion in any case, the percentage of unhappy security holders is still far below 35%.

1.1% of all companies had greater than 35% votes withheld for a director. This further strengthens our opinion that the average security holder is not unhappy and may not be voting simply because he is satisfied with the candidates and simply has decided not to vote. Why should those non-votes be assumed to be "no" votes?

- (b) Furthermore, if a special interest group targets one director, resulting in 35% votes withheld, why should the Board and the company as a whole be penalized? First, we see nowhere in the rule a requirement that the security holder nominee run against that director. So both could be elected, and another candidate eliminated. Second, it is not unusual for a special interest group to target a director for reasons totally unrelated to a company's business, perhaps because the group disagrees with some other company that the director is affiliated with, or because the group disagrees with some social or environmental position that the director has taken a stance on. Even with no nexus to the company, the Proposed Rules, based on voting percentages alone, could potentially change the makeup of a functioning Board of Directors.

3. *Determination of "Largest" Security Holder/Required Filings/Notices*

- (a) How does a company decide which security holder should be allowed to nominate directors? The Commission itself asks whether there should be a cure period for failing to satisfy the Proposed Rules' requirements. If there are two competing security holders (or groups), how long must the company wait before deciding which security holder controls more shares? Can a security holder or group amend its filing to add more security holders to their group (and therefore add more shares) and effectively trump the other competing group? With respect to required filings with the Commission, how can the company be sure that it has identified the appropriate security holder and that there won't be a later entry into the "contest" of who controls more shares?
- (b) What if the company finds out that the security holder or security holder group has sold company stock, thereby reducing their holdings below the minimum percentage required to be an eligible security holder or group—and the company finds this out before the proxy material is mailed—must the company still include the nominees' names or the security holder proposal? What happens if the company finds this information out after the proxy materials have been mailed? Can the company withdraw the materials and distribute amended or supplemental materials? Can the company assess the costs of such actions back against the no longer qualifying security holder?

4. *Costs*

- (a) Why should all security holders, particularly those who have little or no likelihood of eligibility to participate in this exercise, subsidize large security holders? Larger security holders (and certainly those whose holdings are in the magnitude that are contemplated in the Proposing Release as having "standing") have historically had more access to management and the boards of directors of public and private companies simply by virtue of the size of their holdings. The Proposing Release not only gives the large security holder the potential of even more access, it does so at the direct expense of the company *and* at the expense of the small security holders, whose return will inevitably be diminished by the added expense of complying with the Proposed Rules.
- (b) Even if the Commission decides to permit the large security holder or the security holder group to include its nominees with the company's materials, is there really a rationale for not requiring them to bear the cost of such inclusion?

While, as stated earlier, my client is not in agreement with the fundamental premise of the Proposing Release nor in the rules as drafted, we believe that the magnitude of questions, both those asked in the Proposing Release and those being asked by the commenting public, suggests that any final rule must be preceded by further discussion and refinement. It certainly will not be in anyone's interest to have any final rule fail by virtue of its own unanswered questions and lack of foresight.

Sincerely yours,



Lori-jean Gille