

American Federation of Labor and Congress of Industrial Organizations



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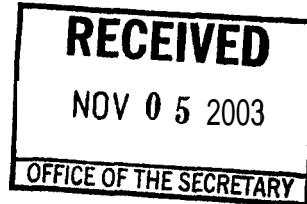
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November 4, 2003

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549



Re: Proposed Amendments to NASD Rules Regarding Board Independence and Independent Committees (Release No. 34-47516; File No. SR-NASD-2002-141)

Dear Mr. Katz,

On behalf of the American Federation of Labor and Congress of Industrial Organizations, I am writing to comment on the National Association of Securities Dealers' proposed rules regarding board independence and independent committees, currently awaiting approval from the Securities and Exchange Commission. In particular, I am concerned that NASD's proposed guidelines for key committees contain loopholes that allow directors to remain on those committees who do not meet the proposed standards of independence.

The AFL-CIO's recent efforts to promote nominating committee independence at the Cintas Corporation, a Nasdaq listed company, has demonstrated to us the practical implications of the proposed exemptions. Furthermore, media reports have suggested that the SEC has delayed approval because it seeks to harmonize the NASD and New York Stock Exchange guidelines.¹ If this is the case, I urge the SEC to persevere in its goal of uniform standards, and to uphold strict standards of director independence, such as those suggested by the Council of Institutional Investors.²

As has been widely reported in the press, both the NYSE and the NASD proposals require, in principle, that a listed company's compensation, nominations and audit committees be composed of independent directors. However, the NASD proposed rules permit exceptions to this rule that have largely escaped media notice. The NASD

¹ "SEC to Approve Governance Rules By NYSE , Nasdaq," Wall Street Journal, October 13, 2003.

² The CII definition of an independent director is available at http://www.cii.org/independent_director.asp.

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has proposed (i) that one affiliated outside director be allowed to serve on key committees for up to two years; and (ii) that an officer of the company may serve on a nominations committee if he or she owns or controls 20 percent or more of the company's common stock or voting power.³

Thus, under the proposed guidelines, non-employee directors may serve on key committees even if they have a material relationship with the company that could impair their independence. Under the proposed rules, the following people may serve on a key committee: a retired company executive; a major consultant, customer or supplier to the company; an officer or director of a non-profit organization that receives significant funding from the company; and the CEO of another company with an interlocking directorship with company executives.

The Sarbanes-Oxley Act specifies that audit committee members must be independent, but grants the SEC the authority to exempt "a particular relationship." If all the above relationships are exempt, this begs the question of why Congress decided to require an independent audit committee in the first place. The proposed guidelines do, at a minimum, bar executives from serving on their own compensation or audit committees. However, they allow executives who control 20 percent or more of a company to serve on the nominations committee, enabling them to handpick their own board.

It has been our experience that executives who are large shareholders already wield power disproportionate to their ownership stake, and thus should be held to a higher, not lower, standard. In fact, the NASD implicitly recognizes the potential for such self-serving behavior by barring large shareholders from serving on audit committees. We see no rationale for exempting the nominations committee from rules barring insiders other than the fact that some prominent companies listed on the Nasdaq exchange, which NASD oversees, currently have executives serving on their nominations committees, and that Nasdaq is in heated competition with NYSE to attract and retain listed companies.

At Cintas, for example, Chairman Richard Farmer served on the nominating committee that selected directors for election at the October 14, 2003 shareholder meeting. A salaried executive of the company, Richard Farmer is also the father of Cintas CEO Scott Farmer. According to Cintas, Richard Farmer's participation on the nominating committee was considered to be compatible with the proposed NASD standards by virtue of his share ownership. This committee was formed after the AFL-CIO filed a shareholder proposal to create a nominating committee comprised entirely of independent directors using the CII definition of director independence.

³ The exception generally allows "one director, who is not independent as defined in Rule 4200 and is not a current officer or employee or a Family Member of such person" to serve on key committees. Additional requirements apply to audit committee members, who may not own or control 20% or more of the company. Affiliated outsiders may even chair the compensation and nominations committees, though not the audit committee.

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The AFL-CIO and two independent proxy voting advisors, Institutional Shareholder Services and Glass Lewis & Co., urged shareholders to withhold support for Mr. Farmer because of his service on the nominating committee. Out of all the Cintas directors, Mr. Farmer received the fewest votes in favor of his re-election to the Board. A majority of outside shareholders not affiliated with management also voted in favor of the AFL-CIO's shareholder proposal. Responding to this shareholder concern, Cintas removed Mr. Farmer from the Board's nominating committee. We believe this experience shows that Nasdaq investors want truly independent nominating committees.

The AFL-CIO is the federation of America's labor unions, representing more than 66 national and international unions and their membership of more than 13 million working women and men. Union members participate in the capital markets as individual investors and through a variety of pension and benefit plans. Pension plans sponsored by unions affiliated with the AFL-CIO hold almost \$400 billion in assets, much of it in companies listed on Nasdaq.

Thank you for your consideration of this important issue. Please do not hesitate to contact William Patterson, the Director of the AFL-CIO Office of Investment at (202) 637-3900 if you have any questions.

Sincerely,



Richard L. Trumka