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SEC Strikes Down Proxy Access Proposals, Resolutions Addressing Emerging Issues

The SEC has granted a number of companies permission to omit from their proxy statements proxy access proposals as well as innovative proposals that shareowners submitted for the first time this proxy season. So far the commission has given companies the go-ahead to ditch resolutions dealing with the following issues:

- proxy access;
- conflicts of interest at credit ratings agencies;
- conflicts of interest within homebuilders that offer mortgages;
- conflicts of interest for directors who are employed by health care companies;
- banks' mortgage business risk; and
- succession planning for executives.

As it pledged at its November 28 open meeting, the commission has barred from 2008 proxy statements proposals that ask companies to place shareowner nominees to the board on management ballots. Binding proxy access proposals submitted by the American Federation of State, County and Municipal Employees to E*Trade Financial, JP Morgan Chase, and Bear Stearns, as well as a binding CalPERS' proposal submitted to Kellwood, will not appear on those companies' proxy statements thanks to the SEC's rulings on these no-action requests. AFSCME has indicated in the past that it will litigate on a company-by-company basis if necessary to see these proposals go to a shareowner vote.

The SEC also ruled out proposals submitted by the Laborers' International Union asking Moody's and McGraw Hill's boards and audit committees to adopt a policy to ensure that they do not employ any individual within one year of that individual being employed by a client, that they rotate the lead analyst for a client every five years and that their audit committees be responsible for managing potential conflicts of interest with clients. The union fund said such a policy could help eliminate the potential conflicts of interest that exist because the credit ratings agencies rate companies that pay for that service. This conflict became more apparent after the ratings agencies failed to issue warnings as the subprime mortgage sector was collapsing. The commission said the proposals related to

the company's ordinary business and therefore could be excluded under Rule 14a(8)i-7.

The subprime debacle also prompted LongView and the Amalgamated Bank Fund to submit proposals to KB Home, Lennar, M.D.C. Holdings, NVR, Pulte Homes, The Ryland Group and Toll Brothers asking that their boards establish "compliance committees" to be composed of independent directors who would conduct a review of the company's regulatory, litigation and compliance risks with respect to their mortgage lending operations and report to shareowners within six months of the 2008 annual meetings on the committee's findings and recommendations. The SEC has ruled that KB Home, The Ryland Group and Toll Brothers may omit the proposals from their proxy statements because they pertain to the companies' ordinary business.

To shed some light on the conflicts of interest that it believes exist at companies where board members have affiliations with the health industry, the AFL-CIO submitted proposals to nine companies asking their boards to adopt policies addressing these conflicts. The proposal specifies that the policy would cover any board members who are also directors, executive officers or former executive officers of a company or trade association for which health insurance or pharmaceuticals are their primary business. The policy would provide recusal from voting and chairing board committees when necessary.

In October, the AFL-CIO sent SEC Chairman Christopher Cox a report outlining the labor federation's concerns about what it views as widespread conflicts of interest by directors from the healthcare industry on the boards of the largest U.S. corporations. The report pointed out that these directors are responsible for decisions about the health care of the employees of the companies they oversee as directors, and these decisions could be influenced by their desire to see increased profits at the health care company that employs them.

The SEC said these AFL-CIO proposals could be omitted from the proxy statements at Electronic Data Systems, Exxon Mobil, Honeywell International, Target, The Williams Companies and Verizon Communications.

Concerned that homebuilders and banks are not providing shareowners with enough information to adequately monitor any risk associated with the companies' mortgage practices, the Laborers submitted proposals to six homebuilders asking their boards to prepare a detailed report within 90 days of their annual meetings evaluating their mortgage practices, including their company's potential losses or liabilities relating to its mortgage operations and/or those of any affiliates or subsidiaries. The SEC allowed Bank of America, Lehman Brothers Holdings, Bear Stearns and Washington Mutual to exclude the proposals because it said the resolutions pertained to the company's ordinary business. The SEC ruled that Beazer Homes USA must include the proposal in

its proxy statement, and Ryland Group agreed to adopt the proposal and begin issuing the requested reports.

Jennifer O'Dell, assistant director of the Laborers' office of corporate affairs, said she thought the SEC staff made the wrong decision in permitting these proposals to be omitted, and her fund plans to redraft and refile. "If there is a singular issue that has shareholders of residential homebuilders and financial services industries concerned, it is certainly the effect that the credit crisis has had on their ownership. We believe that this information MUST be given to shareholders so that we made adequately monitor risk," she said.

Another Laborers' proposal, this one addressing the more general issue of succession planning, also did not survive SEC scrutiny at Bank of America, Merrill Lynch, Toll Brothers and Verizon Communications. The proposal asked the board to amend the company's corporate governance guidelines to adopt and disclose a detailed succession planning policy that contained certain features.

Needless to say, the proponents who drafted and submitted these proposals are not pleased with the SEC's recent decisions. "Given the current uncertainties in the market and the economy, this is a time when shareholders are most in need of ways to talk to management and the board. It's disappointing to see the SEC slamming the door on that kind of dialogue," said attorney Con Hitchcock.