

ViewPoints

A Unique Moment in Time

Nine members of the Compensation Committee Leadership Network (CCLN) met on April 12 and 13, 2007, in Chicago to share their thoughts on the new disclosure rules from the Securities and Exchange Commission (SEC) now that the first batch of proxies has been filed. Members also discussed how to understand and work with shareholder activist and advocacy organizations and expressed their deep concerns about the growing pressure from proxy resolutions and legislation seeking to impose advisory votes on boards of directors, most notably in the form of “say-on-pay” proposals.¹

These discussions were informed and animated by two guests. The first guest, Mark Borges, formerly an attorney at the SEC and currently a leader in Mercer’s Washington Resource Group, publishes a widely read blog that offers detailed analyses of companies’ proxy reports. Mark co-led the members’ discussion on the 2006 proxy season. Our second guest, Christianna Wood, manages CalPERS’ \$120 billion equity portfolio and leads this influential organization’s shareholder advocacy activities, with a focus on corporate governance. Christy joined us for Thursday evening’s reception and led our dinner discussion.

The following members² participated in the meeting:

- Jerry D. Choate, Amgen
- A. Steven Crown, Hilton Hotels Corporation
- Thomas J. Donohue, Union Pacific Corporation
- Diane L. Doubleday, Mercer Human Resource Consulting
- Bonnie Hill, The Home Depot
- William A. Osborn, Caterpillar
- Stephen W. Sanger, Wells Fargo
- Samuel C. Scott, III, Motorola
- Jonathan P. Ward, Sara Lee Corporation

The following members took part in pre-meeting discussions but were not able to attend the meeting:

- J. Thomas Bouchard, Manpower
- John M. Cassaday, SYSCO Corporation
- Michael J. Critelli, Eaton Corporation
- John T. Dillon, DuPont
- Dina Dublon, Microsoft Corporation
- Robert J. Lawless, Constellation Energy Group
- Arthur C. Martinez, ABN AMRO and PepsiCo
- Victor A. Pelson, United Parcel Service of America
- Daniel H. Schulman, Symantec Corporation
- Hugh W. Sloan Jr., Manulife Financial

¹ Members of the Compensation Committee Leadership Network include the compensation committee chairs of some of the largest and most respected companies in North America. Collectively they represent more than 40 publicly traded companies, more than \$700 billion in annual revenues, and more than \$1 trillion in market capitalization.

² The compensation committee chairs are identified by their board membership.

Executive Summary

Compensation committees have become the targets of shareholder activists, legislators, and the SEC – everyone is eager to have their say. In the larger scheme, executive compensation practices have improved over the past five years as corporate governance has strengthened. Committees are working diligently and thoroughly, and in many cases, the entire board has become directly engaged.

Yet, CCLN members believe that much of the input they have been receiving recently neither improves corporate performance nor benefits shareholders.

CCLN members perceive few benefits from the SEC’s new, much-heralded executive compensation disclosure rules. Even SEC chairman Christopher Cox expressed disappointment at the length, complexity, and corresponding lack of clarity in the compensation discussion and analysis documents (CD&As). No particular shareholder segment (e.g., sophisticated investors, retail investors) seems to have benefited from the new rules. Although CCLN members agree that compensation committees have spent more time analyzing executive compensation plans as a result of the SEC’s disclosure rules, they assert that few significant “reforms” have taken root.

Members are skeptical of pension funds’ governance agendas and tactics. Broadly speaking, good governance correlates with good performance – and therein lies a fund manager’s rationale for being in the governance activist business. However, many activist pension fund managers seem to have a shareholder rights agenda only tangentially related to corporate performance objectives. These shareholders are using the “blunt” tool of proxy proposals and the threat of “withhold” votes to push for change in executive pay. For some shareholders the true agenda is shareholder access; for others, it seems to be more communication with directors. However, CCLN members believe they should communicate directly with shareholders only on an exceptional basis and at management’s specific request.

Overwhelmingly and passionately, CCLN members oppose shareholder advisory votes on matters that are within the purview of the board, such as executive compensation. At the very best, members see these measures as unhelpful, uninformed distractions. More fundamentally, they see them as a breach of the core principles of American corporate governance – a breach that will inevitably erode board effectiveness and corporate performance.

Few Benefits from the New SEC Disclosure Rules

Members acknowledge with some pride the progress they have made in evolving compensation plans over the past five years. But they give little credit to the SEC’s new disclosure rules, which they believe might be usefully modified.

I. Specific Innovations in Compensation Plans

One member echoed the group’s general feeling that this year’s changes to compensation plans or compensation philosophies are the result of an overall shift in the corporate governance landscape in America rather than the SEC’s 2006 disclosure requirements. *“In my opinion, [the SEC’s rules] have done nothing ... I think all of [the changes to compensation elements and pay packages are] just a result of improved governance from the last five or six years. I don’t think any of this has to do with the SEC.”* Members generally agreed that the SEC disclosure rules catalyzed few changes in the

compensation plans themselves. However, members did offer some examples of interesting, thoughtful innovations added to executive compensation plans in recent years.

Succession Planning

- *“I’m trying to force our compensation committee to spend a lot of time thinking about succession. The compensation committee has many responsibilities, other than just compensation. I want my folks to realize compensation committees are critical in cultivating talent.”*

CEO Evaluation

- *“During our CEO evaluation, we start with setting the priorities, and then the CEO is evaluated against those priorities by his senior staff. He then allows the senior VP of human resources to come into the compensation committee meeting and share the CEO and senior staff’s discussion with us through verbatim comments. [Members of the compensation committee] get a good understanding of how the team is working and how they view leadership.”*
- *“We’ve made some process changes, and one of those is the evaluation of the CEO by the full board.”*

II. Benefits of the SEC Disclosure Rules

Members do acknowledge that the SEC’s disclosure rules have yielded some positive results for compensation committees, particularly relating to board communication and preparation.

Increased Attention to Compensation Plans

- *“The preparation for the disclosure has brought a lot of benefits. We’re really looking at what we’re doing.”*
- *“We’ve spent a great deal of time trying to make [the proxy reports] readable and to get rid of all the redundancies.”*
- *“In all the boards I’m associated with, we found one compensation element that we’ve said needs to be gotten rid of. For the most part, though, those elements are on the margin.”*

Improved Communication between the Full Board, Management, and the Compensation Committee

- *“It used to be that the CEO and the comp committee were the only ones that knew what was going on.”*
- *“Now the entire board understands CEO compensation and understands [its] accountability and responsibility.”*
- *“Every independent director wants to understand the comp plan now. They’re all asking questions proactively.”*

III. Unintended Outcomes of the SEC Disclosure Rules

Chairman Christopher Cox recently cited a study that found that 40 U.S. corporations didn't write their 2006 proxies in "plain English."³ The media has also been highly critical of the "puzzling" level of complexity in the proxy disclosures. One *New York Times* article quoted Supreme Court justice Louis D. Brandeis in reference to this year's disclosures: "Sunlight is said to be the best of disinfectants. One problem with too much sunlight, however, can be the blinding glare."⁴ Although the SEC hoped these disclosures would be illuminating to investors, the proxies are cryptic and obscure. *"The general reaction is that the information being provided by companies is much too long and much too complicated."*

Members also feel frustrated. They feel that the SEC's disclosure rules are unnecessarily complex and require exhaustive detail. Moreover, companies are concerned that the SEC is requiring them to disclose specific performance target information that, if disclosed, could jeopardize companies' competitive advantage. CCLN members discussed the length of the proxies, the language in the proxies, disclosure of certain performance targets, and the distortions that result from the "eleventh-hour" rule (adopted in December 2006) as the most disturbing effects of the SEC's disclosure rules.

Length of the Proxies - The SEC has asked companies to provide extensive detail in the narrative discussion explaining their compensation plans. Mercer HR Consulting sampled 25 Fortune 500 companies and found the average length of disclosures to be 28.8 pages. The average length of CD&As was 6,141 words.⁵ Some companies are writing 20–30-page explanations of their compensation philosophies.

- *"There is too much detail, and the primary information [the SEC is looking for] is much harder to locate and analyze."*
- *"We put in [to the proxies] what has been asked for."*
- *"We're in the process of working out transparency disclosure. We're trying to address concerns about transparency. But [the SEC] should back off and allow us to get the communication right rather than asking us to build all aspects of this vehicle at the same time."*

Language in the Proxies - There are significantly greater liabilities associated with the proxy statement now than there were in past years.

- *"There are battles within companies these days; there are the 'plain English' people [who want to include simpler language in the proxies] and the 'legalese' lawyers [who are more concerned about ensuring companies are less at risk]."*
- *"Whatever information is provided [in the proxies] always ends up in the hands of lawyers, and that's where a lot of the problems arise."*

³ Chairman Cox made these remarks at a corporate governance conference at the University of Southern California's Marshall School of Business on March 23, 2007.

⁴ Eric Dash, "More Pieces. Still a Puzzle," *New York Times*, April 8, 2007, section 3, 1.

⁵ Mark A. Borges, *Proxy Season 2006 – The Initial Results* (New York: Mercer Human Resource Consulting, 2007), 4.

Performance Targets - One member observed, *“People will start getting smart that their performance metrics are competitive information and that they need to keep that proprietary. If you’re giving away those detailed performance metrics, you’re telling [your competitors] about your strategy.”* Although the SEC insists that it is not putting companies at risk by requiring the disclosure of specific performance targets, compensation committees disagree.

- *“If they push us, you’ll start to see a move towards very vanilla metrics like EPS or TSR. All Australian companies just publish TSR as their performance target to avoid criticism and competitive concerns.”*
- *“[Company name withheld] isn’t going to tell [Company name withheld] where they’re going. Competitive information can be revealed through those performance metrics.”*

The “Eleventh-Hour” Rule - On December 22, 2006, the SEC ruled with regard to SFAS 123 (R) that equity awards must be reported in terms of their annual compensation cost for the required year of disclosure rather than in terms of their full compensation cost. Essentially, the rule requires that awards made in 2006, as well as unvested portion of awards granted in prior years, be included in the summary compensation table.

- *“If we issued options in past years, but they were exercised this year, we have to report those numbers in this year’s proxies, so it looks like we’re rewarding them for this year’s performance, instead of a previous year. Any semblance of what we intended to pay and what shows up in those tables just doesn’t match up.”*
- *“[The eleventh-hour rule] doesn’t allow you to tell the whole story of what your results were for last year and how things turned out.”*

IV. Improvements to the SEC’s Rules

Revisions to the Eleventh-Hour Rule - Members offered a variety of possible improvements to the SEC’s disclosure requirements. Many members remarked that a change in the eleventh-hour rule will be necessary going forward.

- *“[The SEC should consider] making sure that what’s given in a year is explained in a year. That’s what makes the most sense.”*

Moving away from a Single Number - Members also expressed frustration with the SEC’s requirement that companies show executive compensation in a single number.

- *“You can’t get all comp down to one number.”*
- *“They should think about the difference between the accounting nature of this disclosure and the principles behind our plans.”*

A Principles-based Approach - A shift in the SEC’s philosophy, to a more principles-based approach, might improve the quality of disclosures.

- *“[The SEC] should reassess some of the long, voluminous tables that shouldn’t be in the proxy. Companies could just post those on the website.”*
- *“The SEC should also revisit change in control and termination disclosures and provide more guidance on the CD&As by giving people actual illustrations of what they’re looking for.”*

In this nascent stage of companies' attempting to meet new disclosure requirements, it is clear that the dialogue must continue. The process of identifying and perhaps revisiting the SEC's initial objectives while understanding companies' views of the rules' inherent limitations will require a willingness to compromise and a reexamination of tactics from both sides.

Skepticism Regarding Pension Funds' Governance Agendas and Tactics

Navigating the complex corporate governance landscape requires full comprehension of the nuances of different shareholder groups' agendas. CCLN members advise directors to first identify the authors behind shareholder proposals. Once directors have correctly identified the force behind a proposal, they should deconstruct the agenda behind it. In order to help directors understand how best to communicate with shareholder representatives, CCLN members offered some basic guidelines.

I. Forces Behind Shareholder Proposals

It is essential, as one member noted, *"to understand the secondary agendas. If you understand who's behind what project, you can better deal with the proposal."* Members identified a number of organizations and individuals who are behind such proposals, either as their authors or as public supporters of them.

1. Pension funds (e.g. CalPERS and CalSTRS, the AFL-CIO, AFSCME, Amalgamated Bank, UBCJ (Carpenters' union), IBEW, and LIUNA (Laborers' unions))
2. Social investment firms, notably Boston Common Asset Management
3. Shareholder advisory firms such as Glass, Lewis & Company (Glass Lewis) and Institutional Shareholder Services (ISS)
4. The Council of Institutional Investors (CII)
5. The Corporate Library (TCL)
6. Individual investors, including Lucian Bebchuk, and the Steiner and Chevedden families
7. Political leaders, such as Congressman Barney Frank (D-MA), the sponsor of the Shareholder Vote on Executive Compensation Act (HR 1257)

II. Competing Agendas

Members have witnessed an explosion of shareholder proposals in the 2006–2007 proxy season. As of March 30, 2007, ISS is tracking over 340 pending shareholder proposals broken down into four basic categories: anti-takeover proposals, executive compensation proposals, board issues, and social responsibility issue proposals.

CCLN members question the agendas of the groups promoting these resolutions. One member stated, *"Ofentimes the group that is authoring these [shareholder proposals] owns no shares. These people have an agenda, but I want to focus my attention on the legitimate investors and the real owners."* Another added, *"The people who are actually interested in return on their investment aren't out there authoring these bills."* Moreover, directors are concerned that large blocks of their companies' shares are controlled by groups whose agendas are unaligned with corporate performance.

Members pointed out that in the case of majority voting, labor union pension funds, individual activists, and hedge funds joined with ISS to trigger a “wholesale shift from plurality to majority voting in uncontested director elections.”⁶ Directors are troubled that the groups gaining enormous clout in proxy contests are often unconcerned with actual company performance. Many shareholders merely vote with shareholder advisory firms’ recommendations. *“Our portfolio managers don’t care [about corporate governance issues], they’re just looking to ISS for a recommendation [on] how to vote.”* Another member added, *“ISS has so much power in all these voting areas.”*

Larger groups, such as public employee pension funds, use shareholder advisory votes and other corporate governance proposals to influence companies and advance their own agendas. One member said, *“Pension funds, in many ways, are the handmaidens of the larger unions. The association of public employee pension funds in Washington has been taken over by the union pension funds, and they’re the ones directing how the pension funds are voting.”* Companies are pressured into weaker positions when they must fight proxy battles, which make *“these [shareholder] proposals ... just another way to extract concessions or put additional pressure on companies.”*

III. CalPERS as a Case Study

California Public Employees’ Retirement System (CalPERS) states that its primary interest is portfolio performance and that it responds to poor performance, in part, by placing underperforming companies on its annual Focus List.⁷ Companies are placed on this list for poor stock price performance relative to their peers and for operating under governance practices opposed by CalPERS. CalPERS has found that the companies on this list ultimately see improved stock price performance.⁸

However, CCLN members express concern that CalPERS uses weak performance as an opportunity to dictate governance policies (e.g. limits on severance pay without shareholder approval) designed by CalPERS’ own Board. Some members believe that CalPERS presses companies to conform to CalPERS’ approved governance practices, under the threat that they will otherwise pursue shareholder proposals to address their concerns. In its zeal for governance reform, some members believe that CalPERS pays more attention to its governance agenda than to the primary drivers of those companies’ weak performance, such as depressed sector performance, failure in R&D, bloated costs, etc. In this view, the leadership of these underperforming companies focuses on correcting operating and strategic problems, while CalPERS focuses on winning governance concessions.

CCLN members were troubled by the notion that CalPERS’ proxy voting guidelines do not allow for any exceptions or subjectivity. One member remarked, *“They should have more judgment behind these decisions,”* and another added, *“They need to understand the businesses better before taking these positions. They need to be more deliberate in their analysis and understanding. They should be principles based, not rules based.”*

⁶ Eric Finseth and James Carlson, “Storming the Ramparts: The Ongoing Shift in the Balance of Power Between Shareholders and Incumbent Boards of Directors,” *Corporate Governance Update* [Mayer, Brown, Rowe & Maw newsletter], March 16, 2007, 1. Available at <http://www.mayerbrownrowe.com/publications/article.asp?id=3381&nid=6>.

⁷ “CalPERS Focus List Targets 11 Companies for Lagging Stock, Financial, Governance Performance,” Press Release, March 15, 2007. Available at <http://www.calpers.ca.gov/index.jsp?bc=/about/press/pr-2007/march/focus-list-targets-11.xml>

⁸ “Wilshire Associates study of the ‘CalPERS Effect’ of corporate governance found that the stock values of companies on the Focus List subsequently outperformed the Standard & Poor’s 500 Index by 3.1 percent, per year, over five years.” Ibid.

CalPERS would disagree. In its view, the CalPERS' proxy voting guidelines and governance guidance are principles-based, recognize the unique circumstances of each company, and allow for exceptions. "CalPERS recognizes that the adoption of the Core and Global Principles in its entirety may not be appropriate for every company due to differing developmental stages, ownership structure, competitive environment, or a myriad of other distinctions."⁹ Further, CalPERS would reject the notion that they focus on winning governance concessions over operating improvements. In practice, CalPERS finds that it spends roughly equal time on discussion of business drivers and governance issues in management meetings. While acknowledging that their role is not to make strategic decisions about company operations, CalPERS would assert that these multifaceted discussions ultimately contribute to improved company performance.

CalPERS has also expressed a desire for more director communication with shareholders. Members voiced concern with this request, and engaged in a robust discussion about the nature of director communication with shareholder representatives.

IV. Director Communication with Shareholders

Although members understand the importance of keeping shareholders informed, CCLN members agree that direct communication between directors and shareholders and their representatives should occur only on an exceptional basis. *"It shouldn't be a policy of 'just say no' [to shareholder requests for communication], but you do need to figure out where to draw the line."*

CCLN members strongly endorse the traditional view that direct communication with shareholders is the job of management (principally the CEO and investor relations department) and not the responsibility of directors. One member perfectly summarized the group's view: *"I strongly believe that most communication with outside directors should stay within the CEO ranks. The CEO is responsible for communicating the basic rundown of the business and what drives the corporate strategy. To divert dialogue away from that is not fundamentally where any organization should try to push it. There are certainly exceptions ... but to encourage [directors' speaking with shareholder groups] is not the right direction to go. Then you have too many organizations talking, and the subtleties and emphasis changes, which leads to miscommunication."*

When board members do communicate with shareholders, it should be in response to a request by the company's investor relations department or from the shareholder group itself. *"If the CEO and IR people think the directors can be helpful to a conversation [that's fine], but it's got to be by request. You don't want freelancing directors out there."*

Members acknowledged that oftentimes opening up lines of communication between a director and shareholder representatives, within a controlled environment, can yield positive outcomes. One CCLN member shared an experience in which open communication resulted in the withdrawal of numerous shareholder proposals from proxy voting: *"When I met with our shareholder groups, I did it at the request of our investor relations and legal department ... I was asked to meet with six groups, and every group I met with ultimately pulled their shareholder proposals. But in having a straightforward, significant discussion, they began to understand us and be very reasonable."*

⁹ CalPERS, "The Core and Global Principles of Accountability for Corporate Governance." Available at <http://www.calpers-governance.org/principles/default.asp>

Members also drew attention to an incongruity: shareholder groups often say they'd like to discuss executive compensation, but most CCLN members stated that they have rarely seen the topic brought into the conversation. *"I'm struggling with the original question of how to improve communication. I'm sure all of us [directors] can go to talk to our big shareholders. They want to see the CEO, though, not the directors. And they don't want to talk pay with the CEO."* One member suggested a way to minimize the awkwardness of discussing executive compensation with a company's CEO: *"Would it be appropriate for the CEO to take the compensation system and put it together in a deck in simple English and bring this to talk to them?"*

The group agreed upon a basic policy for communication, recognizing the importance of engaging major shareholders while wanting to minimize the potential for misinformation and confusion that would result from multiple-party communication. *"I don't think a director should be out there having discussions freely [with shareholder groups], but I do believe directors should be accessible, and the chairs of various committees should be available to shareholder groups if asked."*

Opposition to Shareholder Advisory Votes, Including "Say-on-Pay"

I. Shareholder Advisory Votes

Members overwhelmingly and passionately oppose shareholder advisory votes, including say-on-pay votes, whether imposed through legislation or proposed through a resolution in the proxy. At the very best, members see these measures as unhelpful and uninformed distractions. More fundamentally, they see them as a breach of the core principles of American corporate governance that will erode board effectiveness and corporate performance.

Corporations are characterized by a separation of ownership and control. Shareholders have the right to elect directors, but shareholders were never intended to have the authority and decision-making power of directors: "Efforts to extend the shareholder franchise are fundamentally misguided. In public corporations ... shareholder voting has very little to do with corporate decision-making. To the contrary, the separation of ownership and control observed in such firms is inherent in the basic structure of the law of corporate governance."¹⁰

Members defend the essential integrity of the American corporate governance system. They acknowledge and support basic shareholders' rights to elect board members and to sell shares of the company if they are unsatisfied. However, members firmly believe that shareholders' rights do not include a right to advisory votes. Corporate governance can be compared with that of "a representative democracy in the political sphere. Just as voters periodically have the right to elect a government, but ... no right to dictate to the government or its officers any specific course of action to be followed, shareholders periodically have the right to elect a board but then generally enjoy no power to dictate any specific course of action to the board."¹¹

Although some in the business community view shareholder advisory votes as benign, non-binding expressions of shareholder satisfaction, CCLN members feel such votes have troubling implications and deem them deceptively benign. Directors feel that external forces, such as activist shareholders or

¹⁰ Stephen M. Bainbridge, "The Case for Limited Shareholder Voting Rights," *UCLA Law Review* 53 (2006), 603. Available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=887789.

¹¹ Eric Finseth and James Carlson, "Storming the Ramparts," 7.

special-interest groups that attempt to control board membership, fundamentally harm companies because they infringe upon directors' ability to exercise their knowledge, wisdom, and experience. Shareholders have certain inviolable rights, but so do directors. Members expressed four primary concerns regarding shareholder advisory votes.

Inconsistent with American corporate governance principles - CCLN members believe the American governance model deserves some credit for the fundamental strength and vitality of American corporations and the U.S. economy. They were disturbed by the notion that shareholders could erode the decision-making power of boards of directors.

- *“When you get into the business of accepting or rejecting these proposals, then you aren't necessarily doing what's in the best interest of the company; you begin doing what the shareholders want you to do.”*
- *“We're not spending the time working on the strategic issues we need to be working on.”*
- *“[The shareholder advisory vote movement] poses a credible threat to the free-enterprise system.”*

Dilutive of director judgment - Members expressed concern that special-interest groups could supplant board members' decisions, creating a truly dire situation in boardrooms.

- *“[Shareholder advisory votes] are a perfect example of an effort to substitute shareholder judgment for director judgment. This [substitution] is quite contrary to our whole governance structure, which is based on the business judgment rule.”*
- *“If you have the special interests coming in and able to control board membership, they will influence the business of running the company. And then you don't have the right people with the right background making the right decisions.”*

Distracting - CCLN members conveyed their frustration at being drawn away from their fiduciary responsibilities by shareholder activism.

- *“Look at it this way: it used to be that 80% of what board members did was company strategy, and 20% was talking about the kind of stuff we're talking about right now – process things. Now it's the other way around; 80% of our time is spent talking about the things we talk about in board meetings, and 20% on the actual important things like corporate strategy and operations.”*

Too vague; too late – CCLN members feel that the ambiguity of a simple yes-or-no vote would not provide sufficient guidance on any number of shareholder issues.

- *“So if it's 90% yes and 10% no, what are [the shareholders] saying? They accept the base salary or the long-term incentives? And what is the 'no' saying, exactly?”*
- *“The shareholder vote might be more an expression of general dislike of the company rather than specific [complaints].”*
- *“What do we do with a yes-or-no vote after the fact?”*

II. Say-on-Pay Proposals

Say-on-pay proposals have become increasingly common. Many voices within the business community cannot comprehend boards' opposition to these advisory say-on-pay votes. CCLN

members commonly hear arguments like, “What’s wrong with an advisory vote?” or “They seem to work fine in the UK,” or “With the options backdating and other scandals, it’s clear that boards need some advice and closer oversight.”

However, say-on-pay proposals are troubling to boards of directors who fear a slippery slope. One member predicted, *“These are only the beginning. First it’s say-on-pay, then it’s an all-out assault on directors.”* Members see the say-on-pay movement as a precursor to an onslaught of resolutions diluting directors’ authority. *“You start with say-on-pay, and then you move to say on cash flow and say on acquisitions. Once the job you’re being asked to do is second-guessed in the marketplace ... then our roles are being undermined.”*

Experts in corporate law agree: “Executive compensation will only be the first of many management issues upon which the shareholder community will focus over time ... A new era of shareholder involvement with and control over American corporations appears to be dawning.”¹²

One member saw say-on-pay proposals as fundamentally more problematic than other proxy issues. The member stated, *“I think say-on-pay is different from the proxy issues of majority voting and classified boards because those give the impression of entrenching management, whereas say-on-pay is attacking board members’ responsibilities.”*

III. Need for action

Shareholder activist groups are strengthening, and shareholder proposals are proliferating. Judging from the success of say-on-pay proposals in the 2006–2007 proxy season, shareholder resolutions and perhaps even shareholder advisory votes could gain traction and credibility within the marketplace.

“We need to make progress on stopping the assault on corporate America and the erosion of directors’ control [that result from these shareholder votes],” said one member. CCLN members underscored the importance of communicating with boards of public corporations about this threat: *“We have to get to those 1,000 public company boards that are under considerable pressure. Those are the ones who think these [shareholder advisory votes] are benign.”* One member said, *“We need to position it as not just a pay issue, but as a governance issue.”*

The Business Roundtable and the U.S. Chamber of Commerce have taken up directors’ positions on these issues, but these two groups are limited by the fact that they are lobbying organizations. Other defenders of boards’ decisions and the American corporate governance system are few and fragmented. One member remarked, *“I don’t think the arguments against say-on-pay are being articulated very well in the market.”* A CEO or director rarely speaks out publicly against shareholder advisory votes. One member explained this, saying, *“Most of the companies don’t weigh in on this because they don’t want to be pulled into the spotlight on this issue.”*

Members suggested a number of avenues for communicating with the boards of public corporations about the pending threat of shareholder advisory votes. One member suggested approaching *“a think tank or major academic institution that is balanced and can speak out on this issue. Perhaps they could focus on this notion of the threats to corporate governance today ... It might even be wise to have a summit of thinkers on this subject.”*

¹² Ibid., 9.

CCLN members also suggested approaching leading figures such as Alan Greenspan or Warren Buffett. These individuals would appreciate the delicate balance between protecting shareholders' rights and ensuring directors' continued control of corporate decision-making.

One member declared, *"Boards and companies must take some leadership [on this issue] either through communicating with shareholder groups or finding a way to make something happen."* Although members have not yet identified the ideal medium for advocating the preservation of American corporate governance, members unanimously agree that reversing the ever-strengthening movement towards shareholder oversight of boards' decisions is critical.

Conclusion

Arguably, the CCLN members represent the very best of corporate directors – accomplished individuals with unimpeachable ethical standards and records of leadership. They are diligent, balanced, and thoughtful. The fact that this group is now seriously concerned about the direction of corporate governance should be troubling to policy makers and shareowners.

CCLN members felt that the SEC's disclosure rules have been marginally helpful at best. Shareholder activism too often does not serve the interests of improved corporate performance, in spite of claims to the contrary, and advisory votes undermine a model of corporate governance proven to be more successful than any competing model. Yet the calls for change are mounting; and the slope is slippery indeed.

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