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September 28, 2007

Nancy M. Morris, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-16-07
File No. S7-17-07

Dear Ms. Morris,

The American Federation of State, County and Municipal Employees ("AFSCME"), is the largest union in the AFL-CIO representing 1.4 million state and local government, health care and child care workers. AFSCME members participate in over 150 public pension systems whose assets total over $1 trillion. In addition, the AFSCME Employees Pension Plan (the "Plan") is a long-term shareholder that manages $850 million in assets for its participants, who are staff members of AFSCME. The funds in which AFSCME members and retirees are participants and beneficiaries provide patient, long-term capital to support sustainable value creation at public companies. These funds are sufficiently diversified that they essentially "own the market"; as a result, AFSCME is keenly interested in corporate governance practices that promote accountability and enhance company performance.

We write in response to the Commission's request for comment on two rulemaking proposals, Files No. S7-16-07 and S7-17-07, regarding Rule 14a-8, the Shareholder Proposal Rule (the "Rule"). For the reasons set forth below, we oppose adoption of either proposal.

As an initial matter, we believe that the Commission should not take any action on either of the proposals until it is back to full strength. With the departure of Roel Campos, the Commission now has only four Commissioners, three of whom were appointed by the Republican party. Acting under these circumstances would harm the credibility of whatever proposal was adopted. In addition, the 2007 proxy season, which took place under the interpretive regime the Commission now wishes to overrule, was not marked by unusual disruption, with just three proxy access shareholder proposals coming to a vote. Accordingly, there is no compelling need to act on the proposals before Mr. Campos's successor is in place.

We view the Commission's proposal in Exchange Act Release No. 56161, eliminating shareholders' ability to file proposals on proxy access, as unsupported by the history and purpose of the Rule and unwise from a public policy perspective.

Given the key role of director elections under state law, it makes no sense to treat proposals regarding shareholder access to the company proxy statement for the purpose of nominating director candidates differently from other kinds of proposals. The Commission's stated concern—that such proposals would lead to contested elections that could circumvent the Commission's proxy rules—can be effectively dealt with using measures short of barring the proposals.

The Commission's proposal in Exchange Act Release No. 56160 to allow only holders of over 5% of a company's shares to submit a binding proxy access proposal is a small step in the right direction. The Commission, however, mistakenly conflates shareholders' right to amend bylaws with actions relating to changes in control. These are distinct situations, which should be separately regulated. William Act thresholds and disclosures requirements are appropriate for change in control situations but not for shareholder procedures to amend bylaws.

Several fundamental aspects of the 5% access rule, including the 5% submission threshold, make it unlikely that it would ever be used by shareholders interested in long-term value creation. Further, the burdensome disclosure requirements contained in the 5% access rule, which in some areas go beyond even the requirements imposed on participants in a proxy contest, would deter use of the rule and could have unintended negative consequences.

In our view, the Rule is an effective mechanism for facilitating communication about important issues, including corporate governance arrangements, affecting public companies. Shareholder proposals have led to key reforms to director elections, including the widespread adoption of majority voting, as well as to changes in executive compensation practices and takeover defense measures. Proposals submitted pursuant to the Rule have also supplied valuable evidence of shareholder support for regulatory reforms such as stock option expensing and auditor independence. Accordingly, we urge the Commission not to alter the basic elements of the Rule, such as the ability of shareholders to submit precatory proposals.

Shareholder Access to the Company Proxy Statement

Over the past several years, AFSCME has been deeply involved in the debate over shareholder access to the company proxy statement. From the beginning, we have believed that the missing link in corporate governance reform continues to be board accountability to long-term shareholders. In our current system, where the incumbent nominating committee controls the composition of the director slate, and mounting a dissident director campaign can easily cost $1 million or more, accountability to shareholders is blunted. As Relational Investors' Ralph Whitworth has observed regarding the board nomination process, "You dance with who brought you, right?"[1]

[1] Interview with Geoffrey Colvin, Wall Street Week with Fortune, broadcast July 19, 2002 (transcript available at http://www.pbs.org/wsw/tvprogram/whitworthinterview.html)

Proxy access helps mitigate the collective action and free rider problems that have long been acknowledged as interfering with shareholder monitoring and a well-functioning system of corporate checks and balances. By shifting some of the cost of nominating director candidates from the nominating shareholder to the company, proxy access would increase the likelihood of a shareholder nominating directors even though much of the benefit accruing as a result of a successful challenge would be enjoyed by other "free riding" shareholders.

Responsibly crafted proxy access schemes, like those advanced by the Plan's shareholder proposals, would confer the right only on significant, long-term shareholders and would require nominating shareholders to comply with all applicable laws and regulations, including the Commission's proxy rules. The proxy access formulation AFSCME supports would allow only the running of a "short slate" of director candidates and not contests for control; accordingly, proxy access could reduce dependence on the market for corporate control as a monitoring device.

For these reasons, AFSCME supported the Commission's 2003 rulemaking that sought to impose a proxy access regime on public companies upon the occurrence of certain triggering events related to breakdown of the proxy process. But when it became clear that the 2003 rulemaking had been abandoned, AFSCME returned to our original strategy—which had prompted the process leading to the 2003 rulemaking proposals—of advocating for proxy access on a company-by-company basis. After the Second Circuit's ruling in AFSCME v. AIG, three proxy access proposals were submitted for a vote during the 2007 proxy season, one at Hewlett-Packard was co-sponsored by the Plan. The level of support they received—one received majority support, while the others were favored by 45% and 43% of shares voted—show the seriousness with which the institutional investor community regards the issue of proxy access.

As we argued in AFSCME v. AIG, the interpretation applied by the Staff after 1990—the one the Commission now seeks to codify in Release No. 56161—erroneously puts proxy access proposals on a different footing from all other generic proposals relating to director election procedures and qualifications. Adopting this approach would be a mistake.

Rule 14a-8(i)(8) (the "Election Exclusion") allows exclusion of proposals that "relate to an election" of directors. The Staff has refused to permit companies to exclude many proposals seeking to establish general procedures or qualifications for director elections, including cumulative voting, majority voting and director qualifications, but, since 1990, has interpreted the Election Exclusion as countenancing exclusion of proxy access proposals, on the theory that such proposals "may result in contested elections." This contested elections basis does not appear in Rule 14a-8 or in any of the Commission's prior releases dealing with the Election Exclusion.

As the court in AFSCME v. AIG held, the Staff's interpretation is inconsistent with the Commission's 1976 release, Exchange Act Release No. 12598, which distinguished between proposals aimed at influencing a particular election (by nominating a candidate or proposing a director's removal, for example), and those seeking to establish general policies or procedures applicable to future director elections.

The Commission asserts that codification of the Staff's interpretation is necessary to prevent circumvention of the Commission's other proxy rules, which require disclosure of certain information in contested director elections. But as the Plan's proposals at Hewlett-Packard, AIG, and Marsh & McLennan show, a proxy access regime need not conflict with the proxy rules. As mentioned above, the proposal analyzed by the court in the AFSCME v. AIG case required that shareholders seeking to use the access right agree to comply with all of the Commission's rules, including the proxy rules. The court cited this fact, as well as the requirement that company proxy statements (including those containing shareholder-nominated candidates) comply with the proxy rules, in questioning whether a proxy access right necessarily conflicts with the proxy rules. The Commission's concern over this conflict does not require the amendment proposed in Release No. 56161; instead, it could be addressed by amending the Election Exclusion to provide that companies may exclude proxy access proposals that do not contain language requiring the nominating shareholder to comply with the proxy rules and/or provide information specified by the Commission.

The Commission's rationale highlights another issue raised by this rulemaking: Nothing prevents companies from adopting a proxy access regime now, without being spurred by a shareholder proposal. Recently, Comverse Technology, Inc. amended its bylaws to create a shareholder proxy access right (one, it is worth pointing out, requiring that nominating shareholders agree to comply with all laws and regulations). If conflicts between a proxy access regime and the Commission's proxy rules are a matter of urgent concern to the Commission, consideration should be given to amending the proxy rules more generally to reflect developments like the one at Comverse.

The interpretation of the Election Exclusion proposed in Exchange Act Release No. 56161 would impair shareholders' state-law rights to propose proxy access bylaws. The law of most states, including Delaware, allows shareholders to amend the bylaws unless there is a limitation in the charter or bylaws. The bylaw proposed in the AFSCME v. AIG case was supported by an opinion of Delaware counsel stating that a Delaware court would likely hold that the bylaw was proper under state law. Using the Election Exclusion to place these proposals out of bounds under the Rule when they would be permissible in an independent solicitation undertaken at the proponent's own expense is not consistent with the Commission's own stated goal of fidelity to state-law governance rights.

The 5% Proposal

In Exchange Act Release No. 56160, the Commission has proposed to allow only those proxy access proposals that satisfy rigorous requirements, including ownership of more than 5% of the company's outstanding stock for one year, submission of a binding proposal and compliance with extensive disclosure requirements. The rule as currently proposed would be unusable by long-term, diversified shareholders such as the funds in which AFSCME's members participate. The disclosure requirements, which are burdensome and could have unintended consequences, are not appropriate for a shareholder proposal that by itself has no effect on the board's composition.

To begin, we do not agree that proxy access proposals should require a higher level of ownership than other proposals submitted pursuant to the Rule. Comparing a proxy access proposal with a proposal to require that directors be elected by holders of a majority of shares, it is difficult to understand why the former should be limited to holders of 5% of outstanding shares while the latter may be submitted by a shareholder owning $2,000 of stock. Both proposals would establish procedures that could, in some future election, make it easier for shareholders to affect the composition of the board. The Commission has cited no evidence that shareholders respond to the size of a proponent's holdings when voting on a proposal; indeed, the fact that the Rule allows companies to omit the identity and holdings of a proponent suggests that this information is not considered material to the voting decision. Williams Act disclosure triggers make sense only in the context of an actual contested election event. Williams Act triggers are not useful or appropriate, nor are they consistent with past precedent for actions directed to amending company bylaws.

Even assuming that a higher threshold is appropriate, the requirement proposed by the Commission of 5% of outstanding shares is too high. Especially at larger public companies, the requirement that proponents own more than 5% of a company's outstanding shares ensures that diversified shareholders like public pension funds would not be eligible to submit a proxy access proposal, even if they joined together. Research by the Council of Institutional Investors shows that the ten largest public pension funds' combined holdings in representative large-, mid- and small-capitalization companies would not reach the 5% threshold. We urge the Commission to consider adopting a 1% threshold, which was proposed in the 2003 rulemaking as the threshold for submitting a proxy access triggering proposal or, in the alternative, studying the size and distribution of shareholdings before setting a threshold.

Further, it is unclear why the Commission has chosen to privilege binding proxy access proposals. The Plan has submitted both binding and precatory proxy access proposals. In many cases, precatory proposals were submitted because a company had a supermajority voting requirement to amend the bylaws or did not allow shareholders to amend the bylaws at all.

At companies with a supermajority voting requirement, it can be difficult even for corporate management, aided by broker voting, to achieve passage of a proposal because the supermajority requirement is calculated as a percentage of outstanding shares; thus, achieving high turnout, in addition to a high level of approval among those who turn out, is required. At companies that have eliminated shareholders' power to amend the bylaws, which research in The Corporate Library's database pegs at approximately 4.5% of companies in the Russell 1000 and Russell 2000 indices, a precatory proposal is the only mechanism to raise the issue of proxy access. No reason has been offered to support imposing a binding proposal limitation at companies that prohibit shareholder bylaw amendments, and we cannot conceive any rational reason for doing so.

As well, proponents may wish to submit proxy access proposals in precatory form because the regime they envision cannot be expressed adequately in a 500-word shareholder proposal. For example, a proponent may wish to incorporate a resubmission threshold concept, like the one used by Apria Healthcare, in its proxy access regime, which could make it very difficult to express the entire bylaw and even a minimal supporting statement in 500 words. A precatory proposal can set forth the general principles without having to draft the entire bylaw.

Moreover, the disclosure requirements proposed in Exchange Release No. 56160 go far beyond anything shareholders would find useful in voting on a proxy access proposal. In fact, they exceed in some respects the disclosure required of nominating shareholders in a proxy contest or of shareholders filing a Schedule 13D to indicate that they intend to engage in activities that may result in a change of control of the company.

The Commission has not supported the notion that additional disclosure is warranted or would be useful to shareholders simply because a proposal concerns proxy access. The proposal itself is not a contest, and a proponent that submits a proxy access proposal may not intend to use the proxy access right. A proponent may favor adoption of a proxy access regime so that a shareholder with greater institutional capacity for undertaking a nomination can do so in the future. Accordingly, disclosures dealing with a proponent's motivation, history and relationships with the company and other similar matters don't make sense at this point in the process. Institutional proxy voting guidelines, which focus on company-specific factors and the substance of the proposal, suggest that institutional shareholders would not use this kind of information in making voting decisions on proxy access proposals.

The proposed disclosures could, we believe, disrupt the process of dialogue between companies and shareholders. One proposed element would require a shareholder that files a proxy access proposal to disclose details regarding each communication with the company for a 12-month period before the proposal was filed. Given the possibility that a shareholder may submit a proxy access proposal at a company in the future even if there is no inclination or forethought to do so in the present, the 12-month disclosure period presents an open-ended and unreasonable obligation upon shareholders to document each and every communication with a company.

This burden could lead proponents to eschew dialogue, which could polarize the governance debate and squelch useful settlements and experimentation with evolving governance practices.

Finally, the proposal that proponents be required to disclose information about individuals "associated with" the plan to submit a proxy access proposal is confusing and not useful to shareholders. First, it is not clear how the proposed requirement would apply to many public pension funds, at which both staff members and boards of trustees make decisions about activism initiatives. In addition, the Commission has offered no reason why information about the selection process and qualifications of such individuals—disclosure that goes beyond what is required in a Schedule 13D of shareholders that intend to influence the control of a company—would be useful to shareholders. To the suggestion that a proponent of an access proposal might intend later to use the access regime to nominate candidates, the same could be said of a proponent of a proposal to declassify the board or adopt cumulative voting. In each case, the answer is the same: require heightened disclosure if and when the shareholder decides to nominate candidates. As with a proponent's holdings, current practice suggests that institutional shareholders focus on the substance of the proposal and its appropriateness at the target company rather than collateral matters like the ones the Commission is now proposing be disclosed.

The Shareholder Proposal Rule

The Rule has served a key function in the debates during the past several decades over corporate governance. Because a proposal's showing depends on other shareholders' opinions of it, the Rule imposes a market test on corporate governance reforms. The graduated resubmission thresholds ensure that an idea that fails to gain significant support cannot be reintroduced at that company in the near term. By focusing reform efforts on a particular company, the Rule permits a more nuanced approach and allows experimentation with newer governance practices.

The vast majority of proposals are precatory (or non-binding), which can also be beneficial to the process. A proponent and a company can engage in dialogue regarding a proposal's subject and may agree on a settlement that works better for the company than the original proposal. This feature is particularly valuable when a proposal deals with a complex topic such as executive compensation or corporate social responsibility.

The Plan's experience with the shareholder proposal process confirms these generalities. Over the last four years, the Plan has filed nearly 100 shareholder proposals. Fifteen of these proposals received a majority of shareholder votes, on topics including board declassification, option expensing, majority voting, and performance-based restricted stock.

Twenty-nine of those proposals were withdrawn before a vote because we had reached agreement with the company on a settlement. Examples of settlements include implementation of majority voting, board declassification, removal of poison pill, agreements to continue dialogue over compensation, and agreement to implement equity holding policies. Proposals the Plan and other shareholders submitted asking companies to provide shareholders with an advisory vote on executive compensation led to the formation of a working group whose members included representatives of both shareholders and companies. The working group explored implementation issues related to the advisory vote, culminating in a July 2007 day-long roundtable aimed at furthering dialogue on the issue.

In light of these factors, AFSCME strongly opposes any effort to curtail shareholders' ability to submit proposals for inclusion in the company proxy statement. Although the impulse to do so may spring from a misguided desire to minimize disruption for companies, we believe that eliminating the shareholder proposal avenue could lead to increased use of tactics such as "vote no" campaigns, which often personalize governance-related disagreements, as well as independent solicitations. Neither companies nor shareholders would be better off in such an environment. Requiring precatory proposals to be presented in an electronic forum, which lacks the inclusiveness of a proxy mailing, could lead proponents to recast many proposals in binding form. It would be surprising if companies preferred that outcome. Put simply, the process works well now and should not be changed in any fundamental way.

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In sum, we strongly urge the Commission not to adopt either of the proposals put forward in Exchange Act Release Nos. 56160 and 56161. Proxy access should remain a work in progress at the Commission for the time being. A new proposal which acknowledges the difference between a proposal that establishes procedures for shareholder access and a contested election itself remains to be crafted. We appreciate the opportunity to make our views known to the Commission. If we can be of further assistance to the Commission, please do not hesitate to contact Richard Ferlauto, Director of Corporate Governance and Investment Policy, on (202) 429-1275.

Very truly yours,

Gerald L. McEntee

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