

**Securities Exchange Commission
Proposed Security Holder Director Nominations Rules
Roundtable Discussion - March 10, 2004
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The Nathan Cummings Foundation

The Nathan Cummings Foundation is an institutional investor with an endowment of approximately \$430 million, of which \$311.8 million is invested in equity-based securities. Approximately \$242.2 million is invested in marketable stocks, domestic and foreign. We directly own \$102.7 million and the balance of \$139.5 million is invested in co-mingled funds.

We actively vote the proxies on the direct holdings in accordance with our Board-approved proxy voting policy; we do not delegate that fiduciary responsibility to the investment managers or to a voting service. In 2003 we voted on 501 resolutions presented to the shareholders of 154 companies whose stocks we held directly. With the new SEC provisions requiring investment managers to have and disclose proxy voting policies and records, we have begun dialogues with our investment managers regarding their proxy voting policies and practices on co-mingled funds.

Duty of Oversight

As a long term investor the Foundation is concerned about corporate conduct that seeks to maximize near-term profits and compensation, but that jeopardizes the long-term viability of those same companies. We believe that such business models are not sustainable and are not in the best interest of investors. Therefore, we consider corporate governance a major issue.

We are not what some refer to as a universal investor. And so, yes, we could sell a stock if we didn't like the company's governance or conduct. We could adopt an exit strategy. However, we prefer a strategy of making companies better for the long term, a strategy of loyalty and voice.

Shareholders have a fiduciary duty of oversight, but only limited ways to exercise that oversight directly. We can and do vote our proxies. We can and do propose non-binding shareholder resolutions as a way to raise issues for discussion. Interestingly, the mechanism for both of these is the company's proxy statement, the same mechanism we are talking about today. Beyond this limited voice for shareholders, oversight is the responsibility of the Board of Directors.

It is the Board that has the primary responsibility to oversee corporate conduct and to represent the long term interests of the shareholders. Unfortunately, the high profile incidents of management abuses over the last few years have highlighted the fact that some boards of directors are not fulfilling these responsibilities. In some cases it was general passivity or too much deference to management. In some cases it was a lack of knowledge of the business model and understanding the financial structure. The result was that between mid-2001 and 2002 nine of the largest 100 corporations were subject to formal SEC investigations for fraudulent financial reporting. In three of those cases alone investors lost \$155 billion while the CEO's netted over \$2 billion from exercising stock options.

Not all companies behave this way and not all boards of directors are complicit. However, the creative financial engineering by companies, their auditors and their lawyers, combined with excessive executive compensation, leads one to ask: Who is minding the store? Who on the board of directors is asking the tough questions? Are many current boards of directors really up to the task?

Access to the Proxy to Nominate Directors

The question before us, then, is the process for electing boards of directors. There is growing evidence that the current process is not working well. What we need are not more layers of regulations, but incentives to make the current process work better.

Recently enacted rules require that most public companies have a majority of independent directors with "independent" defined in terms of employment and direct business dealings. However, this definition of "independent" does not guarantee independent thought or accountability. It does not guarantee the integrity and temperament to provide effective oversight. It does not guarantee the ability to question, the ability to disagree, the ability to speak truth to power if needed.

Some may think this would cause too much disruption in the board room. But when did we decide that debate is bad for decision making, that dissent means dissension, that consensus is better than intelligent collective decision making.

Recently enacted rules put new responsibilities on nominating committees to make sure that well qualified candidates are put forth for the board of directors. The new requirements should increase the transparency of the nominating committee process. While this should be helpful, it may not be. It may turn out to be just another process. The new nominating committee procedures are a necessary, but not a sufficient, condition to promote better corporate governance.

The proposed rules we are discussing today are a very real incentive for nominating committees to function effectively. With access to the proxy to nominate a limited number of directors, long term shareholders will have an orderly mechanism through which to exercise their voice. The only real alternative for shareholder voice now is through a proxy fight. And this public expression of discontent is a costly, disruptive process for all. I think the word that many used to describe the Disney meeting last week was "raucous."

To those who are concerned about giving large, long term shareholders access to the proxy to nominate directors I would say: Any nominees will still have to be elected – and that is far from being a sure thing. We are talking about a very limited number of directors, not a take-

over of the board. If the nominating committee works well, shareholders won't resort to this process. This has been the experience in the United Kingdom and many other countries which do allow shareholder access to the proxy.

You should think of these proposed rules: not as a adversarial contest, but as a limited election competition; not as an assault on corporate authority, but as a safety valve; not as another onerous regulation, but as an incentive to effective board governance.

The Role of the SEC

The Commission's web site states that, "The primary mission of the U.S. Securities and Exchange Commission is to protect investors and maintain the integrity of the securities markets." I would note that the SEC is meant to protect investors, not to entrench managements regardless of their conduct. The basic securities laws are about disclosure of financial and other information so that investors can make well informed decisions. This assists investors in deciding whether to use an "exit" strategy.

The securities laws also give shareholders a "voice" strategy and this is through the proxy. Shareholder approval is required for major corporate transactions and compensations plans. Shareholders can express preferences through non-binding shareholder resolutions. However, on the matter of electing directors – the most important aspect of corporate governance – there is no real vote. "For" and "withhold" is not a choice.

In Conclusion

Granting shareholders access to the proxy to nominate a limited number of director candidates is not about imposing regulation, nor is it about imposing the "activist agenda" of a few on the many.

Shareholder-nominated candidates are likely to be put forth in only a few elections each year. Then they will need to attract broad-based shareholder support in order to actually be elected to the board. Even if elected, they will be a limited number on the board. The prospect of a contested election, though, can be a wake-up call for boards of directors and nominating committees.

Granting shareholders access to the proxy to nominate a limited number of director candidates is about creating incentives for the corporate governance system to work properly. It is about improving corporate governance.