



ALERT
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Executive Summary: Survey of Majority Voting in Director Elections

Until recently, virtually all directors of U.S. public companies were elected under a “plurality” vote standard. Under such a standard, the nominees with the largest number of votes are elected as directors, up to the maximum number of directors to be chosen at the election, without regard to votes “withheld”, “against” or not cast. A nominee in an election to be decided by a plurality could theoretically be elected with as little as one vote, thereby ensuring that, in an uncontested election, nominees slated by a board will be elected and that board seats will not be left vacant. Following the apparent failure of the SEC’s 2003 initiative to give large, long-term security holders direct access to a company’s proxy statement for purposes of nominating a limited number of director candidates, stockholder activists began exploring a majority voting standard (and related changes in state corporate laws, the preponderance of which provide for plurality voting as the default voting standard) as an alternative mechanism which would make stockholder votes cast against a nominee meaningful.

Neal, Gerber & Eisenberg LLP has prepared a comprehensive survey (available at http://www.ngelaw.com/files/upload/survey_callen.pdf) of majority voting in director elections which highlights whether a company listed has adopted: (a) a non-binding policy addressing the potential consequences of a director otherwise elected by a plurality vote failing to garner a majority vote or (b) a binding bylaw provision which requires that a nominee receive a majority vote in order to be elected. The following trends are worth noting:

Policy vs. Bylaw. The survey of responses to the majority vote movement indicates that a clear majority of companies that have taken definitive action have adopted policies rather than bylaws. Of 87 companies listed in the survey, 69 (79%) adopted policies, 14 (16%) adopted bylaws, and four (5%) adopted both a policy and bylaw. Initially, many companies followed the lead of Pfizer, Inc. which adopted a majority vote policy on June 23, 2005 and then amended its policy on October 27, 2005 to include a detailed director resignation policy addressing the status of holdover director nominees who fail to receive support from a majority of votes cast. The trend toward including detailed director resignation policies was also fueled, in part, by Institutional Shareholder Services (“ISS”) announcing on November 18, 2005 that, although it would generally support stockholder proposals calling for directors to be elected by a majority of votes cast, it would consider recommending against such proposals if companies adopted formal governance principles that presented “a meaningful alternative to the majority voting standard” and included, at a minimum, certain stipulated elements addressing the status of nominees who fail to receive support from a majority of votes cast.

However, some of the enthusiasm for adopting a majority vote policy was dampened by FAQs issued by ISS in December 2005 indicating that: (i) ISS would only support “true majority voting standard policies” which address the state-law holdover rule and (ii) ISS’s policy did not constitute a blueprint for a policy acceptable to ISS. Moreover, the SEC’s denial of Hewlett-Packard Company’s request to exclude a non-binding majority vote stockholder proposal from its 2006 proxy statement, on the grounds that the majority vote policy previously adopted by HP “substantially implemented” the substance of the proposal (together with the SEC’s denial of relief to all other companies making similar arguments), also served to make the adoption of a policy less attractive.

Since Intel Corporation adopted a majority vote bylaw on January 19, 2006, which includes a director resignation policy addressing the issue of holdover directors, there has been a marked uptick in the number of majority vote bylaws adopted. Of the 17 other bylaws described in the survey, nine, or 53%, were adopted subsequent to Intel's action. To date, and taking into account the limited number of majority vote bylaws which pre-dated the recent movement, over 16% of the companies in the S&P 500 have adopted either a policy or a bylaw.

Votes Cast vs. Votes Outstanding. Of the 73 policies reflected in the survey, 69, or 95%, are based upon a majority of votes cast standard. The above-described positions of ISS and the SEC served to limit the utility of adopting the more rigorous standard of a majority of outstanding votes, and, as indicated in the survey, two companies that originally adopted policies based upon votes outstanding have modified their policies to refer to a majority of votes cast. Of the 18 majority vote bylaw provisions described in this survey, 17, or 94% require that a nominee receive the affirmative vote of a majority of votes cast in order to be elected, rather than the more rigorous standard of a majority of votes outstanding. The latter standard could, as a practical matter, make it very difficult to elect a director.

Uncontested Elections. Of the 73 policies described in the survey, 59, or 81%, contain a carve-out for contested elections, with the terms of four announced, but as yet unpublished policies not being clear enough to make a determination. By contrast, only 10 of the 18 bylaw provisions described in the survey, or 56%, contain a carve-out for contested elections providing that directors will be elected by a plurality vote in such situations.

Influence of Stockholder Activism. As indicated in the survey, the influence of stockholder activism, particularly from the building trade unions, on the majority vote movement is undeniable. ISS reports that more than 140 majority vote proposals were filed for the 2006 proxy season (including at least 66 from the United Brotherhood of Carpenters and Joiners of America), marking a material increase from the 89 filed in 2005 (of which the 62 that came to a stockholder vote received average support of 44%) and the 12 filed in 2004 (which received average support of 12%). It appears that a number of majority vote policies and bylaws were adopted in the face of an imminent stockholder proposal, in response to the receipt of such a proposal or in response to stockholder litigation. There has also been a marked incidence of majority vote bylaws or policies being announced as part of a package of corporate governance reforms, such as board declassification.

Additionally, any change in the voting policies of mutual funds managed by Vanguard, Fidelity, Putnam and certain others who generally opposed director majority vote proposals during the 2005 proxy season, could have a material influence on the outcome of this year's proposals and the direction of the majority vote movement.

Since companies are continuing to address majority voting and those companies that have adopted policies have sought varying degrees of publicity for their response to the majority vote movement, the statistics in this summary cannot be viewed as definitive. Nonetheless, the survey reveals a number of distinct trends, including the dominance of majority voting as an issue for the 2006 proxy season and the likelihood that majority voting, in one of its forms, is here to stay.

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*The complete 34-page survey may be accessed via the firm's website at http://www.ngelaw.com/files/upload/survey_callen.pdf
If you would prefer a copy by mail, contact Shelly Surdyk at (312) 269-5298 or ssurdyk@ngelaw.com.*