

# OPTIMIZER

HELPING PUBLIC COMPANIES—AND THEIR SUPPLIERS—DELIVER BETTER AND MORE COST-EFFECTIVE PROGRAMS

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NOW IN OUR 20<sup>th</sup> YEAR

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## MORE TAKEAWAYS FROM THE 2013 ANNUAL MEETING SEASON: OUR “NUMBER-ONE THING” WARNING COMES TRUE...IN SPADES, AS DOES OUR WARNING RE: “BIG HATS/NO CATTLE”: THINGS TO THINK ON AS YOU PLAN FOR NEXT YEAR

*The big spring meeting season proved the OPTIMIZER to be a mighty good predictor of the way things would go this year, if we do say so ourselves: So now's the time, we say, to start looking and thinking and planning ahead with next year in mind:*

Meetings were mostly peaceful, as predicted -- and right now, we'd predict an even quieter 2014 – at least where sign-wavers, chanters and other actors-out are concerned: No “Pay your fair share of taxes” folk and no “99-percenters” to speak of. But as we always warn; (1) The need to be alert to and prepared for new and unexpected “flashpoints” is always critically important as you plan your Annual Meeting, (2) Never assume that the upcoming meeting will be “just like last year's” (3) There's no such thing as being “over-prepared” and (4) - and most important to remember - “The only meeting that really counts is your own!”

The mining industry suddenly became the focus of several flare-ups this season – where activists borrowed many of the “99-per-center” tactics. About 20 active and retired workers showed up to demonstrate at the Peabody Energy meeting in normally sleepy Gillette, Wyoming and three protestors were arrested for hanging and displaying banners in off-limits areas and PNC Financial – targeted as a lender to the mining industry by another 20 or so activists from the “Earth Quaker Action Team” – a new group, to us at least – had to cut its meeting short after protestors asked the bank to stop lending to mountain-top coal mining operations and began a sing-in with “Which side are you on.” This, dear readers, is why we always end our annual meeting tune-up articles and webcasts with the same reminder: To have an emergency script in hand in order to summarily conclude the meeting if you have to, for sanity's and safety's sake.

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**At Cablevision Systems the CEO called police into the company's annual meeting to throw out protestors complaining about a labor dispute** – after several warnings were ignored: A good excuse for us to remind again that companies - regardless of their size - and regardless of whether or not they are expecting trouble - **MUST** have a clear and quickly enforceable plan – and enough people at the ready – to deal firmly with meeting attendees who do not respond to “fair warnings” that they are out of order...

**Our prediction that many companies would haplessly ride into their meetings with “a big hat”** (in the form of a high quorum number) **“but no cattle” played out in spades this spring: CTH&A Inspectors of Election** attended four meetings where one or more director candidates resigned the day before the meeting – rather than to be embarrassed by their low vote totals...which, as a consequence of their withdrawals as nominees, were never officially tabulated and reported. At least three of these fiascos could likely have been prevented, had the folks riding herd on the meeting done their math carefully, and developed and launched a decent program to round up the retail vote earlier-on. And readers, as we noted last issue – this makes all the directors feel under-protected – and uneasy – and it's not good for your own careers.

**The “poster child” for the “big hat, no cattle award” turned out to be Occidental Petroleum's long and imperially reigning Chairman Ray Irani** – where, after an earlier and very embarrassing flap, the board decided to cut the CEO's tenure short - on short notice - then had to reverse course amid howls of protests from the investment community that Irani was plotting against his own CEO to entrench *himself*. Ultimately – and yet another unpleasant surprise to directors it seemed – it was Irani who was forced to step down from the board – two years ahead of schedule – when shareholders ended up voting against his reelection by a 3 to 1 margin. Here, we'd bet that a “retail reach-out program” would have been more likely to increase the votes-No...which is always something to think about too. We are also betting that the sudden resignation of long-term **Avon Products** board member and Chairman **Fred Hassan** – just a few days before Avon's Annual Meeting was also prompted by similar low-vote-getting....though we'll never know for sure. P.S. Most market-watchers now expect Oxy to split into three companies before long...so please

read the next section with particular care – and please remember that the *OPTIMIZER* was way, way ahead of the curve in predicting this powerful new trend...

*Our most important prediction in terms of a dramatically shifting governance landscape – that investors would increasingly hold directors' feet to the fire over financial issues – and, in particular, their 'stewardship' of shareholder assets – was borne out in spades this season:*

**In the season's most dramatic example of successfully holding directors' feet to the fire, Amerada Hess settled the proxy fight launched by hedge-fund Elliott Management just hours before the meeting convened -basically caving on everything:** Early on, Hess replaced four of its original candidates with new ones, in response to Elliott's charges of cronyism. Then they promised to back two of Elliott's three candidates if Elliott would back Hess's five, which Elliott quickly nixed. Then – after an “all-nighter” at the Four Seasons Hotel – featuring players from **Goldman Sachs, Wachtell, Lipton and MacKenzie Partners** on the Amerada Hess side – with **Paul Weiss** and fast-emerging proxy-fight superstars **Okapi Partners** working for Elliott – Hess agreed to accept all three Elliott candidates – and to separate the roles of Chairman and CEO – and to have annual rather than staggered board elections to boot. Well beforehand, Hess had announced that it would sell its gas stations, raise its dividend and buy back stock, in an effort to raise the stock price and fend off unhappy investors. But despite these earlier moves, the company's last minute “cattle calls” came up about 16 million votes short. [A secret source gave us a rundown of the fees that advisors booked here, and on the Amerada Hess side alone it is a truly staggering number.]

**In yet another big development – and with a fresh new entrant on the holding-feet-to-fire scene, please note well – the California State Teachers' Retirement System – and their ally and advisor Relational Investors LLC** – which together held 7.3% of **Timken Co.** – saw their nonbinding resolution to split Timken in two achieve a 53% majority vote. Timken immediately formed a special committee of the board to evaluate the deal... “by the end of the third quarter.”

**Also this spring, activist investors forced Murphy Oil Corp. to sell off its retail gas business and forced**

**the firing and ouster from the board of SandRidge Energy's CEO** – who was accused of putting personal interests ahead of shareholder interests - with too-high pay, sweetheart deals with family controlled companies and poor financial results to boot - although his belated “booting” generated a \$90 million severance package because the board deemed his dismissal to be “without cause.” (More to come on this one, we'd bet.)

*As Jeffries & Co. analyst Subash Chandra summed up for the WSJ, “The fact that companies are thinking about returning cash and being accountable for their cash is a sea change.”*

**Despite all this, serial pot-stirrer Carl Icahn has had only modest successes so far this year:** His proposal to have **Transocean Ltd.** pay a \$4 a share dividend was defeated, in favor of a more modest company plan to pay out \$2.24. But the Transocean chairman was forced off the board in favor of Icahn's nominee. At **Navistar**, Icahn and **Mark Rachesky** (in a move that a Jeffries & Co. analyst said “suggests they have concluded that the current management's plan may be an easier path to value”) settled their fight before the meeting – with Navistar agreeing to add three of the dissidents' candidates to the board. And at **Apple**, despite his wins on the proxy front, **David Einhorn's** campaign to return a lot more of Apple's low-yielding cash hoard to investors seems to have fizzled out – along with Apple's stock price too, we note with regret.

**And at Dell – where activists contend that the plan to go private at \$13.65 per share – led and largely funded by Michael Dell himself – will take significant shareholder value off the table and into the pockets of Dell and friends – the pot continues to boil:** Icahn continues his usual huffing and puffing – to borrow big money for a big shareholder dividend, then to somehow muddle through – significantly poorer and deeper in debt as a public company. And big Dell investor **Southeastern Asset Management** – which says Dell is worth almost \$24 a share, and which basically started the brouhaha – has taken half of its money off the table...in a sale to Icahn at \$13.35 a share – which is lower, please note, than Dell's offer, and a lot less than Southeastern paid to accumulate its stake !

*But in what we think is a huge new development on the “holding feet to fire” scene, Gary Lutin - the irrepressible factotum of the Shareholder Forum -*

**and a former investment banker - has formed The Dell Valuation Trust** - registered in Delaware - that will allow Dell shareholders who assign their interest to the trust to demand a valuation by the Delaware Court of Chancery – and meanwhile, in theory at least, (Lutin is still working on the details he says) to be able to monetize the appraisal rights themselves if they wish. Lutin's new trust won a rousing endorsement from New York Times columnist **Gretchen Morgenson** in a lengthy June 23 column. She cited two studies of appraisal results – one that showed a median appraisal in court decided cases that was 50.2% over the initial buyout price and another – of 46 cases since 1985 – where the court found a lower value in only seven cases and where the medium premium was a whopping 72%...which is not far off the value gap that's been cited for the Dell-sponsored deal. The Trust charges just a penny a share (with a \$100 minimum) to exchange Dell shares for Trust units. “*The analytical view of professional investors is fairly consistent*” Lutin noted...“*assuming appraisal rights are marketable, processing a demand essentially reserves a no risk option. Most investors look at this the same way Michael Dell does, and reach the same conclusion. They want the long term value of the company, not the short term value of the stock price.*”

**Meanwhile, even as we write, fresh new fires are being lit and directors' feet are being dragged into them... almost every week it seems:** **Starboard** just dropped its consent solicitation at **Office Depot** – and while it does not oppose the pending merger with **OfficeMax**, they now seek to add four new candidates to the new board, saying it needs to be “significantly enhanced.” **Starboard**, which replaced the entire six-member board slate at **Tessera Technologies** in May, also fired off a letter to **Smithfield Foods**, asking them to explore a breakup, rather than the planned sale to China's **Shuanghui International Holdings** - which they believe will create greater shareholder value than the current all-cash offer.

**Stay tuned for lots more action here...and for many more instances of “holding directors' feet to the fire” over their stewardship of shareholder-owned assets – or the perceived lack thereof...we guarantee.**

P.S. Our original article, “What's The Next Big Thing in Corporate Governance” – which was in our 2nd Q 2011 edition – is still much worth reviewing, we think.

Go to: [www.optimizeronline.com/files/NextBigThingCorpGovernance.pdf](http://www.optimizeronline.com/files/NextBigThingCorpGovernance.pdf)

## **ON A RELATED NOTE...THE COUNCIL OF INSTITUTIONAL INVESTORS HAS PETITIONED THE NYSE AND NASDAQ TO DISALLOW THE REAPPOINTMENT OF DIRECTORS WHO FAIL TO ACHIEVE A MAJORITY**

*Ya'know, we actually think the CII proposal to make majority election of directors a listing requirement is not such a bad idea...although the marketplace seems to be very rapidly ditching plurality voting just fine on its own.*

*But the Council's proposal to absolutely prohibit boards from reappointing directors who do not achieve the ISS "magic number" – or declining to accept their resignations, as most majority-voting companies allow the board to do, after due consideration – and characterizing reappointed folks as "Zombie Directors" and the "Walking Dead" – is just not crude, it's just plain wrong – as are the statistics the Council cites to back up their idea:*

According to their press release, "CII scrutinized ISS's data base and found that in the three-year period from 2010-2012, 74 percent of the uncontested directors who did not win majority support continued to occupy their board seats as of June 14, 2013.

But what CII is not telling us is how many failed to get a majority simply because they failed to attend 70% of the board meetings in the prior year year - which is, by far, the largest cause of votes-no...and which may not be a true "hanging offense" at all on closer scrutiny.

They also fail to tell us what percentage of the votes-no were due to increasing and increasingly inflexible policies on the part of institutional investors – many of which will make no exceptions at all; period – regardless of what the circumstances actually were.

And, Hello, CII...these statistics tell us – as we also reported here before, a few years back – that except for a very few cases where the losers struck out a second time, *the overwhelming majority of the directors in the study were actually re-elected by shareholders in the subsequent year - and usually, very handily so, when the "attendance problem" did not recur.*

Yes, one can probably find a very few egregious cases where directors resignations were refused that might not stand up to careful scrutiny... if one looks hard enough. But good directors are hard to find, as the CII is usually the first to point out. And neither the CII - nor any other person or group without regular access to the board room, we'd note - can possibly have a clue as to which ones are good, bad, indifferent or maybe great.

**Most important to note, the assertion that boards are merely "rubber stamping" return tickets, without scrutinizing the contributions that the individuals in question actually make, simply does not pass a sniff test...**given the risk of making those directors – and the entire board, for that matter – the subject of bigger and angrier and higher-profile vote-no campaigns the next year if there is evidence that they really DO stink!

**Let's let the marketplace continue to do its work here, we say – and let's let directors continue to do *their* proper work too.**

## **THE CRAZIEST DEVELOPMENT OF THE SPRING MEETING SEASON WAS – NO DOUBT – THE FLAP OVER 'SNEAK PEEKS' AT EARLY VOTING RESULTS: A TEMPEST IN A TEAPOT... AT A MAD HATTER'S GARDEN PARTY, WE THOUGHT...AT FIRST**

*What kind of crazies are flying out of what really seems like a cuckoo's nest at The Council of Institutional Investors these days, we asked, when we first saw and heard the demands for continued "sneak peeks" into voting information surrounding the race to strip Jamie Dimon of his Chairmanship at JPMC...and the CII demands for immediate SEC intervention.*

**Our fist question was; "Who knew??"...** We had never seen or heard of such a practice. And it sure sounded as if JPMC was surprised to discover that the shareholder proponents – and maybe anyone else who sent a letter to selected shareholders using the Broadridge distribution

systems – were getting 'sneak peeks' into the early voting returns. This sure came as a surprise to most everyone else we spoke with, although a few proxy solicitors who work mainly for activists knew too, but weren't telling.

**Our second question – putting aside the *propriety* of sneak peeks for a second – was... “What would someone expect to *learn* from a sneak peek?”...**

Unless, like JPMC, one had daily results on the very same proposal from the prior year, the statistics would have no value at all to a proponent. And even here, the idea that this year would be just like last year was not a reasonable assumption to make – as the final numbers confirmed – and especially when such a large percentage of the deciding votes were missing, and would not be cast until the evening before the meeting!

**So then we asked; “How could a shareholder proponent – or the management, for that matter - gain or lose an “advantage” here?”** Early-on, either side might decide to make extra mailings – as several articles speculated – or maybe launch more phone calls, and make personalized appeals – as both sides seemed to be doing anyway...But guess what? Most of the not-yet-voting folks had almost certainly made up their minds before the “flap” hit the fan. And heavily lobbying such folks in the eleventh hour has, historically, had a way of ticking them off – and if anything, further hardening their hearts and minds....If you are an issuer calling, that is.

**And didn’t the whiners already know who was voting with them?** You bet they did! While they mostly refuse to tip their hands to the management team, you can bet your life that activist investors had been networking like crazy, and already knew exactly how most of their compatriots were going to vote. And how many shares they had to vote. So if anyone had an advantage here, with or without sneak peeks, it was the activist community.

And aren’t the very same CII-member-whiners the very same people who “embargo” their votes – and who usually don’t vote until the night before the meeting??? And who, as noted, already know exactly how their CII buddies plan to vote??? Yes indeed...So again, “advantage activists!”...Which begs yet another question...

**How does the big set of advantages that activist investors get from zealously guarding their own actual and planned voting activities comport with their calls for more “openness”...and “transparency” where voting activities are concerned? Are these cries really meant to cover issuers only?**

**The most important question to be asking here - and which seems to us to be the heart of the matter - is “Whose ‘solicitation’ IS it, really?”**... It is the issuer who is officially “soliciting proxies” – NOT the folks whose proposals are enjoying a free ride on the issuers’ materials, we say.

As it turned out, JPMC decided to let proponent AFSCME and friends continue to peek at the voting results. We think it’s because (1) they knew they did not provide an advantage in the end-game, either way...and (2) failing to cave may have cost them votes in the then current “crazy” environment.

And Broadridge has stopped providing info – unless the issuer specifically authorizes it, which is as it should be.

***As to the activists, they’d be wise to cease and desist – and to realize that appeals to the SEC hold perils for them, and the current advantages they enjoy as “exempt solicitors”.***

## **THE SANEST DEVELOPMENT OF THE SEASON WAS THE VOTE ON REPLACING JAMIE DIMON AS JPMORGAN CHASE’S CHAIRMAN**

And yes, once the *sane* people had a chance to mull this over, they realized that the vote really was a referendum on Jamie Dimon himself, rather than on something that would, like magic, instantly produce “better governance.”

And then, the dealin’ was done...and Jamie came up

with a surprisingly high “full-house” of votes against this ill-considered proposal, which, ironically, the CII expects its members to automatically “rubber stamp” in line with their one-size-fits-all recipe for “good governance.” See our Quote of the Quarter, below, for a nifty summation.

## QUOTE OF THE QUARTER

*“This isn’t about good governance; it’s about busybodies without a clue, trying to do the dumbest thing – slapping and shaming a superb CEO for utterly no practical reason.”*

“Media mogul” **Barry Diller**, as quoted by New York Times reporter **Andrew Ross Sorkin** in a May 8 story on the shareholder proposal to split the Chairman & CEO roles at **JPMorgan Chase**

## STOCK SPLITS: WITH SO MANY STOCKS AT OR NEAR RECORD LEVELS, WHY SO FEW IN RECENT YEARS?

*We mentioned in our last issue that we were overdue in covering stock splits – or, more precisely, the notable dearth of splits there’s been over the last few years – even while more and more seemingly split-worthy stocks are at or near record price levels...So here’s our promised update:*

On the day we began drafting this, June 18th to be exact, 41 of the S&P 500 stocks closed at \$70 or above - and that’s excluding the famously never-to-be-split Berkshire Hathaway shares. Another 13 of the 500 closed higher than \$60 that day.

So what’s the magic here? In our long market-watching and split-watching experience, \$35 is the “magic number” – the minimum stock price one would want to see after a two-for-one split – and hello...most stocks selling in the low 60s typically achieve that projected post-split number as soon as such a split is announced.

So why have we been seeing so few stock splits? The answer is a simple one, we think – a near total lack of attention to retail stock ownership on the part of “big companies” – and many smaller ones too.

Many such companies take refuge in the “simple math” – that in mathematical terms, nothing really changes with a split; one simply ends up with twice the number of shares at half the price, for the same dollar value as before. Others, like **Warren Buffett** in particular, point out that “serious investors” get it, and thus, don’t give a hoot about splits...and that a “high stock price” is decidedly not a “bad thing” at all – and maybe will even attract more of the most serious buyers. And, partly due to Buffett and partly to the **Amazons**, **Apples** and **Googles** of today, there is a certain cachet in having a really high stock price these days.

Also, as Buffett is always quick to point out, stock splits actually cost shareholders money, because most brokers - and DRP agents too – tend to tack on a per-share charge to their basic commission rates for buying and

selling. So investors get nicked on both ends. And yes, stock splits cost the issuer “more money” too – though, unlike the old days, when new stock certificates needed to be purchased, and issued, hand-signed and hand-legended - then enclosed, insured and mailed with a little explanatory note – most splits are effected via “book-entry” these days, so cost is not the big factor it used to be – when splits, oddly enough, were a lot more common.

But let’s go back now to that “Magic number” – and ask what exactly makes it so “magical” that stock splits, in our book, make such a great amount of sense – and such a great deal, most times, for investors:

First, most market watchers will say that \$35 is as close to a retail investor’s “ideal price point” for buying in – or for buying more – as one can get: If you want to attract more retail investors – or if you simply don’t want to see retail investors buy **Coke** over **Pepsi**, or **Colgate** over **P&G** let’s say - this is the number to focus on.

Second, and far more important to note, there are a host of factors other than the “pure math” that affect one’s buying decisions – whether one is an ordinary retail investor or a professional – that do indeed affect the longer-term stock price. Just look at the 5-10% “kicker” that the mere announcement of a stock split tends to kick off, for starters: A stock split sends a very bullish signal that management – and the directors – expect the stock to go higher, going forward, as the vast majority of post-split stocks DO.

Most managers also know that a stock that sells at - or drops - below \$30 sends a BAD signal to the marketplace.

So they are likely to be doubly cautious – and mighty certain about maintaining and ideally increasing the dividends too - before authorizing a split...and investors know it.

Now back to that “magic” \$35 number and what makes it so magical: It’s mostly, but not entirely due to “investor psychology” rather than to the pure rationality of the pure math: Yes, average investors DO understand the bullish signals a stock split sends. And yes, average investors are wary – and rightly so, we think, of stocks that are, or that fall below \$30...as signaling “weakness.” But, investors simply *feel richer* owning 100 shares of a \$35 stock than when they own 50 shares of a \$70 stock. Given a choice between two stocks in similar industries – with similar outlooks and similar yields – investors will always favor buying the lower-priced one. So the added demand actually does give it a mathematical “edge” over higher-priced peers. And, let’s face it – it DOES seem to be a much easier hurdle, and a lot more likely – and a lot quicker to achieve too - for a \$35 stock

to go up 10% to \$38.50, or 20% to \$42 – than it is for a \$70 stock to go to \$77, much less than to \$84.

**There is some very strong empirical evidence to back our theory about stock splits producing superior returns to investors:** A mid-June WSJ column by **Mark Hulbert** cited an investment advisory service called “**2-for-1**” that buys only stocks that have split their shares – then holds them for 30 months. That portfolio, according to the **Hulbert Financial Digest**, has produced a 14% annualized return over the past ten years, vs. an 8% gain for the S&P 500 stock index, with dividends reinvested.

Even as we write this we seem to be seeing a sharp and much overdue correction in the number of stock splits: So far this year 25 companies have announced splits of 2-for-1 or larger splits - vs. only 12 in all of 2009 and only 13 last year – including **Coca-Cola** and **Colgate Palmolive**, that split after our initial heads-up - culminating most recently with high-priced **Google**, whose stock rose a nifty \$14+ on the date of the announcement.

## OUT OF OUR IN-BOX:

**Stock certificates destroyed by DTCC – or maybe by hurricane Sandy – create consternation – and potential financial losses:** In June, we got an email from a long-term industry friend, as follows: “I am a former director of [XYZ] Corporation, a company which went public in 1982 and then went ‘dark’ in 1987 i.e. got permission from the S.E.C. to discontinue reporting. It continued to trade sporadically but then eventually stopped due to lack of availability of information.

Years later...[an XYZ] shareholder was surprised to get a letter from his broker (**Fidelity**) telling him that **DTC** has an ongoing program of certificate destruction in those instances where it thinks the issuer is no longer in business. More recent checking seems to confirm that the certificate(s) were destroyed within the past year or two. The shareholder belatedly made efforts to get himself a replacement certificate but remains stuck in stock transfer purgatory with DTC and Fidelity each pointing to the other. The issuer has also been involved but insists, perhaps correctly, that it is a matter for DTC and Fidelity.

Meantime [XYZ] is still in business, almost thriving. Last time I checked...cash in bank was \$.12 per share and there were valuable leases of indeterminate value but

probably at least another \$.12 per share. I am wondering if someone like yourself can point me in the right direction. It is a vexing but ultimately solvable problem. I just need the right person to sort it all out. I already have tons of emails and notes on this so there is a decent documentary trail for the next person to pivot off from.

**Here’s how your editor responded:** “First, I’d have the holder write a very strongly worded letter to his broker - and to the broker’s branch manager at Fidelity - also cc-ing their chief compliance officer - making it clear that (1) Fidelity owes him a fiduciary duty, as the designated “custodian” for the subject shares, to properly safeguard his assets...and (2) it was Fidelity who appears to have designated DTCC as ITS sub-custodian - solely for its own convenience...and did so without the owner’s informed consent...and (3) had the holder known that Fidelity and DTCC were bent on destroying the certificate as “worthless” - he could easily have exercised his right to obtain an actual certificate had Fidelity properly informed him...but (4)...in any event, to demand a replacement certificate IMMEDIATELY - to be issued in the owner’s own name...at Fidelity’s own expense... (Maybe I’d cc the SEC whistleblower hotline too - since

this really IS a serious breach of duty in my opinion... or maybe just threaten to do so if satisfaction is not immediately forthcoming.) One could argue that Fidelity & DTCC had the right to do what they did, although I say NO, absent specific permission from the beneficial owner...But since they were clearly wrong in treating the certificate as worthless, the obligation to replace it is clearly THEIRS.....

P.S. It also strikes me that the certificate in question may have been lost in the hurricane Sandy flood (What was DTCC thinking to have a vault built on landfill, in what used to be part of NY harbor??? And then, despite being given 3-5 days warning that floodwaters would likely fill not just the underground vault, but the entire first floor, as they did, to NOT jackass the certificates to higher ground??? Also...the issuer is correct: Fidelity and or DTCC need to fix the problem - and need to properly indemnify the issuer and its TA against issuing “duplicate certificates” - just in case the originals should somehow wash ashore later, and into the stream of commerce.

*And a P.P.S. for Fidelity and DTCC: We don't know how much value is involved here, but you can almost certainly get a Bond of Indemnity for about 1% of it and maybe less - since the shares are restricted from trading “on their face”...AND, you should move quickly to cut your losses, we'd advise. But also...say the stock rises big...then falls fast: You folks are then exposed to a lawsuit for the lost opportunity the owner had to sell before the selloff - but could not, because you diddled around.*

This prompted us to follow up on a related matter - avowed new efforts by DTCC to do away with stock

certificates altogether, in the wake of hurricane Sandy:

**But hey! Didn't DTCC try to push this twice before? Whatever happened to “Networking for Equities”... and the “Knife System” that were supposed to take the place of legended stock certificates???** Until we have a totally trustworthy and basically universal “system” in place - that will promptly and reliably place unwary stock buyers and sellers “on notice” that certain specified terms need to be met before a legal transfer of ownership can be made - we still need stock certificates to carry those “legends” on unregistered or otherwise “restricted stocks.”

**“So how are those DTCC systems workin' out for ya?” we figured we'd ask...And who better to ask than STA President Charlie Rossi:** Turns out that Networking for Equities (NFE) and the “Knife” system (NFE- get it??) are one and the same old time systems, that were designed to move mutual fund holdings between brokers when clients picked new ones. And yes, DTCC has a new committee to maybe sharpen this rusty and un-sharp “knife.” But it sure seemed to both of us that issuing the few legended certificates that are needed each year (usually at IPO time) to reliably warn buyers and sellers - and transfer agents and depositories too - that they need to check with special care before transferring them - will likely prove to be a lot more reliable - and a lot cheaper too than an expensively redesigned but still dull and very hard to peddle knife! How does anyone figure they'd sign up the hundreds and hundreds of little TAs - in places like Reno, Salt Lake City and Vegas - who handle hundreds of little issuers - where legended certificates tend to be the most commonly issued of all???

## ELSEWHERE ON THE SUPPLIER SCENE:

**THE “BIG SHOE” PREDICTED IN OUR LAST ISSUE FINALLY DROPS ON THE TA WORLD...**In our last issue we cited the “talk on the street” that one of the most widely held stocks anywhere was going to give up its in-house shareholder recordkeeping and servicing infrastructure and move the market-share landscape in a big way. Well, the cat is finally out of the bag: **The Walt Disney Company** - with over 1.3 million registered shareholders - is outsourcing its biz...and the winner is...**Broadridge Financial Solutions**. Transfer agent salespeople who have been telling clients and prospects that Broadridge is too new, too small, or otherwise “not ready for prime time” will need to scramble now - and, as we've been reminding, market share - and marketing momentum - are very big factors these days when choosing *any* vendor....Speaking of which...

**ANOTHER BOMBHELL LANDS IN PROXYLAND:** FactSet Research announced that as of February



2013 its SharkRepellant unit, [www.sharkrepellent.net](http://www.sharkrepellent.net) will make proxy solicitor fees and estimated proxy fight costs available “for definitive proxy fights (fights where the dissident filed definitive proxy statements).”

Starting off with a bang, their study of the 12 largest proxy solicitor fees ever – covering 2006 – 2012 – revealed that **MacKenzie Partners** was involved in eight of them (!) with **Innisfree** logging two – and **D.F. King** and **Morrow & Co.** logging one each. In two of the MacKenzie mandates, **Georgeson** and **Okapi Partners** shared in the fee, although the actual splits were not disclosed.

We are hoping, of course, that FactSet will start tracking and reporting on ALL proxy solicitation fees and expenses – which are all publicly disclosed in 10-K filings, and easy enough for FactSet to collect – and which will reveal a slightly different picture: D.F. King and Georgeson, for example, still derive very significant “annuity revenues” from plain vanilla proxy solicitation efforts – albeit where price competition has been heating up and where margins are thinner – but where MacKenzie & Innisfree are still relatively small players. But ouch! Publishing this data would be a bad thing for most solicitors, since it would intensify the price competition even more.

These days, however, as we’ve noted here before, the real money is in the “advisory business” – a lot of which is not disclosed as “proxy solicitation expense” at all – and which has really been mounting up from companies that merely feel uneasy, or threatened by a potential proxy fight – or are looking to stay way ahead of the curve and off the radar screens here – and/or looking to avoid “says NO on pay” or on directors - or votes YES on shareholder proposals. And where this high margin/high value-added business is concerned, we’d bet a ton that the lion’s share of that money is flowing to the top-two or three “big-fight firms” as well – very much in line with their share of actual fight-fees.

**ABANDONED PROPERTY CONTINUES TO DRAW MORE ATTENTION – and a lot of corporate ire – as Delaware steps up its attempts to take in \$566.5 million from this source in 2013 – up an astonishing 19% vs. 2012.** Reportedly, 310 companies took advantage of Delaware’s “Voluntary Disclosure Program” by mid June, which promises “look backs” only to 1996 instead of to 1981 - an “amnesty” that ended – for good they say – on June 30. But what ever makes Delaware think they have the right to go back so far?? Even the IRS looks back no further than three years – unless there’s real evidence of fraud...and even then, the statute of limitations for bringing actions legally, last time we looked, is seven years at most – not 32 years! “*No records back to 1981 anymore? Well, here’s our estimate of what you owe, so pay up*” say the hired auditors. Sounds more like an extortion racket than the strong governance and judicial systems that Delaware wants to be famous for, we’d say.

**But good news...While the Council on State Taxation – whose directors come from companies like Coca-Cola, General Electric and Johnson & Johnson – and who have been quietly wringing their hands and tut-tutting about this outrage from the sidelines – Select Medical Corp. – and three cheers for them – sued Delaware in US District Court this April, alleging that their program “violates federal common law and the U.S. and Delaware Constitutions.”**

**AND OUCH! A “FINDER” OF “LOST ASSETS” FINDS THEMSELVES FINGERED IN A HALF-PAGE NEW YORK TIMES ARTICLE:** We decided not to name them here, since they are a very good firm – with very good people on the whole – and, as the Times article noted – they have an A-plus rating from the Better Business Bureau...So Google it up yourselves if you’re really curious... But oh...Woe... An over-eager beaver took advantage of a loophole in Ohio law that limits a finders’ “take” to 10% of the value - but only after property is turned over to the state (and please note, many other states have similar caps... and similar loopholes) – and sought - and obtained - an agreement from an heir to pay 36% . Then, when the heir insisted he knew about the shares, and exactly where they were all along, they foolishly failed to negotiate an amicable settlement ...until the *Times* stepped in, that is...

This loophole was a new wrinkle to us – thus one we'd never commented on in our many articles on Best Practices for handling abandoned property. So readers, and finders, and transfer agents, and issuers please take note: Using this loophole to evade the clear intent of a state law – to limit a finders' "take" to a "reasonable amount" – does not really stand up under the light of day – much less in a national newspaper article. We'd also add that this is the first time in your editor's many years of involvement with "finders" that a fingered-finder did NOT promptly reach an amicable agreement on his or her own...so a bit of an outlier here, we'd say.

But it does prompt us to remind readers yet again that it is the corporate issuer who will ultimately be considered accountable for the treatment of shareholders' property – lost or otherwise - and properly so. So please re-read the many tips on our website – particularly, on knowing exactly how many people, and how many dollars are considered to be "lost" before approving investor-paid "search programs" – and exactly what percentage, and how much money in total the finder will take, and/or split with a transfer agent – and whether such 'tying' and fee-splitting arrangements may lead to conflicts of interest...(and usually to higher fees too in our experience)...Last but far from least, DO be sure that you have a good understanding with your vendor of choice about handling any disputes over money that may arise - with fairness, diplomacy, "reasonableness"... and good press relations in mind.

## PEOPLE:

**Scott Gallagher**, formerly with **Georgeson**, then **Keane** – and **Ken Staab**, a former superstar at **AST** - have signed on as a Senior VPs with a new company, **Brownstone Recovery Group**. Brownstone, founded in January of this year, with **Yehuda Neuberger**, a former President of transfer agent **AST** as its president, was formed to assist claimants in the **Visa-Mastercard Class Action Settlement Fund**. A potential goldmine here, we think, since only a very small percentage of claimants in Class Actions – and only the most sophisticated ones – have the time and patience to follow through, and file all the paperwork that's necessary to claim what's due them on their own.

**Keith Higgins** has been named the new Director at the SEC's all-important **Corp Fin Division**. Expert SEC-watcher **Broc Romanek** calls him "The mighty Ken Higgins" for his "wealth of knowledge...and entertaining personality." Always a favorite at Broc's proxy disclosure conference, he noted. Also, **Lola Nallengara** – where Broc noted that "it's great to have someone with a disclosure and deal background" on the job – has been named the SEC's **Chief of Staff**.

**SIFMA**, the **Securities Industry and Financial Markets Association**, has a new CEO – **Judd A. Gregg**, a former three-term Republican senator from New Hampshire, who, the **WSJ** commented, "will become the face of Wall Street's effort to soften financial regulation."

**Cary Klafter**, the VP-Legal & Corporate Affairs and Corporate Secretary at **Intel**, will receive the **Bracebridge H. Young Distinguished Service Award** at the **Society of Corporate Secretaries and Governance Professionals** annual conference in July. Awarded to recognize "persons who have rendered unusual or exceptional service, or consistently rendered service over a period of years, that directly furthers the Society's goals in a significant manner, it is the Society's highest honor." One could hardly imagine a more deserving recipient: Cary has served on and chaired numerous Society committees over many, many years, and as a Director (2001-2004). His work as Chair of the Society's Public Affairs Committee, where he worked on proxy mailing and solicitation, share lending and vote counting issues helped enormously to create awareness of their importance, as well as "a community between issuer members and vendor members...by helping all to recognize our common ground." Everyone who has worked with Cary remarks on his intellect, perceptiveness and understated wit – and notes his leadership as a thinker on governance and disclosure issues and on transparency and the way his role as an early adopter has made Intel a prominent standard setter on the governance scene.

**Steven Walsh** – a long-term and widely known figure at the **New York Stock Exchange** – who left to serve a stint at proxy distribution and voting agent **Mediant** – has returned to the NYSE as Director of Governance, Proxy and Advocacy. An important and most welcome addition to the NYSE's talent pool – and at a very important time, we'd note.

# Regulatory Notes ... And Comment

**ON THE HILL:** President Obama's nominations of Kara Stein to succeed SEC Commissioner Elisse Walter and Michael Piowar to fill the seat of Commissioner Troy Paredes are expected to breeze through the confirmation process, since both candidates served as staffers to senior Senators on the **Senate Banking Committee**....And wow, it would sure be a surprise to find much of anything to wrangle over with either of these very low-profile candidates. "Why, unusually, do you appoint two [staffers] when there are [sic] a much wider range of people with market experience and knowledge and exposure to the key global issues the commission may be facing?" groused former SEC General Counsel Edward Green, now at Cleary Gottlieb. Duuuuh! Any real mystery here?

**AT THE SEC:** Two big issues have been targeted as being the top top-priorities under tough-talking Chairman Mary Jo White...and we are hoping that Obama's warnings against "messing with Mary Jo" hold water: Accounting fraud...and admitting guilt in order to settle the most egregious of cases. Go get'em Mary Jo... who seems off to a good start:

Apropos, and at long last...after years and years of howls from affected companies, the SEC finally *finds* – and *finds* – naked short sellers – and several of their abettors too...with a judge ordering a Maryland broker to disgorge \$2.7 million in profits and to pay a \$2 million civil fine. The judge also ordered **optionsXpress, Inc.** – owned by **Charles Schwab** – to disgorge \$1.6 million in profits and pay a \$2 million civil fine for violating laws that prohibit naked short selling. He also fined its former CFO \$75,000 and barred him from the securities industry.

And double-yippee...immediately thereafter, the SEC fined the CBOE \$6 million – the first ever fine against an exchange for regulatory-oversight violations, noting, among other things, that the CBOE actually helped optionsXpress – one of its biggest customers – to craft its response to the SEC inquiry.

*And triple-yippee – another lawsuit on naked short selling is heading for the Courthouse as we write. But, planet earth to SEC... the barn door I still wide open here – mainly because existing rules – plus a few egregious exceptions to the rules – still allow short-sellers to be "naked" for a period of time before "covering." This at a time when less than a nanosecond is enough to*

*gain an edge, and where outmoded and outclassed SEC monitoring systems are totally blind to the size, scope and indeed, the very nature of "nakedness."*

*And an important P.S.: Naked short selling is one of the major causes of the "over-voting" scandal – which is also mostly invisible to SEC systems – and subject to sloppy and we think conflicted SRO oversight and overseers as well. After more than a decade of howling – from whipsawed companies that have often see quorums of 120% or more showing up as votes at their shareholder meetings – there are still no real rules, and no real procedures to prevent both borrowers and lenders from voting the very same shares! How 'bout it Mary Jo?? Maybe you can push THIS totally shameful mess toward the SEC's front burner?*

NASDAQ OMX got hit with a fine too this quarter – \$10 million – which seems like a tiny tap on the wrist, considering that investor losses are estimated at \$500 million – and the way the SEC's own co-director of enforcement, **George Canellos** described the case as telling "the tale of how poorly designed systems and hasty decision-making not only disrupted one of the largest IPOs in history, but produced serious and pervasive violations of fundamental rules governing our markets."

Speaking of SEC fines...which most financial industry participants currently treat as merely a "cost of doing business" and as a way to "move on" – as NASDAQ and other payers of fines and settlers of suits typically comment...we've been meaning to make a modest proposal of our own:

Repeat offenders should be subject to prohibitions on adding new business – for a period that would be in keeping with the seriousness of the violation AND with the instance of earlier violations.

Banks and Trust Companies – and brokers – and especially their "sharpest" and wiliest stars – and SROs and their "stars" too – would think twice and probably three times before violating rules if they knew their division could suffer a long-term new business hit – or maybe have its Charter revoked altogether for serious and/or repeated violations of the rules...as Japan, for example, threatened Citibank a while back.

And you can bet the ranch that the prospect of losing

one's charter to take on new customers for a while – or maybe losing a franchise altogether – would be a MAJOR incentive to tune up and police one's overall audit and control environment...and one's top dealmakers too...who'd also have major new incentives to self-police!

Your editor's one-time transfer agency business still has SEC regulations that would prohibit a TA from taking on new business – just for falling behind on the required turnaround times for processing paper! So why should so many other SEC regulated industries be so free to “pay a little tax” and “move on” after “serious and pervasive violations of our most fundamental rules governing the markets” ???

**AT the PCAOB:** Ernst & Young became the third of the Big Four audit firms where Peekaboo's “peeks” into actual audits revealed that auditors failed to remedy prior year deficiencies that Peekaboo uncovered... which, under SOX, requires public naming – and, one would think, a preventative shaming – of the firms that failed to address serious deficiencies in their audits of public companies. (Deloitte & Touche and PricewaterhouseCoopers were named and seemingly not shamed earlier, leaving KPMG as the only Big Four firm that has not been cited for failure to fix defects.) The latest report covered 2009 audits that were shared with E&Y in 2010 – after which they had a year to fix them... Then another year passed until “Peekie” could see if things were fixed. The huge delay here seems to us to be a big problem in itself: *Mary Jo – we'd respectfully suggest*

*that if you really want to focus on financial fraud, you need to focus a lot harder on the public accounting firms that audit potential financial-fraudsters...AND to strive for much faster and more aggressive remedial programs than what we have now...AND, we'd add, build in much bigger penalties for repeating bum audits than a mere “naming and [maybe] shaming.”*

**IN THE COURTHOUSE:** In its first case against auditors since the financial crisis, the SEC has asked an administrative law judge to bar a KPMG partner and a second KPMG senior manager who oversaw the audits at TierOne, a Nebraska-based bank, noting that “they merely rubber-stamped TierOne's collateral value estimates and ignored the red flags surrounding the bank's troubled real estate loans” – such as newer estimates of collateral that were much lower than the bank's earlier ones and a warning of “serious problems” from the Office of Thrift Supervision, the bank's primary regulator. *Let's hope this is a good sign from the SEC of more such cases to come.*

**And another footnote on the Abandoned Property front:** California's Controller, John Chiang, has been served with a class action suit filed by Sacramento attorney and abandoned property expert Bill Palmer, demanding that the Controller's office go back to each of the California citizens whose funds were seized and turned over to the state without their names being attached – because the amounts were less than \$50: Some \$68 million in all since 2007. A bill that was introduced to require the submission of owners' names, regardless of the amount, was recently amended to allow a \$25 minimum, in order to “not let the bill die” said its proponent, saying that it was “better than nothing”...Stay tuned here for more...

## “END OF ANNUAL SEASON CELEBRATION” - A SMASH HIT...

Well over 200 people, including many of the “leading lights” of the corporate and supplier communities turned out for the TENTH big bash to celebrate the end of the big spring season, which this year, honored Kathleen Shannon, the recently retired former Corporate Secretary and Deputy General Counsel of AIG, who has been a long-term supporter of the Benefit – and an avid and discerning collector of works by Fountain Gallery artists.

The event raised over \$130,000 to benefit Fountain Gallery – a unit of 65 year old Fountain House – the world's leading provider of rehabilitative services to people with serious mental illnesses.

[http://www.huffingtonpost.com/jim-luce/fountain-gallery-raises-f\\_b\\_3455059.html](http://www.huffingtonpost.com/jim-luce/fountain-gallery-raises-f_b_3455059.html)

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