Research & Advocacy Brief

Walden Asset Management ❋ Advancing sustainable business practices since 1975

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From the mouth of **General Electric**'s (GE) CEO Jeffrey Immelt came these astonishing words in a December 2009 speech at West Point Academy: "*Rewards became perverted. The richest people made the most mistakes with the least accountability... Ethically, leaders do share a common responsibility to narrow the gap between the weak and the strong.*"

Growing income and wealth inequality has long been a key concern of Walden clients. That the chief executive of a renowned corporation would challenge business leadership on this very issue is welcome recognition of the destructive social and economic consequences of the Wall Street−Main Street chasm. Certainly, a culture of corporate excess remains pervasive, as evidenced by near daily headlines reporting huge executive pay packages, including at firms bailed out by the U.S. government. Still, there is forward momentum toward greater corporate accountability on executive compensation.

Say-on-Pay Victories Continue

Walden's leadership calling for the adoption of a shareholder advisory vote to ratify the compensation of executive officers, known as Say-on-Pay, continues to yield meaningful progress. Our advisory vote resolution garnered 46 percent support at **Procter & Gamble**'s October 2009 annual meeting, demonstrating broad-based investor agreement about the need for greater accountability. A Say-on-Pay resolution at **Goldman Sachs** (previously led by Walden and this year by the retirement system of the State of Connecticut) was withdrawn upon its commitment to implement the advisory vote at its 2010 annual meeting. As a major Wall Street firm that recently shed its TARP (Troubled Asset Relief Program) status, therefore ending its obligation to provide Say-on-Pay, Goldman Sachs' response is a significant precedent.

Ironically, our most significant recent achievement with respect to Say-on-Pay was prevailing over GE – the very same company whose CEO we extolled above – in its attempt to convince the U.S. Securities and Exchange Commission (SEC) to omit an advisory vote resolution, claiming primarily that the proposal is vague and misleading. The SEC agreed with Walden's argument to let the resolution stand, marking a dramatic reversal from 2009 when the agency allowed companies to omit the same resolution. GE's efforts are a reminder that words do not necessarily translate into action. But the new SEC position, which applies to numerous companies that were following GE's lead, is evidence of a more supportive regulatory environment for shareholders' rights.

Other Corporate Governance

Walden's ongoing focus on corporate environmental, social and governance (ESG) disclosure is also producing results, including among smaller companies where we have placed increasing emphasis. Three ESG reporting resolutions for 2010 annual meetings have been withdrawn to date with negotiated agreements to initiate or expand such disclosure – **Baldor Electric**, **Credo Petroleum** and **Time Warner Cable**. Additionally, similar dialogues are progressing with numerous companies, including **Carbo Ceramics**, **DENTSPLY**, **Genessee & Wyoming**, **Minerals Technologies**, **Stryker** and **TJX**. On the cutting edge of ESG reporting, **Timberland** produces web-based, quarterly reports, and solicits continuous virtual feedback from stakeholders.

Walden and other investors criticized a different "cutting edge" development at **Intel**, its decision, subsequently reversed, to move to a virtual-only shareholder meeting format in 2010. Notwithstanding the positive aspects of e-meetings – decreased costs, increased access, and environmental benefits – we argued that the lack of a physical meeting reduces director and manager accountability to shareholders. While Intel is generally responsive to stakeholder concerns, other companies following Intel's original plan could use virtual meetings to insulate themselves from shareholders. Hence, we made the case for simultaneously maintaining an in-person capability (even if without frills). In the first week of 2010, Intel shared with us its decision to do just that.

We wrote to approximately three dozen portfolio companies encouraging a phased-in separation of the roles of CEO and Board Chair. Generally considered a best practice by corporate governance experts, a separate and fully independent Board Chair helps minimize perceived or real conflicts of interest in management oversight while freeing up valuable CEO time. Although few are embracing this reform, more than 80 percent responded, including **Staples**, whose representatives met with us at

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Walden. We are also leading a shareholder resolution on separating the CEO and Chair roles at **State Street**, the first on this issue for Walden. In response to pressure from other activist shareholders, **Whole Foods** CEO John Mackey volunteered to relinquish his role as Chair.

A Walden resolution asking **Watts Water Technologies** to take steps to increase board diversity was withdrawn after constructive conversations with representatives of management, including the CEO and the board. Currently without women or people of color among its directors, Watts Water amended its Corporate Governance Guidelines and Nominating and Corporate Governance Committee Charter to include statements promoting diversity in board membership. We believe the company is serious about expanding its candidate pool in future recruitment initiatives. Concurrently, the SEC responded favorably to investor input, including Walden's, advocating for better disclosure on board composition. The new rule, effective in February 2010, "require[s] disclosure of whether, and if so how, a nominating committee (of the board) has a policy with regard to consideration of diversity in indentifying nominees for director…how this policy is implemented, as well as how the nominating committee (of the board) assesses the effectiveness of its policy."

Workplace Policies and Practices

Walden also continues to achieve results on initiatives addressing equal employment opportunity (EEO) and labor standards. **Commercial Metals** amended its non-discrimination policy to include sexual orientation and gender identity, after several years of engagement and strong shareholder support for resolutions led by Walden and Pride Foundation. After our inquiry, **Neogen** posted its inclusive policy to its corporate website. In November **United Natural Foods** developed its first Code of Conduct for suppliers, seeking compliance with internationally recognized labor standards. Walden plans to continue to press for improvements in the Code, particularly adding the right to free association.

But the news is not all positive. In October, after a six month review, the Occupational Safety and Health Administration (OSHA) announced a record high $87.4 million fine against **BP** for failing to adequately address the hazardous work environment that led to the fatal 2005 explosion at its Texas refinery (prompting the second highest penalty in OSHA's history). BP announced it will challenge the fine before the OSHA Review Commission, claiming it has demonstrated substantial improvement. Despite industry leadership on public policy addressing climate change, as well as significant commitments to alternative energy, Walden is extremely concerned by the apparent continuation of a subpar safety culture at the company. We are currently reevaluating our position in BP.

Impacts on Communities and the Natural Environment

Working with CANICCOR, an expert consultancy on corporate responsibility in the financial services industry, Walden is discussing with **SunTrust** and **J.P. Morgan** their process and progress on mortgage loan modifications to help homeowners avoid foreclosure. The industry as a whole has been slow to implement its own or government sponsored programs, but J.P. Morgan appears to be making progress comparatively. On the global community front, a resolution introduced in November 2009 asked **Cisco Systems** to assess how it can avoid complicity in violations of human rights associated with internet use in countries, such as China, with poor records. Over one third of votes cast supported the resolution led by Boston Common Asset Management and co-filed by Walden.

In response to obstructionist lobbying by the U.S. Chamber of Commerce against proposed climate change legislation, Walden helped organize a letter with over 40 investor signatories to fourteen member companies on record as supportive of legislation. The letter asked them to evaluate their continued alliance to the association in light of several highly publicized company departures and public statements asserting the views of the Chamber on climate risk do not represent their own. As an example, prior to our joint letter, **Nike** resigned from the Chamber's Board to express its disappointment.

More Positive Developments at the SEC

In our October 2009 *Research & Advocacy Brief* we highlighted our attendance at a small gathering called by the SEC's Corporation Finance division to discuss its role in allowing companies to omit shareholder resolutions that address risk (e.g. risks posed by climate change). The SEC recently reversed its previous policy and shareholders can now request explicitly that companies assess financial risks posed by material ESG factors.

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