



# NORTH DAKOTA CORPORATE GOVERNANCE COUNCIL

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**Response  
of  
The North Dakota Corporate Governance Council  
to  
The Testimony of the North Dakota Chamber of Commerce on HB 1340**

The president of Integrity Mutual Funds claims that Chapter 10-35:

- “is a political tool which would allow corporate raiders to more easily take over North Dakota publicly-traded companies”
- “strips away all forms of protection that a company currently (and legally) has to protect itself from unscrupulous raiders”

In fact, however, the purpose of Chapter 10-35 is to address the concerns of institutional investors. Chapter 10-35 is not designed to help corporate raiders and actually contains provisions that are problems for corporate raiders:

- Sections 10-35-22 through 10-35-25 specifically permit the board of directors to adopt a poison pill without shareholder approval. Corporate raiders want no poison pills at all.
- Section 10-35-26 permits the shareholders of a company to adopt antitakeover provisions in the articles of incorporation. Corporate raiders want no antitakeover provision at all.

The overreaction of the North Dakota Chamber of Commerce to House Bill 1340 is symptomatic of the disregard of corporate managements for the owners of their companies. Management should be careful stewards of the investment of the owners – but too often management forgets that trust and resents any suggestion that they should be more accountable for the results of their stewardship.

The testimony of the Chamber suggests that no one will support reincorporating to North Dakota. That is simply not the case. The Proxy Voting Guidelines of the Florida State Board of Administration (the “Florida Guidelines”), for example, state that the Florida Board “supports proposals that require the company to reincorporate to a state that is more shareholder friendly.”

The lack of relevance of the major provisions of Chapter 10-35 to corporate raiders is outlined briefly below:

**Majority voting in election of directors (§ 10-35-09).** This section permits shareholders to vote either “for” or “against” each director nominee, and requires that a nominee

receive a majority of “for” votes to be elected.

- Majority voting only applies in an uncontested election of directors – when only management’s slate is up for election and no change of control is threatened. So this provision is irrelevant to corporate raiders.

**Advisory shareholder votes on compensation reports (§ 10-35-12(5)).** This section permits shareholders to cast an advisory vote each year on a report regarding the compensation of the company’s executives.

- The required vote is expressly stated to be “advisory.”
- Executive compensation has never been an issue in takeover attempts.

**Proxy access (§ 10-35-08).** This section gives a shareholder that has owned 5% of a company’s shares for at least two years the right to have director nominees included in the company’s proxy statement.

- Since the 5% shareholders who are given this right must have held their share for at least two years, they are by definition not short-term corporate raiders.
- The Florida Guidelines support proxy access.

**Reimbursement for successful proxy contests (§ 10-35-10).** This section requires a shareholder who wages a proxy contest to be reimbursed for the costs of the contest to the extent the shareholder is successful.

- The cost of running a proxy contest has never deterred a corporate raider from mounting a challenge to management, so this section will have no effect on the number of proxy contests by corporate raiders.

**Separation of roles of Chair and CEO (§ 10-35-06(4)).** This section requires the positions of chair of the board and CEO to be held by different people.

- This is considered a “best practice” and many companies have already voluntarily adopted this restriction.
- Separating these positions has never been an issue in takeover attempts.

**Shareholder approval of issuances of more than 20% of outstanding shares (§ 10-35-17).** This section requires that issuances of 20% or more of a company’s shares must be approved by the shareholders.

- This is already required by the rules of the NYSE for every listed company.

**Supermajority provisions prohibited (§ 10-35-12).** This section prohibits the vote for shareholders to take action from being raised above a majority.

- TIAA-CREF says in its Policy Statement on Corporate Governance that “shareholders should have the right to approve matters submitted for their consideration with a simple majority of the shares voted.”
- The Florida Guidelines similarly state that “we think shareholder desires should be carried out with a majority vote of the disinterested shares.”

**Elimination of classified boards (§ 10-35-06).** This section prohibits a company from classifying its board into three classes so that only one-third of the directors are elected each

year, and requires instead that the entire board of directors be elected each year.

- Companies have been proposing the elimination of classified boards at an increasing rate, and over half of the S&P 500 companies now do not have classified boards.
- The Florida Guidelines provide that the Florida SBA “opposes classified boards and their provisions because we believe that annual accountability will ultimately lead to increased corporate performance.”

**Responses of the North Dakota Corporate Governance Council  
to  
the Comments of Gordon Dihle**

Following is the text of Mr. Dihle's comments, as attached to the testimony of Dave MacIver before the Senate Judiciary Committee, with the responses of the North Dakota Corporate Governance Council shown in **[bold face and underlined]**:

I read the proposed provisions of Engrossed House Bill NO. 1340, proposed as the "North Dakota Publicly Traded Corporations Act" NDCC 10-35 with horror. **[That overblown bit of rhetoric is symptomatic of Mr. Dihle's lack of thoughtful consideration of the substance of HB 1340. There is a lot of heat – but no light – in his comments.]** The provisions of this bill are such that no competent attorney would ever allow a public company to incorporate in North Dakota. **[To the contrary, the provisions of Chapter 10-35 represent the best thinking of corporate governance experts, including the Reporter for the ALI Principles of Corporate Governance, and are endorsed by major institutional investors.]** The board of director provisions, the "poison pill" restrictions and the outlandish franchise fees are simply senseless. **[These items are the opposite of "senseless." The board of director provisions are all proposals that are part of the mainstream debate on corporate governance issues. The poison pill provisions take a responsible position designed to permit companies to protect themselves from abusive takeovers without improperly entrenching management. Instead of being outlandish, the franchise fees are one-half what Delaware charges.]** *{Comments complaining about federal law omitted as irrelevant.}* Every public corporation I am involved with or know of has more than 13,333,333 authorized shares and would therefore be subject to the maximum \$80,000 franchise fee. Compared to similar fees of approximately \$500 a year in most other states, this alone would deter any company from incorporating in North Dakota. **[As noted in the previous response, the franchise fees are one-half what companies pay readily and without any complaint each year in Delaware. The experience of Delaware proves that the franchise fees will be irrelevant to a decision whether to incorporate under Chapter 10-35.]** The other provisions are cumbersome and restrict logical and efficient corporate governance which are necessary to operate a profitable entity. **[To the contrary, studies demonstrate that improved corporate governance correlates directly with improved performance. One summary of the research on this subject concludes "simply put, good corporate governance does, in fact, pay."]** The proposed provisions also invite predatory litigation. **[Again, to the contrary, the legislation should result in less litigation because shareholders will not have to resort to the courts to enforce their rights. The rights given to shareholders in HB 1340 will give them the ability to protect their investment in a corporation without the inefficient and cumbersome need for litigation that is their only resort in other states.]**

The only result I can see from this bill is the harassment and ultimate destruction of the few public corporations which are incorporated in North Dakota by predatory attorneys and professional plaintiffs from outside of the state of North Dakota. This certainly does nothing but harm the citizens of North Dakota, particularly those employed by the public companies or doing business with those public companies. **[We disagree generally with the view that Chapter 10-**

**35 will lead to harassment of public companies subject to it. But, more importantly, the foregoing statements are simply wrong. The existing public corporations incorporated in North Dakota are completely exempt from Chapter 10-35.]** The only result I can envision from this patently anti-business bill is Corporate America fleeing from the state of North Dakota together with what few non-agricultural or mining jobs remain there. **[As noted above, improved corporate governance improves profitability. That is the opposite of anti-business. HB 1340 will be good for American business – and thus good for all of us because we all have part of our future security tied to the continued success of the American economy.]**

**Responses of the North Dakota Corporate Governance Council  
to  
the Comments of Mark Anderson**

Following is the text of Mr. Anderson's comments, as attached to the testimony of Dave MacIver before the Senate Judiciary Committee, with the responses of the North Dakota Corporate Governance Council in **bold face and underlined** following each of Mr. Anderson's numbered paragraphs:

1. This bill does not protect Mom and Pop on Main Street. Rather, it is a political tool which would allow corporate raiders to more easily take over North Dakota publicly-traded companies. This bill will not be utilized by the general public.

**[If the bill were a tool to take over North Dakota publicly-traded companies, as alleged, the bill would prohibit poison pills and the adoption of antitakeover provisions in a company's articles of incorporation. In fact, the bill permits both poison pills and antitakeover provisions.]**

**[One of the most important purposes of the bill is to protect the savings of Mom and Pop on Main Street. Most small investors today have their investments in mutual funds. The retired government employees and school teachers of North Dakota and other states are looking to state pension funds for their retirement. Those mutual funds and pension funds are managed by institutional investors, and those investors strongly support the provisions of Chapter 10-35.]**

2. The definition of "poison pill" includes everything, including the kitchen sink. It strips away all forms of protection that a company currently (and legally) has to protect itself from unscrupulous raiders. One year terms, no staggering, independent director, stock issuance...it is all in there and, cumulatively, it is all bad.

**[As noted above, the bill does not strip away poison pills and antitakeover protections. The bill allows companies to protect themselves from unscrupulous raiders, but it does so in a way that keeps management accountable to the shareholders and focused on improving the performance of the business.]**

3. If anyone in state government is waiting for the franchise fees to start rolling in, they should think again. Two of our corporate attorneys have said that we should immediately begin the process of reincorporating in another state, should this law pass. Not only will they never see another firm organized under this statute, any that might be on the books right now will be gone. Looking at our annual filing fee go from \$25 per year to \$80,000 per year speaks for itself. No firm would willingly agree to that.

**[Mr. Anderson's company will be exempt from Chapter 10-35. There is no reason for it to reincorporate in another state. It will not even have the ability to become subject to Chapter 10-35. Corporations incorporated under North Dakota law after**

**July 1, 2007 will have the choice of becoming subject to Chapter 10-35, but corporations incorporated before that date will not be able to elect into Chapter 10-35. The advice given by its lawyers is inconsistent with the clear provisions of the bill.]**

**[The franchise fee is set at one-half the Delaware corporate franchise tax. Half of the publicly traded corporations in the country are incorporated in Delaware. They pay twice the fee North Dakota will charge with no complaint.]**

4. This bill will effectively kill capital formation in the State of North Dakota. There are already too few publicly-traded companies being organized here. This will be the death knell for capital formation in the future.

**[There is no relationship between the bill and capital formation in North Dakota. At the moment, there are no publicly-traded companies being incorporated in North Dakota. Any companies that come to North Dakota as a result of HB 1340 will be more companies than are coming now.]**