

SEC to Propose Rule Amendments to Facilitate Rights of Shareholders to Nominate Directors

May 29, 2009

The Securities and Exchange Commission (SEC) voted on May 20 to propose rule amendments to facilitate the rights of shareholders to nominate directors of corporate boards. The following summarizes the proposed rules based on statements made at the SEC's open meeting and in its press release. Publication of the text of the proposed rules is expected in the near future.

New Rule 14a-11 will allow certain shareholders to include a nominee or nominees for director in the company's proxy materials.

Under the proposed rule, shareholders would be able to include their nominees for director in the company's proxy materials unless the shareholders are otherwise prohibited—either by applicable state law or by the company's charter or bylaws—from nominating a candidate for election as a director. Shareholders would be allowed to nominate at minimum one nominee, up to a maximum of 25% of the board.[†]

The proposed rule would apply to all Exchange Act reporting companies, including investment companies, other than debt-only companies.

Shareholder Requirements

- A shareholder, or group acting for this purpose, would be eligible to have a nominee or nominees included in the proxy materials if the following ownership levels of voting securities were met for at least one year:

Type of Issuer [‡]	Ownership Level
Large accelerated filer	1%
Accelerated filer	3%
Nonaccelerated filer	5%

[†] Presumably the 25% of the board would apply even for a company with a staggered board, potentially allowing the shareholders to nominate individuals for a majority of the directors elected in a given year.

[‡] These ownership levels also apply to registered investment companies with net assets of more than \$700 million, \$70 million – \$ 700 million, or less than \$70 million, respectively.

Nominee Requirements

- The nominee’s candidacy or, if elected, board membership must not violate applicable laws and regulations.
- The nominee must satisfy the objective independence standards of the applicable national securities exchange or national securities association.
- The nominating shareholder may have no direct or indirect agreement with the company regarding the nomination of the nominee.

Required Disclosure and Liability

- The nominating shareholder would be required to file with the SEC and submit to the company a new Schedule 14N disclosing the amount and percentage of securities owned by the nominating shareholder, the length of ownership, and its intent to continue to hold the securities through the date of the meeting.
- The Schedule 14N would also require the nominating shareholder to certify that it is not seeking to change the control of the company or to gain more than minority representation on the board of directors.
- The company must include in its proxy materials disclosure concerning the nominating shareholder, as well as the shareholder nominee or nominees, that is similar to the disclosure currently required in a contested election.
- As is the case when directors nominate candidates, the nominating shareholder or group would be liable for any false or misleading statements in information provided to the company that is then included in the company’s proxy materials. The company would not be responsible for information provided by the shareholder, unless the company knows or has reason to know the information is false.

Amended Exchange Act Rule 14a-8(i)(8) would allow shareholders to require companies, under certain circumstances, to include proposals in their proxy materials that would amend, or request an amendment to, the company’s governing documents to address the company’s nomination procedures or other director nomination disclosure provisions that do not conflict with SEC rules.

Currently, Exchange Act Rule 14a-8(i)(8) permits companies to exclude shareholder proposals that “relate to an election.” Under the proposal, this so-called “election exclusion” would be narrowed, thereby allowing in the proxy materials more shareholder proposals regarding elections. Specifically, shareholder proposals by qualifying shareholders that would amend, or that request an amendment to, provisions of a company’s governing documents concerning the company’s nomination procedures or other director nomination disclosure provisions (so long as those disclosure provisions did not conflict with proposed new Rule 14a-11 discussion above) would not be excludable.

The current eligibility provisions of Rule 14a-8 would continue to apply. Those provisions require that a shareholder proponent have continuously held at least \$2,000 in market value (or 1%, whichever is less)

of the company's securities entitled to be voted on the proposal at the meeting for a period of one year prior to submitting the proposal.

If you have any questions on any of the issues discussed in this LawFlash, please contact the Morgan Lewis attorney listed below:

New York

Howard A. Kenny

212.309.6843

hkenny@morganlewis.com

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