

ABA
AMERICAN BAR ASSOCIATION

Defending Liberty
Pursuing Justice
Section of Business Law
321 North Clark Street
Chicago, IL 60610
312.988.5000
email: businesslaw@abanet.org
website:
www.abanet.org/buslaw

By Electronic and United States Mail

October 2, 2007

Nancy M. Morris, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-9303

Re: File Nos. S7-16-07 and S7-17-07
Release No. 34-56160; IC-27913 - Shareholder Proposals
Release No. 34-56161; IC-27914 - Shareholder Proposals Relating to the Election of Directors

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Federal Regulation of Securities of the American Bar Association, Section of Business Law (the "Committee") in response to the request by the Securities and Exchange Commission (the "Commission") for comments on the releases described above dated August 3, 2007. This letter was drafted by members of the Task Force on Shareholder Proposals of the Committee (the "Task Force").

The views expressed in this letter have not been approved by the American Bar Association's House of Delegates or Board of Governors and should not be construed as representing policy of the Association. In addition, this letter does not represent the official position of the ABA Section of Business Law, nor does it necessarily reflect the views of all members of the Committee or the Task Force.

OVERVIEW

The Commission has submitted for comment two proposals relating to the director election exclusion currently included in Rule 14a-8 under the Securities Exchange Act of 1934, as amended (the "Exchange Act").¹ Release 34-56161 includes both an interpretation of and a proposed amendment to Rule 14a-8 (the "Exclusion Proposal") that reaffirms the historical application by the Commission and its Staff (the "Staff") of that provision and revises its language to eliminate any ambiguity and better express that interpretation. The other proposing release, No. 34-56160 (the "Access Proposal"), would further amend paragraph (i)(8) of Rule 14a-8 to permit eligible shareholders to include in company proxy materials proposed bylaw amendments that would allow shareholders to use the company's proxy statement and proxy card to solicit votes for shareholder nominees for the board. (We refer in this letter to the right that may be granted under such a bylaw amendment as "access.") The Access Proposal also includes proposed amendments to Schedule 13G and Schedule 14A and a new Rule 14a-17 that would establish disclosure requirements in connection with access bylaw proposals, as well as nominations made pursuant to access bylaw proposals that have been adopted pursuant to the proposed amendment of Rule 14a-8.

In addition, the Access Proposal is accompanied by proposals concerning the submission of precatory proposals under Rule 14a-8 and the possible use of electronic forums to facilitate shareholder communications.

We recognize the substantial effort by the Commission and members of its Staff to seek an appropriate resolution of access issues in time for the 2008 proxy season.

We respectfully recommend that the Exclusion Proposal be adopted in the best interests of investors. The Commission and its Staff have consistently taken the regulatory position since Rule 14a-8 was instituted that Rule 14a-8 is not a mechanism for use in the conduct of election contests. We do not believe that there has been any change in circumstances in recent years that justify a change in this view. The concept of enabling shareholders to use a company's proxy materials to submit an access bylaw for a shareholder vote is inextricably linked to the use of company proxy materials to facilitate an election contest. Otherwise, what purpose would the bylaw serve?

We do not believe that a convincing case has been made that access to company proxy materials is needed to protect or facilitate the rights of shareholders to nominate directors and therefore recommend that the Access Proposal not be adopted. These rights originate under state law and can already be pursued through existing mechanisms under state law and the current proxy rules. Moreover, recent changes made by the Commission to facilitate the use of the Internet in proxy solicitations have largely eliminated the alleged impediments that existed to shareholders conducting cost-effective, widespread solicitations in support of shareholder nominees in opposition to a board's slate.

The Access Proposal would establish an exception to Rule 14a-8(i)(8) permitting shareholders to submit for inclusion in the company's proxy statement an access bylaw subject to the conditions that the submitting shareholder(s) have a minimum 5% share ownership for at least one year, include specific disclosures about the proponent(s) in a Schedule 13G and have no control intent. However, the bylaw to be submitted need satisfy only one condition, namely, its validity under applicable state law and the charter and bylaws of the particular company. Therefore, under the Access Proposal, the content of an access bylaw would largely be unrestricted, and access bylaws could be used both to enable change-in-control elections and potentially to shift the entire cost of change-in-control and other election contests to all of the shareholders. We believe that it is inconsistent to require no control intent in connection with the submission of an access bylaw proposal under Rule 14a-8, but then to enable control contests to be conducted under an access bylaw. This is contrary to the well-established principle that Rule 14a-8 is not to be used as a mechanism for effectuating a change in control of a company, an event which is extensively regulated under other provisions of the Exchange Act, including other provisions of the proxy rules.

In addition, we believe that the unregulated content of Rule 14a-8 eligible access bylaws could lead to an unworkable corporate governance regime, in which many companies would be burdened with bylaws that do not work in practice, are of questionable validity under state law or are otherwise confusing and/or inordinately complicated.² We do not believe that the potential costs and serious risks that we believe would flow from the proposed "free writing" system that would be allowed under the Access Proposal have been justified. We also note that the practical effect of many access bylaws would be to establish a "universal" ballot³ in the election of directors, which would raise novel and difficult disclosure issues and possibly state law issues as well.

Nor do we believe it is appropriate or practical to rely on "private ordering" to prevent or solve the potential issues of workability inherent in the open-ended structure of the Access Proposal. Private ordering has proved valuable and viable when administered by boards and managements who have fiduciary duties to all shareholders and responsibilities to ensure the workability of the company's governance structure. Shareholders have neither any fiduciary duties to other shareholders nor any responsibility for the practicality, effectiveness or consequences of implementation of their access bylaw proposals.

We are sensitive to the issues that would arise if the Commission were to impose content limitations on a proposed access bylaw as a condition to eligibility under a revised Rule 14a(8)(i)(8) to prevent access bylaws from becoming vehicles for control contests and to seek workability and reasonable transparency. Any such prescriptive rules might well raise issues as to the Commission's statutory authority to mandate such prescriptions in an area traditionally regulated by state corporate law. However, we do not believe it is appropriate to ignore the likely proliferation of election contests, including those seeking a change in control, and the fundamental issues of workability, including the effects of adopting a "universal" ballot system of proxy solicitation, that would likely result under the Access Proposal. That the Access Proposal generates this dilemma underscores why the Access Proposal should not be adopted.

The electronic shareholder forum and precatory voting proposals raise novel issues with far-reaching implications. A 60-day comment period is insufficient to give them the attention they deserve. We strongly urge the Commission to consider further rulemaking with respect to both issues, or at least to extend the comment period on these proposals so as to enable a more deliberate and thorough evaluation.

We have organized our detailed comments as follows:

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THE EXCLUSION PROPOSAL

We support and believe it is appropriate that the Commission has confirmed in the Exclusion Proposal release the Commission's and Staff's longstanding interpretation of the director election exclusion of Rule 14a-8(i)(8). We agree with the Commission that excluding access proposals on the basis of Rule 14a-8(i)(8) is consistent with the Commission's past statements and the great majority of the Staff's past interpretations, and that it is important to the overall functioning of the proxy rules that director election contests be separate from the Rule 14a-8 shareholder proposal process.

We also support the Commission's proposal to reiterate the previously well established scope of Rule 14a-8(i)(8) through adoption of the Exclusion Proposal. The court's ruling in *AFSCME v. AIG*⁴ has created the possibility that the director election exclusion in paragraph (i)(8) of the Rule will be applied in an inconsistent manner within different circuits. It is extremely important that the uncertainty caused by the case be resolved in as clear and emphatic a way as possible. Accordingly, we urge the Commission to amend Rule 14a-8(i)(8) to clarify its scope consistent with the Commission's and Staff's prior, long-standing interpretation.

While we strongly support the Commission's amendment of Rule 14a-8(i)(8) in the Exclusion Proposal, we believe the proposed amendment should be further clarified. Specifically, some of the uncertainty over the scope of Rule 14a-8(i)(8) has arisen from the language in the rule, which on its face does not distinguish between proposals that would affect director nominations at a particular meeting or would set up a process for future contests, on the one hand, and proposals that establish procedures generally applicable to future uncontested elections, on the other hand. Thus, we believe that the proposed language for the rule, which refers generally to proposals that relate to "a procedure

for nominations or elections,” could be read too broadly as permitting exclusion of proposals that the Commission and Staff have historically stated are not intended to be excluded, such as proposals recommending that action be taken to adopt cumulative voting in all director elections.

We recommend instead that language be added limiting this aspect of the provision to procedures that apply to or may result in contested elections, so that it is clear that the Rule is not intended to be used to establish means to conduct proxy contests.⁵ Accordingly, we recommend that the amended text of Rule 14a-8(i)(8) be revised to read as follows:

If the proposal relates to a nomination or an election for membership on the company’s board of directors or analogous governing body, including, without limitation, (i) by opposing the nomination for election, the election as a director, or service for his or her full term of a current director or board nominee for election, (ii) by directly or indirectly resulting in the ineligibility of any such person for such nomination, election or service or (iii) by otherwise creating or establishing procedures or practices that in the current or subsequent years apply to or may result in a contested election of directors.

In response to the Commission’s inquiry, we do not believe it is necessary or advisable to include in the regulatory text an enumeration of specific proposals that the rule would allow companies to exclude, beyond addressing the matters that have been raised by the *AIG* decision. We are concerned that including such language in the regulatory text could have the effect of restricting the dynamic and flexible nature of the Rule and discouraging further principles-based development of its parameters as new types of proposals are developed and considered in the future. Instead, we recommend that the Commission include statements in its adopting release that specifically confirm that the rule as amended is not intended to change or reverse past interpretations by the Staff as to the ability to exclude specific types of proposals, including those enumerated in footnote 41 of the Exclusion Proposal release (which include access proposals).

We also urge the Commission to reassess the consistency with the director election exclusion of recent interpretations taking the position that companies may not exclude pursuant to Rule 14a-8(i)(8) proposals providing for reimbursement of shareholder expenses in contested elections. Use of Rule 14a-8 by shareholders as a route to adoption of a bylaw that would generally mandate reimbursement of proxy contest expenses is tantamount to creating a system that would result in contested director elections. We believe that such proposals conflict with other well-established interpretations allowing a company to exclude proposals that would result in a contested election of directors by providing for company funds to be used to finance solicitations against the board of directors’ nominees.⁶ In addition, a departure from this well-established interpretation cannot be justified given the changes reducing the costs and otherwise facilitating contested proxy solicitations that have come into effect in recent years, as discussed below. We believe that the Commission should include a clarifying statement in the adopting release for the Exclusion Proposal to the effect that such cost-shifting proposals would have the effect of resulting in a contested election of directors and are therefore excludable under Rule 14a-8(i)(8).⁷

THE ACCESS PROPOSAL

Policy Considerations

In considering the need for and desirability of the Access Proposal, we believe it is important to consider the significant recent changes that have occurred or are being considered in the processes for election of company directors, including:

- mandated nominating committees composed of independent directors for almost all listed companies;
- significantly increased proxy statement disclosure of the workings of each company's nominating process;
- rapidly spreading adoption of some form of majority vote process for the election of directors;
- proposed revision of NYSE Rule 452 concerning broker non-votes in director elections;
- recent adoption of new SEC proxy rules allowing electronic dissemination of proxy materials (the "Internet Solicitation Rules");
- increasing influence of proxy advisory firm recommendations in director elections, including many instances where proxy advisory firms have recommended "withhold" votes for some or all of management's nominees; and
- increasing influence of institutional shareholders on corporate governance issues, including elimination or modification of poison pills, elimination of staggered boards, adoption of majority voting for directors and director resignation policies.

Against this background of change and evolution in the selection, role, performance and demonstrably increased accountability of directors to shareholders, we question whether a new Commission rule on access is either timely or needed. Rather, we urge the Commission to allow companies and shareholders to gain more experience with existing corporate governance reforms before assessing the need for and desirability of a change as dramatic and controversial as mandating that company proxy materials be available for proposals to institute any type of access regime.

We are, moreover, troubled about the policy decisions that seemingly underlie the Access Proposal. In stating this, we take into account the following:

- There is no dispute that the right of shareholders to nominate directors is universally provided under state law. In general, this right is limited only by charter or bylaw provisions that create classes of directors to be elected by different classes or series of shares or that require advance notice of shareholder nominations. Charter and bylaw provisions may also establish

qualification requirements for directors, but we are not aware of significant instances where director qualification requirements have been used to frustrate the right of shareholders to nominate directors. In short, shareholders today clearly have the right to nominate directors. Nor are we aware of any empirical evidence that the exercise by shareholders of the right to nominate directors is difficult or particularly expensive. Recent disclosure requirements of the Commission have ensured that information is readily available about the procedure and timing requirements for shareholder nominations and also about the process and criteria for presenting shareholder candidates to board nominating committees. Additionally, nominating committees composed of independent directors are required for virtually all listed companies, ensuring disinterested review of shareholder candidates.

- Inasmuch as shareholders already have the legal and practical ability to nominate directors in opposition to board nominees, we assume that the Access Proposal stems primarily from a concern that the exercise of the well-established right of shareholders to make nominations is limited by the costs of a conventional proxy contest to elect shareholder nominee(s). If this is the underlying rationale for the Access Proposal, it amounts to a Commission determination that it is wise and proper policy under Section 14(a) for the Commission to facilitate the transfer of the cost of a proxy contest from the proponents of the insurgent directors to the company (and thus indirectly to all of the company's shareholders), without regard to the outcome of the contest. We do not believe the Commission has stated a persuasive case justifying this policy decision. We also are troubled about the appropriateness of a rulemaking procedure that has not dealt with the underlying factual issues surrounding the dimensions of the cost issues, as well as alternative arrangements for cost transferal, such as a "loser pays" structure. In this regard, we note:
 - The proposing release does not contain any discussion of the costs of proxy solicitation by the company or by insurgents, either historically or in the context of the increasing institutionalization of the equity markets and the revolution in communication technology that have so dramatically affected the practical ability of investors effectively to discuss issues relating to their investments among themselves and with the companies in which they invest.⁸ There seems to be no consideration of the flexibility already provided to shareholders in making limited solicitations under Rule 14a-2(b) or the expected cost reductions from the Commission's recent adoption of the Internet Solicitation Rules.
 - In our experience, the greatest variable cost in a proxy contest has historically been dissemination of printed solicitation materials and running newspaper advertisements as a second principal means of communication with shareholders. In recent years, however, institutional shareholders have found that a combination of telephone calls and Internet-based message dissemination can be very effective in proxy campaigns. The Commission's new Internet Solicitation Rules permit exclusively electronic distribution of proxy materials by shareholders, a significant new regulatory initiative that has the ability to reduce drastically the costs of a proxy solicitation by eliminating the need to print and distribute paper copies of proxy materials and by providing more targeted,

effective and cheaper communications methods than the blunt instrument of very expensive newspaper ads. Accordingly, we believe that the Commission's existing proxy rules already effectively address the cost concern.

- There is substantial evidence that investors today can and do run effective proxy contests at little cost without using the company's proxy materials to state their case. The success of institutional investors in advocating withhold vote campaigns and in opposing merger transactions is clearly the result of informal telephonic and Internet-based communications among investors and the important role of proxy advisory firms in the voting process. We believe the prevalence and success of these shareholder voting initiatives demonstrate that access to a company's proxy statement is not necessary for effective utilization of the shareholder franchise, and that the already effective ability of shareholders to wage low-cost, internet-based proxy contests will be further increased by the Internet Solicitation Rules.
- Without regard to which party will pay the costs of a proxy contest, it is important to note that proxy contests entail important systemic costs. They are, by their nature, very distracting to a company's management and board of directors and can adversely affect the company's performance. The Access Proposal will invariably lead to a number of proxy contests over whether to adopt an access bylaw, and each adopted access bylaw will virtually ensure a proxy contest every time the access bylaw is used to nominate directors in opposition to a board's candidates. Thus, another serious but unaddressed policy issue inherent in the Access Proposal is whether the costs to public companies individually and collectively of a Commission-created regime that promotes an increase in the number of proxy contests that otherwise would not occur and shifts the costs of those contests to all of the company's shareholders is justified by the goal of relieving shareholder proponents of insurgent nominees of the responsibility for their costs in running an election contest. This concern is particularly acute in light of the absence of any restrictions on the terms of access bylaws that could be proposed under amended Rule 14a-8(i)(8), giving rise to the possibility that holders of relatively few shares will be relieved of the cost inhibitions of sponsoring insurgent nominees and therefore be unrestrained in their utilization of bylaw mandated access to launch numerous and possibly repetitive proxy contests.
- Finally, there are meaningful consequential economic and systemic costs to an increased number of proxy contests that are too often overlooked, arising from our far from efficient and effective shareholder voting system. These issues include:
 - The lack of transparency in beneficial ownership attributable to multiple custodial accounts beginning with Depository Trust Company and continuing through one or several layers of custodial and broker-dealer accounts, making it difficult for the company and insurgents alike to communicate directly with the ultimate beneficial owners of shares.

- The dependence of the stock voting system on record dates that often precede the meeting date by as much as 60 days, coupled with the practical inability of investors who acquire shares after the record date to direct the ultimate record holder on voting those shares.
- The cumbersome and costly mechanics by which intermediaries distribute paper proxy materials to ultimate beneficial owners and capture and collect their response, as well as the difficulties of systemically dealing with failures by beneficial owners to provide voting instructions to their brokers (which, of course, is at the heart of the pending rulemaking concerning NYSE Rule 452).
- The prevalence of “over voting” caused in part by inefficiencies and errors in the proxy distribution and vote collection processes and in part by stock lending policies and procedures of large institutions, broker-dealers and professional custodians.
- A variety of market practices that create the opportunity for investors to acquire votes without some or all of the economic risks of ownership (so-called “empty voting”), including “borrowing” shares for “record date capture” and engaging in a variety of hedging strategies.
- The actual or practical delegation by many institutions of voting decisions to proxy advisory firms who wield, with minimal accountability and transparency, an increasingly large influence on the outcome of all proxy votes, particularly in contested situations.
- The practical separation by institutional investors of proxy voting decisions from investment decisions, either because of internal organizational structures or because the institution has delegated the investment function, but not the voting function, to third parties.

These inefficiencies and systemic issues in the stock voting system obviously have limited effect on uncontested elections and for that reason have been ignored or downplayed for many years. We urge the Commission to proceed cautiously before taking any action that would result in an increased number of proxy contests without also addressing the very real and serious implications of our flawed shareholder voting process on the cost and outcome of those proxy contests.

Workability and Authority Considerations

As discussed above, we recommend that the Commission adhere to its longstanding and sound policy that Rule 14a-8 may not be used to include access proposals in a company’s proxy statement. However, if the Commission decides to depart from this policy, we view the approach of limiting shareholder eligibility to propose access bylaws but providing no restrictions on the permissible terms of access bylaws, other than any established under state law, as anomalous. We believe that the lack of conditions on the terms of proposed access bylaws could result in an unworkable system of proxy

regulation: one that could be confusing to both companies and shareholders, that could be used to effect a change in control and that could lead to significant litigation and/or requests for regulatory action by the Commission in order to address structural deficiencies and interpretative issues:

- Because there would be no required limit on the total number of nominees that a single shareholder could propose for any particular election under an access bylaw, it would be possible to propose and adopt access bylaws that would permit a single shareholder or group of shareholders to effect a change in control of the issuer. Such a result would be directly contrary to the Commission's longstanding policy not to allow Rule 14a-8 proposals to be used to effect changes in control.
- A similar problem would occur if Rule 14a-8 access bylaws are not required to impose a cap on the total number of nominees that could be presented by all shareholders in company proxy materials for any given election.
- What if the total number of nominees of various proponents is not subject to a maximum? Situations could easily arise where multiple candidates running for each available board seat create a lengthy and quite possibly confusing election "free-for-all." What principles should be used to deal with a situation where the total number of nominees exceeds a maximum (set by either a Commission rule or a particular bylaw proposal)? Would priority for inclusion in the company's proxy materials be based on the largest number of votes represented by shares beneficially owned by each proponent, or on a first-come, first-served basis or some other mechanism? What if the bylaw were silent on this point?
- In order to be eligible for use of an access bylaw, must the proponent beneficially own a specified percentage of shares? Such a threshold would help to ensure that proponents nominate *bona fide* candidates and avoid what one commentator has described as "the tyranny of the 100 share shareholder."⁹
- Must a qualifying access bylaw relate only to access to the company's proxy materials? What if an access bylaw contains other provisions, such as mandating reimbursement of all solicitation expenses for insurgent candidates or other comparable matters that may affect the procedures for, frequency of or outcome of election contests? Would such matters be outside the purview of a permissible access bylaw under the revised Rule? Shouldn't they be, if the proposed access bylaw exception to Rule 14a-8 is to be truly limited in scope and not an open door to promote and subsidize election contests and change-in-control campaigns?
- Should an access bylaw prohibit the proponent and its nominee(s) from soliciting proxies for any nominee to be voted on in the same election who was not nominated by the same proponent (other than a board nominee in a "short slate" situation)? If not, couldn't the Rule 14a-8 bylaw be used in coordinated control contests that would evade any limit on the number of nominees that could be proposed by any single shareholder? What would be the purpose of allowing access when the same or a related shareholder is distributing

solicitation material for another nominee or other matter to be voted on at the same meeting?

- Should there be a requirement that permissible access bylaws limit the length of supporting statements to some reasonable extent (such as the existing Rule 14a-8 500-word standard)? If not, what would prevent insurgents from forcing the company to print lengthy and verbose statements in support of nominees or otherwise improperly using the company's proxy materials?

We recognize that the development of the appropriate limitations on the content and scope of access bylaws is a complex subject that requires dealing with a significant number of variables. However, if the Commission is going to establish a regulatory system that promotes the use of access bylaws, we believe that it is inappropriate to leave unaddressed the complex and important issues that the Commission's Access Proposal would generate for our shareholder voting system. The alternative of an unrestricted access bylaw regime, including availability of access bylaws for use in control contests, could lead to a plethora of different access bylaws among public companies, embodying different access rules and producing varying outcomes, that would generate confusion about the voting rights of shareholders and in many cases result in unworkable bylaw provisions. Moreover, we have little confidence that "private ordering" can result in workable access bylaws. In our experience, shareholder bylaw proposals are often overly simplistic and proponents and proxy advisory firms rarely seem concerned with or are prepared to deal with the "nitty-gritty" of the complex procedural and practical issues implicated by bylaw proposals. In our view, there are inevitable and obvious workability risks inherent in a "free writing" system that would result from the lack of uniform, minimum substantive provisions for access bylaws under the Access Proposal. We believe these risks clearly outweigh the cost-reduction considerations for proponents of board nominees in opposition to a board's slate, which seemingly is the only policy reason for permitting access bylaw proposals under Rule 14a-8.

We further recognize and are sensitive to the conceptual, drafting and statutory authority issues that might arise if the Commission were to prescribe minimum conditions for the content of permissible access bylaws under a revised Rule 14a-8. However, we do not believe that the difficulties of developing such prescriptions or the statutory authority questions that they might raise justify adoption of the Commission's proposed "free writing" approach to access bylaws. If the Commission is not willing or able for statutory authority reasons to adopt prescriptive rules limiting the content of access bylaws so as to achieve a workable access regime, that in itself, we believe, is a compelling reason why the Access Proposal should not be adopted.¹⁰

State Law Considerations

The Access Proposal release notes that the carve-out for access bylaws from Rule 14a-8(i)(8) is intended, in part, to "facilitate shareholders' exercise of their state law rights to propose amendments to company bylaws concerning director nominations."¹¹ The Commission should consider as a policy matter whether facilitating the proposal and adoption of access bylaws will, on balance, diminish rather than enhance stockholders' state law rights. A bylaw that allows any stockholder to use the company's

proxy materials essentially to subsidize its own personal proxy contest may harm the other stockholders who bear the *pro rata* cost of that subsidy from the company treasury. Moreover, as noted above, the “cost” of a proxy contest involves not simply direct out-of-pocket expenditures but also management time and distraction and potential damage to the company’s performance and valuation.

The costs of administering an access regime under Rule 14a-8 should also take into account the uncertainty surrounding the validity and enforceability of access bylaws under state law. The Staff will no doubt be called upon to consider opinions of counsel concluding that specific access bylaws are excludable from a company’s proxy materials pursuant to Rule 14a-8(i)(2) because the proposal would violate state law if adopted¹² or pursuant to Rule 14a-8(i)(1) because the proposal is not a proper subject for stockholder action under state law.¹³ These issues will add to the existing costs of the Staff’s administration of Rule 14a-8 and will increase the existing tensions surrounding whether and when the Staff (and Commission) will accept opinions of counsel as to matters of state law that have not been expressly ruled on by state courts. Moreover, even if the Staff adopts a position that it will not issue no-action determinations where state law is “unsettled,”¹⁴ the Staff may be asked to decide whether certain facets of a proposed access bylaw conflict with the company charter or an express statutory provision, in which circumstances the Staff has granted a no-action determination in the past.¹⁵

In situations where the Staff is unwilling to issue a no-action determination based on an opinion of counsel because in its view state law has not clearly resolved the validity of the bylaw, the company or the proposing shareholders may incur costs litigating in state court to resolve the validity of the proposal. Yet, the costs of presenting the matter to a state court may not yield any result, as a court may decline to decide the issue until the access bylaw is adopted¹⁶ or until a later point when a stockholder attempts to use the access bylaw.¹⁷

If guidance from a state court is not forthcoming, boards may be forced to expend additional time to consider whether they should amend or repeal a shareholder-adopted access bylaw if they believe it is not enforceable or if they believe that it is being used in a given proxy contest in a manner that harms the other stockholders. Importantly, the decision whether to expend corporate funds on a particular action, including whether to finance a proxy contest, inheres in the board under state law.¹⁸ The board may determine that its fiduciary duties require it to amend or repeal an access bylaw if the directors determine that a stockholder is using the bylaw to waste corporate funds on its own private agenda or in a manner adverse to other stockholders. Yet, amendment or repeal of an access bylaw by the board may raise difficult issues as to whether the directors, as an equitable matter, should be permitted to amend or repeal a stockholder-adopted bylaw.¹⁹

To illustrate the difficult and challenging state law issues that would be presented by virtually any access bylaw, we note that the Commission has rightly identified the stockholders’ power to nominate candidates for director as a key feature of stockholder rights under state law. Indeed, state courts monitor closely any purported limitation on the power to nominate candidates for director because the right to elect directors would be meaningless without the ability to present competing candidates.²⁰ But, enhancing one stockholder’s nomination rights through access to a company’s proxy

statement will diminish the rights of other stockholders, who are entitled to the assurance that company funds and management time and focus are employed only in a manner that the sitting board, as the company's designated fiduciaries, determines is in the best interests of all stockholders. Under state corporation law, incumbent directors are permitted to use company funds to submit their nominees for election or reelection only under the rationale that this expenditure from the company's treasury benefits all stockholders because the directors have made a determination that the election of their nominees will further the best interests of the company. In uncontested elections, incumbents owe a duty to ensure that their successors carry on the business of managing the company. In contested elections, the incumbents owe a duty to defend their management policies against challengers who wish to operate the company in a different way than the incumbents, in the exercise of their fiduciary duties, conclude will not further the company's best interests.²¹

Permitting a stockholder to include nominees in company-funded proxy materials implicates additional considerations. Generally, a stockholder is not required to act in the best interests of all stockholders and is free to exercise its right to nominate candidates to advance any agenda it wishes, including its own selfish interests.²² Other stockholders may be harmed if corporate money is used to fund a proxy contest that advances the private interests of only one faction of stockholders. Given this consideration, it is not surprising that, to our knowledge, no state corporation statute confers on stockholders a right to access the corporate proxy machinery or otherwise access corporate funds to support shareholder nominees.

This uniform state law policy against forcing a company to subsidize a stockholder's proxy contest is hardly novel. For example, governing precedents under Delaware corporation law suggest that corporate funds should not be used to aid a proxy contestant unless the company's directors, in the exercise of their fiduciary duties, determine that the proxy contest involves issues of company policy, and therefore the contest would benefit all stockholders by informing their decision on the policy issues at stake when one candidate is selected over another.²³ An access bylaw that permits a stockholder to use the company proxy to submit its nominees may therefore run counter to important principles of state corporate law if the proxy contest that ultimately develops does not benefit all stockholders by informing them on issues of policy.

Disclosure Considerations

If the Commission adopts the Access Proposal, we share the Commission's views about the disclosures that shareholders should have available to them when voting on access bylaws and nominations made pursuant to such bylaws. We agree that shareholders should be provided "the disclosure that otherwise would be required under the federal proxy rules applicable to elections involving solicitations in opposition to a company's nominees" whenever shareholders are asked to vote on an access bylaw or on the election of a nominee presented pursuant to such a bylaw.²⁴ We concur that "[t]he already significant role that full disclosure plays in our proxy rules is rendered still more important when individual shareholders or groups of shareholders who do not owe a fiduciary duty to the company or to other shareholders, use company assets and resources to propose changes in company governing documents."²⁵ We also concur that the current proxy disclosure system does not adequately address the disclosure issues that would arise if companies were required to include access

proposals in their proxy materials under Rule 14a-8. Accordingly, if the Commission were to adopt the Access Proposal, we generally support the related disclosure requirements that the Commission proposes to establish.

We do have three principal disclosure concerns that arise in the context of the Access Proposal:

- The “control intent” disclosure requirements embodied in Rule 13d-1(e) and (g), in Item 4 of Schedule 13D and in Rules 14a-9 and 14a-12 should not be undermined by the proposed new Items of Schedule 13G and Schedule 14A.
- The disclosure requirements of proposed Item 8B of Schedule 13G and proposed Item 24 of Schedule 14A should not impede the ability of companies and shareholders to communicate on governance matters, including board nomination procedures and criteria, and should ensure adequate disclosure of proponent shareholders’ economic interests in the company.
- Any final rule should provide explicit disclosure requirements for “universal” ballots and accompanying proxy materials under an access regime.

“Control Intent” Issues. Should an access proposal of any sort be allowed under Rule 14a-8, we support the proposed limitation on eligibility to make such a proposal to persons having, individually or as a group, beneficial ownership of more than 5% of a company’s voting securities entitled to vote on the proposal, all of whom have beneficially owned such securities for at least one year. While some may argue that 5% is too high an ownership threshold, we note that it is in fact significantly below the threshold that is typically required for shareholders to call a special meeting, which is an analogous situation under state law where holders of less than a majority of the outstanding shares may by collective action impose costs on a company. We also concur that eligibility to make such a proposal should be conditioned on satisfying the “no control intent” requirement associated with Schedule 13G pursuant to Exchange Act Rule 13d-1(b)(i) and (c)(i) and that it makes sense to apply the Commission’s Schedule 13G reporting system in order to ensure that investors are provided pertinent information regarding the person or group sponsoring the proposal.

We note, however, that under Rule 13d-1(d) certain “grandfathered” holders of shares are permitted to file reports under Schedule 13G even if they have a control intent. We recommend that proposed Rule 14a-8(b)(i)(8)(ii)(B) be amended to clarify that the reference to “an institutional investor or a passive investor” excludes a person relying on Rule 13d-1(d) to file a Schedule 13G unless such person has in fact filed a Schedule 13G containing, along with the information of proposed new Items 8-B and 8-C, an undertaking that the person does not have a control intent comparable to that which would customarily be required under Item 10 of Schedule 13G.

We are also concerned that the “no control intent” representation of the sponsoring shareholder or group of shareholders be credible under the circumstances. Once the beneficial ownership of a company’s shares by a person or group of persons acting in concert exceeds 5% of a company’s outstanding voting securities, the question naturally arises whether the person or group can meaningfully claim it does not have a control intent when it is also sponsoring an access proposal. As

the level of beneficial ownership of a company's shares by the person or group increases, the concentration of voting power in the person or group makes it likely that, at some point, its sponsorship of an access proposal will, as a practical matter, operate as a means for it to exercise influence over company policies. For this reason, we believe it is important that the reference in proposed Rule 14a-8(i)(8)(ii) to minimum beneficial ownership of 5% and to Schedule 13G not be considered to imply that sponsorship of an access bylaw automatically establishes that a person or group satisfies the Schedule 13G eligibility requirement that it hold shares without a purpose or effect of changing or influencing the control of the issuer and not in connection with or as a participant in a transaction that has such an effect. Accordingly, were the Access Proposal adopted, the Commission should make clear in an appropriate instruction that sponsorship of an access bylaw proposal does not act as a "safe harbor" and does not preclude an inquiry into whether the person or group has a "control intent" under the Commission's traditional approach that all relevant facts and circumstances must be analyzed when making such a determination.²⁶

In particular, we believe that a person who seeks to sponsor an access bylaw pursuant to proposed Rule 14a-8(i)(8) and *who at the time of its sponsorship has the intent* to propose a nominee under the bylaw could well be acting with the purpose or effect of influencing control and, if so, would not be eligible to submit an access bylaw proposal under proposed Rule 14a-8(i)(8) nor to report its beneficial ownership on, or continue reporting on, Schedule 13G. In such circumstances, we understand the Commission's Access Proposal would not be available, the person would be required to propose its access bylaw apart from proposed Rule 14a-8(i)(8) (presumably, pursuant to Rule 14a-4) and the same substantive disclosures that would be required by Items 8-B and 8-C would likely be required of the person pursuant to Item 4 of Schedule 13D, along with disclosure regarding its plans to nominate a director pursuant to its access proposal and any other plans it has regarding the issuer.²⁷

Disclosure Clarifications. In general, we endorse the Commission's proposal to add new Items 8A, 8B and 8C to Schedule 13G and new Item 24 to Schedule 14A, as well as new Rule 14a-17, to ensure adequate disclosure to investors when an access proposal is presented for a vote or a nominee is presented for a vote pursuant to an access regime. There is, however, one aspect of the proposed amendments that we believe would establish unnecessary and, in some cases, counterproductive disclosure requirements and another that we think should be expanded to provide greater transparency to investors.

Proposed Item 24(d)(2) of Schedule 14A would require disclosure of any meeting or contact, including direct or indirect communications, by a shareholder proponent about an access bylaw proposal with the management or directors of a company in the 12 months prior to the shareholder proponent forming a plan or proposal regarding such a proposal, including disclosure in reasonable detail about the contents of the communication. Given the wide variety of contexts in which shareholders may make proposals under Rule 14a-8 and the desirability of managements, directors and shareholders discussing matters that may become the subject of shareholder proposals and coming to amicable agreement on such matters, including access proposals, we believe this disclosure requirement is overbroad and unnecessary. We do not question that, if in accordance with the requirements of an amended Rule 14a-8 an access bylaw is to be brought before shareholders for a vote, then the material elements of any discussions leading up to the proposal and any agreements or

understandings reached by the proponent and the management or board of directors in connection with proposal should be disclosed.

We are concerned, however, that the breadth of the language of this provision, which refers to “any contact” within 12 months *preceding* the time when a “shareholder proponent [forms] any plan or proposal” to propose an access bylaw would require a detailed recounting of fundamentally irrelevant preliminary discussions. For example, the discussions may occur at a time when the shareholder may not have decided on a course of action. An access bylaw proposal may be one of ten matters a shareholder proponent may be considering as a means for changing a company’s governance and may mention in a discussion with management. Similarly, the company may well not have made any considered decision on how it would react to an access proposal until a specific proposal is made.

We do not believe that disclosure of this type of preliminary discussion would aid shareholders in voting on a proposal. We also believe that a disclosure requirement of this nature may impede dialogue between companies and shareholders on issues such as access, without any countervailing benefit to shareholders in making a decision to vote on a specific proposal. We believe this sort of dialogue should be encouraged, not discouraged by the prospect that a statement made at a meeting may subsequently be required to be disclosed.

On the other hand, we believe that proposed Item 8B of Schedule 13G and Item 24(d)(2) of Schedule 14A does not assure adequate disclosure to shareholders in an important respect. Each item should be expanded to require a proponent of an access proposal to disclose whether it has and bears the economic incidence of ownership of the shares of the company it beneficially owns or has borrowed the shares or otherwise hedged its economic ownership position so that its interest in the shares may be materially different from other shareholders who own shares outright without any such mitigating relationships.

Universal Ballot Disclosures. If the Commission adopts the Access Proposal, it is likely that most if not all access bylaws adopted under revised Rule 14a-8 would not only require inclusion of shareholder nominees in the company’s proxy statement, but also the inclusion of those nominees on the company’s proxy card—a so-called “universal” ballot. In this context, we think it is imperative that the Commission adopt basic disclosure rules for “universal” proxy statements and “universal” ballots, that might, for example:

- Require that both the proxy statement and proxy card clearly distinguish management’s slate from other nominees and address related issues, including, for example, use of identifying nomenclature for competing slates (such as “board and/or management,” “insurgent,” etc.) and/or colors as a means to distinguish the sources of candidacy;
- Provide that the names and information about management’s nominees and other nominees be presented separately and not be intermingled (whether alphabetically or otherwise) to avoid confusion, particularly if there are a large number of shareholder nominees;

- Explicitly exonerate the company from liability for misstatements or omissions based on information from shareholder nominees, including supporting statements;
- Provide rules for dealing with shareholder “over votes” on a given proxy card (i.e., voting for more candidates than available board seats) and other voting mistakes; and
- Address the ability of management and/or shareholder proponents to prepare and disseminate additional proxy materials and/or proxy cards in traditional format (listing a single slate or short slate only).

The foregoing list is intended to be illustrative, not exhaustive. We believe it is quite likely that drafting and circulating rules for universal ballots will reveal other issues that should be dealt with in this context. Indeed, even if the Commission accepts our recommendation and refrains from adopting of the Access Proposal, shareholders may successfully propose access regimes under Rule 14a-4. Against this eventuality, and in the light of the Commission’s historic concerns for the integrity of the proxy process, we think the Commission should consider asking the Staff to review universal ballot disclosure issues and make appropriate recommendations concerning the need for and content of appropriate disclosure rules.

In light of the state law and authority issues referred to above, we take no position at this time as to the extent of the Commission’s authority to mandate that companies use a universal ballot and related proxy statement and other proxy materials in the election of directors.

Precatory Proposals

The Commission has requested comment on the approach it should take regarding non-binding shareholder proposals under Rule 14a-8. As noted at the Roundtable that the Commission convened in the spring of 2007, non-binding proposals have been a creature, albeit long-standing, of Rule 14a-8 since there is typically no provision made for such proposals as a matter of state corporation law.²⁸

At the outset, it may be useful to identify some basic principles that inform how we believe the Commission should approach non-binding proposals:

- It is important to distinguish between the subject matter of shareholder proposals (including those that are non-binding) and the procedure for submitting shareholder proposals. Rule 14a-8(i)(1) already allows for companies to exclude proposals where the subject is improper under state law. However, the application of this standard in the context of precatory proposals is unclear, because framing a proposal as precatory is an approach permitted by the Division of Corporation Finance to sanction the use of Rule 14a-8 when the proposal would violate state law if it were binding. In addition, the fact that companies have the burden under Rule 14a-8 of demonstrating that a proposal violates state law results in many shareholder proposals being included in companies’ proxy statements when their validity under state law has not been conclusively settled.

- In contrast, Rule 14a-8 is viewed as pre-empting state law standards on the process for introducing proposals at shareholders meetings. For example, it is well established under most state corporation laws that street name shareholders do not have a right to present a proposal at an annual meeting and instead a beneficial owner must have the record owner (typically Cede & Co.) submit the proposal on its behalf, and yet Rule 14a-8 is viewed as pre-empting this standard. In addition, Rule 14a-8 is viewed as pre-empting advance notice bylaw provisions that otherwise govern the timing and information that shareholders must satisfy if they wish to introduce proposals at an annual meeting, and the provisions of Rule 14a-8 allowing a statement in support of a proposal to be included in a company's proxy statement have no counterpart under state law.
- Some companies and shareholders believe that non-binding shareholder proposals provide another method for shareholders to make their views known and can serve to avoid more confrontational binding proposals, whereas other companies and shareholders view such referenda as an improper use of company assets and shareholders' time during the annual meeting.
- The current Rule 14a-8 regime has been expensive and difficult to administer, has consumed significant SEC staff resources and has distracted focus from binding matters to be acted on at shareholder meetings; therefore, alternatives to the current regime deserve consideration.

With these principles in mind, we believe that the Commission should:

- expressly recognize in the proxy rules themselves that non-binding proposals are permitted under Rule 14a-8 only to the extent they are permitted under state law;²⁹ and
- revise Rule 14a-8 to provide that the procedural requirements under the rule apply only in the absence of a bylaw or other state law standard.³⁰

In addition, we note that the fact that companies have the burden under Rule 14a-8 of demonstrating that a proposal violates state law appears to create in practice a presumption that results in many shareholder proposals being included in companies' proxy statements when their validity under state law may be unsettled. We believe that when a company has submitted a legal opinion supporting exclusion of the proposal and the proponent has not demonstrated any basis for questioning the validity of that opinion, it would normally be appropriate to permit the company to exclude the proposal.³¹

This approach would better align the federal proxy rules with state law, so as to be supportive of shareholders' exercise of state law rights but not alter those rights. For example, a corporation could choose to establish an alternative to dealing with non-binding proposals at an annual meeting, and thus avoid cluttering the proxy statement and meeting agenda, by establishing an electronic voting system for non-binding proposals with many of the same characteristics as proxy voting at a meeting.³² Likewise, a company could establish a bylaw so that an electronic forum could be used for proposals

that have not received a specified level of shareholder support. Such a system could have the advantage of facilitating expression of shareholder views more frequently than just annually.

Depending upon applicable state corporation law and the corporation's governing instruments, amendment of a corporation's governing instruments to deal with non-binding proposals could be effected by the directors or by the shareholders, using Rule 14a-8 through either binding or non-binding proposals.

Because individual companies might be reluctant to act separately in this area, the Commission could promote the exploration of alternatives for dealing with non-binding proposals by establishing a pilot program that would allow companies, by whatever action is required as a matter of state corporation law, to establish an alternative electronic voting regime for non-binding proposals that met minimum standards established by the Commission. To encourage participation, participants in the pilot program could be permitted to exclude non-binding proposals under Rule 14a-8.

Electronic Shareholder Forums

We note the Commission's effort to facilitate the use of electronic shareholder forums (or "chat rooms") by removing impediments to the use of these means of communication. We believe that the issues raised under the proxy rules and Section 13(d) and the practical aspects of the utilization of electronic shareholder forums are sufficiently complex that companies, shareholders and other interested parties need a further opportunity to analyze and comment on the electronic forum proposals included in the Access Proposal than is possible by the comment deadline the Commission has established.

For example, we observe that hedge funds and other activist investors frequently use the Internet to communicate among themselves and to propose actions affecting companies in their portfolios. While these communications may not lead to the formation of a group within the meaning of Section 13(d) of the Exchange Act, they often result in parallel actions by these investors which are not subject to any disclosure under the federal securities laws.

We are concerned that adoption of the Commission's rule proposals for electronic shareholder forums could add legitimacy to such parallel action "campaigns" and could reduce transparency concerning shareholder interactions among themselves and with the companies in which they invest. For example, the draft proposals do not establish any standards of required disclosure by parties availing themselves of electronic shareholder forums, and the Commission's commentary approvingly cites the possibility of such forums being available to "shareholders whose anonymity is protected through encrypted unique identifiers." We are puzzled how anonymous messages would facilitate meaningful communications among shareholders and the company. Indeed, we believe that disclosure of the identity of the person posting a message in an electronic chat room should be a prerequisite for obtaining the special exemptions from the proxy rules that the Commission's proposal contemplates. Moreover, merely identifying the contributor would not address very important questions about the person's interests in the company and its contributions to the forum, such as:

- whether the contributor is acting solely for itself, as agent for others or pursuant to a formal or informal campaign of parties who share similar views,
- what voting and economic stakes the contributor has in the company, including the amount and nature of its direct and indirect share ownership and its economic interests in those shares,
- whether the contributor is seeking to exercise or influence control,
- whether it is commenting pursuant to a request or solicitation by another party to do so, and
- whether it has discussed the subject matter of its posted comments with other interested parties, including the company, and if so under what circumstances.

Another area that we believe is not adequately addressed in the Commission's electronic shareholder forum proposals is the very difficult question of whether any "cooling off" period prior to a proxy vote is sufficient practical protection against the ability of a coordinated campaign to so color shareholder perceptions as to make the vote a likely, if not foregone, conclusion. There are numerous examples in the market today of aggressive investors successfully pressuring companies to take significant actions well in advance of a shareholder meeting. In many such cases, the effectiveness of the aggressive investors' campaign to "win over" other large holders has been the deciding factor in causing a board to accede to the investors' demands and not prolong a contest it believes it could not win. All of these "contests" have been waged informally, totally outside of the proxy rules and with extremely limited disclosures. Some market observers and participants have argued that such informal "contests" (many would say "raids") have in many cases forced companies into short-term actions that ultimately harmed shareholder interests. Whatever the merits of the debate, it seems to us that adoption of new Commission rules that would facilitate and legitimize such "contests" requires far greater study and thought than it has received to date.

Unlike the Exclusion Proposal, we do not believe the imminence of the 2008 proxy season serves as a reason for expediting Commission action on electronic shareholder forums. In light of the significant unexplored policy and practical issues involved in the electronic shareholder forum proposal, we urge the Commission to extend the deadline for comment on these proposals or withdraw the proposals pending additional study and review by the Commission and Staff.

CONCLUSION

We believe there should be a direct connection between the purposes of rulemaking proposals and the consequences of their adoption. In light of numerous reforms that have been made concerning director elections and procedures for and cost of proxy contests, we do not believe that the case has been made that the Access Proposal is necessary or appropriate to vindicate shareholder rights under state law or that the dramatic consequences that adoption of the Access Proposal would have on the shareholder voting process are justified.

We can, however, foresee the consequences of the adoption of the proposal and its implementation. Substantively unrestricted access bylaws would likely become weapons in control contests. Difficult state law questions will inevitably arise concerning the permissible content and scope of access bylaws and any attempts by boards to amend shareholder-adopted access bylaws to make them more workable. Extraneous subject matter might often be included in access bylaws, since no limitation on the scope of the bylaws is contemplated under the Access Proposal. Proxy statements and proxy cards could become so lengthy and/or confusing as to be unmanageable and inconsistent with the well-defined policy of the Commission to inform shareholders in a comprehensible manner so that they can efficiently exercise their shareholder franchise. Voting and annual meeting procedures could be mired with uncertainty generated by novel issues. All this would be done at the cost of the company, to be borne by all shareholders.

We urge the Commission not to adopt its Access Proposal. The lack of uniformity, and probably in too many cases workability, of access bylaws that could be adopted under the Access Proposal, the potential authority and interpretive issues that may arise and the lack of compelling purpose support this recommendation.

The Commission's interpretations and proposals in the Exclusion Proposal are clearly within the authority of the Commission and consistent with past practice and historical interpretation. Consistent with the administrative requirements called for by the decision of the Court of Appeals for the Second Circuit in the *AIG* case, clarity, certainty and uniformity have been provided by the Commission's reaffirmation of its long-standing interpretation of Rule 14a-8(i)(8) and would be further advanced by adoption of the Exclusion Proposal. In our opinion, adoption of the Exclusion Proposal would not interfere with the exercise of rights by shareholders, as shareholders would have the same rights to pursue access bylaws that they have historically had. Accordingly, we recommend that the Commission adopt the Exclusion Proposal.

* * *

Nancy M. Morris
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The Committee appreciates the opportunity to comment on the alternative proposals. We will be pleased to discuss with the Commission and its Staff any aspects of this letter. Questions may be directed to the undersigned (617-951-7386), Robert Todd Lang (212-310-8200) or Charles Nathan (212-906-1730).

Respectfully submitted,

Committee on Federal Regulation of Securities

By: Keith F. Higgins
Committee Chair

Task Force on Shareholder Proposals

Robert Todd Lang, Co-Chair

Charles Nathan, Co-Chair

Frederick Alexander

Jay G. Baris

Richard E. Gutman

Stanley Keller

John M. Liftin

Michael R. McAlevey

Robert L. Messineo

James C. Morphy

Ronald O. Mueller

cc: Hon. Christopher Cox, Chairman
Hon. Paul S. Atkins, Commissioner
Hon. Annette L. Nazareth, Commissioner
Hon. Kathleen L. Casey, Commissioner
John W. White, Director, Division of Corporation Finance
Brian Cartwright, General Counsel

ENDNOTES

¹ Rule 14a-8 was adopted in 1942 in order to provide limited shareholder access to a company's proxy statement. Limitations include a maximum of 500 words in any shareholder statement, shareholder eligibility requirements and subject matter limitations embodied in 13 specific exclusions, one of which is for proposals relating to the election of directors. During the past four years, there has been significant debate concerning shareholder entitlement to access, much of which related to proposed Rule 14a-11 in 2003 to provide shareholder access under certain conditions, including measures designed to avoid the use of access for control purposes. The current consideration of shareholder access principally results from a decision of the U.S. Court of Appeals for the Second Circuit in *AFSCME Pension Plan v. American International Group, Inc.*, 462 F.3d 121 (2d Cir. 2006)(the "AIG Case") which held that because the Commission had not explained its reasons for its interpretation of the director election exclusion starting in 1990, the Commission's 1976 interpretation should govern and, therefore, a shareholder proposal to include in the company's proxy materials an access bylaw should not have been excluded. In so ruling, the court specifically took no position on shareholder access, indicating that this was not a matter for the judiciary to decide, but rather for the SEC. In our view, in order to comply with that decision, the Commission need only set forth the reasons for its historical interpretive position on exclusion. We believe that the Commission release that includes the Exclusion Proposal accomplishes this result.

² As discussed under "Access Proposal –Workability and Authority Considerations," the lack of any prescribed content for access bylaws will raise issues about their workability. By way of illustration:

- If there is no limit on the number of shareholder nominees, what standard, if any, would be applied in selecting nominees entitled to access if the number of nominees exceeds the limit on slots? Who would make that decision?
- Would there be any shareholder eligibility standards or could the bylaw provide that any shareholder has the right to nominate one or more directors?
- How would the bylaw deal with various voting processes including cumulative voting, class election of directors, classified board of directors, empty voting and the failure to be elected by the requisite vote?
- What if the access bylaw was in conflict with the company's advance notice bylaw?
- How would disputes concerning implementation of the bylaw be resolved?

It is improbable that most access bylaws would successfully deal with these and other workability issues that would almost certainly emerge from the lack of prescriptive content of access bylaws under the proposed revision of Rule 14a-8. Private ordering in situations where charter and bylaw provisions are proposed by a board, acting in its fiduciary capacity with the input of management and company counsel, is a far different reality than a "free writing" regime where shareholders with no responsibility for assuring workability and coherence are the draftsmen, and shareholder voting is prone to focus on "big picture" policy issues and rarely on practicalities of implementation.

³ The Commission has considered the “universal” ballot in the past. In the adopting release of the 1992 amendments to the proxy rules, the SEC stated that “Proposals to require the company to include shareholder nominees in the company’s proxy statement would represent a substantial change in the Commission’s proxy rules. This would essentially mandate a universal ballot including both management nominees and independent candidates for board seats.” Regulation of Communications Among Shareholders, Exchange Act Release No. 34-31326, 57 Fed. Reg. 48276, at 48288 (October 22, 1992).

A Staff Report released in 2003 added: “Rather than mandating a universal ballot, the Commission revised the bona fide nominee rule to allow shareholders seeking minority board representation to fill out a partial or short slate with management nominees, thus making it easier for shareholders to conduct an election contest in a non-control context.” U.S. Securities and Exchange Commission, Division of Corporation Finance, Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors (July 15, 2003), at <http://www.sec.gov/news/studies/proxyrpt.htm>.

⁴ *AIG Case*, *supra* n.1. We believe the Commission’s Exclusion Proposal will reduce costs to shareholders, companies and the Commission and its staff by improving their respective ability to assess the eligibility of shareholder proposals under Rule 14a-8 without resort to the costly and time consuming dispute resolution process under Rule 14a-8.

⁵ While the Commission proposes to reference that limitation in Commission statements in its adopting release, we believe that the better way of avoiding future questions over the intention of the rule would be to include language in the rule itself.

⁶ *See General Motors Corp.*, SEC No-Action Letter (April 10, 2000); *Bristol Myers Squibb Co.*, SEC No-Action Letter (Feb. 24, 2000); *Pfizer, Inc.*, SEC No-Action Letter (Feb. 22, 2000). In each, the Staff concurred that a proposal that would have the company retain an independent proxy advisory firm to make recommendations on matters up for a vote could be excluded under Rule 14a-8(i)(8).

⁷ As we discuss under the heading “Access Proposal – State Law Considerations,” we believe that permitting binding bylaw proposals under Rule 14a-8(i)(8) requiring company payment of some or all of insurgents’ costs in connection with election contests would raise difficult issues under state law. The state law issues would result in significant systemic costs in the administration of the revised Rule and complicated issues relating to the Commission’s authority to permit Rule 14a-8 to be used to impose proxy contest costs on companies in derogation of state law.

⁸ We note that there was no discussion of these costs in the Commission’s 2003 release proposing mandatory access under certain circumstances to corporate proxy materials for shareholder nominees and that none was contained in the SEC Staff report preceding that release or in the Commission’s recent Roundtables on proxy process which preceded the Access Proposal. *See Proposed Rule: Security Holder Director Nominations*, Exchange Act Release No. 34-48626 (October 14, 2003); U.S. Securities and Exchange Commission, Division of Corporation Finance, Staff Report: Review of the Proxy Process Regarding the Nomination and Election of Directors (July 15, 2003), at

<http://www.sec.gov/news/studies/proxyrpt.htm>; Roundtable Discussions Regarding the Proxy Process, Unofficial Transcripts, at <http://www.sec.gov/spotlight/proxyprocess.htm>.

⁹ John C. Coffee, Remarks at Roundtable Discussions Regarding the Federal Proxy Rules and State Corporation Law (May 7, 2007) (unofficial transcript available at <http://www.sec.gov/spotlight/proxyprocess.htm>).

¹⁰ As established in *The Business Roundtable v. SEC*, 905 F.2d 406 (D.C. 1990), the Commission's authority to regulate fundamental areas of corporate governance, such as shareholder voting rights, is not unlimited. There, the court found that the Commission could not derive authority to regulate on such matters by implication from its powers under Section 14 of the Exchange Act to regulate the disclosures made in proxy solicitations and otherwise to deal with proxy solicitation procedures. The court found that under the Exchange Act there was a clear Congressional determination not to make any broad delegation of power to the Commission with respect to voting rights since this would impinge on state corporate law. We have discussed further the Commission's authority to mandate access to company proxy materials for the election of directors in our letter dated January 7, 2004 concerning Exchange Act Release No. 48626. Inasmuch as the Commission has proposed alternative proposals concerning access and in light of the uncertainties surrounding the application of the Access Proposal in relation to state law considerations, we take no position in this letter with regard to the Commission's authority with respect to adoption or implementation of the Access Proposal.

¹¹ Shareholder Proposals, Exchange Act Release No. 34-56160 (July 27, 2007), at 19.

¹² Rule 14a-8(i)(2) permits a company to exclude a proposal that would, if implemented, "cause the company to violate any state, federal, or foreign law to which it is subject."

¹³ Rule 14a-8(i)(1) permits a company to exclude a proposal that "is not a proper subject for action by shareholders under the laws of the jurisdiction of the company's organization."

¹⁴ *See, e.g., United Parcel Service, Inc.*, SEC No-Action Letter (Feb. 20, 2007) (declining a requested no-action letter that a proposal establishing restrictive criteria for director nominees was excludable even when the company provided a legal opinion to that effect); *PLM International, Inc.*, SEC No-Action Letter (Apr. 28, 1997) (declining a requested no-action determination that a proposal was excludable pursuant to Rule 14a-8(i)(1) as an improper action for stockholders under Delaware law in part because the proposal raised an issue that appeared to be "an unsettled point of Delaware law").

¹⁵ *See, e.g., Northrop Grumman Corporation*, SEC No-Action Letter (Mar. 13, 2007) (concurring with the company's position that a proposal to adopt a bylaw that would be inconsistent with the company charter could be excluded pursuant to Rule 14a-8(i)(2)).

¹⁶ We note that a recent amendment to the Delaware Constitution would permit the Commission to certify questions of law to the Supreme Court of Delaware. *See* Delaware Constitution, Art. IV, § 11. However, the Supreme Court may exercise its discretion to decline to answer a question posed to it. *See id.* (empowering the court to answer certified questions when there are "important and urgent

reasons for an immediate determination”). Moreover, it is unclear how many other jurisdictions are empowered to hear certified questions from the Commission. Courts might also determine that the validity of a proposal is not ripe for judicial determination if it has not been approved by stockholders. *See Bebachuk v. CA, Inc.*, 902 A.2d 737, 743 (Del. Ch. 2006).

In this letter, we illustrate principles of state corporation law by citing to the statutes and judicial precedents from Delaware, the jurisdiction of incorporation for more than half of all publicly traded companies. Obviously the issues and results may not be the same in other jurisdictions.

¹⁷ *Cf. Stroud v. Grace*, 606 A.2d 75, 96 (Del. 1992) (declining to find that a director qualification bylaw was unreasonable on its face and noting that the validity of the bylaw “must await its actual use” by the company).

¹⁸ 8 *Del. C.* § 141(a) (“The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors...”); *UIS, Inc. v. Walbro Corp.*, 1987 WL 18108 (Del. Ch. Oct. 6, 1987) at *2 (refusing to grant a temporary restraining order that would have prevented a corporation from expending corporate funds because the directors “are charged with deciding what is and what is not a prudent or attractive investment opportunity” for the company).

¹⁹ *See Bebachuk*, 902 A.2d at 743 (treating as an unresolved issue the question whether the board should be permitted to repeal a stockholder-adopted bylaw that, if adopted, would limit the directors' power to adopt a rights plan that did not expire within a year of its adoption, but citing authority suggesting that the board may repeal such a bylaw). The laws of some jurisdictions may expressly forbid directors from amending stockholder-adopted bylaws under certain circumstances. *See Revised Model Business Corporation Act*, § 10.20(b)(2) (prohibiting the board from amending a stockholder-adopted bylaw that specifies that it may not be amended by the board).

²⁰ *See, e.g., Harrah's Entertainment, Inc. v. JCC Holding Co.*, 802 A.2d 294, 311 (Del. Ch. 2002) (“[T]he unadorned right to cast a ballot in a contest for [corporate] office . . . is meaningless without the right to participate in selecting the contestants.”) (internal quotations omitted).

²¹ *See, e.g., Hall v. Trans-Lux Daylight Picture Screen Corp.*, 171 A. 226, 228 (Del. Ch. 1934) (noting that directors owe stockholders a duty to inform them of information relevant to matters of corporate policy implicated by a stockholder vote and that “it often happens in practice... that questions of policy come up not as abstract propositions which are referred to the stockholders... but in the form of whether the directors who stand for the given policy shall be re-elected to office”).

²² *See Bershad v. Curtiss-Wright Corp.*, 535 A.2d 840, 845 (Del. 1987) (noting that, in exercising voting rights, “It is not objectionable that [stockholders’]... motives may be for personal profit, or determined by whim or caprice, so long as they violate no duty owed to other shareholders”) (citation omitted).

²³ *See, e.g., Hand v. Missouri-Kansas Pipe Line Co.*, 54 F.Supp. 649, 650 (D. Del. 1944) (noting that, under Delaware law, a company may reimburse a proxy contestant only for reasonable expenditures

when “stockholders are called on to decide controversies over substantial questions of policy as distinguished from inconsequential matters...”); *see also Empire Southern Gas Co. v. Gray*, 46 A.2d 741, 744 (Del. Ch. 1946) (holding that management could not use the company’s proxy materials to present nominees who were not approved by the directors and noting that incumbent directors have the right “speaking through the corporation, to exclude others from purporting to speak for the board”).

For over seventy years courts applying Delaware law have applied this requirement to permit the repayment of proxy solicitation expenses only if the funds expended informed stockholders on policy issues, and are therefore “in the interest of an intelligent exercise of judgment on the part of the stockholders upon policies to be pursued,” rather than solely for the “personal interests” of persons seeking office. *See Hall, supra; Gray, supra; Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 344 (Del. 1983); *Hand v. Missouri-Kansas Pipe Line Co.*, *supra* (applying Delaware law); *Steinberg v. Adams*, 90 F.Supp. 604, 607-608 (S.D.N.Y. 1950) (applying Delaware law); *Levin v. Metro-Goldwyn-Mayer, Inc.*, 264 F.Supp. 797, 802 (S.D.N.Y. 1967) (applying Delaware law).

²⁴ Access Proposal, at 36.

²⁵ Access Proposal, at 24-25.

²⁶ The Access Proposal does not indicate any change in the Commission’s position regarding the availability of Schedule 13G to shareholders who are activist investors, as articulated by the Commission in 1998 when changing the Schedule 13G availability requirements, and we do not believe adoption of the Access Proposal would warrant a departure from the traditional facts and circumstances test.

²⁷ We note that the definition of “shareholder proponent” in proposed Item 8-A of Schedule 13G (which would trigger the disclosure requirements of proposed Items 8-B and 8-C) refers to “A person or group that has formed any plans or proposals regarding an amendment of the company’s bylaws, in accordance with [proposed Rule] 14a-8(i)(8)” and accordingly would not apply to a person proposing an access bylaw other than pursuant to Rule 14a-8. A beneficial owner of 5% or more of a company’s shares with such a plan would presumably disclose its intentions pursuant to Item 4 of Schedule 13D. Items 8-B and 8-C would presumably provide a guide to the pertinent information to be disclosed pursuant to Item 4 in such circumstances but additional information may be required. We also note that proposed Rule 14a-17 similarly refers specifically to an nomination made pursuant to an access bylaw adopted pursuant to Rule 14a-8. We believe this reference to Rule 14a-8 is inappropriate because it seems inconsistent with the Commission’s emphasis on assuring adequate disclosure to shareholders when voting on shareholder nominees pursuant to an access bylaw, disclosure that seems equally necessary regardless of how an access bylaw is adopted. Accordingly, we recommend that this reference to Rule 14a-8 be deleted, so as to confirm that the disclosure specified by proposed Rule 14a-17 is to be provided in all circumstances where a nominee is sponsored pursuant to an access bylaw.

²⁸ *See Dyer v. Securities and Exchange Commission*, 287 F.2d 773 (8th Cir. 1961), in which the U.S. Court of Appeals for the Eighth Circuit held that stockholders’ claims “to have inclusions made in the management’s proxy materials, [were] the according of a privilege to them under the

Commission's regulatory powers and not the enforcing of some legal right existing in their stock ownership."

²⁹ Although already implicit under Rule 14a-8(i)(i), expressly recognizing this position would provide clarity and would give direction to the SEC staff to recognize the role of state law in administering Rule 14a-8.

³⁰ This approach is utilized under Rule 14a-4(c)(1), where for purposes of determining whether a company can exercise discretionary voting authority under proxies it solicits the Commission's rules establish a "default" time for the submission of a non-Rule 14a-8 proposal that applies in the absence of an advance notice provision in a company's bylaws. A company's advance notice bylaw provision can for this purpose establish a deadline that is earlier or later than the default provision standard under Rule 14a-4.

³¹ See note 13, *supra*.

³² Such a system could differ from a chat room by having a more organized approach to seeking and obtaining an expression of shareholder will that paralleled the approach at a meeting (e.g., an "American Idol" model).