



JONES DAY  
**COMMENTARY**

## SEC RELEASES SHAREHOLDER ACCESS PROPOSALS

On July 25, 2007, the Securities and Exchange Commission (the "SEC") issued two proposals regarding shareholder access to a company's proxy statement with respect to director nominations. Although the comment period for both proposals ends on October 2, 2007, SEC Chairman Cox has stated unambiguously that a clear final rule relating to these matters will be in place in time for the 2008 proxy season.

### BACKGROUND

Shareholder access has been a significant corporate governance issue for several years, but it lost steam when the SEC failed to adopt new shareholder access rules in 2003. On September 5, 2006, the United States Court of Appeals for the Second Circuit brought the issue back to center stage in *American Fed'n of State, County & Mun. Employees v. American Intern. Group, Inc.*<sup>1</sup> The SEC's longstanding position has been that

shareholder proposals relating to board elections may categorically be excluded from a company's proxy statement pursuant to Rule 14a-8(i)(8) of the proxy rules. Exclusion of such shareholder proposals was the subject of the Second Circuit's decision last fall. In that case, AFSCME, a shareholder of AIG, attempted to submit a binding shareholder proposal in AIG's 2005 annual proxy statement. The shareholder proposal was in the form of a bylaw amendment that would allow large, long-term shareholders access to the AIG proxy in subsequent years for the purpose of nominating director candidates. AIG excluded the proposal under Rule 14a-8 on the basis that it related to an election of the board of directors. The Second Circuit, however, held that the proposal was not properly excludable under Rule 14a-8(i)(8) because it did not relate to a specific election, but to elections generally. This called into question the SEC's existing interpretation that such proposals were excludable and, as a result, has led to a conflict among the courts.

1. 2006 WL 2557941 (2<sup>nd</sup> Cir. Sept 5, 2006).

In his opening remarks at the July 25 SEC open meeting, Chairman Cox summarized lessons learned from the failed shareholder access rule in 2003 and explained how the current proposals and related procedures differ. His comments focused on the need to:

- respect the role of state law on shareholder rights matters,
- make appropriate changes to the proxy process,
- avoid adding to or creating new shareholder rights under state law, and
- focus on the primary federal interest, which is full and fair disclosure.<sup>2</sup>

## CURRENT PROPOSALS

The first proposal would essentially codify the SEC's long-standing interpretation of Rule 14a-8(i)(8) (the "Status Quo Proposal"). In the Status Quo Proposal, the SEC explicitly states its view that a proposal may be excluded under Rule 14a-8(i)(8) if it would:

- result in an immediate election contest, or
- set up a process for shareholders to conduct a future election contest by requiring the company to include shareholder nominees in the company's proxy materials for future meetings.<sup>3</sup>

The second proposal sets forth a proposal that would allow a shareholder or a group of shareholders who meet certain requirements to submit, for inclusion in an issuer's proxy materials, a proposal to provide for a bylaw amendment that

would specify procedures for shareholder nominations of directors (the "Access Proposal").<sup>4</sup>

The Access Proposal would amend Rule 14a-8, as well as provisions of Schedule 13G, and would prevent companies from excluding shareholder bylaw proposals related to director nominations if:

- the proposal would be binding if approved by the shareholders;
- the proposal is submitted by a shareholder or group of shareholders that has continuously held more than five percent of the company's securities entitled to vote on such proposal for at least one year prior to the submission date of the proposal;
- the shareholder or group of shareholders is eligible to file, and has filed, a Schedule 13G, including, pursuant to the proposed amendments to Schedule 13G, additional information regarding the shareholder's or shareholder group's background and its relationship to the company; and
- the proposal satisfies all other requirements of Rule 14a-8.

The Access Proposal also proposes revisions to the proxy rules that would facilitate greater online interaction among shareholders of a company and create opportunities for shareholders to form the requisite group in order to submit a binding bylaw proposal on shareholder access. The central component of these revisions is a clarification that a company or shareholder who has established or is operating an electronic shareholder forum would not be liable for information provided by a third party on the forum. The third party

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2. See "Speech by SEC Chairman: Opening Remarks at the SEC Open Meeting," at <http://www.sec.gov/news/speech/2007/spch072507cc.htm>

3. See SEC Release No. 34-56161, at <http://www.sec.gov/rules/proposed/2007/34-56161.pdf>.

4. See SEC Release No. 34-56160, at <http://www.sec.gov/rules/proposed/2007/34-56160.pdf>.

would, however, still be subject to liability for the content of those statements under federal securities laws.

It is important to note that in the Access Proposal, the SEC is attempting to avoid much of the criticism of its 2003 shareholder access proposals, in which the SEC was perceived to be impinging on state corporate law by seeking to require, pursuant to the proxy rules, that shareholders have the ability to nominate director candidates in a company's proxy materials. This time, the SEC has emphasized its focus on the objective of enhancing disclosure in order to promote the exercise of shareholder's rights under applicable state corporate law.

## IMPACT OF THE PROPOSALS

The SEC, by releasing these two proposals, seems to be attempting to gather a diverse range of comments from both sides of this contentious issue. We expect that the SEC will receive a range of commentary supporting each of the proposals. Once the comment period ends, the SEC will take final action on the proposals. It is possible that both proposals, or elements of both proposals, could be adopted, with the Status Quo Proposal being used as a basis to exclude shareholder-submitted bylaw amendments that do not meet the requirements set forth in the Access Proposal. This joint adoption approach would allow the SEC to justify its historical position on the exclusion of shareholder proposals, while at the same time achieving its objective of enhancing opportunities for greater shareholder participation in the director nomination process through increased disclosure. The final rules on shareholder access will likely play a significant role in the 2008 proxy season, and companies should be prepared to face rules that embody most, if not all, of the elements of the Access Proposal.

## LAWYER CONTACTS

For further information on the proposals or on submitting comments to the SEC, please contact your principal Firm representative or one of the lawyers listed below. General e-mail messages may be sent using our "Contact Us" form, which can be found at [www.jonesday.com](http://www.jonesday.com).

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