



## SEC PROPOSES RULES ALLOWING SHAREHOLDERS TO NOMINATE DIRECTORS USING THE COMPANY'S PROXY MATERIALS

On June 10, 2009, the Securities and Exchange Commission ("SEC") proposed new rules that would, under certain circumstances, allow shareholders to use the company's proxy materials to nominate directors. Currently, shareholders nominating a director must prepare (and pay for) their own proxy materials. Shareholders taking advantage of the new rules would be required to represent that they are not seeking to change the control of the company. The new rules would limit the number of board seats that could be obtained through this process to the greater of one director or 25% of the total number of directors. Accordingly, shareholders seeking a change in control of the company by replacing a majority of its directors would still be required to produce their own proxy materials.

In addition, the SEC-proposed amendments would enable shareholders, under certain circumstances, to include in the company's proxy materials proposals that would amend, or request an amendment to, a company's governing documents regarding director nomination procedures or related disclosures, as long as the proposals do not impose more onerous requirements on shareholders than the SEC's new rules.

In the release, the SEC describes competing policy arguments about the effect shareholder-nominated directors or shareholder-proposed nomination procedures might have on a company. For example, some believe that the presence of shareholder-nominated directors would make boards more accountable to shareholders, and that the current economic crisis provides evidence of a need for more director accountability. Others believe shareholder-nominated directors may focus primarily on the concerns of the nominating shareholder or group, and that the possibility of more contested elections could deter qualified candidates from seeking to serve as directors.

The highly controversial proposed rules follow earlier efforts by the SEC in 2003 and 2007 to address proxy access. The SEC is likely to receive extensive comments on the new proposals. In addition, it is probable there will be litigation challenging the SEC's authority to adopt the rules. In the meantime, federal legislation has been proposed that would grant the SEC such authority.

The proposed rules would apply to all companies subject to the SEC's proxy rules, other than those having only a class of debt registered under the Securities Exchange Act of 1934. The deadline for submitting comments on the proposed rules is August 17, 2009. The full text of the SEC release can be found [here](#).

### ***Shareholder Access to Company Proxy Materials to Nominate Directors***

As described above, the proposed rules would limit the number of board seats that could be obtained through the new shareholder nomination process to the greater of one director or 25% of the total number of directors. If the company received shareholder nominations for more than the maximum number allowed, the company would include the nominees on a first-come first-served basis.



To be eligible to utilize the company's proxy materials to nominate directors, a shareholder or group of shareholders must individually, or in the aggregate, beneficially own a specified minimum number of shares continuously for at least one year and intend to continue to hold them through the date of the election of directors. The minimum beneficial ownership thresholds are, for large accelerated filers, at least 1% of the company's securities that are entitled to be voted on the election of directors; for accelerated filers, at least 3%; and for non-accelerated filers, at least 5%.

The nominating shareholder must represent that the nominee meets the objective criteria for "independence" of the national securities exchange applicable to the company. The nominee is not required to meet independence requirements specific to membership on audit committees or that require subjective judgments. The nominating shareholder must also represent that neither the nominee nor the nominating shareholder has an agreement with the company regarding the nomination of the nominee. The nominee is not required to be independent of the nominating shareholder or group. The nominee's candidacy or, if elected, board membership, must not violate controlling state or federal law or the rules of the applicable national securities exchange.

In order to have a nominee included in the company's proxy statement and form of proxy, the shareholder(s) would be required to provide a notice on a new Schedule 14N. The Schedule 14N must be provided to the company and filed with the SEC not later than the date specified by the company's advance notice provisions or, if none, generally no later than 120 calendar days before the date the company mailed its proxy materials for the prior year's annual meeting. The notice must contain specified representations concerning the nominating shareholder's or group's eligibility to use the new rules, as well as disclosures similar to those currently required in a contested election. The company would be required to include in its proxy materials this information and, if requested by the shareholder, a statement of the shareholder's support of its nominee(s) not exceeding 500 words.

If a shareholder nomination is included in the company's proxy materials, the proxy card could not provide for voting by group; rather, a vote must be cast for each nominee individually. The company may identify any shareholder nominee as such and recommend how shareholders should vote.

Information provided by the shareholder(s) under the new rules would be subject to the current proxy anti-fraud rules, which prohibit false or misleading statements or omissions in connection with the solicitation of proxies.

The SEC's proposal includes an SEC no-action letter process modeled after the procedure currently used with respect to shareholder proposals submitted under existing Rule 14a-8, by which a company could seek to exclude a shareholder nomination.

The SEC has proposed a number of other provisions designed to facilitate shareholders' use of the new rules. For example, the proposed rules loosen restrictions on shareholders' ability to communicate with each other in connection with the formation of a nominating shareholder group, and permit communications in support of the nominee, generally as long as the shareholder does not seek the power to act as proxy and files all written soliciting material with the SEC.



***Shareholder Proposals Relating to the Director Nomination Process***

Rule 14a-8 of the SEC's current proxy rules requires companies to include certain types of shareholder proposals in the company's proxy statement. However, as indicated above, under the current rules, the company's proxy materials cannot be used by shareholders to nominate directors. In addition, Rule 14a-8 cannot be used to include a shareholder proposal that relates to a nomination or an election for membership on the company's board or a procedure for such nomination or election.

The SEC proposes to amend Rule 14a-8 to require companies to include in company proxy materials shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nominating procedures or disclosures related to shareholder nominations. Such a shareholder proposal could not impose restrictions on shareholders' ability to nominate directors that are more onerous than the proposed SEC rules described above; however, the proposals could provide for more liberal requirements. For example, a shareholder could propose a bylaw that permits any shareholder, no matter how many shares he owns or for how long, to nominate a full slate of directors using the company's proxy materials.

In the release, the SEC notes changes and potential changes to state laws that could lead to an increase in shareholder nominations of directors using the company's proxy materials that fall outside the parameters established by the proposed SEC rules described above. (For a discussion of related newly enacted provisions of the Delaware General Corporation Law, effective August 1, 2009, see our May 2009 Corporate & Securities E\*Bulletin by [clicking here](#).) The SEC's proposed rules require shareholders to provide similar notice and disclosures regardless of whether the shareholder nomination is being made under the new SEC rules or under state law or a company's governing documents.

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*Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:*

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