August 17, 2009

Via email: rule-comments@sec.gov

U.S. Securities and Exchange Commission
One Station Place
100 F Street, NE
Washington, DC 20549

Attention: Elizabeth Murphy, Secretary

Re: File No: S7-10-09; Release Nos. 33-9046; 34-60089; IC-28765
Facilitating Shareholder Director Nominations

Ladies and Gentlemen:

On behalf of the seven law firms listed below, we are writing in response to the request by the Securities and Exchange Commission (the "SEC") for comments on its release entitled "Facilitating Shareholder Director Nominations" (the "Proposal"), published on June 18, 2009.

I. Introduction and Overview

For the reasons we set forth in detail below, we recommend that:

- The SEC should amend Rule 14a-8(i)(8) to permit stockholders to utilize Rule 14a-8 for proxy access proposals.

- The SEC should not adopt proposed Rule 14a-11, or any revised prescriptive proxy access rule, until there has been sufficient experience with private ordering of proxy access under amended Rule 14a-8(i)(8) to permit the SEC to make a more informed decision as to whether a prescriptive rule governing proxy access is necessary and desirable.

- If the SEC disagrees with our view that a prescriptive proxy access rule is neither necessary nor desirable, it should not adopt such a rule any earlier than the 2011 proxy season. This would give the SEC the time to analyze and respond to the comments it will receive on its pending rule proposal without an artificial, and rapidly approaching, practical deadline related to the 2010 proxy season, with annual meetings for calendar year companies beginning in late March 2010. This delay would also give companies, stockholders and the SEC an opportunity to observe and learn from private ordering initiatives that we are confident will take place during the 2010 proxy season.

- Finally, any prescriptive proxy access regime should permit private ordering under state law so as to permit stockholders to modify the SEC's proxy access regime as they see fit, including by opting out of the SEC's proxy access regime in its entirety. In addition, to ensure workability and avoid the need for a special meeting of stockholders, boards should explicitly be permitted to adopt or amend proxy access bylaws in the period between annual meetings, subject to stockholder ratification at the next annual meeting.

Our overarching concerns about the structure and operation of the SEC's Rule 14a-11 proxy access proposal are as follows:

- *The SEC can achieve its goal of removing impediments in the proxy rules to proxy access by amending Rule 14a-8(i)(8) to permit stockholder proposals relating to the election of directors with far less complexity and disruption than a prescriptive "one-size-fits-all" rule.* SEC reliance on Rule 14a-8(i)(8) would also show far greater deference to the value of private ordering under state law which has been the hallmark of our federal system of corporate regulation for decades.

- *The SEC's proposed Rule 14a-11 will have the practical effect of foreclosing much of the potential scope and utility of private ordering in an area of great complexity and factual variation.* Proposed Rule 14a-11 would preclude companies and their stockholders from adopting any form of proxy access that is more "restrictive," thereby largely eliminating the flexibility and experimentation necessary to deal with the complex issues that inevitably will arise.

  - As discussed below, proposed Rule 14a-11 raises substantial "workability" issues. Many of these issues do not have one obvious solution, but rather can rationally be resolved in a number of different ways, illustrating that a "one-size-fits-all" approach is inherently flawed as a regulatory model for proxy access. There are over 7,000 public companies that would be subject to proposed Rule 14a-11 and the appropriate form of proxy access will depend upon a number of factors, including a company's state of incorporation, capital structure, board composition, stockholder base, size of capitalization, governance practices, financial performance, and strategic objectives. The strength of private ordering—its ability to accommodate and adapt to different circumstances and to provide flexibility for change—is the fatal weakness of a prescriptive rule.

  - Given the inherent complexity of delineating a proxy access regime, a single, national prescriptive rule is simply inadequate to address all of the issues and ambiguities that will arise, nor is it readily adaptable to unique or changed circumstances. Private ordering, on the other hand, not only allows flexibility of design but also provides an inherent capability of dealing with error, ambiguity and change of circumstance as companies and their stockholders gain experience with proxy access, without requiring the SEC continually to monitor, interpret and amend its access rules.

- *Private ordering under enabling state corporate statutes has proven responsive to changing stockholder views concerning other governance matters.* The past decade has witnessed a meaningful number of stockholder-led corporate governance changes, including, for example, widespread adoption of majority voting, elimination of classified boards and termination or modification of stockholder rights plans. This is not an aberration but has been driven by the success of stockholder proposals and the specter of withhold or against votes if such proposals are not implemented. In this regard, we note that, prior to the SEC's announcement of its current proxy access proposals, Delaware amended its corporate statute explicitly to enable adoption of a bylaw establishing a proxy access regime (and/or a proxy contest reimbursement policy) by board or stockholder action. In a related development, the committee responsible for drafting revisions to the Model Business Corporation Act (the "MBCA"), which has been adopted in whole or in part in over 30 states, has approved proposed amendments to the MBCA consistent with the new provisions of the Delaware corporate law. We expect many states will follow these leaders and modify their statutes to facilitate adoption of proxy access and proxy reimbursement bylaws. Moreover, "model" proxy access bylaws are emerging, including a concept draft of a proxy access bylaw drafted by the Shareholder Proposal Task Force of the ABA Committee on Federal Regulation of Securities. As a matter of policy and in the interests of federalism, the SEC should step back to allow these developments to flourish.

- *If the SEC adopts proposed Rule 14a-11, stockholders should have the option to opt out of proposed Rule 14a-11 either by a stockholder vote or ratification of board action.* We note the SEC's statement in the Proposal that "investors are best protected when they can exercise the rights they have as shareholders, without unnecessary obstacles imposed by the federal proxy rules." Yet proposed Rule 14a-11 would deprive stockholders of their ability to exercise their rights under enabling state laws to implement the specific form of proxy access that they believe best fits their particular company and fellow stockholders, or alternatively to choose to forego entirely the costs and burdens of proxy access. We think this result is wrong as a matter of policy and raises significant administrative law issues.[1]

- *Although the SEC accepts that Rule 14a-11 should not be available to stockholders who are seeking a change of control or more than a limited number of seats on the board, we have serious concerns that a number of provisions in the proposed rule, taken in combination, would have that effect:*

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[1] *See* Letter from Joseph A. Grundfest, The William A. Franke Professor of Law and Business, Stanford Law School, and Co-Director, Rock Center on Corporate Governance, Stanford University, to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission (July 24, 2009) (available at http://www.sec.gov/comments/s7-10-09/s71009-64.pdf).

- The ability of a single stockholder or group to nominate candidates constituting as much as 25% of a board at a single meeting.

- The ability to nominate and elect candidates constituting an additional 25% of the board the following year, even if any or all of the first group of access directors are re-nominated by the board as part of the board's slate.

- The lack of any independence requirement as between the nominating stockholder and its nominees, and the lack of any disclosure requirement about relationships and understandings between the nominating stockholder or stockholder group with other stockholders, thereby enabling the formation of undisclosed groups.

- The possibility of simultaneous proxy access nominations and a traditional proxy contest, permitting cooperation by the two sets of nominating stockholders, inclusion of the proxy access nominees on the traditional insurgent's proxy card, and active solicitation by the traditional insurgent and the proxy access nominating stockholders of the others' slate of candidates.

- The absence of any "bring-down" requirement for the certification of the absence of a control intent from the initial filing of the Schedule 14N.

- The absence of any limitation on the nominating stockholder's ability to launch a tender offer or commence a proxy fight for a period of time after its nominees have been elected.

- The exemption of a 5% or greater nominating stockholder or group from the disclosure requirements of Schedule 13D, even if the passivity requirements of Section 13(d)(5) of the Securities Exchange Act of 1934 (the "Exchange Act") were not met, which would allow the nominating stockholder or group to avoid disclosure of its plans and proposals for the company and its agreements with respect to stock of the company.

- The ability of a stockholder to solicit an unlimited number of other stockholders with respect to forming a nominating group, thereby allowing a stockholder to "test the waters" in terms of stockholder receptivity to a change in board composition and convert its solicitation for a nominating group into a conventional proxy contest on a widespread basis without the company or stockholders having the protection of the proxy rules.

- The ability of a stockholder to continue to solicit additions to its stockholder nomination group after it has met the threshold for a nomination, permitting formation of groups holding 10% or more of a company's voting securities without compliance with the proxy rules and Schedule 13D disclosure requirements.

If the SEC decides to adopt Rule 14a-11, our principal recommendations which we detail below are:

- The rule should not be effective for the 2010 proxy season. *See* Section III "Application of Rule 14a-11 — If the SEC Adopts Rule 14a-11, the Effective Date Should Be After the 2010 Proxy Season."

- Stockholders should be entitled to modify or opt-out entirely from the SEC's proxy access regime and boards should be entitled to adopt or amend proxy access bylaws subject to stockholder ratification of board action. *See* Section III "Application of Rule 14a-11 — If the SEC Adopts a Prescriptive Proxy Access Regime, Stockholders Should Have the Option to Opt Out of Proposed Rule 14a-11 by a Stockholder Vote."

- If a traditional proxy contest were commenced, the availability of Rule 14a-11 should be suspended. *See* Section III "Application of Rule 14a-11 — Simultaneous Proxy Access Nominations and Traditional Proxy Contest Rules."

- The ownership thresholds to determine eligibility to use Rule 14a-11 should be adjusted upwards to 5% for individual stockholders and higher thresholds for groups of stockholders. *See* Section IV "Nomination Eligibility — We Recommend Adjustments to the Proposed Ownership Thresholds."

- The number of persons solicited for the purpose of forming a stockholder nomination group should be limited to 10 absent compliance with the existing proxy rules. *See* Section IV "Nomination Eligibility — We Recommend Adjustments to the Proposed Ownership Thresholds."

- The nominee's candidacy and election should not violate the company's governing documents or corporate governance guidelines. *See* Section V "Nominee Eligibility and Independence Requirements — The Nominee's Candidacy/Election Should Not Violate the Company's Governing Documents or Corporate Governance Guidelines."

- Each nominating stockholder or stockholder group should be limited to one nominee. *See* Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups."

- The notice period for submitting proxy access nominees should be a uniform specified period prior to the anniversary of the mailing of the prior year's proxy statement and any proxy access rule should provide for a defined, reasonably short window period for stockholder nominations and not merely a deadline. *See* Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups."

- In the event the number of eligible proxy access nominees exceeds the 25% limit, the determination of which nominees to include should be based on the size of the nominating stockholder's holdings rather than a first-in system. *See* Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups."

- Short positions and derivatives should be disclosed, and the ownership requirements should require both voting and dispositive power on a continuous "net long" basis. *See* Section VII "Notice and Disclosure Requirements — The Proposed Rule 14a-11 Disclosure Requirements Fail to Include Critical Topics" and Section IV "Nomination Eligibility — Only Real (Net Long) Ownership Interests Should Count for Proxy Access."

- Persons or groups beneficially owning in excess of 5% of a class of voting securities who act in connection with a nomination should not have a per se exemption from Schedule 13D. *See* Section XI "Beneficial Ownership Reporting Requirements — Issues Under Schedules 13D and 13G."

We have organized this letter in twelve parts (including this Introduction and Overview) which focus on the proposed amendment to Rule 14a-8(i)(8) and on what we believe are the most important aspects of the prescriptive proxy access rule proposals. We emphasize, for the sake of clarity, that our detailed discussion of workability issues should be considered in the context of our fundamental view that the SEC should amend Rule 14a-8(i)(8) but not adopt any prescriptive proxy access rule.

II. Amendment of Rule 14a-8(i)(8)

As the SEC acknowledged in the Proposal, allowing stockholders to propose and vote on governance standards has led to significant reforms, most notably the majority voting provisions that have been adopted by many companies.[2] The proposal to amend Rule 14a-8(i)(8) would permit stockholders to submit proxy access proposals that are designed to fit a company's particular circumstances. Indeed, the amendment of Rule 14a-8(i)(8) would address what is identified in the Proposal as a key reason that stockholders' existing options to hold a board accountable are said to be of limited utility. In that connection, a company and its stockholders would benefit from the flexibility to adopt the type and form of proxy access standard that best

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[2] *See* RiskMetrics Group, 2008 Postseason Report 33 (2008) at 25 (available at http://www.riskmetrics.com/white_papers) (noting that according to Claudia Allen, chair of the corporate governance practice group at the law firm Neal, Gerber, and Eisenberg, as of June 2008 72.8% of companies on the S&P 500 had adopted some form of majority voting); s*ee also* Melissa Klein Aguilar, *Shareholder Voices Getting Louder, Stronger*, Compliance Week, Oct. 21, 2008 (quoting Claudia Allen, who "agrees that majority voting has 'become the *de facto* election standard among large public companies and is trickling down' to mid-cap and small-cap companies") (available at http://www.complianceweek.com/article/5113/shareholder-voices-getting-louder-stronger).

reflects the will of the stockholders, rather than a uniform, one-size-fits-all standard under proposed Rule 14a-11.

Accordingly, we believe that the SEC, in lieu of adopting Rule 14a-11, should amend Rule 14a-8(i)(8) specifically to permit stockholder proposals for proxy access (and for proxy contest expense reimbursement), regardless of whether such proposals are more or less restrictive than Rule 14a-11. We do not, however, support the manner in which the SEC proposes to accomplish this goal. The revised Rule 14a-8(i)(8) process would be far better served if the SEC merely eliminated the 2007 amendment to this exclusionary rule and substituted a provision explicitly permitting proposals on proxy access and proxy contest reimbursement proposals. This would remove any SEC-created impediments to the ability of stockholders to use private ordering to implement or recommend that their board implement proxy access and/or expense reimbursement.

We are troubled that the SEC's proposed wholesale revision of the election exclusion rule may be far more permissive than intended and lead to controversies about the eligibility under amended Rule 14a-8(i)(8) of stockholder proposals unrelated to proxy access and proxy contest expense reimbursement. In effect, the SEC proposal would convert a well-understood and time-tested principle-based exclusion into a new and untested prescriptive list of narrow exceptions. Amending the election exclusion to permit proxy access and proxy reimbursement proposals is sufficient to accomplish the SEC's stated purposes for its rule-making. The SEC's decision to reformulate the election exclusion in its entirety is neither within the SEC's articulated purpose for its rule-making, nor supported by any rationale in the Proposal.

Finally, we are troubled by the lack of transparency in the rule-making process to the extent the SEC, in formulating its proposed amendment to Rule 14a-8(i)(8), is explicitly relying on informal codifications of staff policies and interpretations under the existing exclusion. These policies and interpretations are not publicly available and have not been subjected to any formal rule making process. As a result, we are concerned that the SEC's proposed amendment to the exclusionary rule may have consequences that are not apparent to persons not privy to the non-public staff codifications on which the proposed amendment is based and, in addition, may have unforeseen or unintended consequences because of the limited nature of the proposed revised basis for exclusion.[3]

III. Application of Rule 14a-11

Amending Rule 14a-8(i)(8) first, and delaying consideration of Rule 14a-11, would enable the SEC to consider Rule 14a-11 on a more informed basis. Given the fundamental and complex nature of any workable proxy access regime, we believe the SEC should proceed with caution even if it is not prepared to reject Rule 14a-11 at this time.

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3 The SEC's reliance on informal codifications of staff policies and interpretations, which are not publicly available, for formulating Rule 14a-8(i)(8) raises administrative law issues similar to those that led the United States Court of Appeals for the Second Circuit to overrule the SEC's determination in *American Fed'n of State, County & Municipal Employees v. American Int'l Group, Inc.*, 462 F.3d 121 (2006).

However, in light of the possibility that the SEC may adopt Rule 14a-11 despite the serious misgivings of many commentators including ourselves, we have in this letter addressed various issues raised by proposed Rule 14a-11.

A. *If the SEC Adopts Rule 14a-11, the Effective Date Should Be After the 2010 Proxy Season*

1. Adoption of a Final Rule in Time for the 2010 Proxy Season Is Not Practical

We have serious reservations about the practicality of adopting a final proxy access rule in time for implementation for the 2010 proxy season. Among the more obvious reasons are (i) the shortness of the time frame in light of the need for a rule to be adopted and made effective sufficiently prior to the proposed 120-day cut-off date for proxy access nominations, particularly for companies with annual meetings in late March or early April 2010 (not to mention the time stockholders would need to form a nominating group if they so desired), (ii) the desirability of at least a 60-day waiting period between adoption of a final proxy access rule and its effective date, (iii) the complexity of the subject matter and (iv) the potential unintended consequences of such a fundamental change.

2. Deferral of Adoption Would Provide Valuable Experience

More fundamentally, we believe that it would be far preferable for the SEC to defer adoption of a prescriptive proxy access rule for one or more proxy seasons to gain the benefit of the private ordering that is likely to occur as a result of amending Rule 14a-8(i)(8) to permit stockholder proposals on access. We believe that stockholders will submit access proposals for the 2010 proxy season and that a number of companies will adopt or propose for stockholder adoption proxy access bylaws either in response to stockholder proposals or on their own initiative. These initial forays into private ordering are likely to be highly instructive for purposes of evaluating the need for a prescriptive SEC rule and the views of stockholders as to the desirable scope of its substantive provisions.

3. If an Opt-Out is Adopted, Companies Will Need Time to Transition

As noted above, if the SEC ultimately decides to adopt Rule 14a-11, we believe adoption for the 2010 proxy season is impractical because of the lack of sufficient transition time. The need for a transition period will be particularly acute if, as we strongly recommend below, the SEC adopts a final proxy access rule in 2009 with an opt-out regime. In order for an opt-out regime to be properly implemented, companies will need an annual meeting to allow stockholders to decide whether they prefer Rule 14a-11 or an alternative. Otherwise, companies could be subject to the confusing result of being subject to Rule 14a-11 in the 2010 proxy season and a different stockholder-approved alternative in the 2011 proxy season. A more investor-oriented approach would be for stockholders to consider Rule 14a-11 and various alternatives on an informed basis and then decide the appropriate response in 2010 that would apply for the 2011 season. This would afford companies the opportunity to evaluate and assess the need to adopt their own form of proxy access bylaws, and allow for the marketplace to implement proxy access as a result of stockholder proposals under a revised Rule 14a-8(i)(8) or on a company's own initiative. In any event, the resulting private ordering will inform the market and the SEC with respect both to the need for and desirability of a prescriptive SEC rule and the content of such a rule (including integrating such rules with the SEC's proxy disclosure and solicitation proposal published on July 17, 2009).

B. *If the SEC Adopts a Prescriptive Proxy Access Regime, Stockholders Should Have the Option to Opt Out of Proposed Rule 14a-11 by a Stockholder Vote*

If the SEC disagrees with our view that a prescriptive proxy access rule is not desirable, we recommend that the SEC, at a minimum, include in the final rules an ability for stockholders, either by adoption of stockholder-proposed bylaws or by ratification of board-adopted bylaws at the next annual meeting, to exempt their company from proposed Rule 14a-11. This exemption could be either a complete exemption from all proxy access (including Rule 14a-11) or the creation of an alternate proxy access regime. We believe an express opt-out provision in the final proxy access rules would mitigate concerns that we and others have that the Proposal would impose an inappropriate, cumbersome and potentially unworkable "one-size-fits-all" federalized approach to a governance topic that heretofore has been determined by private ordering under a combination of state law and company and stockholder agreement. Indeed, allowing an opt-out by stockholders would be, as mentioned earlier, consistent with the fundamental mission of the SEC to facilitate rather than foreclose stockholder rights.

Stockholders might choose various alternatives to proposed Rule 14a-11. For example, they could embrace the concept of proxy access but adopt modifications including the level of ownership, duration of ownership, type of ownership (*e.g.*, the Proposal does not address derivatives), maximum number of nominees, priority among nominees, relationships between nominating stockholders and nominees and the interplay between proxy access rights and traditional proxy contests. In that connection, stockholders could, with respect to their own company, be more concerned with the costs associated with proxy access than any possible benefits that may result from facilitating stockholder-nominated directors. Alternatively, a company's stockholders may prefer instead to adopt bylaws providing for the reimbursement of costs incurred by a dissident in connection with a proxy contest, or bylaws that entirely exempt the company from including stockholder nominees in its proxy materials. Indeed, the SEC raises the question whether Rule 14a-11 should not apply at all to a company that has adopted provisions for reimbursement of expenses incurred by a participant in the course of a solicitation in opposition to the company's directors.

Given the SEC's desire to respond to those who view the absence of proxy access as an impediment to effective governance, we understand its caution in facilitating alternatives to proxy access. At the same time, the SEC is aware of the strong policy arguments both for and against proxy access and the degree to which the intrusion into state law has become contentious. We believe that the July 24, 2009 letter to the SEC on behalf of the Delaware State Bar Association was particularly compelling in discussing how the Proposal deprives Delaware stockholders from exercising their state law rights to privately order proxy access and to adopt alternative governance rules.[4] If the SEC were unpersuaded by the benefits of relying on private

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[4] *See* Letter from James L. Holzman, Chair, Council of the Corporation Law Section, Delaware State Bar Association, to Elizabeth M. Murphy, Secretary, U.S. Securities and

ordering pursuant to a revised Rule 14a-8, then a Rule 14a-11 regime that includes an opt-out would be a possible, even if not our preferred, approach. The SEC would be facilitating stockholder rights but deferring to stockholders if they prefer an alternative.

Any final proxy access rule should also explicitly permit boards to act with respect to implementing or modifying a private ordering opt-out bylaw, subject to stockholder ratification at the next annual meeting. This ability would be critical, for example, if stockholders adopt a bylaw that proves unworkable or ambiguous in the absence of more detailed provisions. In any case, the board may want to effect the change in anticipation of the next annual meeting but not want to undertake the expense and burdensome process of calling a special meeting. We are cognizant of the policy issues that would arise if a board were to have the authority to bypass stockholders and unilaterally opt out of Rule 14a-11. Accordingly, we propose that the opt-out provisions of any final access regime allow the board to opt out (including in connection with the adoption of alternative bylaw provisions relating to stockholder nominations), subject to stockholder ratification at the next meeting (akin to a sunset provision if not ratified). This would be consistent with the general principle of stockholder primacy over proxy access but provide the board with the flexibility to address issues between annual meetings. The board would not be permitted to opt out of Rule 14a-11 retroactively (*e.g.*, once a notice to nominate a director pursuant to Rule 14a-11 has been filed).

C. *Simultaneous Proxy Access Nominations and Traditional Proxy Contest Rules*

The Proposal should suspend the availability of proposed Rule 14a-11 for any election of directors in which another party commences a solicitation in opposition subject to Rule 14a-12(c). If a company has already mailed its proxy materials to stockholders when a traditional proxy contest is initiated, the company should be able to amend its materials to remove the stockholder nominee. The premise of the need for Rule 14a-11 is that the nomination of directors by stockholders in opposition to board nominees is too expensive or otherwise too difficult. The existence of a traditional proxy contest, however, clearly demonstrates that the company has stockholders that are in a position to nominate directors without proxy access, and as such belies the need to facilitate that right through proposed Rule 14a-11.

Moreover, the SEC makes clear that proposed Rule 14a-11 should not be available where a nominating stockholder is seeking to change control of the company or gain more than a limited number of board seats. The practical effect, however, of a combination of a traditional proxy contest for the board and stockholder access nominations of up to a quarter of the board size could well result in significant, and possibly a majority, turnover of incumbent directors. This may be especially likely because the proposed access rules do not prohibit a nominating stockholder from recommending or endorsing, or indeed actively soliciting for, the dissident's candidates in the traditional proxy contest alongside its own nominees under Rule 14a-11, nor is there any restriction on the right of the dissident to endorse and solicit for the proxy access nominees. A related concern is that the dissident would be able to add proxy access

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Exchange Commission (July 24, 2009) (available at http://sec.gov/comments/s7-10-09/s71009-65.pdf).

nominees to its "short slate" proxy card under Rule 14a-4(d). Even if the final rules were to provide that any form of cooperation by the nominating stockholder under Rule 14a-11 with dissidents in a traditional proxy context is contrary to the required control certification, such a rule would not prevent the dissident from promoting the proxy access candidates or including their names on the dissident's proxy card or for the two groups of directors following successful election contests to form an alliance. Moreover, seeking to solve these problems by trying to prohibit or police the extent of relationships or understandings between a dissident group engaging in a traditional proxy contest and a nominating group availing itself of Rule 14a-11 is not practical. Accordingly, we conclude that the balance of benefits and risks does not justify subjecting stockholders to the risk of Rule 14a-11 being used in conjunction with a traditional proxy contest given that the objective of having stockholders exercise their rights to nominate directors is fulfilled by the traditional proxy contest outside Rule 14a-11.

Finally, we note that a simultaneous traditional proxy contest coupled with a proxy access proxy contest would likely be confusing to stockholders and fraught with technical issues. The source of these difficulties would start with the utilization of two proxy cards, one a so-called "universal" proxy card listing the board nominees and the access nominees (which we understand would be the exclusive proxy card that the company and the proxy access nominating stockholders would be allowed to use) and a second proxy card distributed by the dissidents in the conventional proxy contest. The dissidents would be entitled to and might include on the dissident card some or all of the proxy access nominees from the company's proxy card if the dissidents were proposing, as is often the case, a "short slate." The possibility of stockholder confusion when confronted with a universal proxy card containing more candidates than available seats and a second proxy card listing some of the same candidates but in combination with the dissident candidates appears to us far higher than in the usual proxy contest. In addition to voter confusion as to which proxy card to use and how to mark that card, there will be the inevitable issues of later dated proxies and potential confusion of intermediaries in the chain conveying voting instructions.

D. *Rule 14a-11 Should Not Apply to Controlled Companies*

We recommend that the SEC exempt "controlled companies" that are majority-owned by one or more stockholders from proposed Rule 14a-11. Since voting at these companies is pre-determined through the sizeable voting block held by the controlling stockholders, subjecting those companies and their stockholders to the proxy access process would impose costs without any possibility of the stockholder nominee's election. Stockholders of controlled companies would continue to have formal avenues to express their views to the company, such as through the Rule 14a-8 process.

IV. Nomination Eligibility

A. *We Recommend Adjustments to the Proposed Ownership Thresholds*

1. The Proposal Will Be Disruptive to Large Public Companies

Under proposed Rule 14a-11, a stockholder or group of stockholders would be eligible to nominate a director candidate and include the candidate in a company's proxy materials if the stockholder (or group) beneficially owns a minimum percentage of the company's stock (a "Threshold") for at least one year. As proposed, the Threshold would be 1% for large accelerated filers, 3% for accelerated filers, and 5% for non-accelerated filers. The Proposal explains that the SEC proposed different thresholds for the three categories of companies out of a concern that the rule could impact companies in those categories differently based on their size. In this context, the SEC suggests that it has designed the Thresholds so that larger companies would be more likely to receive qualifying Rule 14a-11 nominations than smaller companies because the SEC believes that the cost of funding and administering the Rule 14a-11 nominations would be less, on a relative basis, for larger companies than for smaller companies. We believe this theory is insufficient to justify having the burden of these new rules fall disproportionately on larger corporations. Relative ability to bear the direct out-of-pocket expense of a proxy access contest ignores other less tangible but more important costs of the proxy contest that would result from proxy access nominations, such as distraction of the board and senior management, potential loss of trust and collegiality in the board room following election of access nominees and the possibly disruptive agenda of the access directors. Accordingly, as described below, we recommend increasing the Thresholds.

2. We Question Whether the Data Used by the SEC Support the SEC's Proposed Thresholds

The SEC relied on two sets of data to support its proposal of the different Thresholds: (i) a sample of the ownership makeup of 5,327 companies that held meetings between January 1, 2008 and April 15, 2009 and (ii) a sample derived from CDA Spectrum based on filings made on Forms 13F in the third quarter of 2008. For each type of filer, the Proposal reported for each data set (i) the percentage of companies in the applicable category that have a single stockholder who meets the applicable Threshold and a threshold 2% higher than the proposed Threshold and (ii) the percentage (or range of percentages) of companies that have two or more stockholders, each of whom owns at least one-half of the applicable Threshold or the 2% higher threshold.

As an initial matter, we note that the SEC data contemplated nominations made only by a single stockholder or by groups of exactly two stockholders, each of which owns at least 50% of the Threshold. This way of analyzing the data could have been appropriate if the SEC were proposing that nominating groups be made up of no more than two stockholders meeting this specific ownership criteria. But the proposed rule allows any number of stockholders holding any number of shares to join together and aggregate their shares to meet the applicable Threshold. The data, therefore, fail to consider a large range of more likely scenarios (*e.g.*, nominating groups of three or more stockholders) under which stockholders could be eligible to make Rule 14a-11 nominations. Indeed, with unlimited aggregation of even the smallest stockholders, virtually **all** companies would have **some** group of stockholders who could satisfy the Threshold.

Second, the data presented in the Proposal grossly under-represent the number of companies at which even a group of just two stockholders could aggregate their holdings to meet the proposed Threshold, since the reported data is limited to situations where **each** of the two stockholders owns **at least 50%** of the Threshold. For example, an accelerated filer whose two largest holders held 2% and 1% of the total outstanding stock would not be included in the data even though those two holders would satisfy the 3% Threshold. The SEC's data provide no way to determine how many companies have two (or more) stockholders who could aggregate their holdings so as to meet the Threshold but at which no two holders each own at least 50% of the Threshold.

We therefore question whether the SEC has adequately considered the tremendous cost and disruption that groups of stockholders, acting together, could cause by making Rule 14a-11 nominations if the Thresholds are adopted as proposed. If an unlimited number of stockholders owning any shares of a company are allowed to be solicited and aggregate their holdings in order to meet the eligibility threshold, we would expect companies to receive significantly more Rule 14a-11 nominations, with substantially more cost and disruption, than the SEC has acknowledged.

3. We Recommend a 5% Threshold for Single Stockholders and Higher Thresholds for Groups of Stockholders

In order to preserve the balance between stockholder access and avoidance of the cost and disruption inherent in Rule 14a-11 nominations, we recommend two Thresholds that would be uniform for all public companies: (i) a 5% Threshold for a single stockholder, and (ii) a meaningfully higher Threshold (*e.g.*, 7% – 10%) for nominating stockholder groups.

As discussed above, neither the SEC's data nor its stated policy reasons support its proposal to establish different ownership thresholds for different size companies. On the contrary, the SEC's own data support our recommendation that the Threshold for large accelerated filers and accelerated filers be increased to the same 5% threshold that the SEC proposed for non-accelerated filers. A substantial majority of accelerated filers has at least one stockholder who owns 5% or more of its shares. Indeed, according to the SEC's data, compared to non-accelerated filers, *an equal or greater proportion of accelerated filers* has at least one stockholder who owns 5% or more of the outstanding shares, and at least two stockholders who own 2.5% or more of the outstanding shares. While the SEC did not report any data for large accelerated filers at the 5% threshold, our expectation is that the share distribution would be similar or even more concentrated than for accelerated filers, given the high level of institutional ownership of large accelerated filers.

A 5% threshold would be consistent with the level adopted in the North Dakota Publicly Traded Corporations Act in 2007, which, as discussed in the SEC's open meeting approving the Proposal, permits a company to provide a right of proxy access to stockholders who have owned more than 5% of its voting securities for a period of two years.[5] Furthermore, as a matter of policy, we believe that the SEC should consider a 5% threshold as a more conservative and incremental approach that would provide for experimentation and evaluation

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5 North Dakota Publicly Traded Corporations Act, N.D. CENT CODE § 10-35 (2007). It is also similar to the threshold for proxy access provided in the bylaws of RiskMetrics Group, Inc., which permits stockholders who have owned at least 4% of its shares for a period of two years to propose nominees.

before possible consideration of lower thresholds. This is more consistent with the policy position stated by the SEC in its Proposal:

> Amending our rules to provide for the inclusion of shareholder nominees for directors in a company's proxy materials is a significant change. Given the novelty of such a change, we believe it is appropriate to take an incremental approach as a first step and reassess at a later time to determine whether additional changes would be appropriate.[6]

In order to preserve a balance between stockholder access and avoidance of the cost and disruption inherent in Rule 14a-11 nominations, we also believe that the Threshold for nominating groups should be meaningfully higher than the Threshold for a single stockholder acting alone. Applying the same threshold to a unlimited group of stockholders as to a single stockholder undermines the efficacy of the threshold and, we believe, is inconsistent with the SEC's stated intent in the Proposal "that only holders of a significant, long-term interest in a company be able to rely on Rule 14a-11 to have disclosure about their nominees for director included in company proxy materials."

Adopting higher group ownership thresholds would still provide a substantial opportunity for stockholder access. Using the SEC's data, a substantial percentage of non-accelerated filers have at least two stockholders that each own 3.5% of the outstanding shares. As discussed above, the SEC's analysis substantially under-represents the number of companies with holders that could join together to satisfy a higher group threshold, so that the actual number of companies that could have eligible nominating groups would be substantially greater. While the SEC did not report any data for large accelerated and accelerated filers above a 5% threshold, our expectation is that substantially all such companies would have groups of perhaps two to four stockholders that could satisfy a meaningfully higher group threshold.

4. We Would Not Provide a New Proxy Rule Exemption for Activities in Connection with the Formation of Nominating Groups

As noted above, we are troubled by the ability for a stockholder to conduct a broad solicitation to form a group that is unlimited as to the number of stockholders and the aggregate amount of share ownership. We considered a number of alternatives to address this issue including requiring a minimum size for each stockholder and limiting the number of stockholders in the group. As we considered the best solution, we also noted proposed Rule 14a-2(b)(7), a related provision, that would provide an exemption from the proxy solicitation rules for any communication in connection with forming a nominating stockholder group.

Ultimately, we concluded that the best solution to address the formation of a group of unlimited size or unlimited aggregate ownership would be for the proposed new exemption not to be adopted, as described further below in Section IX "Application of Proxy Rules to Solicitation to Form a Group —The Proposed Exemption Is Not Appropriate." This would have the effect of limiting the exemption of solicitations to form a nominating group to

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6 Proposal at 29043.

solicitations of 10 persons under the existing exemption from solicitations pursuant to Rule 14a-2(b)(2), and would address the potential abuse associated with large scale solicitations. While a limit on exempt solicitations would not limit the actual size of the group, reducing the opportunity for testing the waters or running a shadow proxy contest would be addressed, which is a critical concern.

B. *Only Real (Net Long) Ownership Interests Should Count for Proxy Access*

The proxy access question is potentially complicated by the tactic currently popular among certain types of stockholders to disaggregate the economic and voting interests normally associated with share ownership to achieve some objective. The final rule should expressly state that derivatives do not count towards "beneficial ownership" in the context of Rule 14a-11. While there is disagreement around the application of derivatives in the Section 13(d) context, to which different policy issues may apply, there should be no doubt that derivatives do not count for determining eligibility for proxy access.

Similarly, in order to ensure that the interests of nominating stockholders are aligned with those of all stockholders, we believe it is important that nominating stockholders have had for the requisite one-year period both voting power and a "net long" economic interest in the shares of the company that are included for purposes of satisfying the Threshold. To that end, the final rule should provide that, for purposes of Rule 14a-11, (i) shares are not deemed to be beneficially owned unless the holder has both the right to vote and to dispose of the shares in question and (ii) shares beneficially owned by a holder are determined by offsetting any shares subject to hedging or another "short" interest that holder has in the company's stock, including through use of derivatives. Absent these conditions, there can be no assurance that stockholders who make Rule 14a-11 nominations have an economic interest aligned with the long-term (or even short-term) interests of the company and its stockholders.

C. *There Should Be Consequences If a Nominating Stockholder Sells Its Interest or Develops a Change of Control Intent Before the Meeting, or If a Director Candidate Fails to Obtain a Minimum Number of Votes*

As proposed by the SEC, Rule 14a-11 would require that the nominating stockholder (or each member of the nominating stockholder group) make a statement at the time it files its Schedule 14N that it intends to continue to own the requisite amount of securities through the date of the director election and certify that it has no plan or proposal to change the control of the company. We believe that these requirements are appropriate to ensure that, as of the filing of the Schedule 14N, nominating stockholders or groups have a "long-term interest" in the company and are not using Rule 14a-11 as a means of seeking a change of control. However, we believe that there should be meaningful consequences if the nominating stockholder or group, contrary to its stated intention, disposes of shares prior to the annual meeting so as to reduce its ownership below the Threshold or if the stockholder or group later develops a change of control intent. We submit that under these circumstances the purpose of the proxy access rules would not be served by permitting the continued candidacy of the proxy access nominee. Accordingly, we recommend that the final rules provide that in these circumstances the candidate would no longer be eligible for proxy access and the company would be permitted to issue supplemental proxy materials (including a new proxy card) to reflect the termination of the access candidacy.

In addition, we recommend that the nominating stockholder (or, in the case of a nominating stockholder group, any member of the group reducing its ownership level such that the group Threshold is no longer met or changing its control intent) should be barred from making another Rule 14a-11 nomination at the company for the next two annual meetings if it became disqualified because of a disposition of shares or a change in control intent. These limitations on subsequent nominations would provide an enforcement mechanism to protect the integrity of the access rules by helping ensure that the nominating stockholder or stockholders in fact have an appropriate long-term, non-control interest in the company.

We believe the final rule should also provide for consequences if a nominee fails to obtain a minimum number of votes at the annual meeting. We propose that, if a stockholder nominee fails to garner at least 25% of the vote, then the nominating stockholder (or, every member of the nominating group, as the case may be) be prohibited from making another Rule 14a-11 nomination (either alone or as a member of a nominating group) at the company for the next two annual meetings. This limitation would be generally consistent with the rationale for Rule 14a-8(i)(12), which allows companies to exclude proposals that have failed to garner minimum stockholder support in the past. In addition, such a rule would, in view of the limitation on the number of Rule 14a-11 nominees at any annual meeting, provide a greater opportunity for other stockholders to propose more viable candidates. The exclusion of groups whose candidates have failed to draw any meaningful support would appropriately balance the cost and disruption of proxy access with the benefits of greater stockholder participation in the nomination of directors.

V. Nominee Eligibility and Independence Requirements

A. *The Nominee's Candidacy/Election Should Not Violate the Company's Governing Documents or Corporate Governance Guidelines*

Among other changes in corporate governance of public companies in recent years, boards of directors of public companies now routinely perform annual self-evaluations and consider the attributes and characteristics of directors in order to assemble an effective board of directors.[7] In many instances, boards of directors codify the desired attributes – for example, age limits on directors or limitations on the number of boards on which a director serves – in the company's governing documents or in corporate governance guidelines or similar policies. Indeed, Section 141(b) of the Delaware General Corporation Law provides that a company's charter or bylaws may prescribe qualifications for directors.

[7] If Proposed Rule 14a-11 were interpreted to preclude application of non-discriminatory qualification standards to access nominees, it would be inconsistent with the spirit of Item 407(c)(2)(v) of Regulation S-K which implicitly recognizes that minimum qualifications are appropriate considerations for choosing director nominees. Additionally, proposed Rule 14a-11 would be inconsistent with the spirit of expanded disclosure regarding director qualifications and responsibilities as described in the SEC's proxy disclosure and solicitation proposal published on July 17, 2009.

We propose that any nominee proposed under Rule 14a-11 should be required to satisfy any non-discriminatory, generally applicable director eligibility standards set forth in a company's governing documents or corporate governance guidelines. To be applicable, any such standards must be publicly available (including by means of posting on the company's corporate website as required under the NYSE rules for corporate governance guidelines) and must apply, by their terms, to any nominee/director, whether nominated by the board of directors or a stockholder. As the company's board would be similarly constrained to nominating candidates in compliance with the standards articulated in the governing documents or corporate governance guidelines, it would be appropriate to require that a nominee under Rule 14a-11 also satisfy these standards. If the SEC is concerned about company attempts to frustrate the purpose of Rule 14a-11 by changing those criteria in the midst of the proxy access process, this concern could be addressed by limiting the requirement to eligibility standards set forth in governing documents or corporate governance guidelines as in effect on a date some reasonable number of days prior to the deadline (or beginning of the period) for submitting nominations under Rule 14a-11. We believe this approach strikes a reasonable balance between respecting the state law right of companies to adopt eligibility criteria for directors and the ability of stockholders to utilize Rule 14a-11.

B. *Even If Nominees Need Not Satisfy Company-Adopted Independence Criteria and Nomination Standards, They Should Include Disclosure Regarding Subjective Independence Determinations*

As noted in the Proposal, stock exchange rules on director independence have an objective standard as well as a subjective standard. In footnote 159 of the Proposal, the SEC correctly observed that a nominee would ultimately be subject to the subjective independence standard to determine whether he or she could serve on certain board committees. That subjective determination also could impact a listed company's compliance with stock exchange rules requiring that a board consist of a majority of independent directors.

There are good reasons why an access nominee should be required to meet the subjective determinations of independence by the board under applicable listing standards. In the absence of this requirement, companies would be at risk of noncompliance with stock exchange rules, which mandate a majority of independent directors, or the remaining independent directors could be burdened with additional duties by serving on a greater number of board committees requiring independent directors.[8] To address these issues, companies could be forced to increase the size of the board (beyond a size considered optimal) and conduct a search for additional directors who qualify as independent.

In the event the SEC decides not to revise Rule 14a-11 to require nominees to satisfy subjective listing standards for independence, we believe that a nominee's expected failure to satisfy such independence standards and the nominating stockholder's or group's knowledge of such expected failure is material to a stockholder's voting decision and should be required disclosure in the nominating stockholder's or group's Schedule 14N.

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8 For example, NYSE listing standards require that audit, compensation and nominating/governance committees be comprised solely of independent directors.

Further, many companies use a standard directors' questionnaire to elicit facts and relationships that bear on the board's determination of director independence. Any final proxy access rule should make clear that the proxy access nominee will be expected to complete such a questionnaire as soon as feasible following submission of the initial Schedule 14N so that issues of subjective independence can be identified prior to dissemination of the proxy materials.

C. *Nominees Should Be Independent From the Nominating Stockholders If a Stockholder or Group is Allowed to Nominate More Than One Candidate*

As noted in the Proposal, many companies remain concerned about nominees not being independent from nominating stockholders particularly in the context of "special interest" or "single issue" directors who might advance the interests of the nominating stockholder over the interests of stockholders generally. We share this concern which would be substantially heightened if such directors could constitute 25% of the board with the attendant implications for a change of control event. If the SEC adopts our recommendation to limit each nominating stockholder or group to one nominee as described below in Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups," then we would agree with the SEC's decision not to require independence between nominating stockholders or groups and their nominees under Rule 14a-11, provided that the relevant relationships are disclosed on Schedule 14N, as described below in Section VII "Notice and Disclosure Requirements — The Proposed Rule 14a-11 Disclosure Requirements Fail to Include Critical Topics — Relationship Between the Nominating Stockholder and Nominee."

If, however, the SEC determines that it would allow a stockholder or group to nominate more than one candidate, we urge the SEC to revisit its decision not to require independence between a nominating stockholder or group and its nominees under Rule 14a-11.[9] A lack of an independence requirement between multiple nominees and the nominating stockholder could give rise to control issues as up to one-quarter of the board could be beholden to a single nominating stockholder or group. In addition, lack of independence can give rise to "single issue" or "special interest" directors that can cause balkanization of boards that is inimical to the interests of stockholders at large. Also depending on the issue and the interests or conflicts of the "special interest" directors, boards would be required to more frequently establish ad hoc special committees that exclude the "special interest" director. An independence requirement would also help address the risks relating to maintaining the confidentiality of non-public information available to directors and of the fiduciary obligations of directors with respect to the confidential nature of boardroom discussions. We believe requiring a nominee's independence[10] from each nominating stockholder in the case where the nominating stockholder or group is allowed multiple nominees strikes the appropriate balance between stockholders and

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9 We note that when the SEC first proposed proxy access in 2003, an access nominee was required to be independent from the nominating stockholder.

10 "Independence" for these purposes could be defined by reference to the objective independence standard of the relevant stock exchanges, substituting each nominating stockholder for the company.

companies. We note that in the event a stockholder wishes to nominate persons who are not independent from the stockholder, it may continue to do so outside of the Rule 14a-11 framework.

VI. Maximum Number of Stockholder Nominees and Use of "First-In" Process

A. *Maximum Number of Stockholder Nominees*

1. Maximum Number of Nominees Should Be 25% of Board Seats That Are Not Subject to Pre-Existing Contractual Nominating Rights

Companies and their nominating committees are at times restricted in their ability to nominate director candidates by contractual obligations that give a particular stockholder or stockholders the right to nominate or appoint one or more directors to the board. These arrangements, which frequently arise in the context of a new-money or strategic investment in the company, result from stockholders wanting to ensure that their interests will be represented on the board. This is of course the same overarching objective as that reflected in the Proposal. For companies with contractual nominating rights, we believe that proposed Rule 14a-11(d)(1) should be modified so that the maximum number of nominees that stockholders may nominate under Rule 14a-11 may not exceed 25% of the "free" seats on the board – *i.e.*, only those board seats that are not subject to a contractual nomination right that existed as of the date of the submission and filing of a Schedule 14N. Without this modification, companies may not be able to offer contractual nominating rights to stockholders without running a heightened risk of a change of control, with the effect of facing increased costs of capital and decreased strategic alternatives. Directors nominated by stockholders with contractual nominating rights are aligned neither with management nor with the Rule 14a-11 stockholders. We believe the sensible result is for the rule to, in effect, take them off the table, and key the number of permitted stockholder nominees to the number of nominees that the nominating committee has freely available to it.

This approach is consistent with stock exchange rules that carve out such contractual nominees from the requirement that board nominees be subject to an independent nominating committee's recommendation.

2. Agreements Among Companies, Nominating Stockholders and Nominees Should Not Be Precluded

Proposed Rule 14a-18(d) would require that the nominating stockholder represent that neither it nor the nominee has an agreement with the company regarding the nomination. The proposed instruction to this Rule clarifies that negotiations with the nominating committee to have the nominee included on the company's proxy card as a board nominee, where those negotiations are unsuccessful, or negotiations that are limited to whether the company is required to include the nominee for director on the company's proxy card in accordance with Rule 14a-11, would not be considered a direct or indirect agreement with the company.

We do not believe that the eligibility criteria should include this proposed prohibition on agreements, as it would inhibit beneficial negotiations among nominating stockholders, nominees and nominating committees. In prior proposals, those who submitted comments expressed a great deal of concern that the introduction of proxy access could be extremely contentious and could have a disruptive effect on board dynamics and board operations. These concerns persist, so every effort should be made to encourage the parties involved to work toward a mutually agreeable solution. Promoting (or at least not deterring) these discussions would not in any way thwart the objective of the Proposal to facilitate stockholders' ability to nominate directors, as the impetus for these negotiations would come from eligible stockholders exercising their Rule 14a-11 right, and the decision whether a negotiation would result in an ultimate settlement with the company would be made solely by those stockholders. A nominee upon whom both a nominating stockholder and the company can agree has in fact met a higher standard by addressing the needs of each side.

To incentivize constructive negotiations, a proper Rule 14a-11 nomination that is withdrawn following negotiations between the company and the nominating stockholder should not open up an additional Rule 14a-11 slot for another nominating stockholder or group. Accordingly, proposed Instruction 2 to proposed Rule 14a-11(d) should be modified so that any stockholder nomination of a candidate for election that becomes the subject of an agreement between the company, nominee and nominating stockholder after the submission and filing of a Schedule 14N will continue to be included in calculating the maximum number of nominees permitted under proposed Rule 14a-11(d). Otherwise, companies would simply be inclined to wait until the Rule 14a-11 submission deadline has passed before coming to an agreement with a nominating stockholder.

Encouraging negotiations could in fact empower stockholders more than merely providing them an opportunity to make nominations for directors for inclusion in a company's proxy materials, as a company may agree to directly appoint or nominate the candidate presented by the nominating stockholder, making it much more likely that such a candidate will be elected to the board. As demonstrated by the numerous stockholder proposals submitted under Rule 14a-8 each year that are later withdrawn by the stockholders after discussions with companies, companies and their stockholders often do reach agreement.[11] Surely this is a more likely outcome when the nominating stockholder would not risk loss of eligibility to make an access nomination and the company would not expose itself to inclusion in the proxy materials of another stockholder nominee if it reached a negotiated agreement with the nominating stockholder.

3. Incumbent Proxy Access Directors and Dissidents Re-Nominated by the Company Should Count Toward Determination of the 25% Maximum

We encourage the SEC to count toward the calculation of the maximum number of stockholder nominations available for any election in any given year all directors initially nominated pursuant to Rule 14a-11 and elected, within at least two years, who are re-nominated by the company. This would include any director who was initially nominated by the submission and filing of a Schedule 14N and was subsequently elected pursuant to an agreement among the company, the nominee and the nominating stockholder to include the nominee on the company's

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[11] The Proposal itself, in footnote 223, encourages companies and stockholders to attempt to resolve disputes independently without engaging the SEC staff.

slate.[12] A company's board should be encouraged to successfully integrate an elected stockholder nominee into the life of the board, in order to promote effective functioning of the board and board stability. In addition, there is a learning curve for a new director to become familiar with a company's business, operations and industry and, once a company has devoted the resources to educating the director, continued service of that director should be promoted.

Absent such a continued status as an access director, any proxy access rule would discourage boards from re-nominating access directors even if a board or nominating committee determines that a stockholder-nominated director meets the board's own qualifications and criteria for re-nomination. If the access directors were re-nominated by the board and new nominations are made under Rule 14a-11, there could be turnover of up to 50% of the board seats within one year, an untenable risk that could cause a board not to re-nominate the previously elected Rule 14a-11 directors. Under the proposal, companies with staggered boards are able to count toward the calculation of the maximum number of stockholder nominees for an election any currently serving directors who were initially elected as stockholder nominees if their terms extend past the date of the annual meeting, effectively continuing the status of these incumbent directors for their entire (typically three-year) term. This suggests that companies that elect directors annually should also be able to take into account incumbent directors who were initially nominated pursuant to Rule 14a-11 for purposes of determining the maximum number of stockholder nominees for the same period. Proxy access is not an end to itself but rather a means to greater stockholder participation. If that has been achieved, to subject the company annually to the cost and disruption of a proxy access election contest is not an appropriate balancing of the costs and benefits of proxy access.

Similarly, if a dissident nominee is previously elected to the board outside of the Rule 14a-11 process and is re-nominated by the board in a subsequent year, this nominee should count toward the calculation of the available nominee slots under Rule 14a-11 for at least two years so long as he or she continues to serve, or is re-nominated to serve, on the board. This is consistent with the SEC's goal of facilitating a stockholder's right to nominate and elect directors to increase board accountability. Additionally, if a board settles with a bona fide conventional dissident stockholder who has commenced (or publicly stated an intent to commence) a proxy contest by agreeing to include the dissident's nominees on the board's slate, the settlement should also reduce the number of slots available under the 25% maximum provided under Rule 14a-11. Counting dissident directors against the 25% maximum also has the important benefit of reducing the otherwise significant risk that the proxy access directors and dissident directors would combine to effect a change of control.

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12 Proposed Instruction 2 to proposed Rule 14a-11(d) would therefore be modified so that any stockholder nomination of a candidate for election that becomes the subject of an agreement between the company, nominee and nominating stockholder after the submission and filing of a Schedule 14N will continue to be included in calculating the maximum number of nominees permitted under proposed Rule 14a-11(d).

B. *Allocation of Nominees Proposed by Different Stockholder Groups*

1. The SEC Should Adopt a Window Period Rather Than a Deadline for Submitting Nominees

The Proposal asks whether there should be a specified range of time in which a stockholder is permitted to submit a nominee instead of just a deadline. We agree with the need for a specified range, in order to avoid turning the proxy season into a year-round focus for both nominating stockholders and companies. If the SEC rejects our suggestion detailed below to abandon the first-in standard, then absent a window period for nominations, a nominating stockholder is legitimately motivated to make a submission as early as possible – for example, sending a Schedule 14N notice for the annual meeting in 2012 as soon as the deadline for nominations for the 2011 annual meeting expires (and, perhaps, even earlier than that). This may mean that a Schedule 14N is submitted in November 2010 for an annual meeting to be held in May 2012 – almost a year and a half in advance of the meeting.

The race to be first also creates the potential that a nominating stockholder would be encouraged to submit a proposed nomination before it is able to consider and evaluate a company's current board and governance structure. It may even encourage a nominating stockholder to make a submission as a mere placeholder, with the possibility of being withdrawn later (perhaps after the nominee submission deadline) if the stockholder decides to focus on another company instead. The absence of a specified range of time and the use of a deadline therefore harms nominating stockholders as well as the company and its other stockholders who might be precluded from the opportunity to vote on the stockholder nominee.

Even if the SEC adopts the proposal set forth below to substitute a largest holdings standard in place of its proposed first-in standard, we think a range of time for valid notices of proxy access nominations is needed. Otherwise, an early filer of a proxy access notice will set a benchmark that may encourage other nominating stockholders to form a larger group, so as to ensure its priority for its nomination. Encouraging a competition among rival nominating stockholder groups over an extended period, to see which can form the largest group strikes us as not only being wasteful and disruptive, but also inconsistent with the SEC's stated objective of not allowing proxy access to be a vehicle for potential change of control events.

Accordingly, we recommend that the SEC provide in any final access rule a reasonable but limited window for nominations, such as no earlier than 150 and no later than 120 days prior to the anniversary of the date the company mailed its proxy materials in the prior year.

2. Each Nominating Stockholder or Group Should Be Limited to One Nominee

Consistent with the Proposal's overall intent not to permit Rule 14a-11 to raise the potential for a change in control of the board, each nominating stockholder or group should be limited to one nominee. We are concerned that permitting a single stockholder or group to nominate up to 25% of a board could give rise to the kind of significant influence that the SEC itself recognizes can represent control, particularly when one distinguishes between "actual" control (*e.g.*, majority) and control through significant influence. Limiting each nominating stockholder to one nominee would satisfy the SEC's goal of providing stockholder access while allowing nominees to be distributed among a broader stockholder base. If a stockholder or group is seeking to nominate additional candidates, which could more easily give rise to control issues, they should be required to use the traditional proxy contest mechanism. In order to prevent circumvention of this limit, any access rule should also make clear that a stockholder may only participate in one stockholder nominating group.

3. Allocate Excess Nominations Based on Ownership Size Rather Than the First-In Process

To the extent a company receives more stockholder nominations than seats available for Rule 14a-11 nominees, proposed Rule 14a-11(d)(3) provides a first-in standard. Instead of a first-in approach, we recommend that the available slots be allocated to nominating stockholders based on the size of their holdings held for the requisite holding period. This would avoid the race to be first-in, remove the company from making judgments in terms of time of receipt of Schedule 14N, remove the SEC staff from adjudicating the inevitable disputes, and allow nominating stockholders to wait and review candidates proposed by other nominating stockholders before deciding to file, since they would not have an incentive to race to be first. The concerns the SEC raised regarding certainty and administrative difficulties can instead be addressed by revising the timing for the submission of a notice on Schedule 14N, as we suggest elsewhere.[13] A specified date range that provides companies with timely notice would give companies sufficient opportunity to review the information in Schedule 14N, determine how to allocate nominees, and prepare their proxy materials. This would substantially address one of the key concerns that led the SEC to select the first-in standard.

The SEC was also concerned that choosing on the basis of size was not fair to smaller stockholders whose notice is received first. As suggested, we believe that focusing on the timing of notice prioritizes the wrong attributes. We believe that a larger stockholder has a greater stake and is more likely to actually represent the interests of stockholders generally. In the case of nominating groups, we would not simply allocate on the basis of the largest group, however, as this would incentivize the formation of large groups simply to win the "tiebreaker." Rather, we would allocate based on the largest stockholder within any qualifying group. This is consistent with our recommended policy of favoring the stockholder with the largest stake.

VII. Notice and Disclosure Requirements

A. *The Proposed Rule 14a-11 Disclosure Requirements Fail to Include Critical Topics*

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13 *See* Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups — The SEC Should Adopt a Window Period Rather Than a Deadline for Submitting Nominees" and Section VII "Notice and Disclosure Requirements — Advance Notice Bylaws Should Not Override Rule 14a-11 Timing Requirements."

Proposed Rule 14a-11 requires nominating stockholders to provide notice of their nominations to companies on Schedule 14N, which would include certain enumerated representations and disclosures required by proposed Rule 14a-18. We support the concept of the new Schedule 14N because the required disclosures would promote greater transparency with respect to nominations made under Rule 14a-11.

We believe Schedule 14N should be expanded to provide the following additional specific areas of disclosure to ensure that stockholders have available to them sufficient information to make informed decisions respecting their franchise. The additional disclosures we are proposing are neither overly burdensome nor a deterrent to stockholders' exercise of their right to nominate directors. We also note that many companies have advance notice bylaws that require additional information from nominating or proposing stockholders, and nothing in the SEC rules should be read to render these provisions unenforceable if they are permissible under state law.

1. Relationship Between the Nominating Stockholder and Nominee

As indicated above, if the SEC determines that it will allow a stockholder or group to nominate more than one candidate, we propose that the SEC revisit its decision not to require independence between a nominating stockholder or group and its nominees under Rule 14a-11. If, however, the SEC declines to require this independence, we think that greater disclosure concerning the relationships between the nominating stockholder or group members and the nominee are essential to enable all other stockholders to exercise fully informed judgments. While the SEC's point that Rule 14a-11 nominees, if elected, will be subject to the same fiduciary duties as company-nominated directors is well-taken, we do not believe that this should preclude stockholders from having a more detailed understanding of relationships that may exist between nominating stockholders and their nominees in order to make informed voting decisions.[14] Depending on the nature of such relationships, reasonable conclusions might be drawn about unique political, economic or other interests that nominees might bring to the board room. We view such disclosure as neither an impediment to the nomination of directors nor inconsistent with the SEC's goal of replicating an in-person meeting.

We therefore believe that the right balance is to require more information in Schedule 14N about the nature of relationships between nominating stockholders and nominees, including a nominee's (i) familial relationships with a nominating stockholder or group member, (ii) ownership interests (or other participation) in a nominating stockholder or group member or any of their affiliates, (iii) employment history with a nominating stockholder or group member or affiliates, (iv) prior advisory, consulting or other compensatory relationships with a

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[14] This requirement would be consistent with the recognition elsewhere in the SEC's disclosure rules as to the importance of information relating to the source of director nominations, including Item 401(a) of Regulation S-K (requiring disclosure of any "arrangement or understanding" between a director and any other person "pursuant to which he was or is to be selected as a director nominee") and Item 407(c)(2)(vii) of Regulation S-K (requiring disclosure of the category of person that recommended a nominee to the nominating committee).

nominating stockholder or group member or affiliates and (v) agreements with a nominating stockholder or group member or affiliates, other than relating to the nomination.

2. Disclosure Regarding the Nominating Stockholders

We recommend requiring similar disclosure from nominating stockholders on Schedule 14N as those considered by the SEC in the 2007 release regarding stockholder proposals that was subsequently not adopted. The 2007 proposal would have required the nominating stockholder to disclose, among other things, (i) any discussion regarding the stockholder nomination between the nominating stockholder and a proxy advisory firm during the 12 months prior to the formation of any plans or proposals regarding a possible access nomination, or during the pendency of any proposal or nomination and (ii) any holdings of more than 5% of the securities of any competitor of the company. The SEC stated in its Proposal that requiring such additional disclosure in the current proposal may deter stockholders' exercise of their right to nominate directors. While the benefit of additional disclosure should be carefully weighed against the burden imposed on nominating stockholders, we believe, in this case, that the balance is heavily in favor of requiring disclosure. These additional disclosure requirements do not seem overly burdensome and would provide valuable information to stockholders. We further observe that since the SEC published the Proposal, it has also proposed significant additional disclosure requirements for annual meeting proxy statements in an effort to be sure stockholders have all relevant material information in connection with their votes at annual meetings. We believe that this effort to increase transparency and stockholder information applies equally, if not more so, to proxy access election contests.

In addition, as described above in Section V "Nominee Eligibility and Independence Requirements," we believe matters relating to subjective independence should be disclosed in Schedule 14N.

3. Duration of Holdings

We recommend requiring disclosure regarding the specific length of time for which the nominating stockholder or each member of a nominating group has held the required number of securities. As proposed, Rule 14a-11 would only require verification that, as of the time that notice was given to the company on Schedule 14N, the nominating stockholder or each member of the nominating group has continuously held the securities for at least one year, as well as disclosure of the nominating stockholder's or group member's two-year trading history in the company's securities. We recommend additional disclosure stating the total duration of the holding period of the eligible securities for the nominating stockholder or each member of a group. We believe this information will be important to stockholders in making their voting decisions.

In addition, we note that Item 5 of proposed Schedule 14N calls for the filing of a statement by each record holder of securities being used by a nominating stockholder to establish eligibility under a Threshold, verifying that the nominating stockholder "continuously" held the securities for at least one year. Although the concept of verification of the required holding period is warranted, in most cases the record holder will not be able to provide the verification because of the structure of the custodial system. The vast bulk of voting securities are held of record by the Depository Trust Company ("DTC"), as a central depositary. DTC, we understand, keeps its books on a "net clearing" basis and, accordingly, is not able to ascertain how long any shares have been held by the institution depositing those shares at DTC. Moreover, many of the depositing institutions are themselves custodians for other intermediaries in an ownership chain than may be several layers deep. To deal with these issues, Item 5 should be revised to require the verification statement from the broker, dealer or other custodian who holds the shares directly for the beneficial owner and not from custodians and depositories higher up in the custodial chain.

4. Short Positions and Derivatives

As previously discussed in Section IV "Nomination Eligibility — Only Real (Net Long) Ownership Interests Should Count for Proxy Access," in order to be eligible under Rule 14a-11, a nominating stockholder should be required to have held, for the prescribed period, the required net long position necessary to satisfy the Threshold. To be sure, stockholders would be required to give details of derivatives arrangements due to the requirement, under proposed Rule 14a-18, to make the disclosures that would be required under Item 5(b)(viii) of Schedule 14A. Nonetheless, given the fundamental importance of this information as it relates to the nominating stockholder's true economic exposure to the company, companies and stockholders should be entitled to the benefit of additional information regarding "empty voting" arrangements, short positions, share lending arrangements and other uses of equity derivatives, such as copies of agreements, arrangements, understandings and plans or proposals with respect to such derivatives.

We note in support of this position that RiskMetrics Group has provided in its 2009 updates of its domestic corporate governance policy that it will generally support advance notice bylaws intended to ensure full disclosure regarding a stockholder's economic and voting position in a company.[15] Moreover, the required information would be functionally equivalent to that called for under Item 6 of Schedule 13D. We also submit that requiring such disclosure is not burdensome, since it should not be difficult for stockholders to access records of transactions they have entered into for the considered purpose of affecting their economic exposure to, or voting rights in, a company.

5. Affiliates of the Nominating Stockholder

We believe that Schedule 14N should require further disclosure about affiliates of nominating stockholders. This seems to us obvious in the case of controlling entities, but we believe it is equally necessary in the case of controlled entities. Third parties affiliated with nominating stockholders may have special interests or reputational aspects which could give stockholders additional insight into the nature and purpose of the candidacy and the likely views of the nominee. In order to mitigate disclosure regarding affiliates that could be potentially

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15 RiskMetrics Group, U.S. Corporate Governance Policy, 2009 Updates, Nov. 25, 2008 at page 14 (available at www.riskmetrics.com/policy).

burdensome, the disclosure requirement could be limited to those affiliated entities in which the ownership relationship is 20% or more.

B. *Exclusion of Nominees If Information in the Schedule 14N is Materially False or Misleading*

While a company is under no independent duty to verify the information provided to it on Schedule 14N, we do not believe that Rule 14a-11, as drafted, provides sufficient clarity as to the measures a company may take in the event that information provided by nominating stockholders via their notice is materially false or misleading. As a preliminary point, we submit that the SEC should add the words (i) "or other statement" after "No representation or certification" in Rule 14a-11(a)(5) and (ii) "or any other disclosure required by the registrant's governing documents" after "paragraph (c) of this section" in Rule 14a-11(a)(5), the combined effect of which would be to clarify that materially false or misleading statements in any of the information provided on Schedule 14N or to the company in connection with a nomination in accordance with such company's governing documents would be grounds for excluding the nominating stockholder's nominee. We further propose that the words "or permitted" be added after the first "required" in Rule 14a-11(a)(5) in order to clarify that materially false or misleading statements in the nominating stockholder's 500-word supporting statement, which is permitted but not required to be included in the Schedule 14N, would be grounds for excluding the nominee.

More generally, we recommend that the SEC address the issue of excluding nominees as a result of materially false or misleading statements in two respects: (i) clarify that the process for excluding nominees for false and misleading information should not be subject to the 14-day deadline prescribed by proposed Rule 14a-11(f)(3) and (ii) allow exclusion upon a good faith showing if the false and misleading statements are found after the deadline for the company's opportunity to seek no-action relief.

The SEC should clarify in Rule 14a-11(f)(3) that, similar to existing Rule 14a-8(f), only procedural and eligibility deficiencies are subject to the 14-day deadline for challenging a Rule 14a-11 nomination after receipt of a Schedule 14N.[16] In that connection, the SEC should specify that, consistent with current Rule 14a-8(i)(3) for stockholder proposals, deficiencies under the Rule 14a-11(a)(5) materially false and misleading standard are not considered "procedural or eligibility" deficiencies that are subject to Rule 14a-11(f)(3).[17] As one of the enumerated bases for exclusion of stockholder proposals under Rule 14a-8(i), instead of Rule 14a-8(f), companies can submit a no-action letter request 80 days before mailing their proxy materials to exclude stockholder proposals for false and misleading statements, without having to first indicate that they intend to exclude the proposal on that basis in a letter to the proponent within the first 14 days of receipt of the proposal. Similarly, Rule 14a-11(f)(7) should

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[16] This approach is consistent with the language in Rule 14a-11(f)(5).

[17] In addition to Rule 14a-11(a)(5), we recommend that the SEC specify that deficiencies under Rule 14a-11(a)(1) (which is analogous to Rule 14a-8(i)(1) and Rule 14a-8(a)(i)(6)) and Rule 14a-11(a)(2) (which is analogous to Rule 14a-8(i)(2)) also fall outside the "procedural and eligibility" deficiencies subject to Rule 14a-11(f)(3)-(5).

be amended to permit a company to seek no-action relief at any time 80 days before the mailing of its definitive proxy statement (without first following the procedures set forth in Rule 14a-11(f)(3)-(5)) in the case of a deficiency under Rule 14a-11(a)(5) or other deficiencies that do not fall within the "procedural or eligibility" categories.

With respect to the consequence of information being discovered to be false or misleading subsequent to the beginning of the 80-day period before the company files its proxy materials and prior to the mailing, the company should be able to exclude the nominee from its proxy materials by notifying the nominating stockholder and providing its no-action letter submission to the SEC. We therefore suggest a clarifying instruction to Rule 14a-11(f)(7) stating that a good faith showing that the material misstatement or omission was found after the 80-day deadline would presumptively constitute "good cause" for missing the deadline.[18] Moreover, if the materially false or misleading statement or omission is not discovered until after the definitive proxy has been mailed, the company should be free to issue supplemental proxy materials, including a new proxy card, eliminating the nominee from consideration and to not count at its annual meeting any ballots purporting to vote for the dropped nominee.

C. *Advance Notice Bylaws Should Not Override Rule 14a-11 Timing Requirements*

In order to ensure adequate time for the actions required in connection with the proxy access due dates, we recommend that the SEC make the deadline for receiving Rule 14a-11 proposals for all companies 120 days before the anniversary of the prior year's mailing of proxy materials and consistent with the window period described above in Section VI "Maximum Number of Stockholder Nominees and Use of "First-In" Process — Allocation of Nominees Proposed by Different Stockholder Groups — The SEC Should Adopt a Window Period Rather Than a Deadline for Submitting Nominees." Any period less than 120 days prior to mailing, based on a particular company's advance notice bylaws, will simply not be practical under the dispute resolution time periods set forth in Rule 14a-11(f). For example, how could companies with the most common form of advance notice bylaw requiring only 60 or 90 days notice before its annual meeting notify the SEC 80 days before they file their proxy statements of

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18 Separately, and in response to a request for comment in the Proposal, we further suggest an additional clarifying instruction to Rule 14a-11(f)(7) stating that failure to meet the 80-day deadline as a result of the company's transition from full set delivery of proxy materials to the SEC's notice and access regime will presumptively constitute "good cause". In such circumstances, the requirement of Rule 14a-16(a) to make proxy materials available at least 40 calendar days prior to the meeting will mean, effectively, that the deadline for stockholders to propose directors – 120 days before the anniversary of the prior year's mailing – will actually likely be much less than 120 days from the required date of the current year's filing. The timing requirements for communications with nominating stockholders under Rule 14a-11 may therefore result in the company missing the 80-day deadline prior to the date of the filing to provide the SEC with notice of its decision to exclude a Rule 14a-11 stockholder nominee from the company's proxy statement.

their intent to exclude a nomination, without requiring the companies to delay their annual meetings by several months every time they receive a Rule 14a-11 nomination keyed to the end date of their advance notice bylaws?

VIII. Obligations of Companies That Receive Notice

A. *The Universal Proxy Card Should Be Adopted for Rule 14a-11 Nominations*

If the SEC adopts prescriptive rules, we would favor the required use of a universal proxy card for both the company and the nominating stockholder as the SEC suggests. A coupling of proxy access with multiple proxy cards would result in unnecessary cost, complication, and confusion. Company costs would increase because the use of a separate proxy card for each nominating person or group would require the company, on behalf of the nominating group or person, to print additional cards and deliver them with the company's proxy materials. As is the case with traditional proxy contests, the use of multiple cards would give rise to competing cards (*e.g.*, "vote Blue" or "vote White") and exacerbate the issues of "last-dated proxy card" and revocation.

In addition, the use of multiple proxy cards could create voter confusion, particularly if multiple stockholders or stockholder groups submit nominees. Currently, where a dissident stockholder proposes its own short slate of nominees, the stockholder may "round out" the list with board nominees, nominees from other dissident stockholders, or a combination thereof. If current practice were imported into the new rule, multiple proxy cards could contain multiple combinations of nominees, thereby resulting in inevitable voter confusion. A universal proxy card in the proxy access context would avoid this problem by consolidating company nominees and all Rule 14a-11 nominees on one card for selection by stockholders.

B. *Stockholders Should Have the Option to Vote for Management Nominees as a Group*

We strongly oppose the SEC's proposed amendments to Rule 14a-4. Following longstanding practice, stockholders should be given the option to vote for management nominees as a group, even where management and stockholder access nominees share the same universal proxy card. The elimination of the group voting option unnecessarily raises the risk of voter confusion, mistakenly completed proxy cards, and stockholder disenfranchisement. If a stockholder were prepared to support the entire management slate, the risk that such stockholder's intention will not be reflected on the proxy card would be reduced if the stockholder could check one box rather than multiple boxes, particularly where there are more nominees on the proxy card than available board seats.

We understand the SEC's concern that group voting may make it easier to vote for all of management's nominees rather than a combination of management and stockholder access nominees. We believe that the risk that the option to vote for the management slate as a group will, incrementally, discourage a voter from fully considering or supporting stockholder nominees is very low. This speculative risk is outweighed by the desirability of reducing the risk that a proxy card is filled out in error.

Furthermore, boards and nominating committees put considerable effort into selecting director nominees, taking into account the expertise, experience and independence of the board as a whole, in accordance with their fiduciary duties. Stockholders should be permitted to rely on this process and vote for the company's nominees as a group if they so desire.

C. *Blank Proxy Cards Should Be Counted As a Vote for All Management Nominees*

Following current practice, when a proxy card contains a disclosure that the board's recommendations will be followed in the absence of instruction, the proxy card should be voted as contemplated by that disclosure. This longstanding practice has shaped voter expectations so that stockholders who support all management proposals know that they may vote simply by signing and returning the blank card. Many stockholders will continue to follow this practice even if proxy access allows stockholder nominees to appear on the proxy card.[19] Thus, changing the effect of returning a blank proxy card may have the unintended consequence of thwarting stockholder intentions.

D. *Nominating Stockholder Ineligibility, After Proper Notice is Delivered, Should Disqualify Nominees and Preclude Replacement Nominees*

As discussed above in Section IV "Nomination Eligibility — There Should Be Consequences If a Nominating Stockholder Sells Its Interest or Develops a Change of Control Intent Before the Meeting, or If a Director Candidate Fails to Obtain a Minimum Number of Votes," if a nominating stockholder becomes ineligible under proposed Rule 14a-11 after providing notice and submitting nominees, that stockholder's nominees should likewise become ineligible and be excluded from the company proxy materials. Moreover, if this event occurs after the deadline for filing Schedule 14N, then a nominating stockholder or group which had submitted a nominee who was excluded as a result of the relevant process to allocate an excess number of nominees (whether as a result of a first-in or largest stockholder priority allocation system) should not be able to have such nominee subsequently included in the proxy statement. To repeat the time-consuming process of company and SEC review of the eligibility of alternative stockholder nominees would be impractical. Where a company uses the resources necessary to manage the process for a nominating group that becomes ineligible, it should not be forced to start over for replacement nominees.

We recognize that some of the timing concerns could be addressed by creating a "waiting list" of potential nominating stockholders and nominees. The need to resort to such a waiting list would likely, however, be so infrequent that it would not justify the expenditure of company time and resources that would be required to develop and administer such a waiting

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19 *See* Dixie Johnson, Chair, Committee on Federal Regulation of Securities; Robert Todd Lang, Co-Chair, Task Force on Shareholder Proposals; Charles Nathan, Co-Chair, Task Force on Shareholder Proposals, Business Law Section, American Bar Association, Comment re: Security Holder Director Nominations (Release No. 34-48626; IC-26206; File No. S7-19-03; RIN 3235-AI93) January 7, 2004.

list. Moreover, the waiting list would not have any practical benefit if the ineligibility of a nominating stockholder arose with too little time left before the annual meeting.

IX. Application of Proxy Rules to Solicitation to Form a Group

As proposed, Rule 14a-2(b)(7) would provide an exemption from the proxy solicitation rules for a communication in connection with the formation of a nominating stockholder group. The exemption would apply to written communications that are filed with the SEC and that contain only limited information, including a statement of the stockholder's intent to form a nominating group, brief information on the proposed nominee, the stockholder's stock ownership and the means to contact the stockholder.

A. *The Proposed Exemption Is Not Appropriate*

As discussed above in Section IV "Nomination Eligibility — We Recommend Adjustments to the Proposed Ownership Thresholds — We Would Not Provide a New Proxy Rule Exemption for Activities in Connection with the Formation of Nominating Groups," we do not believe that the proposed exemption in Rule 14a-2(b)(7) is appropriate given the attendant control and proxy contest issues associated with the potential formation of a large group. We also believe that this proposed exemption is unnecessary, given the existing exemptions available to nominating stockholders. These include the exemption for communications with up to 10 stockholders under Rule 14a-2(b)(2) and the exemption for communications in an electronic stockholder forum under Rule 14a-2(b)(6).

Moreover, the proposed exemption raises significant regulatory, contractual and disclosure issues. When a group of stockholders acts in concert to coordinate voting or investment decisions, including the nomination of a director, there is a high risk of triggering unintended consequences under, for example, state anti-takeover provisions, poison pills and other requirements under state law and/or a company's governing documents. These unintended consequences could extend to the reporting obligations that may arise under Section 13 and Section 16 of the Exchange Act as discussed further below. The impact of these unintended consequences can be significant to a company and to the group members, and the analysis will in many cases grow more difficult as the number of group members increases. In many of these areas (as in Section 13, Section 16 and Rule 14a-11 itself), the analysis depends on the investment or control "intent" of the group members, which can be extremely difficult to identify and establish in any context, but increasingly so as the number of group members increases. At some point, the sheer size of the holdings of the group has control implications without regard to evidence of control intent. Thus, the SEC does not allow a person holding 20% or more of a company's voting stock to file on Schedule 13G, regardless of intent.

This concern over unintended consequences is elevated because the rules do not impose any upper limit on the size of the holdings of the nominating group being formed. Although much attention has been paid to the minimum aggregate ownership of a nominating group, there is nothing preventing a nominating group that holds a large portion of the company's stock (*e.g.*, 15%, 20 %, 30% or more) from being formed under the proposed rules, and taking advantage of the various proposed exemptions and safe harbors.

For these reasons, stockholders seeking to form a group should be limited to the use of the existing exemptions or, if none is available, should be required to comply with the proxy solicitation rules that have been put in place to provide all stockholders with the information they need to make an informed decision.

B. *If Adopted, the Exemption Should Be Limited*

If proposed Rule 14a-2(b)(7) relating to formation of a nominating group is nevertheless adopted, we believe that the Rule should be limited in a number of respects to reduce the risk that it will be used inappropriately. In particular, we suggest the following limitations:

1. No Use of Multiple Exemptions

The exemption should not be available if the nominating stockholder or any group member is using another available exemption in connection with a nomination at the same annual meeting. For example, a stockholder should not be permitted to utilize Rule 14a-2(b)(7) to communicate its interest in forming a stockholder group to a broad group of other stockholders, while separately using Rule 14a-2(b)(2) to exempt another communication relating to the nomination to a group of 10 or fewer stockholders. If a stockholder is acting such that it needs the benefit of the new exemption, then all solicitations by the stockholder should be subject to the limitations and requirements of the new exemption.

2. Bona Fide Intent to Use Rule 14a-11

We believe that adding a certification on the part of the stockholders making the solicitation of a bona fide intent to use Rule 14a-11 would be salutary but will be difficult to police, which is one of the reasons we believe that the 10-person solicitation exemption is more appropriate. While we have concerns that this type of certification cannot be adequately policed, the absence of any certification would be even less desirable. The Rule should also be modified to prevent the use of the solicitation exemption as a data-gathering strategy for a stockholder who is testing the waters for a conventional proxy contest or for other purposes by explicitly providing that following use of this exemption for solicitation of a nominating group, the stockholder would not be permitted to nominate directors for election at the same meeting other than pursuant to Rule 14a-11. Absent this limitation, a stockholder could use the exemption to gauge the reaction of stockholders broadly, or some subset of stockholders, and then abandon the Rule 14a-11 process and proceed with a full scale traditional proxy contest using the information gleaned from the exempt solicitation process.

3. Exemption Not Available for Oral Communications

We agree with the Proposal that the exemption should not apply to oral communications, as there would be no way to ensure that information is being provided to stockholders in a consistent manner and in accordance with the rule requirements. The Proposal states that the exemption "would not apply to oral communications because such communications could not easily satisfy the filing requirement, which we believe is important in determining compliance with the content restriction in the proposed exemption." However, the proposed rule itself is not structured so as to appropriately implement this intent. Proposed Rule

14a-2(b)(7) exempts "[a]ny solicitation" but only imposes the content limitations on "written communications." We believe that to implement the SEC's stated intent, the word "written" should be added to the first sentence of Rule 14a-2(b)(7) and then deleted (as surplusage) from clause (i) of the Rule. In addition, for the avoidance of doubt, we recommend that the SEC add an instruction to the Rule expressly stating that oral solicitations are not eligible for the exemption.

C. *If Adopted, the Required Disclosures Should Be Expanded*

As proposed, Rule 14a-2(b)(7) would require the notice to include only certain specified information. Consistent with our proposed additions to Schedule 14N discussed above, we believe that the information required in an exempt written communication for the purpose of forming a nominating group should be expanded to include the following:

1. Disclosure of the total length of time for which the soliciting stockholder has held the specified number of securities, consistent with our discussion under Section VII "Notice and Disclosure Requirements — The Proposed Rule 14a-11 Disclosure Requirements Fail to Include Critical Topics — Duration of Holdings" above.

2. A description of any short positions or other hedging arrangements by which the soliciting stockholder has reduced or otherwise altered its economic stake in the company, consistent with our discussion under Section VII "Notice and Disclosure Requirements — The Proposed Rule 14a-11 Disclosure Requirements Fail to Include Critical Topics — Short Positions and Derivatives" above.

3. More broadly, a description of any contracts, arrangements, understandings or relationships (legal or otherwise) between the soliciting stockholder and any other person with respect to any securities of the company. The required disclosure should be consistent with that required by Item 6 of Schedule 13D.

4. Finally, a description of any plans or proposals of the nominating stockholder or group with respect to the organization, business or operations of the company, consistent with the information required by Item 4 of Schedule 13D.

X. Application of Proxy Rules to Solicitation For or Against a Candidate

Proposed Rule 14a-2(b)(8) would provide an exemption for solicitations by a nominating stockholder or group in favor of a candidate included in the company's proxy materials under Rule 14a-11, or against a management-supported candidate. We support this exemption as a means of encouraging an orderly and transparent campaigning process, and believe that the requirement for immediate SEC filing and the prominent legend are appropriate mechanisms to protect stockholders' interests, but we have a recommendation with respect to this exemption.

The proposed exemption refers to solicitation "in support of a nominee placed on the registrant's form of proxy" or "against the registrant's nominee or nominees" but does not clearly provide a time frame for when the solicitation can occur. Language in the proposed legend suggests that the solicitation may occur before the proxy materials are available. We believe that in order to avoid confusion and misunderstandings, the Rule must specify that the exemption only applies to solicitations in favor of a stockholder nominee that occur after the mailing of the company's proxy materials, when it becomes certain that the referenced nominee(s) will in fact be included. The potential for tremendous confusion exists if the exemption is interpreted to cover solicitations for or against nominees that do not ultimately appear in the company's proxy materials. In addition, the solicitations should not occur at a time when the stockholders do not have access to the more complete and balanced disclosure about all of the nominees in the company's proxy materials.

XI. Beneficial Ownership Reporting Requirements

A. *Issues Under Schedules 13D and 13G*

The proposed rules would amend Rule 13d-1 to provide that "activities solely in connection with a nomination" under Rule 14a-11 would not cause a nominating stockholder or group to lose its eligibility to file on Schedule 13G, as opposed to Schedule 13D.

1. Proposed Amendment to Rule 13d-1 Dealing With 13G Eligibility Standard Should Not Change

We believe that the proposed change to the Schedule 13G eligibility standard is not consistent with the purpose or the language of Section 13(d)(5) of the Exchange Act or the rules thereunder. In accordance with Section 13(d)(1), Schedule 13D is designed to provide stockholders and the company with information from greater-than-5% stockholders regarding their level of share ownership, recent trading in shares, plans and proposals regarding the company. This is a Congressionally established requirement. The only exception for greater-than-5% stockholders is for passive investors that meet the statutory test in Section 13(d)(5). The determination of whether a stockholder is a passive investor that can file a short-form Schedule 13G, as permitted by Section 13(d)(5), is based on the relevant facts and circumstances. We do not believe that nominating stockholders under a proxy access regime that hold more than 5% of a company's shares should be treated differently from other holders.

Under Section 13(d)(5), the SEC has authority to permit a short-form filing (*i.e.*, Schedule 13G instead of Schedule 13D) only if it appears to the SEC that the securities "were not acquired for the purpose of and do not have the effect of changing or influencing the control of the issuer." Rule 13d-1(b), (c) and (e) track the use of the phrase "changing or influencing control of the issuer." Assuming the SEC is not claiming that the word "influence" could or should be read out of the statute or the underlying rules, which would be entirely inconsistent with the "passive investor" theory underlying Section 13(d)(5) and Schedule 13G eligibility, it presumably is taking the position that a stockholder or group seeking to nominate a director – or possibly up to 25% of a board of directors if our proposal to limit nominating groups to one nominee is rejected – and to oppose the election of certain incumbent directors is not seeking to "influence control of" the company. We assume most proxy access election contests will be focused on the governance, strategic direction and/or policy initiatives of the company, as directed by the incumbent board of directors, which we believe is clearly within the realm of seeking to influence control.[20] While one could envision circumstances in which a nominating stockholder could establish a lack of intent to influence control, there will be many proxy access situations where this would not be true. Accordingly, we believe that the proposed automatic exemption from Schedule 13D filings is inappropriate and contrary to the governing statute.

We further believe that the level of disclosure provided for in Schedule 13D is appropriate for a stockholder or group of stockholders that has beneficial ownership in excess of 5% of a class of voting securities and that is participating in a process that meets the statutory test of influencing control. Although it is our sense that a Schedule 13D filing would not require significant additional information from a nominating stockholder or group that had no other relationship to the company or to other stockholders and no intent to influence control of the company in specific ways, in cases where the nominating stockholder or group had more complicated relationships or intentions relating to the company or its securities, the Schedule 13D filing would provide useful material information to stockholders, as it is intended to do. A major premise of the SEC initiative is to replicate an in-person meeting. If in the absence of proxies stockholders formed a group to elect a director at an in-person meeting of stockholders, the SEC would not contemplate a per se exemption from Schedule 13D.

For a nominating stockholder or group that has otherwise purely passive investment intent, we believe that the Schedule 13D filing requirement would likely be triggered by the submission to the company of the requisite notice to nominate a director candidate, since this is the first formal act manifesting the intent to affect the composition of the company's board of directors. Once the nomination process is over – whether because the nominee was deemed to be ineligible or was withdrawn, or because the annual meeting has occurred – then the nominating stockholder or group member could once again be deemed to be a passive investor, absent any other non-passive intent or effect. If the stockholder was a Schedule 13G filer prior to making the nomination, then under Rule 13d-1(h) the stockholder would once again be permitted to file on Schedule 13G. In the case of a nominating group that collectively exceeded 5% and became a Schedule 13D filer, the group, so long as it did not continue to act in concert after the election process, would be free to terminate its Schedule 13D filing obligations through an exit filing. If the director nominee is elected, a nominating stockholder or group that held more than 5% of the shares would need to determine whether it can then requalify as a passive investor (based on such factors as any continuing relationship with the director or intent for future action).

During the course of the nomination process, while the nominating stockholder or group is a Schedule 13D filer, the information provided by Schedule 13D would normally not be significantly more than the disclosure in proposed Schedule 14N, and much of the Schedule 13D disclosure could be incorporated by reference to Schedule 14N. The Schedule 13D disclosure would include more details on specific securities transactions, as well as relationships and arrangements relating to the company's securities and plans and proposals regarding the company, but there is no reason to deprive other stockholders of the same disclosure that they

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20 Indeed, a significant portion of contested solicitations were based upon a campaign message to sell the company or take significant corporate actions; s*ee* fn 56 of the Proposal.

would receive in the case of another greater-than-5% non-passive stockholder. In addition, while Schedule 14N would be required to be amended for material changes, all stockholders and potential stockholders would benefit from the greater transparency provided by the Schedule 13D reporting and amendment requirements and practices.

2. Any 13G Eligibility Carve-Out Will Inevitably Raise Difficult Interpretive Issues

As proposed, the scope of the Schedule 13G eligibility carve-out is not clear. Section III.D.1 of the Proposal indicates that the intent is to provide that a nominating stockholder will not lose Schedule 13G eligibility due to "formation of a stockholder group solely for the purpose of nominating one or more directors pursuant to proposed Rule 14a-11, the nomination of one or more directors pursuant to proposed Rule 14a-11, soliciting activities in connection with such a nomination (including soliciting in opposition to a company's nominees), or the election of such a nominee as a director under proposed Rule 14a-11." However, the proposed rule change itself refers broadly to activities "in connection with" a Rule 14a-11 nomination. This could be read much more broadly than the specific list of activities referred to above and could include, for example, negotiations with management about whether the stockholder will seek to include a Rule 14a-11 nomination and what management would need to do in order to convince the stockholder not to propose a nominee. Many actions that are arguably "in connection with" a nomination may be far from passive, and should not be captured by the carve-out.

More importantly, we believe any amendment to Rule 13d-1 to carve out nomination-related activities, no matter how narrowly it is phrased, will raise difficult interpretive issues and will cause every discussion and interaction between nominating stockholders and management to be subject to analysis as to whether it crosses whatever line is drawn. A stockholder seeking to include a nominee in the company's proxy materials should not get the benefit of an absolute "safe harbor" such that other attempts to influence the company do not result in a loss of Schedule 13G eligibility. Even if the nomination activities do not "solely" result in the loss of 13G eligibility, the nomination activities should be considered as part of the facts and circumstances relevant to the passivity determination. A stockholder that is nominating and soliciting for a director candidate is so close to the line that literally any additional action, such as discussions between the stockholder or group members and management about the perceived governance deficiencies, strategy, etc., or any affiliation between the nominee and the nominating stockholder, would raise the specter of a dispute between the company and the nominating stockholder concerning loss of Schedule 13G status. In order to be sure that it can obtain the benefit of the Schedule 13G eligibility carve-out, a nominating stockholder may be hesitant to participate in mutually beneficial and productive discussions about any proposed changes at the company with management of the company or with other stockholders who are not part of the nominating group. The inevitable complexity in applying and interpreting the carve-out supports our recommendation that the Schedule 13G eligibility change should not be made.

3. No Integration of Section 13(d) and Rule 14a-11 Filings

The Proposal requests comment on whether the Schedule 13D or 13G and Schedule 14N filings should be integrated. We see no reason for doing so, given that the forms have different purposes and different content. Schedules 13D and 13G are not required to include the various nomination-specific representations and certifications, and Schedule 14N is not required to include detailed information about plans or purposes or particular securities transactions. Creating a situation where some greater-than-5% stockholders are filing Schedule 13D or 13G, some are filing Schedule 14N, and some are making a combined filing would make it more difficult for other stockholders and interested parties to find the relevant information.

B. *Issues Under Section 16*

We support the SEC's decision to subject nominating stockholders and groups to the same Section 16 analysis as other stockholders and groups. The 10% ownership threshold for Section 16 purposes is above the current proposed ownership levels for Rule 14a-11 purposes and thus should not serve as a deterrent for stockholders to utilize the proposed proxy access rule.

We also agree that the SEC should not propose any standards for determination of whether a director nominee is a "deputized director" for Section 16 purposes. The concept of deputization under Section 16 was developed through case law as a matter of statutory interpretation, beginning with the U.S. Supreme Court decision in *Blau v. Lehman*.[21] Understandably, the SEC and its staff have historically been unwilling to interfere through rule-making with the highly fact-specific analysis set out by case law, and we see no reason to do so here.[22]

C. *Nominating Stockholder Should Not Have a Safe Harbor from Affiliate Status*

We do not believe that the SEC should provide a safe harbor from affiliate status for a nominating stockholder. Courts interpreting control status under the securities laws have stressed the broad nature of the inquiry and the importance of focusing on the purpose behind the particular application of the term.[23] For the SEC to provide a safe harbor from "affiliate" status in the stockholder nomination context would be a stark departure from the historical practice of

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21 368 U.S. 403 (1962).

22 In SEC Release No. 34-28869, [1990-1991 Transfer Binder] Fed. Sec. L. Rep (CCH) ¶ 84,709, at 81,251 n.27 (Feb. 8, 1991), the SEC adopted significant changes to the Section 16 rules, but indicated that the legal doctrine concerning deputized directors "will be left to case law," citing *Blau* as well as *Feder v. Martin Marietta*, 406 F.2d 260 (2d Cir. 1969).

23 *See, e.g., U.S. v. Corr*, 543 F.2d 1042, 1050 (2d Cir. 1976) ("While there is no statutory definition of 'control,' its concept is not a narrow one. Its determination is a question of fact which depends upon the totality of the circumstances including an appraisal of the influence upon management and policies of a corporation by the person involved. Control may be exerted in other ways than by vote, stock ownership being only one aspect of control.") (citations omitted).

the SEC and its staff to leave this as a pure facts-and-circumstances determination.[24] Moreover, this would go beyond addressing the stockholder rights issues raised by the SEC's goal of replicating an in-person meeting.

Furthermore, we do not believe that, as a practical matter, the proposed Instruction 1 to Rule 14a-11(a) significantly reduces the interpretive analysis necessary to determine whether a nominating stockholder is an "affiliate." No matter how such a safe harbor is drafted, there will inevitably be interpretive issues around whether the safe harbor applies – it will rarely be clear that a nominating stockholder's relationship with the company is "solely" its nomination and solicitation activities. As discussed above in connection with Schedule 13G status, the nominating stockholder will often have had some discussions with management about its concerns as to strategy or governance matters, and there will often be questions about whether the stockholder has some "relationship" with the nominee (and questions about what constitutes a "relationship" for purposes of the safe harbor). And, of course, the stockholder will, by definition, have some level of share ownership that weighs into the control analysis. These questions will entail essentially the same level of inquiry and facts-and-circumstances analysis as a standard assessment of affiliate status. In addition, it seems likely that the existence of this safe harbor would discourage nominating stockholders from participating in potentially fruitful discussions with the company about their overall concerns and observations, for fear of being seen as having taking actions that go beyond "solely" nominating and soliciting for a director candidate.

XII. Application of Liability Provisions

We support the SEC's efforts to ensure that a company including material in its proxy statement provided by a nominating stockholder relying on Rule 14a-11, an applicable state law provision or a company's governing documents to propose director nominees will not be liable for materially false or misleading statements provided to it by the nominating stockholder. We think, however, that it is necessary to provide companies with further protection against the frivolous lawsuits and resulting losses that will likely occur if the Proposal's liability provisions stand as drafted. Our view is that companies should have no responsibility for information contained in the notice and included in the company's proxy materials under any circumstances.

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24 *See, e.g., First General Resources Co.*, SEC No-Action Letter (Aug. 23, 1988) ("The Division has historically declined to express any view on the affiliation of any person to an issuer of securities on the ground that the question is a matter of fact best determined by the parties and their advisors.") *See also* SEC Release No. 33-6253, 1 Fed. Sec. L. Rep. (CCH) ¶ 373 at 1,256 (Oct. 28, 1980) (indicating that affiliate or control status is "an area involving factual questions which the staff is not in a position to resolve"). The SEC has in the past proposed to provide a safe harbor from, or definition of, "affiliate" status for certain purposes, but has declined to act on these proposals. *See, e.g.*, SEC Release No. 33-7931 63 S.E.C. 2082 (Feb. 20, 1997) (relating to the definition of "affiliate" for Rule 144 purposes).

The exculpation provision in proposed Rule 14a-11(e) is, by its terms, not applicable where the company knows or has reason to know the information provided by the nominating stockholder or nominee is materially false or misleading. This qualification is subject to three critical objections. First, it can be read to impose a duty of diligence on the company to vet the information provided by the nominating stockholder and the nominee. We submit that it is inappropriate to impose any such duty on the company. Second, the qualification lends itself to spurious lawsuits and to complicated factual issues about who within a company knew what, and when they knew it. To saddle a company with this litigation exposure as part of a proxy access regime is not appropriate. Finally, suppose, for example, that after the mailing of proxy materials including a Rule 14a-11 nominee, the company comes to the conclusion that there is a material misstatement or omission in the information provided by the stockholder, but the stockholder disagrees. The company could well decide, for a variety of perfectly legitimate reasons that it is preferable to abandon the factual dispute and rely on the stockholder's denial rather than get into a war of words with the stockholder. The proviso, however, would seem to put the company at risk of being held liable, notwithstanding the assertions of the stockholder. In view of these issues, we urge the SEC to delete the proviso from the exculpation provision of any final proxy access rules.

XIII. Conclusion

As we have noted above, we unanimously recommend that the SEC not adopt proposed Rule 14a-11 but, rather, amend Rule 14a-8(i)(8) to permit stockholders to utilize Rule 14a-8 for proposals relating to proxy access. In that connection, a number of the firms who are signing this letter are separately addressing the policy issues raised by Rule 14a-11. We have, however, principally used this joint letter to address necessary modifications to Rule 14a-11 if the SEC disagrees with our view. If the SEC chooses to adopt Rule 14a-11, we would urge the SEC to be cautious in implementing what all participants in this debate acknowledge will be one of the most significant rule changes in SEC history. This caution should be reflected in the timing of the transition period, respect for private ordering, sensitivity to control issues and the need for adequate disclosure for stockholders to make informed voting decisions.

We appreciate this opportunity to submit, and the SEC's consideration of, our comments on the proposed proxy access rules. We ask the SEC to contact any of the following firm representatives should it have any questions: Richard Hall from Cravath, Swaine & Moore LLP at 212-474-1293; Phillip R. Mills from Davis Polk & Wardwell LLP at 212-450-4618; Charles M. Nathan from Latham & Watkins, LLP at 212-906-1730; John G. Finley from Simpson Thacher & Bartlett LLP at 212-455-2583; Marc S. Gerber from Skadden, Arps, Slate, Meagher & Flom LLP at 202-371-7233; James C. Morphy from Sullivan & Cromwell LLP at 212-558-4000; and Eric S. Robinson from Wachtell, Lipton, Rosen & Katz at 212-403-1220.

Respectfully,

/s/Cravath, Swaine & Moore LLP
Cravath, Swaine & Moore LLP

/s/Davis Polk & Wardwell LLP
Davis Polk & Wardwell LLP

/s/Latham & Watkins, LLP
Latham & Watkins, LLP

/s/ Simpson Thacher & Bartlett LLP
Simpson Thacher & Bartlett LLP

/s/Skadden, Arps, Slate, Meagher & Flom LLP
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/s/ Sullivan & Cromwell LLP
Sullivan & Cromwell LLP

/s/Wachtell, Lipton, Rosen & Katz
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CC: The Honorable Mary L. Schapiro, Chairman
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