

CORPORATE AND SECURITIES LAW

Alert

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

SEC Releases Proposed Proxy Access Rules

June 15, 2009

On Wednesday, June 10, the SEC released proposed rules addressing the issue of proxy access, under which a shareholder could require a public company to include the stockholder's director nominees in the company's proxy statement. The issue of proxy access has been the source of much debate, as adoption of proxy access rules would greatly facilitate insurgent campaigns to unseat incumbent members of boards of directors.

The SEC's proposed rules generally track those that we summarized for you in our May 22 Corporate and Securities Law Alert. The 250-page proposing release provides significant detail as to the SEC's rationale behind the proposed rules and how such rules would operate in practice. The tone of the release – and the fact that it took almost three weeks for the SEC to release the proposed rules since commissioners met on these issues last month – suggest that the SEC expects significant public feedback and realizes that it may take a substantial amount of time to refine its proposals.

Below we summarize the proposed rules and suggest how our public company clients can begin planning for changes in the public company director election process.

Proposed Rule 14a-11

Proposed Rule 14a-11 under the Securities Exchange Act of 1934 would require a company to include shareholder director nominations in its proxy statement, provided that the nominating shareholder or shareholder group meets certain threshold criteria and follows specified procedures. All companies subject to Exchange Act reporting rules would have to comply with Rule 14a-11, unless state law or the company's governing documents prohibited shareholders from nominating candidates to the board of directors.

In order to be eligible to submit director nominations under the proposed rule, shareholders would be required to meet a specified threshold ownership percentage, which would vary by company size: 1% for large accelerated filers; 3% for accelerated filers; and 5% for non-accelerated filers. Shareholders would be permitted to aggregate their holdings to meet the applicable threshold. Moreover, all of the stock held by the shareholder or aggregated by the shareholder group to meet the applicable threshold percentage would be required to have been held for at least one year (measured as one year from the date notice is provided to the company). The shareholder or shareholder group would also be required to represent that

they intend to hold the subject securities through the date of the company's meeting for the election of directors.

Shareholders would be permitted to nominate no more than 25% of a company's board of directors or one candidate, whichever is greater. If a company had a staggered board of directors and a director elected pursuant to Rule 14a-11 already served on the board and had a term of office beyond the election meeting date, that existing director would count against the 25% ceiling. These restrictions on the number of nominees that could be proposed by a shareholder or group, according to the SEC's release, are meant to prevent a single shareholder or group from utilizing access to the company's proxy materials to achieve a take-over of the majority of a board.

If more shareholder director nominations were submitted than could be included in a company's proxy statement, a "first submitted" rule would be used to determine which nominees would be included in the proxy statement. Under this "first submitted" rule, the company would include in its proxy statement the nominee or nominees from the first shareholder or shareholder group that provided timely notice as required under the new rules. If the first shareholder to submit director nominees did not nominate the maximum number of permitted director nominees, the remaining spaces would be filled by the next shareholders(s) to provide timely notice of their nominee(s). We believe that the "first submitted" rule would create the potential for a race to submit nominees by shareholders, and this formulation for determining priority is one of the many questions with respect to which the SEC is soliciting comments.

Rule 14a-11 requires that the nominating shareholder provide notice on proposed new Exchange Act Schedule 14N of its intent to require a nominee to be included in the company's proxy materials. In most instances, the notice would be required to be given to the company by the date listed in the company's advance notice bylaws, or if no such provision exists, no later than 120 calendar days before the company mailed its proxy statement for the prior year's annual meeting. The proposed rules also set forth a procedure through which a company could attempt to exclude a shareholder's nominees from inclusion in its proxy statement for failure to comply with the Rule 14a-11 process. The exclusion process would require the company to notify both the nominating shareholder and the SEC with notice of its intent to exclude the director nominee from company proxy materials, with the SEC providing at its discretion its views on whether such exclusion is permissible.

If a valid nomination were made by a shareholder under Rule 14a-11, the company would be required to include disclosure regarding the shareholder nominee(s) in its proxy statement and to include the name of the nominee(s) on the proxy card. On the proxy card, the company would identify shareholder nominees as such and recommend how the stockholders should vote on those and management nominees. Importantly, in contrast to the current proxy rules, the company could not give stockholders the option of voting for or withholding authority to vote for all of the company nominees as a group only. Instead, it would be required that each director nominee be voted on separately.

The proposed rules would not interfere with the ability of shareholders to nominate directors within the scope of the current proxy regime (i.e., through the use of the shareholder's own proxy statement). Public companies should be aware that the proposed rules would appear to significantly increase the likelihood of companies being involved in an actual or threatened proxy fight with multiple dissidents, both within and outside of the Rule 14a-11 process.

Proposed Schedule 14N

The proposed Schedule 14N disclosure requirements are more expansive than disclosures required by Schedule 14A under the current rules. Among other things, the proposing shareholder or shareholder group would also be required to: (i) state its intent to continue to own the requisite shares through the shareholder meeting at which directors are elected, as well as provide a statement of its intent with respect to continued ownership after the election; (ii) certify that, to the best of the nominating shareholder's or group's information and belief, its shares in the company are not held for the purpose of changing the control of the company or gaining more than a limited number of seats on the board; (iii) represent that, to the knowledge of the nominating shareholder or group, each candidate's nomination or initial service on the board would not violate controlling state law, federal law or applicable listing standards; (iv) represent that each shareholder nominee would be in compliance with the generally applicable director independence requirements of any national securities exchange (the nominee would not be required to be independent from the nominating stockholder(s)); and (v) include, if desired, any statement, not to exceed 500 words, in support of the shareholder nominee or nominees.

Proposed Amendment to Rule 14a-8(i)(8)

As previously discussed in our Corporate and Securities Law Alert on May 22, the SEC's proposals include an amendment to Rule 14a-8(i)(8) that would allow stockholders to bring shareholder proposals in company proxy materials aimed at altering the company's bylaws to permit proxy access. In order to be eligible to submit such a proposal, stockholders must have held at least \$2,000 in market value of the company's voting securities for at least a year.

Some commentators believe that, rather than specifying the conditions under which proxy access will be permitted, the SEC should simply adopt this proposed amendment to Rule 14a-8(i)(8) in order to facilitate shareholder discussion and action on proxy access, but leave public companies and their shareholders alone with the ability to determine the details of proxy access in accordance with state corporate law. As discussed in our May 15 Corporate and Securities Law Alert, recent changes to the Delaware General Corporation Law clarify that proxy access is permissible under Delaware law and that corporate bylaws may address such issues as how much stock a nominating shareholder must have (and how long that stock must be held) before proxy access is permitted, as well as the number of dissident nominees that may be required to be included in the company's proxy materials. (The ABA is considering similar changes to the Model Business Corporation Act.) Critics of the SEC's proposed rules believe that a federal "one-size fits all" approach to proxy access is misguided and that the issue should be allowed to develop on a state-by-state, company-by-company basis.

What public companies should be doing now

The SEC's proposed proxy access rules will be open to the public for comment until August 17, 2009. After the comment period, the SEC is expected to adopt final rules, although whether and to what extent these rules will be effective for the 2010 proxy season is unclear. In fact, in its proposing release (available at <http://www.sec.gov/rules/proposed/2009/33-9046.pdf>), the SEC included almost 500 questions for public comment before final action is taken. For example, the SEC seeks comment on: (i) whether and to what extent the SEC's proposed rules would conflict with existing state corporate law and stock exchange regulations; (ii) whether, as the SEC has previously proposed, there should be certain triggering events (such as poor economic performance) that serve as prerequisites to proxy access; (iii)

whether the rules should be inapplicable to companies that adopt a provision in their governing documents that provides for or prohibits the inclusion of shareholder director nominees in the company's proxy statement, and (iv) whether the rules should have exceptions for controlled companies or companies subject to shareholder agreements or other contracts that allow shareholders to appoint a set number of directors.

We believe that, in light of the current activist and regulatory environment, some form of proxy access will be implemented in the near future. Thus, we advise our public company clients to consider how the proposed SEC's proposed proxy access rules would apply to them, given the nature of their investor base and the size of the company's market capitalization. This kind of analysis should occur in the context of a review of a company's overall takeover defense profile, including whether or not the company has a staggered board of directors, a poison pill and other defense mechanisms. We also encourage our public company clients to review their current advance notice bylaws and consider the manner in which their bylaws would need to be amended to provide for proxy access in the event these rules are adopted. This will allow companies to familiarize themselves with the complex details surrounding this issue. In addition, in the event that the SEC were to resolve the proxy access issue by amending SEC Rule 14a-8(i)(8) but not immediately prescribing specific pre-conditions for proxy access under proposed Rule 14a-11, companies will need to consider whether it would be advisable to adopt a management-supported proxy access proposal, which may deter stockholders from proposing a more dissident-friendly form of such proposal under Rule 14a-8(i)(8).

As outlined in our May 15 Corporate and Securities Law Alert, public companies are also advised to continue to take note of the Federal Shareholder Bill of Rights that has been proposed by Senator Chuck Schumer (D-NY), which would implement sweeping changes in the corporate governance requirements applicable to U.S. public companies, including abolishing classified boards for exchange-listed companies. Even if certain aspects of this legislation may not have sufficient congressional support to pass in their current form, companies should be aware of the possibility that this legislation could be adopted through inclusion in omnibus legislation approved by Congress.

Bass, Berry & Sims PLC's Shareholder Activism Subgroup monitors and advises on developments in the area of proxy contests, activist campaigns, takeover defenses and shareholder communications. If you have any questions regarding the issues addressed in this Corporate and Securities Law Alert or would like us to discuss these developments in greater detail with you, please feel free to contact your regular contacts in our Corporate and Securities Group or any of the attorneys in our Shareholder Activism Subgroup listed below.

Page Davidson	615-742-6253	pdavidson@bassberry.com
Kevin Douglas	615-742-7767	kdouglas@bassberry.com
Chris Chi	615-742-7819	cchi@bassberry.com
Stephen Hinton	615-742-7799	shinton@bassberry.com
Eric Knox	615-742-7807	eknox@bassberry.com
Frank Pellegrino	615-742-7947	fpellegrino@bassberry.com

Bass, Berry & Sims Corporate and Securities Group

The Corporate and Securities Group includes the following subgroups comprised of our attorneys with a particular expertise who are focused on current trends and developments in these areas of the law. This Alert has been brought to you courtesy of the Shareholder Activism subgroup.

Annual Meetings	Corporate Finance/1933 Act
Corporate Governance	Cross-Border Transactions
Distressed M&A	Executive Compensation
Fiduciary Duties	Financial Institutions
Investor Relations/Earnings Releases	Joint Ventures
M&A Trends and Developments	Periodic and Current Reporting
Private Equity/Venture Capital	Private Placements
Real Estate Capital Markets	Securities Laws Liabilities/ SEC Priorities and Enforcement
Shareholder Activism	Statutory Developments
Trading by Insiders/Equity and Debt Repurchases	

The materials contained herein have been abridged from the statutory sources and should not be construed or relied upon for legal advice. Readers are urged to consult legal counsel concerning particular situations and specific legal questions.

To ensure compliance with requirements imposed by the IRS, we inform you that this message is not intended to be used, and cannot be used by the addressee or any other person for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code

315 Deaderick Street • Suite 2700 • Nashville, TN 37238-3001 • (615) 742-6200
The Tower at Peabody Place • 100 Peabody Place, Suite 900 • Memphis, TN 38103-3672 • (901) 543-5900
1700 Riverview Tower • 900 S. Gay Street • Knoxville, TN 37902 • (865) 521-6200