

KIRKLAND GOVERNANCE WATCH

July 23, 2010

SEC Seeks Comment on Broad Range of Potential Proxy Rule Amendments That Could Result in Significant Changes to Proxy System

The SEC is considering changes to a number of important aspects of the federal proxy rules that would affect the voting of shares of public companies, the outcome of director elections and other matters subject to shareholder votes.

On July 14, 2010, the SEC issued a [concept release](#) seeking public comment on the proxy system and asking whether the federal proxy rules should be amended. The Commission is considering changes to a number of important aspects of the proxy rules that would affect the voting of shares of public companies and the outcome of director elections and other matters subject to shareholder votes, such as mergers. The amendments could affect all public companies, all shareholders in the companies and other parties such as broker-dealers, other securities intermediaries and proxy advisory firms. Comments on the release are due October 20, 2010.

The SEC is considering changes to the federal proxy rules to “promote greater efficiency and transparency in the system and enhance the accuracy and integrity of the shareholder vote.” The Commission seems particularly concerned about issues and problems arising from the fact that the substantial majority of shares of U.S. public companies are held in street name by institutional holders rather than in the names of the beneficial owners themselves.

Specifically, the SEC is seeking comment on the following matters, among others:

- **Empty voting:** Whether “empty voting,” i.e., the separation of the voting rights from the economic interests of shares, and related activities, is being used inappropriately to influence corporate voting results.
- **Dual record dates:** Whether the proxy rules should be revised in light of recent changes to state corporate laws (primarily adopted to address empty voting concerns) that permit companies to set separate record dates for determining who is entitled to receive notice of shareholder meetings and who is entitled to vote (by proxy or in person) at the meetings.
- **Voting by securities lenders:** The voting of shares that are subject to securities lending arrangements, and specifically whether companies should be required to provide shareholders with more advance notice of matters to be voted upon by shareholders so shareholders, who have lent out shares can have more time to re-call them so they can vote them.
- **Company communications with shareholders and OBOs:** Obstacles that companies have in communicating with their own shareholders due to the fact that most shareholders hold their shares in street name. Consequently communications must go through a broker-dealer or other securities intermediary. More specifically, the SEC is seeking comment on whether the ability of shareholders to object to the disclosure of their identity to the company should be preserved, eliminated or limited in some way.
- **Greater retail investor voting participation:** Means to facilitate greater retail investor participation in voting matters, including improving investor education, enhancing brokers’ Internet platforms, permitting advance voting instructions for retail investors, enhancing investor-to-investor communications and improving the use of the Internet for distribution of proxy materials.
- **Role of proxy advisory firms:** Whether rules should be adopted to (i) improve disclosure of potential conflicts of interest of proxy advisory firms, (ii) enhance regulatory oversight over the manner in which the firms formulate their recommendations to shareholders and (iii) require public disclosure of their recommendations in SEC filings.

- **Over-voting and under-voting:** The over-voting and under-voting of shares held by broker-dealers and other securities intermediaries that results from the way securities transactions are cleared and settled in the United States.
- **Vote confirmation:** The required disclosure of voting data by vote tabulators (such as inspectors of elections), securities intermediaries and proxy service firms to one another so investors and companies can better confirm that votes have been properly counted in accordance with shareholders' instructions.

Some of the areas of potential regulatory reform, such as empty voting, dual record dates, over-voting/under-voting and vote confirmation, are arguably matters of state corporate law. Expanding the SEC's regulatory reach to address these matters other than by requiring additional disclosure may exceed the agency's regulatory authority and be subject to challenge. In addition, it is worth noting that the release does not cover the controversial issue of shareholder access to company proxy materials, which is the subject of pending proposed rules that would require, under certain circumstances, a company to include in its proxy materials a shareholder's nominees for director.

This concept release suggests the SEC is considering expanding its traditional regulatory role of ensuring full and fair disclosure in the proxy process to include more substantive regulation of the voting process and which shareholders are entitled to vote. Public companies, shareholders, broker-dealers and other securities intermediaries should be aware that significant changes to the rules of the game are being considered by the SEC.

If you have any questions about the matters addressed in this *Kirkland Governance Watch*, please contact the following Kirkland author or your regular Kirkland contact.

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