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SEC Proposes Competing Alternatives on Shareholder Access to Proxy Materials

The Securities and Exchange Commission (the “SEC”) recently issued two competing proposals relating to shareholder access to a company’s proxy materials. In the first proposal (SEC Release No. 34-56160, available at <http://www.sec.gov/rules/proposed/2007/34-56160.pdf>), the SEC proposed amendments to the federal proxy rules that would require companies, under certain circumstances, to include in their proxy materials shareholder proposals for bylaw amendments regarding the procedures for nominating directors, including bylaw amendments that would require a company to include shareholder nominees for director in the company’s proxy materials. In an unusual step, the SEC simultaneously issued a second, competing proposal (SEC Release No. 34-56161, available at <http://www.sec.gov/rules/proposed/2007/34-56161.pdf>) which, if adopted, would continue to permit companies to exclude from their proxy materials any shareholder proposal which relates to the election, or the process for election, of directors.

The SEC was spurred to take action as a result of last September’s decision issued by the U.S. Court of Appeals for the Second Circuit in *American Federation of State, County & Municipal Employees v. American Intern. Group, Inc.*, 462 F.3d 121 (C.A.2 (N.Y.) 2006). In that case, the Second Circuit held that AIG could not rely on Rule 14a-8 under the Securities Exchange Act of 1934, as amended, to exclude a shareholder proposal seeking to amend AIG’s bylaws to establish a procedure under which AIG would be required to include shareholder nominees to the board of directors in AIG’s proxy materials. This decision rejected the long-standing SEC Staff interpretation that any shareholder proposal that might result in contested elections, even if the proposal only purports to alter general procedures for nominating and electing directors, is properly excludable under Rule 14a-8(i)(8).

Comments on the competing proposals are due by October 2, 2007, and it is expected that final rules will be adopted in time for the 2008 proxy season.

Summary of Proposal Permitting “Proxy Access” Shareholder Proposals

Shareholder Eligibility to Submit a Proposal

If adopted, the SEC’s first proposal would amend Rule 14a-8(i)(8) to require companies to include in their proxy materials shareholder proposals for bylaw amendments which establish a procedure by which shareholder nominees for election of directors would be included in the company’s proxy materials if the following eligibility requirements are met:

- The shareholder (or group of shareholders) that submits the proposal is eligible to file a Schedule 13G (i.e., an institutional or passive investor) and files a Schedule 13G (or an amendment to a previously filed Schedule 13G) that includes certain disclosure regarding its background and its interactions with the company;

- The shareholder (or group of shareholders) that submits the proposal has continuously beneficially owned more than 5% of the company's securities entitled to be voted on the proposal at the meeting for at least one year by the date the shareholder submits the proposal; and
- The proposal otherwise satisfies the requirements of Rule 14a-8.

The proposed rules would allow proponents of such bylaw amendment proposals to offer shareholder nomination procedures as they see fit, subject only to limitations on such procedures imposed by state laws or the company's governing documents. However, in order to provide transparency to shareholders voting on such a bylaw amendment proposal, the proponent and the company would be required to comply with certain disclosure requirements. First, the proponent would have to provide disclosure about its own background, intentions and course of dealings with the company. These additional disclosures would be required in the proponent's Schedule 13G filing. Second, the company would need to disclose in its proxy materials similar information with regard to the nature and extent of its relationship with the proponent.

Disclosure Regarding Nominating Shareholder and Shareholder Nominees for Director

In the proposing release, the SEC expressed its concerns that using proposed Rule 14a-8 to nominate or establish procedures for shareholders to nominate a candidate for director could result in shareholders being asked to vote on a director nominee without adequate disclosure regarding either the nominee or the nominating shareholder. The proposed rules address these concerns by requiring that nominating shareholders provide the company with information about the shareholder's own background, intentions and course of dealings with the company (i.e., those items proposed to be added to Schedule 13G described above) at the time the shareholder forms any plans or proposals with regard to nominating a director. Immediately after receiving this information, the company would need to provide the information (or a link to the information) on its website and would also need to include this information in its proxy materials.

The SEC also proposed that the existing disclosure requirements for solicitations in opposition would apply to nominating shareholders and their nominees under any shareholder nomination procedure. These disclosure requirements provide basic information regarding the nominating shareholder and nominee or nominees, including biography and shareholdings, other interests of the nominating shareholder, methods and costs of the solicitation and other information to enable shareholders to make an informed voting decision. Although the company would be required to include all of this information in its proxy materials, the shareholder making the nomination would be responsible for the accuracy of the information and such information would not be incorporated by reference into the company's other SEC filings.

Summary of Alternative Proposal Excluding "Proxy Access" Shareholder Proposals

In its alternative proposal, the SEC issued interpretative guidance confirming its position that "a proposal may be excluded under Rule 14a-8(i)(8) if it would result in an immediate election contest (e.g., by making or opposing a director nomination for a particular meeting) or would set up a process for shareholders to conduct an election contest in the future by requiring the company to include shareholders' director nominees in the company's proxy materials for subsequent meetings." In addition to the interpretative guidance, which is designed to clear up any confusion resulting from the Second Circuit's decision in AFSCME, the SEC also proposed an amendment to Rule 14a-8(i)(8) to specifically state that a shareholder proposal may be excluded if such proposal relates to a nomination or an election for membership on the company's board of directors or a procedure for such nomination or election. If this proposal is adopted, the Second Circuit's holding in AFSCME would no longer be applicable.

Summary of Proposed Amendments to Facilitate the Use of Electronic Shareholder Forums

In addition to the proposals relating to shareholder access to proxy materials, the SEC also proposed amendments to remove obstacles that may inhibit shareholders and companies from taking advantage of electronic shareholder forums that facilitate communication among shareholders and between shareholders and companies. If adopted, the proposed rules would clarify that a company or a shareholder that establishes, maintains or operates an electronic shareholder forum would not be liable under the federal securities laws for any statement or information provided by another person to the forum. The person providing such information, however, remains liable for the content of those communications under traditional liability theories, such as Rule 10b-5.

The proposed rules also exempt solicitations in an electronic shareholder forum by or on behalf of any person who does not seek, directly or indirectly, the power to act as proxy for a shareholder and does not furnish or otherwise request a form of revocation, abstention, consent or authorization. The solicitation would be exempt so long as it occurs more than 60 days prior to the date announced by the company for its annual or special meeting or, if the company announces the meeting less than 60 days before the meeting date, not more than two days following the company's announcement.