

## Legal Alert: 2009 SEC and Other Initiatives Under Consideration

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While there have been no legal developments during the first five months of 2009 which have a significant impact on public companies, certain SEC and other initiatives under consideration could have wide-ranging effects for public companies.

### **SEC Proposes Shareholder Proxy Access (For the Third Time)**

For the third time in recent years, the SEC proposed a shareholder proxy access rule which would permit a shareholder or group of shareholders satisfying certain conditions to nominate director candidates who meet state law and stock exchange independence standards. The rule as proposed would preempt any proxy access provisions set forth in state law or in a company's charter or bylaws. The basic features of this newest version of the proposed rule include the following: (1) sliding-scale ownership requirements of 1% of voting shares for large accelerated filers, 3% for accelerated filers, and 5% for non-accelerated filers before a shareholder or group may make any nominations; (2) a one-year company stock holding period for any nominating shareholder or group; (3) a cap on the number of shareholder nominees permitted at each meeting - the greater of one nominee or a number equal to 25% of the board; and (4) a 120 day deadline for nominating shareholders to provide notice to the company and the SEC, unless the company has an advance notice bylaw that provides a different timeframe. Nominating shareholders would be required to make a filing with the SEC certifying that they meet all requirements and that the nomination is not intended to result in a change in control or more than minority representation on the board.

The proposed rules also include revising current rules to allow more shareholder proposals relating to the processes for the nomination and election of directors, requiring inclusion of proposals that would amend a company's governing documents regarding election procedures.

### **NYSE Rule Change on Discretionary Voting by Brokers**

The SEC recently announced the filing of a proposal by the New York Stock Exchange to eliminate discretionary voting by brokers in non-contested director elections. If adopted, director elections would be added to the list of matters which are not considered "routine" and therefore may not be voted upon without instructions from the beneficial owner.

This proposal has several important, practical implications for NYSE companies. First, many companies rely on broker votes to establish a quorum at a meeting. If there are not "non-routine" discretionary items to be voted on, then broker votes cannot be counted toward a quorum. Seeking ratification of the independent auditors is the best way to ensure that a discretionary item is on the agenda. In addition, companies with majority vote standards for director elections could find it more difficult to achieve success and combat activist shareholders who are conducting withhold vote campaigns. This is because, traditionally, many brokers will cast discretionary votes in accordance with the Board's recommendations.

If approved by the SEC on or prior to August 31, 2009, the proposal will be effective for all annual meetings held on or after January 1, 2010. If approved later than that, the effective date would not be until at least the second half of calendar 2010.

### **Senators Introduce Shareholder Bill of Rights Act of 2009**

Recently, Senators Charles Schumer (D-NY) and Maria Cantwell (D-WA) introduced the Shareholder Bill of Rights Act of 2009. Although not likely to be passed into law, the Bill of Rights offers key insights into how lawmakers envision increased

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regulatory oversight over corporate governance and compensation practices as part of the solution to the recent economic turmoil and highly publicized corporate scandals. The Bill of Rights provides for a new Section 14A to be added to the Securities Exchange Act of 1934, which would address executive compensation, shareholder proxy access and several other aspects of corporate governance.

With respect to executive compensation, the Bill of Rights calls for a non-binding say-on-pay shareholder resolution in any annual meeting proxy statement and a non-binding say on golden parachutes shareholder proposal in any proxy solicitation materials related to an acquisition sale of assets, merger or consolidation.

The Bill of Rights would also require the SEC to establish proxy access rules for shareholders seeking to nominate directors. Finally, the Bill of Rights would require all national securities exchange-listed companies to have an independent Chairman of the Board, annual elections for all directors, majority voting for directors in uncontested elections, and a newly-established Risk Committee comprised solely of independent directors.

### **Supreme Court to Rule on Certain Provisions of Sarbanes-Oxley**

The Supreme Court recently decided that it will hear the case *Free Enterprise Fund v. PCAOB*, which addresses the question of whether the section of the Sarbanes-Oxley Act of 2002, in establishing the Public Company Accounting Oversight Board (the PCAOB), is unconstitutional because it does not permit the President to elect and remove PCAOB members, but rather gives this power to the SEC.

While the lower courts have consistently sided with the PCAOB on all issues, if the plaintiffs were to succeed before the Supreme Court, the PCAOB would be inoperative, at least until Congress amended Sarbanes-Oxley accordingly. For this reason, it is likely that most companies would continue to comply with Sarbanes-Oxley pending the congressional review and amendment process.

However, the fact that Sarbanes-Oxley could be partially or even completely struck down raises the possibility that Congress may take the opportunity to revise other aspects of the statute.

### **SEC Chairman Provides Insight into Commission's Initiatives**

The Chairman of the Securities and Exchange Commission, Mary Shapiro, who became Chairman in January 2009, has given several public speeches in recent months highlighting the Commission's initiatives for 2009 and beyond. None of the initiatives identified would specifically affect the disclosure scheme for public issuers.

On a high level, Chairman Shapiro says that with these initiatives, the Commission aims to bring transparency and accountability to all corners of the marketplace, vigorously prosecute those who have broken the law and cheated investors, and modernize the regulatory system to match the realities of today's global, interdependent markets.

Specific initiatives that Chairman Shapiro has identified as near-term priorities include: (1) improving the quality of credit ratings by addressing the inherent conflicts of interest credit rating agencies face as a result of their compensation models and limiting the impact of credit ratings on capital requirements of regulated financial institutions; (2) reducing systemic risk to investors and markets by promoting — and regulating appropriately — centralized clearinghouses for credit default swaps; (3) strengthening risk-based oversight of broker-dealers and investment advisers; and (4) improving the quality of audits for nonpublic broker-dealers and promoting the safe and sound custody of customer assets by any broker-dealer or

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