

**SECURITIES AND EXCHANGE COMMISSION PROPOSES RULE PERMITTING
DIRECT SHAREHOLDER INVOLVEMENT IN DIRECTOR NOMINATION PROCESS**

On October 14, 2003, the Securities and Exchange Commission (the “Commission”) issued a Release seeking public comment on proposed Rule 14a-11 under the Securities Exchange Act of 1934, as amended (the “Exchange Act”).¹ Rule 14a-11 would require companies to include in their proxy materials the names of nominees for director that are submitted by certain shareholders, as well as disclosure relating to those nominees. The Commission has asked that comments on the proposal be filed no later than December 22, 2003 and expects to adopt a final rule that would take effect January 1, 2004.

The Commission believes that the proposed rule will enhance the ability of security holders to participate meaningfully in the process for nominating and electing directors. Proposed Rule 14a-11 would apply to all operating companies and investment companies that are subject to the Commission’s proxy rules, however, it does not establish an automatic right of shareholders to nominate candidates for election to the board of directors. The proposed rule would apply only in situations where state law, and presumably a corporation’s governing documents, permit the nomination of directors by shareholders. Although most states, including Delaware, permit shareholders to make nominations, many of those states also allow corporations to restrict or entirely eliminate the right of shareholders to nominate directors through their charters or bylaws. If the governing documents of a corporation prohibit shareholders from nominating directors based on the law of the state in which such corporation was formed, proposed Rule 14a-11 would not be available to the shareholders of such corporation.

Nomination Procedure Triggering Events

Shareholder access is available only upon the occurrence of one or more triggering events. The triggers are intended to be objective indicators of potential deficiencies in the proxy process that prevent shareholder views from adequately being taken into account. Shareholders will be allowed to nominate director candidates in a company’s proxy statement when one or both of the following two triggering event occurs:

¹ Securities Exchange Act Release No. 48626 (October 14, 2003). The text of the Release is available at <http://www.sec.gov/rules/proposed/34-48626.htm>.

- a) a shareholder or group of shareholders holding over 1% of the company's shares for at least one year submits a proposal under Rule 14a-8 of the Exchange Act at an annual meeting of shareholders held after January 1, 2004 seeking that the company be subject to the nomination procedure under proposed Rule 14a-11, and that proposal is approved by a majority of the shares voted on that proposal; or
- b) at least one of the company's nominees for director received "withhold" votes from more than 35% of the shares voted at an annual meeting held after January 1, 2004.

Once triggered, shareholder access to the company's proxy statement process would apply for two years. For example, if shareholder access is triggered by an event at a company's 2004 annual meeting of shareholders, shareholder access would then apply to the company's annual meetings in 2005 and 2006.

Each company would be required to disclose the shareholder vote with regard to any triggering event in its quarterly report on Form 10-Q for the period in which the event occurred. If the triggering event took place during the fourth quarter of the fiscal year, the company would be required to disclose such information in its Form 10-K.

The Commission is requesting comment on a possible third triggering event: a shareholder or group of shareholders holding over 1% of the company's shares submits a proposal under Rule 14a-8 (other than a proposal relating to direct nomination by shareholders), and that proposal is approved by a majority of the shares voted and the company's board fails to implement the proposal within 120 days of mailing its proxy materials for the next annual meeting. The Commission notes that if such a triggering event is included in the final rule, any Rule 14a-8 proposal made by an eligible shareholder and adopted subsequent to January 1, 2004 could be a triggering event under the rules, and recommends that, pending final action on the proposal, companies identify such proposals in their proxy statements. In addition, the company would likely need to disclose on Form 8-K a representation that the board of directors believes in good faith that such shareholder resolution has been implemented.

Who Can Nominate Candidates?

Once shareholder access is triggered, any shareholder or group of shareholders beneficially owning at least 5% of a company's shares for at least the prior two years may propose a nominee for inclusion in the company's proxy materials for the next election of directors. Such shareholder or shareholder group must intend to continue to own these securities through the date of that annual or special meeting. Any shareholder nominating a candidate must be a Section 13G filer, in reliance on either Rule 13d-1(b) or 13d-1(c), thereby offering proof that such shareholder has no intention to seek control of the company. Furthermore, the nominating shareholder cannot have an agreement with the company regarding the director's nomination. The Commission has indicated that a nominating shareholder will not be deemed an affiliate of the company under the Securities Act of 1933, as amended (the "Securities Act") or the Exchange Act solely as a result of nominating a director or soliciting for the election of such a

nominee or against a company nominee pursuant to the procedure set forth in proposed Rule 14a-11.

Who Can Be Nominated?

Nominees must be independent from the company and from the nominating shareholder or shareholder group. *Vis-à-vis* the company, nominees would be required to meet a separate independence standard, *i.e.*, the objective criteria for “independence” in any applicable national securities exchange or national securities association rules.² Any independence standard that requires the board or a committee of the board to make a subjective determination whether such director would be independent will not have to be satisfied by the nominee. *Vis-à-vis* the nominating shareholder or shareholder group, proposed Rule 14a-11 sets forth standards of independence. For example, the nominee cannot be an immediate family member, executive officer or director of the nominating shareholder or any member of the nominating shareholder group or any of their respective affiliates. In addition, if the nominating shareholder is a natural person, he or she may not nominate himself or herself for director. Upon nominating a candidate, the nominating shareholder or shareholder group would need to represent to the company that the candidate meets the objective standards of independence set forth above and that neither the nominating shareholder or shareholder group nor the candidate has entered into an agreement with the company regarding such nomination.

How Many Nominees Must a Company Include in its Proxy Statement?

A company would only be required to include a specified number of shareholder-nominated candidates, determined by the number of directors serving on a company’s board. A company would be required to include one shareholder nominee if the total number of directors is eight or fewer, two shareholder nominees if the number of directors is greater than eight and less than 20 and three shareholder nominees if the number of directors is 20 or more. If multiple shareholders or groups were to seek to nominate more directors than are permitted under the rules, the shareholders or groups with the larger beneficial ownership would be given priority.

Notice Requirements

In order to nominate a candidate, an eligible shareholder or group would be required to provide notice to the company at least 80 days before the anniversary of the date the company mailed its proxy statement to shareholders in connection with the previous year’s annual meeting or, if the date of the meeting has changed more than 30 days from the prior year, at a reasonable time

² For this purpose, the nominee would be required to meet the definition of independence that is generally applicable to all directors of the company, rather than the definition of independence applicable to members of the audit committee of the company’s board of directors

before the proxy statement is to be mailed. The notice must include specified information about each nominee as well as representations as to compliance with the rule. In addition, the nominating shareholder would be required to file such notice with the Commission on Schedule 14A no later than two business days after providing notice to the company.

How Will the Contest Work?

A company that receives a notice of nomination from a shareholder would determine whether the nominating shareholder has complied with proposed Rule 14a-11 and whether the nominee satisfies each of the requirements of the proposed procedure. Unless the company determines that it is not required to include a nominee in its proxy materials, the company must include information regarding the nominee in the company's proxy statement and the name of the nominee on the accompanying proxy card. In addition to the required disclosures related to each candidate, the company may wish to include statements in the proxy statement supporting or opposing shareholder nominees. If the company includes such statements in its proxy materials, other than a mere recommendation to vote in favor of or withhold votes from specified candidates, the nominating shareholder or shareholder group would be given the opportunity to include a statement of support for its nominee, not to exceed 500 words, in the company's proxy statement. The company must also include any web site address or any other method of communication by which the nominating shareholder or shareholder group intends to solicit in favor of its nominee. The company must present the nominees in an impartial manner on its proxy card in accordance with Exchange Act Rule 14a-4.

If the company determines that the nominating shareholder has not satisfied proposed Rule 14a-11, then the company must notify the nominating shareholder or shareholder group in writing and state the specific grounds for its determination. The company would need to provide this notice promptly, but in no case less than 30 days before the anniversary of the date on which the company mailed its proxy statement to shareholders in connection with the previous year's annual meeting. If the company did not hold an annual meeting in the previous year or if the date of the current year's annual meeting has been changed by more than 30 days from the anniversary of the date of the previous year's meeting, the notice must be provided a reasonable time before the company mails its proxy materials for the current year. The company would be required to include and disclose in its proxy statement the information provided to the nominating shareholder relating to that determination. The Commission has not set forth the means by which a company's determination is subject to review and is seeking comment on the subject.

All soliciting materials are subject to Exchange Act Rule 14a-9's prohibition on false and misleading statements. A nominating shareholder will be responsible for any false or misleading statements in the disclosure it provides to the company. Any information that is provided to the company in the notice from the nominating shareholder and then included in the company's proxy materials would not be incorporated by reference into any filing by the company under the Securities Act or the Exchange Act, unless the company specifically determines to do so. Once a statement is incorporated by reference into a filing by the company, that statement is considered

disclosed by the company and the company will be held accountable from the date of the filing for any false or misleading statements that are incorporated by reference.

Investment Companies

The nomination procedure of proposed Rule 14a-11 would apply to investment companies in the same manner that it would apply to operating companies, with modifications that reflect the different circumstances and reporting requirements applicable to investment companies.

Several of the disclosure provisions of proposed Rule 14a-11 have been modified for investment companies to reflect the reporting requirements of the Investment Company Act of 1940, as amended (the “Investment Company Act”). For example, because investment companies do not file quarterly reports on Exchange Act Form 10-Q, each investment company would be required to disclose the shareholder vote with regard to any of the nomination procedure triggering events in its semi-annual report on Form N-CSR. If an investment company did not hold an annual meeting during the prior year, or if the date of the meeting has changed more than 30 days from the prior year, such investment company would be required to disclose the date of the meeting in Item 13 of Exchange Act Form 8-K, so that shareholders are made aware in a timely manner of the date by which they must submit a notice of intent to nominate a director.

The standards of independence have been modified to maintain consistency with the Investment Company Act. A nominee for director of an investment company may not be an “interested person” of the investment company as defined in Section 2(a)(19) of the Investment Company Act, rather than comply with the independence standard required of directors of operating companies. Because shareholders of a mutual fund are not required to make filings on Schedule 13G, the rule will require a nominating shareholder of a mutual fund to include certain information (that would otherwise be required on Schedule 13G) in its notice to the fund of the shareholder’s intent to require its nominee to be included on the company’s proxy card. Such information includes a certification by the shareholder that the securities have been held continuously for at least three years and the percentage of each class of securities of the fund that the individual owns beneficially, directly or indirectly, and the number of shares as to which the person has sole or shared power to vote or dispose (or to direct the vote or disposition).

Effect on Other Rules and Related Amendments

The proposed rules will not alter existing rules relating to the conduct of proxy contests, which will continue to apply to shareholders seeking to exercise control over a corporation. Furthermore, the proposed rules will not otherwise alter Exchange Act Rule 14a-8, which relates to shareholder proposals.

The Commission proposes to amend the instructions to Exchange Act Schedule 13G to clarify its view that an eligible shareholder would not become ineligible to file on Schedule 13G as a result of making a nomination, soliciting under the procedure or having a nominee elected to the board. In addition, the Commission proposes to amend the rules under Exchange Act Section 16 so that a shareholder group formed to nominate a director under the new rules would not be considered a

more than 10% holder for Section 16 purposes, so long as the requisite non-control intent remains.

The Release follows a six-month review of the federal proxy rules by the Division of Corporation Finance and is expected to generate a large number of comments. The Commission believes that the proposed rules reach an appropriate compromise between the interest of shareholders in having input into the process of nominating directors and the interest of the company in not having a divided board of directors.

If you wish to obtain additional information regarding these proposed rules, please contact the corporate partner with whom you regularly work.

Willkie Farr & Gallagher LLP is headquartered at 787 Seventh Avenue, New York, NY 10019. Our telephone number is 212-728-8000 and our facsimile number is 212-728-8111. Our web site is located at www.willkie.com.

October 29, 2003

Copyright © 2003 by Willkie Farr & Gallagher LLP

All Rights Reserved. This memorandum may not be reproduced or disseminated in any form without the express permission of Willkie Farr & Gallagher LLP. This memorandum is provided for news and information purposes only and does not constitute legal advice or an invitation to an attorney-client relationship. While every effort has been made to ensure the accuracy of the information contained herein, Willkie Farr & Gallagher LLP does not guarantee such accuracy and cannot be held liable for any errors in or any reliance upon this information.