

**MEMO# 23725**

August 18, 2009

## **ICI Letter on SEC Proposal to Facilitate Shareholder Director Nominations**

[23725]

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TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 32-09  
ETF ADVISORY COMMITTEE No. 26-09  
SEC RULES MEMBERS No. 90-09  
SMALL FUNDS MEMBERS No. 51-09 RE: ICI LETTER ON SEC PROPOSAL TO FACILITATE  
SHAREHOLDER DIRECTOR NOMINATIONS

The Institute filed the attached comment letter with the Securities and Exchange Commission on a proposal that is intended to facilitate shareholders' ability to nominate directors of companies, including investment companies. [\[1\]](#) The letter is summarized below.

The letter points out that as both shareholders of the companies in which they invest and issuers with their own directors and shareholders, investment companies fully recognize the importance of effective corporate governance and also are cognizant of the need to avoid undue interference with the company's officers and directors who are responsible for its management. The letter states that, accordingly, we have a heightened appreciation for the need to balance these interests when addressing shareholder access to company proxy materials.

The letter supports allowing shareholders who meet appropriate eligibility criteria to submit bylaw amendments concerning director nomination procedures on a public operating company's proxy statement. It opposes permitting shareholders to nominate directors on a public operating company's proxy statement.

With respect to investment companies, the letter states that the Commission has not given sufficient consideration to whether there is a need for proxy access requirements and, if so, how they should work. It therefore recommends that the Commission exclude investment companies from the proposal. The letter calls for the Commission instead to consider whether a proxy access proposal should apply to investment companies at all, and if so, how it could craft a new proposal better suited to the unique attributes of investment companies.

## I. Proposed Bylaw Amendments under Rule 14a-8

To help assure that the interests of shareholder proponents are aligned with those of long-term shareholders, the letter recommends that the Commission require that public operating company shareholders be permitted to submit bylaw amendments regarding director nomination procedures only if they own five percent or more of a company's securities for at least one year. The letter also recommends the application of disclosure requirements along the lines of those in proposed Rule 14a-19, which would help make known whether proponents are seeking bylaw amendments to serve their own interests or the interests of long-term shareholders. The letter further recommends requiring proponents of this type of shareholder proposal to state that they do not hold and have not acquired shares for the purpose of or with the effect of influencing or changing control of the company or to gain more than a limited number of seats on the board. The letter additionally recommends that the Commission take steps to make clear that the nominating shareholder, not the company, will have liability for any false or misleading statements in information provided by the shareholder that is then included in the company's proxy statement.

## II. Shareholder Director Nominations Under Proposed Rule 14a-11

The letter opposes the creation of a federally-mandated right and process for shareholders to nominate directors on a public operating company's proxy statement. Rather, it urges the Commission to facilitate the ability of shareholders and companies to work together to tailor companies' governing documents to suit the specific interests of the company and its shareholders. The letter states that as a result, the Commission should not adopt Rule 14a-11 at this time. If the Commission nevertheless determines to adopt Rule 14a-11, the letter recommends modifying it as described below.

### A. Eligibility Requirements

- *Intent of Ownership.* The letter strongly supports the Commission's proposal to limit access to a company's proxy statement to shareholder proponents who do not hold or have not acquired shares "for the purpose of or with the effect of changing control of the company or to gain more than a limited number of seats on the board" and recommends also denying access to the company's proxy statement to any shareholder proponent who seeks to "influence" control of the issuer.
- *Ownership Thresholds.* The letter recommends that shareholders who own

at least ten percent of a company's securities for the required holding period be permitted to nominate directors on a company's proxy statement. It reasons that this threshold would encourage shareholders to come together to effect change, better assuring that the company's proxy machinery would be used to advance the common interests of many shareholders in addressing legitimate concerns about the management and operation of the company.

- *Holding Period.* The letter states that from what we can tell, the Commission did not analyze holding periods with respect to any issuers and recommends that before adopting any final holding periods, the Commission first analyze relevant data. It points out that this analysis should help the Commission determine how best to achieve the policy goal of establishing a meaningful holding period that will further assure that the interests of shareholder proponents are aligned with the interests of long-term shareholders. The letter also states the Institute's belief that a holding period such as two years would provide greater assurance that shareholder proponents are committed to the long-term mission of the company.
- *Maximum Number of Shareholder Nominees.* The letter recommends limiting the number of nominees to one, given the novelty of permitting shareholders to have their director nominees included in a company's proxy materials.
- *Timing of Submitting Nominees.* The letter recommends permitting the shareholder or group of shareholders with the most significant stake in the company to put forward its nominee.
- *Notice and Disclosure Requirements for Shareholder Proponents.* The letter generally supports the proposed notice and disclosure requirements, and recommends adding a requirement that nominating shareholders disclose their motivation in seeking a nomination (e.g., to gain publicity for a particular policy issue) and any formerly recommended nominees.
- *Universal Proxy.* The letter strongly recommends permitting issuers to provide shareholders with the ability to check a box and vote for the entire company-recommended slate.
- *Liability.* The letter strongly supports the Commission expressly providing in rule text that the nominating shareholder would be liable for statements provided by the nominating shareholder to the company and included in the company's proxy materials. Consistent with this approach, the letter recommends modifying the proposal to provide that a company would not be responsible for any disclosure in the company's proxy statement based on information provided by the nominating shareholder. The letter also recommends modifying the proposal so that the company only would be responsible for false and misleading information provided by a nominating shareholder if the company knows that information is false or misleading.

### III. Applicability to Investment Companies

The letter recommends that the current proposal exclude investment companies, for several reasons, including that the Commission has not articulated its policy rationale for applying the proposed requirements to investment companies; the proposal does not remotely account for the significant differences in governance models between

public operating companies and investment companies, including the most prevalent types of investment company boards—unitary or cluster boards—and other important differences; and the Commission has not given sufficient consideration to the potential impact of the proposed requirements on investment companies, particularly on small fund complexes.

#### IV. Other Comments

The letter states that should the Commission, in the future, develop a new proposal for investment companies, the Commission should consider the following additional comments.

- Access to a company’s proxy statement should be limited to shareholders who do not hold or have not acquired shares “for the purpose of or with the effect of changing or influencing control of the company or to gain more than a limited number of seats on the board.” This is particularly important in the investment company context to make clear that access would be denied to shareholder proponents who intend to “open-end” a closed-end fund.
- Shareholder nominees of investment companies should not be “interested persons” of the investment company, as defined in Section 2(a)(19) of the Investment Company Act.
- Any investment company nominating shareholder and nominee should be required to disclose their motivation, including, among other matters, whether there is any intention to modify the fund’s investment objective or policies.
- Investment companies should not be required to file a Form 8-K. Rather, investment companies should be required to inform shareholder proponents of the date by which a shareholder proponent must submit notice of its intent to require that the company include that shareholder proponent’s nominee on the company’s proxy statement through another method of disclosure that is reasonably designed to provide notice of the date to their shareholders.

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[Attachment](#)

#### endnotes

[1] See [Memorandum](#) to Closed-End Investment Company Members No. 25-09; SEC Rules Members No. 67-09; Small Funds Members No. 38-09 [23572], dated June 22, 2009 (summarizing the proposal).

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