SECURITIES AND EXCHANGE COMMISSION

This file is maintained pursuant to the Freedom of Information Act (5 U.S.C. 552). It contains a copy of each decision, order, rule or similar action of the Commission, for **August 2010,** with respect to which the final votes of individual Members of the Commission are required to be made available for public inspection pursuant to the provisions of that Act.

Unless otherwise noted, each of the following individual Members of the Commission voted affirmatively upon each action of the Commission shown in the file:

MARY L. SCHAPIRO, CHAIRMAN

KATHLEEN L. CASEY, COMMISSIONER

ELISSE B. WALTER, COMMISSIONER

LUIS A. AGUILAR, COMMISSIONER

TROY A. PAREDES, COMMISSIONER

(62 Documents)

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

June 22, 2010

IN THE MATTER OF	:	
Green Energy Resources, Inc.	:	**ORDER OF SUSPENSION OF TRADING**
File No. 500-1	:	

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Green Energy Resources, Inc. ("Green Energy") because of questions regarding the accuracy of statements by Green Energy in press releases concerning, among other things, the company's involvement in the Gulf of Mexico oil spill cleanup effort.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of Green Energy.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed company is suspended for the period from 9:30 a.m. EDT June 22, 2010 through 11:59 p.m. EDT, on July 6, 2010.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9131 / August 2, 2010

In the Matter of **General Electric Company,** **Respondent.**	**ORDER UNDER RULE 602(e) OF THE SECURITIES ACT OF 1933 GRANTING A WAIVER OF THE RULE 602(c)(2) & 602(b)(4) DISQUALIFICATION PROVISIONS**

I.

General Electric Company ("GE") has submitted a letter, dated June 18, 2010, requesting a waiver of the Rule 602(c)(2) and 602(b)(4) disqualifications from the exemption from registration under Regulation E arising from GE's settlement of an injunctive action commenced by the Commission.

II.

On July 30, 2010, the Federal District Court for the District of Columbia entered a final judgment permanently enjoining GE and two of its subsidiaries, Ionics, Inc., currently GE Ionics, Inc. ("Ionics"), and Amersham plc, currently GE Healthcare Ltd. ("Amersham"), from violating Sections 13(b)(2)(A) and 13(b)(2)(B) of the Securities Exchange Act of 1934. The complaint alleges that from 2000 to 2003 GE, Ionics, and Amersham violated the books and records and internal controls provisions of the Foreign Corrupt Practices Act by paying, or agreeing to pay, approximately $3.6 million in illegal kickbacks in connection with the United Nations Oil for Food Program in Iraq. The complaint alleges that GE, Ionics, and Amersham failed to keep books, records, and accounts, which in reasonable detail, accurately and fairly reflected these transactions. The complaint further alleges that GE, Ionics, and Amersham failed to ensure that their subsidiaries maintained systems of internal accounting controls sufficient to provide reasonable assurances that: (i) payments were made in accordance with management's general or specific authorization; and (ii) payments were recorded as necessary to maintain accountability for the companies' assets.

III.

The Regulation E exemption is unavailable for the securities of small business investment company issuers or business development company issuers if such issuer or any of its affiliates is subject to a court order entered within the past five years "permanently restraining or enjoining such person from engaging in or continuing any conduct or practice in connection with the purchase or sale of securities," 17 C.F.R. § 230.602(b)(4), or if any of the issuer's directors, officers or principal security holders, any investment adviser or underwriter of the securities to be offered, or any partner, director or officer of any such investment adviser or underwriter of the securities to be offered is "temporarily or permanently restrained or enjoined by any court from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security or arising out of such person's conduct as an underwriter, broker, dealer or investment adviser." 17 C.F.R. § 230.602(c)(2). Rule 602(e) of the Securities Act of 1933 ("Securities Act") provides, however, that the disqualification "shall not apply . . . if the Commission determines, upon a showing of good cause, that it is not necessary under the circumstances that the exemption be denied." 17 C.F.R. § 230.602(e).

IV.

Based upon the representations set forth in GE's request, the Commission has determined that pursuant to Rule 602(e) under the Securities Act a showing of good cause has been made that it is not necessary under the circumstances that the exemption be denied as a result of the Final Judgment.

Accordingly, **IT IS ORDERED**, pursuant to Rule 602(e) under the Securities Act, that a waiver from the application of the disqualification provisions of Rule 602(c)(2) and 602(b)(4) under the Securities Act resulting from the entry of the Final Judgment is hereby granted.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62627 / August 2, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13990

In the Matter of **UB&T Financial Services Corp.,** **United Community Holdings, Inc.,** **United Homes, Inc.,** **United Magazine Co., and** **United Shields Corp.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents UB&T Financial Services Corp., United Community Holdings, Inc., United Homes, Inc., United Magazine Co., and United Shields Corp.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. UB&T Financial Services Corp. (CIK No. 1070730) is a Georgia corporation located in Rockmart, Georgia with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). UB&T Financial Services is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 1999.

2. United Community Holdings, Inc. (CIK No. 1016130) is a permanently revoked Nevada corporation located in Jackson, Mississippi with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). United Community Holdings is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 2001, which reported a net loss of $73,942 for the prior three months.

3. United Homes, Inc. (CIK No. 1010047) is an Illinois corporation located in Rolling Meadows, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). United Homes is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q/A for the period ended June 30, 1999, which reported a net loss of $442,493 for the prior nine months. On March 9, 2000, the company filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Northern District of Illinois, and the case was still pending as of July 29, 2010.

4. United Magazine Co. (CIK No. 20469) is a canceled Ohio corporation located in Dublin, Ohio with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). United Magazine is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K/A for the period ended October 2, 1999, which reported a net loss of $145,900,000 for the twelve months. On June 23, 1998, a Chapter 11 petition was filed against the company in the U.S. Bankruptcy Court for the Southern District of Ohio, and the case was terminated on August 25, 1998.

5. United Shields Corp. (CIK No. 808432) is a dissolved Colorado corporation located in Cleveland, Tennessee with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). United Shields is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-KSB/A for the period ended December 28, 2001, which reported a net loss of $9,632,068 for the prior year. As of July 29, 2010, the company's stock (symbol "UNSC") was traded on the over-the-counter markets.

B. DELINQUENT PERIODIC FILINGS

6. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission, have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

7. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires issuers to file quarterly reports.

8. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II are true and, in connection therewith, to afford the Respondents an opportunity to establish any defenses to such allegations; and,

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, or fail to appear at a hearing after being duly notified, the Respondents, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents, may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondents personally or by certified, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E Harmon
Deputy Secretary

Chairman Schapiro not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 62630 / August 3, 2010

INVESTMENT ADVISERS ACT OF 1940
Rel. No. 3063 . / August 3, 2010

Admin. Proc. File No. 3-13655

In the Matter of THEODORE W. URBAN c/o John H. Sturc, Esq. Gibson, Dunn & Crutcher LLP 1050 Connecticut Avenue, NW Washington, D.C. 20036	ORDER GRANTING EXTENSION

The Chief Administrative Law Judge, who is presiding over this proceeding, has moved, pursuant to Commission Rule of Practice 360(a)(3),[1] for an extension of time to issue her initial decision. For the reasons set forth below, we have determined to grant the law judge's motion.

On October 19, 2009, we issued an Order Instituting Proceedings ("OIP") against Theodore W. Urban, formerly the General Counsel, the compliance department supervisor, and a director of Ferris Baker Watts, Inc. ("Firm"), a broker-dealer and investment adviser registered with the Commission. The OIP alleged that Urban failed reasonably to supervise a Firm registered representative with a view to detecting the representative's violations of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934, and Exchange Act Rule 10b-5.

The OIP directed the presiding law judge to hold a public hearing to take evidence regarding the allegations and the appropriate sanctions. The OIP further specified that, pursuant to Commission Rule of Practice 360(a)(2),[2] the presiding law judge should issue an initial decision in this proceeding no later than 300 days from the date of service of the OIP. The initial decision is due on August 17, 2010. On July 14, 2010, the Chief Administrative Law Judge filed

---

1 17 C.F.R. § 201.360(a)(3).

2 17 C.F.R. § 201.360(a)(2).

a motion pursuant to Commission Rule of Practice 360(a)(3)[3] requesting an extension of time of thirty days to issue such decision.

II.

We adopted Rules of Practice 360(a)(2) and 360(a)(3) as part of an effort to enhance the timely and efficient adjudication and disposition of Commission administrative proceedings.[4] At that time, we determined that the adoption of mandatory deadlines for completion of administrative hearings would enhance timely completion of the adjudication process. In adopting those guidelines, however, we recognized that a "'one size fits all' approach to timely disposition is not feasible."[5] We therefore established three different deadlines – 120, 210, or 300 days – depending on "the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors."[6]

We further provided for the granting of extensions to those deadlines under certain circumstances. If, during the proceeding, the presiding law judge decides that the proceeding cannot be concluded in the time specified in the OIP, Rule 360(a)(3) provides that the law judge may request an extension of the stated deadline. To obtain an extension, the law judge should consult with the Chief Administrative Law Judge.[7] "Following such consultation, the Chief Administrative Law Judge may determine, in his or her discretion, to submit a motion to the Commission requesting an extension."[8] The motion should "explain [ ] why circumstances require an extension and specify [ ] the length of the extension."[9] While we intend to grant extensions sparingly, we may authorize an extension on the basis of the Chief Administrative Law Judge's motion, if we determine that "additional time is necessary or appropriate in the public interest."[10] We note, however, that a heavy docket alone will not ordinarily be cause for an extension.

---

3 17 C.F.R. § 201.360(a)(3).

4 *See Adopting Release*, Securities Act Rel. No. 8240 (June 11, 2003), 80 SEC Docket 1463.

5 *Id.*

6 17 C.F.R. § 201.360(a)(2).

7 The law judge presiding in this proceeding also serves as the Chief Administrative Law Judge.

8 17 C.F.R. § 201.360(a)(3).

9 *See Adopting Release* at 1463.

10 17 C.F.R. § 201.360(a)(3).

The Chief Administrative Law Judge supports her extension request by stating that the initial decision cannot be issued within the specified time "because of the size of the record and the complexity of the issues." The law judge states that she "held thirteen days of hearing in March 2010" and that the "record consists of 3,000 pages of transcript, over 250 exhibits, and some expert testimony." In light of the complexity of the case and the reasonableness of the requested extension, we believe that it is appropriate in the public interest to extend the deadline for filing the initial decision by thirty days.

Accordingly, IT IS ORDERED that the deadline for filing the initial decision in this matter be, and it hereby is, extended until September 16, 2010.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62636 / August 4, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3163 / August 4, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13993

In the Matter of

THOMAS P. FLANAGAN, CPA,

Respondent.

ORDER INSTITUTING PUBLIC ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 4C AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Thomas P. Flanagan, CPA ("Respondent" or "Flanagan") pursuant to Sections 4C[1] and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 102(e)(1)(ii) and Rule 102(e)(1)(iii) of the Commission's Rules of Practice.[2]

---

[1] Section 4C provides, in relevant part, that the Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others . . . (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations thereunder.

[2] Rule 102(e)(1)(ii) provides, in pertinent part, that "[t]he Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct." Rule 102(e)(1)(iii) provides, in pertinent part,

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[3] that:

A. SUMMARY

This matter involves dozens of violations of the auditor independence rules by an accountant who owned and controlled securities in nine audit clients. Between December 2003 and July 2008, Thomas P. Flanagan ("Flanagan"), a partner and a Vice Chairman at Deloitte & Touche LLP, made 71 trades in which he purchased stock or options in Deloitte audit clients, 62 of which were in the securities of audit clients for whom Flanagan was serving on Deloitte's engagement team as the advisory partner. Flanagan concealed his ownership and control of these securities from Deloitte and the audit clients. During the time Flanagan owned or controlled these securities, Deloitte issued audit reports to these nine audit clients in which it stated that the financial statements contained in the reports had been audited by an independent auditor. These clients then filed with the Commission annual reports and proxy statements, which included these false audit reports.

B. RESPONDENT

1. **Thomas P. Flanagan**, CPA, age 62, of Chicago, Illinois, is a certified public accountant licensed to practice in the state of Illinois. He was a partner at Deloitte & Touche LLP ("Deloitte")

---

that "[t]he Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found…to have willfully violated, or willfully aided and abetted the violation of any provision of the Federal securities laws or the rules and regulations thereunder."

[3] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

and its predecessor firms from 1978 until September 2008. At the time of his departure from Deloitte, Flanagan was a Vice Chairman in Deloitte's Chicago and had over 35 years of public-company audit experience.

C. RELEVANT ENTITIES

2. **Deloitte & Touche LLP** is a Delaware limited liability partnership. Deloitte is a subsidiary of Deloitte LLP, a US member firm of Deloitte Touche Tohmatsu, which is a Swiss Verein that is organized as an association of independent member firms worldwide which provides professional services under the "Deloitte" brand name. Deloitte is registered with the Public Company Accounting Oversight Board ("PCAOB"). At all relevant times and continuing to the present, Deloitte has provided auditing services to a variety of companies, including companies whose securities are registered with the Commission and traded in the U.S. markets.

3. **Allstate Corp. ("Allstate")** is a Delaware corporation based in Northbrook, Illinois. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act [15 U.S.C. §78l(b)] and is traded on the New York Stock Exchange and Chicago Stock Exchange. Deloitte has served as Allstate's auditor since 1994.

4. **Berkshire Hathaway, Inc. ("Berkshire Hathaway")** is a Delaware corporation based in Omaha, Nebraska. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange. Deloitte has served as Berkshire Hathaway's, or one of its predecessor's, auditor since 1985.

5. **Best Buy Co., Inc. ("Best Buy")** is a Minnesota corporation based in Richfield, Minnesota. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange and the Chicago Stock Exchange. Deloitte has served as Best Buy's auditor since 2005.

6. **CBOT Holdings, Inc. ("CBOT")** was a Delaware corporation based in Chicago, Illinois. Its common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and was traded on the New York Stock Exchange. CBOT merged with Chicago Mercantile Exchange Holdings, Inc. in July 2007 and is no longer a publicly traded company. Deloitte served as CBOT's auditor from at least 2001 until 2007.

7. **CNA Financial Corp. ("CNA")** is a Delaware corporation based in Chicago, Illinois. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange and the Chicago Stock Exchange. Deloitte has served as CNA's auditor since at least 1994.

8. **Sears Holding Corporation** (collectively with its predecessor Sears, Roebuck & Co., **"Sears")** is a Delaware corporation based in Hoffman Estates, Illinois. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the NASDAQ. Deloitte has served as Sears' auditor for over 70 years.

9. **ServiceMaster Company ("ServiceMaster")** is a Delaware corporation based in Memphis, Tennessee. In 2006 and 2007, its common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and was traded on the New York Stock Exchange. ServiceMaster was purchased by a private equity firm in 2007 and is no longer a publicly traded company. Deloitte has served as ServiceMaster's auditor since 2002.

10. **USG Corp. ("USG")** is a Delaware corporation based in Chicago, Illinois. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange and Chicago Stock Exchange. Deloitte has served as USG's auditor since 2002.

11. **Walgreen Company ("Walgreens")** is an Illinois corporation based in Deerfield, Illinois. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and is traded on the New York Stock Exchange, NASDAQ, and the Chicago Stock Exchange. Deloitte has served as Walgreens' auditor since 2002.

D. FACTS

Flanagan was Subject to the Commission's Auditor Independence Rules

12. At all relevant times, Deloitte was the auditor responsible for the audits or reviews of the annual and quarterly financial statements for Allstate, Berkshire Hathaway, Best Buy, CBOT, CNA, Sears and its predecessor Sears, Roebuck and Co., ServiceMaster, USG, and Walgreens ("collectively, "the Audit Clients") filed with the Commission.

13. Flanagan served as the Advisory Partner on Deloitte's audit engagements with seven of the nine Audit Clients, including Allstate from 2003 to 2008; Berkshire Hathaway from 2002 to 2008; Best Buy from 2005 to 2008; Sears from 2002 to 2008; ServiceMaster from 2003 to 2006; USG from 2004 to 2008; and Walgreens from 2003 to 2008 (collectively, "the Flanagan Advisory Clients").

14. Advisory Partners are assigned by Deloitte to certain clients and play an important role in these engagements. As the Advisory Partner for the Flanagan Advisory Clients, Flanagan, among other things, served as a liaison between management and the Deloitte audit engagement team, attended Audit Committee meetings, received and had access to nonpublic information regarding the Flanagan Advisory Clients' earnings results and other information, and in some cases, participated in the evaluation of the performance of other partners serving that client.

15. Flanagan was required to comply with the Commission's auditor independence rules with respect to the Flanagan Audit Clients because as the Advisory Partner, he was a "covered person" under those rules. Flanagan was also required to comply with the auditor independence rule with respect to CBOT and CNA because by working in the same office as the lead partner on those engagements, he was a covered person.

16. Under the Commission's auditor independence rules, accountants are not independent as to an audit client if, among other things, the accounting firm, or any covered person in the firm, or any of his or her immediate family members has a direct investment in the audit client, such as stocks, bonds, notes, options, or other securities, or if the accountant serves as the voting trustee of a trust containing securities of an audit client. Flanagan knew and understood this rule.

Flanagan Owned or Controlled the Audit Clients' Securities

17. Between 2003 and 2008, Flanagan made 71 purchases of stock and options in the securities of the Audit Clients. He made all of these purchases in accounts he owned, in accounts he controlled for the benefit of family members, or in a family trust account for which he served as trustee. Flanagan had the authority to make trades in all of these accounts.

18. Flanagan owned or controlled securities in AllState between July 18, 2006 and July 20, 2006.

19. Flanagan owned or controlled securities in Berkshire Hathaway between April 21, 2005 and June 9, 2006.

20. Flanagan owned or controlled securities in Best Buy on or between:

A) September 9, 2005;
B) December 9, 2005 and December 14, 2005;
C) May 25, 2006 and September 21, 2006
D) December 11, 2006 and December 12, 2006;
E) May 1, 2007 and July 13, 2007;
F) December 4, 2007 and December 21, 2007;
G) February 13, 2008 and March 5, 2008;
H) April 1, 2008 and May 19, 2008; and
I) June 4, 2008 and July 18, 2008.

21. Flanagan owned or controlled securities in CBOT between September 28, 2006 and July 10, 2007.

22. Flanagan owned or controlled securities in CNA between November 17, 2003 and February 20, 2004.

23. Flanagan owned or controlled securities in Sears between:

A) December 17, 2003 and April 18, 2004;
B) June 1, 2004 and October 22, 2004;
C) February 17, 2006 and March 23, 2006; and
D) May 19, 2008 and May 30, 2008.

24. Flanagan owned or controlled securities in ServiceMaster between February 3, 2006 and January 19, 2007.

25. Flanagan owned or controlled securities in USG between April 12, 2004 and June 8, 2004, and between July 12, 2007 and July 26, 2007.

26. Flanagan owned or controlled securities in Walgreens between:

A) December 21, 2003 and February 24, 2004;
B) September 22, 2005 and November 1, 2005;
C) March 21, 2006 and April 3, 2006;
D) December 18, 2006 and January 5, 2007;
E) March 16, 2007 and July 20, 2007; and
F) September 10, 2007 and October 5, 2007.

Flanagan Concealed His Trading in the Clients' Securities and Circumvented Deloitte's Independence Compliance System

27. At all relevant times, Deloitte had policies and quality control procedures in place to ensure that its professional personnel maintained their independence relative to Deloitte's audit clients. Deloitte's independence policies were primarily contained in Deloitte's Independence Manual. Deloitte's Independence Compliance system included the use of computer databases to monitor the financial interests of its partners.

28. Flanagan knew and understood these policies and procedures.

29. Deloitte's independence procedures required, among other things, that its professional personnel, including partners, self-report all of their securities holdings and trading activities. These professionals were also required to report all securities trades that they made as a trustee for accounts they controlled. Deloitte created the Deloitte Entity Search and Compliance system ("DESC") and the Tracking and Trading system ("Tracking and Trading") for the employees to use to report these transactions.

30. The DESC contained a "Restricted Entity List," which contained the names of all companies, banks, brokerage firms, and other institutions that Deloitte prohibited employees from, among other things, having a financial interest in or maintaining an account. All of Deloitte's audit clients within the United States, including the Audit Clients at issue here, were included in the Restricted Entity List, which Deloitte updated daily. Prior to making a securities trade, Deloitte required employees to access the DESC and Restricted Entity List to verify that the company, brokerage firm, or other entity involved in the transaction was not restricted. After completing the transaction, employees had 10 calendar days to report it to Deloitte via Tracking and Trading.

31. Deloitte also required its employees to file annual Independence Representations in which the employees were to affirm between 30 and 50 specific statements. These statements concerned the employee's financial transactions during the previous year, the employee's understanding of, and compliance with, Deloitte's independence policies, and other topics. If the employee responded to a statement with anything other than "Agree," the employee had to provide a written explanation, which Deloitte's Independence and Ethics Compliance Group then reviewed.

32. Flanagan concealed from Deloitte his trades in the Audit Clients' securities by failing to report these trades in the Tracking and Trading System, and thereby circumvented Deloitte's Independence Compliance system.

33. Flanagan lied to Deloitte about his compliance with Deloitte's independence policies. In the Independence Representations he filed in 2004, 2005, 2006, and 2007, Flanagan falsely affirmed that:

A) Tracking and Trading accurately reflected the brokerage accounts and financial interests held or controlled by Flanagan;
B) at no time during the representation period did he have a financial interest in a Restricted Entity; and
C) he had not served as a trustee, executor, or administrator of an estate that had a financial interest in a Restricted Entity.

34. In fact, Flanagan owned or controlled several brokerage accounts, as well as stocks and options that he had not reported in Tracking and Trading. He also owned or controlled stocks and options in Restricted Entities, including the Audit Clients for whom he served as an Advisory Partner. In addition, Flanagan served as the trustee for a family trust and controlled brokerage accounts in the name of that trust and in the name of other family members. Flanagan traded in the securities of the Audit Clients in several of these accounts.

35. Flanagan's efforts to conceal from Deloitte his trades in the Audit Clients' securities extended to the furnishing of false information in the preparation of his personal income tax returns. He utilized Deloitte Tax LLP ("Deloitte Tax") to prepare his tax returns. Flanagan provided Deloitte Tax personnel with the names of the securities he purportedly traded during the tax year, the trade dates, and his gains or losses. For the tax years 2004 through 2007, Flanagan substituted the names of Deloitte audit clients whose securities he traded in with the names of other entities for which he had no trading restrictions. Between 2004 and 2007, Flanagan substituted unrestricted company names for 13 trades that he made in the securities of seven of the Audit Clients including Best Buy, CBOT, CNA, Sears, USG, and Walgreens.

Deloitte Represented that it was Independent from the Clients

36. Deloitte represented that it was independent in the Report of Independent Registered Public Accounting Firm ("audit reports") it provided to these Audit Clients for the audit years

listed below. In these reports, Deloitte stated that it had performed the audits in accordance with the standards of the PCAOB.

A) Allstate for its fiscal year 2006;
B) Berkshire Hathaway for its fiscal years 2005 and 2006;
C) Best Buy for its fiscal years 2006, 2007, 2008, and 2009;
D) CBOT for its fiscal year 2007;
E) CNA for its fiscal years 2003 and 2004;
F) Sears for its fiscal years 2003, 2004, and 2008;
G) ServiceMaster for its fiscal years 2006 and 2007;
H) USG for its fiscal years 2004 and 2007; and
I) Walgreens for its fiscal years 2004, 2005, 2006, and 2007.

37. The Audit Clients then filed annual reports and proxy statements with the Commission that included Deloitte's audit reports. The Audit Clients also filed quarterly reports with the Commission that had been reviewed by Deloitte.

38. Deloitte also represented to each of the Audit Clients at the end of each affected fiscal year that it was "independent" within the meaning of the federal securities laws and therefore able to serve as each client's external auditor. These written confirmations – commonly called ISB(1) Letters (for Independence Standards Board Standard No. 1, *Independence Discussions With Audit Committees*) – did not disclose Flanagan's ownership or control of securities in the client. Standard No. 1 was carried forward as part of the PCAOB's interim standards when the ISB ceased operations.

Violations

39. Rule 2-01(c)(1) of Regulation S-X states, in part, that:

> An accountant is not independent if, at any point during the audit and professional engagement period, the accountant has a direct financial interest or a material indirect financial interest in the accountant's audit client, such as:
>
> (i) Investment in audit clients. An ac*countant is not independent when:*
>
>> *A)* ... *any* covered person in the firm, or any of his or her immediate family members, has any direct investment in an audit client, such as stocks, [or] options ...;
>>
>> ...
>>
>> C) ... any covered person in the firm ... serves as voting trustee of a trust, ... containing the securities of an audit client, unless the ... covered person in the firm, ... has no authority to make investment decisions for the trust or estate.

40. Professional independence standards for accountants and auditors, as set forth in AICPA ET Rule 101.02, and adopted by PCAOB as its interim ethical standards under Rule 3600T, state, in part, that:

> Independence shall be considered to be impaired if during the period of the professional engagement a covered member had ... any direct or material indirect financial interest in the client [or] was a trustee ... if such trust ... had ... any direct or material indirect financial interest in the client and the covered member ...had the authority to make investment decisions for the trust ....

41. Flanagan was a covered person as to all of the Audit Clients during the relevant periods.

42. Flanagan lacked independence under Rule 2-01(c)(1) of Regulation S-X, PCAOB Rule 3600T, and AICPA ET Rule 101.02 when he owned securities in the Audit Clients in accounts he owned, in accounts he controlled for the benefit of family members, and in a family trust account for which he served as trustee.

43. Rule 2-02(b)(1) of Regulation S-X requires accountants' reports to state "whether the audit was made in accordance with generally accepted auditing standards." "[R]eferences in Commission rules and staff guidance and in the federal securities laws to GAAS or to specific standards under GAAS, as they relate to issuers, should be understood to mean the standards of the PCAOB . . . ." SEC Release No. 34-49708. Thus, an auditor violates Rule 2-02(b)(1) of Regulation S-X if it issues a report stating that it had conducted its audit in accordance with PCAOB standards when it had not.

44. As a result of Flanagan's conduct described above, Deloitte violated Rule 2-02(b)(1) of Regulation S-X. Deloitte's audits and interim reviews of the Audit Clients were not conducted in accordance with PCAOB standards because Flanagan, a covered person in Deloitte, lacked independence as to those Audit Clients. Flanagan willfully aided and abetted and caused Deloitte's violations of Rule 2-02(b)(1) of Regulation S-X.

45. Flanagan willfully aided and abetted and caused the Audit Clients' violations of Section 13(a) of the Exchange Act, and Rules 13a-1 and 13a-13 thereunder, which require issuers to file annual reports containing financial statements certified by independent public accountants, and violations of Section 14(a) of the Exchange Act, and Rule 14a-3 thereunder, which require that proxy statements contain financial statements certified by independent public accountants.

46. As a result of the conduct described above, Flanagan engaged in improper professional conduct. For accountants, improper professional conduct includes "intentional or knowing conduct, including reckless conduct that results in a violation of applicable professional standards." Rule 102(e)(1)(iv)(A). Flanagan intentionally and knowingly owned and controlled securities of

Deloitte audit clients while a covered person and thus failed to comply with Rule 2-01(c)(1) of Regulation S-X, and violated PCAOB Rule 3600T and AICPA ET Rule 101.02.

Findings

47. Based on the foregoing, the Commission finds that Flanagan engaged in improper professional conduct within the meaning of Rule 102(e)(1)(ii) of the Commission's Rules of Practice.

48. Based on the foregoing, the Commission finds that Flanagan (a) willfully aided and abetted and caused Deloitte's violations of Rule 2-02(b)(1) of Regulation S-X; and (b) willfully aided and abetted and caused the Audit Clients' violations of Sections 13(a) and 14(a) of the Exchange Act, and Rules 13a-1, 13a-13, and 14a-3 promulgated thereunder.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Flanagan's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Flanagan shall cease and desist from causing any violations and any future violations of Sections 13(a) and 14(a) of the Exchange Act, and Rules 13a-1, 13a-13, and 14a-3 promulgated thereunder and of Rule 2-02(b)(1) of Regulation S-X.

B. Flanagan is denied the privilege of appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 62649 / August 4, 2010

Admin. Proc. File No. 3-13888

In the Matter of
BCI TELECOM HOLDING, INC.

ORDER DISMISSING PROCEEDINGS AGAINST BCI TELECOM HOLDING, INC.

On May 11, 2010, we issued an Order Instituting Proceedings ("OIP") against BCI Telecom Holding, Inc. ("BCI"), and other issuers, under Section 12(j) of the Securities Exchange Act of 1934.[1] The OIP alleged that BCI "had a class of securities registered with the Commission pursuant to Exchange Act Section 12(g)" and that BCI was "delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 40-F for the period ended December 31, 2001 . . . ."

On June 7, 2010, the Division of Enforcement moved to dismiss BCI from the proceeding. The Division indicates that its determination to proceed against BCI was the result of confusion between BCI and a corporate affiliate, Bell Canada International, Inc. ("Bell Canada"). Apparently, BCI contacted the Division to clarify its registration status after proceedings were instituted. Based on this clarification and further review of Commission records, the Division determined that the proceedings should be dismissed because, as discussed below, BCI in fact did not have a class of securities registered under Exchange Act Section 12.

According to the Division, BCI originally was named Bell Canada International, Inc. but changed its name to BCI on September 4, 1997. Also on September 4, 1997, Bell Canada, which had been known as 139125 Bell Canada Inc., changed its name to BCI's former name, Bell Canada International, Inc. To further complicate matters, Bell Canada, which had originally been issued a Central Index Key ("CIK") number and file number of 921095 and 0-29456, respectively, inexplicably began using in 2002 the CIK and file numbers, 1119954 and 0-31384

---

1 15 U.S.C. § 78*l*(j).

that had been assigned to BCI.[2] Bell Canada continued using BCI's CIK and file numbers until January 8, 2004, when it filed a Form 15 deregistering its stock.

The Division asserts that "BCI never had a class of securities registered under its CIK or file numbers (CIK No. 1119954 and file number 0-31384), and that the reporting obligations under Exchange Act Section 13(a) were triggered by Bell Canada International, Inc.'s filing under CIK No. 921095 and file number 0-29456." As a result, according to the Division, the proceeding "should be dismissed because [BCI] has no securities registered under Exchange Act Section 12 to be suspended or revoked." Counsel for BCE, Inc., former corporate parent of BCI, filed a brief in support of the Division's motion, in which it confirmed the Division's presentation of the relevant facts, including that BCI has no securities registered under Exchange Act Section 12. BCE further represented that neither BCI nor Bell Canada "remains in existence."

Under the circumstances and because revocation or suspension of registration are the only remedies available in this proceeding, we find it appropriate to grant the Division's motion and dismiss BCI from the proceeding.[3]

Accordingly, it is ORDERED that the proceeding with respect to BCI, Inc. be, and it hereby is, dismissed.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

---

2 The CIK number is designed to be a unique identifier assigned to each entity that is required to file reports with the Commission.

3 *See TelcoBlue, Inc.*, Securities Exchange Act Rel. No. 58061 (June 30, 2008), 93 SEC Docket 7335, 7335 (dismissing Section 12(j) proceeding with respect to a respondent that "no longer [had] a class of securities registered under Section 12 of the Exchange Act").

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 62645 / August 4, 2010

Admin. Proc. File No. 3-13733

In the Matter of the Application of MANUEL P. ASENSIO c/o Mill Rock Investment Advisors 747 Third Avenue, 25th Floor New York, NY 10017 For Review of Disciplinary Action Taken by FINRA	ORDER DENYING MOTION FOR RECONSIDERATION

I.

On June 17, 2010, we issued an order ("June 17 Order") granting NASD's [1] motion to dismiss the application for review filed by Manuel P. Asensio, formerly a registered representative associated with Asensio Brokerage Services, Inc. ("ABSI" or the "Firm"), a former NASD member firm, of a 2006 NASD decision barring him from association with any NASD member (the "2006 Bar Decision") and a 2008 FINRA denial of an application for him to associate with another member firm (the "2008 Eligibility Denial Decision"). We found that Asensio failed to appeal these decisions until well after the applicable thirty-day deadlines.[2] The June 17 Order also rejected numerous motions and requests filed by Asensio. On June 24, 2010,

---

[1] On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD's Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority, Inc. ("FINRA"), in connection with the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. *See* Securities Exchange Act Rel. No. 56146 (July 26, 2007), 91 SEC Docket 517.

[2] *Manuel P. Asensio*, Securities Exchange Act Rel. No. 62315 (June 17, 2010), __ SEC Docket ____.

Asensio filed a motion for reconsideration of the June 17 Order and amended that motion on July 7, 2010.

II.

We consider Asensio's motion under Rule 470 of the Commission's Rules of Practice.[3] The "exceptional remedy" of a motion for reconsideration is designed to correct manifest errors of law or fact, or to permit the presentation of newly discovered evidence.[4] Applicants may not use motions for reconsideration to reiterate arguments previously made or to cite authority previously available. Moreover, we will accept only such additional evidence that "the movant could not have known about or adduced before entry of the order subject to the motion for reconsideration."[5] Asensio's motion does not meet this standard.

In general, Asensio's motion restates arguments made in his previous motions and responses and considered by us in the June 17 Order. We will not readdress those matters here. However, his motion raises some points that we briefly address.

1. Appointments Clause Contention

In the June 17 Order, we rejected Asensio's contention that FINRA's sanction regimen violates the Appointments Clause of the U.S. Constitution, noting, as Asensio himself pointed out, that FINRA "executives and board are not appointed by the U.S. President, nor are they appointed by any other governmental body." Asensio now maintains that we "fundamentally mischaracterized" his argument. He asserts that the:

> imposition and ongoing administration of [his] bar sanction . . . including FINRA's denial of [his] MC-400 and any future denial of a MC-400 submitted by

---

[3] 17 C.F.R. § 201.470. The Comment to Rule 470 states that "[a] motion for reconsideration is intended to be an exceptional remedy." Exchange Act Rel. No. 35833 (Jan. 9, 1995), 59 SEC Docket 1546, 1588.

[4] *John Gardner Black*, Investors Advisers Rel. No. 3040 (June 18, 2010), __ SEC Docket ____, ____; *Mitchell M. Maynard*, Investment Advisers Rel. No. 2901 (July 16, 2009), 96 SEC Docket 18728, 18729; *Perpetual Sec., Inc.*, Exchange Act Rel. No. 56962 (Dec. 13, 2007), 92 SEC Docket 472, 473. *See also KPMG Peat Marwick LLP*, Order Denying Request for Reconsideration, 55 S.E.C. 1, 3 n.7 (2001) (specifying that efficiency and fairness concerns embodied in federal court practice of rejecting motions for reconsideration unless correction of manifest errors of law or fact or presentation of newly discovered evidence is sought "likewise inform our review of motions for reconsideration under Rule 470").

[5] *Perpetual Sec., Inc.*, 92 SEC Docket at 473 (quoting *Feeley & Wilcox Asset Mgmt. Corp.*, 56 S.E.C. 1264, 1269 n.18 (2003)).

> [Asensio], including the anticipated denial of a MC-400 presently filed with FINRA by [Asensio] in conjunction with a New Member Application . . . is unlawful as an unconstitutional exercise of power reserved to the executive branch of government by a private party not subject to the direct control of the executive branch, specifically since the creation of FINRA in 2007 and specifically in the circumstances of [Asensio]'s case, where [he] violated no law, where [his] work benefitted investors, and where [he] was denied the right to his livelihood by a private entity that does not even purport to adhere to the most basic due process standards.

Asensio also contends that NASD's and FINRA's actions violate the Appointments Clause because FINRA:

> exercises federal executive power in administering certain laws and regulations governing interstate commerce, specifically in deciding who may or may not be allowed to partake in interstate commerce, yet FINRA's executives are not appointed by the U.S. President, nor are they appointed by any other governmental body [and] [a]s such, FINRA unlawfully usurps power reserved to the executive branch insofar as FINRA exercises such power without FINRA executives being appointed by the President or by any other government body or official [internal quotations omitted].

Asensio further states that:

> [t]he President has no authority to remove, supervise, or control FINRA executives, even as FINRA exercises power of the executive branch, including decisions to strip individuals or property or livelihood and to exercise discretion over who may be allowed to partake in an entire industry comprising a substantial portion of interstate commerce.

Contrary to Asensio's assertions, FINRA is not exercising federal executive power. FINRA is registered under, and operates subject to, Section 15A of the Exchange Act.[6] Section 15A, as the U.S. Supreme Court has noted, "supplements the Securities and Exchange Commission's regulation of the over-the-counter markets by providing a system of cooperative self-regulation through voluntary associations of brokers and dealers."[7] The Court stated that section 15A "authorizes [these voluntary associations] to promulgate rules designed to prevent fraudulent and manipulative practices; to promote equitable principles of trade; to safeguard against unreasonable profits and charges; and generally to protect investors and the public

---

[6] 15 U.S.C. § 78o-3.

[7] *United States v. NASD*, 422 U.S. 694, 700 n.6 (1975) (statutory citations omitted).

interest."[8] However, although Section 15A authorizes the SEC to exercise a "significant oversight function" over the rules and activities of the registered associations,[9] self-regulatory organizations, such as FINRA, are not "Government-created, Government-appointed entit[ies],"[10] and therefore do not "unlawfully usurp power reserved to the executive branch," as Asensio contends.

2. Claim that Commission Failed to Provide Notice of NASD-NYSE Consolidation

Asensio asserts that, although the NASD-NYSE consolidation that created FINRA caused "changes in the regulatory regime that directly and adversely affect [him]," we "did not provide [him with] notice of such changes." Asensio contends that we "did not notify [him] that the NYSE and the AMEX, owned by the NYSE, would have membership applications processed by FINRA and the impact this would have on [Asensio] seeking remedy for his bar sanction." Asensio also maintains that we "did not notify [him] that NASDAQ and exchanges owned by NASDAQ would surreptitiously have membership applications processed by FINRA, by directing applicants to send applications to NASDAQ at FINRA's address."

However, the proposed consolidation of NASD and NYSE was widely publicized when it was announced in November 2006.[11] The terms and provisions of the proposed consolidation were published and publicly available.[12] Our approval of the consolidation was publicly

---

8 *Id.*

9 *Id.*

10 *Free Enterprise Fund v. Public Company Accounting Oversight Board,* __ US ____, ____, 130 S.Ct. 3138, 3147 (2010) (contrasting "expansive powers" granted to the Public Company Accounting Oversight Board with the more limited powers granted to self-regulatory organizations). Asensio's citation to the *Free Enterprise Fund* litigation in support of his arguments ignores these distinctions between self-regulatory organizations and the Public Company Accounting Oversight Board; *Free Enterprise Fund* is not relevant here.

11 *See, e.g.*, NASD and NYSE Group Announce Plan to Consolidate Regulation of Securities Firms (Nov. 28, 2006), at http://www.finra.org/Newsroom/NewsReleases/2006/P017973; NASD and NYSE Group Announce Plan to Consolidate Regulation of Securities Firms (Nov. 28, 2006), at http://www.nyse.com/press/1164625606086.html; Statement by SEC Chairman Cox at News Conference on Self Regulation Consolidation (Nov. 28, 2006), at http://www.sec.gov/news/press/2006/2006-195.htm.

12 *Id.*

disclosed,[13] as were the final terms and provisions of the approved consolidation.[14] Pursuant to the Federal Register Act, notice provided in the Federal Register is "deemed to have been given to all persons . . . when the notice is published in the Federal Register. . . ."[15]

3. Alleged Futility of Pursuing Bias Claims

Asensio claims that we "implied" that he "should have raised claims of FINRA's bias at the [FINRA National Adjudicatory Council ("NAC")], after such claims were dismissed by the lower FINRA body, the Hearing Panel." According to Asensio, we suggested that "FINRA would be arbiter of its own bias." He maintains that we have "apparently not considered the extent to which even raising a claim of bias before FINRA may predispose FINRA against the individual making such claim." Asensio concludes that we "failed to consider the futility of raising a bias claim before FINRA," and that, in such instances, "an exhaustion of administrative remedies is not required where the effort to seek administrative remedy would prove futile due to a biased administrative body."

We discussed at length in our June 17 Order that Asensio failed to establish the existence of extraordinary circumstances, as required by our Rule of Practice 420(b),[16] that would excuse the late filing of his appeals. Regarding Asensio's contention that it would have been futile to press his bias claims with the NAC, we note, again, that:

> before the NAC on appeal of the Hearing Panel's bar decision, Asensio's counsel declined to challenge the Hearing Panel procedures and agreed that Asensio "had a full opportunity for a hearing." We also note that in both proceedings here, Asensio had notice, was permitted to present evidence, was able to examine witnesses, was given notice of the findings, and was informed of his appeal rights.

---

13 *See, e.g.*, SEC Gives Regulatory Approval for NASD and NYSE Consolidation (July 26, 2007), at http://www.sec.gov/news/press/2007/2007-151.htm.

14 *See Order Approving Proposed Rule Change to Amend the By-Laws of NASD to Implement Governance and Related Changes to Accommodate the Consolidation of the Member Firm Regulatory Functions of NASD and NYSE Regulation, Inc.*, Exchange Act Rel. No. 56145 (July 26, 2007), 91 SEC Docket 496, 72 Fed. Reg. 42,169 (Aug. 1, 2007); *Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change Relating to the Restated Certificate of Incorporation of National Association of Securities Dealers, Inc.*, Exchange Act Rel. No. 56146 (July 26, 2007), 91 SEC Docket 517, 72 Fed. Reg. 42,190 (Aug. 1, 2007).

15 44 U.S.C. § 1508. *Cf. Joseph Abbondante*, Exchange Act Rel. No. 53066 (Jan. 6, 2006), 87 SEC Docket 203, 218 (holding that general securities representative "had an obligation to know the NASD's rules").

16 17 C.F.R. § 420(b).

> Moreover, during the appeal to the NAC in the 2006 disciplinary proceeding, his counsel declined to challenge the Hearing Panel's procedures and agreed that Asensio "had a full opportunity for a hearing."[17]

Moreover, Asensio has failed to show that raising the issue of bias in a timely appeal to us of the 2006 Bar Decision or the 2008 Eligibility Denial Decision would have been futile.

4. Alleged Incorrect Factual Findings

Asensio claims that the June 17 Order contained "mischaracterized or distorted factual findings," including purported misstatements about NASD's information requests that led to its disciplinary proceeding against him; distortions about Asensio's role in a congressional investigation of the American Stock Exchange; "[s]ystemic neglect" of Asensio's "large and unique record of exposing stock fraud;" "questionable assertion[s]" regarding Asensio's opportunities to conduct effective discovery during the NASD proceedings; inaccurate statements about Asensio's identification of other investigations NASD initiated against him; and misstatements about the number of pleadings in which he raised his contentions regarding the asserted Appointments Clause violations.

We do not agree that the facts were mischaracterized. However, the description of underlying facts found in the 2006 Bar Decision and the 2008 Eligibility Denial Decision were provided as background. Because the June 17 Order declined to accept jurisdiction to review Asensio's application for review, that order did not adjudicate those facts.

Accordingly, IT IS ORDERED that the motion for reconsideration filed by Manuel P. Asensio , be, and it hereby is, DENIED. [18]

By the Commission (Commissioners CASEY, AGUILAR, and PAREDES); Chairman SCHAPIRO and Commissioner WALTER not participating.

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

Elizabeth M. Murphy
Secretary

---

[17] *Asensio*, __ SEC Docket at ____ (quotations in original).

[18] We have considered all of the contentions advanced by Asensio. We have rejected or sustained these contentions to the extent that they are inconsistent or in accord with the views expressed in this order.

Commissioner Casey
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9132 / August 5, 2010

SECURITIES EXCHANGE ACT OF 1934
Release No. 62653 / August 5, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3165 / August 5, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13994

In the Matter of

NAVISTAR INTERNATIONAL CORPORATION,
DANIEL C. USTIAN,
ROBERT C. LANNERT,
THOMAS M. AKERS, JR.,
JAMES W. MCINTOSH,
JAMES J. STANAWAY,
ERNEST A. STINSA,
MICHAEL J. SCHULTZ,

Respondents.

ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted against Navistar International Corporation ("Navistar" or the "Company"), Daniel C. Ustian, Robert C. Lannert, Thomas M. Akers, Jr., James W. McIntosh, James J. Stanaway, Ernest A. Stinsa, and Michael J. Schultz (collectively "Respondents") pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Section 21C of the Securities Exchange Act of 1934 ("Exchange Act").

II.

In anticipation of the institution of these proceedings, Respondents have each submitted Offers of Settlement (the "Offers"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings or conclusions contained herein, except as to the Commission's jurisdiction over Respondents and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondents' Offers, the Commission finds[1] that:

A. SUMMARY

1. This is a financial fraud, reporting, and internal controls case against Navistar, a Fortune 200 manufacturer of commercial trucks and engines, and certain current and former employees. At times from 2001 through 2005, Navistar overstated its pre-tax income by a total of approximately $137 million as the result of various instances of misconduct. Fraud at a Wisconsin foundry and in connection with certain vendor rebates and vendor tooling transactions accounted for approximately $58 million of that total. The remaining approximately $79 million resulted from improper accounting for certain warranty reserves and deferred expenses. These findings do not reflect a coordinated scheme by senior management to manipulate the Company's reported results or conduct committed with the intent of personal gain. Instead, these findings reflect misconduct that resulted in large part from a deficient system of internal controls, evidenced in part by insufficient numbers of employees with accounting training, a lack of written accounting policies and procedures, and flaws in the Company's organizational structure. The internal control deficiencies, in turn, resulted from senior management's failure to dedicate sufficient resources and attention to the adequacy of Navistar's accounting and reporting functions. The deficient internal controls failed to provide adequate checks on certain employees' efforts to meet the Company's financial targets.

B. RESPONDENTS

2. Navistar, a Delaware corporation headquartered in Warrenville, Illinois, is a holding company whose principal subsidiary, Navistar, Inc. (f/k/a International Truck and Engine Corporation), manufactures and markets commercial trucks, school buses, diesel engines, and related parts worldwide. During the relevant period, Navistar's securities were registered with the

---

[1] The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

Commission pursuant to Section 12(b) of the Exchange Act and traded on the New York Stock Exchange. As of November 30, 2009, Navistar had 70,718,762 shares outstanding.

3. Daniel C. Ustian ("Ustian"), 60, of Naperville, Illinois, is Chairman, Chief Executive Officer ("CEO") and President of Navistar. Ustian held various titles at the Company during the relevant period. From 1999 through April 2002, Ustian was President of the Engine Division. In April 2002, Ustian was promoted to President and Chief Operating Officer of Navistar. In February 2003, Ustian also became Navistar's CEO. In February 2004, Ustian was elected Board Chairman.

4. Robert C. Lannert ("Lannert"), 70, of Burr Ridge, Illinois, was the Company's Vice Chairman and Chief Financial Officer ("CFO") throughout the relevant period. Lannert had direct responsibility for Navistar's accounting department and the Corporate Controller's Office, and was ultimately responsible for the Company's internal controls. Lannert was terminated by Navistar in October 2007.

5. Thomas M. Akers, Jr. ("Akers"), 58, of Aurora, Illinois, was Director of Purchasing for the Engine Division from April 1996 through August 2004. He was thereafter promoted to Vice President, Purchasing and Logistics and remained in that position until his retirement in January 2009.

6. James W. McIntosh ("McIntosh"), 60, of Naperville, Illinois, was Vice President of Finance for the Engine Division throughout the relevant period. In that position, McIntosh was the CFO of the Engine Division and was directly responsible for its accounting, financial reporting, and internal controls. McIntosh was transferred to the Parts Group in January 2006 and subsequently retired in May 2007.

7. James J. Stanaway ("Stanaway"), 64, of Springfield, Ohio, was Director of Finance for the Engine Division during the relevant period through June 2004, when he retired from the Company. In that role, Stanaway reported directly to McIntosh.

8. Ernest A. Stinsa ("Stinsa"), 41, of Elmhurst, Illinois, replaced Stanaway as Director of Finance for the Engine Division in 2004. Stinsa left Navistar in January 2006, but rejoined the Company in May 2010 in its Global Product Development division. In his new capacity, Stinsa has no direct accounting or financial reporting responsibilities.

9. Michael J. Schultz ("Schultz"), 45, of Waukegan, Illinois, was the Plant Controller at Navistar's foundry in Waukesha, Wisconsin, during the relevant period. Schultz was terminated in April 2005.

C. FACTUAL FINDINGS AND CONCLUSIONS

1. Background

a) Navistar's Restatement

10. In December 2007, the Company filed a delayed Form 10-K for fiscal 2005 that included a restatement of its financial statements for fiscal years 2002-2004 and the first three quarters of fiscal year 2005 ("Restatement Period").[2] For the year ended October 31, 2004, Navistar restated its previously-reported pre-tax profit of $311 million to a pre-tax loss of $35 million. For the year ended October 31, 2003, the previously-reported pre-tax loss of $49 million was restated to a pre-tax loss of $316 million. The previously-reported accumulated deficit as of November 1, 2002 of $731 million was restated to an accumulated deficit of $2.4 billion. In all, Navistar restated or reclassified sixteen different items. The restatement was comprised of widely varying accounting errors, related to different individuals working at different Company locations, and occurred during years of profit and years of loss.

11. The restatement was required because Navistar's previously reported financial statements as filed in its annual reports in Forms 10-K and its quarterly reports in Forms 10-Q for the Restatement Period materially failed to comply with Generally Accepted Accounting Principles ("GAAP") and the financial reporting requirements under the securities laws.

b) Ustian's and Lannert's Bonuses During the Restatement Period

12. During the 12-month period following Navistar's filing of its Form 10-K for fiscal year 2004 (later restated), and based on the Company's originally-reported financial results for that fiscal year, Ustian and Lannert received performance-based bonuses totaling $2 million and $1,049,503 (an original grant of $828,555, later corrected by an additional payment of $220,948) respectively. Ustian and Lannert have not reimbursed Navistar for any portion of the bonuses they received.

2. Internal Control Deficiencies

13. Navistar had numerous deficiencies throughout its system of internal controls during the relevant period, including fifteen material weaknesses,[3] that were attributable, in part, to

[2] In April 2006, the Company announced that its previously issued financial statements for fiscal years ended October 31, 2002 through October 31, 2004 and its previously issued quarterly financial statements for periods after October 31, 2004 should be restated. In its December 2007 filing, the Company restated its income (loss) before income tax for fiscal years 2003 and 2004 and for the first three quarters of fiscal year 2005 to reflect various adjustments, including certain matters discussed herein. With respect to fiscal year 2002, the Company adjusted its accumulated deficit as of November 1, 2002, to reflect corrected items that related to prior periods. The Company did not separately restate its income (loss) for fiscal year 2002.

[3] In its Form 10-K for fiscal year 2005 (filed in December 2007), Navistar disclosed fifteen separate material weaknesses in its internal controls for 2005-06.

the Company's failure to dedicate sufficient resources to those controls. For example, requests by managers to hire additional employees with accounting backgrounds and to assign additional employees to the Company's accounting policies and procedures function were denied because of budgetary concerns; during 2000-2001 there was only one full-time employee dedicated to the policies and procedures function. The Company's failure to address the internal control deficiencies contributed to at least some of the misconduct described below.

14. Ustian, Lannert, and McIntosh each was responsible for certain aspects of the Company's internal controls. Each failed to take certain steps that would have ensured the Company established and maintained adequate internal controls in certain respects, and their failure to act was a cause of certain of the Company's internal control deficiencies. Each knew or should have known that the failure to act would contribute to weaknesses in those controls.

15. For example, in 2002, the Company's Internal Audit department warned senior management that Navistar's accounting policies and procedures needed to be updated. Although Lannert oversaw a plan to address Internal Audit's concerns, the policies and procedures were not updated at that time because of other perceived priorities. Additionally, McIntosh failed to increase the number of Engine Division employees competently trained in GAAP despite being told that additional employees with such capabilities were needed. Deficient accounting policies and procedures and an inadequate number of employees trained in accounting were among the material weaknesses disclosed by the Company in its Form 10-K for fiscal year 2005.

16. In another instance, Lannert and the Corporate Controller's Office proposed a change to Navistar's corporate organizational structure so that finance personnel in the Engine and the Truck divisions, who were then reporting to the division operations managers, would instead report directly to the CFO or the Corporate Controller's Office. Lannert and the Corporate Controller's Office thought that this change would allow divisional finance personnel to voice more freely any concerns or questions regarding accounting issues without fear of reprisal and provide support for divisional finance personnel in addressing the demands of the operational managers. Ustian decided to maintain the established reporting structure, believing it allowed finance personnel to understand more fully the nature of the underlying business. The Company took no other steps to address the underlying concerns that prompted the proposal to change the organizational structure. This structure contributed to the misconduct in recording vendor rebates (described below), in which an Engine Division purchasing finance employee booked certain questionable transactions because of feared reprisal from an Engine Division operations manager. As part of the remedial steps taken in connection with its restatement, Navistar changed this structure so that divisional finance personnel now report directly to the CFO.

3. Improper Accounting Practices at Navistar

a) Vendor Rebates and Vendor Tooling

i) Vendor Rebates

17. During the 2001 to 2004 time period, Navistar ramped up its engine production beyond initial expectations and correspondingly increased its purchases of engine parts from suppliers. Navistar sought to share in those suppliers' unanticipated profits by asking them to pay a portion back to the Company in the form of rebates. Under GAAP, a company could recognize rebates only when they were actually earned, *i.e.,* when the entity had substantially accomplished what was necessary to be entitled to such rebates. Accordingly, Navistar could record the full rebate as income in the then-current period *only* if no contingencies existed on its right to receive the rebate. Conversely, the Company was prohibited from booking rebates as income in the then-current period if they were based on future business.

18. During this period, Navistar booked 35 rebates and related receivables from its suppliers. Of those rebates and receivables, as many as 30 were improperly booked. While these rebates and receivables took different forms -- including volume-based rebates and so-called "signing bonuses" for Navistar's award of new business -- all were improperly booked as income in their entirety upfront, even though, in whole or in part, they were earned in future periods. The Company's eventual restatement of these rebates and receivables totaled $9.7 million of pre-tax income in 2004 and $8.5 million in 2003, which represented 27.7 percent and 2.7 percent, respectively, of the restated loss before income taxes for those years.

19. The vast majority of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of the fiscal year. As contingent consideration for paying these rebates, however, many suppliers required the Company either to agree to new business or to repay the amount of the rebate in the form of waived price concessions on already-agreed upon future business. The Engine Division booked these rebates, often using the same form letter (which in certain instances was back-dated) that falsely stated that the rebate was based on past purchases and had no contingencies. In some instances, certain Engine Division employees also generated side-letter arrangements with vendors that detailed that the rebates were contingent on future purchases and/or the vendor could recoup the rebate through inflated future prices by which the Company would forego agreed-upon price reductions. Additionally, these side-letters stated that Navistar would refund the rebate accordingly if the Company failed to make sufficient future purchases. These side-letters made clear that these rebates had not actually been earned at the time the amounts were recognized.

20. In one instance, "Vendor Rebate 1," a supplier executed a form rebate letter drafted by Navistar, and dated October 19, 2004, that said the supplier was providing the Company a $2.1 million rebate based on "2004 volume and piece price productivity improvements." However, the very next day, October 20, 2004, the parties executed a side-letter arrangement that specifically stated that half of the rebate was based on pulling forward productivity improvements expected to be achieved in 2005. Navistar also agreed to refund any shortfall to the supplier should these

improvements not be achieved. Thus, the side-letter made clear that the supplier's rebate was contingent on future business with the Company. Nevertheless, Navistar approved the rebate and booked the entire dollar amount in fiscal year 2004.

21. Another form of these improperly-booked rebates were so-called "signing bonuses" that Navistar demanded and received from certain suppliers in exchange for awarding new business. Despite the fact that the suppliers' payments were contingent on receiving that new business from Navistar, the Company booked the rebates in their entirety during the then-current period in which they were received, instead of when earned over the period of the future business.

22. In one such instance, "Vendor Rebate 2," McIntosh contacted Stanaway four days after the 2003 fiscal year-end to discuss the need to fill an earnings shortfall. Stanaway, in turn, discussed the shortfall with Akers, who in exchange for promising to provide future business to a particular supplier in 2004, convinced the supplier to agree to pay a $6.2 million signing bonus to the Company and to provide Navistar with a letter that would allow the Company to book the full amount in 2003. The vendor had never before done business with Navistar. Akers had engaged in previous discussions with the vendor about possible future business and the payment of a signing bonus, but the terms of the signing bonus were not finalized until after the 2003 fiscal year-end. Stanaway, who had no direct role in acquiring the rebate, then approved an entry recording the $6.2 million as income in 2003.

23. McIntosh, Akers, and Stanaway understood that to be booked in the current period, such rebates could not be contingent or otherwise based on future business. Despite this understanding, McIntosh and Akers directly negotiated or otherwise arranged for the Company to enter into and book certain rebates during the then-current period knowing, or recklessly failing to know, that such rebates were contingent on future business. As recorded, these rebates were not in compliance with GAAP. Additionally, McIntosh and Akers directly or indirectly approved the creation and use of letters that they knew or recklessly failed to know did not reflect material aspects of the transaction.

24. Akers initiated the concept at Navistar of seeking vendor rebates based on volume increases and often supervised the employees negotiating the vendor rebates and related receivables. In several instances, including Vendor Rebate 1 and Vendor Rebate 2, Akers directly or indirectly approved rebates that he knew, or recklessly failed to know, were tied to future business but would nonetheless be booked in the then-current period. Akers participated directly in the negotiations of multiple rebates and, in certain instances, personally received both a "clean letter" and "side-letter" for the same rebate, which was evidence that the rebate had contingencies.

25. As CFO of the Engine Division, McIntosh was responsible for the accounting for all Engine receivables during the relevant period, including all vendor rebates. McIntosh was involved in the planning of at least three rebates, including Vendor Rebate 2, knowing, or recklessly failing to know, that they were contingent on future business but would nonetheless be booked in their entirety in the then-current period.

26. As Director of Engine Finance, Stanaway approved the recording of receivables from fiscal 2001 through 2003, including all vendor rebates. Stanaway typically was not involved in the negotiation of vendor rebate agreements or the procuring of "clean" letters that supported the booking of such rebates, and usually became involved in these transactions only at the final approval stage. Despite his lack of involvement in obtaining these vendor rebates, Stanaway approved the booking of certain rebates as income, including the booking of Vendor Rebate 2, knowing, or recklessly failing to know, that they were contingent on future business and should not be booked as income in the current period. Stanaway had little accounting background or formal training in GAAP at the time of the transactions.

27. Stinsa succeeded Stanaway for a relatively brief period, from July 2004 until January 2006. As Stanaway's successor, Stinsa was not involved in the negotiation of vendor rebate agreements or the procuring of "clean" letters that supported the booking of such rebates. Instead, Stinsa became involved in the vendor rebate process only when asked on a sporadic basis to approve booking certain rebates. While authorized to approve booking these receivables, Stinsa's primary responsibilities did not include these transactions, and he had little accounting background or formal training in GAAP at the time of the transactions. For example, Stinsa did not specifically know whether booking so-called "signing bonuses" into income in the then-current period was consistent with GAAP; instead, he assumed it was, because he knew the Company had a practice of soliciting and booking such receivables. In fiscal 2004, Stinsa erroneously approved the booking of a $4 million signing bonus based on a letter that, while expressly stating that the bonus was unconditional, also stated that the payment concerned the award of "new" business. Stinsa should have inquired whether the receivable was, in fact, contingent on the vendor's expected new business with Navistar. Stinsa erroneously approved the booking of two other vendor rebates in fiscal 2004, including another signing bonus and a volume-based rebate. In approving these rebates without sufficient inquiry, Stinsa directly or indirectly caused Navistar to enter a false financial book, record or account.

ii) Vendor Tooling

28. Prior to 2003, Navistar periodically entered into amortization agreements concerning the cost of tooling with vendors. Under these arrangements, the vendors purchased the tooling they used to make parts sold to Navistar, and the Company repaid the suppliers for those tooling costs through amortization payments incorporated in the piece-price rates of the parts ultimately sold to Navistar. In 2003, the Company determined that in some instances, instead of continuing these amortization payments, the Company would benefit (in part through beneficial accounting treatment) by purchasing the tooling outright from the suppliers and depreciating the tooling costs going forward over a longer period. Consequently, in 2003, the Company initiated a program pursuant to which Navistar arranged to terminate certain of these amortization agreements and acquired the tooling via lump sum payments to the suppliers. However, instead of paying suppliers the remaining unamortized tooling cost as of the 2003 purchase date, the Company paid the suppliers a dollar amount equivalent to the unamortized tooling cost as of the beginning of the 2003 fiscal year. Since Navistar had already been paying amortization to the suppliers since the start of that fiscal year (*i.e.,* November 1, 2002), the Company arranged to receive back from those suppliers a "rebate" equivalent to those year-to-date amortization payments. The Company then

improperly booked these rebates into income. In addition, the Company improperly deferred depreciation costs related to the tooling buybacks.[4]

29. In 2003, two Navistar employees approached the Company's outside auditor regarding the accounting for certain contemplated tooling buyback transactions. After learning of the planned accounting for the program, e-mails indicate that the auditor informed the employees that the recapture and booking of previously-paid amortization into income was improper. While certain transactions were booked in fiscal year 2003 because they were believed to be of immaterial dollar amounts, e-mails indicate that the auditor informed the Company that no such transactions would be permitted in fiscal year 2004. Despite being informed of these developments, McIntosh used a "60-day rule" and authorized Engine Division employees in 2004 to record 60 days of amortization recaptured as income based on the Company's payment terms. In so doing, McIntosh disregarded employees' warnings that continuing to record the recapture of amortization as income would be inconsistent with the auditor's guidance on the accounting.

30. In disregarding that guidance, McIntosh knew or recklessly failed to know that Navistar booked income in violation of GAAP. In 2004, the Company restated a total of $1.6 million in income related to the vendor tooling buyback program, or 4.6 percent of the restated loss before income taxes for that year.[5]

b) <u>Waukesha</u>

31. From 2001 to 2005, Schultz, the Waukesha plant controller, engaged in various fraudulent accounting practices that collectively caused income during that period to be overstated by a total of approximately $38 million. Specifically, Schultz's conduct included the following:

<u>Accounts Payable.</u> From early 2003 through 2005, Schultz directed the plant manager of accounting to delay processing certain vendor invoices that had been received and to refrain from accruing those unprocessed invoices in accounts payable as current period expenses in order to help reach certain plant financial goals.

---

4 The following hypothetical example illustrates how the program worked. As of November 1, 2002, Navistar has a balance due on tooling to a supplier of $3 million. From November 1, 2002 through May 31, 2003, Navistar pays $1 million in amortization for the tooling. On May 31, 2003, Navistar decides to purchase the tooling outright, stop paying and recording amortization expenses, and begin recording depreciation. At the May 31 sale date, based on its amortization payments to date, Navistar's outstanding obligation to the supplier is $2 million. But instead of paying the supplier $2 million for the tooling, Navistar pays the supplier the tooling's balance due as of November 1, 2002, *i.e.,* $3 million. Since Navistar had already paid $1 million in amortization for the tooling from November 1, 2002, Navistar requires the supplier to simultaneously pay the Company a rebate of $1 million, *i.e.,* the previously-paid amortization. The Company then incorrectly records the $1 million rebate as a reduction in the cost of goods sold, increasing income for the May 2003 quarter. Instead, the Company should have either only paid the remaining balance due on the tooling at the time of purchase without booking a rebate to income or it should have netted the two transactions and effectively recorded the tooling purchase for the balance due at the time of purchase.

5 In its restatement, Navistar combined the adjustments to net income that resulted from vendor rebates and vendor tooling into a single line item. For fiscal year 2004, the combined adjustment resulting from vendor rebates and vendor tooling was $11.3 million of pre-tax income, or 32.3 percent of the restated pre-tax loss for that year.

Inventory. From about 2001 through 2005, Schultz directed the plant manager of accounting to alter the Waukesha inventory numbers at the end of every month in order to improve the plant's financial operating results. Schultz failed to utilize Waukesha's designated accounting software in accounting for the inventory movements and usage and instead tracked the inventory manually, which made it easier for him to record erroneous totals. When periodic physical inventory counts taken at the plant found the recorded inventory balances to be overstated, Schultz failed to record appropriate adjustments to lower the inventory balances. As a result of this conduct, Waukesha's books falsely indicated the plant had $11 million in inventory that did not exist, and consequently understated materials expenses by that amount.

Deferred Costs Pursuant to Purported Contractor Arrangement. Schultz deferred certain costs relating to a purported arrangement with a contractor that provided services relating to parts manufactured at Waukesha. Pursuant to a purported side agreement entered into by a former Waukesha employee, Waukesha had agreed to pay higher upfront costs to the contractor as a means to help finance the start-up of the contractor's business. In return, the contractor purportedly agreed to reduce its prices to Navistar in future periods. The agreement was not in writing; additionally, there was no evidence that the contractor guaranteed to repay any specified higher upfront costs. Nevertheless, beginning in 2002, Schultz deferred the entire dollar amount of certain of the contractor's invoices (*i.e.,* not just a portion representing higher upfront amounts paid to the contractor), effectively understating expenses in order to "smooth out earnings." Schultz deferred approximately $2.4 million of those costs in the first quarter of fiscal 2003, and another $700,000 in the third quarter of fiscal 2003.

Deferred Costs Involving Manufacturing Line. Schultz also improperly deferred certain costs related to Waukesha's installation of a new manufacturing line. Before installation of the manufacturing line was complete, the general contractor stopped work and filed for bankruptcy. As a result, the Company was required to pay off subcontractors' liens and pay to have the installation completed by other subcontractors. From 2002 through 2005, Schultz deferred about $3 million that Navistar incurred in start-up expenses under the supposed theory that the Company would recover those costs from the bankrupt general contractor.

32. Schultz engaged in the aforementioned conduct in an attempt to improve Waukesha's financial results. The aggregate monetary impact of Schultz's accounting misconduct was material to Navistar's financial statements. Schultz knew or recklessly failed to know that the actions described above were not in compliance with GAAP.

c) **Warranty Reserve**

33. Beginning in fiscal year 1999, the Engine Division assumed responsibility for accounting for its warranty reserve, which reflected the Company's estimated future warranty costs on engines installed in the majority of Navistar manufactured trucks. The warranty accrual estimate process began with the Engine Division's Reliability & Quality ("R&Q") group, which generated an estimated warranty cost per unit, or CPU, for each engine sold. This calculation incorporated certain "above-the-line" items, including well-established or known steps (*e.g.,*

implemented engineering fixes) that were viewed, based on historical trends or data, to have effectively reduced warranty costs. The CPU was the primary basis for the warranty reserve amount; the higher the CPU, the higher the reserve.

34. The warranty reserve-setting process should have been governed by accounting rules related to contingent liabilities. Pursuant to Statement of Financial Accounting Standards ("SFAS") No. 5, *Accounting for Contingencies - Appendix A; With Respect to Obligations Related to Product Warranties and Product Defects,* warranty reserves must be established when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated.

35. When R&Q's CPU calculation was presented to Stanaway, and then ultimately to McIntosh, both typically stated that the initial estimated reserve number was too high for the Engine Division's business plan. Without sufficient consideration for the relevant accounting rules, Stanaway and McIntosh typically then directed R&Q to add certain "below-the-line" items to the warranty reserve calculation process because they thought these items would reflect potential reductions that the Company hoped to achieve in future warranty costs. These "below-the-line" items included anticipated vendor reimbursements and engineering fixes[6] that lacked historical trend or other data evidencing their likely effectiveness. For example, Stanaway and McIntosh directed R&Q to include anticipated vendor reimbursements in the warranty reserve calculation despite the lack of any specific language in the vendor contracts providing for such recoveries. Instead, the Company relied on the existence of standard provisions in supply agreements or the Illinois Commercial Code to support the contemplated vendor reimbursements. During the relevant period, approximately 50 percent of the vendor recoveries deducted below the line from warranty reserve calculations were based on something other than specific contractual language. Moreover, the Company often did not receive reimbursements from vendors for engine warranty claims. Stanaway and McIntosh also directed the inclusion in the warranty accrual calculation of anticipated engineering fixes that lacked historical and empirical data evidencing their likely effectiveness. Certain anticipated fixes were incorporated into the CPU calculation before they had even been implemented. At McIntosh and Stanaway's insistence, R&Q included these "below-the-line" items in its warranty reserve calculation, and these components consistently reduced the warranty reserve.

36. The inclusion of these anticipated vendor reimbursements and engineering fixes was not in compliance with GAAP. Stanaway and McIntosh knew or should have known that the warranty reserve-setting process was governed by accounting rules relevant to contingent liabilities, yet failed to consider or apply such rules in establishing Navistar's warranty reserve. Stanaway and McIntosh also knew or should have known that including anticipated vendor reimbursements and engineering fixes without data evidencing their effectiveness was not in compliance with GAAP.

---

[6] Vendor reimbursements concerned payments that Navistar sought to receive from manufacturers of the failed engine parts that were the source of warranty claims against the Company. Engineering fixes included engine design changes (*e.g.*, modifications to engines not yet built) and service kits (*e.g.*, modifications implemented after sale to address engine problems that arose in the field).

37. The below-the-line items inappropriately included in the reserve calculation caused the warranty expense to be understated by $17 million in fiscal year 2002 and by $18.5 million in fiscal year 2003. The $18.5 million total represented 5.9 percent of the restated loss before income tax for that year.

4. Reporting Failures Regarding Certain Deferred Start-up Costs

38. In 2000, the Company entered into a long-term supply contract (the "Agreement") with an automobile manufacturer (the "Automaker") to develop and manufacture V-6 diesel engines commencing with model year 2002 and extending through 2012. From the fourth quarter of 2001 through the fourth quarter of 2002, the Company incurred substantial start-up costs relating to the Agreement, including expenses developing the engine, constructing a plant in Huntsville, Alabama, and leasing engine assembly assets. The Company began deferring some of these start-up costs in the fourth quarter of fiscal 2001 and as of the fourth quarter of 2002 had accumulated $57 million of deferred pre-production costs. Production of these engines was continually delayed by the Automaker until October 2002, when it cancelled the Agreement and discontinued its V-6 engine program with Navistar.

39. Relevant accounting rules provided that such start-up costs could be deferred only if there existed an objectively verified and measured contractual guarantee of reimbursement. *See* FASB Emerging Issues Task Force Issue No. 99-5, *Accounting for Pre-Production Costs Related to Long-Term Supply Arrangements* ("EITF 99-5").

40. The terms of the Agreement standing alone did not provide for reimbursement in a manner sufficient to satisfy the requirements for start-up cost deferral pursuant to EITF 99-5. The start-up costs could be appropriately deferred only if the Company had received from the Automaker a written guarantee of specific reimbursement. Without such a written guarantee, the Company was not entitled to defer these costs.

41. The Company never received from the Automaker a sufficiently specific written guarantee of reimbursement. Beginning in September 2001 and continuing until October 2002, when the Automaker cancelled the Agreement, Company management repeatedly sought such a guarantee in the form of a letter. These efforts were continually rebuffed by the Automaker.

42. Nevertheless, the Company, through its senior accounting staff, deferred these start-up costs from the fourth quarter of 2001 through the fourth quarter of 2002. Specifically, the Company deferred $4.3 million in the fourth quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in each of the second and third quarters of fiscal year 2002.[7]

---

[7] The Company did not file an adjusted consolidated statement of operations for fiscal year 2002 or for the 2002 quarterly periods. *See supra* n. 2. Nevertheless, the dollar amounts that were deferred instead of being expensed are considered material for each of the first three quarters of fiscal year 2002. The $12.8 million and the $13.3 million totals represent 12.5 percent, 65.5 percent, and 25.4 percent, respectively, of the Company's previously reported loss before income tax if adjusted to reverse these deferrals for each of the first three quarters of fiscal year 2002.

43. These deferred start-up costs were not in compliance with GAAP. While senior management did receive oral assurances from Navistar senior managers that the Automaker had in fact committed to reimburse the Company for these start-up costs and Navistar's outside auditor was aware of and accepted the continuing deferral, the Company should not have allowed the deferral because it had not received the aforementioned written guarantee of reimbursement. Navistar, like all issuers registered with the Commission, is ultimately responsible for the accuracy of its books, records and accounts.

5. Reporting Failures Regarding the Company's Parts Segment

44. GAAP and Commission rules require an issuer to report specified operating result items for each business unit that is determined to be a reportable segment. *See* SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*; Regulation S-K, Item 303(A); Financial Reporting Release 54; Section 501.06 of the Financial Reporting Codification. Whether a particular business unit is a reportable segment turns on the manner in which management makes operating decisions and assesses the performance of such units. The segment reporting requirements are intended to enable investors to see an entity "through the eyes of management."

45. Prior to the restatement, Navistar disclosed that it had three reportable segments: Truck, Engine, and Financial Services. These business units met the qualifications for segments because: (1) they earned revenues and incurred expenses; (2) they had their operating results regularly reviewed by the CEO; and (3) discrete financial information was available for each.

46. However, another Navistar business unit, the Parts group, also met the segment reporting criteria. The CEO and the Board received separate monthly financial results, including sales and income, for Engine, Truck and Parts. Additionally, in the fourth quarter of fiscal year 2003, the Company announced a reorganization making the head of the Parts group a President – a co-equal with Engine and Truck – reporting directly to the CEO. The restructuring better enabled the CEO to evaluate, analyze, and make direct resource decisions for the Parts group based on the financial information available. As a result, the CEO and the Board were internally provided a transparent view of how Engine, Truck and Parts were performing independently of one another.

47. Nevertheless, from the first quarter of fiscal year 2004 through the third quarter of 2005, Navistar failed to report Parts as a segment in its publicly-filed financial statements and notes, and instead allocated the Parts group's results between the Truck and Engine divisions' results. As a result, investors were unable to view the Parts group in the same manner as were senior management and the Board. The Company's Forms 10-K for at least fiscal year 2004 and Forms 10-Q for 2004 and the first three quarters of 2005 failed to provide complete segment information required by GAAP and Commission rules.

D. APPLICABLE LAW

1. Section 17(a)(1) of the Securities Act prohibits fraudulent conduct in the offer or sale of securities. Section 10(b) of the Exchange Act and Rule 10b-5 thereunder prohibit fraudulent conduct in connection with the purchase or sale of securities. Establishing violations of these provisions requires a showing of scienter. *Aaron v. SEC*, 446 U.S. 680, 695, 702 (1980). Scienter is "a mental state embracing intent to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976). Recklessness can satisfy the scienter requirement. *See David Disner*, 52 S.E.C. 1217, 1222 & n.20 (1997); *SEC v. Steadman*, 967 F.2d 636, 641-42 (D.C. Cir. 1992). Reckless conduct is conduct that is "highly unreasonable and . . . represents 'an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it.'" *Rolf v. Blyth, Eastman Dillion & Co.*, 570 F.2d 38, 47 (2d Cir. 1978) (*quoting Sanders v. John Nuveen & Co.*, 554 F.2d 790, 793 (7th Cir. 1977)).

2. Section 17(a)(2) of the Securities Act prohibits obtaining money or property by means of untrue statements of material fact or misleading omissions of material fact in the offer or sale of securities. Section 17(a)(3) of the Securities Act prohibits engaging in transactions, practices or courses of business which operate or would operate as a fraud or deceit upon the purchaser in the offer or sale of securities. Establishing violations of Sections 17(a)(2) and 17(a)(3) does not require a showing of scienter; instead, a showing of negligence is sufficient. *Aaron v. SEC*, 446 U.S. at 697 & 701-02; *Weiss v. SEC*, 468 F.3d 849, 855 (D.C. Cir. 2006). Negligence is the failure to exercise reasonable care or competence. *Byron G. Borgardt*, 80 SEC Docket 3559, 3577 & n.35 (Aug. 25, 2003).

3. Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder require all issuers with securities registered under Section 12 of the Exchange Act to file annual and quarterly reports on Form 10-K and Form 10-Q, respectively. Exchange Act Rule 12b-20 further requires that, in addition to the information expressly required to be included in such reports, the issuer must include such additional material information as may be necessary to make the required statements, in light of the circumstances under which they were made, not misleading. The obligation to file these periodic reports includes the obligation that they be complete and accurate in all material respects. *See SEC v. IMC Int'l, Inc.*, 384 F. Supp. 889, 893 (N.D. Tex.), *aff'd mem.*, 505 F.2d 733 (5th Cir. 1974). No showing of scienter is necessary to establish a violation of Section 13(a) of the Exchange Act or Rules 13a-1, 13a-13 or 12b-20. *See SEC v. McNulty*, 137 F.3d 732, 740-741 (2d Cir. 1998).

4. Section 13(b)(2)(A) of the Exchange Act requires issuers to "make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer." Exchange Act Rule 13b2-1 prohibits persons from directly or indirectly falsifying or causing to be falsified any book, record, or account subject to Section 13(b)(2)(A) of the Exchange Act. Establishing violations of these provisions does not require a showing of scienter. *See SEC v. World-Wide Coin Inv., Ltd.*, 567 F. Supp 724, 749-50 (N.D. Ga. 1983); *SEC v. McNulty*, 137 F.3d 732 (2d Cir. 1998).

5. Section 13(b)(2)(B) of the Exchange Act requires all reporting companies to devise and maintain a system of internal controls sufficient to provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP.

6. Section 304(a) of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") provides that if an issuer is required to restate its financials due to material noncompliance with the securities laws as a result of misconduct, then the CEO and CFO shall reimburse the issuer for bonuses, incentive or equity-based compensation, and/or trading profits they received during the twelve-month period following the first public issuance or filing with the Commission of the financial document required to be restated. Section 304(a) creates an obligation on the part of CEOs and CFOs to reimburse issuers by stating that, if its elements are satisfied, the CEO and CFO "shall" reimburse the issuer. If the CEO and CFO do not voluntarily reimburse the issuer, the Commission can bring an enforcement action to compel reimbursement. *See* Sarbanes-Oxley Section 3(b). Section 304 does not require that a CEO or CFO engage in misconduct to trigger the reimbursement requirement. Rather, the reimbursement requirement can be triggered by an issuer's misconduct. Since a company can only act through its employees and agents, the misconduct of others within the company may be imputed to the company and trigger the reimbursement requirement.

7. To "cause" a securities law violation under Section 8A of the Securities Act or Section 21C of the Exchange Act, three elements must be established: (1) a primary violation, (2) an act or omission by the respondent that was a cause of the violation; and (3) the respondent knew, or should have known, that his conduct would contribute to the violation. *Robert M. Fuller*, 80 SEC Docket 3539, 3545 (Aug. 25, 2003). The Commission need not show that respondent's conduct was a proximate cause of the primary violations. *Rita J. McConville*, 85 SEC Docket 3127, 3146 n.45 (June 30, 2005), *pet. denied*, 465 F. 3d 780 (7th Cir. 2006). Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *KPMG Peat Marwick LLP*, 74 SEC Docket 384, 421 (Jan. 19, 2001), *reh'g denied*, 74 SEC Docket 1351 (Mar. 8, 2001), *pet. denied*, 289 F.3d 109 (D.C. Cir. 2002), *reh'g en banc denied*, 2002 U.S. App. LEXIS 14543 (D.C. Cir. July 16, 2002).

E. **VIOLATIONS**[8]

1. As a result of the conduct described above, Navistar violated Sections 13(a) and 13(b)(2)(A) of the Exchange Act and Rules 13a-1, 13a-13, and 12b-20 thereunder in connection with the vendor rebates, vendor tooling, warranty reserve, deferred expenses, and segment reporting matters, and Section 13(b)(2)(B) of the Exchange Act in connection with internal controls requirements;

---

[8] This matter is related to a civil action, *Securities and Exchange Commission v. James W. McIntosh, Thomas M. Akers, Jr., James J. Stanaway, Ernest A. Stinsa, and Michael J. Schultz,* to be filed in the United States District Court for the Northern District of Illinois, in which these individual respondents have consented to pay civil penalties as follows: McIntosh – $150,000; Akers – $100,000; Stanaway – $50,000; and Stinsa – $25,000. A civil penalty was not imposed against Respondent Schultz because of a demonstrated inability to pay.

2. As a result of the conduct described above, Ustian and Lannert were a cause of Navistar's violations of Section 13(b)(2)(B) of the Exchange Act regarding internal controls;

3. As a result of the conduct described above, McIntosh violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and was a cause of the Company's violations of Section 13(b)(2)(A) in connection with the vendor rebates/vendor tooling matter; violated Sections 17(a)(2) and 17(a)(3) of the Securities Act in connection with the warranty reserve matter; and was a cause of Navistar's violations of Section 13(b)(2)(B) of the Exchange Act regarding internal controls;

4. As a result of the conduct described above, Akers violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and was a cause of the Company's violations of Section 13(b)(2)(A) of the Exchange Act in connection with the vendor rebates matter;

5. As a result of the conduct described above, Schultz violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and was a cause of the Company's violations of Section 13(b)(2)(A) of the Exchange Act in connection with the Waukesha matter;

6. As a result of the conduct described above, Stanaway violated Sections 17(a)(2) and 17(a)(3) of the Securities Act in connection with the warranty reserve matter; and violated Exchange Act Rule 13b2-1 and was a cause of McIntosh's and Akers' violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and was a cause of the Company's violations of Section 13(b)(2)(A) of the Exchange Act, in connection with the vendor rebates matter; and

7. As a result of the conduct described above, Stinsa violated Exchange Act Rule 13b2-1 and was a cause of the Company's violations of Section 13(b)(2)(A) of the Exchange Act in connection with the vendor rebates matter.

F. NAVISTAR'S REMEDIAL EFFORTS AND COOPERATION

In determining to accept Navistar's Offer of Settlement and not impose a civil penalty against the Company, the Commission considered the remedial acts undertaken by Navistar and cooperation it afforded the Commission staff. The cooperation included the Company's decision to conduct an independent investigation. Navistar's remedial steps, implemented in response to the independent investigation's findings and in order to cure material weaknesses in the Company's internal controls, included: terminating or removing from financial reporting responsibilities various employees who were identified in the internal investigation as having committed intentional misconduct; adding more than 100 new finance and accounting employees with accounting backgrounds, including a new Director of Accounting Compliance and new accounting compliance managers and analysts in the Truck and Engine divisions; creating a new position, Corporate Compliance Officer, who is responsible for overseeing compliance with federal and state law and Company policy; realigning reporting chains so that finance personnel within the Engine and Truck divisions now report directly to the CFO, and not to operations managers; engaging consultants to improve warranty cost accounting models and methodologies; implementing new accounting policies and procedures; and instituting new employee training on internal controls and ethics.

G. UNDERTAKINGS

1. The goal of these undertakings is to achieve voluntary compliance with Section 304 of Sarbanes-Oxley.

2. To satisfy the forfeiture provisions of Section 304 of Sarbanes-Oxley, Ustian shall tender to the Company a sufficient number of shares of unrestricted Navistar common stock currently owned by Ustian to produce proceeds of $1,320,000 net of fees and commissions at the time of transfer. The time of transfer shall be the intraday market price at the time the shares leave Ustian's possession as determined by Ustian's brokerage firm. The $1,320,000 total represents a *pro rata* portion of Ustian's 2004 bonus based on the percentage of the Restatement Period during which Ustian was CEO of the Company. Ustian may make these transfers of stock on one or more occasions, so long as he completes the tender within 90 days after institution of this Order. Counsel for the Company shall confirm receipt of the shares from Ustian and the intraday price, the number of shares transferred, and the time the shares left Ustian's possession. This confirmation shall be sent to C. Joshua Felker, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549-5030, within seven days following the close of the 90-day period.

3. To satisfy the forfeiture provisions of Section 304 of Sarbanes-Oxley, Lannert shall pay the Company a total of $1,049,503, representing his 2004 bonus, within 90 days after institution of this Order. The payments shall be by certified check, bank cashier's check, or United States postal money order payable to Navistar International Corporation, and shall be delivered or mailed to Navistar International Corporation, c/o Curt A. Kramer, Associate General Counsel and Secretary, Navistar, Inc., 4201 Winfield Road, P.O. Box 1488, Warrenville, IL 60555, and shall be submitted under cover letter that identifies Lannert as a respondent in these proceedings and the file number of these proceedings. A copy of the letter and check or money order shall be sent to C. Joshua Felker, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., N.E., Washington, D.C. 20549-5030.

4. In determining whether to accept Ustian's and Lannert's Offers of Settlement, the Commission has considered these undertakings. Ustian and Lannert agree that if the Division of Enforcement believes that they have not satisfied these undertakings, it may petition the Commission to reopen this matter to compel compliance with Section 304 of Sarbanes-Oxley and determine whether additional sanctions are appropriate.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondents' Offers.

Accordingly, it is hereby ORDERED that:

A. Navistar shall cease and desist from committing or causing any violations and any future violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 thereunder;

B. Ustian shall cease and desist from causing any violations and any future violations of Section 13(b)(2)(B) of the Exchange Act;

C. Lannert shall cease and desist from causing any violations and any future violations of Section 13(b)(2)(B) of the Exchange Act;

D. McIntosh shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act;

E. Akers shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act;

F. Schultz shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act;

G. Stanaway shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rules 10b-5 and 13b2-1 thereunder and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act; and

H. Stinsa shall cease and desist from committing or causing any violations and any future violations of Exchange Act Rule 13b2-1 and from causing any violations and any future violations of Section 13(b)(2)(A) of the Exchange Act.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Casey
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62654 / August 5, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3166 / August 5, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13995

In the Matter of **MARK T. SCHWETSCHENAU,** **Respondent.**	**ORDER INSTITUTING PUBLIC ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 4C AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Mark T. Schwetschenau ("Schwetschenau" or "Respondent") pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 102(e)(1)(ii) of the Commission's Rules of Practice.

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement ("Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings or conclusions contained herein, except as to the Commission's jurisdiction over Respondent and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

9 of 62

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

A. Respondent

1. Mark T. Schwetschenau, 54, of Glen Ellyn, Illinois, was the Corporate Controller and principal accounting officer of Navistar International Corporation ("Navistar" or the "Company") from 1998 through February 2006. Schwetschenau was one of several senior officers responsible for certain aspects of the Company's internal controls. Among other things, he was directly responsible for Navistar's accounting policies and procedures. Schwetschenau is a registered certified public accountant in Illinois. During the relevant period, Schwetschenau was a member of The American Institute of Certified Public Accountants ("AICPA").

B. Related Entity

2. Navistar, a Delaware corporation headquartered in Warrenville, Illinois, is a holding company whose principal subsidiary, Navistar, Inc. (f/k/a International Truck and Engine Corporation), manufactures and markets commercial trucks, school buses, diesel engines, and related parts worldwide. During the relevant period, Navistar's securities were registered with the Commission pursuant to Section 12(b) of the Exchange Act and traded on the New York Stock Exchange. As of November 30, 2009, Navistar had 70,718,762 shares outstanding.

C. Factual Findings

1. Internal Controls

3. In December 2007, Navistar filed a delayed Form 10-K for fiscal year 2005 that disclosed various material weaknesses in its internal accounting controls for 2005-06. One of those material weaknesses concerned the Company's lack of a formalized process for "monitoring, updating, disseminating, and implementing GAAP-compliant accounting policies and procedures."

4. In 2002, the Company's Internal Audit department had advised senior management, including Schwetschenau, that Navistar's financial policies and procedures "have not been updated to keep pace with the changing business environment, which increases the risk of financial reporting misstatements." Internal Audit also had recommended that the Corporate Controllers' Office begin a process to evaluate and update such policies and procedures, and that a further process be implemented to help ensure that once the initial revisions have been made, adequate procedures exist to maintain the policies as current. Although Schwetschenau and another senior officer created and implemented a plan to address the issues identified by Internal Audit, not all of the concerned policies and procedures were updated within the three-year time frame agreed to by Internal Audit, due to the level of resources being devoted to this project. Schwetschenau should

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

have known that his conduct in this matter would contribute to a weakness in those internal controls.

2. Deferred Start-up Costs

5. In 2000, the Company entered into a long-term supply contract (the "Agreement") with an automobile manufacturer (the "Automaker") to develop and manufacture V-6 diesel engines commencing with model year 2002 and extending through 2012. From the fourth quarter of 2001 through the fourth quarter of 2002, the Company incurred substantial start-up costs relating to the Agreement, including expenses developing the engine, constructing a plant in Huntsville, Alabama, and leasing engine assembly assets. The Company began deferring some of these start-up costs in the fourth quarter of fiscal 2001 and as of the fourth quarter of 2002 had accumulated $57 million of deferred pre-production costs. Specifically, the Company deferred $4.3 million in the fourth quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in each of the second and third quarters of fiscal year 2002.[2]

6. Relevant accounting rules provided that such start-up costs could be deferred only if there existed an objectively verified and measured contractual guarantee of reimbursement. *See* FASB Emerging Issues Task Force Issue No. 99-5, *Accounting for Pre-Production Costs Related to Long-Term Supply Arrangements* ("EITF 99-5").

7. The terms of the Agreement standing alone did not provide for reimbursement in a manner sufficient to satisfy the requirements for start-up cost deferral pursuant to EITF 99-5. Based on the requirements of EITF 99-5 and the Company's independent auditor, the Company attempted to secure a letter that would document an oral promise from the Automaker to reimburse the Company for its investment under the Agreement. Without the guarantee, the Company was not entitled to defer these costs.

8. The Company never received from the Automaker a sufficiently specific written guarantee of reimbursement. Beginning in September 2001 and continuing until October 2002, when the Automaker cancelled the Agreement, Company management repeatedly but unsuccessfully sought such a guarantee in the form of a letter.

9. Schwetschenau, as principal accounting officer, and after consultation with senior management and the Company's independent auditor on the financial reporting of the issue, permitted the deferral of these start-up costs from the fourth quarter of 2001 through the fourth quarter of 2002. Schwetschenau was aware of the aforementioned circumstances concerning these costs, including that the Company was unable to obtain a written guarantee of specific reimbursement from the Automaker. Consequently, Schwetschenau should have known that the decision to defer these start-up costs was not in compliance with Generally Accepted Accounting Principles ("GAAP").

---

[2] The $12.8 million, $13.3 million, and $13.3 million totals represent 12.5 percent, 65.5 percent, and 25.4 percent, respectively, of the Company's previously reported loss before income tax if adjusted to reverse these deferrals for each of the first three quarters of fiscal year 2002.

10. While Schwetschenau did receive assurances from Navistar senior officers that the Automaker had in fact committed to reimburse the Company for these start-up costs and Navistar's independent auditor was aware of all related facts and accepted the continuing deferral, these costs still should not have been deferred because the Company had not received the aforementioned written guarantee of reimbursement. Navistar, like all issuers registered with the Commission, is ultimately responsible for the accuracy of its books, records and accounts.

D. Findings

11. Section 13(a) of the Exchange Act requires all issuers with securities registered under Section 12 of the Exchange Act to file periodic reports. The obligation to file these periodic reports includes the obligation that they be complete and accurate in all material respects. *See SEC v. IMC Int'l, Inc.*, 384 F. Supp. 889, 893 (N.D. Tex.), *aff'd mem.*, 505 F.2d 733 (5th Cir. 1974). No showing of scienter is necessary to establish a violation of Section 13(a) of the Exchange Act. *See SEC v. McNulty*, 137 F.3d 732, 740-741 (2d Cir. 1998).

12. Section 13(b)(2)(B) of the Exchange Act requires all reporting companies to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP.

13. Section 21C of the Exchange Act provides that the Commission may issue a cease-and-desist order against a person who is "a cause of" a violation by an issuer "due to an act or omission the person knew or should have known would contribute to such violation . . . ." The Commission need not show that Respondent's conduct was a proximate cause of the primary violations. *Rita J. McConville*, 85 SEC Docket 3127, 3146 n.45 (June 30, 2005), *pet. denied*, 465 F. 3d 780 (7th Cir. 2006). Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. *KPMG Peat Marwick LLP*, 74 SEC Docket 384, 421 (Jan. 19, 2001), *reh'g denied*, 74 SEC Docket 1351 (Mar. 8, 2001), *pet. denied*, 289 F.3d 109 (D.C. Cir. 2002), *reh'g en banc denied*, 2002 U.S. App. Lexis 14543 (D.C. Cir. July 16, 2002).

14. Based on the foregoing, the Commission finds that Respondent was a cause of Navistar's violations of Sections 13(a) and 13(b)(2)(B) of the Exchange Act.[3]

15. Rule 102(e)(1)(ii) of the Commission's Rules of Practice states that the Commission may deny to any person the privilege of appearing or practicing before it if such person engaged in "improper professional conduct."

16. Rule 501 of the AICPA Code of Professional Conduct, among other things, prohibits members from committing negligence in the preparation of financial statements or records through several means, including permitting another to make materially inaccurate

[3] On August 5, 2010, the Commission issued a settled cease-and-desist order against Navistar that found, among other things, that Navistar had violated Sections 13(a) and 13(b)(2)(B) of the Exchange Act. Under terms of its settlement with the Commission, Navistar consented to entry of the cease-and-desist order without admitting or denying the findings or conclusions contained therein.

entries in an entity's financial statements or records. The decisions that allowed Navistar to defer the charges as discussed above from the fourth quarter of fiscal year 2001 through the fourth quarter of fiscal year 2002 constitute a violation of Rule 501. *See Rule 501 of the AICPA Code of Professional Conduct.*

17. Based on the foregoing, the Commission finds that the Respondent engaged in improper professional conduct within the meaning of Rule 102(e)(1)(ii) and Rule 102(e)(1)(iv)(B)(2) of the Commission's Rules of Practice.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Respondent shall cease and desist from causing any violations and any future violations of Sections 13(a) and 13(b)(2)(B) of the Exchange Act;

B. Respondent is denied the privilege of appearing or practicing before the Commission as an accountant;

C. After one year from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Schwetschenau appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

D. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state registration or licensure is current and he has resolved any disciplinary issues with the applicable state boards of accountancy. However, if state registration or licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Schwetschenau's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.[4]

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

[4] In addition to the relief ordered herein, Schwetschenau has consented to the filing of a parallel civil action in the United States District Court for the Northern District of Illinois in which he has consented to pay a civil penalty of $37,500.

SECURITIES AND EXCHANGE COMMISSION
Washington D.C.

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 62656 / August 5, 2010

Admin. Proc. File No. 3-13535

In the Matter of the Application of

GATELY & ASSOCIATES, LLC
and
JAMES P. GATELY, CPA

c/o Roddy B. Lanigan, Esq.
Lanigan & Lanigan, PL
222 S. Pennsylvania Ave., #101
Winter Park, FL 32789

For Review of Disciplinary Action by

PCAOB

OPINION OF THE COMMISSION

PUBLIC COMPANY ACCOUNTING OVERSIGHT BOARD – REVIEW OF DISCIPLINARY PROCEEDINGS

Violation of Board Rule

Failure to Cooperate with Inspection

Registered public accounting firm and associated person failed to cooperate with board inspection. *Held*, findings of violation and sanction imposed are *sustained*.

APPEARANCES:

Roddy B. Lanigan, of Lanigan & Lanigan, PL, for Gately & Associates, LLC, and James P. Gately.

J. Gordon Seymour and *Mary I. Peters*, for the Public Company Accounting Oversight Board.

Appeal filed: June 26, 2009
Last brief received: October 14, 2009

10 of 62

James P. Gately and Gately & Associates, LLC, a registered public accounting firm (the "Firm" and together with Gately, "Applicants"), filed an application pursuant to Section 107(c) of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley")[1] for review of disciplinary action taken by the Public Company Accounting Oversight Board (the "Board" or "PCAOB"). The Board found that Applicants failed to cooperate with an inspection by the Board's Division of Registration and Inspections ("Inspections") and thereby violated Board Rule 4006 ("Rule 4006" or the "Rule"). The Board barred Gately from associating with any registered public accounting firm and permanently revoked the Firm's registration. We base our findings on an independent review of the record.

I.

BACKGROUND

Congress established the Board to "protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports."[2] In furtherance of these goals, Sarbanes-Oxley requires the Board to conduct a "continuing program of inspections to assess the degree of compliance of each registered public accounting firm and associated persons . . . with [Sarbanes-Oxley], the rules of the Board, the rules of the Commission, or professional standards."[3] Highlighting the importance of these inspections, the statute establishes guidelines regarding the frequency, scope, procedures and reports for inspections.[4] In addition, recognizing that the effectiveness of the Board's inspections depends on full cooperation by the auditing firms, Section 102 of Sarbanes-Oxley requires any firm participating in the preparation of any issuer audit report to consent "to cooperat[e] . . . and compl[y] with any request for testimony or the production of documents made by the Board in furtherance of its authority and responsibilities under this title."[5] In order to secure cooperation with inspections on a going-forward basis, Section 102 also requires firms to acknowledge "that [the] firm understands and agrees that cooperation and compliance" with any such request for testimony or documents "shall

---

[1] 15 U.S.C. § 7217(c).

[2] 15 U.S.C. § 7211(a).

[3] 15 U.S.C. § 7214(a).

[4] 15 U.S.C. § 7214(a)-(h). For example, the statute requires Board inspections every three years or annually, depending on the number of audit reports issued by the firm. 15 U.S.C. § 7214(b)(1)(B) (requiring triannual inspections for firms that regularly provide audit reports for 100 or fewer issuers); 15 U.S.C. § 7214(b)(1)(A) (requiring annual inspections for firms that regularly provide audit reports for more than 100 issuers).

[5] 15 U.S.C. § 7212(b)(3)(A).

be a condition to the continuing effectiveness of the registration of the firm with the Board."[6] The Board's periodic inspections, and full cooperation therewith by registered firms, are pivotal to the Board's ability to enhance investor protection and the accuracy of issuer auditor reports through its oversight of registered accounting firms.

This is the first litigated appeal of a PCAOB disciplinary decision, and will address the parameters of the Board's authority to discipline a failure to provide documents and information in connection with its inspections. Applicants do not contest the timing and content of the Board's inspection requests or their own longstanding delays in providing the requested information, but argue that their conduct should be excused based on Gately's personal circumstances and state of mind during the Board's attempted inspection. Given the Board's necessary reliance on the inspection process in order to inspect audit reports for informativeness, accuracy, and independence, disposition of these defenses will impact the Board's effectiveness in fulfilling this regulatory mandate.

II.

FACTS

Gately, a certified public accountant, is the Firm's managing member, president, and sole owner and employee. As required under Sarbanes-Oxley, the Firm's application for Board registration in 2003, which was completed by Gately, consented to cooperate with Board inspections and acknowledged that cooperation with such inspections was a condition to the Firm's continued registration.

Beginning in early 2007, Inspections attempted to contact Gately to initiate an inspection of the Firm. Between May and September 2007, Inspections made repeated attempts to schedule an inspection date. However, scheduling was difficult because Gately was receiving treatment in the Miami area for a chemical dependency (the "Condition"),[7] and had difficulty accessing Firm workfiles stored in Orlando, Florida.[8] As of September 12, the inspection was scheduled for October 1, 2007. On September 12, however, Gately informed Inspections that he would not be able to retrieve the files from Orlando in time for the scheduled October 1 inspection. Inspections

---

6 15 U.S.C. § 7212(b)(3)(B). The applying firm must also agree to require a comparable agreement and acknowledgment from each person associated with the Firm. *Id.*

7 On December 14, 2009, we granted in part Gately's request for a protective order regarding the discussion of the Condition. *Order Granting Partial Protective Order* (Dec. 14, 2009), Admin. Proc. File. No. 3-13535. Consistent with that order, this opinion discusses the Condition and treatment to the extent necessary to resolve the issues before us.

8 The Firm was originally located in the Orlando area.

agreed to reschedule for November 5. Gately asserts that he discussed with Inspections staff the option of deregistering the Firm, but he ultimately decided against deregistration.

That same day, Inspections e-mailed Gately an Issuer Information Form ("IIF") and asked Gately to complete the IIF by September 20. The IIF required disclosure of the Firm's client names, locations, industries, and audit report release dates. Inspections told Gately that, once the staff received the completed IIF, "we will try to let you know which engagements we have selected as soon as possible so that you will have plenty of time before the November 5, 2007 planned inspection date to retrieve the work papers from storage." Noting the previous postponement, Inspections warned that "it is not likely that we will be able to accommodate a request to move the inspection to a date any later in the year."

Later that month, a Florida state court placed Gately on two years' probation for a traffic-related offense. The terms of probation required advance notice in order to travel outside of the Miami area, including to Orlando (the location of his audit files).

Gately did not meet the September 20 deadline for submitting the IIF. Throughout October, Inspections asked Gately for the IIF in multiple voice mail messages, e-mails, and letters. On October 15, Inspections sent Gately a Data Request form ("Data Request Form") listing documents to be prepared and available to be reviewed during the November 5 inspection. The Data Request Form asked for information about, among other things, the nature of the Firm's practice, quality control policies and procedures, any litigation against the Firm, communications with regulatory agencies, and professional education programs.

On October 17 and October 30, Gately notified Inspections that his computer had been stolen and that he would need to travel to Orlando to recreate the IIF information.[9] On October 31, Inspections warned Gately that:

> failure on your part either to provide all the information requested of you or to allow the inspection team to commence field work of the inspection of your firm on Monday November 5, 2007 may result in this matter being referred to the PCAOB's Division of Enforcement and Investigations. This could result in disciplinary action for failure to cooperate with an inspection as required by PCAOB Rule 4006, even if you later permit the inspection.

As of October 31, Inspections had not received the IIF from Gately. Inspections staff nonetheless sent Gately an October 31 e-mail identifying two audit engagements that had been selected for review (the "Selected Engagements"), and indicating that additional audit engagements might be selected for review during the course of the inspection. The e-mail further

---

9 Although Gately informed Inspections on October 17, 2007 that he had earlier returned the IIF, Inspections did not receive the form. He does not currently contend that he returned the IIF in 2007.

advised that the November 5 inspection would require Gately to make available all workpapers for the Selected Engagements, to "discuss [the Firm]'s quality control policies and practices," and to "schedule interviews/meetings related to each engagement to be inspected."

By e-mail on November 2, Gately stated that he was "not confirming" the November 5 inspection, and that he would be "preparing a deregistration form sometime next week." Referencing an earlier discussion with Inspections staff regarding the possibility of avoiding an inspection by deregistering from PCAOB, Gately stated:

> When I first spoke with [an Inspections staff member] I was going to deregister from the PCAOB as I was [undergoing treatment in Miami] and would be spending months there and not able to participate in an inspection. I then contacted [the staff member] later to see if she would give me a chance to have files collected for me and if it did not work out for the timetables I would deregister.

Gately's e-mail explained that he had again decided to deregister because he would not have time to make travel arrangements under the terms of his probation to gather his files, and that he "ha[d] been getting rid of the public companies due to [his] personal commitments."

Responding that same day, Inspections confirmed its understanding that Gately intended to file the deregistration form during the week of November 5. Inspections stated that it would postpone the inspection field work to allow Gately time to deregister, and that it would postpone the inspection itself if Gately in fact filed the deregistration form. It warned, however, that if the form was not filed by November 26:

> we will commence the inspection field work on that date. In that event, you should have the [IIF] and all of the other information we have requested available for us on November 26, 2007, as well as audit engagement file(s) for the two engagements previously communicated to you, including the audit work papers, permanent files and report files and any other relevant documentation supporting the firm's audit opinion.

Like the October 31 letter, this letter warned that failure to provide all requested information or to allow the inspection to begin as scheduled could result in disciplinary action.

The day after Gately sent his November 2 e-mail stating his intention to deregister, however, he sent another e-mail to Inspections stating that he had not received notice of the two Selected Engagements. In its reply, Inspections identified the Selected Engagements, but also asked Gately to clarify whether he still intended to deregister. On November 5, Gately replied, "If you are willing, I can go to Orlando to search the storage units for the files and give you an answer on withdrawal a week from today if the files are easily accessible."

Inspections replied by e-mail on November 7, declining to advise Gately on whether to deregister or prepare for inspection, stating "[b]ased on your facts and circumstances, you should determine how best to respond." It also reminded him that the inspection would take place on November 26, 2007 if the Firm did not deregister, reiterated the documentation required for the inspection, and again warned that failure to allow the inspection or to supply all requested documentation by the applicable deadlines could result in an enforcement action.

In response to these e-mails discussing deregistration as an alternative to the inspection, Gately responded, "Got it. Going to Orlando to pick up the files." On November 19, Gately again confirmed via e-mail that he would prepare the relevant documentation for the inspection, stating, "My intention is to have the two companies available on the 26th. I returned with them from Orlando this past Saturday."

Less than a week later, on November 22, Gately e-mailed Inspections that he would "not be available for the inspection." He briefly stated, "[w]hen arriving back to the Miami area I was confronted with . . . the old house having had fire damage," and that "unfortunately my stuff is in the old house." Gately's e-mails did not describe which, if any, of his audit files were damaged in the fire. Inspections expressed sympathy, and asked Gately to call the next day, Friday, November 23, to "discuss how to proceed." Applicants now contend that Gately "could not complete the [IIF] because the necessary files were destroyed" and that the fire "destroyed most of the necessary files requested in the PCAOB audit," but Applicants have not identified or described which files were damaged.

Although the inspection was scheduled to begin the following Monday, November 26, Gately had not called the previous Friday as requested by Inspections staff. Inspections sent Gately another message on the 26th again asking Gately to call. Gately finally responded that day with an e-mail stating, "I will call," but did not. Gately now asserts that he was preoccupied with finding a new home.

On November 27, Inspections staff sent Gately another letter, this time stating that it was "imperative" that he reschedule the inspection. The letter warned that failure to contact Inspections staff could result in disciplinary action. Gately rescheduled for December 10. Inspections agreed to conduct the inspection remotely – receiving all materials in the Board's Atlanta office prior to the inspection and conducting the inspection interview by telephone. On November 29, 2007, Inspections sent a letter confirming the December 10 inspection date and again requesting return of the IIF. The letter also requested by December 7, 2007: (a) copies of the audit engagement files for the two Selected Engagements and (b) other documents and information described in the Data Request Form. Although Inspections followed up with several messages, Gately did not provide the requested documentation.

On December 7, Inspections e-mailed Gately, pointing out that:

> the inspection leader . . . has called and left you two voice mail messages . . . to which you have not responded, to confirm the date of the inspection and to address any questions you may have concerning the inspection. Also, we have not yet received the copies of your audit work papers and other requested information, which were due to us today.

On December 10, the rescheduled inspection date, Gately emailed that he "[j]ust saw [the December 7 e-mail] message" from Inspections, that there had been an "[u]nexpected slow up on my side," and that he would call with an update. Gately did not call. Gately contends that he was planning another trip to Orlando to supplement and complete fire-damaged files.

When Inspections did not receive a further update from Gately, the Director of Inspections sent Gately a letter via e-mail and Federal Express on December 20. The letter recounted Inspections' longstanding efforts to schedule the inspection, reiterated Gately's obligation to supply the requested information, and gave a final deadline of December 28 (the "Final 2007 Deadline"). The letter stated that failure to meet the Final 2007 Deadline would be referred to the Board's Division of Enforcement and Investigations ("Enforcement") and could lead to disciplinary proceedings even if the requested information were provided after the Final 2007 Deadline. The letter stated, "Potential sanctions for [violations of Rule 4006] include, among other things, suspension or revocation of the firm's registration, a suspension or bar on your ability to be an associated person of a registered firm, a limitation on the activities or operations of the firm, or the assessment of monetary penalties."

On January 2, 2008, Gately informed Inspections that he had not received the December 20 letter because he had been traveling during the end of December, and no longer resided at the address to which the letter was sent. Gately requested another extension of the deadline and declared that his "intention was to cooperate with the team." By e-mail on January 3, Inspections declined to further extend the deadline, and advised Gately that the "demand for the requested materials . . . still stands, and we encourage you to provide the materials and permit the inspection as soon as possible."

The next day, Gately confirmed that he was able to open the January 3 e-mail message. Gately asserts that after receiving this January 3 message, he "understood that [the] matter would further be handled by [Enforcement] given that the deadline of December 28 had already [passed]." Applicants eventually returned an IIF on August 15, 2008, four months after these proceedings were instituted.[10] However, Applicants never provided the requested documents for the Selected Engagements or the information identified in the Data Request Form.

Gately issued fourteen audit reports for public company clients between August 18, 2007 and February 25, 2008, each of which was included in filings with the Commission. Three of the fourteen reports were issued prior to the Final 2007 Deadline, and the remaining eleven reports were issued in January and February 2008, including audit reports for both Selected Engagements in February 2008.

III.

PROCEEDINGS BELOW

The Board's Order Instituting Disciplinary Proceedings charged that Applicants violated Board Rule 4006 "throughout much of 2007 and into 2008 by failing to provide requested . . . access to records" and by "failing to provide information by written responses, including information specified in an Issuer Information Form and a Data Request form." On summary disposition, the Board hearing officer (the "Hearing Officer") found that Gately's failure to submit timely the IIF, the audit engagement files for the Selected Engagements, and the Data Request Form violated Rule 4006, but declined to find that the agreed-upon inspection postponements prior to September 2007 had violated the Rule. Although the Hearing Officer held that a scienter finding is not required to find liability under the Rule, in determining sanctions he held that "any rational finder of fact would have to conclude that Respondents' failure to cooperate . . . was at least reckless." He noted Inspections' repeated warnings, and Applicants' failure to provide any "of the requested information . . . or any detailed explanation of their efforts to comply . . . or any colorable justification for failing to provide information after December 2007." The summary disposition order permanently revoked the Firm's registration and permanently barred Gately from association with any registered public accounting firm.

The Board affirmed the summary disposition order, finding that Applicants' failure to submit the IIF, the Data Request Form, and the files for the Selected Engagements violated Rule 4006. The Board held that Applicants failed to "demonstrate[] a genuine issue of fact about whether Gately was so incapacitated throughout the period in question as to be unable to provide any of the requested information." This appeal followed.

---

10 This August 15, 2008 submission was apparently sent in response to an e-mailed request from Inspections on June 5, 2008, but Applicants did not notify the Board hearing officer about this submission before the hearing officer issued the summary disposition order, and it is not included in the record.

IV.

STANDARD FOR SUMMARY DISPOSITION UNDER BOARD RULE 5427

Applicants challenge the appropriateness of the Board's resolution of the case by summary disposition. Applicants focus on Gately's Condition, treatment, and other obstacles to accessing his records. Applicants primarily argue that these circumstances made his compliance with Inspections requests "impossible" and demonstrate that he did not act with the requisite state of mind to establish liability under Rule 4006 or merit the sanctions imposed by the Board, claiming that they should have been afforded a hearing to develop those defenses.[11] Under Board Rule 5427(d), summary disposition is appropriate "if the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a disposition as a matter of law." Summary disposition "on the issue of liability alone" is authorized even when "there is a genuine issue as to a sanction." Our analysis of the summary disposition issue is guided by the Board's interpretation of its summary disposition standard.[12] As the Board noted, Rule 5427 mirrors the summary judgment standard in Rule 56 of the Federal Rules of Civil Procedure,[13] and accordingly federal court interpretations of Rule 56 are instructive in interpreting the Board rule.

Not every alleged factual dispute precludes summary disposition. To prevent summary disposition, the opposing party must present facts demonstrating a genuine issue of fact that is

---

[11] Quoting *Charbonnages de France v. Smith*, 597 F.2d 406, 414 (4th Cir. 1979) (stating that "summary judgment is seldom appropriate in cases wherein particular states of mind are decisive as elements of a claim or defense").

[12] *Cf. Fogel v. Chestnutt,* 533 F.2d 731, 753 (2d Cir. 1975) (Friendly, J.) ("[A]n exchange has a substantial degree of power to interpret its own rules."), *cert. denied,* 429 U.S. 824 (1976); *Shultz v. SEC*, 614 F.2d 561, 571 (7th Cir. 1980) ("[B]ecause these are rules of the Exchange, the Exchange should be allowed discretion in determining their meaning." (internal citations omitted)); *Intercontinental Indus., Inc. v. Am. Stock Exch.*, 452 F.2d 935, 940 (5th Cir. 1971) ("Since these are the rules of the Exchange, it should be allowed broad discretion in the determination of their meaning and application."), *cert. denied,* 409 U.S. 842 (1972).

[13] Fed. R. Civ. P. 56(c), (d)(2) ("The [motion for summary judgment] should be rendered if the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law. . . . An interlocutory summary judgment may be rendered on liability alone, even if there is a genuine issue on the amount of damages.").

material to the charged violation.[14] In determining whether a genuine dispute has been identified, the record should be "viewed most favorably to the non-moving party," but the hearing officer "need not credit purely conclusory allegations, indulge in rank speculation, or draw improbable inferences."[15] As the Board noted, "Where the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, there is no 'genuine issue for trial.'"[16]

Rule 56 guidance regarding the materiality of a factual dispute is also instructive.[17] Materiality analysis under Rule 56 is driven by the underlying "substantive law," *i.e.*, "[o]nly disputes over facts that might affect the outcome of the suit under the governing law will properly preclude the entry of summary judgment."[18] Similarly, the party opposing summary disposition in a Board disciplinary action should identify a factual issue meriting development at a hearing that is germane to the liability and/or sanctioning determination. Applicants' defenses were material for summary disposition purposes only if they were relevant to the Board's findings in support of the liability and sanctioning analysis.

V.

RULE 4006 VIOLATION

Pursuant to Section 19(e) of the Securities Exchange Act of 1934,[19] we will sustain the Board's finding of violation if the record shows that Applicants engaged in the conduct found by

---

14 *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986).

15 *Nat'l. Amusements, Inc. v. Town of Dedham*, 43 F.3d 731, 735 (1st Cir. 1995).

16 Quoting *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986) (quoting Fed. R. Civ. P. 56(e)).

17 *Cf. Thomas W. Heath*, Securities Exchange Act Rel. No. 59223 (Jan. 9, 2009), 94 SEC Docket 3466 & n.64, *petition denied*, 586 F.3d 122 (2d Cir. 2009) (applying Rule 56 guidance to motion for summary disposition of a NYSE proceeding when the NYSE Rules did not include a legal standard for summary disposition); *Frank P. Quattrone*, Exchange Act Rel. No. 53547 (Mar. 24, 2006), 87 SEC Docket 2155 (applying Rule 56 guidance to an NASD proceeding when the NASD standard indicated that a motion for summary disposition "may [be] grante[ed] . . . if there is no genuine issue with regard to any material fact and the Party that files the motion is entitled to summary disposition as a matter of law").

18 *Anderson*, 477 U.S. at 248.

19 15 U.S.C. § 78s(e); 15 U.S.C. § 7217(c)(2).

the Board, that such conduct violated Rule 4006, and that the Rule was applied in a manner consistent with the purposes of the Exchange Act and Sarbanes-Oxley.[20]

A. Applicants Engaged in the Conduct Found by the Board

Undisputed record evidence establishes that Applicants failed to comply with multiple deadlines for written responses to the IIF, the information identified in the Data Request Form, and the audit records for the Selected Engagements. Applicants failed to comply or cooperate with the following deadlines that were scheduled, and then rescheduled, in 2007:

Deadline	**Information/records requested**	**Date request made to Applicants**
September 20, 2007	IIF	September 12, 2007
November 5, 2007	Data Request Form Selected Engagement records	October 15, 2007 October 31, 2007
November 26, 2007	IIF Data Request Form Selected Engagement records	November 2, 2007
December 7, 2007	Data Request Form Selected Engagement records	November 29, 2007
December 28, 2007 (Final 2007 Deadline)	IIF Data Request Form Selected Engagement records	December 20, 2007

Applicants further admit that when these proceedings were instituted in April 2008, four months after the Final 2007 Deadline, they still had not produced any of the information or records requested by Inspections and provided only the IIF in August 2008.

B. Applicants' Conduct Violated Rule 4006 and the Rule was Applied in a Manner Consistent with Sarbanes-Oxley

Rule 4006 requires every registered public accounting firm and every associated person of a registered public accounting firm to "cooperate with . . . any Board inspection." The Rule states that "[c]ooperation shall include, but is not limited to, cooperating and complying with any request, made in furtherance of the Board's authority and responsibilities under [Sarbanes-Oxley],

---

20 15 U.S.C. § 7212(c)(2).

to – (a) provide access to, and the ability to copy, any record in the possession, custody, or control of such firm or person, and (b) provide information by oral interviews, written responses, or otherwise." The obligations under Rule 4006 are unequivocal, and apply to "any request[] made in furtherance of the Board's authority and responsibilities."

Applicants failed to comply with these requirements. They never provided the requested documents in connection with the Selected Engagements in violation of Rule 4006(a). Applicants also failed to provide the information requested in the IIF and Data Request Form in response to the September 20 and November 5 deadlines, violating Applicants' obligation to supply information to the Board under Rule 4006(b).

Applicants assert that they did not have access to unspecified records because they were damaged by fire in late November 2007. However, by that time they had already missed the November 5 deadline for producing the Selected Engagement records. Moreover, they failed to provide any records that remained in their "possession, custody or control" under Rule 4006(a) and failed to provide a detailed description of the destroyed documents or an explanation of steps taken to retrieve any missing records. These failures support a finding that Applicants violated the duty to comply with the Board's requests for records. As we have previously held in the context of self-regulatory organization ("SRO") requests, "if an associated person cannot provide the information sought by the [SRO], the associated person has the obligation to explain the deficiencies in his responses as completely as he is able" and be prepared to describe "any attempts he made to locate the records or the information they apparently contained."[21]

Applicants further assert that the Board improperly found liability without giving a full hearing to their defense that Gately did not act with the requisite state of mind, arguing that he was "mentally and physically unable to perform" as a result of his Condition. We conclude that the Board is not required to establish that Applicants acted with a particular state of mind in order to establish a violation of Rule 4006.[22] Nothing on the face of either the Rule or Section 102 of

---

[21] *Robert A. Quiel*, 53 S.E.C. 165, 168 (1997) (rejecting claim that applicant "could not access readily the information that the NASD requested" when "he failed to explain the deficiencies in his responses or to answer as completely as he was able"); *see also Joseph Patrick Hannan*, 53 S.E.C. 854, 859 (1998); *Robert Fitzpatrick*, 55 S.E.C. 419, 424 n.11 (2001).

[22] We note that this interpretation of the Rule is consistent with the obligations of other securities professionals to provide SROs with access to their books and records. *See, e.g.*, FINRA Rule 8210 (setting forth the right of FINRA staff to "inspect and copy the books, records, and accounts of such member or person with respect to any matter involved in the investigation, complaint, examination, or proceeding"). Scienter is not an element of the FINRA rule, *Howard Brett Berger*, Exchange Act Rel. No. 58950 (Nov. 14, 2008), 94 SEC Docket 11615, 11629-30 (affirming a bar for failure to appear for NASD interview), and we have specifically rejected

(continued...)

Sarbanes-Oxley refers to state of mind. Rather, auditing firms knowingly take on the burden of compliance with these inspections when they acknowledge that their registration is contingent on their "continued cooperation . . . and compliance with any request for testimony or the production of documents made by the Board." We also think this interpretation of Rule 4006 is consistent with the fact that Sarbanes-Oxley provides for an assessment of knowledge, recklessness and negligence in the Board's analysis of appropriate sanctions, and provides for certain Board penalties and other sanctions in the absence of such findings.[23] Given these guideposts for balancing state of mind evidence in the statute itself, we do not believe that the initial Rule 4006 liability determination must be based on a finding that Applicants "intentionally and recklessly disregarded any duty to follow the rule," as Applicants claim.

Applicants also assert that they are entitled to the defense of "impossibility of performance," which they argue was not, and could not have been, properly considered by the Board in the context of a summary disposition. While "impossibility" may be a common law defense to a breach of contract,[24] Applicants cite no authority, and we are aware of none, suggesting that this common law contract principle gives rise to an affirmative defense to a violation of the Board's rules. Nor do they adequately explain why their various justifications for their non-compliance would qualify for such a defense or how their completion of fourteen audits during the period at issue can be reconciled with such a defense.[25] In the proceedings below, Applicants cited a case analyzing and rejecting an impossibility defense to a failure to comply

---

22 (...continued)
contentions that violations of such rules must be based on "an intentional or deliberate effort to withhold information." *Quiel*, 53 S.E.C. at 168 (rejecting applicant's assertions "that he cooperated to the best of his ability and that lack of information and documentation prevented his more complete cooperation with the NASD's requests" when Commission decisions under the SRO rule "make clear that . . . it is unnecessary to find an 'intentional or deliberate effort to withhold information'" (quoting *Richard J. Rouse*, 51 S.E.C. 581, 585 (1993)). Both the Commission and the courts have recognized the authority of SROs to discipline persons for rule violations that are not predicated on state of mind findings, even when "the lack of a scienter requirement may make for a more flexible rule." *Heath*, 586 F.3d at 140. These principles are equally applicable to discipline by the Board.

23 *See* 15 U.S.C. §§ 7215(c)(5) and 7215(c)(4)(D)(i), (E)-(G) (authorizing penalties up to $100,000 for individuals or $2 million for firms, censure, professional training or education and other appropriate remedies without mental state findings); *see also infra* Section VI. Sanctions.

24 *See, e.g.*, Posner & Rosenfield, *Impossibility and Related Doctrines in Contract Law: An Economic Analysis*, 6 J. Legal Studies 83 (1977).

25 This defense is discussed more fully *infra* in Section VI. Sanctions.

with a court order to produce documents, but they offer no explanation for why such analysis should be applied to Rule 4006.[26] Such an interpretation would be particularly inappropriate when we have rejected similar attempts to apply civil contempt principles to violations of the rules of SROs.[27]

In light of the unavailability of state of mind and impossibility as defenses to conduct violating the Rule, these claims were not material to the Board's findings in support of the violation, and Applicants were not entitled to a hearing exploring their merits in connection with the Board's liability analysis. Because undisputed record evidence establishes that Applicants failed to cooperate with the 2007 Board inspection, we find that Applicants violated Rule 4006.

VI.

SANCTIONS

Under Section 107(c)(3) of Sarbanes-Oxley, we review sanctions imposed by the Board to determine if, "having due regard for the public interest and the protection of investors," the sanction "(A) is not necessary or appropriate in furtherance of [Sarbanes-Oxley] or the securities laws; or (B) is excessive, oppressive, inadequate, or otherwise not appropriate to the finding or the basis on which the sanction was imposed."[28] Based on our review, we "may enhance, modify, cancel, reduce, or require the remission of a sanction imposed by the Board upon a registered public accounting firm or associated person thereof."[29]

---

26 Citing *United States v. Plath*, 2003 WL 23138778 at *3 (S.D. Fla. 2003) (rejecting an "inability to comply" defense for a failure to comply with IRS subpoena in a civil contempt proceeding and stating that such a defense creates a "substantial" burden of establishing that the respondent has made "in good faith all reasonable efforts to comply" (internal citations omitted)).

27 *Cf. Berger*, 94 SEC Docket at 11627-28 (finding that cases addressing "subpoena power, judicial enforcement of subpoena power, and civil contempt powers" do not apply to failures to cooperate with NASD investigations).

28 15 U.S.C. § 7217(c)(3).

29 *Id.*

A. Sarbanes Oxley Authorizes Bars and Revocation Based on Reckless Conduct

Sarbanes-Oxley generally authorizes "such disciplinary or remedial sanctions as [the Board] determines appropriate" if the Board finds, "based on all of the facts and circumstances," that Applicants engaged in conduct violating a Board rule.[30] As apposite here, in order to impose a bar on future association and/or revocation of registration, Sarbanes-Oxley Section 105(c)(5) requires the Board to find that the conduct at issue was "intentional or knowing," which "include[s] reckless conduct," that results in a violation of the applicable regulatory standard. Here, the Board found Gately's conduct "at least reckless." Applicants challenge the Board's recklessness finding, arguing that their claims regarding Gately's state of mind and related circumstances created a material factual dispute precluding any finding of intentional or reckless conduct absent a hearing.

Although this is the first Commission case applying the knowledge, recklessness, and negligence standards in Section 105(c)(5), these standards are similar to the standards for Commission discipline of accountants under Rule 102(e) of our Rules of Practice (now also codified in Exchange Act Section 4C by Sarbanes-Oxley).[31] Given these similar formulations, our interpretations of the Rule 102(e) standards inform our analysis under Sarbanes-Oxley Section 105(c)(5).

Recklessness in this context, as under Rule 102(e), is an "extreme departure from the standards of ordinary care, . . . which presents a danger" to investors or the markets "that is either known to the (actor) or is so obvious that the actor must have been aware of it."[32] This standard

---

[30] 15 U.S.C. § 7215(c)(4).

[31] 15 U.S.C. § 78d-3. For example, the Board's authority under Section 105(c)(5)(A) extends to "intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standards," 15 U.S.C. § 7215(c)(5)(A), and the Commission's authority under Section 4C covers "intentional or knowing conduct, including reckless conduct, that results in a violation of applicable professional standards." 15 U.S.C. § 78d-3(b)(1). Whereas Section 105(c)(5)(B) covers "repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standards," Section 4C covers "negligent conduct in the form of . . . repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission." 15 U.S.C. §§ 7215(c)(5)(B) and 78d-3(b)(2)(B), respectively.

[32] *Amendment to Rule 102(e) of the Commission's Rules of Practice ("Amendment to Rule 102(e)")*, 63 Fed. Reg. 57,164, 57,166 (Oct. 26, 1998) (quoting *SEC v. Steadman*, 976 F.2d 636, 641 (D.C. Cir. 1992) (ellipsis in original) (quoting *Sundstrand Corp. v. Sun Chemical*

(continued...)

calls us to compare Applicants' violative conduct against the relevant professional standard of care and to assess evidence revealing Applicants' state of mind at the time they engaged in the violative conduct.[33]

B. Applicants' Failure to Cooperate with the Inspection Was Reckless

1. Extreme departure from the standard of ordinary care under Rule 4006

The first element of this recklessness standard considers whether Applicants' conduct departed from "applicable statutory, regulatory, or professional standard[s],"[34] in this case the standard for inspections under Rule 4006, and if so, the degree of such departure. As the hearing officer observed, the Rule requires "full and prompt cooperation" with Board requests,[35] and if Applicants "were unable to provide all of the information requested by Inspections within the time they were given," the duty to cooperate still "required [them] to provide as much responsive information as they could and to explain, as completely as possible, their efforts to obtain and provide the remaining information."[36]

---

32 (...continued)
Corp., 553 F.2d 1033, 1045 (7th Cir.), *cert. denied*, 434 U.S. 875 (1977)). Although this framework for establishing recklessness was borrowed from the anti-fraud context, the other elements for a fraud-based violation are not imported to the recklessness standard under Rule 102(e), *Marrie v. SEC*, 374 F.3d 1196, 1205 (D.C. Cir. 2004), or by extension, Section 105(c)(5).

33 *Michael J. Marrie*, 56 S.E.C. 760, 774 (2003) ("The definition of reckless conduct establishes the mental state that must be shown with respect to conduct that results in a violation of applicable professional standards. The question is not whether an accountant recklessly intended to aid in the fraud committed by the audit client, but rather whether the accountant recklessly violated applicable professional standards."), *rev'd on other grounds*, 374 F.3d at 1206.

34 15 U.S.C. § 7215(c)(5)(A).

35 Citing *Michael David Borth*, 51 S.E.C. 178, 180 (1992) (finding that a "[f]ailure to provide information fully and promptly undermines the NASD's ability to carry out its regulatory mandate").

36 *Cf. Rooney A. Sahai*, Exchange Act Rel. No. 55046 (Jan. 5, 2007), 89 SEC Docket 2402, 2407 ("We have long said that if a respondent is unable to provide the information requested, there remains a duty to explain that inability" and "we would have expected such an explanation . . . to detail his efforts to obtain the information requested") (internal citations omitted)); *Barry C. Wilson*, 52 S.E.C. 1070, 1073 n.14 (1996) (rejecting applicant's "contention

(continued...)

Applicants' conduct was an extreme departure from this "full and prompt" standard of care. Not only did Applicants fail to provide the requested information and records in response to reasonable deadlines, but they also failed to make reasonable efforts to explain and remedy their ongoing failure. This failure continued for almost seven months between the first deadline for completion of the IIF in September 2007 and the institution of the Board disciplinary proceedings in April 2008. The e-mails and other correspondence in the record confirm that Gately knew of each of the deadlines before they passed, and that he disregarded multiple warnings and reminders by Inspections staff.

Any restrictions on Gately's access to stored records, limitations on his travel, or claimed fire damage of records do not outweigh the evidence establishing an extreme departure from the objective standard of care for inspections. Inspections tried to accommodate his circumstances and facilitate his cooperation by rescheduling deadlines, agreeing to conduct the inspection remotely, and accepting Gately's shifting explanations for his failures. Moreover, the e-mail correspondence between Gately and Inspections in early November 2007 confirms that Gately was aware that he could deregister the Firm if he were unable to cooperate with the inspection requirements. He had considered this option several times before confirming his intention to cooperate with the inspection later in November. Even after Gately stated on November 22 he would not be available for an inspection scheduled for November 26, Inspections again tried to initiate a discussion with Gately on "how to proceed." Rather than reciprocating Inspections' repeated attempts to accommodate his circumstances or clarify his intentions, Gately's responses to these efforts were intermittent, cryptic, and non-committal at best. Many times, he simply failed to respond. Even when Gately promised to call Inspections to discuss missed deadlines on November 26 and December 10, he did not call. In light of Gately's egregious refusal to respond to Inspections' efforts at accommodation, any accidental destruction of files or other difficulties in securing files do not justify Applicants' prolonged failure to produce any of those documents within their control, to respond to routine questions, or to provide a detailed account of the missing records together with steps taken to retrieve them.

Nor do Gately's Condition and treatment excuse the extreme departure from the standard of care in this case. Applicants issued fourteen audit reports during the same period for which they contend that it was impossible to meet the professional standard of care for inspections, and we are not persuaded by Applicants' attempt to reconcile their "impossibility" claim with this conduct. Applicants assert that the public audits were not compromised by the circumstances making cooperation with the inspection impossible because the audits presented limited challenges. But, as the Board pointed out, Applicants failed to produce *any* materials or

---

[36] (...continued)
that 'he did his best'" to respond to NASD examination request when respondent "was unable to specify what documents he claims to have provided or when he provided them"); *see also supra* note 21 and accompanying text.

information in response to Inspections' requests before these proceedings were instituted. Applicants' failure means there is no basis on this record to assess whether the audit reports were in fact conducted in accordance with Board standards as Applicants represented in those reports. Applicants also assert that one of those audits was performed in order to secure audit files that had been damaged. However, the failure to cooperate persisted even after that audit. These facts compel the conclusion that Applicants' departure from the professional standard of care was extreme.

2. Risk of harm to investors and the markets

The second prong of the recklessness standard focuses on assessing the actor's state of mind based on evidence establishing what he or she knew or must have known when committing the violation.[37] But the actor cannot forestall a recklessness finding merely by denying that he or she knew of the risk posed by the violative conduct.[38] The recklessness standard is ultimately meant to identify conduct which, "under the circumstances of a given case, results in the conclusion that the reckless man should bear the risk of his" conduct.[39] Recklessness can be established by an "egregious refusal to investigate the doubtful and to see the obvious."[40] Courts have recognized that "[a]s a practical matter . . . knowledge is inferable from [the] gravity [of a danger]. . . . When the facts known to a person place him on notice of a risk, he cannot ignore the facts and plead ignorance of the risk."[41]

Applicants' prolonged failure to submit to Board inspection presented a risk of harm to investors and the markets that was so obvious that Applicants must have been aware of it. Applicants do not, and cannot credibly, claim that they "genuinely forgot" about the Board's unfulfilled inspection requests, or that their conduct resulted from "mere inexcusable neglect" of their inspection obligations.[42] In the Firm's registration application, Applicants themselves

---

37 *Sundstrand*, 553 F.2d at 1046.

38 *See Sundstrand*, 553 F.2d at 1046, 1048 (finding that recklessness was "established as a matter of law" even when respondent "denie[d] actual knowledge of the danger" posed by his conduct).

39 *Sundstrand*, 553 F.2d at 1045.

40 *Marrie*, 56 S.E.C. at 793, *rev'd on other grounds*, 374 F.3d at 1206; *see also Potts v. SEC*, 151 F.3d 810, 812 (8th Cir. 1998).

41 *Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 513 F.3d 702, 704 (7th Cir. 2008).

42 *See Sundstrand*, 553 F.2d at 1047 (indicating that the second prong of the recklessness standard would not be met in the anti-fraud context if the defendant "genuinely

(continued...)

knowingly agreed to cooperate with Board inspections and acknowledged that their continued registration was contingent on their cooperation with inspections. Although Gately claims that the Condition so "impaired his ability to engage in normal business and professional discourse" that he was simply unable to provide any information, records, or meaningful explanation in response to Board's inspection requests,[43] Applicants knew about each of the inspection deadlines that they missed, and also knew that deregistration was an option if Gately was unable to cooperate. Gately told Inspections staff at least twice in 2007 that he intended to apply to withdraw the Firm's registration due to his personal circumstances. In fact, his November 2 e-mail to Inspections stating his intention to deregister also stated that he had been "getting rid of the public companies." Moreover, Inspections repeatedly reminded Applicants that a failure to cooperate would violate Rule 4006 and warned that failures to meet inspection deadlines could result in discipline.

In light of this known failure to cooperate with the inspection or deregister, Applicants acted with reckless indifference to those relying on their audit reports when they continued to issue reports through 2007 and 2008. The risks to investors and markets posed by this conduct were so obvious that Applicants must have been aware of them, particularly given the Firm's statutorily-required acknowledgment that the inspections are a condition to registration.[44] Section 102 of Sarbanes-Oxley reflects Congress' judgment that auditing firms -- not public investors or

---

42 (...continued)
forgot to disclose information or that it never came to his mind" or if the conduct resulted from "mere inexcusable neglect").

43 The record includes an affidavit from a licensed therapist describing Gately's treatment for the Condition in 2007 and describing Gately as having "a general inability to function in otherwise normal business circumstances, an inability to maintain focus, and an avoidance pattern when presented with stressful circumstances." Although it is unclear whether this affidavit was in fact admitted as part of the record below, both the Hearing Officer and the Board considered the affidavit in their opinions, and the affidavit was included with the record certified by the Board to the Commission. We accordingly accept it as part of the record. Gately has represented that the treatment described in the affidavit continued through February 29, 2008. The record evidence indicates, however, that the failure to cooperate continued past April 2008 – past the period described in the affidavit, and past the treatment period accounted for in the record, and while Respondents continued to perform audits of public companies.

44 *See Inv. Registry of America, Inc.*, 21 S.E.C. 745, 760 (1946) (revoking registration of broker-dealer and investment adviser based on false and misleading statements in a registration statement and stating "even were we to assume the ignorance claimed by the [respondent's controlling persons], it would not follow that respondent should be permitted to continue its licensed activities. Such ignorance would amount to such a lack of necessary awareness and attention to responsibility as to establish in itself a disqualification to discharge the fiduciary duties which respondent has undertaken to perform for the public.").

markets -- should bear the consequences for any firm's inability to comply with inspections. Regardless of the reason for such inability or Applicants' characterization of the audits they conducted in 2007 and 2008 as routine, the statute makes it clear that failure to comply with this obligation presumptively disqualifies a firm from conducting public company audits. Permitting continued public audits under such circumstances would upend the regulatory framework -- forcing investors and the markets to bear the risks associated with public audits conducted without the benefit of Board oversight.

Applicants do not claim that they were not conscious of their repeated failures to cooperate and comply with the Board's inspection requests -- the facts that made obvious the risk of harm to investors and the markets. Nor have they argued that they would have presented evidence demonstrating that they lacked consciousness of these facts when they were violating Rule 4006. As such, Applicants have identified no evidence that might have been presented at a hearing that could have created a genuine issue of fact material to our findings, based on undisputed contemporaneous record evidence, that Applicants' conduct was an extreme departure from the standard for inspections under Rule 4006 and that the risk to investors and the markets posed by such conduct was so obvious that Applicants must have been aware of it.[45] Accordingly, we agree that the Board was entitled to conclude that this conduct was reckless within the meaning of Section 105(c)(5) without conducting a hearing.

C. Revocation of Registration and Bar from Association are Appropriate Remedial Sanctions

Having determined that Gately's conduct was reckless, the Board was authorized to select from any of the sanctions enumerated in Section 105(c)(4), including revocation and bar, "as it determine[d] appropriate." We review the Board's sanctions determination, "having due regard for the public interest and the protection of investors,"[46] based on both "the nature of the violation and the mitigating factors presented in the record."[47] We are mindful of the responsibility to be

---

45 *See Sundstrand*, 553 F.2d at 1047 (a hearing regarding subjective mindset is unnecessary where it is undisputed that the violator acted with a consciousness of the facts that made it obvious that the violative conduct presented a risk of harming investors).

46 15 U.S.C. § 7217(c)(2)-(3).

47 *McCarthy v. SEC*, 406 F.3d 179, 190 (2d Cir. 2005); *see also Paz Sec., Inc. v. SEC*, 494 F.3d 1059, 1065-66 (D.C. Cir. 2007) (stating that Commission review of sanctions under Section 19(e)(2) of the Exchange Act requires an inquiry into whether the sanctions serve a remedial purpose); *Assoc. Sec. Corp. v. SEC*, 283 F.2d 773, 775 (1960) (10th Cir. 1960) ("Exclusion from the securities business is a remedial device for the protection of the public.").

"particularly careful to address potentially mitigating factors"[48] and the "remedial and protective efficacy" of sanctions involving expulsion of a firm or individual from the securities industry.[49]

Applicants urge remand or reversal of the sanctions imposed by the Board. They challenge the bar and permanent revocation as "unduly harsh and draconian" and argue that "to deny [Gately] the right to permanently practice in his ch[o]sen profession as a result of his [treatment] runs contrary to the public interest." Applicants further argue that the summary disposition improperly denied them the opportunity to present testimony in support of mitigation of the sanctions.

Mitigating factors are among the mix of facts and circumstances considered by the Board in the exercise of its discretion under Section 105(c)(4). However, these factors and Applicants' desire to continue to participate in public audits, must ultimately be evaluated in light of their past conduct, which reflects "too great a risk to the markets and investors to be permitted"[50] in a registered accountant that issues audit reports that are relied upon by the public.

Here, the Board considered and rejected Applicants' argument that Gately's Condition was mitigative. The Board found that "this argument misapprehends the threat to the system of Board oversight posed by noncooperation with PCAOB inspections." The Board also rejected Applicants' attempts to downplay the seriousness of the violation, noting that the inspections "are fundamental to the Board's . . . protecti[ion] of the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports." The Board also noted that "the absence of fraud or deceit does not . . . diminish the seriousness of Respondents' failure to cooperate in an inspection designed, among other things, to uncover any such misconduct," and cited "Congress['s] recogni[tion] that cooperation with the Board by registered public accounting firms and their associated persons was critical to the system of oversight it put in place" in Sarbanes-Oxley.

We find that Applicants have failed to demonstrate a genuine issue of material fact. Applicants argue that they were inappropriately denied the opportunity to present further testimony regarding "the devastating effect [Gately's Condition] had on [his] ability to perform," and supporting their claims that Gately "intend[ed] to cooperate with the PCAOB to the extent

---

48 *Paz*, 494 F.3d at 1065 (citing *Steadman v. SEC*, 603 F.2d 1126, 1137-40 (5th Cir. 1979)).

49 *McCarthy v. SEC*, 406 F.3d at 190; *but see Paz v. SEC*, 566 F.3d 1172, 1176 (D.C. Cir. 2009) (stating that the remedial analysis regarding a bar from association with any SRO member firm does not require the Commission to "state why a lesser sanction would be insufficient").

50 *Paz Sec., Inc.*, Exchange Act Rel. No. 57656 (Apr. 11, 2008), 93 SEC Docket 5122, 5127.

possible under the circumstances" or "to the best of his ability." However, Gately has not identified any specific additional evidence that he might have adduced in support of these assertions warranting further development at a hearing.[51]

Applicants' claims regarding their purported intention to cooperate with the inspection process are not mitigating. We note that some of Inspections' requests covered routine information about, for example, Firm partners, affiliates, and litigation. Even viewing the record most favorably to Applicants, we cannot credit Applicants' assertions that they intended to cooperate given their longstanding failure to provide even the most routine information. We believe the Board evaluated Applicants' claims in accordance with the standard for summary disposition and properly concluded that "there is an absence of evidence to support [Applicants'] claim that Gately was so incapacitated as to be unable to cooperate with the inspection of Gately LLC," especially given the fact that the Firm continued to issue audit reports for public companies during this same period of time.

In fact, despite Inspections' diligent efforts to accommodate Gately's personal circumstances, as the Board observed, Applicants "have offered no representation or evidence that they made any efforts to comply with Inspections' requests between January 3, 2008 and well after the date this proceeding was instituted." If Gately intended to comply with the inspection and later became capable of such compliance, the record should reflect good faith attempts to remedy the past failures to cooperate. Gately does not point to evidence indicating that he did so.

Applicants' other attempts to downplay the seriousness of their conduct are similarly unavailing. They note that their conduct did not involve fraud or deceit. As the Board observed, however, "[t]he absence of fraud or deceit does not . . . diminish the seriousness of [Applicants']

---

[51] Applicants also point to two SRO disciplinary cases in which efforts at rehabilitation were considered in mitigation, to argue that Gately's Condition, treatment, and other limitations on his access to his records should mitigate the sanction. *Lawrence R. Klein,* 52 S.E.C. 535 (1995); *Robin Earl Hayden*, 1988 WL 858046 (Board of Governors NASD Regulation, Inc. Apr. 28, 1998). Both *Klein* and *Hayden* involved isolated, one-time violations, whereas Applicants' violative conduct involved a failure to meet multiple deadlines over a period of months. In analogous circumstances, we have declined to hold personal circumstances mitigating when such delays continue over a protracted period of time despite reasonable efforts to accommodate such circumstances. *See, e.g., Toni Valentino*, 57 S.E.C. 330, 337, 339 n.12, 340 (2004) (affirming bar for failure to appear for SRO interviews "after numerous [scheduling] attempts" when applicant "engaged in dilatory tactics to evade questioning," and noting that SRO "members and associated persons may not impose conditions . . . under which they will respond to [SRO] requests for information").

failure to cooperate in an inspection designed, among other things, to uncover any such misconduct."[52]

Nor is the seriousness of the violation diminished by their eventual submission of an IIF to Inspections in August 2008 -- months after the institution of proceedings and the Final 2007 Deadline. In the context of SRO requests for information, we have long held that the institution of disciplinary proceedings should not be required in order to compel compliance with such requests,[53] and we think the same principles should apply to PCAOB Rule 4006 requests. Moreover, Applicants do not claim that they ever produced any of the information required by the Data Request Form or the records for the Selected Engagements. Given the protracted nature of the violation and Gately's continued issuance of public audit reports while the original 2007 inspection requests remained outstanding, Applicants offer no assurance that the underlying cause of such delays has been remedied or that this pattern will not be repeated in connection with future inspections mandated under Sarbanes-Oxley.[54]

---

[52] *Cf. Paz,* 93 SEC Docket at 5131 ("[A] request for information is no less serious because NASD issues the request in an effort to prevent or uncover misconduct rather than to unearth the details of misconduct of which it is already aware."). Although Applicants argue that the bar and revocation are disproportionate in comparison to a settled case in which the Board imposed lesser sanctions for violations Applicants characterize as more serious, the appropriate sanctions in any case depend on the particular facts and circumstances presented rather than on a comparison with other cases involving different circumstances. *See Butz v. Glover Livestock Comm'n Co.*, 411 U.S. 182, 187 (1973); *see also McCarthy*, 406 F.3d at 188; *Hiller v. SEC*, 429 F.2d 856, 858 (2d Cir. 1970). We have previously pointed out, moreover, that comparisons to sanctions in settled cases are particularly inappropriate because "pragmatic factors may result in lesser sanctions" in settlements. *Anthony A. Addonino*, 56 S.E.C. 1273, 1295 (2003); *cf. Dennis Todd Lloyd Gordon*, Exchange Act Rel. No. 57655 (Apr. 11, 2008), 93 SEC Docket 5089, 5118 ("[I]t is well established that those who offer to settle may properly receive lesser sanctions than they otherwise might have based on 'pragmatic considerations such as the avoidance of time-and-manpower-consuming adversary proceedings.'").

[53] *Cf., e.g., CMG Institutional Trading, LLC*, Exchange Act Rel. No. 59325 (Jan. 30, 2009), 95 SEC Docket 13802, 13810 ("[W]e have emphasized repeatedly that NASD should not have to initiate a disciplinary action to elicit a response to its information requests . . . ."). Applicants focus on the Hearing Officer's expressed willingness to consider whether subsequent submission of requested information or files could serve as a mitigating factor. The record suggests, however, that Applicants did not submit evidence of any late submission to the Hearing Officer before he issued the summary disposition order. *See supra* note 10.

[54] We note that a different record might yield a different conclusion concerning the need for a hearing to evaluate a defense based on a condition such as Gately's. *Cf. Frank P. Quattrone*, Exchange Act Rel. No. 53547 (Mar. 24, 2006), 87 SEC Docket 2155, 2166 (setting

(continued...)

Applicants also attempt to shift blame for their own violative conduct to the Board. For instance, Applicants attempt to explain their failure to produce any audit records by claiming that Inspections' letters called for complete cooperation and did not notify them that partial compliance might mitigate sanctions in a future disciplinary action. However, Applicants cite nothing to support their premise that Inspections had any obligation to provide such notification, and we have long held that regulated persons cannot avoid responsibility for their own violative conduct by blaming the Commission or other regulators.[55] Their defense is particularly unconvincing in light of Applicants' failures to respond meaningfully to Inspections' other repeated attempts to accommodate Gately's circumstances, including when Inspections postponed deadlines, offered opportunities to withdraw registration, warned Applicants that missed deadlines could result in disciplinary action, and even encouraged Gately to comply after the Final 2007 Deadline had passed.[56] Applicants also claim that the disciplinary sanctions imposed in this case were motivated by a desire to target Gately for the Condition, but do not substantiate this claim, and we find no support for it in the record.

Applicants' continuing failure to acknowledge their responsibility for the 2007 inspection requests weighs heavily against permitting them to participate in future public audits. As the Board observed, any such participation would necessarily involve periodic inspections required under Sarbanes-Oxley, providing Applicants with opportunities for similar violations. Moreover, given the risk to markets and investors ultimately posed by Applicants' conduct,[57] we do not find

---

[54] (...continued)
aside NASD action when "NASD improperly granted summary disposition on" the issue of liability). Here, however, the facts already in this record concerning Gately's misconduct and the risk of harm to investors overwhelmingly support the appropriately remedial nature of the revocation and bar.

[55] *Cf. Perpetual Sec., Inc.*, Exchange Act Rel. No. 56613 (Oct. 4, 2007), 91 SEC Docket 2489, 2501 ("Applicants cannot blame NASD or their counsel for their failure to comply with the Suspension Order."); *Quest Capital Strategies*, 55 S.E.C. 362, 377-78 (2001) ("We have repeatedly pointed out that a broker-dealer cannot shift its responsibility for compliance with applicable requirements to the NASD or to [the Commission].").

[56] Applicants also suggest that a new inspection initiated in 2008 somehow was an "attempt to prevent Gately from mitigating possible sanctions" in connection with the 2007 requests, but do not explain the purport of this argument.

[57] *Cf. Paz*, 93 SEC Docket at 5131-32 (affirming bar of former president of NASD member firm from association with any NASD member in any capacity for failure to provide information requested by NASD), *petition denied*, 566 F.3d 1172 (D.C. Cir. 2009).

that the sanction must accommodate "some structured mechanism for . . . re-entry into the field of public accounting" as Applicants claim.[58]

Given the nature and pattern of violative conduct reflected in this case, the revocation of registration and bar imposed by the Board are appropriate to protect the public interest in securing regulatory oversight over the activities of registered accounting firms. We further find that Gately's state of mind and other claims do not justify mitigation, and that, in light of other record evidence, these claims did not present a genuine issue of material fact precluding summary disposition of the sanctions.

For these reasons, we sustain the Board's findings of violation and imposition of sanctions. An appropriate order will issue.[59]

By the Commission (Chairman SCHAPIRO and Commissioners CASEY, WALTER and PAREDES); Commissioner AGUILAR not participating.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

---

[58] *Cf. Paz*, 566 F.3d at 1176, *supra* note 49.

[59] We have considered all of the parties' contentions. We have rejected or sustained them to the extent that they are inconsistent or in accord with the views expressed in this opinion.

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Rel. No. 62656 / August 5, 2010

Admin. Proc. File No. 3-13535

In the Matter of the Application of

GATELY & ASSOCIATES, LLC
and
JAMES P. GATELY, CPA

c/o Roddy B. Lanigan, Esq.
Lanigan & Lanigan, PL
222 S. Pennsylvania Ave., #101
Winter Park, FL 32789

For Review of Disciplinary Action by
PCAOB

ORDER SUSTAINING DISCIPLINARY ACTION

On the basis of the Commission's opinion issued this day, it is

ORDERED that the disciplinary actions taken by PCAOB against Gately & Associates, LLC, and James P. Gately, CPA, be, and they hereby are, sustained.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E. Harmon

By: Florence E. Harmon
Deputy Secretary

Chairman Schapiro not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3065 / August 5, 2010

INVESTMENT COMPANY ACT OF 1940
Release No. 29377 / August 5, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-11590

In the Matter of **JANUS CAPITAL MANAGEMENT LLC** **Respondent.**	**ORDER MODIFYING ORDER INSTITUTING ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 203(e) AND 203(k) OF THE INVESTMENT ADVISERS ACT OF 1940 AND SECTIONS 9(b) AND 9(f) OF THE INVESTMENT COMPANY ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

On August 18, 2004, the Securities and Exchange Commission ("Commission") instituted administrative and cease-and-desist proceedings pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 ("Advisers Act") and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act"), making findings, and imposing remedial sanctions and a cease-and-desist order (the "2004 Order") against Janus Capital Management LLC ("JCM").[1]

II.

In anticipation of the proceedings, JCM consented to the entry of the 2004 Order. Among other things, the 2004 Order required JCM to cease and desist from further violations of the federal securities laws, directed JCM to pay disgorgement and civil money penalties, and directed JCM to comply with various undertakings.

1 See Advisers Act Rel. No. IA-2277, August 18, 2004, Admin. Proc. File No. 3-11590.

III.

JCM has submitted an Amended Offer of Settlement (the "Offer") proposing to relieve it of the obligations to continue to: (1) undertake a periodic compliance review in accordance with paragraph 32 of the 2004 Order; (2) establish and maintain an Internal Compliance Controls Committee in accordance with paragraph 30(b) of the 2004 Order; and (3) hold a shareholder's meeting at which the Board of Trustees for each registered investment company is elected not less than every fifth calendar year in accordance with paragraph 28(c) of the 2004 Order. Solely for purposes of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, JCM consents to the entry of this Order Modifying Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940 and Sections 9(b) and 9(f) of the Investment Company Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

IV.

The Commission deems it appropriate and in the public interest to amend the 2004 Order as agreed to in JCM's Offer.

Accordingly, IT IS HEREBY ORDERED that:

A. Paragraph 32 of the 2004 Order is amended as follows to order:

> 32. *Periodic Compliance Review.* Commencing in 2006, and at least once every other year thereafter through at least 2009, JCM shall undergo a compliance review by a third party, who is not an interested person, as defined in the Investment Company Act, of JCM. At the conclusion of the review, the third party shall issue a report of its findings and recommendations concerning JCM's supervisory, compliance, and other policies and procedures designed to prevent and detect breaches of fiduciary duty, breaches of the Code of Ethics and federal securities law violations by JCM and its employees in connection with their duties and activities on behalf of and related to the Janus funds. Each such report shall be promptly delivered to JCM's Internal Compliance Controls Committee and to the Legal and Regulatory Committee of the Board of Trustees of each Janus fund.

B. Paragraph 30(b) of the 2004 Order is amended as follows to order:

> b. Until at least June 1, 2010, JCM shall establish an Internal Compliance Controls Committee to be chaired by JCM's Chief Compliance Officer, which Committee shall have as its members senior managers of JCM's business units. Notice of all meetings of the Internal Compliance Controls Committee shall be given to the independent Trustees of the Janus funds, who shall be invited to

attend and participate in such meetings. The Internal Compliance Controls Committee shall review compliance issues throughout the business of JCM, endeavor to develop solutions to those issues as they may arise from time to time, and oversee implementation of those solutions. The Internal Compliance Controls Committee shall provide reports on internal compliance matters to the Legal and Regulatory Committee of the Trustees of the Janus funds with such frequency as the independent Trustees of such funds may instruct, and in any event at least quarterly. JCM shall also provide to the Audit Committee of JCG the same reports of the Code of Ethics Oversight Committee and the Internal Compliance Controls Committee that it provides to the Legal and Regulatory Committee of the Janus funds.

C. Paragraph 28(c) of the 2004 Order is amended as follows to order:

c. Commencing in 2005 and not less than every fifth calendar year thereafter through at least 2010, each Janus fund will hold a meeting of shareholders at which the Board of Trustees will be elected.

D. All other provisions of the 2004 Order remain in effect.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62666 / August 9, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3171 / August 9, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13997

In the Matter of

DOHAN + COMPANY CPAs,
STEVEN H. DOHAN, CPA,
NANCY L. BROWN, CPA, and
EREZ BAHAR, CA,

Respondents.

ORDER INSTITUTING PUBLIC ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 4C OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative proceedings be, and hereby are, instituted against Dohan + Company CPAs ("Dohan + Co."), Steven H. Dohan, CPA ("Dohan"), Nancy L. Brown, CPA ("Brown"), and Erez Bahar, CA ("Bahar") (collectively, "Respondents") pursuant to Section 4C[1] of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 102(e)(1)(ii) of the Commission's Rules of Practice to determine whether Respondents engaged in improper professional conduct.[2]

---

[1] Section 4C provides, in relevant part, that: "The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others . . . (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations thereunder."

[2] Rule 102(e)(1)(ii) provides, in pertinent part, that: "The Commission may . . . deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . . to have engaged in unethical or improper professional conduct."

II.

After an investigation, the Division of Enforcement and the Office of the Chief Accountant allege that:

A. SUMMARY

1. These proceedings arise out of Respondents' improper professional conduct during their audit of International Commercial Television, Inc.'s ("ICTV") 2007 financial statements. During fiscal year 2007, ICTV improperly recognized revenue and incorrectly recorded product returns, resulting in a material overstatement of revenue and net income. Respondents' audit of ICTV's 2007 financial statements recklessly failed to comply with numerous Public Company Accounting Oversight Board ("PCAOB") auditing standards. These included failing to demonstrate the required level of proficiency, failing to exercise due care and professional skepticism, failing to obtain sufficient evidential matter, and failing to plan and supervise the audit staff. As a result, Respondents Dohan, Brown, and Bahar caused Respondent Dohan + Co. to issue an unqualified audit report for ICTV's 2007 Form 10-K/SB that falsely stated that the audit had been conducted in accordance with the PCAOB's auditing standards and that ICTV's financial statements were fairly reported in conformity with Generally Accepted Accounting Principles ("GAAP"). Respondents' conduct, as further described below, constituted improper professional conduct within the meaning of Rule 102(e)(1)(ii) and (iv) and Section 4C of the Exchange Act.

B. RESPONDENTS

2. **Dohan + Company CPAs** is an accounting and auditing firm based in Miami, Florida. The firm provides services to public companies registered with the Commission and has been registered with the PCAOB since October 2003. The firm conducted audits of ICTV's financial statements for the years ended 2004, 2005, 2006, and 2007. As auditor, Dohan + Co. opined that ICTV's financial statements were prepared in conformity with GAAP and that Dohan + Co. had conducted audits in accordance with the PCAOB's standards.

3. **Steven H. Dohan**, CPA, age 62, is a resident of Miami, Florida. Dohan is the founder and managing director of Dohan + Co. and was the concurring partner on the ICTV audits and quarterly reviews during the relevant period. Dohan is a Certified Public Accountant licensed in Florida.

4. **Nancy L. Brown**, CPA, age 58, is a resident of Miami, Florida. Until recently, Brown was a director at Dohan + Co. and was the engagement partner on the ICTV audits and quarterly reviews during the relevant period. Brown is a Certified Public Accountant licensed in Florida.

5. **Erez Bahar**, CA, age 32, is a resident of Vancouver, Canada. Bahar is a principal at Davidson & Company, LLP ("Davidson") and was the manager on the field work performed by Davidson on the ICTV audits and quarterly reviews during the relevant period. Bahar holds an active Chartered Accountant designation issued in 2004 in British Columbia, Canada.

C. RELATED PARTIES

6. **International Commercial Television, Inc.** is a Nevada corporation headquartered in Bainbridge Island, Washington. Founded in 2001, the Company sells health and beauty products internationally via infomercials and through various televised shopping networks. ICTV's common stock is registered under Section 12(g) of the Exchange Act and is quoted on the Pink Sheets under the symbol "ICTL."

7. **Davidson & Company, LLP** is an accounting and auditing firm based in Vancouver, Canada. Davidson performed the field work for Dohan + Co. on the ICTV audits and quarterly reviews during the relevant period. The firm has been registered with the PCAOB since December 2003.

D. FACTS

ICTV's Improper Revenue Recognition

8. ICTV is a marketer of consumer retail goods, specializing in "fountain of youth" health and beauty products it owns or holds the right to sell. ICTV's best-selling product is the Derma Wand, a skin care appliance that purportedly "reduces fine lines and wrinkles and improves overall skin appearance."

9. ICTV sells product through two main channels: (1) direct sales to end users via infomercials produced by ICTV ("direct sales"), and (2) distribution through third-party distributors for sell-through to end users. ICTV's distributors include televised shopping networks such as the Home Shopping Network ("HSN").

10. Over a six-quarter period from early 2007 and continuing into 2008, ICTV improperly recognized revenue on sales through HSN. In addition, ICTV failed to properly record revenue, and estimate and account for returns, for product sold through its direct sales channels.

11. ICTV began selling product through HSN in 2007, predominantly through a "drop-ship" contract entered into between ICTV and HSN in or about May 2007. Under the drop-ship contract, HSN did not purchase the product itself, but instead facilitated sales to HSN's customers (*i.e.*, the end users). Generally, HSN sent ICTV written requests to pre-order product that would be sold during future HSN television broadcasts. ICTV retained title to the product until HSN sold the product on-air to its customers and the product was shipped to the end users. HSN did not guarantee the purchase of any product, and any unsold product remained under the ownership of ICTV. The contract also allowed HSN to return any product from its customers up to 60 days after delivery to the customer.[3]

[3] ICTV also sold product directly to HSN under the terms of a separate, "traditional" contract, in which HSN issued a purchase order, retrieved the product, sold the product to end users, and paid ICTV after the sell-through. However, only the first HSN sale was made per the terms of the traditional contract. All other sales were made per the drop-ship arrangement.

12. Despite these contractual provisions governing sell-through and right of return, ICTV recognized revenue in most cases upon HSN's order of the product, before HSN sold through to its customers and before the right of return expired. In some instances, ICTV also recognized revenue without a corresponding written request from HSN. In those cases, ICTV booked HSN sales upon alleged confirmation from its third-party fulfillment warehouse that product had been physically segregated for HSN's use.

13. ICTV failed to ensure that HSN sold through the units booked by the end of the quarter, resulting in a mounting accounts receivable balance with each successive HSN order. This accounting treatment violated multiple revenue recognition criteria under Generally Accepted Accounting Principles ("GAAP").

14. In addition to prematurely recognizing revenue on sales through HSN, ICTV also booked revenue in 2007 on a product that failed an HSN quality control inspection and was never sold through HSN. The purported sale remained on ICTV's books through the 2007 audit and was not reversed until ICTV issued a restated Form 10-K/SB in March 2009.

15. In total, ICTV booked seven HSN sales in 2007 totaling $2.8 million. This figure was reported in ICTV's trial balance and ultimately reported by ICTV in its 2007 Form 10-K. Respondents' working papers allege that the auditors tested the HSN sales and traced certain of the sales to ICTV's sales journal, which in turn showed the amount that ICTV booked as revenue. A list of each HSN sale recognized for 2007 is attached hereto as Appendix A.

16. Each HSN sale set forth in Appendix A was improperly recognized, resulting in a material overstatement of revenue for ICTV's fiscal 2007.

17. ICTV also failed to properly record revenue on its direct sales. ICTV provided its direct sales customers a 30-day free trial period whereby the customer could try the ordered product prior to purchase, and billed customers upon expiration of the 30-day period. Despite this provision, ICTV recognized revenue upon shipment of the product, and before expiration of the trial period, in violation of GAAP. ICTV also failed to properly estimate and record product returns on direct sales.

18. Over the course of the six-quarter period, ICTV filed periodic reports with the Commission on Forms 10-Q and 10-K. As a result of the improper accounting discussed above, ICTV reported materially inflated revenue and net income to investors and to the Commission. Investors determining whether to buy or sell ICTV stock were thus basing their decisions on false information about ICTV's financial performance.

ICTV's Restatement

19. In October 2008, ICTV announced that it intended to restate its financial statements for the fiscal year ended 2007 and the first two quarters of 2008 as a result of improper revenue recognition. ICTV filed its restated Form 10-K/A for fiscal year 2007 on March 31, 2009. The restatement resulted in a $1.4 million reduction in 2007 revenue related to the HSN errors, and an $840,000 reduction in 2007 revenue related to the failure to properly record direct sales returns.

20. In March 2010, ICTV's new outside auditors uncovered additional revenue recognition errors and ICTV reported that it intended to restate its previously-restated financial statements for the fiscal year ended 2007 and the first two quarters of 2008. In April 2010, ICTV again restated its financial statements for the fiscal year ended 2007. The restatement included an additional $550,000 revenue reduction related to the premature recognition of direct sales revenue prior to expiration of a free trial period.

21. The chart below shows that the errors were material to ICTV's financial statements:

Period	Previously Reported Net Income	Restated Net Income (Loss)	Reduction to Reported Net Income
FY 2007	$1,475,775	($1,081,988)	($2,557,763)
1Q 2008	$109,980	($164,773)	($274,753)
2Q 2008	$260,298	($862,399)	($1,122,697)

<u>Applicable Revenue Recognition Principles and Guidance</u>

22. The basic principles of revenue recognition under GAAP provide that revenue must be realized or realizable and earned before it can be recognized. SEC Staff Accounting Bulletin ("SAB") No. 101, *Revenue Recognition in Financial Statements* (as superseded in part by SAB No. 104, *Revenue Recognition*), reflects these basic principles of revenue recognition and provides guidance in the application of GAAP with respect to recognizing revenue. SAB 101 sets forth four criteria that must be considered when determining whether revenue has been realized or realizable and earned. Specifically, revenue generally may be recognized when persuasive evidence of an arrangement exists, delivery has occurred, the seller's price is fixed or determinable, and collectibility is reasonably assured.

23. GAAP also provides that, when a right of return exists, revenue can be recognized at the time of sale only if all of the following conditions are met: (1) the seller's price is substantially fixed or determinable at the date of sale; (2) the buyer has paid, or the buyer is obligated to pay and the obligation is not contingent on resale of the product; (3) the buyer's obligation would not be changed in the event of theft, physical destruction, or damage of the product; (4) the buyer acquiring the product for resale has economic substance apart from that provided by the seller; (5) the seller does not have significant obligations for future performance to directly bring about resale of the product by the buyer; and (6) the amount of future returns can be reasonably estimated. Statement of Financial Accounting Standards No. 48, *Revenue Recognition When Right of Return Exists*.

<u>Respondents' Deficient 2007 Audit</u>

<u>Background</u>

24. Dohan + Co. issued the audit report filed with ICTV's 2007 financial statements and reviewed ICTV's quarterly statements during 2007 through the second quarter of 2008.

25. Dohan + Co. contracted with Davidson to provide an audit manager and senior accountant to perform the field work at ICTV. Dohan + Co. and Davidson had worked together in a similar arrangement on several other engagements. Under PCAOB auditing standards, the staff sharing arrangement between Dohan + Co. and Davidson was subject to the supervision rules and responsibilities set forth in AICPA Codification of Statements on Auditing Standards (as adopted and amended by the PCAOB) ("AU") § 311, *Planning and Supervision.*

26. Dohan + Co. reviewed the Davidson working papers and satisfied itself with both the quality and the amount of work performed by Davidson. The firm also made the decision to adopt the Davidson working papers, with little modification, and performed few additional substantive procedures.

27. The audit team for the 2007 ICTV audit primarily consisted of Brown, the engagement partner; Dohan, the concurring partner; Bahar, the audit manager; and a senior accountant who conducted all substantive audit procedures and field work (the "Senior Accountant"). The Senior Accountant conducted the onsite work for the audit over a two-to-three day period in March 2008. Bahar's responsibilities included planning the audit, supervising the onsite work and reviewing any work performed by the Senior Accountant. Brown's responsibilities included the overall planning and supervision of the audit. Dohan's responsibilities included providing an objective review of the audit and the financial statements that were the subject of the report.

The Auditors' Working Papers

28. On their face, the year-end 2007 audit working papers reveal that Respondents knew of an agreement between ICTV and HSN that claimed to contribute to a 280% increase in revenue over fiscal year-end 2006. The revenue lead sheet stated:

> The Company is also now using the Home Shopping Network for sales in the US market. HSN buys product from the Company (DermaWand and CellRX so far) and features the product on various shows. The Company records the sales once HSN has placed the order and the order has been shipped. HSN does not pay until they have sold the products. This process sometimes takes a few months as HSN will pre-order for future shows.

29. A similar notation appeared on the accounts receivable lead sheet:

> HSN buys a certain amount of product from the Company prior to showing the infomercials. The Company records the sale at this time. HSN pays the Company once the product has actually been sold.

30. The year-end 2007 audit working papers also documented that the HSN relationship was a new and material development in ICTV's business. An analytical review worksheet highlighted a 280% increase in ICTV's annual sales revenue, from \$3 million in 2006 to \$11.3 million in 2007 due to "an agreement with the Home Shopping Network during the year to sell the Company's product." The worksheet also reported a 414% increase to accounts receivable, from \$555,000 in 2006 to \$2.9 million in 2007, as a result of increased sales. The material increase in ICTV's revenue, ICTV's new relationship with HSN, the contingent payment terms associated

with that relationship, and Respondents' knowledge of ICTV's deficient internal controls, among other factors, required Respondents to apply heightened scrutiny to the ICTV audit.

Audit Failures by Bahar, Brown, Dohan, and Dohan + Co.

31. Bahar and Brown both reviewed and signed off on the working papers. Dohan, before signing off on the audit, reviewed the majority of the working papers, including the revenue, accounts receivable, and analytical review working papers. Thus, Bahar, Brown, Dohan, and Dohan + Co. each knew of certain terms of ICTV's arrangement with HSN, including that HSN did not pay ICTV until it sold the product to end users. This should have alerted Respondents that ICTV's revenue recognition practices did not comply with GAAP.

32. Indeed, Dohan understood at the time of the audit that the sell-through of ICTV's product by HSN presented a revenue recognition issue under SAB 101, but failed to research the issue at the time of his review nor direct any other member of the audit team to research the issue.

33. Despite knowledge of the above, Respondents recklessly, highly unreasonably, and/or unreasonably failed to properly audit ICTV's revenue recognition practices. For example, Bahar, Brown, Dohan, and Dohan + Co. failed to obtain a copy of the applicable agreement between ICTV and HSN. Bahar knew that ICTV had a "business arrangement" with HSN to sell product, and was aware that the working papers stated that ICTV entered into an "agreement" with HSN. Brown knew that there was an agreement between ICTV and HSN to sell ICTV's product. Dohan knew that ICTV's revenue and accounts receivable had increased "dramatically" in 2007 as a result of an agreement entered into with HSN. Yet, Bahar, Brown, Dohan, and Dohan + Co. each failed to inquire as to the existence of any written agreement and failed to obtain a copy of any written agreement. Respondents' failure to inquire about the terms of the applicable ICTV agreement with HSN, to obtain a copy of the agreement, or to adequately understand the nature of ICTV's relationship with HSN was an extreme departure from professional standards. Because of these failures, Bahar, Brown, Dohan, and Dohan + Co. failed to recognize that under the HSN drop-ship agreement, no sale occurred, and revenue should not have been recognized, until the product was sold to end users.

34. Respondents also failed to issue audit confirmations to confirm ICTV's accounts receivable and inventory, or perform adequate alternative procedures. Bahar, Brown, Dohan, and Dohan + Co. knew that their own audit program called for the confirmations of receivables and inventory. Had confirmations been sent and received by the auditors, Respondents could have learned that the sales and inventory levels reported by ICTV were not supported.

35. Bahar, Brown, and Dohan + Co. also neglected to perform other audit procedures dictated by the audit program. For example, the audit program required the auditors to review and attend physical inventory counts. This step was marked "NA" in the working papers, indicating that it was not performed. The audit program also recommended that the auditors consider extended procedures to confirm sales terms and conditions with customers; this step was marked "NA" as well. Dohan knew that these procedures were not performed.

36. The working papers also contain a number of internal inconsistencies that should have been resolved by Respondents. For instance, although the revenue and accounts receivable lead sheets described how HSN did not pay ICTV until sell-through, which sometimes took "a few months," the working papers elsewhere indicated that there were no "unusual or long payment terms" or "buyer conditions which must be met in order to complete the sale." In addition, the revenue working papers reported that cash had been received for a $990,000 sale to HSN on December 21, 2007, while the accounts receivable working papers reported the $990,000 balance as still outstanding. Bahar, Brown, Dohan, and Dohan + Co. failed to reconcile any of these inconsistencies during their review of the working papers.

37. Bahar, Brown, and Dohan + Co. also failed to properly audit ICTV's stated revenue and returns for direct consumer sales. The working papers do not reflect that the audit team considered ICTV's revenue recognition practices for such sales in light of the 30-day free trial period extended to direct sales customers. The working papers also do not show that the auditors performed any substantive testing of ICTV's stated returns for direct sales, or that the auditors considered the impact of applicable GAAP guidance on estimating future returns for such sales. The auditors also failed to reconcile an inherent inconsistency between ICTV's stated returns and its disclosed historical return rate for direct consumer sales.

The Auditors Issue Unqualified Audit Reports on ICTV's 2007 Financial Statements Despite Numerous Audit Failures

38. Despite these failures, Bahar, Brown, and Dohan caused Dohan + Co. to issue an unqualified audit report on ICTV's 2007 financial statements, which falsely represented that the audit had been conducted in accordance with the PCAOB's auditing standards and that ICTV's financial statements were fairly reported in conformity with GAAP. The audit completion documents, which included a checklist and the auditors' assessment that the audit was complete, reflect that Bahar, Brown, and Dohan were each satisfied with the work performed and signed off on the release of the audit report.

39. Respondents also conducted the audit and review work on ICTV's restatement for the fiscal year ended 2007 and the first two quarters of 2008. In March 2009, Dohan + Co. issued an unqualified audit report on ICTV's restated 2007 financial statements. The restatement working papers indicate that Bahar, Brown, and Dohan each reviewed the restated financial statements and signed off on the release of the audit report.

40. In September 2009, ICTV retained new auditors. The new auditors found additional revenue recognition errors and brought them to ICTV's attention. Based upon this information, ICTV concluded that the restated 2007 financial statements needed to be restated. This additional restatement and information arising in connection with PCAOB inquiries further call into question Dohan + Co.'s competence under applicable PCAOB standards.

Respondents' Improper Professional Conduct

41. The "applicable professional standards" for accountants practicing before the Commission include the PCAOB auditing standards.

42. PCAOB auditing standards require that the auditor be proficient in accounting matters and that the "auditor with final responsibility for the engagement should know, at a minimum, the relevant professional accounting and auditing standards and should be knowledgeable about the client." AU § 230.06, *Due Professional Care in the Performance of Work*; *see also* AU § 210, *Training and Proficiency of the Auditor*. AU Section 230 also requires an auditor to exercise due professional care and professional skepticism, which includes demonstrating a questioning mind and a critical assessment of audit evidence.

43. PCAOB auditing standards require that "competent evidential matter . . . be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit." AU § 326.01, *Evidential Matter*. This "includes both written and electronic information such as . . . contracts." AU § 326.17. The auditor is also to send out audit confirmations. AU § 330, *The Confirmation Process*.

44. Auditors must adequately plan, staff, and supervise the audit. *See* AU §§ 150.02, *Generally Accepted Auditing Standards*; 210.01; 230.06; 311.01 *et seq.*, *Planning and Supervision*; 311.11 *et seq.* This includes "obtain[ing] a level of knowledge of the entity's business that will enable" the auditor to understand transactions and practices that may have a significant effect on the financial statements. AU § 311.06.

45. Further, AU § 316, *Consideration of Fraud in a Financial Statement Audit*, requires the auditor to assess the risks of material misstatement due to fraud and to presume that revenue recognition is a fraud risk.

46. As audit manager, Bahar was responsible for supervising and reviewing documentation of field work performed. As the engagement partner, Brown had overall responsibility for the engagement to ensure that Dohan + Co.'s audit of ICTV's 2007 financial statements was conducted in accordance with PCAOB auditing standards, including planning and supervising the audit and the review of field work. Dohan, as the concurring partner, knew that his role was to "give a fresh, clean look at a job, to provide a fresh set of eyes on the engagement, and to assist where necessary in making sure the engagement goes out to the best of the firm's ability."

47. Indeed, Dohan and Brown were already on notice that the PCAOB had identified material audit deficiencies with respect to many of the auditing standards discussed above, per an inspection of Dohan + Co. by the PCAOB prior to Respondents' 2007 ICTV audit. As a result of that inspection, Dohan and Brown learned that the PCAOB found a number of deficiencies regarding the firm's audits of other clients, including the failure to adequately test revenue and to obtain sufficient evidential matter, as well as deficiencies in Dohan + Co.'s quality control procedures, including concurring partner reviews.

48. During the 2007 ICTV audit, Respondents recklessly, highly unreasonably, and/or unreasonably departed from the PCAOB auditing standards in numerous instances, including in the manner further described below.

49. Respondents failed to demonstrate the required level of proficiency. Brown and Bahar were not aware of applicable GAAP guidance that prohibit revenue recognition if payment

of the related sales receivable was dependent upon sell-through by the customer. Although Dohan was aware of some of the applicable GAAP guidance, and knew that ICTV's revenue recognition practices potentially violated GAAP, he failed to conduct additional research or direct another member of the audit team to follow up.

50. Respondents failed to obtain sufficient evidential matter. Bahar, Brown, Dohan, and Dohan + Co. failed to understand, or obtain a copy of, ICTV's written contract with HSN, despite the fact that each knew that ICTV had an "agreement" or "business arrangement" with HSN to sell ICTV's product. In addition, Bahar, Brown, and Dohan each reviewed the working papers that expressly stated that ICTV's revenue had materially increased in 2007 due to an "agreement" with HSN.

51. Respondents failed to exercise due professional care and skepticism in the face of numerous red flags and inconsistencies. Bahar, Brown, Dohan, and Dohan + Co. never asked ICTV for a copy of any HSN agreement or documentation of the terms of the agreement. Brown, Bahar, and Dohan + Co. ignored or disregarded specific audit program steps regarding, among others, long payment terms, buyer conditions in the sale of product, the confirmation of significant accounts receivable, and the observation of physical inventory counts. Dohan, during his review, either agreed that such procedures were not necessary or failed to identify his fellow auditors' disregard for these auditing steps. Bahar, Brown, Dohan, and Dohan + Co. also failed to reconcile numerous inconsistencies during their review of the working papers.

52. Respondents failed to send out accounts receivable confirmations as required by the audit program or to ensure adequate alternative procedures. Further, Brown, Bahar, and Dohan + Co. knew that the audit program also recommended that they send out sales terms and conditions and inventory confirmations but elected not to do so. Dohan supported these decisions despite his belief that ICTV's revenue recognition practice with respect to HSN presented an issue under SAB 101 and with the knowledge that the audit program recommended these confirmations be sent.

53. Respondents failed to adequately plan, staff and supervise the audit. Bahar failed to adequately supervise the Senior Accountant during the course of the audit. Bahar was never onsite with the Senior Accountant during the field work. Had he done so, he might have discovered inconsistencies contained within the working papers, including that his staff claimed to have vouched HSN sales to alleged purchase orders that stated, "This is not a purchase order!" Bahar also never asked the Senior Accountant to review certain applicable GAAP requirements governing revenue recognition in connection with the audit. Brown never visited ICTV or the Davidson office, and relied upon Bahar to manage all of the field work. Dohan failed to ensure that Brown and Bahar were adequately proficient to conduct the audit.

54. Brown, Bahar, and Dohan + Co. failed to sufficiently understand ICTV's business to enable them to understand transactions that had a significant effect on ICTV's financial statements. Brown, Bahar, and Dohan + Co. failed to identify the impact of ICTV's 30-day free trial period, or applicable GAAP standards prohibiting revenue recognition prior to customer acceptance where a trial or evaluation period exists. The working papers also do not reflect that Brown, Bahar, or Dohan + Co. performed any substantive testing of ICTV's stated returns for direct sales, or that they considered the impact of applicable GAAP guidance on estimating future

returns for such sales. The auditors also failed to reconcile an inherent inconsistency between ICTV's stated returns and its disclosed historical return rate for direct consumer sales.

55. Finally, Respondents also failed to consider other Standards of Field Work contained in AU Section 300, including AU Section 316, *Consideration of Fraud in a Financial Statement Audit*; AU Section 329, *Analytical Procedures*; and AU Section 331, *Inventories*.

E. VIOLATIONS

As a result of the conduct described above, Respondents engaged in improper professional conduct as defined in Section 4C of the Exchange Act and Rule 102(e)(1)(ii) and (iv), in that their conduct constituted (A) intentional or knowing conduct, including reckless conduct, that resulted in violation of applicable professional standards, or in the alternative, (B) negligent conduct, consisting of (1) a single instance of highly unreasonable conduct that resulted in a violation of applicable professional standards in circumstances in which Respondents knew, or should have known, that heightened scrutiny was warranted, or (2) repeated instances of unreasonable conduct by Respondents, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission.

III.

In view of the allegations made by the Division of Enforcement and the Office of the Chief Accountant, the Commission deems it necessary and appropriate that public administrative proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondents an opportunity to establish any defenses to such allegations; and

B. What, if any, remedial action is appropriate against Respondents pursuant to Rule 102(e) of the Commission's Rules of Practice, including, but not limited to, censure and/or denying, temporarily or permanently, the privilege of appearing or practicing before the Commission.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice [17 C.F.R. § 201.220].

If Respondents fail to file the directed Answer, or fail to appear at a hearing after being duly notified, the Respondents may be deemed in default and the proceedings may be determined against them upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served upon Respondents in accordance with the provisions of Rule 141 of the Commission's Rules of Practice [17 C.F.R. § 201.141].

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 300 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. §201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E Harmon
Deputy Secretary

Appendix A

Improperly Recognized 2007 HSN Sales By ICTV

DATE	AMOUNT	UNITS	PRODUCT
2/22/2007	$89,050.50	1,799	Derma Wand
6/12/2007	$198,049.50	4.001	Derma Wand
6/15/2007	$297,000.00	6,000	Derma Wand
9/30/2007	$1,028,362.50	20,775	Derma Wand
11/19/2007	$93,598.25	3,499	Cell RX
12/21/2007	$990,000.00	20,000	Derma Wand
12/26/2007	$200,574.00	4,052	Derma Wand
TOTAL	**$2,896,634.75**		

Appendix A

Improperly Recognized 2007 HSN Sales By ICTV

DATE	AMOUNT	UNITS	PRODUCT
2/22/2007	$89,050.50	1,799	Derma Wand
6/12/2007	$198,049.50	4.001	Derma Wand
6/15/2007	$297,000.00	6,000	Derma Wand
9/30/2007	$1,028,362.50	20,775	Derma Wand
11/19/2007	$93,598.25	3,499	Cell RX
12/21/2007	$990,000.00	20,000	Derma Wand
12/26/2007	$200,574.00	4,052	Derma Wand
TOTAL	**$2,896,634.75**		

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62674 / August 10, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13998

In the Matter of **Appiant Technologies, Inc.,** **Cobalis Corp.,** **FutureLink Corp.,** **STM Wireless, Inc.,** **Supermail International, Inc.** **(n/k/a PBHG, Inc.), and** **Women First Healthcare, Inc.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Appiant Technologies, Inc., Cobalis Corp., FutureLink Corp., STM Wireless, Inc., Supermail International, Inc. (n/k/a PBHG, Inc.), and Women First Healthcare, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Appiant Technologies, Inc. ("APPS") [1] (CIK No. 1025985) is a void Delaware corporation located in Pleasanton, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). APPS is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K for the period ended September 30, 2002, which reported a net loss of $15,321,000 for the prior year. As of August 5, 2010, the common stock of APPS was quoted on the Pink Sheets operated by

[1] The short form of each issuer's name is also its stock symbol.

Pink OTC Markets Inc. ("Pink Sheets"), had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. Cobalis Corp. ("CLSC") (CIK No. 1166414) is a Nevada corporation located in Laguna Beach, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). CLSC is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 2007, which reported a net loss of $695,116 for the prior nine months. On August 1, 2007, CLSC was the subject of an involuntary Chapter 7 petition in the U.S. Bankruptcy Court for the Central District of California, which was converted to Chapter 11, and was still pending as of August 5, 2010. As of August 5, 2010, the common stock of CLSC was quoted on the Pink Sheets, had thirteen market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

3. FutureLink Corp. ("FTRLQ") (CIK No. 1061399) is a void Delaware corporation located in Lake Forest, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). FTRLQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended March 31, 2001, which reported a net loss of $15,631,000 for the prior three months. On August 14, 2001, FTRLQ filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Southern District of New York, which was still pending as of August 5, 2010. As of August 5, 2010, the common stock of FTRLQ was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

4. STM Wireless, Inc. ("STMIQ") (CIK No. 765414) is a void Delaware corporation located in Irvine, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). STMIQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 30, 2002, which reported a net loss of $7,867,000 for the prior nine months. On February 20, 2003, STMIQ filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Central District of California, which was closed on June 22, 2010. As of August 5, 2010, the common stock of STMIQ was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

5. Supermail International, Inc. (n/k/a PBHG, Inc.) ("PBHN") (CIK No. 832508) is an expired Utah corporation located in Sacramento, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). PBHN is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-KSB for the period ended December 31, 1997, which reported a net loss of $2,090,740 for the prior year. Between November 2003 and July 2004, PBHN underwent several corporate and Pink Sheet name changes culminating in the adoption of its current name of PBHG, Inc. None of these changes were reported to the Commission on Form 8-K or recorded in the Commission's EDGAR database as required by Commission rules. As of August 5, 2010, the common stock of PBHN was quoted on the Pink Sheets, had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

6. Women First Healthcare, Inc. ("WFHCQ") (CIK No. 1081004) is a dissolved Delaware corporation located in San Diego, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). WFHCQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K for the period ended December 31, 2003, which reported a net loss of $73,340,000 for the prior year. On April 29, 2004, WFHCQ filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Delaware, which was terminated on December 18, 2008. As of August 5, 2010, the common stock of WFHCQ was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

B. DELINQUENT PERIODIC FILINGS

7. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission, have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

8. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports, and Rule 13a-13 requires issuers to file quarterly reports.

9. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II hereof are true and, in connection therewith, to afford the Respondents an opportunity to establish any defenses to such allegations; and,

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II hereof, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, or fail to appear at a hearing after being duly notified, the Respondents, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents, may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondents personally or by certified, registered, or Express Mail, or by other means permitted by the Commission Rules of Practice.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

August 10, 2010

In the Matter of **Appiant Technologies, Inc.,** **Cobalis Corp.,** **FutureLink Corp.,** **STM Wireless, Inc.,** **Supermail International, Inc.** **(n/k/a PBHG, Inc.), and** **Women First Healthcare, Inc.,** **File No. 500-1**

ORDER OF SUSPENSION OF TRADING

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Appiant Technologies, Inc. because it has not filed any periodic reports since the period ended September 30, 2002.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Cobalis Corp. because it has not filed any periodic reports since the period ended December 31, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of FutureLink Corp. because it has not filed any periodic reports since the period ended March 31, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of STM Wireless, Inc. because it has not filed any periodic reports since the period ended September 30, 2002.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Supermail International, Inc. (n/k/a PBHG, Inc.) because it has not filed any periodic reports since the period ended December 31, 1997.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Women First Healthcare, Inc. because it has not filed any periodic reports since the period ended December 31, 2003.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed companies. Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed companies is suspended for the period from 9:30 a.m. EDT on August 10, 2010, through 11:59 p.m. EDT on August 23, 2010.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

August 10, 2010

In the Matter of **Geotec, Inc.,** **InnoPet Brands Corp.,** **Marbledge Group, Inc.** **(n/k/a AR Growth Finance Corp.),** **Phlo Corp.,** **Pliant Systems, Inc.,** **Southeast Banking Corp.,** **TNX Television Holdings, Inc., and** **WestPoint Stevens, Inc.** **File No. 500-1**	**ORDER OF SUSPENSION OF TRADING**

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Geotec, Inc. because it has not filed any periodic reports since the period ended March 31, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of InnoPet Brands Corp. because it has not filed any periodic reports since the period ended March 31, 1998.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Marbledge Group, Inc. (n/k/a AR Growth Finance Corp.) because it has not filed any periodic reports since the period ended November 30, 1996.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Phlo Corp. because it has not filed any periodic reports since the period ended December 31, 2007.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Pliant Systems, Inc. because it has not filed any periodic reports since the period ended June 30, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Southeast Banking Corp. because it has not filed any periodic reports since the period ended June 30, 1991.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of TNX Television Holdings, Inc. because it has not filed any periodic reports since the period ended September 30, 2004.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of WestPoint Stevens, Inc. because it has not filed any periodic reports since the period ended September 30, 2004.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed companies. Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed companies is suspended for the period from 9:30 a.m. EDT on August 10, 2010, through 11:59 p.m. EDT on August 23, 2010.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62676 / August 10, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13999

In the Matter of Geotec, Inc., InnoPet Brands Corp., Marbledge Group, Inc. (n/k/a AR Growth Finance Corp.), Phlo Corp., Pliant Systems, Inc., Southeast Banking Corp., TNX Television Holdings, Inc., and WestPoint Stevens, Inc., Respondents.	ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Geotec, Inc., InnoPet Brands Corp., Marbledge Group, Inc. (n/k/a AR Growth Finance Corp.), Phlo Corp., Pliant Systems, Inc., Southeast Banking Corp., TNX Television Holdings, Inc., and WestPoint Stevens, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Geotec, Inc. ("GETC")[1] (CIK No. 1087717) is a Florida corporation located in Delray Beach, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). GETC is delinquent in its periodic filings with the Commission,

[1]The short form of each issuer's name is also its stock symbol.

16 of 62

having not filed any periodic reports since it filed a Form 10-Q for the period ended March 31, 2007, which reported a net loss of $513,568 for the prior three months. As of August 5, 2010, the common stock of GETC was quoted on the Pink Sheets operated by Pink OTC Markets Inc. ("Pink Sheets"), had eight market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. InnoPet Brands Corp. ("INBC") (CIK No. 1018158) is a void Delaware corporation located in Fort Lauderdale, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). INBC is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 1998, which reported a net loss of $2,589,087 for the prior three months. As of August 5, 2010, the common stock of INBC was quoted on the Pink Sheets, had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

3. Marbledge Group, Inc. (n/k/a AR Growth Finance Corp.) ("ARGW") (CIK No. 907161) is a delinquent Delaware corporation located in Lake Worth, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). ARGW is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended November 30, 1996, which reported a net loss of $938,190 for the prior nine months. On February 16, 2007, ARGW changed its name in the records of the Delaware Secretary of State to AR Growth Finance Corp., and in the Pink Sheets the following month but failed to report that change to the Commission on Form 8-K or record it in the Commission's EDGAR database, as required by Commission rules. As of August 5, 2010, the common stock of ARGW was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

4. Phlo Corp. ("PHCP") (CIK No. 1012130) is a void Delaware corporation located in Jacksonville, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). PHCP is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended December 31, 2007, which reported a net loss of $4,455,053 for the prior nine months. On March 30, 2007, the Commission entered an order that, among other things, ordered that PHCP cease-and-desist from committing or being a cause of any violations of Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder. In the Matter of Phlo Corporation, et al., Admin. Proc. File No. 3-11909, Exchange Act Rel. No. 55562 (March 30, 2007). PHCP has violated the cease-and-desist order. As of August 5, 2010, the common stock of PHCP was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

5. Pliant Systems, Inc. ("PLNS") (CIK No. 904898) is a void Delaware corporation located in Durham, North Carolina with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). PLNS is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 2001, which reported a net loss of $14,644,428 for the prior six months. On May 1, 2001, PLNS filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Eastern District of North Carolina, which was terminated on October 24, 2008. As of March 4, 2010, the

common stock of PLNS was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

6. Southeast Banking Corp. ("STBPQ") (CIK No. 91980) is a Florida corporation located in Miami, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). STBPQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 1991, which reported a net loss of $264,947,000 for the prior six months. On September 20, 1991, STBPQ filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Southern District of Florida, which was converted to Chapter 11, and was still pending as of August 5, 2010. As of August 5, 2010, the common stock of STBPQ was quoted on the Pink Sheets, had nine market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

7. TNX Television Holdings, Inc. ("TNXT") (CIK No. 1156867) is a void Delaware corporation located in Boca Raton, Florida with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). TNXT is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 2004, which reported a net loss of $8,178,596 for the prior nine months. As of August 5, 2010, the common stock of TNXT was quoted on the Pink Sheets, had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

8. WestPoint Stevens, Inc. ("WSPTQ") (CIK No. 852952) is a Delaware corporation located in West Point, Georgia with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). WSPTQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 30, 2004, which reported a net loss of $91,512,000 for the prior nine months. On June 1, 2003, WSPTQ filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Southern District of New York, which was still pending as of August 5, 2010. As of August 5, 2010, the common stock of WSPTQ was quoted on the Pink Sheets, had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

B. DELINQUENT PERIODIC FILINGS

9. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission, have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

10. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports, and Rule 13a-13 requires issuers to file quarterly reports.

11. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II hereof are true and, in connection therewith, to afford the Respondents an opportunity to establish any defenses to such allegations; and,

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II hereof, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, or fail to appear at a hearing after being duly notified, the Respondents, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents, may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondents personally or by certified, registered, or Express Mail, or by other means permitted by the Commission Rules of Practice.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

EXCHANGE ACT OF 1934
587 / August 11, 2010

TIVE PROCEEDING

JONATHAN BLECH,

espondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND NOTICE OF HEARING

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") against Richard Jonathan Blech ("Respondent" or "Blech").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

1. Blech was the Chief Executive Officer of Credit Bancorp, Ltd. ("Credit Bancorp"), a Netherlands Antilles corporation. Blech was a principal and registered representative with Credit Bancorp & Co., a Credit Bancorp affiliate, during the time it was registered as a broker-dealer with the Commission. Blech had the sole signature authority over all the Credit Bancorp & Co. brokerage accounts.

B. CRIMINAL CONVICTION

2. Blech pleaded guilty to three counts of securities fraud and fraud by wire, radio or television in violation of 15 U.S.C. §§ 78(j),1343 and 1346 before the United

17 of 62

States District Court for the Southern District of New York, United States v. Blech, et al., 1:02-CR-122. On June 24, 2005, a criminal judgment was entered against Blech. He was sentenced to a prison term of 72 months followed by three years of supervised release and ordered to make restitution in the amount of $18,128,599.40.

3. The counts for which Blech was convicted alleged, inter alia, that Blech defrauded investors and obtained money and property by means of materially false and misleading statements, using the United States mails and telephone in furtherance of the scheme. The misconduct underlying the criminal charges occurred during the period in which Blech was associated with a broker-dealer.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations; and

B. What, if any, remedial action is appropriate in the public interest against Respondent pursuant to Section 15(b)(6) of the Exchange Act.

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against him upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondent personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 210 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

Chairm[...] not participating.

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62688A; File Nos. SR-BATS-2010-018; SR-BX-2010-044; SR-CBOE-2010-065; SR-CHX-2010-14; SR-EDGA-2010-05; SR-EDGX-2010-05; SR-FINRA-2010-033; SR-ISE-2010-66; SR-NYSE-2010-49; SR-NYSEAmex-2010-63; SR-NYSEArca-2010-61; SR-NASDAQ-2010-079; SR-NSX-2010-08)

August 11, 2010

Self-Regulatory Organizations; BATS Exchange, Inc.; Chicago Board Options Exchange, Incorporated; Chicago Stock Exchange, Inc.; EDGA Exchange, Inc.; EDGX Exchange, Inc.; Financial Industry Regulatory Authority, Inc.; International Securities Exchange LLC; NASDAQ OMX BX, Inc.; The NASDAQ Stock Market LLC; National Stock Exchange, Inc.; New York Stock Exchange LLC; NYSE Amex LLC; NYSE Arca, Inc.; Notice of Designation of Longer Period for Commission Action on Proposed Rule Changes Relating to Trading Pauses Due to Extraordinary Market Volatility

On June 30, 2010, each of BATS Exchange, Inc., Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., International Securities Exchange, LLC, The NASDAQ Stock Market LLC, NASDAQ OMX BX, Inc., National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE Amex LLC, and NYSE Arca, Inc. filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 ("Act"),[2] and Rule 19b-4 thereunder,[3] proposed rule changes to amend certain of their respective rules to add additional securities to the single-stock circuit breaker pilot program.[4]

---

1 15 U.S.C. 78s(b)(1).

2 15 U.S.C. 78a.

3 17 CFR 240.19b-4.

4 The single-stock circuit breaker pilot program was initially approved on Ju[...] 2010. See Securities Exchange Act Release Nos. 62251 (June 10, 2010), [...] 34183 (June 16, 2010); 62252 (June 10, 2010), 75 FR 34186 (June 16, 20[...]

Section 19(b)(2) of the Act[5] provides that, within thirty-five days of the publication of notice of the filing of a proposed rule change, or within such longer period as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, the Commission shall either approve the proposed rule change or institute proceedings to determine whether the proposed rule change should be disapproved. The 35th day for these filings is August 11, 2010.

The Commission finds it appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider these proposed rule changes, which relate to the addition of additional securities to the single-stock circuit breaker pilot program, and the comment letters that have been submitted in connection with these filings.

---

5 15 U.S.C. 78s(b)(2).

Accordingly, the Commission, pursuant to Section 19(b)(2) of the Act,[6] designates August 25, 2010, as the date by which the Commission should either approve or institute proceedings to determine whether to disapprove the proposed rule changes.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

6 15 U.S.C. 78s(b)(2).

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62691 / August 11, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14003

In the Matter of **American Bullion Minerals, Ltd., American Industries Ltd., American Resource Corp., American Transportation Television Network, Inc., Amerimmune Pharmaceuticals, Inc., and Anaconda Venture Corp.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents American Bullion Minerals, Ltd., American Industries Ltd., American Resource Corp., American Transportation Television Network, Inc., Amerimmune Pharmaceuticals, Inc., and Anaconda Venture Corp.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. American Bullion Minerals, Ltd. (CIK No. 948341) is a British Columbia corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). American Bullion is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 20-F for the period ended December 31, 1997.

2. American Industries Ltd. (CIK No. 276298) is a defaulted Nevada corporation located in Las Vegas, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). American Industries is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended December 31, 2000, which reported a net loss of $75,895 for the prior nine months.

3. American Resource Corp. (CIK No. 797088) is a permanently revoked Nevada corporation located in Greenbrae, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). American Resource is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-K/A for the period ended December 31, 1995.

4. American Transportation Television Network, Inc. (CIK No. 811207) is a Canadian federal corporation located in Vancouver, British Columbia, Canada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). American Transportation is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended December 31, 1993, which reported a deficit of over $11.8 million for the prior twelve months.

5. Amerimmune Pharmaceuticals, Inc. (CIK No. 818808) is a delinquent Colorado corporation located in Las Vegas, Nevada with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Amerimmune is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended December 31, 2002, which reported a net loss of over $7.58 million since the company's April 10, 1998 inception. On April 4, 2003, the company filed a Chapter 7 petition in the U.S. Bankruptcy Court for the District of Colorado, which was terminated on October 9, 2003.

6. Anaconda Venture Corp. (CIK No. 1109302) is a suspended California corporation located in Irvine, California with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). Anaconda is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended September 30, 2001, which reported a net loss of over $22,358 since the company's February 17, 2000 inception.

B. DELINQUENT PERIODIC FILINGS

7. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission, have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

8. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the

Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports and Rule 13a-13 requires domestic issuers to file quarterly reports. Rule 13a-16 requires foreign private issuers to furnish quarterly and other reports to the Commission under cover of Form 6-K if they make or are required to make the information public under the laws of the jurisdiction of their domicile or in which they are incorporated or organized; if they file or are required to file information with a stock exchange on which their securities are traded and the information was made public by the exchange; or if they distribute or are required to distribute information to their security holders.

9. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 or 13a-16 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II are true and, in connection therewith, to afford the Respondents an opportunity to establish any defenses to such allegations; and,

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, or fail to appear at a hearing after being duly notified, the Respondents, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents, may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondents personally or by certified, registered, or Express Mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 200

[Release No. 34-62690]

Delegation of Authority to the Director of its Division of Enforcement

Agency: Securities and Exchange Commission.

Action: Final rule.

SUMMARY: The Commission is amending its rules to remove a sunset provision from the delegation of authority to the Director of the Division of Enforcement to issue formal orders of investigation. Formal orders designate the enforcement staff authorized to issue subpoenas in connection with investigations under the federal securities laws. On August 5, 2009, the Commission issued a release authorizing the Division Director to issue such orders for a one-year period beginning on August 11, 2009 and ending on August 11, 2010. The sunset provision was included to permit the Commission to evaluate the Division's use of the delegation and to consider whether extension of the delegation was appropriate.

EFFECTIVE DATE: [Insert date of publication in the Federal Register].

FOR FURTHER INFORMATION CONTACT: Kenneth H. Hall, Assistant Chief Counsel, 202-551-4936, Office of Chief Counsel, Division of Enforcement, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-6553.

SUPPLEMENTARY INFORMATION: The Commission is authorized to conduct investigations of possible violations of the federal securities laws, which provide that "any member of the Commission or any officer designated by it is empowered to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda, or other records which the

Commission deems relevant or material to the inquiry." Section 21(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(b). See also Section 19(c) of the Securities Act of 1933, 15 U.S.C. 77(c); Section 42(b) of the Investment Company Act of 1940, 15 U.S.C. 80a-41(b); and Section 209(b) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-9(b). The Commission issues formal orders of investigation that authorize specifically-designated enforcement staff to exercise the Commission's statutory power to subpoena witnesses and take the other actions authorized by the relevant cited provisions. The Commission delegated authority to issue formal orders of investigation to the Director of the Division of Enforcement on August 11, 2009. "Delegation of Authority to Director of Division of Enforcement," 74 FR 40068 (Aug. 11, 2009). The delegation was made effective for a one-year period, ending on August 11, 2010, to allow Commission review of the Division's exercise of formal order authority.

The Commission has determined that it is appropriate to extend the Division's authority to issue formal orders of investigation. In making this determination, the Commission considered the increased efficiency in the Division's conduct of its investigations permitted by the delegation, and the Division's continued effective communication and coordination in addressing pertinent legal and policy issues with other Commission Divisions and Offices when formal order authority is invoked.

Administrative Law Matters:

The Commission finds, in accordance with the Administrative Procedure Act ("APA") (5 U.S.C. 553(b)(3)(A)), that this amendment relates solely to agency organization, procedure, or practice and does not relate to a substantive rule. Accordingly, the provisions of the APA regarding notice of the proposed rulemaking, opportunities for public participation, and publication of the amendment prior to its effective date, 5 U.S.C. 553, are not applicable. For the same reason, and because this amendment does not substantively affect the rights or obligations of non-agency parties, the provisions of the Small Business Regulatory Enforcement Fairness Act, 5 U.S.C. 804(3)(C), are not applicable. Additionally, the provisions of the Regulatory Flexibility Act, which apply only when notice and comment are required by the APA or other law, 5 U.S.C. 603, are not applicable. Section 23(a)(2) of the Securities Exchange Act, 15 U.S.C. 78w(a)(2), requires the Commission, in adopting rules under that Act, to consider the anticompetitive effects of any rules it adopts. Because the amendment imposes no new burdens on parties in investigations, the Commission does not believe it will have any impact on competition. Finally, this amendment does not contain any collection of information requirements as defined by the Paperwork Reduction Act of 1980, as amended. Accordingly, the amendment is effective [Insert date of publication in the Federal Register].

List of Subjects in 17 CFR Part 200

Administrative practice and procedure, Authority delegations (Government agencies).

Text of Amendment

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 200—ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS

1. The authority citation for part 200, subpart A, continues to read in part as follows:

Authority: 15 U.S.C. 77o, 77s, 77sss, 78d, 78d-1, 78d-2, 78w, 78ll(d), 78mm, 80a-37, 80b-11, and 7202, unless otherwise noted.

* * * * *

2. Section 200.30-4 is amended by revising paragraph (a)(13) to read as follows:

§ 200.30-4 Delegation of authority to Director of Division of Enforcement.

* * * * *

(a) * * *

(13) To order the making of private investigations pursuant to section 19(c) of the Securities Act of 1933 (15 U.S.C. 77s(c)), section 21(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(b)), section 42(b) of the Investment Company Act of 1940 (15 U.S.C. 80a-41(b) and section 209(b) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-9(b)).

* * * * *

By the Commission

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Dated: August 11, 2010

SECURITIES AND EXCHANGE COMMISSION

[Release Nos. 33-9133; 34-62699; File No. 4-607]

NOTICE OF SOLICITATION OF PUBLIC COMMENT ON CONSIDERATION OF INCORPORATING IFRS INTO THE FINANCIAL REPORTING SYSTEM FOR U.S. ISSUERS

AGENCY: Securities and Exchange Commission.

ACTION: Request for comment.

SUMMARY: The Securities and Exchange Commission is requesting public comment on behalf of the staff on three topics related to its ongoing consideration of incorporating International Financial Reporting Standards ("IFRS") into the financial reporting system for U.S. issuers. These three topics, derived from the staff's work plan on consideration of the incorporation of IFRS, involve the impact of such incorporation on: U.S. investors' current knowledge of IFRS and preparedness for incorporation of IFRS into the financial reporting system for U.S. issuers; how investors educate themselves on changes in accounting standards and the timeliness of such education; and the extent of, logistics for, and estimated time necessary to undertake changes to improve investor understanding of IFRS and the related education process to ensure investors have a sufficient understanding of IFRS prior to potential incorporation.

DATES: Comments should be received on or before [Insert date 60 days after publication in the Federal Register].

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's Internet comment form (http://www.sec.gov/rules/other.shtml);

On February 24, 2010, the Commission issued a Statement in Support of Convergence and Global Accounting Standards (the "Statement"), reiterating its belief "that a single set of high-quality globally accepted accounting standards will benefit U.S. investors and that this goal is consistent with our mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation."[1] In this Statement, the Commission directed its staff to develop and execute a work plan ("Work Plan"), the purpose of which is to consider specific areas and factors before potentially transitioning our current financial reporting system for U.S. issuers to a system incorporating IFRS.[2]

The Work Plan identifies a number of topics for further study, including the three topics described below that are the subject of this solicitation for comment.

II. Investors' Current Knowledge of IFRS and Preparedness for Incorporation of IFRS[3]

A. Background

The consideration of incorporating IFRS into the financial reporting system for U.S. issuers requires, among other things, consideration of the impact on investors. This consideration requires an assessment of investor understanding and education regarding IFRS, because the main benefits to investors of a single set of high-quality globally accepted accounting standards would be realized only if investors understand and have confidence in the basis for the reported results.

IFRS currently differs from U.S. GAAP in a number of areas. Consequently, incorporation of IFRS into the financial reporting system for U.S. issuers may require

---

1 Release Nos. 33–9109; 34–61578 (Feb. 24, 2010) [75 FR 9494] (Mar. 2, 2010).

2 Available at: http://www.sec.gov/spotlight/globalaccountingstandards/globalaccountingstandards.pdf.

3 See the Work Plan, 75 FR at 9507.

To what extent and in what ways would that change if IFRS were incorporated into the financial reporting system for U.S. issuers?

- How much time do investors currently devote to understanding or maintaining an understanding of accounting standards? To what extent would the time increase or decrease if IFRS were incorporated into the financial reporting system for U.S. issuers?
- If IFRS were to be incorporated into the financial reporting system for U.S. issuers, to what extent would an investor (or an investor's organization) have adequate resources to develop an understanding of IFRS, such as knowledgeable professionals, training materials, and access to standards?
- To what extent and in what ways do investors think incorporation of IFRS would affect comparability among different issuers' financial statements? Which standards or treatments in IFRS that are elective are most important? To what extent do reporting format and disclosures affect any lack of comparability?
- To what extent and in what ways would an investor's investment decision-making processes change if a U.S. issuer's financial statements were prepared using IFRS? Would investors need additional or different information to perform their analysis and, if so, what?
- To what extent and in what ways would an investor's investment decision-making processes change if U.S. issuers were given a choice to elect to prepare their financial statements using either U.S. GAAP or IFRS? Would an investor have greater or

- At what point do investors educate themselves about standard-setting activities? Is it during the standard-setting process? Is it after completion of the standard-setting process? Would the timing of investors' education processes change if accounting standards for U.S. issuers were primarily developed by an organization other than the FASB?
- To what extent and in what ways do investors participate in the standard-setting process when the FASB and IASB set standards? Do they monitor standard-setting deliberations? Do they prepare response letters to requests for comment? Do they participate in the standard setters' working groups and roundtables?
- To what extent does the timing of an investor's education about a possible outcome of the accounting standard-setting process affect investment decisions? Do investors consider possible changes in accounting standards when analyzing an issuer's reported financial information, even before any such change in accounting is required to be adopted?
- Are there ways to improve the representation and communication of investors' perspectives in connection with accounting standard setting?
- To what extent do investors believe more education or communication about accounting standards or accounting standard-setting is needed? If more education or communication is needed, how should the education or communication be delivered? By whom?

IV. Extent of, Logistics for, and Estimated Time Necessary to Undertake any Necessary Changes

A. Background

SECURITIES AND EXCHANGE COMMISSION

[Release Nos. 33-9134; 34-62700; File No. 4-608]

NOTICE OF SOLICITATION OF PUBLIC COMMENT ON CONSIDERATION OF INCORPORATING IFRS INTO THE FINANCIAL REPORTING SYSTEM FOR U.S. ISSUERS

AGENCY: Securities and Exchange Commission.

ACTION: Request for comment.

SUMMARY: The Securities and Exchange Commission is requesting public comment on behalf of the staff on three topics related to its ongoing consideration of incorporating International Financial Reporting Standards ("IFRS") into the financial reporting system for U.S. issuers. These three topics, derived from the staff's Work Plan on considering the incorporation of IFRS into the financial reporting system for U.S. issuers, involve the impact of such incorporation on: issuers' compliance with contractual arrangements that require the use of U.S. Generally Accepted Accounting Principles ("U.S. GAAP"); issuers' compliance with corporate governance requirements; and the application of certain legal standards tied to amounts determined for financial reporting purposes.

DATES: Comments should be received on or before [Insert date 60 days after publication in the Federal Register]..

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's Internet comment form (http://www.sec.gov/rules/other.shtml);
- Send an e-mail to rule-comments@sec.gov. Please include File Number 4-608 on the subject line; or

I. Introduction

On February 24, 2010, the Commission issued a Statement in Support of Convergence and Global Accounting Standards (the "Statement"), reiterating its belief "that a single set of high-quality globally accepted accounting standards will benefit U.S. investors and that this goal is consistent with our mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation."[1] In this Statement, the Commission directed the Staff to develop and execute a work plan ("Work Plan"), the purpose of which is to consider specific areas and factors before potentially transitioning our current financial reporting system for U.S. issuers to a system incorporating IFRS.[2]

The Work Plan identifies a number of topics for further study, including the three topics that are the subject of this solicitation for comment.

II. Contractual Arrangements[3]

A. Background

Companies' contracts often, either explicitly or implicitly, require reporting under U.S. GAAP or include metrics that are based off of current U.S. GAAP reporting. For example, companies may have issued debt instruments which include financial covenants based on U.S. GAAP or require periodic reporting of financial statements prepared in accordance with U.S. GAAP. Similarly, lease contracts and employee compensation plans

---

1 Release Nos. 33-9109; 34-61578 (Feb. 24, 2010) [75 FR 9494] (Mar. 2, 2010).

2 Available at: http://www.sec.gov/spotlight/globalaccountingstandards/globalaccountingstandards.pdf.

3 See the Work Plan, 75 FR at 9511.

differently as compared to how a change in an existing financial reporting standard under U.S. GAAP would be treated today? If so, how?

- To the extent that incorporating IFRS into the financial reporting system for U.S. issuers would affect the application, interpretation, or enforcement of contractual commercial arrangements, how would parties to such arrangements most likely address such effects (e.g., by modifying the contract, or adopting multiple accounting systems)?
- To what extent would any potential effects of incorporating IFRS into the financial reporting system for U.S. issuers on the application of contractual commercial arrangements likely be mitigated or otherwise affected by providing for a transition or phase-in period for compliance with the incorporation of IFRS into the financial reporting system for U.S. issuers? What length of a transition or phase-in period would be necessary to reasonably mitigate the effects? Are there any other means by which such effects can be mitigated or avoided?

III. Corporate Governance; Stock Exchange Listing Requirements[5]

A. Background

Incorporation of IFRS into the financial reporting system for U.S. issuers may affect an issuer's compliance with corporate governance requirements. For example, in 2003, as required by the Sarbanes-Oxley Act, the Commission adopted rules that require a registrant to disclose whether it has at least one "audit committee financial expert," as defined, serving

5 See the Work Plan, 75 FR at 9511.

and we believe it would be important for audit committee members to do so in light of their responsibility for oversight of the preparation and audit of financial statements that are presented to U.S. investors. To what extent would current members of boards of directors likely have the education or experience needed to meet the requirements of the definition of "audit committee financial expert"[9] or the stock exchange listing requirements related to accounting or financial management expertise[10] following the incorporation of IFRS into the financial reporting system for U.S. issuers? Would there be adverse effects if an issuer were required to disclose that it does not have any audit committee financial experts while its audit committee members are in the process of obtaining the necessary expertise?

- To the extent that incorporating IFRS into the financial reporting system for U.S. issuers would adversely affect board members' ability to meet the requirements or result in disclosure that the issuer does not have an audit committee financial expert, how would issuers and individual directors most likely address such effects (e.g., by additional training)? To what extent and in what ways would such effects be likely to differ from similar effects in jurisdictions that have adopted, or are in the process of adopting, IFRS?
- To what extent and in what ways would incorporating IFRS into the financial reporting system for U.S. issuers likely affect an issuer's ability to comply with quantitative securities exchange listing standards?

---

9 Item 407(d)(5) of Regulation S-K.

10 E.g., NYSE Listed Company Manual § 303A.07; Nasdaq Listing Rule 5605(c)(2).

Certain legal standards in state laws may be tied to amounts determined for financial reporting purposes. For example, while the amount, timing, and manner of the payment of dividend distributions and repurchases of stock are typically determined by companies' boards of directors, the actual amounts available to distribute or to repurchase may be restricted by state statute. Some jurisdictions provide in this regard that dividends may be paid only from retained earnings or may be paid from current earnings despite an accumulated deficit.

To the extent that jurisdictions base legal standards on amounts determined for financial reporting purposes, incorporation of IFRS into the financial reporting system for U.S. issuers could affect a company's ability to undertake certain actions, such as declaring dividends or repurchasing stock, which would, in turn, affect investors' expectations. In addition, to the extent that legal standards do not change based on changes in financial reporting requirements, companies could need to maintain two sets of records.

B. Request for Comment

- To what extent and in what ways would incorporating IFRS into the financial reporting system for U.S. issuers likely affect the application of limits in state statutes on the ability of issuers to make distributions to holders of equity securities, either through dividends or similar distributions in respect of those securities, or to repurchase such securities?[12]

---

12 E.g., Del. Code Ann., tit. 8, §154 (defining surplus); Model Bus. Corp. Act §6.40 (prohibiting distributions to shareholders if total assets would be less than total liabilities).

- To what extent would any potential effects of incorporating IFRS into the financial reporting system for U.S. issuers on the application of statutory limits on distributions to equity security holders likely be mitigated or otherwise affected by providing for a transition or phase-in period for compliance with the incorporation of IFRS into the financial reporting system for U.S. issuers? What length of a transition or phase-in period would be necessary to reasonably mitigate the effects? Are there any other means by which such effects can be mitigated or avoided?
- To what extent and in what ways would incorporating IFRS into the financial reporting system for U.S. issuers likely affect the application of state statutes requiring a shareholder vote for a sale of "all or substantially all" of the issuer's property or assets?[15] For example, would the determination of whether such a vote is required change as a result of a change in accounting standards?
- Are there any particular asset sale statutes from any particular jurisdictions the application of which is especially likely to be affected by incorporating IFRS into the financial reporting system for U.S. issuers? Which statutes, and why?
- To the extent that incorporating IFRS into the financial reporting system for U.S. issuers would affect the application of statutes governing sales of assets, how would

---

Allowing corporations to revalue assets and liabilities to reflect current realities complies with the statute [specifying permissible sources for distributions to stockholders] and serves well the policies behind this statute."); Model Bus. Corp. Act §6.40(d) (permitting the board of directors to determine whether a distribution is permissible based "either on financial statements prepared on the basis of accounting practices and principles that are reasonable in the circumstances or on a fair valuation or other method that is reasonable in the circumstances.").

15 E.g., Del. Code Ann., tit. 8, §271(a); Model Bus. Corp. Act §12.02(a).

Persons submitting comments on any of these questions are invited to consider and comment on whether the manner in which IFRS incorporation is implemented would affect the responses to the questions above.

All interested parties are invited to submit their views, in writing, on these questions.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

August 12, 2010

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

August 12, 2010

In the Matter of **Atchison Casting Corp.** **(n/k/a Bradken-Atchison/St. Joseph, Inc.),** **CityFed Financial Corp.,** **Divine, Inc.** **(n/k/a Enivid, Inc.),** **Genesis Worldwide, Inc.,** **Hampton Consulting Corp., and** **Jake's Pizza International, Inc.,** **File No. 500-1**	**ORDER OF SUSPENSION OF TRADING**

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Atchison Casting Corp. (n/k/a Bradken-Atchison/St. Joseph, Inc.) because it has not filed any periodic reports since the period ended March 31, 2003.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of CityFed Financial Corp. because it has not filed any periodic reports since the period ended March 31, 2006.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Divine, Inc. (n/k/a Enivid, Inc.) because it has not filed any periodic reports since the period ended September 30, 2002.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Genesis Worldwide, Inc. because it has not filed any periodic reports since the period ended June 30, 2001.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Hampton Consulting Corp. because it has not filed any periodic reports since the period ended June 30, 2004.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Jake's Pizza International, Inc. because it has not filed any periodic reports since the period ended June 30, 1997.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed companies. Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed companies is suspended for the period from 9:30 a.m. EDT on August 12, 2010, through 11:59 p.m. EDT on August 25, 2010.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson
By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62698 / August 12, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14005

In the Matter of **Atchison Casting Corp.** **(n/k/a Bradken-Atchison/St. Joseph, Inc.),** **CityFed Financial Corp.,** **Divine, Inc.** **(n/k/a Enivid, Inc.),** **Genesis Worldwide, Inc.,** **Hampton Consulting Corp., and** **Jake's Pizza International, Inc.,** **Respondents.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that public administrative proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondents Atchison Casting Corp. (n/k/a Bradken-Atchison/St. Joseph, Inc.), CityFed Financial Corp., Divine, Inc. (n/k/a Enivid, Inc.), Genesis Worldwide, Inc., Hampton Consulting Corp., and Jake's Pizza International, Inc.

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENTS

1. Atchison Casting Corp. (n/k/a Bradken-Atchison/St. Joseph, Inc.) ("AHNCQ")[1] (CIK No. 911115) is a Delaware corporation located in Atchison, Kansas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). AHNCQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since

[1]The short form of each issuer's name is also its stock symbol.

it filed a Form 10-Q for the period ended March 31, 2003, which reported a net loss of $38,756,000 for the prior nine months. On August 4, 2003, AHNCQ filed a Chapter 7 petition in the U.S. Bankruptcy Court for the Western District of Missouri, which was converted to Chapter 11, and was still pending as of August 5, 2010. On November 6, 2008 AHNCQ terminated its existence as a Kansas corporation by merging into Bradken-Atchison/St. Joseph, Inc., a Delaware corporation but failed to report that change to the Commission on Form 8-K or record it in the Commission's EDGAR database, as required by Commission rules. As of August 5, 2010, the common stock of AHNCQ was quoted on the Pink Sheets operated by Pink OTC Markets Inc. ("Pink Sheets"), had five market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

2. CityFed Financial Corp. ("CTYF") (CIK No. 744765) is a Delaware corporation located in Ann Arbor, Michigan with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). CTYF is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended March 31, 2006, which reported a net loss of $2,185,000 for the prior three months. As of August 5, 2010, the common stock of CTYF was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

3. Divine, Inc. (n/k/a Enivid, Inc.) ("DVINQ") (CIK No. 1097516) is a dissolved Delaware corporation located in Lisle, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). DVINQ is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended September 30, 2002, which reported a net loss of $159,807,000 for the prior nine months. On February 25, 2003, DVINQ filed a Chapter 11 petition in the U.S. Bankruptcy Court for the District of Massachusetts, which was terminated on February 3, 2010. On February 18, 2004, DVINQ changed its name in the records of the Delaware Secretary of State to Enivid, Inc. but failed to report that change to the Commission on Form 8-K or record it in the Commission's EDGAR database, as required by Commission rules. As of August 5, 2010, the common stock of DVINQ was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

4. Genesis Worldwide, Inc. ("GWOW") (CIK No. 67532) is an Ohio corporation located in Dayton, Ohio with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). GWOW is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-Q for the period ended June 30, 2001, which reported a net loss of $11,864,000 for the prior six months. On September 17, 2001, GWOW filed a Chapter 11 petition in the U.S. Bankruptcy Court for the Southern District of Ohio, which was terminated on October 11, 2007. As of August 5, 2010, the common stock of GWOW was quoted on the Pink Sheets, had six market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

5. Hampton Consulting Corp. ("HCNP") (CIK No. 756767) is a Utah corporation located in Pratt, Kansas with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). HCNP is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 2004, which reported a net loss of $722,249 for the prior nine months. As of August 5, 2010, the

common stock of HCNP was quoted on the Pink Sheets, had seven market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

6. Jake's Pizza International, Inc. ("JAKE") (CIK No. 904148) is a forfeited Delaware corporation located in Rolling Meadows, Illinois with a class of securities registered with the Commission pursuant to Exchange Act Section 12(g). JAKE is delinquent in its periodic filings with the Commission, having not filed any periodic reports since it filed a Form 10-QSB for the period ended June 30, 1997, which reported a net loss of $337,715 for the prior nine months. As of August 5, 2010, the common stock of JAKE was quoted on the Pink Sheets, had four market makers, and was eligible for the "piggyback" exception of Exchange Act Rule 15c2-11(f)(3).

B. DELINQUENT PERIODIC FILINGS

7. As discussed in more detail above, all of the Respondents are delinquent in their periodic filings with the Commission, have repeatedly failed to meet their obligations to file timely periodic reports, and failed to heed delinquency letters sent to them by the Division of Corporation Finance requesting compliance with their periodic filing obligations or, through their failure to maintain a valid address on file with the Commission as required by Commission rules, did not receive such letters.

8. Exchange Act Section 13(a) and the rules promulgated thereunder require issuers of securities registered pursuant to Exchange Act Section 12 to file with the Commission current and accurate information in periodic reports, even if the registration is voluntary under Section 12(g). Specifically, Rule 13a-1 requires issuers to file annual reports, and Rule 13a-13 requires issuers to file quarterly reports.

9. As a result of the foregoing, Respondents failed to comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II hereof are true and, in connection therewith, to afford the Respondents an opportunity to establish any defenses to such allegations; and,

B. Whether it is necessary and appropriate for the protection of investors to suspend for a period not exceeding twelve months, or revoke the registration of each class of securities registered pursuant to Section 12 of the Exchange Act of the Respondents identified in Section II hereof, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondents shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondents fail to file the directed Answers, or fail to appear at a hearing after being duly notified, the Respondents, and any successor under Exchange Act Rules 12b-2 or 12g-3, and any new corporate names of any Respondents, may be deemed in default and the proceedings may be determined against them upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondents personally or by certified, registered, or Express Mail, or by other means permitted by the Commission Rules of Practice.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62701 / August 12, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14006

In the Matter of

PANWORLD MINERALS INTERNATIONAL, INC.,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934 AND NOTICE OF HEARING

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors that proceedings be, and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act"), against PanWorld Minerals International, Inc. ("PanWorld" or "Respondent").

After an investigation, the Division of Enforcement alleges that:

A. PanWorld was a Nevada corporation with its principal place of business in Salt Lake City, Utah. At relevant times, PanWorld's purported main business activity was to acquire and operate various mineral properties in South America and the United States. The Commission suspended trading in the shares of PanWorld on May 10, 1995, after which PanWorld ceased operations and abandoned its mining properties. On September 1, 1996, the Nevada Secretary of State revoked PanWorld's status as a corporation. On January 1, 2005, following reinstatement, PanWorld's status as a corporation was again revoked by the Nevada Secretary of State. PanWorld became defunct after its principals were criminally charged and imprisoned.

B. PanWorld has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder, while its common stock was registered with the Commission, in that it has not filed an Annual Report on Form 10-K since August 3, 1995.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate in the public interest that public administrative proceedings be instituted to determine:

A. Whether the allegations set forth in Section II are true and, in connection therewith, to afford Respondent an opportunity to establish any defenses to such allegations;

B. What, if any, remedial action is appropriate in the public interest against Respondent pursuant to Section 12(j) of the Exchange;

IV.

IT IS ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice, 17 C.F.R. § 201.110.

IT IS FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within twenty (20) days after service of this Order, as provided by Rule 220 of the Commission's Rules of Practice, 17 C.F.R. § 201.220.

If Respondent fails to file the directed answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f) and 310 of the Commission's Rules of Practice, 17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f) and 201.310.

This Order shall be served forthwith upon Respondent personally or by certified mail.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice.

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62705 / August 12, 2010

Administrative Proceeding
File Nos. 3-12749, 3-12750 and 3-12751

In the Matter of COMMONWEALTH EQUITY SERVICES, LLP d/b/a COMMONWEALTH FINANCIAL NETWORK, Respondent.	
In the Matter of DETWILER, MITCHELL, FENTON & GRAVES, INC., Respondent.	ORDER DIRECTING DISBURSEMENT OF FAIR FUND
In the Matter of JAMES X. MCCARTY, Respondent.	

On December 18, 2007, the Commission published a Notice of Proposed Distribution Plan and Opportunity for Comment ("Plan") submitted by the Division of Enforcement in connection with these proceedings (Exchange Act Rel. No. 56981). No comments were received on the Plan and on February 12, 2008, the Plan was approved (Exchange Act Rel. No. 57310).

By an Order Directing Disbursement of Fair Fund dated May 21, 2008, the Commission authorized the first disbursement in the amount of $537,000 (Exchange Act Release No. 57843).

The Fund Administrator has requested that the Commission approve a second disbursement of funds in the amount of $10,880.98 from the Fair Fund to Eligible Investors as described in the Plan.

Accordingly, it is ORDERED that $10,880.98 shall be disbursed from the Fair Fund to Eligible Investors, as provided for in the Plan.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62721 / August 13, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13862

In the Matter of **APOGEE TECHNOLOGY, INC.** **Respondent.**	**ORDER ON THE BASIS OF OFFER OF SETTLEMENT OF APOGEE TECHNOLOGY, INC., IMPLEMENTING SETTLEMENT.**

I.

The Securities and Exchange Commission ("Commission") instituted an Order Instituting Administrative Proceedings and Notice of Hearing Pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Apogee Technology, Inc. ("Apogee" or "Respondent") on April 16, 2010.

II.

Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of this proceeding and any other proceedings brought by or on behalf of the Commission or in which the Commission is a party, and without admitting or denying the findings contained in the Order on the Basis of Offer of Settlement of Apogee Technology, Inc., Implementing Settlement ("Order"), except as to the Commission's jurisdiction over it and the subject matter of this proceeding, which are admitted, Respondent consents to the entry of this Order containing the following findings, conditions for company filings, and consequent remedies set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

A. Apogee is a Delaware corporation headquartered in Norwood, Massachusetts. The common stock of Apogee was registered under Section 12(g) of the Exchange Act until October 2003, when it then became registered under Section 12(b) of the Exchange Act and listed on the American Stock Exchange. In January 2008, Apogee's stock was delisted and deregistered from

[1] The findings herein are made pursuant to the Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Section 12(b). It reverted to its Section 12(g) registration and is currently still registered under Section 12(g) of the Exchange Act. Apogee's securities are currently quoted on the Pink Sheets OTC Markets, Inc. under the symbol "ATCS." Apogee files as a smaller reporting company.

B. On April 16, 2010, the Commission issued an Order Instituting Administrative Proceedings and Notice of Hearing Pursuant to Section 12(j) of the Securities Exchange Act of 1934, alleging that:

1. Respondent is delinquent in its periodic filings with the Commission. In particular, Apogee has filed a materially deficient Form 10-K for the 2008 fiscal year and materially deficient Forms 10-Q for the three quarters of 2009 with the Commission since November 14, 2008, and has failed to file a Form 10-K for the 2009 fiscal year.

2. Respondent's annual report for the year ended December 31, 2008, was originally due by March 31, 2009.

3. Respondent did not file a Form 10-K for the fiscal year ended December 31, 2008, until December 18, 2009.

4. The financial statements contained in the December 18, 2009 filing are unaudited and the filing was materially deficient because Respondent's outside auditor disclaimed its opinion on those financial statements.

5. On January 15, 2010, Respondent subsequently filed its Forms 10-Q for the quarters ended March 31, June 30, and September 30, 2009. These filings had been due originally on May 15, on August 14, and on November 16, 2009, respectively. However, the financial statements in these filings were based on Apogee's unaudited 2008 financial statements, rendering these reports materially deficient.

6. Respondent's Form 10-K for the fiscal year ended December 31, 2009, was not filed by its original due date of March 31, 2010, and has not been filed to date.

7. Section 13(a) of the Exchange Act and the rules promulgated thereunder require issuers of securities registered pursuant to Section 12 of the Exchange Act to file with the Commission current and accurate information in periodic reports. Specifically, Rule 13a-1 requires issuers to file annual reports (Forms 10-K), and Rule 13a-13 requires issuers to file quarterly reports (Forms 10-Q).

8. Section 13(a)(2) of the Exchange Act requires annual reports to be certified by independent public accountants if required by the rules and regulations of the Commission.

9. Rule 8-02 under Article 8 of Regulation S-X requires smaller reporting companies following the end of their fiscal year to file an audited balance sheet, and statements of income and cash flows.

10. Rule 8-03 under Article 8 of Regulation S-X requires smaller reporting companies to file interim financial statements with a balance sheet as of the end of the issuer's preceding fiscal year.

11. As a result of its violation of Rules 8-02 and 8-03 of Article 8 of Regulation S-X, Respondent failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder.

C. On August 11, 2010, Apogee submitted an Offer of Settlement under which it would agree to the following:

1. Apogee shall file with the Commission, in accordance with the technical and substantive requirements for EDGAR documents, and in accordance with the requirements of the Exchange Act and rules and regulations thereunder, the following filings (the "Filings"):
   a. a Form 10-K for the period ended December 31, 2008, which contains an opinion, not a disclaimed or otherwise qualified opinion, from Apogee's outside auditor;
   b. Forms 10-Q for the periods ended March 31, 2009, June 30, 2009, and September 30, 2009, which contain financial statements that are based on audited 2008 financial statements and reviewed by an independent public accountant;
   c. a Form 10-K for the period ended December 31, 2009, which has not yet been filed;
   d. a Form 10-Q for the period ended March 31, 2010, which has not yet been filed; and
   e. a Form 10-Q for the period ended June 30, 2010, which will become due on August 16, 2010.

2. Apogee shall make each of the Filings by no later than 5:30 p.m. EDT on August 16, 2010 (the "Deadline").

3. If Apogee makes all of the Filings by the Deadline, the Division of Enforcement ("Division") will notify the Office of the Secretary of the Commission of that fact, and the Secretary will thereupon enter, without further notice, an order of the Commission in the form attached as Exhibit A to Respondent's Offer of Settlement, terminating this proceeding without the requested remedy of revocation or suspension of registration, unless, as further described in paragraph III.C.5., the Division, in consultation with the Division of Corporation Finance and any other appropriate Commission staff, and in its sole discretion, concludes that the Filings made by Apogee are not in accordance with the technical and substantive requirements for EDGAR documents, or in accordance with the requirements of Section 13(a) of the Exchange Act and rules and regulations thereunder.

4. If Apogee fails to make any of the Filings by the Deadline, the Division will notify the Office of the Secretary of the Commission of that fact, and the Secretary will

thereupon enter, without further notice, an order of the Commission pursuant to Exchange Act Section 12(j), in the form attached as Exhibit B to Respondent's Offer of Settlement, that finds Apogee to have failed to comply with Exchange Act Section 13(a), and Rules 13a-1 and 13a-13 thereunder, and revokes the registration of each class of Apogee's securities registered with the Commission pursuant to Exchange Act Section 12.

5. If, by the Deadline, Apogee makes all of the Filings but any of such Filings is in a form the Division, in consultation with the Division of Corporation Finance and any other appropriate Commission staff, and in its sole discretion, concludes is not in accordance with the technical and substantive requirements for EDGAR documents, or not in accordance with the requirements of Section 13(a) of the Exchange Act and rules and regulations thereunder:

    a. The Division will inform Apogee, by 5:30 p.m. EDT on August 20, 2010, of the nature of the deficiency/ies in any Filing;
    b. Apogee will have until 5:30 p.m. EDT on August 26, 2010, to remedy the identified deficiency/ies in all Filings and to resubmit such Filings in accordance with the technical and substantive requirements for EDGAR documents, and in accordance with the requirements of the Exchange Act and rules and regulations thereunder;
    c. If Apogee fails to resubmit such filings, or if Apogee resubmits such Filings pursuant to Paragraph 5.b. above, and the Division, in consultation with the Division of Corporation Finance, and any other appropriate Commission staff, and in its sole discretion, determines that any such Filing is not in accordance with the technical and substantive requirements for EDGAR documents, or in accordance with the requirements of Section 13(a) of the Exchange Act and rules and regulations thereunder, the Division will notify the Office of the Secretary of the Commission of that fact, and the Secretary will thereupon enter, without further notice, an order of the Commission pursuant to Exchange Act Section 12(j), in the form attached as Exhibit B to Respondent's Offer of Settlement, that finds Apogee to have failed to comply with Exchange Act Section 13(a), and Rules 13a-1 and 13a-13 thereunder, and revokes the registration of each class of Apogee's securities registered with the Commission pursuant to Exchange Act Section 12.
    d. If, after Apogee resubmits such Filings pursuant to Paragraph 5.b. above, and Apogee remedies the identified deficiency/ies, the Division will notify the Office of the Secretary of the Commission of that fact, and the Secretary will thereupon enter, without further notice, an order of the Commission in the form attached as Exhibit A to Respondent's Offer of Settlement, terminating this proceeding without the requested remedy of revocation or suspension of registration.

IV.

On the basis of the foregoing, IT IS ORDERED THAT:

Respondent's Offer of Settlement is accepted and a subsequent order resolving the proceeding will be issued in accordance with the terms of the Offer of Settlement described above.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

EXHIBIT A

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No.

ADMINISTRATIVE PROCEEDING
File No. 3-13862

In the Matter of **APOGEE TECHNOLOGY, INC.** **Respondent.**	**ORDER TERMINATING ADMINSTRATIVE PROCEEDINGS PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

For good cause shown

It is hereby ORDERED that this administrative proceeding is terminated and that final judgment shall enter without the imposition of a remedy pursuant to Section 12(j) of the Exchange Act.

By the Commission.

Elizabeth M. Murphy
Secretary

EXHIBIT B

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No.

ADMINISTRATIVE PROCEEDING
File No. 3-13862

In the Matter of **APOGEE TECHNOLOGY, INC.** **Respondent.**	**ORDER MAKING FINDINGS, AND REVOKING REGISTRATION OF SECURITIES PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

I.

The Securities and Exchange Commission ("Commission") deems it necessary and appropriate for the protection of investors to institute this Order Making Findings, and Revoking Registration of Securities Pursuant to Section 12(j) of the Securities Exchange Act of 1934 (the "Order") pursuant to the Offer or Settlement submitted by Apogee Technology, Inc. ("Apogee" or "Respondent"), which was accepted by the Commission in an Order on the Basis of Offer of Settlement of Apogee Technology, Inc., Implementing Settlement, filed on August __, 2010 (the "August __Order").

II.

Solely for the purpose of this proceeding and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of this proceeding, Respondent consents to the entry of this Order, as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

A. Apogee is a Delaware corporation headquartered in Norwood, Massachusetts. The common stock of Apogee was registered under Section 12(g) of the Exchange Act until October 2003, when it then became registered under Section 12(b) of the Exchange Act and listed on the American Stock Exchange. In January 2008, Apogee's stock was delisted and deregistered from Section 12(b). It reverted to its Section 12(g) registration and is currently still registered under

Section 12(g) of the Exchange Act. Apogee's securities are currently quoted on the Pink Sheets OTC Markets, Inc. under the symbol "ATCS." Apogee files as a smaller reporting company.

B. Apogee has failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder, while its common stock was registered with the Commission in that:

[Insert paragraph(s) that correspond to material deficiencies and/or missing Filings, such as:

1. Apogee failed to file [FORM(S) DESCRIPTION] by its/their required due date of [DATE] as described in Section III.C.4. of the August __Order; and/or

2. The Division of Enforcement has determined that Apogee's [FORM(S) DESCRIPTION] were not [made in accordance with the technical and substantive requirements for EDGAR documents, and/or in accordance with the requirements of Section 13(a) of the Exchange Act and the rules and regulations thereunder] as described in Section III.C.5. of the August ___Order.]

IV.

Section 12(j) of the Exchange Act provides as follows:

> The Commission is authorized, by order, as it deems necessary or appropriate for the protection of investors to deny, to suspend the effective date of, to suspend for a period not exceeding twelve months, or to revoke the registration of a security, if the Commission finds, on the record after notice and opportunity for hearing, that the issuer of such security has failed to comply with any provision of this title or the rules and regulations thereunder. No member of a national securities exchange, broker, or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security the registration of which has been and is suspended or revoked pursuant to the preceding sentence.

In view of the foregoing, the Commission finds that it is necessary and appropriate for the protection of investors to revoke the registration of each class of Respondent's securities registered pursuant to Section 12 of the Exchange Act.

Accordingly, it is hereby ORDERED, pursuant to Section 12(j) of the Exchange Act, that registration of each class of Respondent's securities registered pursuant to Section 12 of the Exchange Act be, and hereby is, revoked.

By the Commission.

Elizabeth M. Murphy
Secretary

Chairman Schapiro not participating

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62716; File No. 10-198)

August 13, 2010

In the Matter of the Application of
BATS Y-Exchange, Inc.
for Registration as a National Securities Exchange

Findings, Opinion, and Order of the Commission

I. Introduction

On October 20, 2009, BATS Y-Exchange, Inc. ("BATS Y Exchange" or "Exchange") submitted to the Securities and Exchange Commission ("Commission") a Form 1 application ("Form 1") under the Securities Exchange Act of 1934 ("Act"), seeking registration as a national securities exchange pursuant to Section 6 of the Act.[1] Notice of the application was published for comment in the Federal Register on January 28, 2010.[2] The Commission received no comments regarding the BATS Y Exchange Form 1. On July 1, 2010, BATS Y Exchange submitted Amendment No. 1 to its Form 1.[3]

---

1 15 U.S.C. 78f.

2 See Securities Exchange Act Release No. 61400 (January 22, 2010), 75 FR 4595 ("Notice").

3 In Amendment No. 1, the Exchange modified its application by amending or adding the following rules to align the proposed rules of BATS Y Exchange with the rules of BATS Exchange, Inc. ("BATS Exchange") as of the date of the Amendment, due to changes to BATS Exchange rules filed with and approved by the Commission or filed as immediately effective, as applicable, since the Form 1 was filed: Table of Contents; Rule 1.6 (Procedures for Exemptions); Rule 2.5 Interpretation and Policy .02 (Continuing Education Requirements); Rule 2.5 Interpretation and Policy .03 (Registration Procedures); Rule 2.5 Interpretation and Policy .04 (Termination of Employment); Rule 2.6(g) (Application Procedures for Membership or to become an Associated person of a Member); Rule 2.13 (Fidelity Bonds); Rule 3.22 (Gratuities); Rule 5.5 (Prevention of the Misuse of Material, Non-Public Information); Rule 11.9(c)(12) (Destination Specific Order); and Rule 12.13 (Trading Ahead of Research Reports). In addition, the Exchange modified certain Exhibits to the Form 1 to: (1) reflect minor changes to certain corporate documents; (2) update the Exchange's proposed User's manual and certain administrative documents; (3) include a representation that the Exchange's parent corporation will make

II. Statutory Standards

Under Sections 6(b) and 19(a) of the Act,[4] the Commission shall by order grant a registration as a national securities exchange if it finds that the exchange is so organized and has the capacity to carry out the purposes of the Act and can comply, and can enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulations thereunder, and the rules of the exchange.

As discussed in greater detail below, the Commission finds that BATS Y Exchange's application for exchange registration meets the requirements of the Act and the rules and regulations thereunder. Further, the Commission finds that the proposed rules of BATS Y Exchange are consistent with Section 6 of the Act in that, among other things, they are designed to: (1) assure fair representation of an exchange's members in the selection of its directors and administration of its affairs and provide that, among other things, one or more directors shall be representative of investors and not be associated with the exchange, or with a broker or dealer; (2) prevent fraudulent and manipulative acts and practices, promote just and equitable principles of trade, foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, remove impediments to and perfect the mechanisms of a free and open market and a national market

---

a capital contribution into the Exchange's capital account and provide adequate funding of Exchange operations; (4) update the list of anticipated Exchange officers; (5) indicate that the Exchange has executed a regulatory services agreement with the Financial Industry Regulatory Authority ("FINRA") to conduct various regulatory services on behalf of the Exchange; and (6) indicate that the Exchange intends to file with the Commission a plan setting forth the allocation of certain regulatory responsibilities between itself and FINRA pursuant to Rule 17d-2 of the Act for Members of the Exchange that are also members of FINRA. The changes proposed in Amendment No. 1 either are not material or are otherwise responsive to the concerns of Commission staff.

4 15 U.S.C. 78f(b) and 78s(a).

system; and (3) protect investors and the public interest. The Commission also believes that the rules of BATS Y Exchange are consistent with Section 11A of the Act.[5] Finally, the Commission finds that the proposed rules of BATS Y Exchange do not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.[6]

III. Discussion

A. Corporate Structure

BATS Y Exchange has applied to the Commission to register as a national securities exchange. BATS Global Markets, Inc. ("BATS Global Markets"), a Delaware corporation, will wholly own BATS Y Exchange as well as (1) BATS Exchange, a registered national securities exchange, and (2) BATS Trading, Inc. ("BATS Trading"), a registered broker-dealer that currently provides order routing services to BATS Exchange, and would provide such services to BATS Y Exchange.

1. Self-Regulatory Function of BATS Y Exchange; Relationship between BATS Global Markets, Inc. and BATS Y Exchange; Jurisdiction over BATS Global Markets, Inc.

Although BATS Global Markets will not itself carry out regulatory functions, its activities with respect to the operation of BATS Y Exchange must be consistent with, and not interfere with, the Exchange's self-regulatory obligations. The proposed BATS Global Markets corporate documents include certain provisions that are designed to maintain the independence of the Exchange's self-regulatory function from BATS Global Markets, enable the Exchange to operate in a manner that complies with the federal securities laws, including the objectives of

---

5 15 U.S.C. 78k-1.

6 15 U.S.C. 78f(b)(8).

Sections 6(b) and 19(g) of the Act, and facilitate the ability of the Exchange and the Commission to fulfill their regulatory and oversight obligations under the Act.[7]

For example, BATS Global Markets submits to the Commission's jurisdiction with respect to activities relating to BATS Y Exchange,[8] and agrees to provide the Commission and BATS Y Exchange with access to its books and records that are related to the operation or administration of BATS Y Exchange.[9] In addition, to the extent they are related to the operation or administration of BATS Y Exchange, the books, records, premises, officers, directors, agents, and employees of BATS Global Markets shall be deemed the books, records, premises, officers, directors, agents, and employees of BATS Y Exchange for purposes of, and subject to oversight pursuant to, the Act.[10] BATS Global Markets also agrees to keep confidential non-public information relating to the self-regulatory function[11] of BATS Y Exchange and not to use such information for any non-regulatory purpose.[12] In addition, the board of directors of BATS Global Markets, as well as its officers, employees, and agents, are required to give due regard to

---

7 See BATS Global Markets proposed Amended and Restated By-Laws Article XII and Article XIV, Sections 14.01, 14.02, 14.03, 14.04, 14.05, and 14.06.

8 See BATS Global Markets proposed Amended and Restated By-Laws Article XIV, Section 14.05.

9 See BATS Global Markets proposed Amended and Restated By-Laws Article XIV, Section 14.03.

10 Id.

11 This requirement to keep confidential non-public information relating to the self-regulatory function shall not limit the Commission's ability to access and examine such information or limit the ability of directors, officers, or employees of BATS Global Markets to disclose such information to the Commission. See BATS Global Markets proposed Amended and Restated By-Laws Article XIV, Section 14.02.

12 See BATS Global Markets proposed Amended and Restated By-Laws Article XIV, Section 14.02.

the preservation of the independence of the Exchange's self-regulatory function.[13] Further, BATS Global Markets By-Laws require that any changes to the BATS Global Markets Certificate of Incorporation and By-Laws be submitted to the Board of Directors of the Exchange ("Exchange Board"), and, if such amendment is required to be filed with the Commission pursuant to Section 19(b) of the Act, such change shall not be effective until filed with, or filed with and approved by, the Commission.[14] The Commission finds that these provisions are consistent with the Act, and that they will assist the Exchange in fulfilling its self-regulatory obligations and in administering and complying with the requirements of the Act.

The Commission also believes that under Section 20(a) of the Act[15] any person with a controlling interest in BATS Y Exchange would be jointly and severally liable with and to the same extent that BATS Y Exchange is liable under any provision of the Act, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action. In addition, Section 20(e) of the Act[16] creates aiding and abetting liability for any person who knowingly provides substantial assistance to another person in violation of any provision of the Act or rule thereunder. Further, Section 21C of the Act[17] authorizes the Commission to enter a cease-and-desist order against any person who has been "a cause of" a violation of any provision of the Act through an act or omission that the

---

13 See BATS Global Markets proposed Amended and Restated By-Laws Article XIV, Section 14.01.

14 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation TWELFTH and BATS Global Markets proposed Amended and Restated By-Laws Article XII.

15 15 U.S.C. 78t(a).

16 15 U.S.C. 78t(e).

17 15 U.S.C. 78u-3.

person knew or should have known would contribute to the violation. These provisions are applicable to BATS Global Markets' dealings with BATS Y Exchange.

2. Ownership and Voting Limitations; Changes in Control of BATS Y Exchange

The BATS Global Markets proposed Amended and Restated Certificate of Incorporation includes restrictions on the ability to own and vote shares of capital stock of BATS Global Markets.[18] These limitations are designed to prevent any shareholder from exercising undue control over the operation of BATS Y Exchange and to assure that the Exchange and the Commission are able to carry out their regulatory obligations under the Act.

Generally, no person, either alone or together with its related persons,[19] may beneficially own more than forty percent of any class of capital stock of BATS Global Markets.[20] The BATS Global Markets proposed Amended and Restated Certificate of Incorporation prohibits BATS Y Exchange members, either alone or together with their related persons, from beneficially owning more than twenty percent of shares of any class of capital stock of BATS

18 These provisions are generally consistent with ownership and voting limits approved by the Commission for other SROs. See e.g., Securities Exchange Act Release Nos. 61698 (March 12, 2010), 75 FR 13151 (March 18, 2010) (order granting the exchange registration of EDGX Exchange, Inc. and EDGA Exchange, Inc.) ("EDGX and EDGA Exchange Order"); 58375 (August 18, 2008), 73 FR 49498 (August 21, 2008) (File No. 10-182) (order granting the exchange registration of BATS Exchange, Inc.) ("BATS Exchange Order"); 53963 (June 8, 2006), 71 FR 34660 (June 15, 2006) (File No. SR-NSX-2006-03) ("NSX Demutualization Order"); 51149 (February 8, 2005), 70 FR 7531 (February 14, 2005) (File No. SR-CHX-2004-26) ("CHX Demutualization Order"); and 49098 (January 16, 2004), 69 FR 3974 (January 27, 2004) (File No. SR-Phlx-2003-73) ("Phlx Demutualization Order").

19 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (a)(ii).

20 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (b)(i)(A).

Global Markets.[21] If any stockholder violates these ownership limits, BATS Global Markets will redeem the shares in excess of the applicable ownership limit for their fair market value.[22] In addition, no person, alone or together with its related persons, may vote or cause the voting of more than twenty percent of the voting power of the then issued and outstanding capital stock of BATS Global Markets.[23] If any stockholder purports to vote, or cause the voting of, shares that would violate this voting limit, BATS Global Markets will not honor such vote in excess of the voting limit.[24]

The BATS Global Markets Board may waive the forty percent ownership limitation applicable to non-BATS Y Exchange member stockholders and the twenty percent voting limitation, pursuant to a resolution duly adopted by the Board of Directors, if it makes certain findings. Any such waiver would not be effective until approved by the Commission pursuant to Section 19 of the Act.[25] However, as long as BATS Global Markets directly or indirectly controls BATS Y Exchange, the BATS Global Markets Board cannot waive the voting and ownership limits above twenty percent for BATS Y Exchange members and their related persons.[26]

---

21 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (b)(i)(B).

22 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (e).

23 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (b)(i)(C).

24 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (d).

25 See BATS Global Markets proposed Amended and Restated Certificate of Incorporation FIFTH (b)(ii)(B).

26 These provisions are generally consistent with waiver of ownership and voting limits approved by the Commission for other SROs. See e.g., EDGX and EDGA Exchange Order, supra note 18; BATS Exchange Order, supra note 18; NSX Demutualization

Members that trade on an exchange traditionally have ownership interests in such exchange. As the Commission has noted in the past, however, a member's interest in an exchange could become so large as to cast doubt on whether the exchange can fairly and objectively exercise its self-regulatory responsibilities with respect to that member.[27] A member that is a controlling shareholder of an exchange might be tempted to exercise that controlling influence by directing the exchange to refrain from, or the exchange may hesitate to, diligently monitor and surveil the member's conduct or diligently enforce its rules and the federal securities laws with respect to conduct by the member that violates such provisions.

In addition, as proposed, BATS Y Exchange will be a wholly-owned subsidiary of BATS Global Markets. The BATS Y Exchange proposed Amended and Restated By-Laws identifies this ownership structure.[28] Any changes to the BATS Y Exchange Amended and Restated By-Laws, including any change in the provision that identifies BATS Global Markets as the sole owner, must be filed with and approved by the Commission pursuant to Section 19 of the Act.[29] Further, pursuant to the BATS Y Exchange proposed Amended and Restated By-Laws, BATS Global Markets may not transfer or assign, in whole or in part, its ownership interest in BATS Y Exchange.[30]

Order, supra note 18; CHX Demutualization Order, supra note 18; and Securities Exchange Act Release No. 49718 (May 17, 2004), 69 FR 29611 (May 24, 2004) (SR-PCX-2004-08).

27 See, e.g., Securities Exchange Act Release Nos. 53128 (January 13, 2006), 71 FR 3550 (January 23, 2006) (File No. 10-131) ("Nasdaq Exchange Registration Order") and 53382 (February 27, 2006), 71 FR 11251 (March 6, 2006) (SR-NYSE-2005-77) ("NYSE/Archipelago Merger Approval Order").

28 See BATS Y Exchange proposed Amended and Restated By-Laws Article I(cc).

29 See 15 U.S.C. 78s.

30 See BATS Y Exchange proposed Amended and Restated By-Laws Article IV, Section 7.

The Commission believes that these provisions are consistent with the Act. These requirements should minimize the potential that a person could improperly interfere with or restrict the ability of the Commission or the Exchange to effectively carry out their regulatory oversight responsibilities under the Act.

3. BATS Y Exchange

BATS Y Exchange has applied to the Commission to register as a national securities exchange. As part of its exchange application, the Exchange has filed the BATS Y Exchange Certificate of Incorporation and the proposed Amended and Restated By-Laws of BATS Y Exchange. In these documents, among other things, BATS Y Exchange establishes the composition of the Exchange Board and the BATS Y Exchange committees.

a. The BATS Y Exchange Board of Directors

The Exchange Board will be the governing body of BATS Y Exchange and possess all of the powers necessary for the management of the business and affairs of the Exchange and the execution of its responsibilities as an SRO. Under the BATS Y Exchange proposed Amended and Restated By-Laws:

- The Exchange Board will be composed of ten directors;[31]
- One director will be the Chief Executive Officer of BATS Y Exchange;[32]

[31] See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2(a).

[32] See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2(b).

- The number of Non-Industry Directors,[33] including at least one Independent Director,[34] will equal or exceed the sum of the number of Industry Directors[35] and Member Representative Directors;[36] and
- At least twenty percent of the directors on the Exchange Board will be Member Representative Directors.[37]

BATS Global Markets will appoint the initial Exchange Board, including the Member Representative Directors, which shall serve until the first annual meeting of stockholders.[38] The

---

33 "Non-Industry Director" means a Director who is an Independent Director or any other individual who would not be an Industry Director. See BATS Y Exchange proposed Amended and Restated By-Laws Article I(v).

34 "Independent Director" means a "Director who has no material relationship with the [Exchange], or any Exchange Member or any affiliate of any such Exchange Member; provided, however, that an individual who otherwise qualifies as an Independent Director shall not be disqualified from serving in such capacity solely because such Director is a Director of the [Exchange] or its stockholder." See BATS Y Exchange proposed Amended and Restated By-Laws Article I(m).

35 Generally, an "Industry Director" is, among other things, a Director that is or has been within the past three years an officer, director, employee, or owner of a broker-dealer. In addition, persons who have a consulting or employment relationship with the Exchange and its affiliates, are considered "Industry." See BATS Y Exchange proposed Amended and Restated By-Laws Article I(o).

36 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2(b)(i).

37 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2(b)(ii). "Member Representative Director" means a "Director who has been appointed as such to the initial Board of Directors pursuant to Article III, Section 4(g) of these By-Laws, or elected by stockholders after having been nominated by the Member Nominating Committee or by an Exchange Member pursuant to these By-Laws and confirmed as the nominee of Exchange Members after majority vote of Exchange Members, if applicable. A Member Representative Director must be an officer, director, employee, or agent of an Exchange member that is not a Stockholder Exchange Member." See BATS Y Exchange proposed Amended and Restated By-Laws Article I(s). See also BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 4(b).

38 See BATS Y Exchange proposed Amended and Restated By-Laws Article I(s) and Article III, Section 4(g).

first annual meeting of the stockholders will be held prior to BATS Y Exchange commencing operations as a national securities exchange.[39] At the first annual meeting of stockholders, a new Exchange Board will be elected pursuant to the BATS Y Exchange proposed Amended and Restated By-Laws. Therefore, prior to commencing operations as a national securities exchange, BATS Y Exchange Members will have the opportunity to participate in the selection of Member Representative Directors, and the Exchange Board will be in compliance with the compositional requirements contained in the BATS Y Exchange proposed Amended and Restated By-Laws.[40]

BATS Global Markets will appoint the initial Nominating Committee[41] and Member Nominating Committee,[42] consistent with each committee's compositional requirements,[43] to nominate candidates for election to the Exchange Board. Each of the Nominating Committee and Member Nominating Committee, after completion of its respective duties for nominating directors for election to the Board for that year, shall nominate candidates to serve on the succeeding year's Nominating Committee or Member Nominating Committee, as applicable. Additional candidates for the Member Nominating Committee may be nominated and elected by BATS Y Exchange Members pursuant to a petition process.[44]

---

39 See BATS Y Exchange proposed Amended and Restated By-Laws Article IV, Section 1(b).

40 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2.

41 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 2. The Nominating Committee will be comprised of at least three directors, and the number of Non-Industry members on the Nominating Committee must equal or exceed the number of Industry members.

42 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 3. The Member Nominating Committee will be comprised of at least three directors, and each member of the Member Nominating Committee shall be a Member Representative member.

43 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 1.

44 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 1.

The Nominating Committee will nominate candidates for each director position other than the Member Representative Directors, and BATS Global Markets, as the sole shareholder, will elect those directors. The Member Nominating Committee will nominate candidates for each Member Representative Director position on the Exchange Board.[45] Additional candidates may be nominated for the Member Representative Director positions by BATS Y Exchange Members pursuant to a petition process.[46] If no candidates are nominated pursuant to a petition process, then the initial nominees of the Member Nominating Committee will be nominated as Member Representative Directors by the Nominating Committee. If a petition process produces additional candidates, then the candidates nominated pursuant to a petition process, together with those nominated by the Member Nominating Committee, will be presented to BATS Y Exchange Members for election to determine the final nomination of Member Representative Directors.[47] The candidates who receive the most votes will be nominated as Member Representative Directors by the Nominating Committee.[48] BATS Global Markets, as the sole shareholder, will

---

45 The Member Nominating Committee will solicit comments from BATS Y Exchange Members for the purpose of approving and submitting names of candidates for election to the position of Member Representative Director. See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 4(b).

46 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 4(c). The petition must be signed by executive representatives of ten percent or more of the Exchange members. No Exchange member, together with its affiliates, may account for more than fifty percent of the signatures endorsing a particular candidate. Id.

47 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 4(e) and (f). Each BATS Y Exchange Member shall have the right to cast one vote for each available Member Representative Director nomination, provided that any such vote must be cast for a person on the List of Candidates and that no BATS Y Exchange Member, together with its affiliates, may account for more than twenty percent of the votes cast for a candidate. Id.

48 See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 4(f).

elect those candidates nominated by the Nominating Committee as Member Representative Directors.[49]

The Commission believes that the requirement in the BATS Y Exchange proposed Amended and Restated By-Laws that twenty percent of the directors be Member Representative Directors and the means by which they are chosen by members provides for the fair representation of members in the selection of directors and the administration of BATS Y Exchange consistent with the requirement in Section 6(b)(3) of the Act.[50] As the Commission has previously noted, this requirement helps to ensure that members have a voice in the use of self-regulatory authority, and that an exchange is administered in a way that is equitable to all those who trade on its market or through its facilities.[51]

The Commission has previously stated its belief that the inclusion of public, non-industry representatives on exchange oversight bodies is critical to an exchange's ability to protect the public interest.[52] Further, public, non-industry representatives help to ensure that no single group of market participants has the ability to systematically disadvantage other market participants through the exchange governance process. The Commission believes that public directors can provide unique, unbiased perspectives, which should enhance the ability of the Exchange Board

---

49 Id.

50 15 U.S.C. 78f(b)(3).

51 See Nasdaq Exchange Registration Order and NYSE/Archipelago Merger Approval Order, supra note 27; BATS Exchange Order, supra note 18; and EDGX and EDGA Exchange Order, supra note 18.

52 See, e.g., Regulation of Exchanges and Alternative Trading Systems, Securities Exchange Act Release No. 40760 (December 8, 1998), 63 FR 70844 (December 22, 1998) ("Regulation ATS Release").

to address issues in a non-discriminatory fashion and foster the integrity of BATS Y Exchange.[53] The Commission believes that the proposed composition of the Exchange Board satisfies the requirements in Section 6(b)(3) of the Act,[54] which requires that one or more directors be representative of issuers and investors and not be associated with a member of the exchange, or with a broker or dealer.[55]

b. BATS Y Exchange Committees

In the BATS Y Exchange proposed Amended and Restated By-Laws, BATS Y Exchange has proposed to establish several committees. Specifically, BATS Y Exchange has proposed to establish the following committees that would be appointed by the Chairman of the Exchange Board, with the approval of the Exchange Board: a Compensation Committee;[56] Audit

---

53 See Nasdaq Exchange Registration Order and NYSE/Archipelago Merger Approval Order, supra note 27; BATS Exchange Order, supra note 18; and EDGX and EDGA Exchange Order, supra note 18.

54 15 U.S.C. 78f(b)(3).

55 The number of Non-Industry Directors on the Exchange Board must equal or exceed the sum of the Industry and Member Representative Directors, and the Exchange Board must include at least one Independent Director. See BATS Y Exchange proposed Amended and Restated By-Laws Article III, Section 2(b)(i).

56 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(a). The Compensation Committee will be comprised of at least three people, and each voting member of the Compensation Committee shall be a Non-Industry Director. Id.

Committee;[57] Regulatory Oversight Committee;[58] Appeals Committee;[59] Executive Committee;[60] and Finance Committee.[61] In addition, BATS Y Exchange has proposed to establish a Nominating Committee[62] and a Member Nominating Committee, which would be elected on an annual basis by vote of stockholders.[63] The Commission believes that BATS Y Exchange's proposed committees should enable BATS Y Exchange to carry out its responsibilities under the Act and are consistent with the Act.

B. Regulation of BATS Y Exchange

---

57 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(b). The Audit Committee will be comprised of at least three people, and a majority of the Audit Committee members shall be Non-Industry Directors and a Non-Industry Director shall serve as Chairman of the Audit Committee. Id.

58 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(c). The Regulatory Oversight Committee will be comprised of at least three people, and each member of the Regulatory Oversight Committee shall be a Non-Industry Director. Id.

59 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(d). The Appeals Committee shall consist of one Independent Director, one Industry Director, and one Member Representative Director. Id.

60 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(e). The number of Non-Industry Directors on the Executive Committee shall equal or exceed the number of Industry Directors. The percentage of Independent Directors on the Executive Committee shall be at least as great as the percentage of Independent Directors on the whole Exchange Board, and the percentage of Member Representative Directors on the Executive Committee shall be at least as great as the percentage of Member Representative Directors on the whole Exchange Board. Id.

61 See BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(f).

62 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 2, and supra note 41.

63 See BATS Y Exchange proposed Amended and Restated By-Laws Article VI, Section 1, and supra note 42. Additional candidates for the Member Nominating Committee may be nominated and elected by BATS Exchange members pursuant to a petition process. See supra note 46 and accompanying text.

As a prerequisite for the Commission's approval of an exchange's application for registration, an exchange must be organized and have the capacity to carry out the purposes of the Act.[64] Specifically, an exchange must be able to enforce compliance by its members, and persons associated with its members, with the federal securities laws and the rules of the exchange.[65]

1. Membership

Membership on BATS Y Exchange will be open to any registered broker or dealer that is a member of another registered national securities exchange or association (other than or in addition to BATS Exchange), or any natural person associated with such a registered broker or dealer.[66] To remain eligible for membership in BATS Y Exchange, a BATS Y Exchange member must be a member of another SRO at all times.[67]

For a temporary 90-day period after approval of BATS Y Exchange's application, an applicant that is a current member of BATS Exchange and an active member of another SRO will be able to apply through an expedited process to become a BATS Y Exchange member by submitting a waive-in application form, including membership agreements.[68] BATS Y Exchange may request additional documentation in addition to the waive-in application form in

---

64 See Section 6(b)(1) of the Act, 15 U.S.C. 78f(b)(1).

65 Id. See also Section 19(g) of the Act, 15 U.S.C. 78s(g).

66 See BATS Y Exchange Rules 2.3 and 2.5(a)(4). BATS Y Exchange will only have one class of membership, with all members enjoying the same rights and privileges on the Exchange. Although BATS Y Exchange will permit members to register as Exchange Market Makers, such Market Makers will not receive special privileges or rights vis-à-vis other members.

67 Id.

68 See BATS Y Exchange Rule 2.4.

order to determine that a waive-in applicant meets BATS Y Exchange's qualification standards.[69]

All other applicants (and after the 90-day period has ended, those that could have waived in through the expedited process) may apply for membership in BATS Y Exchange by submitting a full membership application to BATS Y Exchange.[70] Applications for association with an Exchange Member shall be submitted to the Exchange on Form U-4 and such other forms as BATS Y Exchange may prescribe.

BATS Y Exchange will receive and review all applications for membership in the Exchange. If the Exchange is satisfied that the applicant is qualified for membership, the Exchange will promptly notify the applicant, in writing, of such determination, and the applicant shall be a member of the Exchange.[71] If the Exchange is not satisfied that the applicant is qualified for membership, the Exchange shall promptly notify the applicant of the grounds for denial.[72] Once an applicant is a member of the Exchange, it must continue to possess all the qualifications set forth in the BATS Y Exchange rules. When the Exchange has reason to believe that an Exchange member or associated person of a member fails to meet such qualifications, the Exchange may suspend or revoke such person's membership or association.[73]

---

69 Id.

70 See BATS Y Exchange Rule 2.6.

71 See BATS Y Exchange Rule 2.6(c).

72 See BATS Y Exchange Rule 2.6(d).

73 See BATS Y Exchange Rule 2.7; see also BATS Y Exchange Rules Chapters VII and VIII.

Appeal of a staff denial, suspension, or revocation of membership will be heard by the Appeals Committee.[74] Decisions of the Appeals Committee will be made in writing and will be sent to the parties to the proceeding. The decisions of the Appeals Committee will be subject to review by the Exchange Board, on its own motion, or upon written request by the aggrieved party or by the Chief Regulatory Officer ("CRO"). The Exchange Board will have sole discretion to grant or deny the request. The Exchange Board will conduct the review of the Appeals Committee's decision. The Exchange Board may affirm, reverse, or modify the Appeals Committee's decision. The Exchange Board's decision is final.[75]

The Commission finds that the BATS Y Exchange's membership rules are consistent with Section 6 of the Act,[76] specifically Section 6(b)(2) of the Act,[77] which requires that a national securities exchange have rules that provide that any registered broker or dealer or natural person associated with such broker or dealer may become a member and any person may become associated with an exchange member. The Commission notes that pursuant to Section 6(c) of the Act, an exchange must deny membership to any person, other than a natural person, that is not a registered broker or dealer, any natural person that is not, or is not associated with, a registered broker or dealer, and registered broker-dealers that do not satisfy certain standards, such as financial responsibility or operational capacity. As a registered exchange, BATS Y

---

[74] See BATS Y Exchange Rule 10.3; see also BATS Y Exchange proposed Amended and Restated By-Laws Article V, Section 6(d).

[75] See BATS Y Exchange Rule 10.5(b). Membership decisions are subject to review by the Commission. See BATS Y Exchange Rule 10.7.

[76] 15 U.S.C. 78f.

[77] 15 U.S.C. 78f(b)(2).

Exchange must independently determine if an applicant satisfies the standards set forth in the Act, regardless of whether an applicant is a member of another SRO.[78]

2. Regulatory Independence

BATS Y Exchange has proposed several measures to help ensure the independence of its regulatory function from its market operations and other commercial interests. The regulatory operations of BATS Y Exchange will be supervised by the CRO and monitored by the Regulatory Oversight Committee. The Regulatory Oversight Committee will consist of three members, each of whom must be a Non-Industry Director.[79] The Regulatory Oversight Committee will be responsible for monitoring the adequacy and effectiveness of the Exchange's regulatory program, assessing the Exchange's regulatory performance, and assisting the Exchange Board in reviewing the Exchange's regulatory plan and the overall effectiveness of the Exchange's regulatory functions.[80] The Regulatory Oversight Committee also will meet with the CRO in executive session at regularly scheduled meetings and at any time upon request of the CRO or any member of the Regulatory Oversight Committee.[81]

BATS Y Exchange proposes that its CRO have general supervision of the regulatory operations of the Exchange, including overseeing surveillance, examination, and enforcement functions.[82] The CRO also will administer any regulatory services agreement with another SRO to which BATS Y Exchange is a party.[83] The CRO will be an Executive Vice President or

---

78 See Nasdaq Exchange Registration Order, supra note 27.

79 See BATS Y Exchange proposed Amended and Restated By-Laws Articles I(v) and V, Section 6(c).

80 See BATS Exchange Amended and Restated By-Laws Article V, Section 6(c).

81 See BATS Y Exchange proposed Amended and Restated By-Laws Article VII, Section 9.

82 Id.

83 Id.

Senior Vice President that reports directly to the Chief Executive Officer.[84] The CRO also may serve as BATS Y Exchange's General Counsel.[85]

In addition, BATS Y Exchange has taken steps designed to provide sufficient funding for the Exchange to carry out its responsibilities under the Act. Specifically, BATS Y Exchange has represented that: (1) BATS Global Markets will allocate sufficient operational assets and make a capital contribution to the Exchange's capital account prior to the launch of the Exchange; (2) such an allocation and contribution will be adequate to operate the Exchange, including the regulation of the Exchange; and (3) there will be an explicit agreement between the Exchange and BATS Global Markets that requires BATS Global Markets to provide adequate funding for BATS Y Exchange's operations, including the regulation of the Exchange.[86] In addition, any revenues received by BATS Y Exchange from fees derived from its regulatory function or regulatory penalties will not be used for non-regulatory purposes.[87]

3. Regulatory Contract

Although BATS Y Exchange will be an SRO with all of the attendant regulatory obligations under the Act, it has entered into a regulatory services agreement with FINRA ("Regulatory Contract"), under which FINRA will perform certain regulatory functions on BATS Y Exchange's behalf.[88] Specifically, BATS Y Exchange represents that FINRA will assist Exchange staff on registration issues on an as-needed basis, investigate potential violations

---

84 Id.

85 Id. See also Nasdaq Exchange Registration Order, supra note 27.

86 See Amendment No. 1.

87 See BATS Y Exchange proposed Amended and Restated By-Laws Article X, Section 4.

88 See BATS Y Exchange Rule 13.7; see also Amendment No. 1. Pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission regulations thereunder, 17 CFR 200.83, BATS Y Exchange has requested confidential treatment for the Regulatory Contract.

of BATS Y Exchange's rules or federal securities laws related to activity on the Exchange, conduct examinations related to market conduct on the Exchange by Members, assist the Exchange with disciplinary proceedings pursuant to BATS Y Exchange's Rules, including issuing charges and conducting hearings, and provide dispute resolution services to BATS Y Exchange Members on behalf of the Exchange, including operation of the Exchange's arbitration program. BATS Y Exchange represents that FINRA also will provide the Exchange with access to FINRA's WebCRD system, and will assist with programming BATS Y-specific functionality relating to such system.[89] Notwithstanding the Regulatory Contract, BATS Y Exchange will retain ultimate legal responsibility for the regulation of its members and its market.

The Commission believes that it is consistent with the Act to allow BATS Y Exchange to contract with FINRA to perform examination, enforcement, and disciplinary functions.[90] These functions are fundamental elements to a regulatory program, and constitute core self-regulatory functions. The Commission believes that FINRA has the expertise and experience to perform these functions on behalf of BATS Y Exchange.[91]

---

89 See Amendment No. 1.

90 See, e.g., Regulation ATS Release, supra note 52. See also Securities Exchange Act Release Nos. 50122 (July 29, 2004), 69 FR 47962 (August 6, 2004) (SR-Amex-2004-32) (order approving rule that allowed Amex to contract with another SRO for regulatory services) ("Amex Regulatory Services Approval Order"); 57478 (March 12, 2008), 73 FR 14521 (March 18, 2008) (SR-NASDAQ-2007-004) ("NOM Approval Order"); Nasdaq Exchange Registration Order, supra note 27; BATS Exchange Order, supra note 18; and EDGX and EDGA Exchange Order, supra note 18.

91 See, e.g., Amex Regulatory Services Approval Order, supra note 90; NOM Approval Order, supra note 90; and Nasdaq Exchange Registration Order, supra note 27. The Commission notes that the Regulatory Contract is not before the Commission and, therefore, the Commission is not acting on it.

At the same time, BATS Y Exchange, unless relieved by the Commission of its responsibility,[92] bears the responsibility for self-regulatory conduct and primary liability for self-regulatory failures, not the SRO retained to perform regulatory functions on the Exchange's behalf. In performing these regulatory functions, however, FINRA may nonetheless bear liability for causing or aiding and abetting the failure of BATS Y Exchange to perform its regulatory functions.[93] Accordingly, although FINRA will not act on its own behalf under its SRO responsibilities in carrying out these regulatory services for BATS Y Exchange, FINRA may have secondary liability if, for example, the Commission finds that the contracted functions are being performed so inadequately as to cause a violation of the federal securities laws by BATS Y Exchange.[94]

4. 17d-2 Agreement

Section 19(g)(1) of the Act[95] requires every SRO to examine its members and persons associated with its members and to enforce compliance with the federal securities laws and the SRO's own rules, unless the SRO is relieved of this responsibility pursuant to Section 17(d) of the Act.[96] Section 17(d) was intended, in part, to eliminate unnecessary multiple examinations

---

92 See Section 17(d)(1) of the Act and Rule 17d-2 thereunder, 15 U.S.C. 78q(d)(1) and 17 CFR 240.17d-2. See also infra notes 95-103 and accompanying text.

93 For example, if failings by FINRA have the effect of leaving BATS Y Exchange in violation of any aspect of BATS Y Exchange's self-regulatory obligations, BATS Y Exchange would bear direct liability for the violation, while FINRA may bear liability for causing or aiding and abetting the violation. See, e.g., Nasdaq Exchange Registration Order, supra note 27; BATS Exchange Order, supra note 18; EDGX and EDGA Exchange Order, supra note 18; and Securities Exchange Act Release No. 42455 (February 24, 2000), 65 FR 11388 (March 2, 2000) (File No. 10-127) (order approving the International Securities Exchange LLC's application for registration as a national securities exchange).

94 Id.

95 15 U.S.C. 78s(g)(1).

96 15 U.S.C. 78q(d).

and regulatory duplication with respect to members of more than one SRO ("common members").[97] Rule 17d-2 of the Act permits SROs to propose joint plans allocating regulatory responsibilities concerning common members.[98] These agreements, which must be filed with and approved by the Commission, generally cover such regulatory functions as personnel registration, branch office examinations, and sales practices. Commission approval of a 17d-2 plan relieves the specified SRO of those regulatory responsibilities allocated by the plan to another SRO.[99] Many existing SROs have entered in to such agreements.[100]

BATS Y Exchange has represented to the Commission that BATS Y Exchange and FINRA intend to file a 17d-2 agreement with the Commission covering common members of BATS Y Exchange and FINRA. This agreement would allocate to FINRA regulatory responsibility, with respect to common members, for the following:[101]

- FINRA will examine common members of BATS Y Exchange and FINRA for compliance with federal securities laws, rules and regulations, and rules of BATS

97 See Securities Exchange Act Release No. 12935 (October 28, 1976), 41 FR 49091 (November 8, 1976) ("Rule 17d-2 Adopting Release").

98 17 CFR 240.17d-2.

99 See Rule 17d-2 Adopting Release, supra note 97.

100 See, e.g., Securities Exchange Act Release Nos. 13326 (March 3, 1977), 42 FR 13878 (March 14, 1977) (NYSE/Amex); 13536 (May 12, 1977), 42 FR 26264 (May 23, 1977) (NYSE/BSE); 14152 (November 9, 1977), 42 FR 59339 (November 16, 1977) (NYSE/CSE); 13535 (May 12, 1977), 42 FR 26269 (May 23, 1977) (NYSE/CHX); 13531 (May 12, 1977), 42 FR 26273 (May 23, 1977) (NYSE/PSE); 14093 (October 25, 1977), 42 FR 57199 (November 1, 1977) (NYSE/Phlx); 15191 (September 26, 1978), 43 FR 46093 (October 5, 1978) (NASD/BSE, CSE, CHX and PSE); 16858 (May 30, 1980), 45 FR 37927 (June 5, 1980) (NASD/BSE, CSE, CHX and PSE); 42815 (May 23, 2000), 65 FR 34762 (May 31, 2000) (NASD/ISE); and 54136 (July 12, 2006), 71 FR 40759 (July 18, 2006) (NASD/Nasdaq).

101 See Amendment No 1.

Exchange that have been certified by BATS Y Exchange as identical or substantially similar to FINRA rules.

- FINRA will investigate common members of BATS Y Exchange and FINRA for violations of federal securities laws, rules or regulations, or BATS Y Exchange rules that has been certified by BATS Y Exchange as identical or substantially identical to a FINRA rule.
- FINRA will enforce.compliance by common members with federal securities laws, rules and regulations, and rules of BATS Y Exchange that have been certified by BATS Y Exchange as identical or substantially similar to FINRA rules.

Because BATS Y Exchange anticipates entering into this 17d-2 agreement, it has not made provision to fulfill the regulatory obligations that would be undertaken by FINRA under this agreement with respect to common members of BATS Y Exchange and FINRA.[102] Accordingly, the Commission is conditioning the operation of BATS Y Exchange on approval by the Commission of a 17d-2 agreement between BATS Y Exchange and FINRA that allocates the above specified matters to FINRA.[103]

5. Discipline and Oversight of Members

As noted above, a prerequisite for the Commission approval of an exchange's application for registration, an exchange must be organized and have the capacity to carry out the purposes of the Act. Specifically, an exchange must be able to enforce compliance by its members and

---

102 The Commission notes that regulation that is to be covered by the 17d-2 agreement for common members will be carried out by FINRA under the Regulatory Contract for BATS Y Exchange members that are not also members of FINRA.

103 Alternatively, BATS Y Exchange could demonstrate that it has the ability to fulfill its regulatory obligations.

persons associated with its members with federal securities laws and the rules of the exchange.[104] As noted above, pursuant to the Regulatory Contract, FINRA will perform many of the initial disciplinary processes on behalf of BATS Y Exchange.[105] For example, FINRA will investigate potential securities laws violations, issue complaints, and conduct hearings pursuant to BATS Y Exchange rules. Appeals from disciplinary decisions will be heard by the Appeals Committee[106] and the Appeals Committee's decision shall be final. In addition, the Exchange Board may on its own initiative order review of a disciplinary decision.[107]

The BATS Y Exchange proposed Amended and Restated By-Laws and BATS Y Exchange rules provide that the Exchange has disciplinary jurisdiction over its members so that it can enforce its members' compliance with its rules and the federal securities laws.[108] The Exchange's rules also permit it to sanction members for violations of its rules and violations of the federal securities laws by, among other things, expelling or suspending members, limiting members' activities, functions, or operations, fining or censuring members, or suspending or barring a person from being associated with a member, or any other fitting sanction.[109] BATS Y Exchange's rules also provide for the imposition of fines for certain minor rule violations in lieu of commencing disciplinary proceedings.[110] Accordingly, as a condition to the operation of

---

104 See 15 U.S.C. 78f(b)(1).

105 See supra note 90 and accompanying text.

106 See BATS Y Exchange Rule 8.10(b).

107 See BATS Y Exchange Rule 8.10(c).

108 See generally BATS Y Exchange proposed Amended and Restated By-Laws Article X and BATS Y Exchange Rules Chapters II and VIII.

109 See BATS Y Exchange Rules 2.2 and 8.1(a).

110 See BATS Y Exchange Rule 8.15.

BATS Y Exchange, a Minor Rule Violation Plan ("MRVP") filed by BATS Y Exchange under Act Rule 19d-1(c)(2) must be declared effective by the Commission.[111]

The Commission finds that the BATS Y Exchange's proposed Amended and Restated By-Laws and rules concerning its disciplinary and oversight programs are consistent with the requirements of Sections 6(b)(6) and 6(b)(7)[112] of the Act in that they provide fair procedures for the disciplining of members and persons associated with members. The Commission further finds that the rules of BATS Y Exchange provide it with the ability to comply, and with the authority to enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulations thereunder, and the rules of BATS Y Exchange.[113]

C. BATS Y Exchange Trading System

1. Trading Rules

BATS Y Exchange will operate a fully automated electronic order book. Exchange members and entities that enter into sponsorship arrangements with Exchange members will have access to the BATS Y Exchange system (collectively, "Users").[114] Users will be able to electronically submit market and various types of limit orders to the Exchange from remote locations. BATS Y Exchange will not have a trading floor, but will allow firms to register as market makers with affirmative and negative market making obligations.[115] All orders submitted

111 17 CFR 240.19d-1(c)(2).

112 15 U.S.C. 78f(b)(6) and (b)(7).

113 See Section 6(b)(1) of the Act, 15 U.S.C. 78f(b)(1).

114 To obtain authorized access to the BATS Y Exchange System, each User must enter in to a User Agreement with the Exchange. See BATS Y Exchange Rule 11.3(a).

115 See BATS Y Exchange Rules 11.5 through 11.8. BATS Y Exchange's rules relating to maker makers are consistent with the rules of other national securities exchanges. See,

to BATS Y Exchange will be displayed unless designated otherwise by the BATS Y Exchange member submitting the order. Displayed orders will be displayed on an anonymous basis at a specified price. Non-displayed orders will not be displayed but will be ranked in the BATS Y Exchange system at a specified price. The BATS Y Exchange system will continuously and automatically match orders pursuant to price/time priority, except that displayed orders will have priority over non-displayed orders at the same price.[116]

The BATS Y Exchange system is designed to comply with Rule 611 of Regulation NMS[117] by requiring that, for any execution to occur on the Exchange during regular trading hours, the price must be equal to, or better than, any "protected quotation" within the meaning of Regulation NMS ("Protected Quotation"), unless an exception to Rule 611 of Regulation NMS applies.[118] BATS Y Exchange will direct any orders or portion of orders that cannot be executed in their entirety to away markets for execution through BATS Trading, unless the terms of the orders direct the Exchange not to route such orders away.[119]

BATS Y Exchange intends to operate as an automated trading center in compliance with Rule 600(b)(4) of Regulation NMS.[120] BATS Y Exchange will display automated quotations at all times except in the event that a systems malfunction renders the system incapable of displaying automated quotations.[121] The Exchange has designed its rules relating to orders,

---

e.g., BATS Exchange Rules 11.5 through 11.8; and National Stock Exchange, Inc. Rules 11.5 through 11.8.

116 See BATS Y Exchange Rule 11.12.

117 17 CFR 242.611.

118 See BATS Y Exchange Rule 11.13.

119 See BATS Y Exchange Rule 11.13(a)(2).

120 17 CFR 242.600(b)(4).

121 See BATS Y Exchange Rule 11.13(c); see also 17 CFR 242.600(b)(3).

modifiers, and order execution to comply with the requirements of Regulation NMS, including an immediate-or-cancel functionality.[122] These proposed rules include accepting orders marked as intermarket sweep orders, which will allow orders so designated to be automatically matched and executed without reference to Protected Quotations at other trading centers,[123] and routing orders marked as intermarket sweep orders by a User to a specific trading center for execution.[124] In addition, BATS Y Exchange rules address locked and crossed markets,[125] as required by Rule 610(d) of Regulation NMS.[126] The Commission believes that BATS Y Exchange's rules are consistent with the Act, in particular with the requirements of Rule 610(d) and Rule 611 of Regulation NMS.

As stated above, BATS Y Exchange intends to operate as an automated trading center and have its best bid and best offer be a Protected Quotation.[127] To meet their regulatory responsibilities under Rule 611(a) of Regulation NMS, market participants must have sufficient notice of new Protected Quotations, as well as all necessary information (such as final technical specifications).[128] Therefore, the Commission believes that it would be a reasonable policy and procedure under Rule 611(a) for industry participants to begin treating BATS Y Exchange's best bid and best offer as a Protected Quotation within 90 days after the date of this order, or such later date as BATS Y Exchange begins operation as a national securities exchange.

---

122 See BATS Y Exchange Rules 11.9 and 11.13; see also 17 CFR 242.600(b)(3).

123 See BATS Y Exchange Rule 11.9(d)(1).

124 See BATS Y Exchange Rule 11.9(d)(2).

125 See BATS Y Exchange Rule 11.20.

126 17 CFR 242.610(d).

127 17 CFR 242.600(b)(58).

128 See Securities Exchange Act Release No. 53829 (May 18, 2006), 71 FR 30038, 30041 (May 24, 2006) (File No. S7-10-04) (extending the compliance dates for Rule 610 and Rule 611 of Regulation NMS under the Act).

2. Section 11 of the Act

Section 11(a)(1) of the Act[129] prohibits a member of a national securities exchange from effecting transactions on that exchange for its own account, the account of an associated person, or an account over which it or its associated person exercises discretion (collectively, "covered accounts") unless an exception applies. Rule 11a2-2(T) under the Act,[130] known as the "effect versus execute" rule, provides exchange members with an exemption from the Section 11(a)(1) prohibition. Rule 11a2-2(T) permits an exchange member, subject to certain conditions, to effect transactions for covered accounts by arranging for an unaffiliated member to execute the transactions on the exchange. To comply with Rule 11a2-2(T)'s conditions, a member: (i) must transmit the order from off the exchange floor; (ii) may not participate in the execution of the transaction once it has been transmitted to the member performing the execution;[131] (iii) may not be affiliated with the executing member; and (iv) with respect to an account over which the member has investment discretion, neither the member nor its associated person may retain any compensation in connection with effecting the transaction except as provided in the Rule.

In a letter to the Commission, BATS Y Exchange requested that the Commission concur with BATS Y Exchange's conclusion that BATS Y Exchange members that enter orders into the BATS Y Exchange system satisfy the requirements of Rule 11a2-2(T).[132] For reasons set forth below, the Commission believes that BATS Y Exchange members entering orders into the BATS Y Exchange system would satisfy the conditions of the Rule.

129 15 U.S.C. 78k(a)(1).

130 17 CFR 240.11a2-2(T).

131 The member may, however, participate in clearing and settling the transaction.

132 See to Elizabeth M. Murphy, Secretary, Commission, from Anders Franzon, Vice President and Associate General Counsel, BATS Exchange, Inc., dated June 30, 2010 ("BATS Y Exchange 11(a) Letter").

The Rule's first condition is that orders for covered accounts be transmitted from off the exchange floor. The BATS Y Exchange system receives orders electronically through remote terminals or computer-to-computer interfaces. In the context of other automated trading systems, the Commission has found that the off-floor transmission requirement is met if a covered account order is transmitted from a remote location directly to an exchange's floor by electronic means.[133] Since the BATS Y Exchange system receives orders electronically through remote terminals or computer-to-computer interfaces, the Commission believes that the BATS Y Exchange system satisfies the off-floor transmission requirement.

Second, the rule requires that the member not participate in the execution of its order. BATS Y Exchange represented that at no time following the submission of an order is a member able to acquire control or influence over the result or timing of an order's execution.[134]

---

133 See, e.g., Securities Exchange Act Release Nos. 59154 (December 23, 2008) 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48) (order approving proposed rules of NASDAQ OMX BX); 49068 (January 13, 2004), 69 FR 2775 (January 20, 2004) (order approving the Boston Options Exchange as an options trading facility of the Boston Stock Exchange); 44983 (October 25, 2001), 66 FR 55225 (November 1, 2001) (order approving Archipelago Exchange as electronic trading facility of the Pacific Exchange ("PCX")("ArcaEx Order")); 29237 (May 24, 1991), 56 FR 24853 (May 31, 1991) (regarding NYSE's Off-Hours Trading Facility); 15533 (January 29, 1979), 44 FR 6084 (January 31, 1979) (regarding the American Stock Exchange ("Amex") Post Execution Reporting System, the Amex Switching System, the Intermarket Trading System, the Multiple Dealer Trading Facility of the Cincinnati Stock Exchange, the PCX Communications and Execution System, and the Philadelphia Stock Exchange's ("Phlx") Automated Communications and Execution System ("1979 Release")); and 14563 (March 14, 1978), 43 FR 11542 (March 17, 1978) (regarding the NYSE's Designated Order Turnaround System ("1978 Release")).

134 See BATS Y Exchange 11(a) Letter, supra note 132. The member may cancel or modify the order, or modify the instructions for executing the order, but only from off the Exchange floor. Id. The Commission has stated that the non-participation requirement is satisfied under such circumstances so long as such modifications or cancellations are also transmitted from off the floor. See Securities Exchange Act Release No. 14563 (March 14, 1978), 43 FR 11542 (March 17, 1978) (stating that the "non-participation requirement does not prevent initiating members from canceling or modifying orders (or the instructions pursuant to which the initiating member wishes orders to be executed) after

According to BATS Y Exchange, the execution of a member's order is determined solely by what orders, bids, or offers are present in the system at the time the member submits the order. Accordingly, the Commission believes that a BATS Y Exchange member would not participate in the execution of an order submitted into the BATS Y Exchange system.

Third, Rule 11a2-2(T) requires that the order be executed by an exchange member who is unaffiliated with the member initiating the order. The Commission has stated that this requirement is satisfied when automated exchange facilities, such as the BATS Y Exchange system, are used, as long as the design of these systems ensures that members do not possess any special or unique trading advantages in handling their orders after transmitting them to the exchange.[135] BATS Y Exchange has represented that the design of the BATS Y Exchange system ensures that no member has any special or unique trading advantage in the handling of its orders after transmitting its orders to BATS Y Exchange.[136] Based on BATS Y Exchange's representation, the Commission believes that the BATS Y Exchange system satisfies this requirement.

Fourth, in the case of a transaction effected for an account with respect to which the initiating member or an associated person thereof exercises investment discretion, neither the initiating member nor any associated person thereof may retain any compensation in connection

---

the orders have been transmitted to the executing member, provided that any such instructions are also transmitted from off the floor").

135 In considering the operation of automated execution systems operated by an exchange, the Commission noted that while there is no independent executing exchange member, the execution of an order is automatic once it has been transmitted into the systems. Because the design of these systems ensures that members do not possess any special or unique trading advantages in handling their orders after transmitting them to the exchange, the Commission has stated that executions obtained through these systems satisfy the independent execution requirement of Rule 11a2-2(T). See 1979 Release, supra note 133.

136 See BATS Y Exchange 11(a) Letter, supra note 132.

with effecting the transaction, unless the person authorized to transact business for the account has expressly provided otherwise by written contract referring to Section 11(a) of the Act and Rule 11a2-2(T).[137] BATS Y Exchange represented that BATS Y Exchange members trading for covered accounts over which they exercise investment discretion must comply with this condition in order to rely on the rule's exemption.[138]

D. Section 11A of the Act

Section 11A of the Act and the rules thereunder form the basis of our national market system and impose requirements on exchanges to implement its objectives. Specifically, national securities exchanges are required, under Rule 601 of Regulation NMS,[139] to file transaction reporting plans regarding transactions in listed equity and Nasdaq securities that are executed on their facilities. Currently registered exchanges satisfy this requirement by participating in the Consolidated Transaction Association Plan ("CTA Plan") for listed equities and the Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination of Quotation and Transaction Information for Nasdaq-Listed Securities Traded on Exchanges on an Unlisted Trading Privileges Basis ("Nasdaq UTP Plan") for Nasdaq

---

137 17 CFR 240.11a2-2(T)(a)(2)(iv). In addition, Rule 11a2-2(T)(d) requires a member or associated person authorized by written contract to retain compensation, in connection with effecting transactions for covered accounts over which such member or associated person thereof exercises investment discretion, to furnish at least annually to the person authorized to transact business for the account a statement setting forth the total amount of compensation retained by the member in connection with effecting transactions for the account during the period covered by the statement. See 17 CFR 240.11a2-2(T)(d). See also 1978 Release, supra note 133 (stating "[t]he contractual and disclosure requirements are designed to assure that accounts electing to permit transaction-related compensation do so only after deciding that such arrangements are suitable to their interests").

138 See BATS Y Exchange 11(a) Letter, supra note 132.

139 17 CFR 242.601.

securities.[140] Before BATS Y Exchange can begin operating as an exchange, it must join these plans as a participant.

National securities exchanges are required, under Rule 602 of Regulation NMS,[141] to collect bids, offers, quotation sizes and aggregate quotation sizes from those members who are responsible broker or dealers. National securities exchanges must then make this information available to vendors at all times when the exchange is open for trading. The current exchanges satisfy this requirement by participating in the Consolidated Quotation System Plan ("CQ Plan") for listed equity securities and the Nasdaq UTP Plan for Nasdaq securities. Before BATS Y Exchange can begin operating as an exchange it also must join the CQ Plan as a participant, in addition to the CTA Plan and the Nasdaq UTP Plan.

Finally, national securities exchanges must make available certain order execution information pursuant to Rule 605 of Regulation NMS.[142] Current exchanges have standardized the required disclosure mechanisms by participating in the Order Execution Quality Disclosure Plan.[143] BATS Y Exchange must join this plan before it begins operations as an exchange.

E. Order Routing

As discussed above, BATS Global Markets wholly owns BATS Y Exchange, BATS Exchange, and BATS Trading.[144] As such, BATS Y Exchange and BATS Exchange are

140 These plans also satisfy the requirement in Rule 603 that national securities exchanges and national securities associations act jointly pursuant to an effective national market system plan to disseminate consolidated information, including a national best bid and offer, and quotations for and transactions in NMS stocks. See 17 CFR 242.603. See also Nasdaq Exchange Registration Order, supra note 27.

141 17 CFR 242.602.

142 17 CFR 242.605.

143 See Securities Exchange Act Release No. 44177 (April 12, 2001), 66 FR 19814 (April 17, 2001).

144 See supra Section III.A.

affiliated with BATS Trading, which is a registered broker-dealer and member of FINRA. BATS Trading is a member of BATS Exchange and will become a member of BATS Y Exchange.

BATS Y Exchange's proposed Rule 2.10 provides generally that, without prior Commission approval, the Exchange may not, directly or indirectly, acquire or maintain an ownership interest in a member organization of such Exchange. In addition, BATS Y Exchange's Rule 2.10 provides that, without prior Commission approval, none of the Exchange's members may be or become an affiliate of the Exchange or an affiliate of an affiliate of the Exchange. However, BATS Y Exchange proposes that its affiliate, BATS Trading, become a member of the Exchange to provide certain routing services on behalf of the Exchange. Specifically, BATS Y Exchange proposes to (1) operate BATS Trading as a facility of the Exchange to provide outbound routing services to other securities exchanges,[145] automated trading systems, electronic communications networks, or other broker-dealers (collectively, "Trading Centers"), and (2) receive through BATS Trading orders routed inbound to the Exchange from its affiliated exchange (i.e., BATS Exchange). Accordingly, BATS Y Exchange seeks Commission approval of an exception in the Exchange's Rule 2.10 that will permit the affiliation between the Exchange and its member, BATS Trading.

Recognizing that the Commission has previously expressed concern regarding the potential for conflicts of interest in instances where a member firm is affiliated with an exchange, particularly where a member is routing orders to such affiliated exchange,[146] BATS Y Exchange has proposed limitations and conditions on BATS Trading's affiliation with the Exchange.

---

[145] Securities exchanges to which BATS Y Exchange proposes to route orders include its affiliated exchange (i.e., BATS Exchange).

[146] See e.g., Securities Exchange Act Release No. 53382 (February 27, 2006), 71 FR 11251 FR (March 6, 2006).

Specifically, BATS Y Exchange proposes that BATS Trading operate as an affiliated outbound router on behalf of the Exchange, subject to certain conditions set forth in the Exchange's Rule 2.11; and that BATS Trading operate as an affiliated inbound router on behalf of the Exchange subject to certain conditions set forth in the Exchange's Rule 2.12.[147]

1. <u>BATS Trading as Outbound Router</u>

BATS Y Exchange proposes that BATS would operate as a facility (as defined in Section 3(a)(2) of the Act) of the Exchange providing outbound routing services from the Exchange to other Trading Centers.[148] BATS Trading's operation as a facility providing outbound routing services for BATS Y Exchange is subject to the conditions that:

- BATS Y Exchange regulates BATS Trading as a facility of the Exchange;
- FINRA, a self-regulatory organization unaffiliated with the Exchange or any of its affiliates, is BATS Trading's designated examining authority;
- BATS Trading will not engage in any business other than (a) its outbound router function, (b) its inbound router function as described in Exchange Rule 2.12, and (c) any other activities it may engage in as approved by the Commission;
- the use of BATS Trading for outbound routing by Exchange members is optional;
- the Exchange will establish and maintain procedures and internal controls reasonably designed to adequately restrict the flow of confidential and proprietary information between the Exchange and its facilities (including BATS Trading) and any other entity;[149] and

147 <u>See</u> BATS Y Exchange Rules 2.11 and 2.12.

148 <u>See</u> BATS Y Exchange Rule 2.11.

149 <u>Id</u>.

- the books, records, premises, officers, agents, directors and employees of BATS Trading as a facility of the Exchange shall be deemed to be the books, records, premises, officers, agents, directors and employees of the Exchange for purposes of, and subject to oversight pursuant to, the Act.

As a facility of BATS Y Exchange, BATS Trading will be subject to the Exchange's and the Commission's regulatory oversight, and BATS Y Exchange will be responsible for ensuring that BATS Trading's outbound routing function is operated consistent with Section 6 of the Act and the Exchange's rules. In addition, BATS Y Exchange will be required to file with the Commission proposed rule changes and fees relating to BATS Trading's outbound routing function. Any such rules and fees relating to BATS Trading's outbound router function will be subject to exchange non-discrimination requirements. The Commission notes that the proposed conditions for the operation of BATS Trading as affiliated outbound router on behalf of the Exchange are consistent with conditions the Commission has approved for other exchanges.[150] The Commission therefore finds the proposed operation of BATS Trading as an affiliated outbound router of BATS Y Exchange to be consistent with the Act.

2. BATS Trading as Inbound Router

BATS Y Exchange also proposes that BATS Trading, operating as a facility of the BATS Exchange, provide routing services from BATS Exchange to BATS Y Exchange (i.e., "inbound" routing), subject to the following conditions and limitations:

---

150 See, e.g., Securities Exchange Act Release No. 59153 (December 23, 2008), 73 FR 80485 (December 31, 2008) (order approving outbound routing by broker-dealer affiliate of Nasdaq Stock Exchange); BATS Exchange Order, supra note 18; and EDGX and EDGA Exchange Order, supra note 18.

- The Exchange enter into (1) a 17d-2 agreement with FINRA, a non-affiliated SRO,[151] to relieve the Exchange of regulatory responsibilities for BATS Trading with respect to rules that are common rules between the Exchange and the non-affiliated SRO, and (2) the Regulatory Contract with FINRA,[152] a non-affiliated SRO, to perform regulatory responsibilities for BATS Trading for unique Exchange rules.
- The Regulatory Contract requires the Exchange to provide the non-affiliated SRO with information, in an easily accessible manner, regarding all exception reports, alerts, complaints, trading errors, cancellations, investigations, and enforcement matters (collectively "Exceptions") in which BATS Trading is identified as a participant that has potentially violated Exchange or Commission Rules, and requires that FINRA provide a report, at least quarterly, to the Exchange quantifying all Exceptions in which BATS Trading is identified as a participant that has potentially violated Exchange or Commission rules.
- BATS Y Exchange has in place a rule that requires BATS Global Market to establish and maintain procedures and internal controls reasonably designed to ensure that BATS Trading does not develop or implement changes to its system based on non-public information obtained as a result of its affiliation with the Exchange, until such information is available generally to similarly situated members of the Exchange.
- Routing of orders from BATS Trading to the Exchange, in BATS Trading's

---

151 See supra Section III.B.4 for a discussion of the Rule 17d-2 agreement.

152 See supra Section III.B.3 for a discussion of the Regulatory Contract.

capacity as a facility of BATS Exchange, be authorized for a pilot period of 12 months.[153]

Although the Commission continues to be concerned about potential unfair competition and conflicts of interest between an exchange's self-regulatory obligations and its commercial interest when the exchange is affiliated with one of its members, for the reasons discussed below, the Commission believes that it is consistent with the Act to permit BATS Trading to be affiliated with BATS Y Exchange and to provide inbound routing to BATS Y Exchange on a pilot basis, subject to the conditions described above.

BATS Y Exchange has proposed five conditions applicable to BATS Trading's inbound routing activities, which are enumerated above. The Commission believes that these conditions mitigate its concerns about potential conflicts of interest and unfair competitive advantage. In particular, the Commission believes that FINRA's oversight of BATS Trading,[154] combined with FINRA's monitoring of BATS Trading's compliance with the equity trading rules and quarterly reporting to the Exchange, will help to protect the independence of the Exchange's regulatory responsibilities with respect to BATS Trading. The Commission also believes that the requirement that BATS Y Exchange establish and maintain procedures and internal controls reasonably designed to ensure that BATS Trading does not develop or implement changes to its system based on non-public information obtained as a result of its affiliation with the Exchange, until such information is available generally to similarly situated members of the Exchange, is reasonably designed to ensure that BATS Trading cannot misuse any information advantage it may have because of its affiliation with the Exchange. Furthermore, the Commission believes

153 See BATS Y Exchange Rule 2.12.

154 This oversight will be accomplished through the Rule 17d-2 agreement and the Regulatory Contract.

that BATS Y Exchange's proposal to allow BATS Trading to route orders inbound to the Exchange from its affiliated exchange (i.e. BATS Exchange), on a pilot basis, will provide BATS Y Exchange and the Commission an opportunity to assess the impact of any conflicts of interest of allowing an affiliated member of an Exchange to route orders inbound to the Exchange and whether such affiliation provides an unfair competitive advantage.

Further, the Commission notes that the proposed conditions for the operation of BATS Trading as affiliated inbound router on behalf of BATS Y Exchange are consistent with conditions the Commission has approved for other exchanges.[155] The Commission therefore finds the proposed operation of BATS Trading as an affiliated inbound router of BATS Y Exchange is consistent with the Act.

F. Listing Requirements/Unlisted Trading Privileges

BATS Y Exchange initially does not intend to list any securities. Accordingly, BATS Y Exchange has not proposed rules that would allow it to list any securities at this time.[156] Instead, BATS Y Exchange has proposed to trade securities pursuant to unlisted trading privileges, consistent with Section 12(f) of the Act and Rule 12f-5 thereunder. Rule 12f-5 requires an exchange that extends unlisted trading privileges to securities to have in effect a rule or rules providing for transactions in the class or type of security to which the exchange extends unlisted

155 See e.g., Securities Exchange Release Nos. 60598 (September 1, 2009), 74 FR 46280 (September 8, 2009) (SR-ISE-2009-45); 59154 (December 23, 2008) 73 FR 80468 (December 31, 2008) (SR-BSE-2008-48) (order approving proposed rulebook of NASDAQ OMX BX); 59009 (November 24, 2008), 73 FR 73363 (December 2, 2008) (order granting accelerated approval to File No. SR-NYSEALTR-2008-07); and EDGX and EDGA Exchange Order, supra note 18.

156 BATS Y Exchange has incorporated listing standards for certain derivative securities products in its rules. However, BATS Y Exchange's rules will prohibit BATS Y Exchange from listing any derivative security product pursuant to these listing standards until BATS Y Exchange submits a proposed rule change to the Commission to amend its listing standards to comply with Rule 10A-3 under the Act and incorporate qualitative listing criteria. See BATS Y Exchange Rule 14.1(a).

trading privileges.[157] BATS Y Exchange's rules allow it to extend unlisted trading privileges to any security listed on another national securities exchange or with respect to which unlisted trading privileges may otherwise be extended in accordance with Section 12(f) of the Act.[158] BATS Y Exchange's proposed rules provide for transactions in the class or type of security to which the exchange intends to extend unlisted trading privileges.[159] In addition, pursuant to its rules, BATS Y Exchange will cease trading any equity security admitted to unlisted trading privileges that is no longer listed on another national securities exchange or to which unlisted trading privileges may no longer be extended, consistent with Section 12(f). The Commission finds that these rules are consistent with the Act.

IV. Exemption from Section 19(b) of the Act with Regard to FINRA Rules Incorporated by Reference

BATS Y Exchange proposes to incorporate by reference certain FINRA rules as Exchange rules. Thus, for certain Exchange rules, Exchange members will comply with an Exchange rule by complying with the FINRA rule referenced.[160] In connection with its proposal to incorporate FINRA rules by reference, BATS Y Exchange requested, pursuant to Rule 240.0-12,[161] an exemption under Section 36 of the Act from the rule filing requirements of Section 19(b) of the Act for changes to those BATS Y Exchange rules that are effected solely by virtue

---

157 17 CFR 240.12f-5. See also Securities Exchange Act Release No. 35737 (April 21, 1995), 60 FR 20891 (April 28, 1995) (adopting Rule 12f-5).

158 See BATS Y Exchange Rule 14.1(a).

159 Id. BATS Y Exchange's rules currently do not provide for the trading of options, security futures, or other similar instruments.

160 BATS Y Exchange proposes to incorporate by reference the 12000 and 13000 Series of FINRA's NASD Manual, the NASD Code of Arbitration Procedure for Customer and Industry Disputes. See BATS Y Exchange Rule 9.1.

161 See 17 CFR 240.0-12.

of a change to a cross-referenced FINRA rule.[162] BATS Y Exchange proposes to incorporate by reference categories of rules (rather than individual rules within a category) that are not trading rules. BATS Y Exchange agrees to provide written notice to its members whenever a proposed rule change to a FINRA rule that is incorporated by reference is proposed.[163]

Using its authority under Section 36 of the Act,[164] the Commission previously exempted certain SROs from the requirement to file proposed rule changes under Section 19(b) of the Act.[165] Each such exempt SRO agreed to be governed by the incorporated rules, as amended from time to time, but is not required to file a separate proposed rule change with the Commission each time the SRO whose rules are incorporated by reference seeks to modify its rules.

In addition, each such exempt SRO incorporated by reference only regulatory rules (i.e., margin, suitability, arbitration), not trading rules, and incorporated by reference whole categories of rules (i.e., did not "cherry-pick" certain individual rules within a category). Each such exempt SRO had reasonable procedures in place to provide written notice to its members each time a change is proposed to the incorporated rules of another SRO in order to provide its members with notice of a proposed rule change that affects their interests, so that they would have an opportunity to comment on it.

---

162 See to Elizabeth M. Murphy, Secretary, Commission, from Anders Franzon, Vice President and Associate General Counsel, BATS Exchange, Inc., dated June 30, 2010.

163 BATS Exchange will provide such notice via a posting on the same Web site location where BATS Exchange will post its own rule filings pursuant to Commission Rule 19b-4(l). The posting will include a link to the location on the FINRA Web site where the proposed rule change is posted. See id.

164 15 U.S.C. 78mm.

165 See, e.g., NOM Approval Order, supra note 90; Nasdaq Exchange Registration Order, supra note 27; BATS Exchange Order, supra note 18; and EDGX and EDGA Exchange Order, supra note 18.

The Commission is granting BATS Y Exchange's request for exemption, pursuant to Section 36 of the Act, from the rule filing requirements of Section 19(b) of the Act with respect to the rules that BATS Y Exchange proposes to incorporate by reference. This exemption is conditioned upon BATS Y Exchange providing written notice to its members whenever FINRA proposes to change a rule that BATS Y Exchange has incorporated by reference. The Commission believes that this exemption is appropriate in the public interest and consistent with the protection of investors because it will promote more efficient use of Commission and SRO resources by avoiding duplicative rule filings based on simultaneous changes to identical rules sought by more than one SRO. Consequently, the Commission grants BATS Y Exchange's exemption request.

V. Conclusion

IT IS ORDERED that the application of BATS Y Exchange for registration as a national securities exchange be, and hereby is, granted.

IT IS FURTHER ORDERED that operation of BATS Y Exchange is conditioned on the satisfaction of the requirements below:

A. Participation in National Market System Plans. BATS Y Exchange must join the CTA Plan, the CQ Plan, the Nasdaq UTP Plan, and the Order Execution Quality Disclosure Plan.

B. Intermarket Surveillance Group. BATS Y Exchange must join the Intermarket Surveillance Group.

C. Minor Rule Violation Plan. A MRVP filed by BATS Y Exchange under Rule 19d-1(c)(2) must be declared effective by the Commission.[166]

[166] 17 CFR 240.19d-1(c)(2).

D. 17d-2 Agreement. An agreement pursuant to Rule 17d-2[167] between FINRA and BATS Y Exchange that allocates to FINRA regulatory responsibility for those matters specified above[168] must be approved by the Commission, or BATS Y Exchange must demonstrate that it independently has the ability to fulfill all of its regulatory obligations.

E. Examination by the Commission. BATS Y Exchange must have, and represent in a letter to the staff in the Commission's Office of Compliance Inspections and Examinations that it has, adequate procedures and programs in place to effectively regulate BATS Y Exchange.

F. Trade Processing and Exchange Systems. BATS Y Exchange must have, and represent in a letter to the staff in the Commission's Division of Trading and Markets that it has, adequate procedures and programs in place, as noted in Commission Automation Policy Review guidelines,[169] to effectively process trades and maintain the confidentiality, integrity, and availability of the Exchange's systems.

G. BATS Exchange Inbound Routing. BATS Exchange must have in place rules approved by the Commission relating to an inbound routing structure that is consistent with what the Commission has approved for other national securities exchanges that receive orders from affiliated routers.[170]

---

167 17 CFR 240.17d-2.

168 See supra notes 95 to 103 and accompanying text.

169 On November 16, 1989, the Commission published its first Automation Review Policy ("ARP I"), in which it created a voluntary framework for self-regulatory organizations to establish comprehensive planning and assessment programs to determine systems capacity and vulnerability. On May 9, 1991, the Commission published its second Automation Review Policy ("ARP II") to clarify the types of review and reports that were expected from self-regulatory organizations. See Securities Exchange Act Release Nos. 27445 (November 16, 1989), 54 FR 48703 (November 24, 1989); and 29185 (May 9, 1991), 56 FR 22490 (May 15, 1991).

170 See supra note 155.

IT IS FURTHER ORDERED, pursuant to Section 36 of the Act,[171] that BATS Y Exchange shall be exempt from the rule filing requirements of Section 19(b) of the Act[172] with respect to the FINRA rules BATS Y Exchange proposes to incorporate by reference into BATS Y Exchange's rules, subject to the conditions specified in this Order.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

171 15 U.S.C 78mm.

172 15 U.S.C 78s(b).

SECURITIES AND EXCHANGE COMMISSION;
COMMODITY FUTURES TRADING COMMISSION

RIN 3235-AK65

RELEASE NO. 34-62717; File No. S7-16-10;

Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act

AGENCY: Securities and Exchange Commission; Commodity Futures Trading Commission

ACTION: Advance Joint Notice of Proposed Rulemaking; request for comments

SUMMARY: The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), provides for the comprehensive regulation of swaps and security-based swaps. Title VII of the Dodd-Frank Act ("Title VII"), provides that the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC") (collectively, "the Commissions"), in consultation with the Board of Governors of the Federal Reserve System, shall jointly further define certain key terms (specifically, "swap", "security-based swap", "swap dealer", "security-based swap dealer", "major swap participant", "major security-based swap participant", "eligible contract participant", and "security-based swap agreement"), and shall jointly prescribe regulations regarding "mixed swaps", as that term is used in Title VII of the Dodd-Frank Act. To assist the SEC and CFTC in further defining such terms, the Commissions are issuing this Notice and request for public comment.

DATES: Comments must be in writing and received by [INSERT DATE THAT IS 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: Comments may be submitted by any of the following methods:

SEC:

Electronic comments:

•Use the Commission's Internet comment form (http://www.sec.gov/rules/proposed.shtml);

•Send an e-mail to rule-comments@sec.gov. Please include File Number S7-16-10 on the subject line; or

•Use the Federal eRulemaking Portal (http://www.regulations.gov). Follow the instructions for submitting comments.

Paper comments:

•Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-16-10. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (http://www.sec.gov/rules/proposed.shtml). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

CFTC: Comments may be submitted by any of the following methods:

- *Mail:* David A. Stawick, Secretary, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.
- *Hand Delivery/Courier:* Same as mail above.
- *Fax:* 202-418-5521.
- *E-mail*: Comments may be submitted via e-mail at *dfadefinitions@cftc.gov*.

- *Agency Web Site*: Comments may be submitted to http://www.cftc.gov. Follow the instructions for submitting comments on the Web site.
- *Federal eRulemaking Portal*: Comments also may be submitted at http://www.regulations.gov. Follow the instructions for submitting comments. "Definitions" must be in the subject field of responses submitted via e-mail, and clearly indicated on written submissions. All comments must be submitted in English, or if not, accompanied by an English translation. All comments provided in any electronic form or on paper will be published on the CFTC Web site, without review and without removal of personally identifying information. All comments are subject to the CFTC Privacy Policy.

FOR FURTHER INFORMATION CONTACT: SEC: Matthew A. Daigler, Senior Special Counsel, at 202-551-5578, Joshua Kans, Senior Special Counsel, at 202-551-5591, or Cristie L. March, Attorney Advisor, at 202-551-5574, Division of Trading and Markets, or Michael J. Reedich, Special Counsel, at 202-551-3279, Office of Chief Counsel, Division of Corporation Finance, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7010;

CFTC: Terry S. Arbit, Deputy General Counsel, at 202-418-5357, tarbit@cftc.gov, Julian E. Hammar, Assistant General Counsel, at 202-418-5118, jhammar@cftc.gov, Mark Fajfar, Assistant General Counsel, at 202-418-6636, mfajfar@cftc.gov, or David Aron, Counsel, at 202-418-6621, daron@cftc.gov, Office of General Counsel, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, N.W., Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. BACKGROUND

The Dodd-Frank Act was enacted on July 21, 2010.[1] Title VII of the Dodd-Frank Act provides for the comprehensive regulation of swaps and security-based swaps and includes definitions of key terms relating to such regulation.[2] Section 712(d) of the Dodd-Frank Act provides that the SEC and CFTC, in consultation with the Board of Governors of the Federal Reserve System, shall jointly further define the terms "swap", "security-based swap", "swap dealer", "security-based swap dealer", "major swap participant", "major security-based swap participant", "eligible contract participant", and "security-based swap agreement" (collectively "Key Definitions").[3] Section 712(d) further provides that such jointly prescribed rules and regulations shall be comparable to the maximum extent possible, taking into consideration differences in instruments and in the applicable statutory requirements.

Further, Section 721(c) requires the CFTC to adopt a rule to further define the terms "swap", "swap dealer", "major swap participant", and "eligible contract participant", and Section 761(b) requires the SEC to adopt a rule to further define the terms "security-based swap", "security-based swap dealer", "major security-based swap participant" and "eligible contract participant", with regard to security-based swaps, for the purpose of including transactions and entities that have been structured to evade Title VII of the Dodd-Frank Act. Finally, Section 712(a) of the Dodd-Frank Act provides that the SEC and CFTC, after

---

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[2] Under Section 701 of the Dodd-Frank Act, Title VII may be cited as the "Wall Street Transparency and Accountability Act of 2010."

[3] These terms are defined in Sections 721 and 761 of the Dodd-Frank Act and, with respect to the term "eligible contract participant", in Section 1a(18) of the Commodity Exchange Act, 7 U.S.C. 1a(18), as re-designated and amended by Section 721 of the Dodd-Frank Act.

consultation with the Board of Governors of the Federal Reserve System, shall jointly prescribe regulations regarding "mixed swaps,"[4] as may be necessary to carry out the purposes of Title VII.

To assist the SEC and CFTC in further defining the Key Definitions specified above, and to prescribe regulations regarding "mixed swaps" as may be necessary to carry out the purposes of Title VII, the Commissions are seeking comment from interested parties.

II. SOLICITATION FOR COMMENTS ABOUT THE KEY DEFINITIONS AND THE REGULATION OF "MIXED SWAPS"

The Commissions invite comment with respect to all aspects of the Key Definitions, and also the regulation of "mixed swaps" as may be necessary to carry out the purposes of Title VII. Commenters are encouraged to address aspects of the Key Definitions such as the extent to which the definitions should be based on qualitative or quantitative factors and what those factors should be, any analogous areas of law, economics, or industry practice, and any factors specific to the commenter's experience. Commenters also are encouraged to express views on the regulation of "mixed swaps", as may be necessary to carry out the purposes of Title VII. Please comment generally and specifically, and please include empirical data and other information in support of such comments, where appropriate and available, regarding any of the Key Definitions described above and the regulation of "mixed swaps".

When commenting, please also take into account the statutory definitions of these terms that have been enacted in the Dodd-Frank Act. These statutory definitions are reprinted herein as follows:

[4] Sections 721 and 761 of the Dodd-Frank Act amend the Commodity Exchange Act, 7 U.S.C. 1 *et seq.*, and the Securities Exchange Act of 1934, 15 U.S.C. 78a *et seq.*, respectively, to define "mixed swap".

Swap: Section 721(a)(21) of the Dodd-Frank Act:

"(47) SWAP.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'swap' means any agreement, contract, or transaction—

(i) that is a put, call, cap, floor, collar, or similar option of any kind that is for the purchase or sale, or based on the value, of 1 or more interest or other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind;

(ii) that provides for any purchase, sale, payment, or delivery (other than a dividend on an equity security) that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence;

(iii) that provides on an executory basis for the exchange, on a fixed or contingent basis, of 1 or more payments based on the value or level of 1 or more interest or other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind, or any interest therein or based on the value thereof, and that transfers, as between the parties to the transaction, in whole or in part, the financial risk associated with a future change in any such value or level without also conveying a current or future direct or indirect ownership interest in an asset (including any enterprise or investment pool) or liability that incorporates the financial risk so transferred, including any agreement, contract, or transaction commonly known as—

(I) an interest rate swap;

(II) a rate floor;

(III) a rate cap;

(IV) a rate collar;

(V) a cross-currency rate swap;

(VI) a basis swap;

(VII) a currency swap;

(VIII) a foreign exchange swap;

(IX) a total return swap;

(X) an equity index swap;

(XI) an equity swap;

(XII) a debt index swap;

(XIII) a debt swap;

(XIV) a credit spread;

(XV) a credit default swap;

(XVI) a credit swap;

(XVII) a weather swap;

(XVIII) an energy swap;

(XIX) a metal swap;

(XX) an agricultural swap;

(XXI) an emissions swap; and

(XXII) a commodity swap;

(iv) that is an agreement, contract, or transaction that is, or in the future becomes, commonly known to the trade as a swap;

(v) including any security-based swap agreement which meets the definition of 'swap agreement' as defined in section 206A of the Gramm-Leach-Bliley Act (15 U.S.C. 78c note) of which a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein; or

(vi) that is any combination or permutation of, or option on, any agreement, contract, or transaction described in any of clauses (i) through (v).

(B) EXCLUSIONS.—The term 'swap' does not include—

(i) any contract of sale of a commodity for future delivery (or option on such a contract), leverage contract authorized under section 19, security futures product, or agreement, contract, or transaction described in section 2(c)(2)(C)(i) or section 2(c)(2)(D)(i);

(ii) any sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled;

(iii) any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities, including any interest therein or based on the value thereof, that is subject to—

(I) the Securities Act of 1933 (15 U.S.C. 77a et seq.); and

(II) the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.);

(iv) any put, call, straddle, option, or privilege relating to a foreign currency entered into on a national securities exchange registered pursuant to section 6(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78f(a));

(v) any agreement, contract, or transaction providing for the purchase or sale of 1 or more securities on a fixed basis that is subject to—

(I) the Securities Act of 1933 (15 U.S.C. 77a et seq.); and

(II) the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.);

(vi) any agreement, contract, or transaction providing for the purchase or sale of 1 or more securities on a contingent basis that is subject to the Securities Act of 1933 (15 U.S.C. 77a et seq.) and the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), unless the agreement, contract, or transaction predicates the purchase or sale on the occurrence of a bona fide contingency that might reasonably be expected to affect or be affected by the creditworthiness of a party other than a party to the agreement, contract, or transaction;

(vii) any note, bond, or evidence of indebtedness that is a security, as defined in section 2(a)(1) of the Securities Act of 1933 (15 U.S.C. 77b(a)(1));

(viii) any agreement, contract, or transaction that is—

(I) based on a security; and

(II) entered into directly or through an underwriter (as defined in section 2(a)(11) of the Securities Act of 1933 (15 U.S.C. 77b(a)(11)) by the issuer of such security for the purposes of raising capital, unless the agreement, contract, or transaction is entered into to manage a risk associated with capital raising;

(ix) any agreement, contract, or transaction a counterparty of which is a Federal Reserve bank, the Federal Government, or a Federal agency that is expressly backed by the full faith and credit of the United States; and

(x) any security-based swap, other than a security-based swap as described in subparagraph (D).

(C) RULE OF CONSTRUCTION REGARDING MASTER AGREEMENTS.—

(i) IN GENERAL.—Except as provided in clause (ii), the term 'swap' includes a master agreement that provides for an agreement, contract, or transaction that is a swap under subparagraph (A), together with each supplement to any master agreement, without regard to whether the master agreement contains an agreement, contract, or transaction that is not a swap pursuant to subparagraph (A).

(ii) EXCEPTION.—For purposes of clause (i), the master agreement shall be considered to be a swap only with respect to each agreement, contract, or transaction covered by the master agreement that is a swap pursuant to subparagraph (A).

(D) MIXED SWAP.—The term 'security-based swap' includes any agreement, contract, or transaction that is as described in section 3(a)(68)(A) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(68)(A)) and also is based on the value of 1 or more interest or other rates, currencies, commodities, instruments of indebtedness, indices, quantitative measures, other financial or economic interest or property of any kind (other than a single security or a narrow-based security index), or the occurrence, non-occurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence (other than an event described in subparagraph (A)(iii)).

(E) TREATMENT OF FOREIGN EXCHANGE SWAPS AND FORWARDS.—

(i) IN GENERAL.—Foreign exchange swaps and foreign exchange forwards shall be considered swaps under this paragraph unless the Secretary makes a written determination under section 1b that either foreign exchange swaps or foreign exchange forwards or both—

(I) should be not be regulated as swaps under this Act; and

(II) are not structured to evade the Dodd-Frank Wall Street Reform and Consumer Protection Act in violation of any rule promulgated by the [Commodity Futures Trading] Commission pursuant to section 721(c) of that Act.

(ii) CONGRESSIONAL NOTICE; EFFECTIVENESS.—The Secretary shall submit any written determination under clause (i) to the appropriate committees of Congress, including the Committee on Agriculture, Nutrition, and Forestry of the Senate and the Committee on Agriculture of the House of Representatives. Any such written determination by the Secretary shall not be effective until it is submitted to the appropriate committees of Congress.

(iii) REPORTING.—Notwithstanding a written determination by the Secretary under clause (i), all foreign exchange swaps and foreign exchange forwards shall be reported to either a swap data repository, or, if there is no swap data repository that would accept such swaps or forwards, to the [Commodity Futures Trading] Commission pursuant to section 4r within such time period as the [Commodity Futures Trading] Commission may by rule or regulation prescribe.

(iv) BUSINESS STANDARDS.—Notwithstanding a written determination by the Secretary pursuant to clause (i), any party to a foreign exchange swap or forward that is a swap dealer or major swap participant shall conform to the business conduct standards contained in section 4s(h).

(v) SECRETARY.—For purposes of this subparagraph, the term 'Secretary' means the Secretary of the Treasury.

(F) EXCEPTION FOR CERTAIN FOREIGN EXCHANGE SWAPS AND FORWARDS.—

(i) REGISTERED ENTITIES.—Any foreign exchange swap and any foreign exchange forward that is listed and traded on or subject to the rules of a designated contract market or a swap execution facility, or that is cleared by a derivatives clearing organization, shall not be exempt from any provision of this Act or amendments made by the Wall Street Transparency and Accountability Act of 2010 prohibiting fraud or manipulation.

(ii) RETAIL TRANSACTIONS.—Nothing in subparagraph (E) shall affect, or be construed to affect, the applicability of this Act or the jurisdiction of the [Commodity Futures Trading] Commission with respect to agreements, contracts, or transactions in foreign currency pursuant to section 2(c)(2)."

Security-Based Swap: Section 761(a)(6) of the Dodd-Frank Act:

"(68) SECURITY-BASED SWAP.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'security-based swap' means any agreement, contract, or transaction that—

(i) is a swap, as that term is defined under section 1a of the Commodity Exchange Act (without regard to paragraph (47)(B)(x) of such section); and

(ii) is based on—

(I) an index that is a narrow-based security index, including any interest therein or on the value thereof;

(II) a single security or loan, including any interest therein or on the value thereof; or

(III) the occurrence, nonoccurrence, or extent of the occurrence of an event relating to a single issuer of a security or the issuers of securities in a narrow-based security index, provided that such event directly affects the financial statements, financial condition, or financial obligations of the issuer.

(B) RULE OF CONSTRUCTION REGARDING MASTER AGREEMENTS.—The term 'security-based swap' shall be construed to include a master agreement that provides for an agreement, contract, or transaction that is a security-based swap pursuant to subparagraph (A), together with all supplements to any such master agreement, without regard to whether the master agreement contains an agreement, contract, or transaction that is not a security-based swap pursuant to subparagraph (A), except that the master agreement shall be considered to be a security-based swap only with respect to each agreement, contract, or transaction under the master agreement that is a security-based swap pursuant to subparagraph (A).

(C) EXCLUSIONS.—The term 'security-based swap' does not include any agreement, contract, or transaction that meets the definition of a security-based swap only because such agreement, contract, or transaction references, is based upon, or settles through the transfer, delivery, or receipt of an exempted security under paragraph (12), as in effect on the date of enactment of the Futures Trading

Act of 1982 (other than any municipal security as defined in paragraph (29) as in effect on the date of enactment of the Futures Trading Act of 1982), unless such agreement, contract, or transaction is of the character of, or is commonly known in the trade as, a put, call, or other option.

(D) MIXED SWAP.—The term 'security-based swap' includes any agreement, contract, or transaction that is as described in subparagraph (A) and also is based on the value of 1 or more interest or other rates, currencies, commodities, instruments of indebtedness, indices, quantitative measures, other financial or economic interest or property of any kind (other than a single security or a narrow-based security index), or the occurrence, non-occurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence (other than an event described in subparagraph (A)(ii)(III)).

(E) RULE OF CONSTRUCTION REGARDING USE OF THE TERM INDEX.—The term 'index' means an index or group of securities, including any interest therein or based on the value thereof."

Swap Dealer: Section 721(a)(21) of the Dodd-Frank Act:

"(49) SWAP DEALER.—

(A) IN GENERAL.—The term 'swap dealer' means any person who—

(i) holds itself out as a dealer in swaps;

(ii) makes a market in swaps;

(iii) regularly enters into swaps with counterparties as an ordinary course of business for its own account; or

(iv) engages in any activity causing the person to be commonly known in the trade as a dealer or market maker in swaps,

provided however, in no event shall an insured depository institution be considered to be a swap dealer to the extent it offers to enter into a swap with a customer in connection with originating a loan with that customer.

(B) INCLUSION.—A person may be designated as a swap dealer for a single type or single class or category of swap or activities and considered not to be a swap dealer for other types, classes, or categories of swaps or activities.

(C) EXCEPTION.—The term 'swap dealer' does not include a person that enters into swaps for such person's own account, either individually or in a fiduciary capacity, but not as a part of a regular business.

(D) DE MINIMIS EXCEPTION.—The [Commodity Futures Trading] Commission shall exempt from designation as a swap dealer an entity that engages in a de minimis quantity of swap dealing in connection with transactions with or on behalf of its customers. The [Commodity Futures Trading] Commission shall promulgate regulations to establish factors with respect to the making of this determination to exempt."

Security-Based Swap Dealer: Section 761(a)(6) of the Dodd-Frank Act:

"(71) SECURITY-BASED SWAP DEALER.—

(A) IN GENERAL.—The term 'security-based swap dealer' means any person who—

(i) holds themself out as a dealer in security-based swaps;

(ii) makes a market in security-based swaps;

(iii) regularly enters into security-based swaps with counterparties as an ordinary course of business for its own account; or

(iv) engages in any activity causing it to be commonly known in the trade as a dealer or market maker in security-based swaps.

(B) DESIGNATION BY TYPE OR CLASS.—A person may be designated as a security-based swap dealer for a single type or single class or category of security-based swap or activities and considered not to be a security-based swap dealer for other types, classes, or categories of security based swaps or activities.

(C) EXCEPTION.—The term 'security-based swap dealer' does not include a person that enters into security-based swaps for such person's own account, either individually or in a fiduciary capacity, but not as a part of regular business.

(D) DE MINIMIS EXCEPTION.—The [Securities and Exchange] Commission shall exempt from designation as a security-based swap dealer an entity that engages in a de minimis quantity of security-based swap dealing in connection with transactions with or on behalf of its customers. The [Securities and Exchange] Commission shall promulgate regulations to establish factors with respect to the making of any determination to exempt."

Major Swap Participant: Section 721(a)(16) of the Dodd-Frank Act:

"(33) MAJOR SWAP PARTICIPANT.—

(A) IN GENERAL.—The term 'major swap participant' means any person who is not a swap dealer, and—

(i) maintains a substantial position in swaps for any of the major swap categories as determined by the [Commodity Futures Trading] Commission, excluding—

(I) positions held for hedging or mitigating commercial risk; and

(II) positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002) for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan;

(ii) whose outstanding swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or

(iii)(I) is a financial entity that is highly leveraged relative to the amount of capital it holds and that is not subject to capital requirements established by an appropriate Federal banking agency; and

(II) maintains a substantial position in outstanding swaps in any major swap category as determined by the [Commodity Futures Trading] Commission.

(B) DEFINITION OF SUBSTANTIAL POSITION.—For purposes of subparagraph (A), the [Commodity Futures Trading] Commission shall define by rule or regulation the term 'substantial position' at the threshold that the [Commodity Futures Trading] Commission determines to be prudent for the effective monitoring, management, and oversight of entities that are systemically important or can significantly impact the financial system of the United States. In setting the definition under this subparagraph, the [Commodity Futures Trading] Commission shall consider the person's relative position in uncleared as opposed to cleared swaps and may take into consideration the value and quality of collateral held against counterparty exposures.

(C) SCOPE OF DESIGNATION.—For purposes of subparagraph (A), a person may be designated as a major swap participant for 1 or more categories of swaps without being classified as a major swap participant for all classes of swaps.

(D) EXCLUSIONS.—The definition under this paragraph shall not include an entity whose primary business is providing financing, and uses derivatives for the purpose of hedging underlying commercial risks related to interest rate and foreign currency exposures, 90 percent or more of which arise from financing that facilitates the purchase or lease of products, 90 percent or more of which are manufactured by the parent company or another subsidiary of the parent company."

Major Security-Based Swap Participant: Section 761(a)(6) of the Dodd-Frank Act:

"(67) MAJOR SECURITY-BASED SWAP PARTICIPANT.—

(A) IN GENERAL.—The term 'major security-based swap participant' means any person—

(i) who is not a security-based swap dealer; and

(ii)(I) who maintains a substantial position in security-based swaps for any of the major security-based swap categories, as such categories are determined by the [Securities and Exchange] Commission, excluding both positions held for hedging or mitigating commercial risk and positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002) for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan;

(II) whose outstanding security-based swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or

(III) that is a financial entity that—

(aa) is highly leveraged relative to the amount of capital such entity holds and that is not subject to capital requirements established by an appropriate Federal banking agency; and

(bb) maintains a substantial position in outstanding security-based swaps in any major security-based swap category, as such categories are determined by the [Securities and Exchange] Commission.

(B) DEFINITION OF SUBSTANTIAL POSITION.—For purposes of subparagraph (A), the [Securities and Exchange] Commission shall define, by rule or regulation, the term

'substantial position' at the threshold that the [Securities and Exchange] Commission determines to be

prudent for the effective monitoring, management, and oversight of entities that are systemically important or can significantly impact the financial system of the United States. In setting the definition under this subparagraph, the [Securities and Exchange] Commission shall consider the person's relative position in uncleared as opposed to cleared security-based swaps and may take into consideration the value and quality of collateral held against counterparty exposures.

(C) SCOPE OF DESIGNATION.—For purposes of subparagraph (A), a person may be designated as a major security-based swap participant for 1 or more categories of security-based swaps without being classified as a major security-based swap participant for all classes of security-based swaps."

Eligible Contract Participant: Section 1a(18) of the Commodity Exchange Act, 7 U.S.C. 1a(18), as re-designated and amended by Sections 721(a)(9) and 741(b)(10)[5] of the Dodd-Frank Act:

[5] Section 741(b)(10) of the Dodd-Frank Act provides that "Section 1a(19)(A)(iv)(II) of the Commodity Exchange Act (7 U.S.C. 1a(19)(A)(iv)(II)) (as redesignated by section 721(a)(1)) is amended by inserting before the semicolon at the end the following: "provided, however, that for purposes of section 2(c)(2)(B)(vi) and section 2(c)(2)(C)(vii), the term 'eligible contract participant' shall not include a commodity pool in which

"(18) ELIGIBLE CONTRACT PARTICIPANT.—The term 'eligible contract participant' means—

(A) acting for its own account—

(i) a financial institution;

(ii) an insurance company that is regulated by a State, or that is regulated by a foreign government and is subject to comparable regulation as determined by the [Commodity Futures Trading] Commission, including a regulated subsidiary or affiliate of such an insurance company;

(iii) an investment company subject to regulation under the Investment Company Act of 1940 (15 U.S.C. 80a–1 et seq.) or a foreign person performing a similar role or function subject as such to foreign regulation (regardless of whether each investor in the investment company or the foreign person is itself an eligible contract participant);

(iv) a commodity pool that—

(I) has total assets exceeding $5,000,000; and

(II) is formed and operated by a person subject to regulation under this Act or a foreign person performing a similar role or function subject as such to foreign regulation (regardless of whether each investor in the commodity pool or the foreign person is itself an eligible contract

---

any participant is not otherwise an eligible contract participant"." The probable intent of Congress was to amend the definition of "eligible contract participant", which is in paragraph (18)(A)(iv)(II), not paragraph (19)(A)(iv)(II).

participant) provided, however, that for purposes of section 2(c)(2)(B)(vi) and section 2(c)(2)(C)(vii), the term 'eligible contract participant' shall not include a commodity pool in which any participant is not otherwise an eligible contract participant;

(v) a corporation, partnership, proprietorship, organization, trust, or other entity—

(I) that has total assets exceeding $10,000,000;

(II) the obligations of which under an agreement, contract, or transaction are guaranteed or otherwise supported by a letter of credit or keepwell, support, or other agreement by an entity described in subclause (I), in clause (i), (ii), (iii), (iv), or (vii), or in subparagraph (C); or

(III) that—

(aa) has a net worth exceeding $1,000,000; and

(bb) enters into an agreement, contract, or transaction in connection with the conduct of the entity's business or to manage the risk associated with an asset or liability owned or incurred or reasonably likely to be owned or incurred by the entity in the conduct of the entity's business;

(vi) an employee benefit plan subject to the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001 et seq.), a governmental employee benefit plan, or a foreign person performing a similar role or function subject as such to foreign regulation—

(I) that has total assets exceeding $5,000,000; or

(II) the investment decisions of which are made by—

(aa) an investment adviser or commodity trading advisor subject to regulation under the Investment Advisers Act of 1940 (15 U.S.C. 80b–1 et seq.) or this Act;

(bb) a foreign person performing a similar role or function subject as such to foreign regulation;

(cc) a financial institution; or

(dd) an insurance company described in clause (ii), or a regulated subsidiary or affiliate of such an insurance company;

(vii)(I) a governmental entity (including the United States, a State, or a foreign government) or political subdivision of a governmental entity;

(II) a multinational or supranational government entity; or

(III) an instrumentality, agency, or department of an entity described in subclause (I) or (II);

except that such term does not include an entity, instrumentality, agency, or department referred to in subclause (I) or (III) of this clause unless (aa) the entity, instrumentality, agency, or department is a person described in clause (i), (ii), or (iii) of paragraph (17)(A); (bb) the entity, instrumentality, agency, or department owns and invests on a discretionary basis $50,000,000 or more in investments; or (cc) the agreement, contract, or transaction is offered by, and entered into with, an entity that is listed in any of subclauses (I) through (VI) of section 2(c)(2)(B)(ii);

(viii)(I) a broker or dealer subject to regulation under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) or a foreign person performing a similar role or function subject as such to foreign regulation, except that, if the broker or dealer or foreign person is a natural person or proprietorship, the broker or dealer or foreign person shall not be considered to be an eligible contract participant unless the broker or dealer or foreign person also meets the requirements of clause (v) or (xi);

(II) an associated person of a registered broker or dealer concerning the financial or securities activities of which the registered person makes and keeps records under section 15C(b) or 17(h) of the Securities Exchange Act of 1934 (15 U.S.C. 78o--5(b), 78q(h));

(III) an investment bank holding company (as defined in section 17(i) of the Securities Exchange Act of 1934 (15 U.S.C. 78q(i));

(ix) a futures commission merchant subject to regulation under this Act or a foreign person performing a similar role or function subject as such to foreign regulation, except that, if the futures commission merchant or foreign person is a natural person or proprietorship, the futures commission merchant or foreign person shall not be considered to be an eligible contract participant unless the futures commission merchant or foreign person also meets the requirements of clause (v) or (xi);

(x) a floor broker or floor trader subject to regulation under this Act in connection with any transaction that takes place on or through the facilities of a registered entity (other than an electronic trading facility with respect to a significant price discovery contract) or an exempt board of trade, or any affiliate thereof, on which such person regularly trades; or

(xi) an individual who has amounts invested on a discretionary basis, the aggregate of which is in excess of—

(I) $10,000,000; or

(II) $5,000,000 and who enters into the agreement, contract, or transaction in order to manage the risk associated with an asset owned or liability incurred, or reasonably likely to be owned or incurred, by the individual;

(B)(i) a person described in clause (i), (ii), (iv), (v), (viii), (ix), or (x) of subparagraph (A) or in subparagraph (C), acting as broker or performing an equivalent agency function on behalf of another person described in subparagraph (A) or (C); or

(ii) an investment adviser subject to regulation under the Investment Advisers Act of 1940, a commodity trading advisor subject to regulation under this Act, a foreign person performing a similar role or function subject as such to foreign regulation, or a person described in clause (i), (ii), (iv), (v), (viii), (ix), or (x) of subparagraph (A) or in subparagraph (C), in any such case acting as investment manager or fiduciary (but excluding a person acting as broker or performing an equivalent agency function) for another person described in subparagraph (A) or (C) and who is authorized by such person to commit such person to the transaction; or

(C) any other person that the [Commodity Futures Trading] Commission determines to be eligible in light of the financial or other qualifications of the person."

Security-Based Swap Agreement: Section 761(a)(6) of the Dodd-Frank Act:

"(78) SECURITY-BASED SWAP AGREEMENT.—

(A) IN GENERAL.—For purposes of sections 9, 10, 16, 20, and 21A of this Act, and section 17 of the Securities Act of 1933 (15 U.S.C. 77q), the term 'security-based swap agreement' means a swap agreement as defined in section 206A of

the Gramm-Leach-Bliley Act (15 U.S.C. 78c note) of which a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein.

(B) EXCLUSIONS.—The term 'security-based swap agreement' does not include any security-based swap."

By the Securities and Exchange Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Date: August 13, 2010

By the Commodity Futures Trading Commission.

David A. Stawick
Secretary

Date: August 13, 2010

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62723 / August 16, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14008

In the Matter of	
Four Crystal Funding, Inc.	**ORDER INSTITUTING PROCEEDINGS AND NOTICE OF HEARING PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**
Respondent.	

I.

The Securities and Exchange Commission ("Commission") deems it necessary

and hereby are, instituted pursuant to Section 12(j) of the Securities Exchange Act of 1934 ("Exchange Act") against Respondent Four Crystal Funding, Inc. ("Respondent" or "Four Crystal").

II.

After an investigation, the Division of Enforcement alleges that:

A. RESPONDENT

1. Four Crystal Funding, Inc. (CIK No. 0000945481) is a Florida corporation currently located in Weston, Connecticut. Four Crystal has a class of equity securities registered with the Commission pursuant to Section 12(g) of the Exchange Act. Four Crystal is delinquent in its periodic filings with the Commission, having not filed any periodic reports since its predecessor Pro Tech Communications, Inc., filed a Form 10-Q for the period ended June 30, 2006, which reported a net loss of $1,940,433 for the prior three months. Its securities are quoted on the Pink Sheets operated by Pink OTC Markets, Inc. ("Pink Sheets") under the symbol "FCRS."

B. DELINQUENT PERIODIC FILINGS

2. Respondent is delinquent in its periodic filings with the Commission (*see* Chart of Delinquent Filings, attached hereto as Appendix 1). In particular, it has not filed a periodic report with the Commission since August 2006.

3. The Division of Corporation Finance sent a delinquency letter to Respondent requesting compliance with its periodic filing obligations. The Respondent has not filed any periodic report after being sent the delinquency letter.

4. Section 13(a) of the Exchange Act and the rules promulgated thereunder require issuers of securities registered pursuant to Section 12 of the Exchange Act to file with the Commission current and accurate information in periodic reports. Specifically, Rule 13a-1 requires issuers to file annual reports (Form 10-K), and Rule 13a-13 requires issuers to file quarterly reports (Form 10-Q).

5. As a result of the foregoing, Respondent failed to comply with Section 13(a) of the Exchange Act and Rules 13a-1 and 13a-13 thereunder.

III.

In view of the allegations made by the Division of Enforcement, the Commission deems it necessary and appropriate for the protection of investors that public administrative proceedings be instituted to determine:

A. Whether the allegations contained in Section II are true and, in connection therewith, to afford the Respondent an opportunity to establish any defenses to such allegations; and

B. Whether it is necessary or appropriate for the protection of investors to suspend for a period not exceeding twelve months, or to revoke the registration of each class of securities of the Respondent registered pursuant to Section 12 of the Exchange Act.

IV.

IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the questions set forth in Section III hereof shall be convened at a time and place to be fixed, and before an Administrative Law Judge to be designated by further order as provided by Rule 110 of the Commission's Rules of Practice [17 C.F.R. § 201.110].

IT IS HEREBY FURTHER ORDERED that Respondent shall file an Answer to the allegations contained in this Order within ten (10) days after service of this Order, as provided by Rule 220(b) of the Commission's Rules of Practice [17 C.F.R. § 201.220(b)].

If Respondent fails to file the directed Answer, or fails to appear at a hearing after being duly notified, the Respondent may be deemed in default and the proceedings may be determined against it upon consideration of this Order, the allegations of which may be deemed to be true as provided by Rules 155(a), 220(f), 221(f), and 310 of the

Commission's Rules of Practice [17 C.F.R. §§ 201.155(a), 201.220(f), 201.221(f), and 201.310].

This Order shall be served forthwith upon Respondent personally or by certified mail, or by other means of verifiable delivery.

IT IS FURTHER ORDERED that the Administrative Law Judge shall issue an initial decision no later than 120 days from the date of service of this Order, pursuant to Rule 360(a)(2) of the Commission's Rules of Practice [17 C.F.R. § 201.360(a)(2)].

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice. Since this proceeding is not "rule making" within the meaning of Section 551 of the Administrative Procedure Act, it is not deemed subject to the provisions of Section 553 delaying the effective date of any final Commission action.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Attachment

Appendix 1

Chart of Delinquent Filings for Four Crystal Funding, Inc.

Form Type	**Period Ended**	**Due Date**	**Months Delinquent (as of 7/19/2010)**
10-Q	09/30/06	11/14/06	44
10-K	12/31/06	03/31/07	39
10-Q	03/31/07	05/15/07	38
10-Q	06/30/07	08/14/07	35
10-Q	09/30/07	11/14/07	33
10-K	12/31/07	03/31/08	27
10-Q	03/31/08	05/15/08	26
10-Q	06/30/08	08/14/08	23
10-Q	09/30/08	11/14/08	20
10-K	12/31/08	03/31/09	15
10-Q	03/31/09	05/15/09	14
10-Q	06/30/09	08/14/09	11
10-Q	09/30/09	11/14/09	8
10-K	12/31/09	03/31/10	3
10-Q	3/31/09	05/15/10	2

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 16, 2010

IN THE MATTER OF	:	
Four Crystal Funding, Inc.	:	**ORDER OF SUSPENSION OF TRADING**
File No. 500-1	:	

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Four Crystal Funding, Inc. ("Four Crystal") because it has not filed any periodic reports since the period ended June 30, 2006. Four Crystal is quoted on the Pink Sheets operated by Pink OTC Markets, Inc. under the ticker symbol FCRS.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed company, and any equity securities of any entity purporting to succeed to this issuer.

Therefore, it is ordered, pursuant to Section 12(k) of the Securities Exchange Act of 1934, that trading in the securities of the above-listed company, and any equity securities of any entity purporting to succeed to this issuer, is suspended for the period from 9:30 a.m. EDT on August 16, 2010, through 11:59 p.m. EDT on August 27, 2010.

By the Commission.

Elizabeth M. Murphy
Elizabeth M. Murphy
Secretary

COMMODITY FUTURES TRADING COMMISSION

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-62725; File No. 4-609]

Joint Public Roundtable on Governance and Conflicts of Interest in the Clearing and Listing of Swaps and Security-Based Swaps

AGENCIES: Commodity Futures Trading Commission ("CFTC") and Securities and Exchange Commission ("SEC") (each, an "Agency," and collectively, the "Agencies").

ACTION: Notice of roundtable discussion; request for comment.

SUMMARY: On August 20, 2010, commencing at 9:00 a.m. and ending at 12:00 p.m., staff of the Agencies will hold a public roundtable discussion at which invited participants will discuss governance and conflicts of interest in the context of certain authority that Sections 726 and 765 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act") granted to the Agencies respectively. The discussion will be open to the public with seating on a first-come, first-served basis. Members of the public may also listen by telephone. Call-in participants should be prepared to provide their first name, last name, and affiliation. The information for the conference call is set forth below.

- US/Canada Toll-Free: (866) 312-4390
- International Toll: (404) 537-3379
- Conference ID: 94280143

A transcript of the public roundtable discussion will be published on the CFTC's governance rulemaking page at

http://www.cftc.gov/LawRegulation/OTCDerivatives/OTC_9_DCOGovernance.html.

The roundtable discussion will take place in Lobby Level Hearing Room (Room 1000) at the CFTC's headquarters at Three Lafayette Centre, 1155 21st Street, NW, Washington, DC.

FOR FURTHER INFORMATION CONTACT: the CFTC's Office of Public Affairs at (202) 418-5080 or the SEC's Office of Public Affairs at (202) 551-4120.

SUPPLEMENTARY INFORMATION: The roundtable discussion will take place on Friday, August 20, 2010, commencing at 9:00 a.m. and ending at 12:00 p.m. Members of the public who wish to submit their views on the topics addressed at the discussion, or on any other topics related to governance and conflicts of interest in the context of the Act, may do so via:

- paper submission to David Stawick, Secretary, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, N.W., Washington, DC 20581, or Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090; or
- electronic submission to the e-mail address provided on the CFTC's governance rulemaking page (all emails must reference "Dodd-Frank Governance" in the subject field); and/or by email to rule-comments@sec.gov or through the comment form available at: http://www.sec.gov/news/press/2010/2010-148.htm.

All submissions will be reviewed jointly by the Agencies. All comments must be in English or be accompanied by an English translation. All submissions provided to either Agency in any electronic form or on paper will be published on the website of the respective Agency, without review and without removal of personally identifying information. Please submit only information that you wish to make publicly available.

By the Securities and Exchange Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

August 16, 2010

By the Commodity Futures Trading Commission.

David A. Stawick

David A. Stawick
Secretary

August 16, 2010

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62733 / August 16, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13446

In the Matter of **American Skandia Investment Services, Inc.** **Respondent.**	**ORDER APPROVING PLAN OF DISTRIBUTION, APPOINTING FUND ADMINISTRATOR, AND WAIVING BOND**

On April 17, 2009, the Securities and Exchange Commission ("Commission") issued a settled Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order against American Skandia Investment Services, Inc. ("ASISI") finding that ASISI accommodated widespread market timing in American Skandia Trust ("AST") portfolios or sub-accounts that serve as funding vehicles for variable annuities issued by American Skandia Life Assurance Corporation ("ASLAC") from at least January 2000 through in or around September 2003. See Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 203(e) and 203(k) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, Investment Advisers Act Release No. 2867 ("Order"). Among other things, the Commission ordered the Respondent to pay a total of $68 million in disgorgement and civil penalties, which the Respondent paid in full. Pursuant to the Order, ASISI selected Professor Francis E. McGovern, Professor of Law at Duke University, as the Independent Distribution Consultant ("IDC"), to develop a distribution plan for the distribution of disgorgement and penalties (the "Fair Fund"). Since then, the IDC has developed a proposed distribution plan (the "Distribution Plan") in consultation with the staff and ASISI.

The IDC proposed Rust Consulting, Inc. ("Rust") as the Fund Administrator. In accordance with the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1100, *et seq.*, the Distribution Plan proposes a Fund Administrator and sets forth, among other things, procedures for the distribution of proceeds to funds or shareholders of funds; procedures for the administration of the Fair Fund, including provisions for filing tax returns; and a proposed timeframe for the termination of the Distribution Plan.

Rust Consulting, Inc., proposed in the Distribution Plan as the Fund Administrator, has not posted the bond generally required of third parties under Fair Fund Rule 1105(c). Rather, the Plan incorporates several layers of protection for the Fair Fund. Among other things, under the Plan: (1) the Fund Administrator will have no custody, and only limited control, of the Fair Fund; (2) the Fair Fund will be held by the U.S. Treasury Bureau of Public Debt until the funds are transferred to the Escrow Bank[1] immediately before transmittal of checks or electronic transfers to eligible investors; (3) upon transfer from the U.S. Treasury, funds will be held in an escrow account, separate from the Escrow Bank's assets until presentation of a check or electronic transfer, at which time funds will be transferred to a controlled distribution account; (4) presented checks or electronic transfers will be subject to "positive pay" controls before being honored by the Escrow Bank; and (5) both the Escrow Bank and the Fund Administrator will maintain, throughout this process, insurance and/or a financial institution bond that covers errors and omissions, misfeasance and fraud.

On May 13, 2010, the Commission published a "Notice of Proposed Distribution Plan and Opportunity for Comment" ("Notice") pursuant to Rule 1103 of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1103. See Exchange Act Release No. 62106. The Notice advised all interested parties that they may obtain a copy of the Distribution Plan from the Commission's public website, http://www.sec.gov, or by submitting a written request to Christopher R. Conte, Associate Director, United States Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5561.

The Notice also advised that all persons desiring to comment on the Distribution Plan could submit their views, in writing, within thirty (30) days of the date of the Notice, to the Office of the Secretary, United States Securities and Exchange Commission, 100 F Street, N.E., Washington, D.C. 20549-1090; by using the Commission's Internet comment form; or by sending an email to rule-comments@sec.gov. The Commission received no comments on the Distribution Plan and no modification has been made to the Distribution Plan since publication of the Notice.

Accordingly, IT IS HEREBY ORDERED that:

A. Pursuant to Rule 1104 of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. §201.1104, the Distribution Plan is approved.

B. Pursuant to Rule 1105(a) of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1105(a), Rust Consulting, Inc. is appointed as Fund Administrator; and

---

1 The "Escrow Bank" refers to Huntington Bank as defined in paragraph 5 and described in paragraph 54 of the Distribution Plan.

C. The bond requirement of Rule 1105(c) of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1105(c), is waived for good cause shown.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62728 / August 16, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13019

In the Matter of **Gabelli Funds LLC,** **Respondent.**	**ORDER DIRECTING DISBURSEMENT OF FAIR FUND**

On September 11, 2009, the Commission published a Notice of Proposed Plan of Distribution and Opportunity for Comment ("Notice") in connection with this proceeding pursuant to Rule 1103 of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1103. (Exchange Act Release No. 60656). The Notice advised parties they could obtain a copy of the Proposed Plan of Distribution ("Distribution Plan") at www.sec.gov. The Notice also advised that all persons desiring to comment on the Distribution Plan could submit their comments, in writing, within 30 days of the date of the Notice. No comments were received by the Commission in response to the Notice. On December 30, 2009, the Commission issued an Order Approving Distribution Plan. (Exchange Act Rel. No. 61256).

The Distribution Plan provides that the Fair Fund consisting of disgorgement, prejudgment interest, civil penalties, plus any accrued interest less a reserve for expenses and taxes, be transferred by the Commission to U.S. Bank for distribution by the Fund Administrator when a validated list of payees with the identification information required to make the distribution has been received and accepted by the staff. The validated list of payees, which is in the amount of $6,199,426.66, has been received and accepted.

Accordingly, it is ORDERED that the Commission staff shall transfer $6,199,426.66 of the Fair Fund to U.S. Bank, and the Fund Administrator shall distribute such monies to investors, as provided for in the Distribution Plan.

By the Commission.

Elizabeth M. Murphy
Elizabeth M. Murphy
Secretary

Chairman Schapiro not participating

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62729; File No. SR-FINRA-2010-032)

August 16, 2010

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Designation of a Longer Period for Commission Action on Proposed Rule Change Relating to Clearly Erroneous Transactions

On June 17, 2010, the Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 ("Act"),[2] and Rule 19b-4 thereunder,[3] a proposed rule change to amend its rules to set forth clearer standards and curtail its discretion with respect to breaking erroneous trades.

Section 19(b)(2) of the Act[4] provides that within thirty-five days of the publication of notice of the filing of a proposed rule change, or within such longer period as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, the Commission shall either approve the proposed rule change or institute proceedings to determine whether the proposed rule change should be disapproved. The 35th day for this filing was August 2, 2010.[5] The Commission had received an extension of time from FINRA until August 16, 2010.[6]

---

1 15 U.S.C. 78s(b)(1).

2 15 U.S.C. 78a.

3 17 CFR 240.19b-4.

4 15 U.S.C. 78s(b)(2).

5 See Securities Exchange Act Release No. 62341 (June 21, 2010), 75 FR 36756 (June 28, 2010).

6 FINRA submitted through the Commission's Electronic Form 19b-4 Filing System an extension of time period for Commission action through August 16, 2010.

The Commission finds it appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider this proposed rule change, relating to the amendment of clearly erroneous execution rules to provide greater transparency and certainty to the process of breaking trades, and the comment letters that have been submitted in connection with the filing.

Accordingly, the Commission, pursuant to Section 19(b)(2) of the Act,[7] designates August 30, 2010, as the date by which the Commission should either approve or institute proceedings to determine whether to disapprove the proposed rule change.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

---

7 15 U.S.C. 78s(b)(2).

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62730; File Nos. SR-BATS-2010-016; SR-BX-2010-040; SR-CBOE-2010-056; SR-CHX-2010-13; SR-EDGA-2010-03; SR-EDGX-2010-03; SR-ISE-2010-62; SR-NASDAQ-2010-076; SR-NSX-2010-07; SR-NYSE-2010-47; SR-NYSEAmex-2010-60; SR-NYSEArca-2010-58)

August 16, 2010

Self-Regulatory Organizations; BATS Exchange, Inc.; NASDAQ OMX BX, Inc.; Chicago Board Options Exchange, Incorporated; Chicago Stock Exchange, Inc.; EDGA Exchange, Inc.; EDGX Exchange, Inc.; International Securities Exchange LLC; The NASDAQ Stock Market LLC; National Stock Exchange, Inc.; New York Stock Exchange LLC; NYSE Amex LLC; NYSE Arca, Inc.; Notice of Designation of a Longer Period for Commission Action on Proposed Rule Changes Relating to Clearly Erroneous Transactions

On June 17, 2010, each of BATS Exchange, Inc. ("BATS"), NASDAQ OMX BX, Inc. ("BX"), Chicago Board Options Exchange, Incorporated ("CBOE"), Chicago Stock Exchange, Inc. ("CHX"), EDGA Exchange, Inc. ("EDGA"), EDGX Exchange, Inc. ("EDGX"), International Securities Exchange LLC ("ISE"), The NASDAQ Stock Market LLC ("Nasdaq"), National Stock Exchange, Inc. ("NSX"), New York Stock Exchange LLC ("NYSE"), NYSE Amex LLC ("NYSE Amex"), and NYSE Arca, Inc. ("NYSE Arca") (collectively, the "Exchanges") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 ("Act"),[2] and Rule 19b-4 thereunder,[3] proposed rule changes to amend certain of their respective rules to set forth clearer standards and curtail their discretion with respect to breaking erroneous trades.

Section 19(b)(2) of the Act[4] provides that within thirty-five days of the publication of notice of the filing of a proposed rule change, or within such longer period as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and

---

1 15 U.S.C. 78s(b)(1).

2 15 U.S.C. 78a.

3 17 CFR 240.19b-4.

4 15 U.S.C. 78s(b)(2).

publishes its reasons for so finding, the Commission shall either approve the proposed rule change or institute proceedings to determine whether the proposed rule change should be disapproved. The 35th day for the filings submitted by BATS, BX, CBOE, CHX, EDGA, EDGX, ISE, Nasdaq, NSX, NYSE, and NYSE Amex, was August 2, 2010.[5] The 35th day for the filing submitted by NYSE Arca was August 3, 2010.[6] The Commission had received an extension of time from the Exchanges until August 16, 2010.[7]

The Commission finds it appropriate to designate a longer period within which to take action on the proposed rule changes so that it has sufficient time to consider these proposed rule changes, relating to the amendment of clearly erroneous execution rules to provide greater transparency and certainty to the process of breaking trades, and the comment letters that have been submitted in connection with these filings.

---

5 See Securities Exchange Act Release Nos. 62330 (June 21, 2010), 75 FR 36725 (June 28, 2010); 62331 (June 21, 2010), 75 FR 36746 (June 28, 2010); 62332 (June 21, 2010), 75 FR 36749 (June 28, 2010); 62333 (June 21, 2010), 75 FR 36759 (June 28, 2010); 62334 (June 21, 2010), 75 FR 36732 (June 28, 2010); 62336 (June 21, 2010), 75 FR 36743 (June 28, 2010); 62337 (June 21, 2010), 75 FR 36739 (June 28, 2010); 62338 (June 21, 2010), 75 FR 36762 (June 28, 2010); 62339 (June 21, 2010), 75 FR 36765 (June 28, 2010); 62340 (June 21, 2010), 75 FR 36768 (June 28, 2010); and 62342 (June 21, 2010), 75 FR 36752 (June 28, 2010).

6 See Securities Exchange Act Release No. 62335 (June 21, 2010), 75 FR 37494 (June 29, 2010).

7 The Exchanges submitted through the Commission's Electronic Form 19b-4 Filing System extensions of the time period for Commission action through August 16, 2010.

Accordingly, the Commission, pursuant to Section 19(b)(2) of the Act,[8] designates August 30, 2010, as the date by which the Commission should either approve or institute proceedings to determine whether to disapprove the proposed rule changes.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

8 15 U.S.C. 78s(b)(2).

Commissioner Walter and Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3069 / August 18, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14010

In the Matter of

EZRA C. LEVY,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against Ezra C. Levy ("Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(f) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. From approximately 2000 until October 2009, Respondent was the Chief Financial Officer of Boston Provident, L.P., an unregistered investment adviser located in New York, New York ("Boston Provident"). Levy, 33 years old, is a resident of Ocean Township, New Jersey.

2. On March 11, 2010, Respondent pled guilty to one count of securities fraud in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, and one count of wire fraud in violation of Title 18 of the United States Code, Section 1343, before the United States District Court for the Southern District of New York, in United States v. Ezra Levy, Case No. 10-CR-199 (PKC). On June 29, 2010, a judgment in the criminal case was entered against Respondent. Respondent was sentenced to a prison term of 67 months followed by three years of supervised release and ordered to make restitution in the amount of $2,987,000, and to pay a fine of $12,500 and an assessment of $200.

3. The counts of the criminal information to which Respondent pled guilty alleged, inter alia, that, first, in June 2009, Respondent caused his employer firm to purchase stocks at inflated prices from Respondent's personal brokerage account, resulting in a gain to Respondent of over $537,000; and, second, that between February 2006 and October 2009, Respondent diverted approximately $2.45 million owed to his employer into a bank account that Respondent controlled and then used that money to, among other things, pay personal expenses.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act, that Respondent Ezra C. Levy be, and hereby is barred from association with any investment adviser.

Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9135 / August 18, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14009

In the Matter of STATE OF NEW JERSEY, Respondent.	ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 ("Securities Act"), against the State of New Jersey (the "State," "New Jersey" or "Respondent").

II.

In anticipation of the institution of these proceedings, the State has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, which are admitted, the State consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and the State's Offer, the Commission finds that:

Summary

1. This matter involves New Jersey's violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act in connection with the offer and sale of over $26 billion in municipal bonds from August 2001 through April 2007. In 79 municipal bond offerings, the State misrepresented and failed to disclose material information regarding its under funding of New Jersey's two largest

pension plans, the Teachers' Pension and Annuity Fund ("TPAF") and the Public Employees' Retirement System ("PERS"). More specifically, the State did not adequately disclose that it was under funding TPAF and PERS, why it was under funding TPAF and PERS, or the potential effects of the under funding.

2. In disclosure documents prepared in connection with each of the bond offerings, including preliminary official statements, official statements,[1] and Treasurer's Annual Reports[2] (collectively, "disclosure documents" or "bond offering documents"), the State made material misrepresentations and omissions regarding: (1) legislation adopted in 2001 (the "2001 legislation") which increased retirement benefits for employees and retirees enrolled in TPAF and PERS; (2) special Benefit Enhancement Funds ("BEFs") created by the 2001 legislation initially intended to fund the costs associated with the increased benefits; (3) the State's use of the BEFs as part of a five-year "phase-in plan" to begin making contributions to TPAF and PERS; and (4) the State's alteration and eventual abandonment of the five-year phase-in plan. These misrepresentations and omissions created the fiscal illusion that TPAF and PERS were being adequately funded and masked the fact that New Jersey was unable to make contributions to TPAF and PERS without raising taxes or cutting other services, or otherwise impacting the budget. Accordingly, disclosure documents failed to provide adequate information for investors to evaluate the State's ability to fund TPAF and PERS or the impact of the State's pension obligations on the State's financial condition.

Respondents and Related Entities

3. New Jersey possesses all powers, functions, rights, privileges and immunities authorized by the New Jersey Constitution and the State's laws, including the power to issue debt. The State has approximately 8.7 million residents, and is the second wealthiest State based on per capita personal income.

4. Teachers' Pension and Annuity Fund is a defined benefit plan[3] operated by the

[1] An official statement is a document prepared by an issuer of municipal bonds that discloses material information regarding the issuer and the particular offering. A preliminary official statement is a preliminary version of the official statement which is used to describe the proposed new issue of municipal securities prior to the determination of the interest rate(s) and offering price(s). The preliminary official statement may be used to gauge interest in an issue and is often relied upon by potential purchasers in making their investment decisions.

[2] Treasurer's Annual Reports are continuing disclosures filed by the State with the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system ("EMMA") under Rule 15c2-12 of the Securities Exchange Act of 1934 ("Exchange Act").

[3] A defined benefit plan is a pension plan that specifies the amount of pension benefits to be provided at a future date based on various factors, including age, years of service, and compensation.

State to provide retirement, death, and disability benefits to its members.[4] TPAF is the State's largest pension plan, and, as of June 30, 2009, had an actuarial value of assets of more than $34 billion. As of June 30, 2009, TPAF had an active membership of 157,109 as well as 78,782 retirees and beneficiaries receiving annual pensions totaling more than $2.8 billion.

5. Public Employees' Retirement System is a defined benefit plan operated by the State to provide retirement, death, and disability benefits to its members. PERS is the State's second largest pension plan, and, as of July 1, 2009, had an actuarial value of assets of more than $28 billion. In addition to the State, local governments within New Jersey participate as employers. As of July 1, 2009, the State portion of PERS had assets of more than $10 billion. As of July 1, 2009, PERS had an active membership of 316,849[5] as well as 136,957 retirees and beneficiaries[6] receiving annual pensions totaling more than $2.2 billion.

State Law Requires Certain Annual Calculations and
<u>Measures of New Jersey's Pension Plans</u>

6. State law regulates the administration of New Jersey's pension plans. The Division of Pensions and Benefits ("DPB"), a division of New Jersey's Department of the Treasury ("Treasury"), administers all aspects of TPAF and PERS, except the investment of pension plan assets. Plan assets consist of contributions by employers, including the State, contributions by TPAF's and PERS' members, and investment returns. Liabilities of the plans consist of pension benefits owed to current and retired TPAF and PERS members based on past years of service and the plans' administrative expenses.

7. State law requires that TPAF and PERS engage actuaries to conduct actuarial valuations at the end of each fiscal year – June 30. These valuations include calculating the "annual required contribution" and the "statutory contribution." While the annual required contribution is governed by industry standards,[7] the statutory contribution is calculated in accordance with State law. According to State law and as disclosed in bond offering documents, employers are required to contribute to TPAF and PERS at an actuarially determined rate.

8. In addition to calculating both the annual required contribution and the statutory contribution, an actuarial valuation also calculates the actuarial accrued liability and the actuarial

---

[4] Plan members include employees in active service, terminated employees who have accumulated benefits but are not yet receiving them, and retired employees and beneficiaries currently receiving benefits.

[5] This includes 93,283 State employees and 223,566 employees from local employers.

[6] This includes 43,764 State employees and 93,193 employees from local employers.

[7] The annual required contribution is calculated in accordance with Statements 25 and 27 of the Governmental Accounting Standards Board ("GASB").

value of assets of each of the pension plans.[8] The actuarial accrued liability estimates on the basis of demographic and economic assumptions the present value of pension benefits TPAF and PERS owe to their active and retired members based on past years of service. The actuarial value of assets is the value of cash, investments, and other property belonging to a pension plan using a five-year smoothing method that smoothes the difference between the market value of assets and the actuarial value of assets over a five-year period to prevent short-term fluctuations that may result from economic and market conditions. For each year, this method recognizes 20 percent of the investment gains or losses for the prior five years.

9. The actuarial valuations compare the actuarial accrued liability with the actuarial value of assets for TPAF and PERS and any excess of that liability over the assets forms an unfunded actuarial accrued liability ("UAAL"). The UAAL is the State's unfunded obligation to TPAF's and PERS' members for past service. The actuarial valuations also express the percentages that the plans are funded through a "funded ratio" which represents the quotient obtained by dividing the actuarial value of assets of TPAF and PERS by the actuarial accrued liability of each plan. The trend in the funded ratio provides information as to whether the financial strength of a pension plan is improving or deteriorating over time. The financial strength of a pension plan is generally improving if the funded ratio is increasing. During the relevant time period, New Jersey's funded ratio decreased significantly. As of June 30, 2001, TPAF had a funded ratio of 108 percent and the State portion of PERS had a funded ratio of 112.5 percent. As of June 30, 2009, TPAF had a funded ratio of 63.8 percent and an unfunded actuarial accrued liability of $18.7 billion, and the State portion of PERS had a funded ratio of 56.4 percent and an unfunded actuarial accrued liability of $8.2 billion.[9]

10. The statutory contribution for TPAF and PERS consists of two main components: (1) the normal cost, which represents the portion of the present value of pension benefits that are allocated to active members' current year of service, and (2) an amortized portion of the UAAL. TPAF and PERS use a statutorily set closed 30-year amortization period[10] for calculating the amount of the UAAL that is included in the statutory contribution.[11]

---

[8] The actuarial valuations calculate the actuarial accrued liability and actuarial value of assets in accordance with New Jersey statutes and Statements 25 and 27 of GASB.

[9] Although contributions by State and local governments to PERS are invested together, PERS segregates the actuarial accrued liabilities between the State and local governments.

[10] As of the June 30, 2006 actuarial valuations, the State used an open 30-year amortization period.

[11] The State's amortization method amortizes the UAAL over a 30-year period as a level percentage of the projected payroll or "level percent of pay." Under this method, the UAAL amortization payments are calculated so that they are a constant percentage of the projected payroll of active members over the 30-year period. Because the actuarial valuations assume a payroll growth rate of 4 percent each year, the amortization payments increase over time.

11. Although bond offering documents disclosed that the State was required to contribute to TPAF and PERS at an actuarially determined rate and discussed the budget process generally, bond offering documents did not adequately disclose that the amount actually contributed to the pension plans is subject to the Governor's budget request and annual appropriations by the State legislature. Each year, the Governor, based on recommendations received from Treasury, presents a budget request to the legislature, which may include a request for the State's pension contribution. Once the legislature adopts the budget, it is signed into law as the Appropriations Act for the coming fiscal year. In adopting the budget, the legislature is not required to follow the recommendations of the actuaries or the Governor in determining the State's contribution to the pension plans. The appropriations for the State contribution to the pension plans are credited to "Contingent Reserve Funds," existing funds within TPAF and PERS.

12. State law requires members of TPAF and PERS to contribute annually to the pension plans. Member contributions are based on a percentage of compensation. The State legislature must approve any changes to employer or member contributions. State law also provides that any changes in the pension benefits for TPAF's and PERS' members or any changes in the funding methods of the plans must be approved by the State legislature. In addition, each pension related bill submitted to the State legislature must be accompanied by a fiscal note stating the cost of the proposal.

New Jersey Has Access to the National
Public Markets through Municipal Bond Offerings

13. From August 2001 through April 2007, New Jersey issued over $26 billion in municipal bonds in approximately 79 offerings. The State's preliminary official statements and official statements contained an appendix with several subsections, three of which provided information relating to the State's funding of TPAF and PERS (the "State Appendix"). Appendix I provided financial and other information relating to the State, including a section titled "Financing Pensions." The Financing Pensions section provided a description of the State's pension plans, a description of pension related legislation, a summary of the State's contributions to its pension plans for the current and upcoming fiscal years, and a table setting forth the actuarial accrued liability and the actuarial value of assets from the most recent actuarial valuations for each of the State's pension plans. Appendix I-A, which was an excerpt from the State's most recent Comprehensive Annual Financial Report ("CAFR"),[12] contained a footnote to the financial statements titled "Retirement Systems" that provided general information regarding the State's pension plans, including significant legislation and contribution requirements, as well as a table setting forth statistical information relating to the pension plans. Appendix I-D, an unaudited appendix found in the back of the State's disclosure documents, contained statistical tables for each of the State's three largest pension plans, including TPAF and PERS, that provided the actuarial value of assets and accrued liabilities, and the funded ratio for the previous six years.

14. Various divisions and offices within Treasury were responsible for the pension funding disclosures in the State Appendix. The updating of the pension funding sections generally

[12] The State's CAFR included audited financial statements prepared pursuant to standards established by GASB.

occurred three times a year – following the issuance of the Governor's budget message, after the passage of the Appropriations Act, and following the issuance of the actuarial valuations. At these times, various divisions and offices within Treasury updated their sections of the State Appendix. They viewed the updating of the pension funding sections as a routine process, requiring the insertion of new numbers or facts into an existing document. The DPB updated the pension disclosures at the request of the Office of Public Finance ("OPF"), another office of the Treasury. The OPF inserted the new information into the State Appendix without verifying the information. The Office of Management and Budget ("OMB") included in the State's CAFR the pension fund related excerpts which were also found in the State Appendix.

15. Prior to the release of an official statement, the State Treasurer, or his designee, signed a Rule 10b-5 certification, certifying that the official statement did not contain any material misrepresentations or omissions. During the relevant time period, the Treasurers did not read official statements, and relied on their staff to ensure the accuracy of information contained in the documents.

16. Treasury had no written policies or procedures relating to the review or update of the bond offering documents. In addition, Treasury did not provide training to its employees concerning the State's disclosure obligations under the accounting standards or the federal securities laws. Accordingly, the State's procedures were inadequate for ensuring that material information concerning TPAF and PERS or the State's financing of TPAF and PERS was disclosed and accurate in bond offering documents.

New Jersey Did Not Adequately Disclose the Creation of the BEFs

17. On June 29, 2001, the State legislature approved legislation (P.L. 2001, c. 133) that, effective November 1, 2001, increased retirement benefits for employees and retirees enrolled in TPAF and PERS by 9.09 percent. In order to fund the enhanced benefits, without increased costs to the State or taxpayers, the legislation revalued TPAF and PERS assets to reflect their full market value as of June 30, 1999, near the height of the bull market.[13] Bond offering documents did not disclose the retroactive mark-to-market revaluation of the pension assets under the 2001 legislation until March 2003 or the reason for the reevaluation. More specifically, bond offering documents did not disclose that the State used the market value as of June 30, 1999 in order to make it appear that the State could afford the benefit improvements.

18. The legislation contemplated that the increased assets resulting from the retroactive mark-to-market revaluation would be used to offset the additional liabilities created by the increased benefits. The additional liabilities included the accrued liability resulting from providing the increased benefits to existing members and retirees as well as the normal cost to ensure that the future liability for the benefit enhancement was funded.

[13] In the actuarial valuations as of June 30, 1999 for TPAF and PERS, the actuarial value of assets was replaced with the market value of assets. Subsequent actuarial valuations, including actuarial valuations as of June 30, 2000 and June 30, 2001, applied the five-year smoothing method.

19. The legislation created "benefit enhancement funds" or BEFs in TPAF and PERS to set aside a portion of the increased assets or "excess valuation assets"[14] to pay the future annual normal cost associated with the enhanced benefits. After the increased assets were used to fund the accrued liability, a portion of the remaining excess valuation assets were placed in the BEFs to cover the future costs associated with the enhanced benefits. Bond offering documents did not disclose the creation of the BEFs until March 2003.

20. The BEFs were special accounts within TPAF and PERS. Each of the BEFs was credited with excess valuation assets, from the Contingent Reserve Funds, which are existing funds within TPAF and PERS used to hold employer contributions, which excess valuation assets resulted from the revaluation in 2001.

21. On July 11 and 13, 2001, approximately two weeks after the passage of the 2001 legislation, the Office of Legislative Services ("OLS")[15] issued fiscal notes analyzing the impact of the Assembly and Senate bills which had been adopted as the 2001 legislation. The fiscal notes acknowledged that valuing the pension assets as of June 30, 1999 did not reflect recent market losses in TPAF and PERS. The fiscal notes further acknowledged that, had the 2001 legislation revalued the pension assets as of April 30, 2001 rather than June 30, 1999, the remaining balance of excess assets in TPAF and PERS would have been $2.4 billion less. Bond offering documents did not disclose the $2.4 billion decline in the market value of the pension assets used to create the BEFs.

22. Bond offering documents did not disclose the reason for and impact of the retroactive mark-to-market revaluation of the pension assets. By revaluing TPAF and PERS assets and creating the BEFs to fund the ongoing costs of the benefit enhancements, the State gave the false appearance that it could afford the increased benefits. The revaluation of the pension assets to reflect their full market value as of June 30, 1999 resulted in a significant difference between the actuarial value and market value of assets in TPAF and PERS. Because the State's contributions to TPAF and PERS are based on the actuarial value of assets, the revaluation created the false appearance that the plans were "fully funded" and allowed the State to justify not making contributions to the pension plans despite the fact that the market values of the plans' assets were rapidly declining.

23. On May 25, 2005, the State's Acting Governor created the Benefits Review Task Force to examine and make recommendations regarding employee benefits. On December 1, 2005, the New Jersey Benefits Review Task Force issued its final report (the "Benefits Review Task Force Report") which offered strong criticism of the State's pension funding practices. In particular, the report recommended that the State stop using actuarial and valuation "gimmicks," like the State's alteration of the valuation method in the 2001 legislation. The report advised that

---

[14] Excess valuation assets is a term defined by New Jersey statute (P.L. 1997, c. 115), which refers to the difference between the valuation assets and the actuarial accrued liability, and other enumerated deductions.

[15] OLS is a nonpartisan agency of the State legislature that provides support services to the legislature and its members.

"[m]ethodologies for determining pension fund values and contribution requirements should not again be changed in order to mask the true cost of benefit enhancements." The Benefits Review Task Force Report also concluded that the State must regularly contribute to its pension plans and end its use of "pension holidays" – not contributing to its pension plans.

24. The Benefits Review Task Force Report was publicly available and published on the Benefit Review Task Force's website. New Jersey, however, did not disclose the existence of, or the findings from, the Benefits Review Task Force Report in its bond offering documents.

New Jersey Faced Financial Challenges Due, in Part, to Its
<u>Historical Failure to Contribute to TPAF and PERS</u>

25. During fiscal year 2002, the State learned from the actuaries for TPAF and PERS that New Jersey would be required to begin contributing to the State's pension plans in fiscal year 2004 based on the actuaries' calculations.[16] Between fiscal years 1997 and 2003, the State had made no or only minimal contributions to TPAF and PERS because based upon the actuarial value of assets, both plans were fully or over funded prior to fiscal year 2003. From 1997 through 2003, the State did not contribute approximately $916.4 million and $487.4 million to TPAF and PERS, respectively. During this period and continuing through 2006, in the context of the State's budgetary process, the State viewed monies not contributed to pension funds as "savings" in that any monies not contributed could be used for other budgetary purposes.

26. Beginning in fiscal year 2003, TPAF and PERS experienced a significant increase in each plan's UAAL and a decrease in the funded ratios. TPAF and the State portion of PERS went from being over funded to having UAALs of $2.7 billion and $1.1 billion, respectively. TPAF's funded ratio decreased from 103.9 percent in fiscal year 1997 to 92.7 percent in fiscal year 2003. The funded ratio for the State portion of PERS decreased from 105.8 percent in fiscal year 1997 to 90.7 in fiscal year 2003. The significant change in the financial health of TPAF and PERS was due to a variety of factors, including, the State's failure to contribute to the plans since 1997, market declines, and the enactment of various benefit enhancements, including the 2001 legislation.

27. After a seven-year pension holiday, during which virtually no monies were appropriated in the State's budget for pensions, the State recognized that it would have to begin contributing to TPAF and PERS. The State, however, now faced significant budget pressures which made it difficult for New Jersey to fund its pension plans absent cutting other programs and services, or raising taxes. Following Treasury's recommendation, the Governor requested and the legislature provided in the annual Appropriations Act that the BEFs be used in lieu of the State contributing to TPAF and PERS.

---

[16] Actuarial valuations of TPAF and PERS are completed approximately 6 to 8 months after the end of a fiscal year. Because of the delay, the statutory contribution calculated by the actuaries applies not to the fiscal year immediately following the fiscal year covered by the actuarial valuations, but to the second fiscal year. For example, the statutory contribution in the actuarial valuations as of June 30, 2003 applied to the fiscal year ended June 30, 2005.

New Jersey Continued to Forego Making Contributions to
Its Pension Plans Through the Use of the BEFs and the Five-Year Phase-In Plan

28. In 2003, while preparing the 2004 fiscal year budget, the State, faced with increased UAALs and declining funded ratios, had to choose between making contributions to the pension plans, or raising taxes or reducing spending in other areas. Accordingly, Treasury recommended, and the State announced, a five-year phase-in plan, in conjunction with using the BEFs, designed to gradually put New Jersey on track to making the State's full statutory contributions to its pension plans. Under the initial five-year phase-in plan, the State would contribute, subject to Constitutional provisions restricting each legislature's ability to mandate spending by future legislatures, 20 percent of the required statutory contribution to its pension plans in fiscal year 2004, 40 percent in fiscal year 2005, 60 percent in fiscal year 2006, 80 percent in fiscal year 2007, and 100 percent in fiscal year 2008. Beginning with fiscal year 2008, the State would be making the full statutory contribution to its pension plans.

29. Disclosures in bond offering documents regarding the State's five-year phase-in plan and use of the BEFs likely falsely led investors to believe that: (1) the State would be contributing to TPAF and PERS in fiscal years 2004, 2005, and 2006; (2) the State had a plan for making its full statutory contributions; and (3) the State would begin making full statutory contributions in fiscal year 2008.

30. Rather than making phase-in contributions to the pension plans, beginning in fiscal year 2004, the State began using the BEFs in conjunction with the five-year phase-in plan. The State continued to use the BEFs as part of the phase-in plan in fiscal years 2005 and 2006. As a result, the State did not contribute any monies to TPAF and PERS in fiscal years 2004 and 2005. In fiscal year 2006, the State did not contribute to PERS, but did contribute a minimal amount to TPAF to cover the portion of the State's contribution not covered by the BEF.

31. Bond offering documents did not disclose that the State was not contributing to TPAF and PERS during this time. When assets from the BEFs were used to fund the State's pension contributions in fiscal years 2004, 2005, and 2006, funds were transferred from the BEFs back to the Contingent Reserve Funds, the original source of the assets in the BEFs. These inter-fund transfers created the false appearance that the State was making contributions to TPAF and PERS, when no actual contributions were being made. Bond offering documents did not disclose that the BEFs allowed the State to forego making contributions to TPAF and PERS. Rather, disclosures in bond offering documents created the false impression that the BEFs were being used to make New Jersey's pension contributions even though no incremental funds were being received by TPAF and PERS. Disclosure documents misleadingly referred to the BEFs as "reserves" that were being utilized to fund the State's contributions to TPAF and PERS which created the misleading impression that the State was making cash contributions to its pension plans.

32. Although bond offering documents referenced the BEFs in connection with the State's contributions, they never disclosed what they were, how they were being used, or why they

were being used. Bond offering documents did not disclose that the State was using the BEFs in conjunction with a five-year phase-in plan because of significant budgetary constraints, and was unable to contribute to TPAF and PERS. In addition, bond offering documents did not disclose the impact of using the BEFs as part of the five-year phase-in plan. The State recognized that delaying the resumption of the State's contributions could result in substantially increasing the pension plans' unfunded liabilities in the future. The State also recognized that by depleting the BEFs, the State would now be faced with paying the normal costs of the enhanced benefits granted by the 2001 legislation. More than $704.2 million was used from the BEFs to fund the State's fiscal year 2004, 2005, and 2006 pension obligations, and thus this amount was no longer available to offset the future costs of the benefit enhancement legislation.

33. By the end of fiscal year 2006, the State had depleted the BEFs. Bond offering documents did not disclose that the State, during each budget cycle, intended to forego making contributions to TPAF and PERS until it had exhausted the BEFs. By disclosing that the State had adopted a five-year phase-in plan, the bond offering documents gave the impression that the State would be contributing its full statutory contributions to TPAF and PERS by fiscal year 2008.

New Jersey Altered and Then Abandoned
the Five-Year Phase-In Plan Because of Financial Difficulties

34. Although New Jersey's bond offering documents referenced the five-year phase-in plan, the State treated the phase-in plan as a flexible plan that could be altered on a year-to-year basis depending on other budgetary demands. Because other budgetary priorities existed, the State's contributions to TPAF and PERS were reduced to 30 percent of the statutory contribution in fiscal year 2005 and 40 percent in fiscal year 2006. Bond offering documents did not disclose the changes to the phase-in plan or the reasons for the State's reduced contributions. These reduced contributions increased, in part, the UAALs for TPAF and the State portion of PERS by $8.2 billion and $3 billion, respectively.

35. Funding for TPAF and PERS was governed by the annual Appropriations Act. The Appropriations Act for fiscal years 2004, 2005, and 2006 also set forth the State's use of the BEFs. In fiscal year 2004, the Appropriations Act specified the amounts to be used from the BEFs in lieu of the State's contributions to TPAF and PERS. However, the Appropriations Act for fiscal years 2005 and 2006 did not identify the amounts to be used from the BEFs or the phase-in percentages. Rather, for those years, the Appropriations Act provided that the Treasurer would determine the amount to be used from the BEFs.

36. The language in the Appropriations Act for fiscal years 2005 and 2006 gave the Treasurer the flexibility to alter the amount of the BEFs to be used to cover the State's contributions to TPAF and PERS, up until the last day of the fiscal year when the contributions were due. In addition, this language gave the Treasurer the ability to alter the phase-in percentages under the phase-in plan. This was particularly important, since by adjusting the amount of the BEFs to be used in fiscal year 2005 and the phase-in percentage, the Treasurer was able to ensure that there were sufficient assets in the BEFs in fiscal year 2006 to cover all or almost all of the State's contributions to TPAF and PERS. In fiscal year 2005, the Treasurer exercised his authority

under the Appropriations Act by reducing the amount of the State's contributions to TPAF and PERS, and thus the phase-in percentage, following the enactment of the Appropriations Act. This change in the phase-in plan, however, was not disclosed in bond offering documents.

37. The State recognized that because of severe budgetary constraints, it would not be able to achieve full funding of its pension plans by fiscal year 2008 without cutting State services or finding other sources of revenue. In fact, the State only contributed 57.5 percent of the required statutory contribution to its pension plans in fiscal year 2007 and 50 percent in fiscal year 2008.

38. The State abandoned its five-year phase-in plan in approximately May 2006. Bond offering documents did not disclose that the State had abandoned the five-year phase-in plan. Rather, the State stopped using the term "five-year" when referring to the phase-in plan in disclosure documents. The State's continued use of the term "phase-in plan" gave the false impression that New Jersey still had a plan to achieve full statutory contributions. Moreover, bond offering documents did not disclose that New Jersey was unable to fully implement the five-year phase-in plan without causing New Jersey to suffer severe economic hardship.

New Jersey Failed to Provide Certain Present and
<u>Historical Financial Information Regarding Its Pension Funding</u>

39. The State's bond offering documents contained inadequate information regarding the State's present and historical contributions to TPAF and PERS. Statistical tables for TPAF and PERS found in Appendix I-D set forth the amount of the State's contributions for the most recent fiscal year and the prior five fiscal years. This information, however, was misleading to investors because the amounts set forth included pension contributions, if any, as well as payments made by the State to members of TPAF and PERS for post-retirement medical benefits.[17] This contribution information conflicted with other statistical information found in the Retirement Systems footnote of Appendix I-A, which showed the actual pension contributions made by the State, but did not include payments for post-retirement medical benefits, for the most recent fiscal year as well as the two prior fiscal years. In addition, the State's bond offering documents lacked sufficient information for investors to understand the State's historical failure – since 1997 – to contribute to TPAF and PERS.

40. Appendix I-A of the State's disclosure documents also excluded a key statistical table from the State's CAFR called the "Required Supplementary Information Schedule of Funding Progress" ("RSI Schedule"), which is defined by GASB. The RSI Schedule is designed to provide a long-term actuarial perspective on the State's funding of its pension plans. The RSI Schedule provided important financial information regarding TPAF and PERS for the three prior fiscal years, including the UAAL and the UAAL as a percentage of covered payroll.[18] The ratio of

---

[17] Under statutes for TPAF and PERS, the State's contributions for post-retirement medical benefits flowed through the pension plans.

[18] Covered payroll includes all elements of compensation paid to active employees on which contributions to the pension plans are based.

UAAL to covered payroll is a measure of the significance of the UAAL relative to the capacity to pay it. The trend in the ratio provides information as to whether the financial strength of the pension plan is improving or deteriorating over time. The financial strength of a pension plan is generally improving if the ratio of UAAL to covered payroll is decreasing. In fact, from 2002 through 2007, the UAAL as a percentage of covered payroll steadily increased. The UAAL and the UAAL to covered payroll for TPAF and PERS is shown below.

TPAF

Fiscal Year	UAAL	UAAL as a Percentage of Covered Payroll
2002	$(1,654,591)	0.0%
2003	$2,731,906,950	35.5%
2004	$5,813,899,790	72.2%
2005	$9,178,537,424	108.6%
2006	$11,008,573,863	125.8%
2007	$12,446,668,618	137.1%

PERS (State Portion)

Fiscal Year	UAAL	UAAL as a Percentage of Covered Payroll
2002	$(312,599,482)	(8.9)%
2003	$1,112,345,981	31.1%
2004	$1,926,870,843	51.4%
2005	$2,801,180,057	69.5%
2006	$4,129,039,284	97.1%
2007	$5,004,619,993	112.8%

41. The bond offering documents failed to provide information regarding the actuarial methodology used by the State to calculate the actuarial value of assets, and the impact of using this methodology on the State's funding of its pension plans. The bond offering documents did not disclose the effect of the State's use of a five-year smoothing method to measure the actuarial value of assets. As a result of the 2001 legislation and market declines, the actuarial value of assets exceeded the market value of assets for TPAF and PERS, resulting in net unsmoothed losses in both plans beginning in fiscal year 2002. The ratio of the actuarial value of assets to market value of assets for TPAF and PERS is shown below.

Actuarial Value as a Percent of Market Value

Fiscal Year	TPAF	PERS
2002	129.5%	126.8%
2003	131.0%	127.7%
2004	121.0%	118.3%
2005	117.4%	113.9%
2006	112.8%	106.7%

2007	104.7%	101.9%

Since the State's contributions to TPAF and PERS are based on the actuarial value of assets, the significant difference between the actuarial value of assets and the market value of assets reduced the State's statutory contributions to the pension plans.

42. The bond offering documents also failed to provide information regarding the actuarial methodology used by the State to calculate the actuarial accrued liabilities of TPAF and PERS, and the impact of using this methodology on the State's funding of its pension plans. The bond offering documents did not disclose the effect of the State's use of a closed 30-year amortization period[19] based on a level percent of pay for measuring the actuarial accrued liability. Under this recognized actuarial method, the UAALs of TPAF and PERS will continue to rise indefinitely even if the State were to contribute the full statutory contribution to the pension plans. Under New Jersey statute, if the UAALs for TPAF and PERS increase from one year to the next, the actuarial valuations will continue to use the full 30-year amortization period. As a result, the State has been unable to and will continue to be unable to effectively amortize TPAF's and PERS' UAALs.

43. In addition, although available in actuarial reports for TPAF and PERS, the bond offering documents did not provide asset and funded ratio information on a market value basis. Because of the significant difference between the actuarial value and market value of assets in TPAF and PERS, the actuarial value did not accurately present the current value of the pension plans. Rather, the actuarial value of assets for TPAF and PERS provided a limited measure of the pension plans' financial health since they did not fully reflect the effects of the 2001 legislation or market declines. Investors lacked sufficient information to assess the current financial health of TPAF and PERS as a result of the absence of asset and funded ratio information on a market value basis. New Jersey's historical funded ratios using actuarial value of assets and market value of assets are shown below:

TPAF

Fiscal Year	Actuarial Value of Assets	Market Value of Assets	Funded Ratio (actuarial value)	Funded Ratio (market value)
2002	$35,148,246,433	$27,121,744,264	100.0%	77.2%
2003	$34,651,825,932	$26,447,330,285	92.7%	70.7%
2004	$34,633,790,549	$28,618,463,144	85.6%	70.8%
2005	$34,789,389,875	$29,610,249,605	79.1%	69.0%
2006	$35,531,294,790	$31,495,000,296	76.4%	69.3%
2007	$36,714,578,745	$35,070,757,170	74.7%	72.9%

[19] As of the June 30, 2006 actuarial valuations, the State used an open 30-year amortization period.

PERS (State Portion)

Fiscal Year	Actuarial Value of Assets	Market Value of Assets	Funded Ratio (actuarial value)	Funded Ratio (market value)
2002	$11,073,156,965	$8,727,927,022	102.9%	81.1%
2003	$10,829,953,189	$8,479,326,527	90.7%	71.0%
2004	$10,693,508,592	$9,038,299,523	84.7%	71.6%
2005	$10,631,348,826	$9,325,929,009	79.1%	69.4%
2006	$10,668,645,162	$9,996,185,459	72.1%	67.6%
2007	$11,024,255,608	$10,817,111,560	68.8%	67.5%

New Jersey Enhances Its Pension Funding Disclosures

44. Subsequent to an April 2007 news article that raised questions regarding disclosures in the State's bond offering documents relating to New Jersey's funding of its pensions, the State hired disclosure counsel to advise the State on an on-going basis regarding its disclosure obligations under the federal securities laws. During 2007 and early 2008, the State, with the assistance of disclosure counsel, reviewed its bond offering documents and enhanced its disclosures.

45. With the assistance of disclosure counsel, the State has reviewed, evaluated, and enhanced its disclosure process by instituting formal, written policies and procedures. In its written policies and procedures, among other things, the State established a committee comprised of senior Treasury officials, representatives from the Attorney General's Office, and disclosure counsel to oversee the entire disclosure process and to review and make recommendations regarding the State's disclosures and disclosure practices. In addition, the State has implemented an annual mandatory training program conducted by disclosure counsel for the State's employees involved in the disclosure process to ensure compliance with the State's disclosure obligations under the federal securities laws.

Legal Discussion

46. Municipal securities represent an important part of the financial markets available to investors. At the end of 2009, individual investors held approximately 35 percent of outstanding municipal securities directly and up to another 34 percent indirectly through money market funds, mutual funds, and closed end funds. There is also substantial trading volume in the municipal securities market — almost $3.8 trillion of long and short-term municipal securities were traded in 2009 in over 10 million transactions. Issuers of municipal securities have an obligation to ensure that financial information contained in their disclosure documents is not materially misleading. Proper disclosure allows investors to understand and evaluate the financial health of the state or local municipality in which they invest.

47. New Jersey, as an issuer of municipal securities, is subject to the antifraud provisions of the federal securities laws. In addition, the Commission has promulgated a broker-dealer rule, Exchange Act Rule 15c2-12, which in general limits market access for certain municipal securities issues to those offerings in which the issuer agrees to file annual disclosures of

specified financial and operating information as well as notices of certain events, if material, and notices of any failures to file with certain repositories designated by the Commission.[20] The antifraud provisions apply to such disclosure and to any other statements made to the market.

48. Section 17(a) of the Securities Act prohibits the making of any untrue statement of material fact or omitting to state a material fact in the offer or sale of securities. A fact is material if there is a substantial likelihood that its disclosure would be considered significant by a reasonable investor. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1987); TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). Violations of Sections 17(a)(2) and (3) may be established by showing negligence. SEC v. Hughes Corp., 124 F.3d 449, 453-54 (3d Cir. 1997); SEC v. Steadman, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992).

Violations

49. As a result of the negligent conduct described above, the State violated Sections 17(a)(2) and 17(a)(3) of the Securities Act. Specifically, the State made material misrepresentations and omissions in preliminary official statements, official statements, and continuing disclosures regarding the State's under funding of TPAF and PERS. TPAF and PERS represent a significant and growing obligation for New Jersey. The State's misrepresentations and omissions were material in that they failed, over the course of an almost six-year period, to provide investors with adequate information regarding the State's funding of TPAF and PERS as well as the financial condition of the pension plans. Information regarding the State's under funding of TPAF and PERS and their financial health was important to investors in evaluating New Jersey's overall financial condition and future financial prospects.

50. The State was aware of the under funding of TPAF and PERS and the potential effects of the under funding. However, due to a lack of disclosure training and inadequate procedures relating to the drafting and review of bond disclosure documents, the State made material representations and failed to disclose material information regarding TPAF and PERS in bond offering documents.

Remedial Efforts

51. In determining to accept the State's Offer, the Commission considered the cooperation afforded the Commission's staff during the investigation and remedial acts taken by the State, referenced in paragraphs 44 and 45.

---

[20] On December 5, 2008, the Commission amended Rule 15c2-12 to require issuers to agree to file annual disclosures of specified financial and operating information as well as notices of certain events, if material, and notices of any failures to file with the Municipal Securities Rulemaking Board. Issuers are no longer permitted to use other repositories. Rule 15c2-12 was further amended on May 27, 2010 to eliminate the materiality determination for certain types of events and to make other changes to improve the quality and timeliness of municipal securities disclosure.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in the State's Offer.

Accordingly, it is hereby ORDERED that pursuant to Section 8A of the Securities Act, the State shall cease and desist from committing or causing any violations and any future violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Casey and
Commissioner Paredes
Disapproved

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT COMPANY ACT OF 1940
Release No. 29382 / August 18, 2010

In the Matter of

GOLDMAN, SACHS & CO
200 West Street
New York, NY 10282

GOLDMAN SACHS ASSET MANAGEMENT, L.P.
200 West Street
New York, NY 10282

GOLDMAN SACHS ASSET MANAGEMENT INTERNATIONAL
Christchurch Court
10-15 Newgate Street
London, England, EC1A7HD

GOLDMAN SACHS HEDGE FUND STRATEGIES LLC
200 West Street
New York, NY 10282

COMMONWEALTH ANNUITY AND LIFE INSURANCE COMPANY
132 Turnpike Road
Southborough, MA 01772

FIRST ALLMERICA FINANCIAL LIFE INSURANCE COMPANY
132 Turnpike Road
Southborough, MA 01772

EPOCH SECURITIES, INC.
132 Turnpike Road
Southborough, MA 01772

(812-13796)

ORDER PURSUANT TO SECTION 9(c) OF THE INVESTMENT COMPANY ACT OF 1940 GRANTING A PERMANENT EXEMPTION FROM SECTION 9(a) OF THE ACT

Goldman, Sachs & Co., Goldman Sachs Asset Management, L.P., Goldman Sachs Asset Management International, Goldman Sachs Hedge Fund Strategies LLC, Commonwealth Annuity and Life Insurance Company, First Allmerica Financial Life Insurance Company and Epoch Securities, Inc. filed an application on July 16, 2010, and an amendment to the application on July 21, 2010, requesting temporary and permanent orders under section 9(c) of the Investment Company Act of 1940 ("Act") exempting applicants and any other company of which Goldman, Sachs & Co. is or hereafter becomes an affiliated person (together, "Covered Persons") from section 9(a) of the Act with respect to an injunction entered by the U.S. District Court for the Southern District of New York on July 20, 2010.

On July 21, 2010, the Commission simultaneously issued a notice of the filing of the application and a temporary conditional order exempting the Covered Persons from section 9(a) of the Act (Investment Company Act Release No. 29366) until the Commission takes final action on the application for a permanent order. The notice gave interested persons an opportunity to request a hearing and stated that an order disposing of the application would be issued unless a hearing was ordered. No request for a hearing has been filed, and the Commission has not ordered a hearing.

The matter has been considered and it is found that the conduct of the applicants has been such as not to make it against the public interest or protection of investors to grant the permanent exemption from the provisions of section 9(a) of the Act.

Accordingly,

IT IS ORDERED, pursuant to section 9(c) of the Act, on the basis of the representations contained in the application filed by Goldman, Sachs & Co. et al. (File No. 812-13796) that Covered Persons be and hereby are permanently exempted from the provisions of section 9(a) of the Act, operative solely as a result of an injunction, described in the application, entered by the U.S. District Court for the Southern District of New York on July 20, 2010.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

SECURITIES AND EXCHANGE COMMISSION

[Release No. PA-44; File No. S7 -17-10]

Privacy Act of 1974: Systems of Records.

AGENCY: Securities and Exchange Commission.

ACTION: Notice to establish systems of records.

SUMMARY: In accordance with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a, the U. S. Securities and Exchange Commission ("Commission" or "SEC") gives notice of a proposal to establish the following two new Privacy Act systems of records: "Municipal Advisor Records (SEC-61)" and "Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs (SEC-62)".

DATES: The proposed systems will become effective [insert date that is 40 days after publication in the Federal Register] unless further notice is given. The Commission will publish a new notice if the effective date is delayed to review comments or if changes are made based on comments received. To be assured of consideration, comments should be received on or before [insert date that is 30 days after publication in the Federal Register].

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/other.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-17-10 on the subject line.

Paper Comments:

Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090. All submissions should refer to File Number S7-17-10. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (http://www.sec.gov/rules/other.shtml). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Barbara A. Stance, Chief Privacy Officer, Office of Information Technology, 202-551-7209.

SUPPLEMENTARY INFORMATION: The Commission gives notice of the proposed establishment of new systems of records as follows: "Municipal Advisor Records (SEC- 61)," which contains records relating to Municipal Advisor applicants, registrants, and their associated or related persons, and "Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs (SEC-62)", which contains records of correspondence, inquiries, requests, comments or other communications submitted to the Commission or SEC staff relating to Municipal Advisors.

The Commission has submitted a report of the new systems of records to the appropriate Congressional committees and to the Director of the Office of Management and Budget ("OMB") as required by 5 U.S.C. 552a(r) (Privacy Act of 1974) and guidelines issued by OMB on December 12, 2000 (65 FR 77677).

Accordingly, the Commission is proposing two new systems of records to read as follows:

SEC- 61

SYSTEM NAME:

Municipal Advisor Records

SYSTEM LOCATION:

U.S. Securities and Exchange Commission ("Commission" or "SEC") 100 F Street, NE, Washington, DC 20549.

CATEGORIES OF INDIVIDUALS COVERED BY THE SYSTEM:

This system of records covers applicants for registration or exemption from registration as Municipal Advisors, current and former registrants, and individuals having a relationship with or a transaction with a registrant including: partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, and other related persons or entities; and their representatives or counsel.

CATEGORIES OF RECORDS IN THE SYSTEM:

Both electronic and paper records in this system may include: name, business address, residential address (for sole proprietor only), telephone/cellular/facsimile number, email address, web site or Internet address, IRS employer identification number, IA SEC File Number, Broker Dealer SEC File Number, CRD Number, areas of business, other SEC registrations, SRO memberships, and related information; past and present employment; disciplinary history; business relationships; and similar information relating to the categories of individuals covered by the system. Paper records may include, but are not limited to, application and other forms, records, or documents relating to registration; letters, facsimiles, imaged documents, and other forms of written communication; and related documentation.

AUTHORITY FOR MAINTENANCE OF THE SYSTEM:

Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 975(a), Pub. L. No. 111-203 (2010); 15 U.S.C. 78a et seq.; 80b-1 et seq.; and 17 CFR 202.1 to 202.10.

PURPOSE(S):

The records are used by authorized staff to review and process applications for registration or exemption as Municipal Advisors; with respect to the regulation and oversight of registrations and registrants and their associated or related persons as stated in the section relating to Categories of Individuals Covered by the System; to maintain and disclose in accordance with statutory or regulatory provisions records relating to such applications, registrations, registrants, and associated or related persons; and to implement and administer the federal securities laws and rules.

ROUTINE USES OF RECORDS MAINTAINED IN THE SYSTEM, INCLUDING CATEGORIES OF USERS AND THE PURPOSES OF SUCH USES:

In addition to those disclosures generally permitted under 5 U.S.C. 552a(b) of the Privacy Act, these records or information contained therein may specifically be disclosed outside the Commission as a routine use pursuant to 5 U.S.C. 552a(b)(3) as follows:

1. To appropriate agencies, entities, and persons when (a) it is suspected or confirmed that the security or confidentiality of information in the system of records has been compromised; (b) the SEC has determined that, as a result of the suspected or confirmed compromise, there is a risk of harm to economic or property interests, identity theft or fraud, or harm to the security or integrity of this system or other systems or programs (whether maintained by the SEC or another agency or entity) that rely upon the compromised information; and (c) the disclosure made to such agencies, entities, and persons is reasonably necessary to assist in connection

with the SEC's efforts to respond to the suspected or confirmed compromise and prevent, minimize, or remedy such harm.

2. To other federal, state, local, or foreign law enforcement agencies; securities self-regulatory organizations; and foreign financial regulatory authorities to assist in or coordinate regulatory or law enforcement activities with the SEC.
3. To national securities exchanges and national securities associations that are registered with the SEC, the Municipal Securities Rulemaking Board; the Securities Investor Protection Corporation; the Public Company Accounting Oversight Board; the federal banking authorities, including, but not limited to, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; state securities regulatory agencies or organizations; or regulatory authorities of a foreign government in connection with their regulatory or enforcement responsibilities.
4. By SEC personnel for purposes of investigating possible violations of, or to conduct investigations authorized by, the federal securities laws.
5. In any proceeding where the federal securities laws are in issue or in which the Commission, or past or present members of its staff, is a party or otherwise involved in an official capacity.
6. In connection with proceedings by the Commission pursuant to Rule 102(e) of its Rules of Practice, 17 CFR 201.102(e).
7. To a bar association, state accountancy board, or other federal, state, local, or foreign licensing or oversight authority; or professional association or self-regulatory authority to the extent that it performs similar functions (including the Public Company Accounting Oversight Board) for investigations or possible disciplinary action.

8. To a federal, state, local, tribal, foreign, or international agency, if necessary to obtain information relevant to the SEC's decision concerning the hiring or retention of an employee; the issuance of a security clearance; the letting of a contract; or the issuance of a license, grant, or other benefit.
9. To a federal, state, local, tribal, foreign, or international agency in response to its request for information concerning the hiring or retention of an employee; the issuance of a security clearance; the reporting of an investigation of an employee; the letting of a contract; or the issuance of a license, grant, or other benefit by the requesting agency, to the extent that the information is relevant and necessary to the requesting agency's decision on the matter.
10. To produce summary descriptive statistics and analytical studies, as a data source for management information, in support of the function for which the records are collected and maintained or for related personnel management functions or manpower studies; may also be used to respond to general requests for statistical information (without personal identification of individuals) under the Freedom of Information Act.
11. To any trustee, receiver, master, special counsel, or other individual or entity that is appointed by a court of competent jurisdiction, or as a result of an agreement between the parties in connection with litigation or administrative proceedings involving allegations of violations of the federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)) or pursuant to the Commission's Rules of Practice, 17 CFR 201.100 – 900 or the Commission's Rules of Fair Fund and Disgorgement Plans, 17 CFR 201.1100-1106, or otherwise, where such trustee, receiver, master, special counsel, or other individual or entity is specifically designated to perform particular functions with respect to, or as a result of, the pending action or proceeding or in connection with the

administration and enforcement by the Commission of the federal securities laws or the Commission's Rules of Practice or the Rules of Fair Fund and Disgorgement Plans.

12. To any persons during the course of any inquiry, examination, or investigation conducted by the SEC's staff, or in connection with civil litigation, if the staff has reason to believe that the person to whom the record is disclosed may have further information about the matters related therein, and those matters appeared to be relevant at the time to the subject matter of the inquiry.

13. To interns, grantees, experts, contractors, and others who have been engaged by the Commission to assist in the performance of a service related to this system of records and who need access to the records for the purpose of assisting the Commission in the efficient administration of its programs, including by performing clerical, stenographic, or data analysis functions, or by reproduction of records by electronic or other means. Recipients of these records shall be required to comply with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a.

14. In reports published by the Commission pursuant to authority granted in the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), which authority shall include, but not be limited to, section 21(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(a).

15. To members of advisory committees that are created by the Commission or by Congress to render advice and recommendations to the Commission or to Congress, to be used solely in connection with their official designated functions.

16. To any person who is or has agreed to be subject to the Commission's Rules of Conduct, 17 CFR 200.735-1 to 200.735-18, and who assists in the investigation by the Commission of

possible violations of the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), in the preparation or conduct of enforcement actions brought by the Commission for such violations, or otherwise in connection with the Commission's enforcement or regulatory functions under the federal securities laws.

17. To a Congressional office from the record of an individual in response to an inquiry from the Congressional office made at the request of that individual.
18. To members of Congress, the press, and the public in response to inquiries relating to particular Registrants and their activities, and other matters under the Commission's jurisdiction.
19. To prepare and publish information relating to violations of the federal securities laws as provided in 15 U.S.C. 78c(a)(47), as amended.
20. To respond to subpoenas in any litigation or other proceeding.
21. To a trustee in bankruptcy.
22. To members of Congress, the General Accountability Office, or others charged with monitoring the work of the Commission or conducting records management inspections.
23. To any governmental agency, governmental or private collection agent, consumer reporting agency or commercial reporting agency, governmental or private employer of a debtor, or any other person, for collection, including collection by administrative offset, federal salary offset, tax refund offset, or administrative wage garnishment, of amounts owed as a result of Commission civil or administrative proceedings.

POLICIES AND PRACTICES FOR STORING, RETRIEVING, ACCESSING, RETAINING, AND DISPOSING OF RECORDS IN THE SYSTEM:

STORAGE:

Records are maintained in electronic and paper format. Electronic records are stored in computerized databases and/or on computer disc. Paper records and records on computer disc are stored in locked file rooms and/or file cabinets.

RETRIEVABILITY:

Records may be retrieved by any of the following: name, address, receipt date, entity name, registration number, telephone/cellular/facsimile number, email or Internet address, subject matter, or other indexed information.

SAFEGUARDS:

Records are safeguarded in a secured environment. Buildings where records are stored have security cameras and 24 hour security guard service. The records are kept in limited access areas during duty hours and in locked file cabinets and/or locked offices or file rooms at all other times. Apart from information publicly disclosed pursuant to statutory or regulatory provisions, access is limited to those personnel whose official duties require access. Computerized records are safeguarded through use of access codes and information technology security. Contractors and other recipients providing services to the Commission are contractually obligated to maintain equivalent safeguards.

RETENTION AND DISPOSAL:

These records will be maintained until they become inactive, at which time they will be retired or destroyed in accordance with records schedules of the United States Securities and Exchange Commission and as approved by the National Archives and Records Administration.

SYSTEM MANAGERS AND ADDRESSES:

Assistant Director, Division of Trading and Markets, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7561.

NOTIFICATION PROCEDURE:

All requests to determine whether this system of records contains a record pertaining to the requesting individual may be directed to the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

RECORD ACCESS PROCEDURES:

Persons wishing to obtain information on the procedures for gaining access to or contesting the contents of these records may contact the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

CONTESTING RECORD PROCEDURES:

See Record Access Procedures above.

RECORD SOURCE CATEGORIES:

Information collected is received primarily from applicants for registration or exemption from registration, current and former registrants, and partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, other related persons or entities, members of the public, and their representatives or counsel, via form, correspondence, or other written or verbal forms of communication, including without limitation telephone calls, emails and other forms of electronic communication, letters, or facsimiles to the Commission and SEC staff.

EXEMPTIONS CLAIMED FOR THE SYSTEM:

None.

SEC- 62

SYSTEM NAMES:

Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs.

SYSTEM LOCATION:

U.S. Securities and Exchange Commission ("Commission" or "SEC") 100 F Street, NE, Washington, DC 20549.

CATEGORIES OF INDIVIDUALS COVERED BY THE SYSTEM:

Persons applying for registration or exemption from registration as a Municipal Advisor, persons currently or formerly registered with the Commission as a Municipal Advisor, and their partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, other related persons, and their representatives or counsel; and representatives of regulated entities and their counsel, members of the public, representatives of other governmental agencies or Congress, and others who submit correspondence, inquiries, information, comments, or other forms of communication to the Commission or SEC staff relating to Municipal Advisors.

CATEGORIES OF RECORDS IN THE SYSTEM:

Both electronic and paper records in this system may include information concerning an individual's activities, transactions, and disciplinary history as or pertaining to, or relationships with, a Municipal Advisor; the name of the correspondent or inquirer/requester/commenter/communicant or their representative; the name, residential and/or business address, telephone/cellular/facsimile number, and email or Internet address of the correspondent or entity; the subject of the correspondence, inquiry/request/comment or communication; the date of the correspondence, inquiry/request/comment or communication; and the Commission or SEC staff response provided, or other disposition, on a formal or informal basis. Paper records may include, but are not limited to, letters, facsimiles, imaged documents, other written forms of communication, and related documentation.

AUTHORITY FOR MAINTENANCE OF THE SYSTEM:

Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 975(a), Pub. L. No. 111-203 (2010); 15 U.S.C. 78a et seq.; 80b-1 et. seq.; and 17 CFR 202.1 to 202.10.

PURPOSE(S):

The records are used by authorized SEC staff to track, process, respond to, and maintain documentation of correspondence, inquiries/requests/comments, communications, and related information from members of the public, including industry representatives, counsel, and others, relating to Municipal Advisors; to document Commission or SEC staff responses on a formal or informal basis.

ROUTINE USES OF RECORDS MAINTAINED IN THE SYSTEM, INCLUDING CATEGORIES OF USERS AND THE PURPOSES OF SUCH USES:

In addition to those disclosures generally permitted under 5 U.S.C. 552a(b) of the Privacy Act, these records or information contained therein may specifically be disclosed outside the Commission as a routine use pursuant to 5 U.S.C. 552a(b)(3) as follows:

1. To appropriate agencies, entities, and persons when (a) it is suspected or confirmed that the security or confidentiality of information in the system of records has been compromised; (b) the SEC has determined that, as a result of the suspected or confirmed compromise, there is a risk of harm to economic or property interests, identity theft or fraud, or harm to the security or integrity of this system or other systems or programs (whether maintained by the SEC or another agency or entity) that rely upon the compromised information; and (c) the disclosure made to such agencies, entities, and persons is reasonably necessary to assist in connection

with the SEC's efforts to respond to the suspected or confirmed compromise and prevent, minimize, or remedy such harm.

2. To other federal, state, local, or foreign law enforcement agencies; securities self-regulatory organizations; and foreign financial regulatory authorities to assist in or coordinate regulatory or law enforcement activities with the SEC.
3. To national securities exchanges and national securities associations that are registered with the SEC, the Municipal Securities Rulemaking Board; the Securities Investor Protection Corporation; the Public Company Accounting Oversight Board; the federal banking authorities, including, but not limited to, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; state securities regulatory agencies or organizations; or regulatory authorities of a foreign government in connection with their regulatory or enforcement responsibilities.
4. By SEC personnel for purposes of investigating possible violations of, or to conduct investigations authorized by, the federal securities laws.
5. In any proceeding where the federal securities laws are in issue or in which the Commission, or past or present members of its staff, is a party or otherwise involved in an official capacity.
6. In connection with proceedings by the Commission pursuant to Rule 102(e) of its Rules of Practice, 17 CFR 201.102(e).
7. To a bar association, state accountancy board, or other federal, state, local, or foreign licensing or oversight authority; or professional association or self-regulatory authority to the extent that it performs similar functions (including the Public Company Accounting Oversight Board) for investigations or possible disciplinary action.

8. To a federal, state, local, tribal, foreign, or international agency, if necessary to obtain information relevant to the SEC's decision concerning the hiring or retention of an employee; the issuance of a security clearance; the letting of a contract; or the issuance of a license, grant, or other benefit.
9. To a federal, state, local, tribal, foreign, or international agency in response to its request for information concerning the hiring or retention of an employee; the issuance of a security clearance; the reporting of an investigation of an employee; the letting of a contract; or the issuance of a license, grant, or other benefit by the requesting agency, to the extent that the information is relevant and necessary to the requesting agency's decision on the matter.
10. To produce summary descriptive statistics and analytical studies, as a data source for management information, in support of the function for which the records are collected and maintained or for related personnel management functions or manpower studies; may also be used to respond to general requests for statistical information (without personal identification of individuals) under the Freedom of Information Act.
11. To any trustee, receiver, master, special counsel, or other individual or entity that is appointed by a court of competent jurisdiction, or as a result of an agreement between the parties in connection with litigation or administrative proceedings involving allegations of violations of the federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)) or pursuant to the Commission's Rules of Practice, 17 CFR 201.100 – 900 or the Commission's Rules of Fair Fund and Disgorgement Plans, 17 CFR 201.1100-1106, or otherwise, where such trustee, receiver, master, special counsel, or other individual or entity is specifically designated to perform particular functions with respect to, or as a result of, the pending action or proceeding or in connection with the

administration and enforcement by the Commission of the federal securities laws or the Commission's Rules of Practice or the Rules of Fair Fund and Disgorgement Plans.

12. To any persons during the course of any inquiry, examination, or investigation conducted by the SEC's staff, or in connection with civil litigation, if the staff has reason to believe that the person to whom the record is disclosed may have further information about the matters related therein, and those matters appeared to be relevant at the time to the subject matter of the inquiry.
13. To interns, grantees, experts, contractors, and others who have been engaged by the Commission to assist in the performance of a service related to this system of records and who need access to the records for the purpose of assisting the Commission in the efficient administration of its programs, including by performing clerical, stenographic, or data analysis functions, or by reproduction of records by electronic or other means. Recipients of these records shall be required to comply with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a.
14. In reports published by the Commission pursuant to authority granted in the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), which authority shall include, but not be limited to, section 21(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(a).
15. To members of advisory committees that are created by the Commission or by Congress to render advice and recommendations to the Commission or to Congress, to be used solely in connection with their official designated functions.
16. To any person who is or has agreed to be subject to the Commission's Rules of Conduct, 17 CFR 200.735-1 to 200.735-18, and who assists in the investigation by the Commission of

possible violations of the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), in the preparation or conduct of enforcement actions brought by the Commission for such violations, or otherwise in connection with the Commission's enforcement or regulatory functions under the federal securities laws.

17. To a Congressional office from the record of an individual in response to an inquiry from the Congressional office made at the request of that individual.
18. To members of Congress, the press, and the public in response to inquiries relating to particular Registrants and their activities, and other matters under the Commission's jurisdiction.
19. To prepare and publish information relating to violations of the federal securities laws as provided in 15 U.S.C. 78c(a)(47), as amended.
20. To respond to subpoenas in any litigation or other proceeding.
21. To a trustee in bankruptcy.
22. To members of Congress, the General Accountability Office, or others charged with monitoring the work of the Commission or conducting records management inspections.
23. To any governmental agency, governmental or private collection agent, consumer reporting agency or commercial reporting agency, governmental or private employer of a debtor, or any other person, for collection, including collection by administrative offset, federal salary offset, tax refund offset, or administrative wage garnishment, of amounts owed as a result of Commission civil or administrative proceedings.

POLICIES AND PRACTICES FOR STORING, RETRIEVING, ACCESSING, RETAINING, AND DISPOSING OF RECORDS IN THE SYSTEM:

STORAGE:

Records are maintained in electronic and paper format. Electronic records are stored in computerized databases and/or on computer disc. Paper records and records on computer disc are stored in locked file rooms and/or file cabinets.

RETRIEVABILITY:

Records may be retrieved by any of the following: name, receipt date, entity name, registration number, telephone/cellular/facsimile number, email or Internet address, subject matter, or other indexed information.

SAFEGUARDS:

Records are safeguarded in a secured environment. Buildings where records are stored have security cameras and 24 hour security guard service. The records are kept in limited access areas during duty hours and in locked file cabinets and/or locked offices or file rooms at all other times. Access is limited to those personnel whose official duties require access. Computerized records are safeguarded through use of access codes and information technology security. Contractors and other recipients providing services to the Commission are contractually obligated to maintain equivalent safeguards.

RETENTION AND DISPOSAL:

These records will be maintained until they become inactive, at which time they will be retired or destroyed in accordance with records schedules of the United States Securities and Exchange Commission and as approved by the National Archives and Records Administration.

SYSTEM MANAGERS AND ADDRESSES:

Assistant Director, Division of Trading and Markets, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7561.

NOTIFICATION PROCEDURE:

All requests to determine whether this system of records contains a record pertaining to the requesting individual may be directed to the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

RECORD ACCESS PROCEDURES:

Persons wishing to obtain information on the procedures for gaining access to or contesting the contents of these records may contact the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

CONTESTING RECORD PROCEDURES:

See Record Access Procedures above.

RECORD SOURCE CATEGORIES:

Information collected is received from individuals primarily through correspondence or other written or verbal forms of communication, including without limitation telephone calls, emails and other forms of electronic communication, letters, or facsimiles to the Commission and SEC staff.

EXEMPTIONS CLAIMED FOR THE SYSTEM:

None.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Date: August 19, 2010

SECURITIES AND EXCHANGE COMMISSION **CORRECTION**

[Release No. PA-44A; File No. S7-17-10]

Privacy Act of 1974: Systems of Records.

AGENCY: Securities and Exchange Commission.

ACTION: Notice to establish systems of records.

SUMMARY: In accordance with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a, the U. S. Securities and Exchange Commission ("Commission" or "SEC") gives notice of a proposal to establish the following two new Privacy Act systems of records: "Municipal Advisor Records (SEC-61)" and "Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs (SEC-62)".

DATES: The proposed systems will become effective September 29, 2010 unless further notice is given. The Commission will publish a new notice if the effective date is delayed to review comments or if changes are made based on comments received. To be assured of consideration, comments should be received on or before September 22, 2010.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/other.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-17-10 on the subject line.

Paper Comments:

Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090. All submissions should refer to File Number S7-17-10. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (http://www.sec.gov/rules/other.shtml). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Barbara A. Stance, Chief Privacy Officer, Office of Information Technology, 202-551-7209.

SUPPLEMENTARY INFORMATION: The Commission gives notice of the proposed establishment of new systems of records as follows: "Municipal Advisor Records (SEC- 61)," which contains records relating to Municipal Advisor applicants, registrants, and their associated or related persons, and "Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs (SEC-62)", which contains records of correspondence, inquiries, requests, comments or other communications submitted to the Commission or SEC staff relating to Municipal Advisors.

The Commission has submitted a report of the new systems of records to the appropriate Congressional committees and to the Director of the Office of Management and Budget ("OMB") as required by 5 U.S.C. 552a(r) (Privacy Act of 1974) and guidelines issued by OMB on December 12, 2000 (65 FR 77677).

Accordingly, the Commission is proposing two new systems of records to read as follows:

SEC- 61

SYSTEM NAME:

Municipal Advisor Records

SYSTEM LOCATION:

U.S. Securities and Exchange Commission ("Commission" or "SEC") 100 F Street, NE, Washington, DC 20549.

CATEGORIES OF INDIVIDUALS COVERED BY THE SYSTEM:

This system of records covers applicants for registration or exemption from registration as Municipal Advisors, current and former registrants, and individuals having a relationship with or a transaction with a registrant including: partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, and other related persons or entities; and their representatives or counsel.

CATEGORIES OF RECORDS IN THE SYSTEM:

Both electronic and paper records in this system may include: name, business address, residential address (for sole proprietor only), telephone/cellular/facsimile number, email address, web site or Internet address, IRS employer identification number, IA SEC File Number, Broker Dealer SEC File Number, CRD Number, areas of business, other SEC registrations, SRO memberships, and related information; past and present employment; disciplinary history; business relationships; and similar information relating to the categories of individuals covered by the system. Paper records may include, but are not limited to, application and other forms, records, or documents relating to registration; letters, facsimiles, imaged documents, and other forms of written communication; and related documentation.

AUTHORITY FOR MAINTENANCE OF THE SYSTEM:

Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 975(a), Pub. L. No. 111-203 (2010); 15 U.S.C. 78a et seq.; 80b-1 et seq.; and 17 CFR 202.1 to 202.10.

PURPOSE(S):

The records are used by authorized staff to review and process applications for registration or exemption as Municipal Advisors; with respect to the regulation and oversight of registrations and registrants and their associated or related persons as stated in the section relating to Categories of Individuals Covered by the System; to maintain and disclose in accordance with statutory or regulatory provisions records relating to such applications, registrations, registrants, and associated or related persons; and to implement and administer the federal securities laws and rules.

ROUTINE USES OF RECORDS MAINTAINED IN THE SYSTEM, INCLUDING CATEGORIES OF USERS AND THE PURPOSES OF SUCH USES:

In addition to those disclosures generally permitted under 5 U.S.C. 552a(b) of the Privacy Act, these records or information contained therein may specifically be disclosed outside the Commission as a routine use pursuant to 5 U.S.C. 552a(b)(3) as follows:

1. To appropriate agencies, entities, and persons when (a) it is suspected or confirmed that the security or confidentiality of information in the system of records has been compromised; (b) the SEC has determined that, as a result of the suspected or confirmed compromise, there is a risk of harm to economic or property interests, identity theft or fraud, or harm to the security or integrity of this system or other systems or programs (whether maintained by the SEC or another agency or entity) that rely upon the compromised information; and (c) the disclosure made to such agencies, entities, and persons is reasonably necessary to assist in connection

with the SEC's efforts to respond to the suspected or confirmed compromise and prevent, minimize, or remedy such harm.

2. To other federal, state, local, or foreign law enforcement agencies; securities self-regulatory organizations; and foreign financial regulatory authorities to assist in or coordinate regulatory or law enforcement activities with the SEC.
3. To national securities exchanges and national securities associations that are registered with the SEC, the Municipal Securities Rulemaking Board; the Securities Investor Protection Corporation; the Public Company Accounting Oversight Board; the federal banking authorities, including, but not limited to, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; state securities regulatory agencies or organizations; or regulatory authorities of a foreign government in connection with their regulatory or enforcement responsibilities.
4. By SEC personnel for purposes of investigating possible violations of, or to conduct investigations authorized by, the federal securities laws.
5. In any proceeding where the federal securities laws are in issue or in which the Commission, or past or present members of its staff, is a party or otherwise involved in an official capacity.
6. In connection with proceedings by the Commission pursuant to Rule 102(e) of its Rules of Practice, 17 CFR 201.102(e).
7. To a bar association, state accountancy board, or other federal, state, local, or foreign licensing or oversight authority; or professional association or self-regulatory authority to the extent that it performs similar functions (including the Public Company Accounting Oversight Board) for investigations or possible disciplinary action.

8. To a federal, state, local, tribal, foreign, or international agency, if necessary to obtain information relevant to the SEC's decision concerning the hiring or retention of an employee; the issuance of a security clearance; the letting of a contract; or the issuance of a license, grant, or other benefit.
9. To a federal, state, local, tribal, foreign, or international agency in response to its request for information concerning the hiring or retention of an employee; the issuance of a security clearance; the reporting of an investigation of an employee; the letting of a contract; or the issuance of a license, grant, or other benefit by the requesting agency, to the extent that the information is relevant and necessary to the requesting agency's decision on the matter.
10. To produce summary descriptive statistics and analytical studies, as a data source for management information, in support of the function for which the records are collected and maintained or for related personnel management functions or manpower studies; may also be used to respond to general requests for statistical information (without personal identification of individuals) under the Freedom of Information Act.
11. To any trustee, receiver, master, special counsel, or other individual or entity that is appointed by a court of competent jurisdiction, or as a result of an agreement between the parties in connection with litigation or administrative proceedings involving allegations of violations of the federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)) or pursuant to the Commission's Rules of Practice, 17 CFR 201.100 – 900 or the Commission's Rules of Fair Fund and Disgorgement Plans, 17 CFR 201.1100-1106, or otherwise, where such trustee, receiver, master, special counsel, or other individual or entity is specifically designated to perform particular functions with respect to, or as a result of, the pending action or proceeding or in connection with the

administration and enforcement by the Commission of the federal securities laws or the Commission's Rules of Practice or the Rules of Fair Fund and Disgorgement Plans.

12. To any persons during the course of any inquiry, examination, or investigation conducted by the SEC's staff, or in connection with civil litigation, if the staff has reason to believe that the person to whom the record is disclosed may have further information about the matters related therein, and those matters appeared to be relevant at the time to the subject matter of the inquiry.

13. To interns, grantees, experts, contractors, and others who have been engaged by the Commission to assist in the performance of a service related to this system of records and who need access to the records for the purpose of assisting the Commission in the efficient administration of its programs, including by performing clerical, stenographic, or data analysis functions, or by reproduction of records by electronic or other means. Recipients of these records shall be required to comply with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a.

14. In reports published by the Commission pursuant to authority granted in the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), which authority shall include, but not be limited to, section 21(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(a).

15. To members of advisory committees that are created by the Commission or by Congress to render advice and recommendations to the Commission or to Congress, to be used solely in connection with their official designated functions.

16. To any person who is or has agreed to be subject to the Commission's Rules of Conduct, 17 CFR 200.735-1 to 200.735-18, and who assists in the investigation by the Commission of

possible violations of the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), in the preparation or conduct of enforcement actions brought by the Commission for such violations, or otherwise in connection with the Commission's enforcement or regulatory functions under the federal securities laws.

17. To a Congressional office from the record of an individual in response to an inquiry from the Congressional office made at the request of that individual.
18. To members of Congress, the press, and the public in response to inquiries relating to particular Registrants and their activities, and other matters under the Commission's jurisdiction.
19. To prepare and publish information relating to violations of the federal securities laws as provided in 15 U.S.C. 78c(a)(47), as amended.
20. To respond to subpoenas in any litigation or other proceeding.
21. To a trustee in bankruptcy.
22. To members of Congress, the General Accountability Office, or others charged with monitoring the work of the Commission or conducting records management inspections.
23. To any governmental agency, governmental or private collection agent, consumer reporting agency or commercial reporting agency, governmental or private employer of a debtor, or any other person, for collection, including collection by administrative offset, federal salary offset, tax refund offset, or administrative wage garnishment, of amounts owed as a result of Commission civil or administrative proceedings.

POLICIES AND PRACTICES FOR STORING, RETRIEVING, ACCESSING, RETAINING, AND DISPOSING OF RECORDS IN THE SYSTEM:

STORAGE:

Records are maintained in electronic and paper format. Electronic records are stored in computerized databases and/or on computer disc. Paper records and records on computer disc are stored in locked file rooms and/or file cabinets.

RETRIEVABILITY:

Records may be retrieved by any of the following: name, address, receipt date, entity name, registration number, telephone/cellular/facsimile number, email or Internet address, subject matter, or other indexed information.

SAFEGUARDS:

Records are safeguarded in a secured environment. Buildings where records are stored have security cameras and 24 hour security guard service. The records are kept in limited access areas during duty hours and in locked file cabinets and/or locked offices or file rooms at all other times. Apart from information publicly disclosed pursuant to statutory or regulatory provisions, access is limited to those personnel whose official duties require access. Computerized records are safeguarded through use of access codes and information technology security. Contractors and other recipients providing services to the Commission are contractually obligated to maintain equivalent safeguards.

RETENTION AND DISPOSAL:

These records will be maintained until they become inactive, at which time they will be retired or destroyed in accordance with records schedules of the United States Securities and Exchange Commission and as approved by the National Archives and Records Administration.

SYSTEM MANAGERS AND ADDRESSES:

Assistant Director, Division of Trading and Markets, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7561.

NOTIFICATION PROCEDURE:

All requests to determine whether this system of records contains a record pertaining to the requesting individual may be directed to the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

RECORD ACCESS PROCEDURES:

Persons wishing to obtain information on the procedures for gaining access to or contesting the contents of these records may contact the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

CONTESTING RECORD PROCEDURES:

See Record Access Procedures above.

RECORD SOURCE CATEGORIES:

Information collected is received primarily from applicants for registration or exemption from registration, current and former registrants, and partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, other related persons or entities, members of the public, and their representatives or counsel, via form, correspondence, or other written or verbal forms of communication, including without limitation telephone calls, emails and other forms of electronic communication, letters, or facsimiles to the Commission and SEC staff.

EXEMPTIONS CLAIMED FOR THE SYSTEM:

None.

SEC- 62

SYSTEM NAMES:

Correspondence Files Pertaining to Municipal Advisors; Municipal Advisor Logs.

SYSTEM LOCATION:

U.S. Securities and Exchange Commission ("Commission" or "SEC") 100 F Street, NE, Washington, DC 20549.

CATEGORIES OF INDIVIDUALS COVERED BY THE SYSTEM:

Persons applying for registration or exemption from registration as a Municipal Advisor, persons currently or formerly registered with the Commission as a Municipal Advisor, and their partners, officers, directors, associated persons, control persons, control affiliates, employees, owners, principal shareholders, other related persons, and their representatives or counsel; and representatives of regulated entities and their counsel, members of the public, representatives of other governmental agencies or Congress, and others who submit correspondence, inquiries, information, comments, or other forms of communication to the Commission or SEC staff relating to Municipal Advisors.

CATEGORIES OF RECORDS IN THE SYSTEM:

Both electronic and paper records in this system may include information concerning an individual's activities, transactions, and disciplinary history as or pertaining to, or relationships with, a Municipal Advisor; the name of the correspondent or inquirer/requester/commenter/communicant or their representative; the name, residential and/or business address, telephone/cellular/facsimile number, and email or Internet address of the correspondent or entity; the subject of the correspondence, inquiry/request/comment or communication; the date of the correspondence, inquiry/request/comment or communication; and the Commission or SEC staff response provided, or other disposition, on a formal or informal basis. Paper records may include, but are not limited to, letters, facsimiles, imaged documents, other written forms of communication, and related documentation.

AUTHORITY FOR MAINTENANCE OF THE SYSTEM:

Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 975(a), Pub. L. No. 111-203 (2010); 15 U.S.C. 78a et seq.; 80b-1 et. seq.; and 17 CFR 202.1 to 202.10.

PURPOSE(S):

The records are used by authorized SEC staff to track, process, respond to, and maintain documentation of correspondence, inquiries/requests/comments, communications, and related information from members of the public, including industry representatives, counsel, and others, relating to Municipal Advisors; to document Commission or SEC staff responses on a formal or informal basis.

ROUTINE USES OF RECORDS MAINTAINED IN THE SYSTEM, INCLUDING CATEGORIES OF USERS AND THE PURPOSES OF SUCH USES:

In addition to those disclosures generally permitted under 5 U.S.C. 552a(b) of the Privacy Act, these records or information contained therein may specifically be disclosed outside the Commission as a routine use pursuant to 5 U.S.C. 552a(b)(3) as follows:

1. To appropriate agencies, entities, and persons when (a) it is suspected or confirmed that the security or confidentiality of information in the system of records has been compromised; (b) the SEC has determined that, as a result of the suspected or confirmed compromise, there is a risk of harm to economic or property interests, identity theft or fraud, or harm to the security or integrity of this system or other systems or programs (whether maintained by the SEC or another agency or entity) that rely upon the compromised information; and (c) the disclosure made to such agencies, entities, and persons is reasonably necessary to assist in connection

with the SEC's efforts to respond to the suspected or confirmed compromise and prevent, minimize, or remedy such harm.

2. To other federal, state, local, or foreign law enforcement agencies; securities self-regulatory organizations; and foreign financial regulatory authorities to assist in or coordinate regulatory or law enforcement activities with the SEC.
3. To national securities exchanges and national securities associations that are registered with the SEC, the Municipal Securities Rulemaking Board; the Securities Investor Protection Corporation; the Public Company Accounting Oversight Board; the federal banking authorities, including, but not limited to, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation; state securities regulatory agencies or organizations; or regulatory authorities of a foreign government in connection with their regulatory or enforcement responsibilities.
4. By SEC personnel for purposes of investigating possible violations of, or to conduct investigations authorized by, the federal securities laws.
5. In any proceeding where the federal securities laws are in issue or in which the Commission, or past or present members of its staff, is a party or otherwise involved in an official capacity.
6. In connection with proceedings by the Commission pursuant to Rule 102(e) of its Rules of Practice, 17 CFR 201.102(e).
7. To a bar association, state accountancy board, or other federal, state, local, or foreign licensing or oversight authority; or professional association or self-regulatory authority to the extent that it performs similar functions (including the Public Company Accounting Oversight Board) for investigations or possible disciplinary action.

8. To a federal, state, local, tribal, foreign, or international agency, if necessary to obtain information relevant to the SEC's decision concerning the hiring or retention of an employee; the issuance of a security clearance; the letting of a contract; or the issuance of a license, grant, or other benefit.
9. To a federal, state, local, tribal, foreign, or international agency in response to its request for information concerning the hiring or retention of an employee; the issuance of a security clearance; the reporting of an investigation of an employee; the letting of a contract; or the issuance of a license, grant, or other benefit by the requesting agency, to the extent that the information is relevant and necessary to the requesting agency's decision on the matter.
10. To produce summary descriptive statistics and analytical studies, as a data source for management information, in support of the function for which the records are collected and maintained or for related personnel management functions or manpower studies; may also be used to respond to general requests for statistical information (without personal identification of individuals) under the Freedom of Information Act.
11. To any trustee, receiver, master, special counsel, or other individual or entity that is appointed by a court of competent jurisdiction, or as a result of an agreement between the parties in connection with litigation or administrative proceedings involving allegations of violations of the federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)) or pursuant to the Commission's Rules of Practice, 17 CFR 201.100 – 900 or the Commission's Rules of Fair Fund and Disgorgement Plans, 17 CFR 201.1100-1106, or otherwise, where such trustee, receiver, master, special counsel, or other individual or entity is specifically designated to perform particular functions with respect to, or as a result of, the pending action or proceeding or in connection with the

administration and enforcement by the Commission of the federal securities laws or the Commission's Rules of Practice or the Rules of Fair Fund and Disgorgement Plans.

12. To any persons during the course of any inquiry, examination, or investigation conducted by the SEC's staff, or in connection with civil litigation, if the staff has reason to believe that the person to whom the record is disclosed may have further information about the matters related therein, and those matters appeared to be relevant at the time to the subject matter of the inquiry.

13. To interns, grantees, experts, contractors, and others who have been engaged by the Commission to assist in the performance of a service related to this system of records and who need access to the records for the purpose of assisting the Commission in the efficient administration of its programs, including by performing clerical, stenographic, or data analysis functions, or by reproduction of records by electronic or other means. Recipients of these records shall be required to comply with the requirements of the Privacy Act of 1974, as amended, 5 U.S.C. 552a.

14. In reports published by the Commission pursuant to authority granted in the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), which authority shall include, but not be limited to, section 21(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78u(a).

15. To members of advisory committees that are created by the Commission or by Congress to render advice and recommendations to the Commission or to Congress, to be used solely in connection with their official designated functions.

16. To any person who is or has agreed to be subject to the Commission's Rules of Conduct, 17 CFR 200.735-1 to 200.735-18, and who assists in the investigation by the Commission of

possible violations of the federal securities laws (as such term is defined in section 3(a)(47) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(47)), in the preparation or conduct of enforcement actions brought by the Commission for such violations, or otherwise in connection with the Commission's enforcement or regulatory functions under the federal securities laws.

17. To a Congressional office from the record of an individual in response to an inquiry from the Congressional office made at the request of that individual.
18. To members of Congress, the press, and the public in response to inquiries relating to particular Registrants and their activities, and other matters under the Commission's jurisdiction.
19. To prepare and publish information relating to violations of the federal securities laws as provided in 15 U.S.C. 78c(a)(47), as amended.
20. To respond to subpoenas in any litigation or other proceeding.
21. To a trustee in bankruptcy.
22. To members of Congress, the General Accountability Office, or others charged with monitoring the work of the Commission or conducting records management inspections.
23. To any governmental agency, governmental or private collection agent, consumer reporting agency or commercial reporting agency, governmental or private employer of a debtor, or any other person, for collection, including collection by administrative offset, federal salary offset, tax refund offset, or administrative wage garnishment, of amounts owed as a result of Commission civil or administrative proceedings.

POLICIES AND PRACTICES FOR STORING, RETRIEVING, ACCESSING, RETAINING, AND DISPOSING OF RECORDS IN THE SYSTEM:

STORAGE:

Records are maintained in electronic and paper format. Electronic records are stored in computerized databases and/or on computer disc. Paper records and records on computer disc are stored in locked file rooms and/or file cabinets.

RETRIEVABILITY:

Records may be retrieved by any of the following: name, receipt date, entity name, registration number, telephone/cellular/facsimile number, email or Internet address, subject matter, or other indexed information.

SAFEGUARDS:

Records are safeguarded in a secured environment. Buildings where records are stored have security cameras and 24 hour security guard service. The records are kept in limited access areas during duty hours and in locked file cabinets and/or locked offices or file rooms at all other times. Access is limited to those personnel whose official duties require access. Computerized records are safeguarded through use of access codes and information technology security. Contractors and other recipients providing services to the Commission are contractually obligated to maintain equivalent safeguards.

RETENTION AND DISPOSAL:

These records will be maintained until they become inactive, at which time they will be retired or destroyed in accordance with records schedules of the United States Securities and Exchange Commission and as approved by the National Archives and Records Administration.

SYSTEM MANAGERS AND ADDRESSES:

Assistant Director, Division of Trading and Markets, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7561.

NOTIFICATION PROCEDURE:

All requests to determine whether this system of records contains a record pertaining to the requesting individual may be directed to the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

RECORD ACCESS PROCEDURES:

Persons wishing to obtain information on the procedures for gaining access to or contesting the contents of these records may contact the FOIA/PA Officer, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-5100.

CONTESTING RECORD PROCEDURES:

See Record Access Procedures above.

RECORD SOURCE CATEGORIES:

Information collected is received from individuals primarily through correspondence or other written or verbal forms of communication, including without limitation telephone calls, emails and other forms of electronic communication, letters, or facsimiles to the Commission and SEC staff.

EXEMPTIONS CLAIMED FOR THE SYSTEM:

None.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Date: August 19, 2010

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62746 / August 19, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-11701

In the Matter of **AIM Advisors, Inc. and AIM Distributors, Inc.,** **Respondents.**	**ORDER DIRECTING DISBURSEMENT**

On July 6, 2007, the Securities and Exchange Commission (the "Commission") issued a Notice of Proposed Distribution Plan and Opportunity for Comment (Exchange Act Release No. 56027) pursuant to Rule 1103 of the Commission's Rules on Fair Fund and Disgorgement Plans, 17 C.F.R. § 201.1103. The Commission received comments and, on May 23, 2008, the Commission approved the proposed Plan of Distribution as modified (Exchange Act Release No. 57859).

The Plan provides that a Fair Fund consisting of $50,000,000 in disgorgement and civil penalties, plus any accrued interest, less any amounts necessary to pay taxes due on Fair Fund earnings be transferred in increments to Deutsche Bank Trust Company Americas (the "Bank") to be distributed to injured investors according to the methodology set forth in the Plan.

In addition, the distribution amount of $28,166,976.18 in disgorgement and civil penalties, plus any accrued interest, less any amounts necessary to pay taxes due on Fair Fund earnings from the Banc of America Capital Management, LLC, BACAP Distributors, LLC, and Banc of America Securities, LLC Fair Fund and Bear, Stems & Co., Inc. and Bear, Stearns Securities Corp. and Bear, Stearns & Co. Fair Fund were transferred to the Bank for distribution by the Plan Administrator to injured investors according to the methodology set forth in the Plan. On May 14, 2009 the Commission approved the distribution of $78,166,976.18 to investors (Exchange Act Release No. 59929).

42 of 62

The Plan provides that any monies not distributed directly to investors (the "Residual"), less any remaining amounts needed for taxes and related expenses, shall be distributed to the AIM Funds in the same proportion as the amount of harm calculated on a fund by fund basis.

Accordingly, it is ORDERED that the Fund Administrator shall disburse the Residual, in the amount stated in the validated payment file, of $13,141,658.77, as provided for in the Plan of Distribution.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Chairman Schapiro not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62750 / August 20, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13871

In the Matter of **Ronald S. Bloomfield,** **Robert Gorgia,** **Victor Labi,** **John Earl Martin, Sr., and** **Eugene Miller**	**ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER PURSUANT TO SECTIONS 15(b) AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AS TO EUGENE MILLER**

I.

On April 27, 2010, the Securities and Exchange Commission ("Commission") instituted administrative and cease-and-desist proceedings pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") and Sections 15(b) and 21C of the Securities Exchange Act of 1934 ("Exchange Act") against Eugene Miller ("Miller" or "Respondent") and four other individuals.

II.

Respondent has submitted an Offer of Settlement (the "Offer"), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Making Findings and Imposing Remedial Sanctions Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

Summary

1. During the relevant period, from April 2005 to April 2007 ("Relevant Period"), Miller was the president of Leeb Brokerage Services, Inc. ("Leeb"), a now-defunct broker-dealer, and held significant supervisory responsibilities. During this period, certain customers of Leeb routinely delivered into their accounts large blocks of privately obtained shares of penny stocks, which Leeb then sold to the public on its customers' behalf, without any registration statements being in effect. Miller, as president of Leeb with supervisory responsibilities over the trading desk and penny stock activity, failed to respond to red flags indicating that certain registered representatives were not conducting reasonable inquiries into facts that could indicate unlawful distributions of stock, in order to prevent and detect violations of Section 5 of the Securities Act of 1933. Miller also willfully aided and abetted and caused Leeb's failure to file suspicious activity reports, as required by Section 17(a) of the Exchange Act and Rule 17a-8 thereunder, regarding suspicious penny stock trading in certain Leeb customer accounts.

Respondent

2. Miller, 52 years old, is a resident of Park Ridge, New Jersey. He was the president of Leeb from April 2004 to April 2007.

Other Relevant Entity

3. Leeb was a broker-dealer incorporated under New York law, with a main office in New York and an Office of Supervisory Jurisdiction ("OSJ") in California. Leeb was registered with the Commission from March 1999 to July 20, 2007, when the firm filed a broker-dealer withdrawal form ("BDW").

Background

4. Throughout the Relevant Period, Miller was president of Leeb and supervisor of Leeb's home office. He was the trading desk supervisor, was responsible for supervising firm-wide "penny stocks/microcap" activity, and was responsible for reviewing all trading activity for the firm, including activity at the OSJ.

5. During the Relevant Period, certain customers of Leeb routinely delivered into their accounts large blocks of privately obtained shares of penny stocks, which Leeb then sold to the public on behalf of the customers, without any registration statements being in effect.

6. The sales of penny stock shares were accompanied by a number of warning signs, or "red flags," involving the customers for whom the stocks were sold, the method and timing under which the penny stocks were sold, and the way that proceeds from the sales were subsequently routed.

7. For example, red flags associated with certain Leeb customers engaged in penny stock transactions included: (a) an individual with a prior pump-and-dump related consent

judgment; (b) persons whom registered representatives at Leeb knew or should have known were engaged in promotional activity in the same stocks they were selling; and (c) individuals who controlled more than one brokerage account under different corporate names.

8. Red flags associated with the way the penny stock shares were sold included: (a) repeated delivery in and selling to the public of privately obtained shares of penny stocks; (b) selling within weeks of receipt; (c) selling while promotional activity was occurring; and (d) sales that represented a high percentage of trading volume or of an issuer's public float.

9. In addition to the red flags described above, the accounts controlled by these customers and their transaction histories were suspicious in other respects. In one case, a stock promoter customer sold hundreds of millions of privately obtained shares of penny stocks through two separate corporate accounts that he controlled. Account opening documents for the accounts, however, identified his daughter as the sole proprietor and officer of both companies. In another case, there was an account held by a customer incorporated in Nevis that: was operated by persons in Vancouver; was submitting orders through traders in Costa Rica; was routinely delivering into its account privately obtained shares of penny stocks; and had, from October 2005 to June 2007, wired proceeds totaling over $30 million to a bank in Liechtenstein.

10. Despite the red flags described above suggesting that certain of Leeb's customers could be violating Section 5 of the Securities Act by engaging in illegal distributions of securities through their Leeb accounts, the registered representatives responsible for these accounts failed to conduct a reasonable inquiry regarding the securities delivered into Leeb customer accounts. They also failed to obtain documentation concerning how their customers acquired those securities or to make adequate inquiries into: the nature of the underlying transactions in which the purportedly "free-trading" stock had been obtained; the length of time the customers had held stock; the customers' intent to sell additional shares; or how the customers' selling activities compared with the issuer's outstanding share balance and trading volume.

11. The Leeb customer trading activity described above, as well as the absence of Low-Priced Securities Questionnaires for numerous penny stocks traded through customer accounts, reflected numerous red flags concerning whether the firm's registered representatives had made adequate inquiry into facts that could indicate unlawful distributions of stock were taking place.

12. Although Miller regularly reviewed the firm's penny stock trading activity and regularly communicated with the branch manager of the OSJ regarding penny stock activity conducted through the OSJ, Miller did not identify any red flags or question the source of any of the stock sold through the firm.

13. In addition, Miller ignored other red flags that he was aware of, such as repeated regulatory inquiries concerning certain customer accounts or specific penny stocks. Despite his concern over the number of such inquiries, Miller did not subject any registered representative or customer account to heightened scrutiny, did not question the registered

representatives regarding whether they conducted inquiries into the customers' penny stocks, and did not conduct additional account reviews.

14. As a result of the conduct described above, Miller failed reasonably to supervise certain registered representatives, within the meaning of Sections 15(b)(4) and 15(b)(6) of the Exchange Act, with a view to preventing their violations of Section 5 of the Securities Act.

15. The Bank Secrecy Act ("BSA"),[2] as implemented under rules promulgated by the U.S. Treasury Department's Financial Crimes Enforcement Network ("FinCEN"), requires that broker-dealers file Suspicious Activity Reports ("SARs") with FinCEN to report a transaction (or a pattern of transactions of which the transactions is a part) involving or aggregating to at least $5,000 that the broker-dealer knows, suspects, or has reason to suspect: (1) involves funds derived from illegal activity or was conducted to disguise funds derived from illegal activities; (2) is designed to evade any requirements of the BSA; (3) has no business or apparent lawful purpose and the broker-dealer knows of no reasonable explanation for the transaction after examining the available facts; or (4) involves use of the broker-dealer to facilitate criminal activity.[3]

16. Exchange Act Rule 17a-8 requires broker-dealers to comply with the reporting, recordkeeping and record retention requirements of the rules promulgated under the BSA. The failure to file a SAR as required by the SAR Rule is a violation of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder.

17. Leeb's Anti-Money Laundering ("AML") program enumerated a number of examples that could be indicative of the need to a file a SAR, including (i) a history of criminal, civil, or regulatory violations by the customer or an associate; (ii) multiple LLCs with the same address; (iii) multiple transfers of funds to or from bank secrecy jurisdictions, tax havens, or non-cooperative jurisdictions as identified by the Financial Action Task Force ("FATF") or FinCEN; and (iv) penny stock activity. Furthermore, Leeb's AML program charged all employees with responsibility for AML compliance, including identifying red flags that would be indicative of the need for Leeb to file a SAR.

18. The transactions described above were suspicious and Miller should have caused Leeb to file SARs. Miller knew of his obligation to assist Leeb in fulfilling its requirement to file SARs, and knew or was reckless in not knowing that significant suspicious activity was not being reported by Leeb as a result of his actions.

---

2 Currency and Financial Transactions Reporting Act of 1970 (the "Bank Secrecy Act"), 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959, and 31 U.S.C. §§ 5311-5330. The Bank Secrecy Act was most recently amended by the USA PATRIOT Act. *See* Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. L. No. 107-56, 115 Stat. 296 (2001).

3 31 C.F.R. §103.19 ("SAR Rule").

19. Based on the conduct described above, Miller willfully aided and abetted and caused Leeb's violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder.

Undertakings

20. Respondent undertakes to cooperate fully with the Commission in any and all investigations, litigations or proceedings relating to or arising from the matters described in the Order. In connection with such cooperation, Respondent undertakes:

a. To produce, without service of a notice or subpoena, any and all documents and other information reasonably requested by the Commission's staff;

b. To be interviewed by the Commission's staff at such times as the staff may reasonably request and to appear and testify truthfully and completely without service of a notice or subpoena in such investigations, depositions, hearings or trials as may be requested by the Commission's staff; and

c. That in connection with any testimony of Respondent to be conducted at deposition, hearing or trial pursuant to any notice or subpoena, Respondent agrees that any such notice or subpoena for his appearance and testimony may be served by regular mail and facsimile on his counsel, George Brunelle, Brunelle & Hadjikow, P.C., 1 Whitehall Street, 18th Floor, New York, NY 10004, Fax No. (212) 809-3219.

21. Respondent shall provide to the Commission, within thirty days after the end of the twelve-month suspension period described below, an affidavit that he has complied fully with the sanctions described in Section IV.A, IV.B, and IV.C below.

In determining whether to accept the Offer, the Commission has considered these undertakings.

IV.

On the basis of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer.

Accordingly, pursuant to Sections 15(b) and 21C of the Exchange Act it is hereby ORDERED that:

A. Respondent Miller shall cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder;

B. Respondent Miller be, and hereby is, suspended from association in a supervisory capacity with any broker or dealer for a period of twelve months, effective on the second Monday following the entry of this Order.

C. Respondent shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of $50,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Such payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies Eugene Miller as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to David Stoelting, Senior Trial Counsel, and to Robert J. Keyes, Associate Regional Director, Securities and Exchange Commission, 3 World Financial Center, Room 400, New York, New York, 10281-1022.

D. Respondent shall comply with the undertaking set forth in paragraph 21 above.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62752 / August 20, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3173 / August 20, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14013

In the Matter of **MATTHEW W. HARDEY,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against Matthew W. Hardey ("Respondent" or "Hardey") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

been written-off as required by Generally Accepted Accounting Principles ("GAAP"), the associated bad debt expenses would have caused Newpark to report a significant net loss in its Form 10-K for the fiscal year ended December 31, 2003 as opposed to the $494,000 of net income that the company actually reported in the filing.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent Hardey's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that Hardey is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62751 / August 20, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3172 / August 20, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14012

In the Matter of **L. CYRUS DeBLANC,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against L. Cyrus DeBlanc ("Respondent" or "DeBlanc") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III. 3 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. DeBlanc, age 58, was a comptroller and CFO of Newpark Resources, Inc.'s ("Newpark") subsidiary Soloco, LLC ("Soloco") from 1992 until his termination in 2006. In that capacity, DeBlanc was responsible for the accuracy of Soloco's financial statements. DeBlanc has never had a CPA license. Newpark dismissed DeBlanc in June 2006 for his involvement in the transactions at issue in the civil proceeding filed against him by the Commission.

2. Newpark was, at all relevant times, a Delaware corporation with its principal place of business in New Orleans, Louisiana. Newpark was engaged in the business of operating as a diversified oil and gas industry supplier with three operating segments: fluid systems and engineering, mat and integrated services, and environmental services. At all relevant times, Newpark's common stock was registered with the Commission pursuant to Section 12(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and traded on the New York Stock Exchange.

3. On July 16, 2009, the Commission filed a complaint against DeBlanc in SEC v. Matthew W. Hardey, L. Cyrus DeBlanc and Joe E. Penland, Civil Action No. 09-4414 (E.D. La.). On May 14, 2010, the court entered an order permanently enjoining DeBlanc, by consent, from future violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5, 13b2-1 and 13b2-2 thereunder, and from aiding and abetting violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11 and 13a-13 thereunder. DeBlanc was also ordered to pay a $75,000 civil money penalty and was barred from serving as an officer and director of a public company.

4. The Commission's Complaint alleged, among other things, that DeBlanc engaged in a fraudulent scheme which resulted in Newpark filing materially false and misleading financial statements in the company's annual report on Form 10-K for the fiscal year ended December 31, 2003. The Complaint alleged that DeBlanc engaged in a number of improper accounting practices that enabled Newpark to avoid writing-off approximately $4.2 million of its reported receivables in the annual financial statements for fiscal year 2003. If such receivables had

been written-off as required by Generally Accepted Accounting Principles ("GAAP"), the associated bad debt expenses would have caused Newpark to report a significant net loss in its Form 10-K for the fiscal year ended December 31, 2003 as opposed to the $494,000 of net income that the company actually reported in the filing.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent DeBlanc's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that DeBlanc is suspended from appearing or practicing before the Commission as an accountant.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Commissioner Casey
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62749 / August 20, 2010

INVESTMENT ADVISERS ACT OF 1940
Release No. 3070 / August 20, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14011

In the Matter of **GREGORY TODD FRONING,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against Gregory Todd Froning ("Respondent").

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Section 203(f) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. Froning, age 48, is a resident of Coppell, Texas. From at least January 1, 2005 through October 29, 2009, Froning was a registered representative associated with broker-dealers and investment advisers registered with the Commission.

2. On August 3, 2010, an Interlocutory Judgment of Permanent Injunction was entered by consent against Froning, permanently enjoining him from future violations of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder, in the civil action entitled *Securities and Exchange Commission v. Gregory Todd Froning*, Civil Action Number 3:10-cv-01503 in the United States District Court for the Northern District of Texas.

3. The Commission's complaint in the civil action alleged, among other things, that, while serving as a registered representative associated with broker-dealers and investment advisers, Froning conducted an unregistered offering of promissory notes to his brokerage and advisory clients without disclosing material information pertaining to the offering or the use of funds.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Froning's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 15(b)(6) of the Exchange Act and Section 203(f) of the Advisers Act, that Respondent Froning be, and hereby is barred from association with any broker, dealer, or investment adviser.

Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62761 / August 24, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3175 / August 24, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14018

In the Matter of **STEPHEN BURKE, CPA** **Respondent.**	**ORDER INSTITUTING PUBLIC ADMINISTRATIVE AND CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTIONS 4C AND 21C OF THE SECURITIES EXCHANGE ACT OF 1934 AND RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS AND A CEASE-AND-DESIST ORDER**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate that public administrative and cease-and-desist proceedings be, and hereby are, instituted against Stephen Burke, CPA ("Respondent" or "Burke") pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 102(e)(l)(iii) of the Commission's Rules of Practice.

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Sections 4C and 21C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

1. These proceedings arise out of material misstatements of revenue and net income by Fischer Imaging Corporation ("Fischer") in its filings on Form 10-Q for the second and third quarters of 2002. From January 2000 through September 2002, Fischer materially misstated revenue and net income in its financial statements as a result of, among other things, Fischer's improper recognition of revenue from equipment orders upon shipment to warehouses controlled by Fischer. Burke was hired as a consultant by Fischer's board of directors in March, 2002, and received information regarding this practice shortly thereafter. After Burke became Fischer's CFO in October 2002, Burke signed an amended quarterly filing for Fischer's second quarter of 2002 and signed Fischer's quarterly filing for the third quarter of 2002 without taking sufficient steps to determine whether Fischer's revenue recognition practices were appropriate. Further, despite his knowledge of Fischer's shipments to storage facilities, Burke did not take sufficient steps to implement a system of internal accounting controls to ensure that Fischer's revenue and net income were properly reported. Through his inactions, Burke violated and aided and abetted violations of the reporting, internal controls and books and records provisions of the Exchange Act. Burke also made or caused to be made false or misleading statements to Fischer's external auditors regarding Fischer's revenue recognition practices and provided false certifications in connection with Fischer's amended filing for the second quarter of 2002 and Fischer's quarterly filing for the third quarter of 2002.

Respondent

2. Stephen Burke, age 61, of Lake Bluff, Illinois, was a consultant for Fischer's board of directors from March 2002 through October 2002. Burke was Fischer's CFO, executive vice president of finance, and secretary from October 2002 to January 2004. Burke has held a Minnesota CPA license since 1998, which is currently inactive. In 2005, the Commission filed a civil injunctive action in the U. S. District Court for the District of Colorado against Burke and five other Fischer executives and board members based on their roles in Fischer's improper revenue recognition and other accounting misstatements. SEC v. Louis E. Rivelli, et al., Civil Action No. 1:05-cv-01039 (D.Colo).

Other Relevant Entity

3. Fischer Imaging Corporation, during the relevant period, was a Delaware corporation with its principal place of business in Denver, Colorado. Fischer was dissolved as of May 18, 2007, pursuant to a Chapter 11 Liquidating Plan. Prior to its dissolution, Fischer designed, manufactured, and marketed specialty medical imaging systems used for the diagnosis and screening of disease. Fischer's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act and Fischer was required to file periodic reports with the SEC on Forms 10-K and 10-Q. In 2004, the Commission imposed a cease-and-desist order

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

against Fischer for violations of the anti-fraud, reporting, internal controls and books and records provisions of the federal securities laws resulting from Fischer's improper revenue recognition and other accounting misstatements. In the Matter of Fischer Imaging Corp., Exchange Act Rel. No. 34-50663 (Nov. 15, 2004).

Facts

A. Fischer's Improper Revenue Recognition

4. From January 2000 through September 2002, Fischer improperly recognized revenue upon shipment of products to storage facilities rather than upon shipment to customers or customer designated locations. Fischer paid for the storage costs while the equipment was at these storage facilities, insured the equipment, and continued to exercise control over it. It was improper under Generally Accepted Accounting Principles ("GAAP") for Fischer to recognize revenue on these orders at the time they were shipped to the storage facilities because, among other reasons, delivery had not occurred and the revenue had not been earned. As a result of these and other improper revenue recognition practices, Fischer materially misstated its revenue and net income in its filings with the Commission from January 2000 through September 2002.

B. Burke's Conduct

5. In March 2002, Burke was hired by Fischer's board of directors to work at Fischer's headquarters as a consultant and was charged with addressing various accounting issues about which the board had concerns. Through his role as a Fischer consultant Burke became aware that Fischer recognized revenue for certain sales when products were shipped to storage facilities, rather than when they were shipped to customers or customer designated locations. Burke also learned that Fischer was constrained from collecting accounts receivable related to products that were in storage.

6. Burke became Fischer's CFO in October 2002. Despite Burke's knowledge of Fischer's practice of recognizing revenue upon shipment to storage facilities rather than to customer locations, he failed to implement a sufficient system of internal controls designed to provide reasonable assurances that Fischer reported its revenue and net income in conformity with GAAP. Burke also circumvented or failed to implement the internal controls Fischer did have and caused Fischer's revenue and net income to be falsified through his failure to fully investigate Fischer's practice of recognizing revenue on shipments to storage facilities.

7. After Burke became Fischer's CFO in October 2002, he reviewed and signed Fischer's amended filing on Form 10-Q for the quarter ended June 30, 2002, which Fischer filed on November 14, 2002, and Fischer's quarterly filing on Form 10-Q for the quarter ended September 29, 2002. Fischer's revenue and net income were materially misstated in these filings and in Fischer's books and records as a result of Fischer's improper revenue practices. In connection with these filings, Burke signed certifications that falsely stated that to the best of his knowledge, they complied with the requirements of Section 13(a) of the Exchange Act and fairly presented, in all material respects, the financial condition and results of operations of Fischer. Burke signed these certifications without taking sufficient steps to investigate whether Fischer's revenue recognition practices rendered the certifications false.

8. Burke also made materially false or misleading statements to Fischer's external auditors in connection with their reviews of Fischer's filings for the second and third quarters of 2002 regarding Fischer's revenue recognition practices and aged accounts receivable associated with orders that were in storage. Additionally, Burke signed management representation letters that contained false or misleading statements regarding, among other things, Fischer's revenue recognition practices and the validity of sales and associated receivables recorded in Fischer's accounting records.

Violations

9. Section 13(a) of the Exchange Act and Rule 13a-13 thereunder require issuers with securities registered under Section 12 of the Exchange Act to file quarterly and other periodic reports with the Commission and to keep this information current. The obligation to file such reports embodies the requirement that they be true and correct. *See, e.g., SEC v. Savoy Indus., Inc.*, 587 F.2d 1149, 1165 (D.C. Cir. 1978), *cert. denied*, 440 U.S. 913 (1979). In addition to the information expressly required to be included in a statement or report, Rule 12b-20 requires that there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.

10. As discussed above, Burke caused Fischer to file false and misleading quarterly reports with the Commission for the second and third quarters of 2002 that misrepresented the revenue and net income of Fischer. By his conduct described above, Burke willfully aided and abetted and caused Fischer's violations of Section 13(a) of the Exchange Act and Rules 13a-13 and Rule 12b-20 thereunder.

11. Section 13(b)(2)(A) of the Exchange Act requires Section 12 registrants to make and keep books, records, and accounts that accurately and fairly reflect the transactions and dispositions of their assets. Section 13(b)(2)(B) requires registrants to devise and maintain a system of internal accounting controls that, among other things, provides reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP. Section 13(b)(5) provides that no person shall knowingly falsify any book, record, or account or circumvent internal controls. Rule 13b2-1 prohibits the falsification of any book, record, or account subject to Section 13(b)(2)(A).

12. As a result of the conduct described above, Burke willfully violated Section 13(b)(5) of the Exchange Act and Rule 13b2-1 thereunder, and willfully aided and abetted and caused Fischer's violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act.

13. As a result of the conduct described above, Burke willfully violated Rule 13b2-2 under the Exchange Act which prohibits a director or officer of an issuer from, among other things, directly or indirectly, making or causing to be made a materially false or misleading statement to an accountant in connection with any audit, review or examination of the financial statements of the issuer required to be made pursuant to Section 13(b)(2) of the Exchange Act.

14. As a result of the conduct described above, Burke willfully violated Rule 13a-14 under the Exchange Act which sets forth the requirements for certain reports filed under Section

13(a) of the Exchange Act to include specified certifications by each principal executive and principal financial officer of the issuer.

Findings

Based on the foregoing, the Commission finds that Burke (a) willfully violated Section 13(b)(5) of the Exchange Act and Rules 13b2-1, 13b2-2, and 13a-14 promulgated thereunder; and (b) willfully aided and abetted and caused Fischer's violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act, and Rules 12b-20 and 13a-13 promulgated thereunder.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Burke's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Burke shall cease and desist from committing or causing any violations and any future violations of Section 13(b)(5) of the Exchange Act and Rules 13b2-1, 13b2-2, and 13a-14 promulgated thereunder; and from causing any violations and any future violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act, and Rules 12b-20 and 13a-13 promulgated thereunder.

B. Burke is denied the privilege of appearing or practicing before the Commission as an accountant.

C. After 36 months from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the Respondent's or the firm's quality control system that would indicate that the Respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

D. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Casey and Commissioner Paredes Disapproved

SECURITIES AND EXCHANGE COMMISSION

17 CFR PARTS 200, 232, 240 and 249

[Release Nos. 33-9136; 34-62764; IC-29384; File No. S7-10-09]

RIN 3235-AK27

FACILITATING SHAREHOLDER DIRECTOR NOMINATIONS

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: We are adopting changes to the federal proxy rules to facilitate the effective exercise of shareholders' traditional state law rights to nominate and elect directors to company boards of directors. The new rules will require, under certain circumstances, a company's proxy materials to provide shareholders with information about, and the ability to vote for, a shareholder's, or group of shareholders', nominees for director. We believe that these rules will benefit shareholders by improving corporate suffrage, the disclosure provided in connection with corporate proxy solicitations, and communication between shareholders in the proxy process. The new rules apply only where, among other things, relevant state or foreign law does not prohibit shareholders from nominating directors. The new rules will require that specified disclosures be made concerning nominating shareholders or groups and their nominees. In addition, the new rules provide that companies must include in their proxy materials, under certain circumstances, shareholder proposals that seek to establish a procedure in the company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. We also are adopting related changes to certain of our other rules and regulations, including the existing solicitation exemptions from our proxy rules and the beneficial ownership reporting requirements.

EFFECTIVE DATE: [insert date 60 days after the date of publication in the Federal Register]

COMPLIANCE DATES: [insert date 60 days after the date of publication in the Federal Register], except that companies that qualify as "smaller reporting companies" (as defined in § 17 CFR 240.12b-2) as of the effective date of the rule amendments will not be subject to Rule 14a-11 until three years after the effective date.

FOR FURTHER INFORMATION CONTACT: Lillian Brown, Tamara Brightwell, or Ted Yu, Division of Corporation Finance, at (202) 551-3200, or, with regard to investment companies, Kieran G. Brown, Division of Investment Management, at (202) 551-6784, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549.

SUPPLEMENTARY INFORMATION: We are adding new Rule 82a of Part 200 Subpart D – Information and Requests,[1] and new Rules 14a-11,[2] and 14a-18,[3] and new Regulation 14N[4] and Schedule 14N,[5] and amending Rule 13[6] of Regulation S-T,[7] Rules 13a-11,[8] 13d-1,[9] 14a-2,[10] 14a-4,[11] 14a-5,[12] 14a-6,[13] 14a-8,[14] 14a-9,[15] 14a-12,[16] and 15d-11,[17] Schedule 13G,[18] Schedule 14A,[19]

---

1 17 CFR 200.82a.

2 17 CFR 240.14a-11.

3 17 CFR 240.14a-18.

4 17 CFR 240.14n et seq.

5 17 CFR 240.14n-101.

6 17 CFR 232.13.

7 17 CFR 232.10 et seq.

8 17 CFR 240.13a-11.

9 17 CFR 240.13d-1.

10 17 CFR 240.14a-2.

11 17 CFR 240.14a-4.

12 17 CFR 240.14a-5.

and Form 8-K,[20] under the Securities Exchange Act of 1934.[21] Although we are not amending Schedule 14C[22] under the Exchange Act, the amendments will affect the disclosure provided in Schedule 14C, as Schedule 14C requires disclosure of some items contained in Schedule 14A.

---

13 17 CFR 240.14a-6.

14 17 CFR 240.14a-8.

15 17 CFR 240.14a-9.

16 17 CFR 240.14a-12.

17 17 CFR 240.15d-11.

18 17 CFR 240.13d-102.

19 17 CFR 240.14a-101.

20 17 CFR 249.308.

21 15 U.S.C. 78a et seq. (the "Exchange Act"). Part 200 Subpart D – Information and Requests and Regulation S-T are also promulgated under the Securities Act of 1933 [15 U.S.C. 77a et seq.] (the "Securities Act").

22 17 CFR 240.14c-101.

Table of Contents

I. BACKGROUND AND OVERVIEW OF AMENDMENTS

A. Background

On June 10, 2009, we proposed a number of changes to the federal proxy rules designed to facilitate shareholders' traditional state law rights to nominate and elect directors. Our proposals sought to accomplish this goal in two ways: (1) by facilitating the ability of shareholders with a significant, long-term stake in a company to exercise their rights to nominate and elect directors by establishing a minimum standard for including disclosure concerning, and enabling shareholders to vote for, shareholder director nominees in company proxy materials; and (2) by narrowing the scope of the Commission rule that permitted companies to exclude shareholder proposals that sought to establish a procedure for the inclusion of shareholder nominees in company proxy materials.[23] We recognized at that time that the financial crisis that the nation and markets had experienced heightened the serious concerns of many shareholders about the accountability and responsiveness of some companies and boards of directors to shareholder interests, and that these concerns had resulted in a loss of investor confidence. These concerns also led to questions about whether boards were exercising appropriate oversight of management, whether boards were appropriately focused on shareholder interests, and whether boards need to be more accountable for their decisions regarding issues such as compensation structures and risk management.

---

[23] See Facilitating Shareholder Director Nominations, Release No. 33-9046, 34-60089 (June 10, 2009) [74 FR 29024] ("Proposal" or "Proposing Release"). The Proposing Release was published for comment in the Federal Register on June 18, 2009, and the initial comment period closed on August 17, 2009. The Commission re-opened the comment period as of December 18, 2009 for thirty days to provide interested persons the opportunity to comment on additional data and related analyses that were included in the public comment file at or following the close of the original comment period. In total, the Commission received approximately 600 comment letters on the proposal. The public comments we received are available on our website at http://www.sec.gov/comments/s7-10-09/s71009.shtml. Comments also are available for website viewing and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m.

A principal way that shareholders can hold boards accountable and influence matters of corporate policy is through the nomination and election of directors. The ability of shareholders to effectively use their power to nominate and elect directors is significantly affected by our proxy regulations because, as has long been recognized, a federally-regulated corporate proxy solicitation is the primary way for public company shareholders to learn about the matters to be decided by the shareholders and to make their views known to company management.[24] As discussed in detail below, in light of these concerns, we reviewed our proxy regulations to determine whether they should be revised to facilitate shareholders' ability to nominate and elect directors. We have taken into consideration the comments received on the proposed amendments as well as subsequent congressional action[25] and are adopting final rules that will, for the first time, require company proxy materials, under certain circumstances, to provide shareholders with information about, and the ability to vote for a shareholder's, or group of shareholders', nominees for director. We also are amending our proxy rules to provide

---

24 See, e.g., Securit[ies] and Exchange Commission Proxy Rules: Hearings on H.R. 1493, H.R. 1821, and H.R. 2019 Before the House Comm. on Interstate and Foreign Commerce, 78th Cong., 1st Sess., at 17-19 (1943) (Statement of the Honorable Ganson Purcell, Chairman, Securities and Exchange Commission) (explaining the initial Commission rules requiring the inclusion of shareholder proposals in company proxy materials: "We give [a stockholder] the right in the rules to put his proposal before all of his fellow stockholders along with all other proposals ... so that they can see then what they are and vote accordingly. ... The rights that we are endeavoring to assure to the stockholders are those rights that he has traditionally had under State law, to appear at the meeting; to make a proposal; to speak on that proposal at appropriate length; and to have his proposal voted on. But those rights have been rendered largely meaningless through the process of dispersion of security ownership through[out] the country.... [T]he assurance of these fundamental rights under State laws which have been, as I say, completely ineffective ... because of the very dispersion of the stockholders' interests throughout the country[;] whereas formerly ... a stockholder might appear at the meeting and address his fellow stockholders[, t]oday he can only address the assembled proxies which are lying at the head of the table. The only opportunity that the stockholder has today of expressing his judgment comes at the time he considers the execution of his proxy form, and we believe ... that this is the time when he should have the full information before him and ability to take action as he sees fit."); see also S. Rep. 792, 73d Cong., 2d Sess., 12 (1934) ("[I]t is essential that [the stockholder] be enlightened not only as to the financial condition of the corporation, but also as to the major questions of policy, which are decided at stockholders' meetings.").

25 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §971, 124 Stat. 1376 (2010) ("Dodd-Frank Act").

shareholders the ability to include in company proxy materials, under certain circumstances, shareholder proposals that seek to establish a procedure in the company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials.

Regulation of the proxy process was one of the original responsibilities that Congress assigned to the Commission as part of its core functions in 1934. The Commission has actively monitored the proxy process since receiving this authority and has considered changes when it appeared that the process was not functioning in a manner that adequately protected the interests of investors.[26] One of the key tenets of the federal proxy rules on which the Commission has consistently focused is whether the proxy process functions, as nearly as possible, as a replacement for an actual in-person meeting of shareholders.[27] This is important because the proxy process represents shareholders' principal means of participating effectively at an annual or special meeting of shareholders.[28] In our Proposal we noted our concern that the federal proxy rules may not be facilitating the exercise of shareholders' state law rights to nominate and elect

---

26 For example, the Commission has considered changes to the proxy rules related to the election of directors in recent years. See Security Holder Director Nominations, Release No. 34-48626 (October 14, 2003) [68 FR 60784] ("2003 Proposal"); Shareholder Proposals, Release No. 34-56160 (July 27, 2007) [72 FR 43466] ("Shareholder Proposals Proposing Release"); Shareholder Proposals Relating to the Election of Directors, Release No. 34-56161 (July 27, 2007) [72 FR 43488] ("Election of Directors Proposing Release"); and Shareholder Proposals Relating to the Election of Directors, Release No. 34-56914 (December 6, 2007) [72 FR 70450] ("Election of Directors Adopting Release"). When we refer to the "2007 Proposals" and the comments received in 2007, we are referring to the Shareholder Proposals Proposing Release and the Election of Directors Proposing Release and the comments received on those proposals, unless otherwise specified.

27 Professor Karmel has described the Commission's proxy rules as having the purpose "to make the proxy device the closest practicable substitute for attendance at the [shareholder] meeting." Roberta S. Karmel, The New Shareholder and Corporate Governance: Voting Power Without Responsibility or Risk: How Should Proxy Reform Address the De-Coupling of Economic and Voting Rights?, 55 VILL. L. REV. 93, 104 (2010).

28 Historically, a shareholder's voting rights generally were exercised at a shareholder meeting. As discussed in the Proposing Release, in passing the Exchange Act, Congress understood that the securities of many companies were held through dispersed ownership, at least in part facilitated by stock exchange listing of shares. Although voting rights in public companies technically continued to be exercised at a meeting, the votes cast at the meeting were by proxy and the voting decision was made during the proxy solicitation process. This structure continues to this day.

directors. Without the ability to effectively utilize the proxy process, shareholder nominees do not have a realistic prospect of being elected because most, if not all, shareholders return their proxy cards in advance of the shareholder meeting and thus, in essence, cast their votes before the meeting at which they may nominate directors. Recognizing that this failure of the proxy process to facilitate shareholder nomination rights has a practical effect on the right to elect directors, the new rules will enable the proxy process to more closely approximate the conditions of the shareholder meeting. In addition, because companies will be required to include shareholder-nominated candidates for director in company proxy materials, shareholders will receive additional information upon which to base their voting decisions. Finally, we believe these changes will significantly enhance the confidence of shareholders who link the recent financial crisis to a lack of responsiveness of some boards to shareholder interests.[29]

The Commission has, on a number of prior occasions, considered whether its proxy rules needed to be amended to facilitate shareholders' ability to nominate directors by having their nominees included in company proxy materials.[30] Most recently, in June 2009, we proposed amendments to the proxy rules that included both a new proxy rule, Exchange Act Rule 14a-11, that would require a company's proxy materials to provide shareholders with information about, and the ability to vote for, candidates for director nominated by long-term shareholders or groups

29 See letters from American Federation of Labor and Congress of Industrial Organizations ("AFL-CIO"); California Public Employees' Retirement System ("CalPERS"); Council of Institutional Investors ("CII"); Lynne L. Dallas ("L. Dallas"); Los Angeles County Employees Retirement Association ("LACERA"); Laborers' International Union of North America ("LIUNA"); The Nathan Cummings Foundation ("Nathan Cummings Foundation"); Pax World Management Corp. ("Pax World"); Pershing Square Capital Management, L.P. ("Pershing Square"); Relational Investors, LLC ("Relational"); RiskMetrics Group, Inc. ("RiskMetrics"); Shareowner Education Network and Shareowners.org ("Shareowners.org"); Social Investment Forum ("Social Investment Forum"); State of Wisconsin Investment Board ("SWIB"); International Brotherhood of Teamsters ("Teamsters"); Trillium Asset Management Corporation ("Trillium"); Universities Superannuation Scheme – UK ("Universities Superannuation"); Washington State Investment Board ("WSIB").

30 For a discussion of the Commission's previous actions in this area, see the Proposing Release and the 2003 Proposal.

of long-term shareholders with significant holdings, and amendments to Rule 14a-8(i)(8) to prohibit exclusion of certain shareholder proposals seeking to establish a procedure in the company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. We received significant comment on the proposed amendments. Overall, commenters were sharply divided on the necessity for, and the workability of, the proposed amendments. Supporters of the amendments generally believed that, if adopted, they would facilitate shareholders' ability to exercise their state law right to nominate directors and provide meaningful opportunities to effect changes in the composition of the board.[31] These commenters predicted that the amendments would lead to more accountable, responsive, and effective boards.[32] Many commenters saw a link between the recent economic crisis and shareholders' inability to have nominees included in a company's proxy materials.[33]

Commenters opposed to our Proposal believed that recent corporate governance developments, including increased use of a majority voting standard for the election of directors and certain state law changes, already provide shareholders with meaningful opportunities to participate in director elections.[34] These commenters viewed the amendments as inappropriately

---

31 See letters from CII; Colorado Public Employees' Retirement Association ("COPERA"); CtW Investment Group ("CtW Investment Group"); L. Dallas; Thomas P. DiNapoli ("T. DiNapoli"); Florida State Board of Administration ("Florida State Board of Administration"); International Corporate Governance Network ("ICGN"); Denise L. Nappier ("D. Nappier"); Ohio Public Employees Retirement System ("OPERS"); Pax World; Teamsters.

32 Id.

33 See letters from AFL-CIO; CalPERS; California State Teachers' Retirement System ("CalSTRS"); CII; L. Dallas; LACERA; LIUNA; Nathan Cummings Foundation; Pax World; Pershing Square; Relational; RiskMetrics; Shareowners.org; Social Investment Forum; SWIB; Teamsters; Trillium; Universities Superannuation; WSIB.

34 See letters from Group of 26 Corporate Secretaries and Governance Professionals ("26 Corporate Secretaries"); 3M Company ("3M"); Advance Auto Parts, Inc. ("Advance Auto Parts"); The Allstate Corporation ("Allstate"); Avis Budget Group, Inc. ("Avis Budget"); American Express Company ("American Express"); Anadarko Petroleum Corporation ("Anadarko"); Association of Corporate Counsel ("Association of Corporate Counsel"); AT&T Inc. ("AT&T"); Lawrence Behr ("L. Behr"); Best Buy Co., Inc. ("Best Buy"); The Boeing Company ("Boeing"); Business Roundtable ("BRT"); Robert N. Burt ("R.

intruding into matters traditionally governed by state law or imposing a "one size fits all" rule for all companies and expressed concerns about "special interest" directors, forcing companies to focus on the short-term rather than the creation of long-term shareholder value, and other perceived negative effects of the amendments, if adopted, on boards and companies.[35] Finally,

---

Burt"); State Bar of California, Corporations Committee of Business Law Section ("California Bar"); Sean F. Campbell ("S. Campbell"); Carlson ("Carlson"); Caterpillar Inc. ("Caterpillar"); U.S. Chamber of Commerce Center for Capital Markets Competitiveness ("Chamber of Commerce/CMCC"); Chevron Corporation ("Chevron"); CIGNA Corporation ("CIGNA"); W. Don Cornwell ("W. Cornwell"); CSX Corporation ("CSX"); Cummins Inc. ("Cummins"); Davis Polk & Wardwell LLP ("Davis Polk"); Dewey & LeBoeuf ("Dewey"); E.I. du Pont de Nemours and Company ("DuPont"); Eaton Corporation ("Eaton"); Michael Eng ("M. Eng"); FedEx Corporation ("FedEx"); FMC Corporation ("FMC Corp."); FPL Group, Inc. ("FPL Group"); Frontier Communications Corporation ("Frontier"); General Electric Company ("GE"); General Mills, Inc. ("General Mills"); Charles O. Holliday, Jr. ("C. Holliday"); Honeywell International Inc. ("Honeywell"); Constance J. Horner ("C. Horner"); International Business Machines Corporation ("IBM"); Jones Day ("Jones Day"); Keating Muething & Klekamp PLL ("Keating Muething"); James M. Kilts ("J. Kilts"); Reatha Clark King, Ph.D. ("R. Clark King"); Ned C. Lautenbach ("N. Lautenbach"); MeadWestvaco Corporation ("MeadWestvaco"); MetLife, Inc. ("MetLife"); Motorola, Inc. ("Motorola"); O'Melveny & Myers LLP ("O'Melveny & Myers"); Office Depot, Inc. ("Office Depot"); Pfizer Inc. ("Pfizer"); Protective Life Corporation ("Protective"); Sullivan & Cromwell LLP ("S&C"); Safeway Inc. ("Safeway"); Sara Lee Corporation ("Sara Lee"); Shearman & Sterling LLP ("Shearman & Sterling"); The Sherwin-Williams Company ("Sherwin-Williams"); Sidley Austin LLP ("Sidley Austin"); Simpson Thacher & Bartlett LLP ("Simpson Thacher"); Tesoro Corporation ("Tesoro"); Textron Inc. ("Textron"); Texas Instruments Corporation ("TI"); Gary L. Tooker ("G. Tooker"); UnitedHealth Group Incorporated ("UnitedHealth"); Unitrin, Inc. ("Unitrin"); U.S. Bancorp ("U.S. Bancorp"); Wachtell, Lipton, Rosen & Katz ("Wachtell"); Wells Fargo & Company ("Wells Fargo"); West Chicago Chamber of Commerce & Industry ("West Chicago Chamber"); Weyerhaeuser Company ("Weyerhaeuser"); Xerox Corporation ("Xerox"); Yahoo! ("Yahoo").

35 See letters from 26 Corporate Secretaries; American Bar Association ("ABA"); ACE Limited ("ACE"); Advance Auto Parts; AGL Resources ("AGL"); Aetna Inc. ("Aetna"); Allstate; Alston & Bird LLP ("Alston & Bird"); American Bankers Association ("American Bankers Association"); The American Business Conference ("American Business Conference"); American Electric Power Company, Inc. ("American Electric Power"); Anadarko; Applied Materials, Inc. ("Applied Materials"); Artistic Land Designs LLC ("Artistic Land Designs"); Association of Corporate Counsel; Avis Budget; Atlantic Bingo Supply, Inc. ("Atlantic Bingo"); L. Behr; Best Buy; Biogen Idec Inc. ("Biogen"); James H. Blanchard ("J. Blanchard"); Boeing; Tammy Bonkowski ("T. Bonkowski"); BorgWarner Inc. ("BorgWarner"); Boston Scientific Corporation ("Boston Scientific"); The Brink's Company ("Brink's"); BRT; Burlington Northern Santa Fe Corporation ("Burlington Northern"); R. Burt; California Bar; Callaway Golf Company ("Callaway"); S. Campbell; Carlson; Carolina Mills ("Carolina Mills"); Caterpillar; Chamber of Commerce/CMCC; Chevron; Rebecca Chicko ("R. Chicko"); CIGNA; Comcast Corporation ("Comcast"); Competitive Enterprise Institute's Center for Investors and Entrepreneurs ("Competitive Enterprise Institute"); W. Cornwell; CSX; Edwin Culwell ("E. Culwell"); Cummins; Darden Restaurants, Inc. ("Darden Restaurants"); Daniels Manufacturing Corporation ("Daniels Manufacturing"); Davis Polk; Delaware State Bar Association ("Delaware Bar"); Tom Dermody ("T. Dermody"); Devon Energy Corporation ("Devon"); DTE Energy Company ("DTE Energy"); Eaton; The Edison Electric Institute ("Edison Electric Institute"); Eli Lilly and Company ("Eli Lilly"); Emerson Electric Co. ("Emerson Electric"); M. Eng; Erickson Retirement Communities, LLC ("Erickson"); ExxonMobil Corporation ("ExxonMobil"); FedEx; Financial Services Roundtable ("Financial Services Roundtable"); Flutterby Kissed Unique Treasures ("Flutterby"); FPL Group; Frontier; GE; Allen C. Goolsby ("A. Goolsby"); C.

commenters worried about the impact of the proposed amendments on small businesses.[36]

After considering the comments and weighing the competing interests of facilitating shareholders' ability to exercise their state law rights to nominate and elect directors against

---

Holliday; IBM; Investment Company Institute ("ICI"); Intelect Corporation ("Intelect"); JPMorgan Chase & Co. ("JPMorgan Chase"); Jones Day; R. Clark King; Leggett & Platt Incorporated ("Leggett"); Teresa Liddell ("T. Liddell"); Little Diversified Architectural Consulting ("Little"); McDonald's Corporation ("McDonald's"); MeadWestvaco; MedFaxx, Inc. ("MedFaxx"); Medical Insurance Services ("Medical Insurance"); MetLife; Mary S. Metz ("M. Metz"); Microsoft Corporation ("Microsoft"); John R. Miller ("J. Miller"); Marcelo Moretti ("M. Moretti"); Motorola; National Association of Corporate Directors ("NACD"); National Association of Manufacturers ("NAM"); National Investor Relations Institute ("NIRI"); O'Melveny & Myers; Office Depot; Omaha Door & Window ("Omaha Door"); The Procter & Gamble Company ("P&G"); PepsiCo, Inc. ("PepsiCo"); Pfizer; Realogy Corporation ("Realogy"); Jared Robert ("J. Robert"); Marissa Robert ("M. Robert"); RPM International Inc. ("RPM"); Ryder System, Inc. ("Ryder"); Safeway; Ralph S. Saul ("R. Saul"); Shearman & Sterling; Sherwin-Williams; Raymond F. Simoneau ("R. Simoneau"); Society of Corporate Secretaries and Governance Professionals, Inc. ("Society of Corporate Secretaries"); The Southern Company ("Southern Company"); Southland Properties, Inc. ("Southland"); The Steele Group ("Steele Group"); Style Crest Enterprises, Inc. ("Style Crest"); Tesoro; Textron; Theragenics Corporation ("Theragenics"); TI; Richard Trummel ("R. Trummel"); Terry Trummel ("T. Trummel"); Viola Trummel ("V. Trummel"); tw telecom inc. ("tw telecom"); Laura D'Andrea Tyson ("L. Tyson"); United Brotherhood of Carpenters and Joiners of America ("United Brotherhood of Carpenters"); UnitedHealth; U.S. Bancorp; VCG Holding Corporation ("VCG"); Wachtell; The Way to Wellness ("Wellness"); Wells Fargo; Whirlpool Corporation ("Whirlpool"); Xerox; Yahoo; Jeff Young ("J. Young").

36 See letters from ABA; American Mailing Service ("American Mailing"); All Cast, Inc. ("All Cast"); Always N Bloom ("Always N Bloom"); American Carpets ("American Carpets"); John Arquilla ("J. Arquilla"); Beth Armburst ("B. Armburst"); Artistic Land Designs; Charles Atkins ("C. Atkins"); Book Celler ("Book Celler"); Kathleen G. Bostwick ("K. Bostwick"); Brighter Day Painting ("Brighter Day Painting"); Colletti and Associates ("Colletti"); Commercial Concepts ("Commercial Concepts"); Complete Home Inspection ("Complete Home Inspection"); Debbie Courtney ("D. Courtney"); Sue Crawford ("S. Crawford"); Crespin's Cleaning, Inc. ("Crespin"); Don's Tractor Repair ("Don's"); Theresa Ebreo ("T. Ebreo"); M. Eng; eWareness, Inc. ("eWareness"); Evans Real Estate Investments, LLC ("Evans"); Fluharty Antiques ("Fluharty"); Flutterby; Fortuna Italian Restaurant & Pizza ("Fortuna Italian Restaurant"); Future Form Inc. ("Future Form Inc."); Glaspell Goals ("Glaspell"); Cheryl Gregory ("C. Gregory"); Healthcare Practice Management, Inc. (Healthcare Practice"); Brian Henderson ("B. Henderson"); Sheri Henning ("S. Henning"); Jaynee Herren ("J. Herren"); Ami Iriarte ("A. Iriarte"); Jeremy J. Jones ("J. Jones"); Juz Kidz Nursery and Preschool ("Juz Kidz"); Kernan Chiropractic Center ("Kernan"); LMS Wine Creators ("LMS Wine"); Tabitha Luna ("T. Luna"); Mansfield Children's Center, Inc. ("Mansfield Children's Center"); Denise McDonald ("D. McDonald"); Meister's Landscaping ("Meister"); Merchants Terminal Corporation ("Merchants Terminal"); Middendorf Bros. Auctioneers and Real Estate ("Middendorf"); Mingo Custom Woods ("Mingo"); Moore Brothers Auto Truck Repair ("Moore Brothers"); Mouton's Salon ("Mouton"); Doug Mozack ("D. Mozack"); Ms. Dee's Lil Darlins Daycare ("Ms. Dee"); Gavin Napolitano ("G. Napolitano"); NK Enterprises ("NK"); Hugh S. Olson ("H. Olson"); Parts and Equipment Supply Co. ("PESC"); Pioneer Heating & Air Conditioning ("Pioneer Heating & Air Conditioning"); RC Furniture Restoration ("RC"); RTW Enterprises Inc. ("RTW"); Debbie Sapp ("D. Sapp"); Southwest Business Brokers ("SBB"); Security Guard IT&T Alarms, Inc. ("SGIA"); Peggy Sicilia ("P. Sicilia"); Slycers Sandwich Shop ("Slycers"); Southern Services ("Southern Services"); Steele Group; Sylvron Travels ("Sylvron"); Theragenics; Erin White Tremaine ("E. Tremaine"); Wagner Health Center ("Wagner"); Wagner Industries ("Wagner Industries"); Wellness; West End Auto Paint & Body ("West End"); Y.M. Inc. ("Y.M."); J. Young.

potential disruption and cost to companies, we are convinced that adopting the proposed amendments to the proxy rules serves our purpose to regulate the proxy process in the public interest and on behalf of investors. We are not persuaded by the arguments of some commenters that the provisions of Rule 14a-11 are unnecessary.[37] Those commenters argued that changes in corporate governance over the past six years have obviated the need for a federal rule to allow shareholders to place their nominees in company proxy materials and that shareholders should be left to determine whether, on a company-by-company basis, such a rule is necessary at any particular company.

While we recognize that some states, such as Delaware,[38] have amended their state corporate law to enable companies to adopt procedures for the inclusion of shareholder director nominees in company proxy materials,[39] as was highlighted by a number of commenters, other

---

37 See, e.g., letters from 26 Corporate Secretaries; 3M; Advance Auto Parts; Allstate; Avis Budget; American Express; Anadarko; Association of Corporate Counsel; AT&T; L. Behr; Best Buy; Boeing; BRT; R. Burt; California Bar; S. Campbell; Carlson; Caterpillar; Chamber of Commerce/CMCC; Chevron; CIGNA; W. Cornwell; CSX; Cummins; Davis Polk; Dewey; DuPont; Eaton; M. Eng; FedEx; FMC Corp.; FPL Group; Frontier; GE; General Mills; Joseph A. Grundfest, Stanford Law School (July 24, 2009) ("Grundfest"); C. Holliday; Honeywell; C. Horner; IBM; Jones Day; Keating Muething; J. Kilts; R. Clark King; N. Lautenbach; MeadWestvaco; Metlife; Motorola; O'Melveny & Myers; Office Depot; Pfizer; Protective; S&C; Safeway; Sara Lee; Shearman & Sterling; Sherwin-Williams; Sidley Austin; Simpson Thacher; Tesoro; Textron; TI; G. Tooker; UnitedHealth; Unitrin; U.S. Bancorp; Wachtell; Wells Fargo; West Chicago Chamber; Weyerhaeuser; Xerox; Yahoo.

38 We refer to Delaware law frequently because of the large percentage of public companies incorporated under that law. The Delaware Division of Corporations reports that over 50% of U.S. public companies are incorporated in Delaware. See http://www.corp.delaware.gov.

39 Del. Code Ann. tit. 8, §112. In December 2009, the Committee on Corporate Laws of the American Bar Association Section of Business Law Committee adopted amendments to the Model Act that explicitly authorize bylaws that prescribe shareholder access to company proxy materials or reimbursement of proxy solicitation expenses. See ABA Press Release, "Corporate Laws Committee Adopts New Model Business Corporation Act Amendments to Provide For Proxy Access And Expense Reimbursement," December 17, 2009, available at http://www.abanet.org/abanet/media/release/news_release.cfm?releaseid=848.

In addition, in 2007, North Dakota amended its corporate code to permit 5% shareholders to provide a company notice of intent to nominate directors and require the company to include each such shareholder nominee in its proxy statement and form of proxy. N.D. Cent. Code § 10-35-08 (2009); see North Dakota Publicly Traded Corporations Act, N.D. Cent. Code §10-35 et al. (2007).

states have not.[40] These commenters noted that, as a result, companies not incorporated in Delaware could frustrate shareholder efforts to establish procedures for shareholders to place board nominees in the company's proxy materials by litigating the validity of a shareholder proposal establishing such procedures, or possibly repealing shareholder-adopted bylaws establishing such procedures. In addition, due to the difficulty that shareholders could have in establishing such procedures, we believe that it would be inappropriate to rely solely on an enabling approach to facilitate shareholders' ability to exercise their state law rights to nominate and elect directors. Even if bylaw amendments to permit shareholders to include nominees in company proxy materials were permissible in every state, shareholder proposals to so amend company bylaws could face significant obstacles.

We also considered whether the move by many companies away from plurality voting to a general policy of majority voting in uncontested director elections should lead to a conclusion that our actions are unnecessary or whether we should premise our actions on the failure of a company to adopt majority voting.[41] We agree with commenters[42] who argued that a majority voting standard in director elections does not address the need for a rule to facilitate the inclusion

40 See letters from American Federation of State, County and Municipal Employees ("AFSCME"); AllianceBernstein L.P. ("AllianceBernstein"); Amalgamated Bank LongView Funds ("Amalgamated Bank"); Association of British Insurers ("British Insurers"); CalPERS; CII; The Corporate Library ("Corporate Library"); L. Dallas; Florida State Board of Administration; ICGN; LIUNA; D. Nappier; Paul M. Neuhauser ("P. Neuhauser"); Comment Letter of Nine Securities and Governance Law Firms ("Nine Law Firms"); Pax World; Pershing Square; theRacetotheBottom.org ("RacetotheBottom"); RiskMetrics; Schulte Roth & Zabel LLP ("Schulte Roth & Zabel"); Sodali ("Sodali"); Teachers Insurance and Annuity Association of America and College Retirement Equities Fund ("TIAA-CREF"); United States Proxy Exchange ("USPE"); ValueAct Capital, LLC ("ValueAct Capital").

41 Despite the rate of adoption of a majority voting standard for director elections by companies in the S&P 500, only a small minority of firms in the Russell 3000 index have adopted them. See discussion in footnote 69 in the Proposing Release.

42 See letters from AFSCME; AllianceBernstein; CalPERS; CII; L. Dallas; D. Nappier; P. Neuhauser; RiskMetrics; TIAA-CREF. One commenter characterized a majority voting standard as a mechanism for "registering negative sentiment" about an incumbent board nominee, not a mechanism to ensure board accountability. See letter from AFSCME.

of shareholder nominees for director in company proxy materials. While majority voting impacts shareholders' ability to elect candidates put forth by management, it does not affect shareholders' ability to exercise their right to nominate candidates for director.

We also do not believe that the recent amendments to New York Stock Exchange (NYSE) Rule 452, which eliminated brokers' discretionary voting authority in director elections, negate the need for the rule. Certain commenters specifically noted their concurrence with us on this point.[43] The amendments to NYSE Rule 452 address who exercises the right to vote rather than shareholders' ability to have their nominees put forth for a vote. While these and other changes have been important events, they bolster shareholders' ability to elect directors who are already on the company's proxy card, not their ability to affect who appears on that card. We therefore are convinced that the federal proxy rules should be amended to better facilitate the exercise of shareholders' rights under state law to nominate directors.

We also considered whether we should amend Rule 14a-8 to narrow the "election exclusion," without also adopting Rule 14a-11. We note that a significant number of commenters supported the proposed amendments to Rule 14a-8(i)(8).[44] We concluded, however, as certain commenters pointed out, that adopting only the proposed amendments to Rule 14a-8(i)(8), without Rule 14a-11, would not achieve the Commission's stated objectives.[45] We believe that the amendments to Rule 14a-8(i)(8) will provide shareholders with an important mechanism for including in company proxy materials proposals that would address the inclusion of shareholder director nominees in the company's proxy materials in ways that supplement Rule

---

43 See letters from CII; Sodali; USPE.

44 For a list of these commenters, see footnotes 677, 678, and 679 below.

45 See letters from CII; USPE.

14a-11, such as with a lower ownership threshold, a shorter holding period, or to allow for a greater number of nominees if shareholders of a company support such standards.

We recognize that many commenters advocated that shareholders' ability to include nominees in company proxy materials should be determined exclusively by what individual companies or their shareholders affirmatively choose to provide, or that companies or their shareholders should be able to opt out of Rule 14a-11 or otherwise alter its terms for individual companies (the "private ordering" arguments).[46] After careful consideration of the numerous comments advocating this perspective,[47] we believe that the arguments in favor of this perspective are flawed for several reasons.

First, corporate governance is not merely a matter of private ordering. Rights, including shareholder rights, are artifacts of law, and in the realm of corporate governance some rights cannot be bargained away but rather are imposed by statute. There is nothing novel about mandated limitations on private ordering in corporate governance.[48]

---

46 See letters from 26 Corporate Secretaries; ABA; ACE; Advance Auto Parts; AGL; Aetna; Allstate; Alston & Bird; American Bankers Association; American Business Conference; American Electric Power; Anadarko; Applied Materials; Artistic Land Designs; Association of Corporate Counsel; Avis Budget; Atlantic Bingo; L. Behr; Best Buy; Biogen; J. Blanchard; Boeing; T. Bonkowski; BorgWarner; Boston Scientific; Brink's; BRT; Burlington Northern; R. Burt; California Bar; Callaway; S. Campbell; Carlson; Carolina Mills; Caterpillar; Chamber of Commerce/CMCC; Chevron; R. Chicko; CIGNA; Comcast; Competitive Enterprise Institute; W. Cornwell; CSX; E. Culwell; Cummins; Darden Restaurants; Daniels Manufacturing; Davis Polk; Delaware Bar; T. Dermody; Devon; DTE Energy; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; M. Eng; Erickson; ExxonMobil; FedEx; Financial Services Roundtable; Flutterby; FPL Group; Frontier; GE; A. Goolsby; Grundfest; C. Holliday; IBM; ICI; Intelect; JPMorgan Chase; Jones Day; R. Clark King; Leggett; T. Liddell; Little; McDonald's; MeadWestvaco; MedFaxx; Medical Insurance; Metlife; M. Metz; Microsoft; J. Miller; M. Moretti; Motorola; NACD; NAM; NIRI; O'Melveny & Myers; Office Depot; Omaha Door; P&G; PepsiCo; Pfizer; Realogy; J. Robert; M. Robert; RPM; Ryder; Safeway; R. Saul; Shearman & Sterling; Sherwin-Williams; R. Simoneau; Society of Corporate Secretaries; Southern Company; Southland; Steele Group; Style Crest; Tesoro; Textron; Theragenics; TI; R. Trummel; T. Trummel; V. Trummel; tw telecom; L. Tyson; United Brotherhood of Carpenters; UnitedHealth; U.S. Bancorp; VCG; Wachtell; Wellness; Wells Fargo; Whirlpool; Xerox; Yahoo; J. Young.

47 See id.

48 For example, quite a few aspects of Delaware corporation law are mandatory (i.e., not capable of modification by agreement or provision in the certificate of incorporation or bylaws), including: (i) the

Second, the argument that there is an inconsistency between mandating inclusion of shareholder nominees in company proxy materials and our concern for the rights of shareholders under the federal securities laws[49] mistakenly assumes that basic protections of, and rights of, particular shareholders provided under the federal proxy rules should be able to be abrogated by "the shareholders" of a particular corporation, acting in the aggregate. The rules we adopt today provide individual shareholders the ability to have director nominees included in the corporate proxy materials if state law[50] and governing corporate documents permit a shareholder to nominate directors at the shareholder meeting and the requirements of Rule 14a-11 are satisfied. Those rules similarly facilitate the right of individual shareholders to vote for those nominated, whether by management or another shareholder, if the shareholder has voting rights under state law and the company's governing documents. The rules we adopt today reflect our judgment that the proxy rules should better facilitate shareholders' effective exercise of their traditional state law rights to nominate directors and cast their votes for nominees. When the federal securities laws establish protections or create rights for security holders, they do so individually,

---

requirement to hold an annual election of directors (Del. Code Ann., tit. 8, §211(b); Jones Apparel Group v. Maxwell Shoe Co., 883 A.2d 837, 848-849 (Del. Ch. 2004) citing Rohe v. Reliance Training Network, Inc., 2000 Del. Ch. LEXIS 108 at *10-*11 (Del. Ch. July 21, 2000)); (ii) the limitation against dividing the board of directors into more than three classes (Del. Code Ann., tit. 8, §141(d); see also Jones Apparel); (iii) the entitlement of stockholders to inspect the list of stockholders and other corporate books and records (Del. Code Ann., tit. 8, §§219(a) and 220(b); Loew's Theatres, Inc. v. Commercial Credit Co., 243 A.2d 78, 81 (Del. Ch. 1968)); (iv) the right of stockholders to vote as a class on certain amendments to the certificate of incorporation (Del. Code Ann., tit. 8, §242(b)(2)); (v) appraisal rights (Del. Code Ann., tit. 8, §262(b)); and (vi) fiduciary duties of corporate directors (Siegman v. Tri-Star Pictures, Inc., C.A. No. 9477 (Del. Ch. May 5, 1989, revised May 30, 1989), reported at 15 Del. J. Corp. L. 218, 236 (1990); cf. Del. Code Ann., tit. 8, §102(b)(7), permitting elimination of director liability for monetary damages for breach of the duty of care). See also Edward P. Welch and Robert S. Saunders, What We Can Learn From Other Statutory Schemes: Freedom And Its Limits In The Delaware General Corporation Law, 33 Del. J. Corp. L. 845, 857-859 (2008); Jeffrey N. Gordon, Contractual Freedom In Corporate Law: Articles & Comments; The Mandatory Structure Of Corporate Law, 89 Colum. L. Rev. 1549, 1554 n.16 (1989) (identifying several of these and other mandatory aspects of Delaware corporation law).

49 See letters from Grundfest; Form Letter Type A. Cf. letter from Nine Law Firms.

50 In the case of a non-U.S. domiciled issuer that does not qualify as a foreign private issuer (as defined in Exchange Act Rule 3b-4), we will look to the underlying law of the jurisdiction of organization. See Rule 14a-11(a).

not in some aggregated capacity. No provision of the federal securities laws can be waived by referendum. A rule that would permit some shareholders (even a majority) to restrict the federal securities law rights of other shareholders would be without precedent and, we believe, a fundamental misreading of basic premises of the federal securities laws. In addition, allowing some shareholders to impair the ability of other shareholders to have their director nominees included in company proxy materials cannot be reconciled with the purpose of the rules we are adopting today. In our view, it would be no more appropriate to subject a federal proxy rule that provides the ability to include nominees in the company proxy statement to a shareholder vote than it would be to subject any other aspect of the proxy rules – including the other required disclosures – to abrogation by shareholder vote.

Third, the net effect of our rules will be to expand shareholder choice, not limit it. Our rules will result in a greater number of nominees appearing on a proxy card. Shareholders will continue to have the opportunity to vote solely for management candidates, but our rules will also give shareholders the opportunity to vote for director candidates who otherwise might not have been included in company proxy materials.

In addition to these basic conclusions, we note that there are other significant concerns raised by a private ordering approach. A company-by-company shareholder vote on the applicability of Rule 14a-11 would involve substantial direct and indirect, market-wide costs, and it is possible that boards of directors, or shareholders acting with their explicit or implicit encouragement, might seek such shareholder votes, perhaps repeatedly, at no financial cost to themselves but at considerable cost to the company and its shareholders. Another concern relates to the nature of the shareholder vote on whether to opt out of Rule 14a-11: specifically, in that context management can draw on the full resources of the corporation to promote the adoption of an opt-out, while disaggregated shareholders have no similarly effective platform from which to advocate against an opt-out.

In addition, the path to shareholder adoption of a procedure to include nominees in company proxy materials is by no means free of obstructions. While shareholders may ordinarily have the state law right to adopt bylaws providing for inclusion of shareholder nominees in company proxy materials even in the absence of an explicit authorizing statute like Delaware's, the existence of that right in the absence of such a statute may be challenged. Moreover, we understand that under Delaware law, the board of directors is ordinarily free, subject to its fiduciary duties, to amend or repeal any shareholder-adopted bylaw.[51] In addition, not all state statutes confer upon shareholders the power to adopt and amend bylaws, and even where shareholders have that power it is frequently limited by requirements in the company's governing documents that bylaw amendments be approved by a supermajority shareholder vote.[52]

After careful consideration of the options that commenters have suggested, we have determined that the most effective way to facilitate shareholders' exercise of their traditional state law rights to nominate and elect directors would be through Rule 14a-11 and the related amendments to the proxy rules that we proposed in June 2009. We have concluded that the ability to include shareholder nominees in company proxy materials pursuant to Rule 14a-11[53]

---

51 It has been argued to us, as a basis for excluding a shareholder proposal under Rule 14a-8, that Delaware law does not permit a bylaw to deprive the board of directors of the power to amend or repeal it, where the corporation's certificate of incorporation confers upon the board the power to adopt, amend and repeal bylaws. See, e.g., CVS Caremark Corp., No-Action Letter (March 9, 2010). See also Del. Code Ann., tit. 8, §109(b) and Centaur Partners, IV v. National Intergroup, Inc., 582 A.2d 923, 929 (Del. 1990).

52 See Beth Young, The Corporate Library, "The Limits of Private Ordering: Restrictions on Shareholders' Ability to Initiate Governance Change and Distortions of the Shareholder Voting Process" (November 2009), available at http://www.sec.gov/comments/s7-10-09/s71009-568.pdf. See, e.g., Ind. Code §23-1-39-1; Okla. Stat., tit. 18, §18-1013.

53 Throughout this release, when we refer to "a nomination pursuant to Rule 14a-11," a "Rule 14a-11 nomination," or other similar statement, we are referring to a nomination submitted for inclusion in a company's proxy materials pursuant to Rule 14a-11.

must be available to shareholders who are entitled under state law to nominate and elect directors, regardless of any provision of state law or a company's governing documents that purports to waive or prohibit the use of Rule 14a-11. In this regard, we note that although the rules we are adopting do not permit a company or its shareholders to opt out of or alter the application of Rule 14a-11, the amendments do contemplate that any additional ability to include shareholder nominees in the company's proxy materials that may be established in a company's governing documents will be permissible under our rules. Moreover, our amendments to Rule 14a-8 will facilitate the presentation of proposals by shareholders to adopt company-specific procedures for including shareholder nominees for director in company proxy materials, and our adoption of new Exchange Act Rule 14a-18 (which requires disclosure concerning the nominating shareholder or group and the nominee or nominees that generally is consistent with that currently required in an election contest) will help assure that investors are adequately informed about shareholder nominations made through such procedures.

In contrast, if state law[54] or a provision of the company's governing documents were ever to prohibit a shareholder from making a nomination (as opposed to including a validly nominated individual in the company's proxy materials), Rule 14a-11 would not require the company to include in its proxy materials information about, and the ability to vote for, any such nominee. The rule defers entirely to state law as to whether shareholders have the right to nominate directors and what voting rights shareholders have in the election of directors.

While we have concluded that we should provide shareholders the means to have nominees included in proxy materials in certain circumstances, we also are mindful that to accomplish this goal the regulatory structure must arrive at a solution that ultimately is workable.

[54] In the case of a non-U.S. domiciled issuer that does not qualify as a foreign private issuer, we will look to the underlying law of the jurisdiction of organization. See footnote 50 above.

Accordingly, we are adopting a number of significant changes to the rules we proposed in order to address the many thoughtful and constructive comments we received on the specifics of our proposed amendments. The changes that we are making to the amendments are described in detail throughout this release. There also were a number of suggested changes that we considered and decided not to adopt, as detailed below.

B. Our Role in the Proxy Process

Several commenters challenged our authority to adopt Rule 14a-11.[55] We considered those comments carefully but continue to believe that we have the authority to adopt Rule 14a-11 under Section 14(a) as originally enacted.[56] In any event, Congress confirmed our authority in this area and removed any doubt that we have authority to adopt a rule such as Rule 14a-11.[57] As described more fully below, Rule 14a-11 is necessary and appropriate in the public interest and for the protection of investors.[58] Additionally, as explained below, the terms and conditions of Rule 14a-11 are also in the interests of shareholders and for the protection of investors.[59] Therefore, this challenge is now moot.

---

55 See letters from Ameriprise; AT&T; L. Behr; BRT; Burlington Northern; CMCC; Dewey; M. Eng; FedEx; Grundfest; Keating Muething; OPLP; Sidley Austin.

56 When it adopted Section 14(a) of the Exchange Act, Congress determined that the exercise of shareholder voting rights via the corporate proxy is a matter of federal concern, and the statute's grant of authority is not limited to regulating disclosure. Roosevelt v. E.I. DuPont de Nemours & Co., 958 F.2d 416, 421-422 (D.C. Cir. 1992) (Congress "did not narrowly train [S]ection 14(a) on the interest of stockholders in receiving information necessary to the intelligent exercise of their" state law rights; Section 14(a) also "shelters use of the proxy solicitation process as a means by which stockholders ... may communicate with each other."); see also, e.g., TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 n.10 (1976) (Section 14(a) is a grant of "broad statutory authority"). The adoption of Rule 14a-11 reflects our continuing purpose to ensure that proxies are used as a means to enhance the ability of shareholders to make informed choices, especially on the critical subject of who sits on the board of directors.

57 Dodd-Frank Act § 971(a) and (b). These provisions expressly provide that the Commission may issue rules permitting shareholders to use an issuer's proxy solicitation materials for the purpose of nominating individuals to membership on the board of directors of the issuer.

58 Exchange Act § 14(a) and Investment Company Act § 20(a).

59 Dodd- Frank Act § 971(b).

Although our statutory authority to adopt Rule 14a-11 is no longer at issue, the constitutionality of Rule 14a-11 also has been challenged by commenters. We disagree with their arguments.[60] Proxy regulations do not infringe on corporate First Amendment rights both because "management has no interest in corporate property except such interest as derives from the shareholders," and because such regulations "govern speech by a corporation to itself" and therefore "do not limit the range of information that the corporation may contribute to the public debate."[61] Even if statements in proxy materials are viewed as more than merely internal communications, this communication is of a commercial – not political – nature, and regulation of such statements through Rule 14a-11 is consistent with applicable First Amendment standards.[62]

C. Summary of the Final Rules

As noted above, we carefully considered the comments and have decided to adopt new Exchange Act Rule 14a-11 with significant modifications in response to the comments. We believe that the new rule will benefit shareholders and protects investors by improving corporate suffrage, the disclosure provided in connection with corporate proxy solicitations, and communication between shareholders in the proxy process. Consistent with the Proposal, Rule 14a-11 will apply only when applicable state law or a company's governing documents do not prohibit shareholders from nominating a candidate for election as a director. In addition, as adopted, the rule will apply to a foreign issuer that is otherwise subject to our proxy rules only

---

60 See letter from BRT.

61 Pacific Gas and Electric Company v. Public Utilities Comm'n of California, 475 U.S. 1, 14 n.10 (1986) (emphasis in original).

62 Nor does Rule 14a-11 violate the Fifth Amendment, as it does not constitute a regulatory taking. See, e.g., Lingle v. Chevron U.S.A., 544 U.S. 528, 546-47 (2005); Penn Central Transp. Co. v. City of New York, 438 U.S. 104 (1978).

when applicable foreign law does not prohibit shareholders from making such nominations. Also consistent with the Proposal, companies may not "opt out" of the rule – either in favor of a different framework for inclusion of shareholder director nominees in company proxy materials or no framework. In addition, as was proposed, the rule will apply regardless of whether any specified event has occurred to trigger the rule and will apply regardless of whether the company is subject to a concurrent proxy contest.[63] Also as proposed, the final rule will apply to companies that are subject to the Exchange Act proxy rules, including investment companies and controlled companies, but will not apply to "debt-only" companies. The rule will apply to smaller reporting companies, but we have decided to delay the rule's application to these companies for three years. We believe that a delayed effective date for smaller reporting companies should allow those companies to observe how the rule operates for other companies and should allow them to better prepare for implementation of the rules. Delayed implementation for these companies also will allow us to evaluate the implementation of Rule 14a-11 by larger companies and provide us with the additional opportunity to consider whether adjustments to the rule would be appropriate for smaller reporting companies before the rule becomes applicable to them. To use Rule 14a-11, a nominating shareholder or group will be required to satisfy an ownership threshold of at least 3% of the voting power of the company's securities entitled to be voted at the meeting. Shareholders will be able to aggregate their shares to meet the threshold. The required ownership threshold has been modified from the Proposal, which would have required that a nominating shareholder or group hold 1%, 3%, or 5% of the company's securities entitled to be voted on the election of directors, depending on accelerated

63 Throughout this release, the terms "proxy contest," "election contest," and "contested election" refer to any election of directors in which another party commences a solicitation in opposition subject to Exchange Act Rule 14a-12(c).

filer status or, in the case of registered investment companies, depending on the net assets of the company. The final rule requires that a nominating shareholder or group must hold both investment and voting power, either directly or through any person acting on their behalf, of the securities. In calculating the ownership percentage held, under certain conditions, a nominating shareholder or member of the nominating shareholder group would be able to include securities loaned to a third party in the calculation of ownership. In determining the total voting power held by the nominating shareholder or any member of the nominating shareholder group, securities sold short (as well as securities borrowed that are not otherwise excludable) must be deducted from the amount of securities that may be counted towards the required ownership threshold. In addition, a nominating shareholder (or in the case of a group, each member of the group) will be required to have held the qualifying amount of securities continuously for at least three years as of the date the nominating shareholder or group submits notice of its intent to use Rule 14a-11 (on a filed Schedule 14N), rather than for one year, as was proposed. Consistent with the proposed amendments, we are adopting a requirement that the nominating shareholder or members of the group must continue to own the qualifying amount of securities through the date of the meeting at which directors are elected and provide disclosure concerning their intent with regard to continued ownership of the securities after the election of directors. In addition, the nominating shareholder (or where there is a nominating shareholder group, any member of the nominating shareholder group) may not be holding the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11, and may not have a direct or indirect agreement with the company regarding the nomination of the nominee or nominees prior to filing the Schedule 14N.

The nominating shareholder or group must provide notice to the company of its intent to use Rule 14a-11 no earlier than 150 days prior to the anniversary of the mailing of the prior year's proxy statement and no later than 120 days prior to this date. The final rule differs from the Proposal, which would have required the nominating shareholder or group to provide notice to the company no later than 120 days prior to the anniversary of the mailing of the prior year's proxy statement or in accordance with the company's advance notice provision, if applicable. As was proposed, under the final rule the nominating shareholder or group will be required to file on EDGAR and transmit to the company its notice on Schedule 14N on the same date.

The rule also includes certain requirements applicable to the shareholder nominee. Consistent with the Proposal, the final rule provides that the company will not be required to include any nominee whose candidacy or, if elected, board membership would violate controlling state or federal law, or the applicable standards of a national securities exchange or national securities association, except with regard to director independence requirements that rely on a subjective determination by the board, and such violation could not be cured during the provided time period.[64] In addition, the rule we are adopting provides that a company will not be required to include any nominee whose candidacy or, if elected, board membership would violate controlling foreign law. As we proposed, the rule does not include any restrictions on the relationships between the nominee and the nominating shareholder or group.

As was proposed, under Rule 14a-11, a company will not be required to include more than one shareholder nominee, or a number of nominees that represents up to 25% of the company's board of directors, whichever is greater. Where there are multiple eligible

---

64 In the case of an investment company, the nominee may not be an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(19)). See Section II.B.3.b. for a more detailed discussion of the applicability of Rule 14a-11 to registered investment companies.

nominating shareholders, the nominating shareholder or group with the highest percentage of the company's voting power would have its nominees included in the company's proxy materials, rather than the nominating shareholder or group that is first to submit a notice on Schedule 14N, as we had proposed. We also have clarified in the final rule that when a company has a classified (staggered) board, the 25% calculation would still be based on the total number of board seats. In addition, in response to public comment, we have added a provision to the rule designed to prevent the potential unintended consequences of discouraging dialogue and negotiation between company management and nominating shareholders. Under this provision, shareholder nominees of an eligible nominating shareholder or group with the highest qualifying voting power percentage that a company agrees to include as company nominees after the filing of the Schedule 14N would count toward the 25%.

The notice on Schedule 14N will be required to include:

- Disclosure concerning:
  - The amount and percentage of voting power of the company's securities entitled to be voted by the nominating shareholder or group and the length of ownership of those securities;
  - Biographical and other information about the nominating shareholder or group and the shareholder nominee or nominees, similar to the disclosure currently required in a contested election;
  - Whether or not the nominee or nominees satisfy the company's director qualifications, if any (as provided in the company's governing documents);
- Certifications that, after reasonable inquiry and based on the nominating shareholder's or group's knowledge, the:

- Nominating shareholder (or where there is a nominating shareholder group, each member of the nominating shareholder group) is not holding any of the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11;

- Nominating shareholder or group otherwise satisfies the requirements of Rule 14a-11, as applicable; and
- Nominee or nominees satisfy the requirements of Rule 14a-11, as applicable;

- A statement that the nominating shareholder or group members will continue to hold the qualifying amount of securities through the date of the meeting and a statement with regard to the nominating shareholder's or group member's intended ownership of the securities following the election of directors (which may be contingent on the results of the election of directors); and
- A statement in support of each shareholder nominee, not to exceed 500 words per nominee (the statement would be at the option of the nominating shareholder or group).

These requirements for Schedule 14N are largely consistent with the Proposal, with some modifications made in response to comments. Among the modifications is the new disclosure requirement concerning whether, to the best of the nominating shareholder's or group's knowledge, the nominee or nominees satisfy the company's director qualifications, if any (as provided in the company's governing documents). We also have revised the certifications to require certification not only with regard to control intent, but also with regard to the other nominating shareholder and nominee eligibility requirements.

A company that receives a notice on Schedule 14N from an eligible nominating shareholder or group will be required to include in its proxy statement disclosure concerning the nominating shareholder or group and the shareholder nominee or nominees, and include on its proxy card the names of the shareholder nominees. The nominating shareholder or group will be liable for any statement in the notice on Schedule 14N which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact or that omits to state any material fact necessary to make the statements therein not false or misleading, including when that information is subsequently included in the company's proxy statement. The company will not be responsible for this information. These liability provisions are included in the final rules largely as proposed, but with two changes in response to comments. Final Rule 14a-9(c) makes clear that the nominating shareholder or group will be liable for any statement in the Schedule 14N or any other related communication that is false or misleading with respect to any material fact, or that omits to state any material fact necessary to make the statements therein not false or misleading, regardless of whether that information is ultimately included in the company's proxy statement. In addition, consistent with the existing approach in Rule 14a-8, under Rule 14a-11 as adopted, a company will not be responsible for any information provided by the nominating shareholder or group and included in the company's proxy statement. Under the Proposal, a company would not have been responsible for any information provided by the nominating shareholder or group except where the company knows or has reason to know that the information is false or misleading.

A company will not be required to include a nominee or nominees if the nominating shareholder or group or the nominee fails to satisfy the eligibility requirements of Rule 14a-11. A company that determines it may exclude a nominee or nominees must provide a notice to the Commission regarding its intent to exclude the nominee or nominees. The company also may submit a request for the staff's informal view with respect to the company's determination that it may exclude the nominee or nominees (commonly referred to as "no-action" requests). In addition, a company could exclude a nominating shareholder's or group's statement of support if the statement exceeds 500 words per nominee and could seek a no-action letter from the staff with regard to this determination if it so desired. In the event that a nominating shareholder or group or nominee withdraws or is disqualified prior to the time the company commences printing the proxy materials, under certain circumstances companies will be required to include a substitute nominee if there are other eligible nominees. Therefore, companies seeking a no-action letter from the staff with respect to their decision to exclude any Rule 14a-11 nominee or nominees would need to seek a no-action letter on all nominees that they believe they can exclude at the outset.

We also have adopted two new exemptions, slightly modified from the Proposal, to the proxy rules for solicitations in connection with a Rule 14a-11 nomination. The first exemption applies to written and oral solicitations by shareholders who are seeking to form a nominating shareholder group. Reliance on this new exemption will require:

- that the shareholder not be holding the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11;
- limiting the content of written communications to certain information specified in the rule;
- filing all written soliciting materials sent to shareholders in reliance on the exemption with the Commission or, in the case of oral communications, a filing under cover of Schedule 14N with the appropriate box checked before or at the same time as the first solicitation in reliance on the new exemption; and
- no solicitations in connection with the subject election of directors other than pursuant to the provisions of Rule 14a-11 and the new exemption described below.

Shareholders that do not want to rely on this new exemption could opt to rely on other exemptions from the proxy rules (e.g., Rule 14a-2(b)(2), which is limited to solicitations of not more than 10 persons).

The second new exemption applies to written and oral solicitations by or on behalf of a nominating shareholder or group whose nominee or nominees are or will be included in the company's proxy materials pursuant to Rule 14a-11 in favor of shareholder nominees or for or against company nominees. Reliance on this new exemption will require:

- that the nominating shareholder or group does not seek the power to act as a proxy for another shareholder;
- disclosing certain information (including the identity of the nominating shareholder or group, and a prominent legend about availability of the proxy materials) in all written communications;
- filing all written soliciting materials sent to shareholders in reliance on the exemption with the Commission under cover of Schedule 14N with the appropriate box checked; and
- no solicitations in connection with the subject election of directors other than pursuant to the provisions of Rule 14a-11 and this new exemption.

Consistent with the Proposal, we also are amending our beneficial ownership reporting rules so that shareholders relying on Rule 14a-11 would not become ineligible to file a Schedule 13G, in lieu of filing a Schedule 13D, solely as a result of activities in connection with inclusion of a nominee under Rule 14a-11. Also consistent with the proposed amendments, we are not adopting an exclusion from Exchange Act Section 16 for activities in connection with a nomination under Rule 14a-11 that may trigger a filing requirement by nominating shareholders.

In addition, after considering the comments, we are not adopting a specific exclusion from the definition of affiliate for nominating shareholders.

Finally, consistent with the Proposal, we are narrowing the scope of the exclusion in Rule 14a-8(i)(8) relating to the election of directors. The revised rule will provide that companies must include in their proxy materials, under certain circumstances, shareholder proposals that seek to establish a procedure in the company's governing documents for the inclusion of one or more shareholder director nominees in a company's proxy materials.

As we proposed, the final rules provide that a nominating shareholder that is relying on a procedure under state law or a company's governing documents to include a nominee in a company's proxy materials would be required to provide disclosure concerning the nominating shareholder and nominee or nominees to the company on Schedule 14N and file the Schedule 14N on EDGAR. In response to comment, we have clarified that the disclosure also would be required for nominations made pursuant to foreign law.[65] The disclosure requirements on Schedule 14N for nominations made pursuant to a procedure under state or foreign law, or a company's governing documents largely mirror those for a Rule 14a-11 nomination. As with Rule 14a-11 nominees, a company would include in its proxy materials disclosure concerning the nominating shareholder or group and shareholder nominee similar to the disclosure currently required in a contested election. The nominating shareholder or group would have liability for any statement in the notice on Schedule 14N or in information otherwise provided to the company and included in the company's proxy materials which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact or that omits to state any material fact necessary to make the statements therein not false or

65 See Section II.C.5. below.

misleading. The company would not be responsible for the information provided to the company and required to be included in the company proxy statement.

II. CHANGES TO THE PROXY RULES

A. Introduction

After careful consideration of the comments received on the Proposal, we are adopting amendments to the proxy rules to facilitate the effective exercise of shareholders' traditional state law rights to nominate and elect directors to company boards of directors. Under the new rules, shareholders meeting certain requirements will have two ways to more fully exercise their right to nominate directors. First, we are adopting a new proxy rule, Rule 14a-11, which will, under certain circumstances, require companies to provide shareholders with information about, and the ability to vote for, a shareholder's, or group of shareholders', nominees for director in the companies' proxy materials. This requirement will apply unless state law, foreign law,[66] or a company's governing documents[67] prohibits shareholders from nominating directors.[68] In addition to the standards provided in new Rule 14a-11, provisions under state law, foreign law, or a company's governing documents[69] could provide an additional avenue for shareholders to submit nominees for inclusion in company proxy materials, but would not act as a substitute for Rule 14a-11. Thus, Rule 14a-11 will continue to be available to shareholders regardless of whether they also can avail themselves of a provision under state law, foreign law, or a

66 See discussion in footnote 50 above.

67 Under state law, a company's governing documents may have various names. When we refer to governing documents throughout the release and rule text, we generally are referring to a company's charter, articles of incorporation, certificate of incorporation, declaration of trust, and/or bylaws, as applicable.

68 We are not aware of any law in any state or in the District of Columbia or in any country that currently prohibits shareholders from nominating directors. Nonetheless, should any such law be enacted in the future, Rule 14a-11 will not apply.

69 See discussion in Section II.C.5. below.

company's governing documents.

Second, we are amending Rule 14a-8(i)(8) to preclude companies from relying on Rule 14a-8(i)(8) to exclude from their proxy materials shareholder proposals by qualifying shareholders that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. A company must include such a shareholder proposal under the final rules as long as the procedural requirements of Rule 14a-8 are met and the proposal is not subject to exclusion under one of the other substantive bases. In this regard, a shareholder proposal seeking to limit or remove the availability of Rule 14a-11 would be subject to exclusion under Rule 14a-8.[70]

As described throughout this release, we have made many changes to the final rules in response to comments received. We believe the final rules reflect a careful balancing of the policy, workability, and other comments we received on the Proposal.

B. Exchange Act Rule 14a-11

1. Overview

Based on the comments received in response to our solicitation of public input on the Proposal and on prior releases and in roundtables,[71] we understand that shareholders face significant obstacles to effectively exercising their rights to nominate and elect directors to corporate boards. We have received significant public comment supporting the view that including shareholder nominees for director in company proxy materials would be the most

---

70 As would currently be the case if a state law permitted a company to prohibit shareholders from nominating candidates for director, a shareholder proposal seeking to prohibit shareholder nominations for director generally or, conversely, to allow shareholder nominations for director, would not be excludable pursuant to Rule 14a-8(i)(8).

71 See the Proposing Release; the 2003 Proposal; the Election of Directors Proposing Release; and the Shareholder Proposals Proposing Release. See also the Roundtable on the Federal Proxy Rules and State Corporation Law and the Roundtable on Proposals of Shareholders available at http://www.sec.gov/spotlight/proxyprocess.htm.

direct and effective method of facilitating shareholders' rights in connection with the nomination and election of directors.[72]

On the other hand, many commenters have expressed concern that mandating shareholder access to company proxy materials would lead to more proxy contests or "politicized elections,"[73] which would be distracting, expensive, time-consuming, and inefficient for companies, boards, and management.[74] Commenters also opined that the increased likelihood of a contested election could discourage experienced and capable individuals from serving on boards, making it more difficult for companies to recruit qualified directors or create boards with the proper mix of experience, skills, and characteristics.[75] The current filing and other

---

72 See letters from CII; COPERA; CtW Investment Group; L. Dallas; T. DiNapoli; Florida State Board of Administration; ICGN; D. Nappier; OPERS; Pax World; Teamsters.

73 See letters from ABA; Advance Auto Parts; Atlas Industries, Inc. ("Atlas"); J. Blanchard; Samuel W. Bodman ("S. Bodman"); Boeing; Brink's; BRT; Burlington Northern; Callaway; Cargill ("Cargill"); Carlson; Carolina Mills; Chamber of Commerce/CMCC; Jaime Chico ("J. Chico"); Consolidated Edison, Inc. ("Con Edison"); Anthony Conte ("A. Conte"); W. Cornwell; Crown Battery Manufacturing Co. ("Crown Battery"); CSX; Darden Restaurants; Eaton; FedEx; FPL Group; Frontier; Hickory Furniture Mart ("Hickory Furniture"); IBM; Keating Muething; Little; Louisiana Agencies LLC ("Louisiana Agencies"); Massey Services, Inc. ("Massey Services"); John B. McCoy ("J. McCoy"); D. McDonald; MedFaxx; Metlife; M. Metz; Norfolk Southern Corporation ("Norfolk Southern"); O3 Strategies, Inc. ("O3 Strategies"); Office Depot; Victor Pelson ("V. Pelson"); PepsiCo; Pfizer; Ryder; Sidley Austin; Southland; Style Crest; Tenet Healthcare Corporation ("Tenet"); TI; tw telecom; L. Tyson; United Brotherhood of Carpenters; T. White.

74 See letters from ABA; Anonymous letter dated June 26, 2009 ("Anonymous #2"); Atlas; AT&T; Book Celler; Carlson; Carolina Mills; Chamber of Commerce/CMCC; Chevron; Crespin; M. Eng; Erickson; ExxonMobil; Fenwick & West LLP ("Fenwick"); GE; General Mills; Glass, Lewis & Co., LLC ("Glass Lewis"); Glaspell Goals ("Glaspell"); Intelect; R. Clark King; Koppers Inc. ("Koppers"); MCO Transport, Inc. ("MCO"); MeadWestvaco; MedFaxx; Medical Insurance; Merchants Terminal; Dana Merilatt ("D. Merilatt"); NAM; NIRI; NK; O3 Strategies; Roppe Holding Company ("Roppe"); Rosen Hotels and Resorts ("Rosen"); Safeway; Sara Lee; Schneider National, Inc. ("Schneider"); Southland; Style Crest; Tenet; TI; tw telecom; Rick VanEngelenhoven ("R. VanEngelenhoven"); Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

75 See letters from 3M; ABA; American Electric Power; Atlantic Bingo; AT&T; Avis Budget; Biogen; Boeing; BRT; Burlington Northern; Callaway; Carlson; Chamber of Commerce/CMCC; CIGNA; Columbine Health Plan ("Columbine"); Cummins; CSX; John T. Dillon ("J. Dillon"); Emerson Electric; Erickson; ExxonMobil; FedEx; Headwaters Incorporated ("Headwaters"); C. Holliday; IBM; Intelect; R. Clark King; Lange Transport ("Lange"); Louisiana Agencies; MetLife; NIRI; O3 Strategies; V. Pelson; PepsiCo; Pfizer; Roppe; Rosen; Ryder; Sara Lee; Sidley Austin; tw telecom; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

requirements applicable to shareholders who wish to propose an alternate slate are, in the view of these commenters, more appropriate than including shareholder nominees for director in company proxy materials.[76]

As we also noted in the Proposing Release, we recognize that there are long-held and deeply felt views on every side of these issues. To the extent shareholders have the right to nominate directors at meetings of shareholders, the federal proxy rules should facilitate the exercise of this right. We believe the rules we are adopting today will better accomplish this goal and will further our mission of investor protection.

New Rule 14a-11 will require companies to include information about shareholder nominees for director in company proxy statements, and the names of the nominee or nominees as choices on company proxy cards, under specified conditions.[77] The rule will permit companies to exclude a nominee or nominees from the company's proxy materials under certain circumstances, such as when a nominating shareholder or group fails to satisfy the eligibility requirements of the rule. In the following sections we describe, in detail, the final rules, comments received on the Proposal, and changes made in response to the comments.

2. When Rule 14a-11 Will Apply

In this section, we address the rule's application, including when there are conflicting or overlapping provisions under state or foreign law or a company's governing documents, during concurrent proxy contests, and in the absence of any specific triggering events. We also address the reasons why neither an opt-in nor opt-out provision is necessary or appropriate.

---

76 See letters from Ameriprise; Anonymous #2; Artistic Land Designs; Chamber of Commerce/CMCC; Crown Battery; Evelyn Y. Davis ("E. Davis"); Kernan; Medical Insurance; Mouton; Unitrin; R. VanEngelenhoven; Wells Fargo.

77 See new Exchange Act Rule 14a-11.

a. Interaction with state or foreign law

While we are not aware of any law in any state or in the District of Columbia that prohibits shareholders from nominating directors, consistent with the Proposal, a company to which the rule would otherwise apply will not be subject to Rule 14a-11 if applicable state law or the company's governing documents prohibit shareholders from nominating candidates for the board of directors. The final rule also clarifies that, in the case of a non-U.S. domiciled issuer that does not meet the definition of foreign private issuer under the federal securities laws, the rule will not apply if applicable foreign law prohibits shareholders from nominating a candidate for election as a director.[78] If a company's governing documents prohibit shareholder nominations, shareholders could seek to amend the provision by submitting a shareholder proposal under Rule 14a-8.[79]

Consistent with the Proposal, Rule 14a-11 will apply regardless of whether state or foreign law or a company's governing documents prohibit inclusion of shareholder director nominees in company proxy materials or set share ownership or other terms that are more restrictive than Rule 14a-11 under which shareholder director nominees will be included in company proxy materials. For example, if applicable state or foreign law or a company's governing documents were to require that shareholder nominees be included in company proxy materials only if submitted by a 10% shareholder of the company, a shareholder who does not meet the 10% threshold but does meet the requirements of Rule 14a-11, including the 3% ownership threshold described below, would be able to submit their nominee or nominees for inclusion in the company's proxy materials pursuant to Rule 14a-11. If, on the other hand,

---

[78] See letters from S&C; Curtis, Mallet-Prevost, Colt & Mosle LLP ("Curtis").

[79] See footnote 70 above.

applicable state or foreign law or a company's governing documents sets the ownership threshold lower than the 3% ownership threshold required under Rule 14a-11, then Rule 14a-11 would not be available to holders with ownership below the Rule 14a-11 threshold. Those shareholders meeting the lower ownership threshold would have the ability to have their nominees included in the company's proxy materials to whatever extent is provided under applicable state or foreign law or the company's governing documents. In this instance, new Exchange Act Rule 14a-18, discussed in Section II.C.5. below, would require specified disclosures concerning the nominating shareholder or group and the shareholder nominee or nominees.

There also may be situations where applicable state or foreign law or a company's governing documents are more permissive in certain respects, and more restrictive in other respects, than Rule 14a-11. For example, applicable state or foreign law or a company's governing documents could require 10% ownership to have a nominee or nominees included in a company's proxy materials, but allow a shareholder that owns 10% to have nominees up to the full number of board seats included in a company's proxy materials or to otherwise have a change in control intent. While Rule 14a-11 would continue to be available in that case for a shareholder that is eligible to use it, a shareholder could choose to proceed under the alternate procedure and standards. In this instance, a shareholder would be required to clearly evidence its intent to rely either on Rule 14a-11 or on the applicable state or foreign law or company's governing documents, and then meet all of the requirements of whichever procedure it selects.[80] A shareholder could not "pick and choose" different aspects of different procedures. If a

80 New Schedule 14N, which is described further in Section II.B.8. below, includes check boxes where a nominating shareholder or group must specify whether it is seeking to include the nominee or nominees in the company's proxy materials under Rule 14a-11 or pursuant to a provision in state law, foreign law, or a company's governing documents.

shareholder chooses to rely on a provision under applicable state or foreign law or a company's governing documents to include a nominee in a company's proxy materials, it would be required to satisfy the disclosure requirements of new Rule 14a-18.

b. Opt-in not required

In the Proposing Release, we requested comment on whether Rule 14a-11 should apply only if shareholders of a company elect to have it apply at their company. While commenters did not specifically address the possibility of shareholders opting into Rule 14a-11, many commenters opposed the Commission's Proposal on the basis that it would create a "one size fits all" federal rule that intrudes into matters that traditionally have been the province of state or local law.[81] Those commenters asked the Commission to permit private ordering so that companies and shareholders could devise, if they chose to, a process for the inclusion of shareholder director nominees in company proxy materials that best suits their particular circumstances. Commenters also expressed fears that the Commission's Proposal, if adopted, would stifle future innovations relating to inclusion of shareholder director nominees in company

---

81 See letters from 26 Corporate Secretaries; ABA; ACE; Advance Auto Parts; AGL; Aetna; Allstate; Alston & Bird; American Bankers Association; American Business Conference; American Electric Power; Anadarko; Applied Materials; Artistic Land Designs; Association of Corporate Counsel; Avis Budget; Atlantic Bingo; L. Behr; Best Buy; Biogen; J. Blanchard; Boeing; T. Bonkowski; BorgWarner; Boston Scientific; Brink's; BRT; Burlington Northern; R. Burt; California Bar; Callaway; S. Campbell; Carlson; Carolina Mills; Caterpillar; Chamber of Commerce/CMCC; Chevron; R. Chicko; CIGNA; Comcast; Competitive Enterprise Institute; W. Cornwell; CSX; E. Culwell; Cummins; Darden Restaurants; Daniels Manufacturing; Davis Polk; Delaware Bar; T. Dermody; Devon; DTE Energy; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; M. Eng; Erickson; ExxonMobil; FedEx; Financial Services Roundtable; Flutterby; FPL Group; Frontier; GE; A. Goolsby; Grundfest; C. Holliday; IBM; ICI; Intelect; JPMorgan Chase; Jones Day; R. Clark King; Leggett; T. Liddell; Little; McDonald's; MeadWestvaco; MedFaxx; Medical Insurance; MetLife; M. Metz; Microsoft; J. Miller; M. Moretti; Motorola; NACD; NAM; NIRI; O'Melveny & Myers; Office Depot; Omaha Door; P&G; PepsiCo; Pfizer; Realogy; J. Robert; M. Robert; RPM; Ryder; Safeway; R. Saul; Shearman & Sterling; Sherwin-Williams; R. Simoneau; Society of Corporate Secretaries; Southern Company; Southland; Steele Group; Style Crest; Tesoro; Textron; Theragenics; TI;. R. Trummel; T. Trummel; V. Trummel; tw telecom; L. Tyson; United Brotherhood of Carpenters; UnitedHealth; U.S. Bancorp; VCG; Wachtell; Wellness; Wells Fargo; Whirlpool; Xerox; Yahoo; J. Young.

proxy materials and corporate governance in general.[82] On the other hand, some commenters expressed general support for uniform applicability of proposed Rule 14a-11, unless state law or the company's governing documents prohibit shareholders from nominating candidates to the board.[83]

Though we considered commenters' views concerning a private ordering approach, as discussed in Section I.A. above, we have concluded that our rules should provide shareholders the ability to include director nominees in company proxy materials without the need for shareholders to bear the burdens of overcoming the substantial obstacles to creating that ability on a company-by-company basis. Rule 14a-11 is designed to facilitate the effective exercise of shareholder director nomination and election rights. Requiring shareholders to persuade other shareholders to opt into a system that better facilitates such state law rights would frustrate the benefits that our new rule seeks to promote.

c. No opt-out

In the Proposing Release, we sought comment on whether Rule 14a-11 should be inapplicable where a company has or adopts a provision in its governing documents that provides for, or prohibits, the inclusion of shareholder director nominees in the company's proxy materials. We also sought comment on whether Rule 14a-11 should apply in various circumstances, such as where shareholders approve provisions in the governing documents that are more or less restrictive than Rule 14a-11.

Commenters were divided on whether companies and shareholders should be permitted to adopt alternative requirements for shareholder director nominations, or to completely opt out

---

82 See letters from ABA; BRT; Davis Polk; Delaware Bar; Frontier; IBM; Protective.

83 See letters from 13D Monitor ("13D Monitor"); AFL-CIO; CalPERS; CFA Institute Centre for Market Integrity ("CFA Institute"); CII; Florida State Board of Administration; ICGN; LIUNA; D. Nappier; P. Neuhauser; OPERS; Pax World; RiskMetrics; SWIB; Teamsters; USPE.

of Rule 14a-11. Many commenters generally supported a provision that would permit companies and shareholders to adopt alternative requirements for shareholder director nominations that could be either more restrictive or less restrictive than those of Rule 14a-11.[84] Among these commenters, some argued that creating a "one-size-fits-all" rule that cannot be altered by companies and shareholders conflicts with the traditional enabling approach of state corporation laws and denies shareholder choice.[85] Some commenters advocated allowing companies to opt out of Rule 14a-11 through a shareholder-approved bylaw (including through a Rule 14a-8 shareholder proposal), with some suggesting that Rule 14a-11 apply initially only to companies that have not opted out through a shareholder-approved process by the time of the first annual meeting held after the adoption of the proposed rules.[86]

On the other hand, several commenters expressed support for the uniform applicability of Rule 14a-11.[87] These commenters expressed general support for the Commission's Proposal that Rule 14a-11 apply to all companies subject to the federal proxy rules unless state law or the company's governing documents prohibit shareholders from nominating candidates to the

---

84 See letters from ABA; Advance Auto Parts; Aetna; American Bankers Association; American Electric Power; American Express; Applied Materials; Association of Corporate Counsel; Best Buy; BRT; California Bar; Carlson; J. Chico; Cleary Gottlieb Steen & Hamilton LLP ("Cleary"); Comcast; Con Edison; CSX; Cummins; L. Dallas; Davis Polk; Devon; Dupont; ExxonMobil; Financial Services Roundtable; FPL Group; IBM; JPMorgan Chase; Keating Muething; Koppers; Alexander Krakovsky ("A. Krakovsky"); Group of 10 Harvard Business School and Harvard Law School Professors ("Lorsch et al."); Brett H. McDonnell ("B. McDonnell"); Motorola; O'Melveny & Myers; P&G; Pfizer; S&C; Sara Lee; Group of Seven Law Firms ("Seven Law Firms"); Shearman & Sterling; Securities Industry and Financial Markets Association ("SIFMA"); Society of Corporate Secretaries; Southern Company; U.S. Bancorp; Wachtell.

85 See letters from ABA; BRT; Delaware Bar.

86 See letters from DTE Energy (endorsing the opt-out approach described in the letter submitted by the Society of Corporate Secretaries); JPMorgan Chase; P&G; Seven Law Firms; Society of Corporate Secretaries; U.S. Bancorp.

87 See letters from 13D Monitor; AFL-CIO; CalPERS; CFA Institute; CII; Florida State Board of Administration; ICGN; LIUNA; D. Nappier; P. Neuhauser; Pax World; OPERS; RiskMetrics; SWIB; Teamsters; USPE.

board.[88] Several commenters stated they oppose a provision that would permit companies to opt out of Rule 14a-11.[89] Some commenters expressed a general concern that if companies are allowed to opt out of the rule, boards would adopt provisions in a company's governing documents that are so restrictive that it would be impossible for shareholders to have their candidates included in company proxy materials,[90] with one commenter noting that the laws of most states would allow a board to adopt such provisions in a company's bylaws without a shareholder vote.[91] Further, a commenter warned that boards would use corporate funds to defeat shareholders' attempts to change such board-adopted provisions through shareholder proposals.[92] One commenter argued that the "idea that individual corporations should be given the right to 'opt out' of the proposed regulations through bylaws or otherwise is contrary to the Commission's entire regulatory scheme" and referred to Section 14 of the Securities Act,[93] which voids "[a]ny condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission…."[94]

After carefully considering the comments, we have determined that Rule 14a-11 should

[88] See letters from 13D Monitor; AFL-CIO; CalPERS; CFA Institute; CII; Florida State Board of Administration; ICGN; LIUNA; D. Nappier; P. Neuhauser; Pax World; OPERS; RiskMetrics; SWIB; Teamsters; USPE.

[89] See letters from AFL-CIO; Amalgamated Bank; William Baker ("W. Baker"); Florida State Board of Administration; International Association of Machinists and Aerospace Workers ("IAM"); The Marco Consulting Group ("Marco Consulting"); P. Neuhauser; Nine Law Firms; Norges Bank Investment Management ("Norges Bank"); Relational; Shamrock Capital Advisors, Inc. ("Shamrock"); TIAA-CREF; USPE; ValueAct Capital.

[90] See letters from Florida State Board of Administration; P. Neuhauser; Shamrock.

[91] See letter from Shamrock.

[92] See letter from P. Neuhauser.

[93] Letter from Nine Law Firms.

[94] 15 U.S.C. 77n.

not provide an exemption for companies that have or adopt a provision in their governing documents that provides for or prohibits the inclusion of shareholder director nominees in the company's proxy materials. Thus, regardless of whether a company has a provision for the inclusion of shareholder nominees in its proxy materials, Rule 14a-11 will apply. As noted, the only exception is if state or foreign law or a company's governing documents prohibits shareholders from making director nominations.

We believe the rights to nominate and elect directors are traditional state law rights of all shareholders and we believe the current proxy rules could better facilitate the effective exercise of these state law rights. We do not believe that it is appropriate for our rules to permit a company's board or a majority of shareholders to elect to opt out of Rule 14a-11 and thus deprive other shareholders of an effective means to exercise their state law right to nominate directors and to freely exercise their franchise rights. Thus, allowing a vote to opt out of the rule would contravene a fundamental rationale of Rule 14a-11 – improving the degree to which shareholders participating through the proxy process are able "to control the corporation as effectively as they might have by attending a shareholder meeting."[95]

When shareholders have the right to nominate candidates for director at a shareholder meeting, we believe shareholder choice is enhanced if our rules facilitate the ability of shareholders to nominate candidates for director through the proxy process. Allowing a company or a majority of its shareholders to opt out of the rule would diminish the rights of shareholders who participate by proxy by preventing shareholder nominees from being included in company proxy materials, thus reducing shareholder choice in the critical area of director

[95] Business Roundtable v. SEC, 905 F.2d 406, 410 (D.C. Cir. 1990).

elections. Similarly, allowing a company or a majority of its shareholders to opt out of the rule would diminish the ability of shareholders to vote for nominees put forth by other shareholders.

In addition, companies and their shareholders do not have the option to elect to opt out of other federal proxy rules and we do not believe they should have the ability to do so with this rule. In our view, shareholders' electoral rights through the proxy process should not be impaired by a unilateral act of the board of directors, or even by a shareholder vote supported by management. Further, as we describe above, allowing some portion of shareholders to alter the application of Rule 14a-11 would effectively reduce choices for shareholders who do not favor that decision.[96]

Finally, we considered the objections of some commenters to a "one-size-fits-all" rule and concerns that for some companies with various capital structures the rule may raise more complex issues.[97] As we have noted, no federal proxy rule allows shareholders or boards to alter

---

96 Our view in this regard has been sharply criticized. E.g., Joseph A. Grundfest, The SEC's Proposed Proxy Access Rules: Politics, Economics, and the Law, 65 BUS. LAW. 361, 370 (2010) (this article also was included as an attachment to the January 18, 2010 letter from Joseph A. Grundfest ("Grundfest II")) ("there is no intellectually credible argument that shareholders are ... competent to elect directors but incompetent to determine the rules governing the election of directors. There is also no support for the proposition that shareholders can be trusted to relax the mandatory minimum standards established by the Commission, but not to strengthen them."). In our view, these assertions are flawed. This is not an issue of shareholder competence. It is, instead, a recognition that permitting a company or a group of shareholders to prevent shareholders from effectively participating in governing the corporation through participation in the proxy process is fundamentally inconsistent with the goal of federal proxy regulation. See Business Roundtable, 905 F.2d at 410.

97 See letters from 26 Corporate Secretaries; ABA; ACE; Advance Auto Parts; AGL; Aetna; Allstate; Alston & Bird; American Bankers Association; American Business Conference; American Electric Power; Anadarko; Applied Materials; Artistic Land Designs; Association of Corporate Counsel; Avis Budget; Atlantic Bingo; L. Behr; Best Buy; Biogen; J. Blanchard; Boeing; T. Bonkowski; BorgWarner; Boston Scientific; Brink's; BRT; Burlington Northern; R. Burt; California Bar; Callaway; S. Campbell; Carlson; Carolina Mills; Caterpillar; Chamber of Commerce/CMCC; Chevron; R. Chicko; CIGNA; Comcast; Competitive Enterprise Institute; W. Cornwell; CSX; E. Culwell; Cummins; Darden Restaurants; Daniels Manufacturing; Davis Polk; Delaware Bar; T. Dermody; Devon; DTE Energy; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; M. Eng; Erickson; ExxonMobil; FedEx; Financial Services Roundtable; Flutterby; FPL Group; Frontier; GE; A. Goolsby; C. Holliday; IBM; ICI; Intelect; JPMorgan Chase; Jones Day; R. Clark King; Leggett; T. Liddell; Little; McDonald's; MeadWestvaco; MedFaxx; Medical Insurance; Metlife; M. Metz; Microsoft; J. Miller; M. Moretti; Motorola; NACD; NAM; NIRI; O'Melveny & Myers; Office Depot; Omaha Door; P&G; PepsiCo; Pfizer; Realogy; J. Robert; M. Robert; RPM; Ryder; Safeway; R. Saul; Shearman & Sterling; Sherwin-Williams; R. Simoneau; Society of

how the rules apply to companies. The concept that our rules are not subject to company-by-company variation is entirely consistent with our mandate to protect all investors. In this regard, we are not persuaded that we should allow our rules to be altered by shareholders or boards to the potential detriment of other shareholders. We believe that having a uniform standard that applies to all companies subject to the rule will simplify use of the rule for shareholders and allowing different procedures and requirements to be adopted by each company could add significant complexity and cost for shareholders and undermine the purposes of our new rule. While other procedures and standards could be adopted by companies or shareholders to supplement Rule 14a-11, shareholders would benefit from the predictability of the uniform application of Rule 14a-11 at all companies.

It is important to note that while Rule 14a-11 facilitates the existing rights of shareholders and we do not believe the rule should be altered, it is not the exclusive way by which a candidate other than a management nominee may be put to a shareholder vote. Shareholders may continue to choose to conduct traditional proxy contests. Regardless of whether a shareholder uses Rule 14a-11 or conducts a traditional proxy contest to nominate a candidate for director, a company concerned about how such a shareholder nominee fits into its particular capital structure or other unique fact patterns presumably would address that concern in its proxy materials.

d. No triggering events

Under the Commission's 2003 Proposal, a company would have been subject to the shareholder director nomination requirements after the occurrence of one or both of two possible triggering events. The first triggering event was that at least one of the company's nominees for

---

Corporate Secretaries; Southern Company; Southland; Steele Group; Style Crest; Tesoro; Textron; Theragenics; TI;. R. Trummel; T. Trummel; V. Trummel; tw telecom; L. Tyson; United Brotherhood of Carpenters; UnitedHealth; U.S. Bancorp; VCG; Wachtell; Wellness; Wells Fargo; Whirlpool; Xerox; Yahoo; J. Young.

the board of directors for whom the company solicited proxies received withhold votes from more than 35% of the votes cast at an annual meeting of shareholders at which directors were elected.[98] The second triggering event was that a shareholder proposal submitted under Rule 14a-8 providing that a company become subject to the proposed shareholder nomination procedure was submitted for a vote of shareholders at an annual meeting by a shareholder or group of shareholders that held more than 1% of the company's securities entitled to vote on the proposal and the shareholder or group of shareholders held those securities for one year as of the date the proposal was submitted, and the proposal received more than 50% of the votes cast on that proposal at the meeting.[99] In 2003, these triggering events were included because they were believed to be indications that a company had a demonstrated corporate governance issue, such that shareholders should have the opportunity to include director nominees in the company's proxy materials.

Unlike the 2003 Proposal, our current proposal did not include a triggering event requirement in Rule 14a-11. As noted in the Proposing Release, we did not include such a requirement because we were concerned that the federal proxy rules may be impeding the exercise of shareholders' ability under state law to nominate and elect directors at all companies, not just those with demonstrated governance issues. In addition, we noted our concern, and the concern expressed by commenters on the 2003 Proposal, that the inclusion of triggering events would result in unnecessary complexity and would delay the operation of the rule. However, we solicited comment about whether triggers for the application of Rule 14a-11 would be appropriate.

---

98 This triggering event could not occur in a contested election to which Rule 14a-12(c) would apply or an election to which the proposed shareholder nomination procedure would have applied.

99 Only votes for and against a proposal would have been included in the calculation of the shareholder vote.

Many commenters opposed the inclusion of a triggering event requirement,[100] with some commenters expressing concern that triggering events would cause significant delays and introduce undue complexity into the rule.[101] On the other hand, other commenters supported the inclusion of a triggering event requirement, believing that such a requirement would serve as a useful indicator of the companies with demonstrated governance issues (e.g., companies that do not act within a certain time period on a shareholder proposal that received majority support).[102]

We remain concerned that the federal proxy rules may not be facilitating the exercise of shareholders' ability under state law to nominate and elect directors and this concern is not limited to shareholders' ability to nominate directors at companies with demonstrated governance issues. Indeed, allowing shareholders to include nominees in company proxy materials before there are demonstrated governance failures could have the benefit of increasing director responsiveness and avoiding future governance failures. In addition, we share the concerns of some commenters that inclusion of triggering events would introduce undue complexity to the rule. Therefore, we are adopting the rule as proposed, without a triggering event requirement.

e. Concurrent proxy contests

As proposed, Rule 14a-11 would apply regardless of whether a company is engaged in, or

---

100 See letters from AFSCME; CalSTRS; CFA Institute; CII; COPERA; T. DiNapoli; Florida State Board of Administration; ICGN; N. Lautenbach; LIUNA; D. Nappier; Nathan Cummings Foundation; OPERS; Pax World; Relational; Sodali; SWIB; TIAA-CREF; G. Tooker; USPE; ValueAct Capital.

101 See letters from AFSCME; CFA Institute; CII; T. DiNapoli; LIUNA.

102 See letters from Automatic Data Processing, Inc. ("ADP"); Alaska Air Group, Inc. ("Alaska Air"); Allstate; American Electric Power; Anadarko; AT&T; Avis Budget; Barclays Global Investors ("Barclays"); Biogen; Boeing; BRT; Burlington Northern; R. Burt; Callaway; Chevron; CIGNA; CNH Global N.V. ("CNH Global"); Comcast; Cummins; Deere & Company ("Deere"); Eaton; ExxonMobil; FedEx; FMC Corp.; FPL Group; Frontier; General Mills; C. Holliday; IBM; ITT Corporation ("ITT"); J. Kilts; Ellen J. Kullman ("E.J. Kullman"); N. Lautenbach; McDonald's; J. Miller; Motorola; Office Depot; O'Melveny & Myers; P&G; PepsiCo; Pfizer; Protective; Ryder; Sara Lee; Sherwin-Williams; Theragenics; TI; tw telecom; G. Tooker; UnitedHealth; Xerox.

anticipates being engaged in, a concurrent proxy contest; however, we requested comment on whether a company should be exempted from complying with Rule 14a-11 if another party commences or evidences its intent to commence a solicitation in opposition subject to Rule 14a-12(c). Of the commenters that responded, a few stated that shareholders of a company that is the subject of a traditional proxy contest should be allowed to use Rule 14a-11 to have nominees included in the company's proxy materials,[103] and others stated that shareholders of a company engaged in a traditional proxy contest should not be allowed to use Rule 14a-11 to have nominees included in the company's proxy materials.[104]

In support of enabling shareholders to use Rule 14a-11 during a traditional proxy contest, one commenter argued that exempting companies subject to a traditional proxy contest from Rule 14a-11 would be inconsistent with the Commission's objective of changing the proxy process to better reflect the rights shareholders would have at a shareholder meeting, and that dissatisfied shareholders who are not seeking a change in control and who otherwise meet the eligibility criteria under Rule 14a-11 would be disenfranchised.[105] The commenter stated that dissatisfied shareholders should not be forced to make a choice between a change in control or "business as usual." Another commenter stated that contested elections have been conducted successfully with more than two slates.[106]

On the other hand, commenters that sought a limitation on use of Rule 14a-11 during a traditional proxy contest were concerned that Rule 14a-11 could have the effect of facilitating a

103 See letters from CII; Florida State Board of Administration; Sodali; USPE.

104 See letters from ABA; American Express; Biogen; BorgWarner; BRT; Davis Polk; Dewey; Eli Lilly; Fenwick; Honeywell; JPMorgan Chase; Leggett; PepsiCo; Seven Law Firms; Society of Corporate Secretaries; Tenet; U.S. Bancorp; Verizon; Wachtell.

105 See letter from CII.

106 See letter from Florida State Board of Administration.

change in control of the company.[107] Commenters noted that under certain staff positions,[108] as well as the Commission's discussion of Rule 14a-4(d)(4), as set forth in the Proxy Disclosure and Solicitation Enhancements proposing release,[109] a dissident shareholder could "round out" its short-slate proxy card by seeking authority to vote for Rule 14a-11 shareholder nominees, thereby facilitating a change in control.[110] Further, commenters believed that under the Proposal shareholders that submit nominees in reliance on Rule 14a-11 would not be barred from actively soliciting for the nominees of a shareholder using a traditional proxy contest and, conversely, a shareholder using a traditional proxy contest could actively engage in soliciting activities for Rule 14a-11 shareholder nominees.[111] Commenters also worried that multiple groups of shareholders who simultaneously propose different directors for different purposes could lead to substantial confusion for other shareholders.[112] Commenters warned that shareholder confusion would increase if there are two or more proxy cards with more than twice the number of nominees than available slots.[113] According to these commenters, further confusion would result from any assumption by shareholders that the Rule 14a-11 slate is allied with the insurgent slate, despite the Rule 14a-11 representation regarding the lack of control intent.[114] One commenter

107 See letters from ABA; BRT; Davis Polk; Eli Lilly; Seven Law Firms; Society of Corporate Secretaries.

108 See Eastbourne Capital LLC No-Action Letter (March 30, 2009) and Icahn Associates Corp. No-Action Letter (March 30, 2009).

109 Release No. 33-9052, 34-60280 (July 10, 2009) [74 FR 35076].

110 See letters from ABA; Eli Lilly; JPMorgan Chase; Society of Corporate Secretaries.

111 See letters from ABA; Society of Corporate Secretaries.

112 See letters from ABA; BRT; Davis Polk; Eli Lilly; PepsiCo; Seven Law Firms; Society of Corporate Secretaries.

113 See letters from ABA; Davis Polk.

114 See Section II.B.4. below for a further discussion of change in control intent and the certifications required by the new rules.

also argued that, despite the Rule 14a-11 representation regarding the lack of control intent, it is "easy to imagine that in some contested elections, a [R]ule 14a-11 nominee would be the swing vote, tipping the majority of the board and thus control of the company."[115] Citing these same concerns, another commenter recommended that when a company's board receives notice of a traditional proxy contest, the company should be permitted to exclude Rule 14a-11 nominees from the company's proxy materials (and, if the proxy materials have already been distributed, to issue supplemental proxy materials eliminating these nominees from the company's materials).[116]

Finally, some commenters argued that Rule 14a-11 is unnecessary when a company is engaged in a traditional proxy contest because the company's shareholders are already effectively exercising their rights under state law to nominate and elect directors.[117] One commenter stated that if the Commission decides not to prohibit a concurrent vote on Rule 14a-11 nominees and nominees presented through a traditional proxy contest, it should at least provide that the nominees presented through the traditional proxy contest be counted against the number of permissible Rule 14a-11 nominees to reduce the likelihood of a change in control.[118] The commenter stated that if Rule 14a-11 could be used concurrently with a traditional proxy contest, the nominating shareholder should not be allowed to be a "participant" (as defined under Schedule 14A) in the traditional proxy contest or to engage in any soliciting activity for a nominee of another shareholder. The commenter also suggested that dissidents in a traditional proxy contest be precluded from including Rule 14a-11 nominees on their proxy card. Acknowledging the possibility of collusion, shareholder confusion, and change in control, one

---

115 Letter from Davis Polk.

116 See letter from Society of Corporate Secretaries.

117 See letters from BRT; Verizon.

118 See letter from ABA.

commenter expressed support for reasonable limitations on a Rule 14a-11 nomination if there is a simultaneous proxy contest.[119]

While we appreciate commenters' concerns, we do not believe that our efforts to facilitate the exercise of shareholders' state law right to nominate directors should be limited by the activities of other persons engaged in a traditional proxy contest. We also believe that, as described below, Rule 14a-11 and the related rule amendments, together with our staff review process, can adequately address concerns about investor confusion and potential abuse of the process by those seeking a change in control. Therefore, we are adopting the rule as proposed, without an exception for companies that are subject to or anticipate being subject to a concurrent proxy contest. In this regard, we agree with those commenters that opposed including a limitation because to do so would be inconsistent with the goals of our rulemaking, which are not limited by the nomination activities of other persons. In addition, we note that there is no current limitation in the federal proxy rules on the number of proxy contests that can take place simultaneously and we do not believe that there is sufficient reason to provide such a limitation in this circumstance. Companies and shareholders have been able, to date, to successfully navigate multiple slates on those occasions when more than one person undertakes a proxy contest. In addition, we believe that a company can address commenters' concerns through disclosure in its proxy materials. For example, the company may disclose in its proxy statement potential effects of electing non-management nominees (whether those nominees are included in the company's materials or in other soliciting persons' materials), such as the potential to cause the company to violate law or the independence requirements of the exchange listing standards, and allow shareholders to consider that information when making their voting decisions.

---

119 See letter from P. Neuhauser.

Similarly, we believe that appropriate disclosure in the company's proxy materials, as well as the dissident's proxy materials, could serve to potentially avoid shareholder confusion about how many nominees a shareholder may vote for and how to mark the card.

We also have not revised Rule 14a-11, as suggested by commenters, to count nominees put forth by persons outside of Rule 14a-11 for purposes of the calculation of the maximum number of nominees required to be included in the company's proxy materials pursuant to Rule 14a-11. We believe that to do so would, like an outright exception, be inconsistent with the goal of our rulemaking – to change the proxy process to better reflect the rights shareholders would have at a shareholder meeting, which are not limited by the nomination activities of other persons.

While we are not adopting an exception from the rule for companies that are, or anticipate being, subject to a concurrent proxy contest, we do understand concerns about the possibility of confusion and abuse in this area absent clear guidance.[120] Accordingly, we have made clear in our discussion, in Section II.B.10. below, that a nominating shareholder or group relying on new Rule 14a-2(b)(7) or (8) to engage in an exempt solicitation to form a nominating shareholder group or in connection with a nomination included in the company's proxy materials pursuant to Rule 14a-11 would lose the exemption if they engage in a non-Rule 14a-11 solicitation for directors or another person's solicitation with regard to the election of directors. In addition, we are adopting an instruction to Rule 14a-11[121] to make clear that, in order to rely on Rule 14a-11 to have a nominee or nominees included in a company's proxy materials, a nominating shareholder or group or any member of the nominating shareholder or group may not

120 See, e.g., letters from ABA; Seven Law Firms.

121 See Instruction to Rule 14a-11(b).

be a member of any other group with persons engaged in solicitations or other nominating activities in connection with the subject election of directors; may not separately conduct a solicitation in connection with the subject election of directors other than a Rule 14a-2(b)(8) exempt solicitation in relation to those nominees it has nominated pursuant to Rule 14a-11 or for or against the company's nominees; and may not act as a participant in another person's solicitation in connection with the subject election of directors.

3. Which Companies Are Subject to Rule 14a-11

a. General

In this section, we discuss which companies will be subject to new Rule 14a-11, including the rule's application to investment companies, controlled companies, "debt-only" companies, voluntary registrants, and smaller reporting companies.

New Rule 14a-11 will apply to companies that are subject to the Exchange Act proxy rules, including investment companies registered under Section 8 of the Investment Company Act of 1940.[122] The rule also will apply to controlled companies and those companies that choose to voluntarily register a class of securities under Section 12(g). Smaller reporting companies will be subject to the rule, but on a delayed basis. Consistent with the Proposal, we have excepted from the rule's application companies that are subject to the proxy rules solely because they have a class of debt registered under Section 12 of the Exchange Act. In addition, foreign private issuers are exempt from the Commission's proxy rules with respect to

---

122 15 U.S.C. 80a et seq. Registered investment companies currently are required to comply with the proxy rules under the Exchange Act when soliciting proxies, including proxies relating to the election of directors. See Investment Company Act Rule 20a-1 [17 CFR 270.20a-1] (requiring registered investment companies to comply with regulations adopted pursuant to Section 14(a) of the Exchange Act that would be applicable to a proxy solicitation if it were made in respect of a security registered pursuant to Section 12 of the Exchange Act).

solicitations of their shareholders, so the rule will not apply to these issuers.[123]

b. Investment companies

Under the Proposal, Rule 14a-11 would apply to registered investment companies. We sought comment on whether Rule 14a-11 should apply to these companies.[124]

Several commenters supported including registered investment companies in the rule.[125] Commenters noted that investment company boards, like other boards, must be responsive and accountable to their shareholders;[126] that some investment company boards are "too cozy" with the company's investment adviser;[127] and that the proposed rule will add competition to the board nomination process, which may create some traction in board negotiations with the company's investment adviser.[128] A number of commenters did not believe that the rule would result in unreasonable cost or an excessive number of contested elections.[129] One commenter suggested that investment company shareholders would use the rule infrequently and then only if the investment company is experiencing a real governance or other failure.[130]

On the other hand, a number of commenters, largely from the investment company

123 Exchange Act Rule 3a12-3 [17 CFR 240.3a12-3] exempts securities of certain foreign issuers from Section 14(a) of the Exchange Act.

124 The Commission has considered the impact of this issue on investment companies on prior occasions. See, e.g., 2003 Proposal.

125 See, e.g., letters from AFSCME; CalPERS; CII; Mutual Fund Directors Forum ("MFDF"); Julian Reid ("J. Reid"); Jennifer S. Taub ("J. Taub"); TIAA-CREF.

126 See letter from MFDF.

127 Letter from J. Reid.

128 See letter from J. Taub.

129 See, e.g., letters from AFSCME; J. Taub.

130 See letter from J. Taub.

industry, opposed the inclusion of registered investment companies in the rule.[131] Commenters asserted that the Commission had not presented any empirical evidence of governance problems with respect to investment companies that would support extending the rule to them and that the trend for investment company boards is to have strong governance practices.[132] Commenters also argued that investment companies are subject to a unique regulatory regime under the Investment Company Act that provides additional protection to investors, such as the requirement to obtain shareholder approval to engage in certain transactions or activities,[133] and that investment companies and their boards have very different functions from non-investment companies and their boards.[134] One commenter noted that the Proposal would be inappropriate and not

---

131 See, e.g., letters from ABA; American Bar Association (September 18, 2009) ("ABA II"); Barclays; ICI; Investment Company Institute and Independent Directors Counsel ("ICI/IDC"); Independent Directors Council ("IDC"); S&C; T. Rowe Price Associates, Inc. ("T. Rowe Price"); The Vanguard Group, Inc. ("Vanguard"). One commenter opposed the inclusion of business development companies in the rule for the same reasons that it opposed including registered investment companies in the rule. See letter from ICI. Business development companies are a category of closed-end investment companies that are not registered under the Investment Company Act, but are subject to certain provisions of that Act. See Sections 2(a)(48) and 54-65 of the Investment Company Act [15 U.S.C. 80a-2(a)(48) and 80a-53-64]. We are including business development companies in the rule for the same reasons provided below with respect to registered investment companies.

132 See letters from ICI; ICI/IDC; IDC; T. Rowe Price; S&C. Among other things, commenters noted that 90% of fund complexes have boards that are 75% or more comprised of independent directors and the vast majority of fund boards have an independent director serving as chairman or as lead independent director. See letters from ICI/IDC; IDC. Two letters also cited a 1992 report by Commission staff that observed that the governance model embodied by the Investment Company Act is sound and should be retained with limited modifications. See letters from ICI; ICI/IDC.

133 One joint comment letter noted that the Investment Company Act requires investment companies to obtain shareholder approval of contracts with the company's investment adviser and distributor and to change from an open-end, closed-end, or diversified company; to borrow money; to issue senior securities; to underwrite securities issued by other persons; to purchase or sell real estate or commodities; to make loans to other persons, except in accordance with the policy in the company's registration statement; to change the nature of its business so as to cease to be an investment company; or to deviate from a stated policy with respect to concentration of investments in an industry or industries, from any investment policy which is changeable only by shareholder vote, or from any stated fundamental policy. The commenters also noted that investment company shareholders have the right to bring an action against the company's investment adviser for breach of fiduciary duty with respect to receipt of compensation. See letter from ICI/IDC.

134 See letters from ABA; Barclays; ICI; ICI/IDC; IDC; T. Rowe Price; S&C; Vanguard. However, we note that, in response to the 2003 Proposal, ABA and ICI indicated that there were no reasons to treat investment companies differently from non-investment companies. See letter from Investment Company Institute (December 22, 2003) on File No. S7-19-03; letter from American Bar Association (January 7,

particularly useful for most open-end management investment companies, because open-end management investment company shares are held on a short-term basis and open-end management investment companies are not typically required to hold annual meetings under state law.[135]

Commenters also were concerned about the costs of the Proposal, particularly for fund complexes that utilize a "unitary" board consisting of one group of individuals who serve on the board of every fund in the complex, or "cluster" boards consisting of two or more groups of individuals that each oversee a different set of funds in the complex.[136] Commenters noted that if a shareholder-nominated director were to be elected to a unitary or cluster board, the investment companies in the fund complex would incur significant additional administrative costs and burdens (e.g., the shareholder-nominated director would have to leave during discussions that pertain to the other investment companies in the complex, board materials would have to be

---

2004) on File No. S7-19-03.

135 See letter from ABA. See also letter from S&C (urging that at a minimum Rule 14a-11 should not apply to open-end investment companies, "which do not generally hold regular meetings and for which compliance would be particularly burdensome"). An open-end management investment company is an investment company, other than a unit investment trust or face-amount certificate company, that offers for sale or has outstanding any redeemable security of which it is the issuer. See Sections 4 and 5(a)(1) of the Investment Company Act [15 U.S.C. 80a-4 and 80a-5(a)(1)].

136 See letters from ABA; ICI; ICI/IDC; IDC; MFDF; S&C; T. Rowe Price; Vanguard. Commenters noted that a recent survey of fund complexes representing 93% of the industry's total net assets indicated that 83% of fund complexes had a unitary board structure and 17% of fund complexes had a cluster board structure. See letters from ICI/IDC; IDC. However, one comment letter included materials noting that, while the average number of registered investment companies per fund complex is five, the median number of registered investment companies per fund complex is one. See letter from ICI/IDC. In cases where the fund complex consists of only one company, commenters' concerns about the loss of the unitary board would not be present.

Commenters also noted that among fund complexes that use unitary or cluster boards there are other aspects of board organization that vary from complex to complex. See letter from ICI/IDC. For example, one board may oversee all of the open-end funds in the complex and all but three of its closed-end funds, while a second board oversees the other closed-end funds. Alternatively, one board may oversee the open-end and closed-end fixed income funds advised by one particular adviser, while a second board oversees the open-end and closed-end equity and international funds advised by a second adviser, etc. However, the commenters did not note any specific issues that would be raised by the use of different structures among fund complexes using unitary or cluster boards if the Proposal were to be adopted.

customized for the director, and the fund complex would face challenges in preserving the status of privileged information) and the benefits of the unitary or cluster board that result in the increased effectiveness of such boards would be lost.[137] One commenter also stated that if a shareholder nomination causes an election to be "contested" under rules of the New York Stock Exchange, brokers would not be able to vote client shares on a discretionary basis, making it difficult and more expensive for investment companies to achieve a quorum for a meeting.[138]

After considering these comments, we agree with the commenters who believe that Rule 14a-11 should apply to registered investment companies, as was proposed. The purpose of Rule 14a-11 is to facilitate the exercise of shareholders' traditional state law rights to nominate and elect directors to boards of directors and thereby enable shareholders to participate more meaningfully in the nomination and election of directors at the companies in which they invest. These state law rights apply to the shareholders of investment companies, including each investment company in a fund complex, regardless of whether or not the fund complex utilizes a unitary or cluster board.[139] Moreover, although investment companies and their boards may have different functions from non-investment companies and their boards, investment company boards, like the boards of other companies, have significant responsibilities in protecting

137 Commenters noted that unitary and cluster boards can result in enhanced board efficiency and greater board knowledge of the many aspects of fund operations that are complex-wide in nature. See, e.g., letters from ABA; ICI; ICI/IDC; IDC; MFDF; S&C; T. Rowe Price; Vanguard. For instance, commenters noted that many of the same regulatory, valuation, compliance, disclosure, accounting, and business issues may arise for all of the funds that the unitary or cluster board oversees and that consistency among funds in the complex greatly enhances both board efficiency and shareholder protection. See, e.g., letter from ICI/IDC. One joint comment letter also suggested that "[b]ecause they are negotiating on behalf of multiple funds, unitary and cluster boards have a greater ability than single fund boards to negotiate with management over matters such as fund expenses; the level of resources devoted to technology; and compliance and audit functions." See id.

138 See letter from S&C.

139 We note that "unitary" or "cluster" boards are not required by state law.

shareholder interests, such as the approval of advisory contracts and fees.[140] Therefore, we are not persuaded that exempting registered investment companies would be consistent with our goals. We also do not believe that the regulatory protections offered by the Investment Company Act (including requirements to obtain shareholder approval to engage in certain transactions and activities), the trend asserted by commenters for investment companies to have good governance practices, or the fact that open-end management investment companies are not required by state law to hold annual meetings serves to decrease the importance of the rights that are granted to shareholders under state law.[141] In fact, the separate regulatory regime to which investment companies are subject emphasizes the importance of investment company directors in dealing with the conflicts of interest created by the external management structure of most investment companies.[142] We also note that some commenters have raised governance concerns regarding

---

140 See Jones v. Harris Assocs., 130 S.Ct. 1418, 1423, 176 L. Ed. 2d 265, 273-274 (2010). See also S. Rep. No. 91-184; 91st Congress 1st Session; S. 2224 (1969) ("This section is not intended to authorize a court to substitute its business judgment for that of the mutual fund's board of directors in the area of management fees. . . . The directors of a mutual fund, like directors of any other corporation will continue to have . . . overall fiduciary duties as directors for the supervision of all of the affairs of the fund."); letter from ICI/IDC ("The Investment Company Act of 1940 and the rules under it impose significant responsibilities on fund directors in addition to the duties of loyalty and care to which directors are typically bound under state law.").

141 In the 1992 report cited by two comment letters in footnote 132 above, the Commission staff also observed that the Investment Company Act "establishes a comprehensive regulatory framework predicated upon principles of corporate democracy" and was intended to provide an additional safeguard for investors by according "voting powers to investment company shareholders beyond those required by state corporate law." Division of Investment Management, U.S. Securities and Exchange Commission, Protecting Investors: A Half Century of Investment Company Regulation, at pp. 251-52, 260 (May 1992) (emphasis added).

142 See, e.g., Commission Guidance Regarding the Duties and Responsibilities of Investment Company Boards of Directors with Respect to Investment Adviser Portfolio Trading Practices, Release No. IC-28345 (July 30, 2008) [73 FR 45646, 45649 (August 6, 2008)] ("In addition to statutory and common law obligations, fund directors are also subject to specific fiduciary obligations relating to the special nature of funds under the Investment Company Act. . . . A fund board has the responsibility, among other duties, to monitor the conflicts of interest facing the fund's investment adviser and determine how the conflicts should be managed to help ensure that the fund is being operated in the best interest of the fund's shareholders.") (footnotes omitted); Interpretive Matters Concerning Independent Directors of Investment Companies, Release No. IC-24083 (October 14, 1999) [64 FR 59877, 59877-78 (November 3, 1999)] (listing various duties and responsibilities of the independent directors of an investment company and noting that "Each of these duties and responsibilities is vital to the proper functioning of fund operations and, ultimately, the

the relationship between boards and investment advisers.[143]

We are cognizant of the fact that the rule will impose some costs on investment companies. We believe, however, that policy goals and the benefits of the rule justify these costs. As discussed above, we believe that facilitating the exercise of traditional state law rights to nominate and elect directors is as much of a concern for investment company shareholders as it is for shareholders of non-investment companies. We continue to believe that parts of the proxy process may frustrate the exercise of shareholders' rights to nominate and elect directors arising under state law, and thereby fail to provide fair corporate suffrage. The new rules seek to facilitate shareholders' effective exercise of their rights under state law to both nominate and elect directors. In this regard, we note that commenters have stated that interest in mutual fund governance has increased in recent years.[144]

We recognize that it may be more costly for investment companies to achieve a quorum at shareholder meetings if a shareholder director nomination causes an election to be "contested" under rules of the New York Stock Exchange and brokers cannot vote customer shares on a discretionary basis. Furthermore, for fund complexes that utilize unitary or cluster boards, the election of a shareholder director nominee may, in some circumstances, increase costs and potentially decrease the efficiency of the boards.

We note, however, that these costs are associated with the state law right to nominate and elect directors, and are not costs incurred for including shareholder nominees in the company's proxy statement. With respect to fund complexes utilizing unitary or cluster boards, we note that

---

protection of fund shareholders.").

143 See letters from J. Reid; J. Taub.

144 See letters from AFSCME; J. Taub.

any increased costs and decreased efficiency of an investment company's board as a result of the fund complex no longer having a unitary or cluster board would occur, if at all, only in the event that investment company shareholders elect the shareholder nominee. Investment companies may include information in the proxy materials making investors aware of the company's views on the perceived benefits of a unitary or cluster board and the potential for increased costs and decreased efficiency if the shareholder nominees are elected. Moreover, we note that a fund complex can take steps to minimize the cost and burden of a shareholder-nominated director by, for example, entering into a confidentiality agreement in order to preserve the status of confidential information regarding the fund complex.[145]

We believe that the costs imposed on investment companies will be less significant than the costs imposed on other companies for three reasons. First, to the extent investment companies do not hold annual meetings as permitted by state law, investment company shareholders will have less opportunity to use the rule.[146] Second, even when investment company shareholders do have the opportunity to use the rule, the disproportionately large and generally passive retail shareholder base of investment companies will probably mean that the rule will be used less frequently than will be the case with non-investment companies.[147] Third, because we have sought to limit the cost and burden on all companies, including investment

---

145 Two commenters argued in a joint comment letter that there are a number of practical and legal issues that prevent confidentiality agreements from being sufficient to address the issues that arise when a shareholder-nominated director is elected to the board of an investment company in a fund complex using a unitary or cluster board. See letter from ICI/IDC. We emphasize that entering into a confidentiality agreement is only one method of preserving the confidentiality of information revealed in board meetings attended by the shareholder-nominated director. The fund complex can have separate meetings and board materials for the board with the shareholder-nominated director, especially if particularly sensitive legal or other matters will be discussed or to protect attorney-client privilege. For a further discussion of this comment, see Section IV.E.1.

146 See letters from ABA; MFDF.

147 See letter from J. Taub.

companies, by limiting use of Rule 14a-11 to shareholders who have maintained significant continuous holdings in the company for at least three years, and because many funds, such as money market funds, are held by shareholders on a short-term basis,[148] we believe that the situations where shareholders will meet the eligibility requirements will be limited.

Although commenters argued that the election of a shareholder-nominated director to a unitary or cluster board will necessarily result in decreased effectiveness of the board, we disagree. In this regard, one commenter argued that competition in the board nomination process may improve efficiency by providing additional leverage for boards in negotiations with the investment adviser.[149] In any event, we believe that investment company shareholders should have a more meaningful opportunity to exercise their traditional state law rights to elect a non-unitary or non-cluster board if they so choose.

c. Controlled companies

As proposed, Rule 14a-11 would allow eligible shareholders to submit director nominees at all companies subject to the Exchange Act proxy rules other than companies that are subject to the proxy rules solely because they have a class of debt registered under Section 12 of the Exchange Act. We sought comment on whether Rule 14a-11 also should provide an exception for controlled companies.

In response to our request for comment, one commenter argued that controlled companies should not be excluded from Rule 14a-11,[150] acknowledging that while there may be no mathematical possibility of a shareholder nominee submitted pursuant to Rule 14a-11 being

---

148 See letter from ABA.

149 See letter from J. Taub.

150 See letter from P. Neuhauser.

elected at a controlled company, in a controlled company there could be an even greater need for non-controlling shareholders to express their concerns. The commenter noted that a large – even if not a majority – vote by non-controlling shareholders could send an important message to the board. Other commenters noted that controlled companies are commonly structured with dual classes of stock, which allows shareholders of the non-controlling class of stock to elect a set number of directors that is less than the full board.[151] Another commenter noted that dual-class companies with supervoting stock often can benefit the most from having the interests of non-controlling shareholders better represented in the boardroom.[152] This commenter encouraged the Commission to include some means by which minority shareholders of dual-class and parent-controlled companies could meaningfully avail themselves of the rule, even if a different set of eligibility or disclosure requirements is determined to be more appropriate in these cases.

On the other hand, several commenters argued that controlled companies should be excluded from Rule 14a-11.[153] According to these commenters, providing shareholders the ability to include nominees in company proxy materials in this context would be ineffective and needlessly disruptive and costly because there is no prospect that a shareholder nominee would be elected.[154] Two of these commenters also noted that subjecting these companies to Rule 14a-11 would possibly cause investor confusion.[155] These commenters remarked that shareholders would continue to have other avenues to express their views to the company, such as through the

---

151 See letters from ABA; Duane Morris; Media General, Inc. ("Media General"); The New York Times Company ("New York Times").

152 See letter from T. Rowe Price.

153 See letters from ABA; AllianceBernstein; Cleary; Seven Law Firms; Duane Morris LLP ("Duane Morris"); Sidley Austin.

154 See letters from ABA; AllianceBernstein; Cleary; Seven Law Firms; Duane Morris; Sidley Austin.

155 See letters from ABA; Seven Law Firms.

Rule 14a-8 process. Commenters who supported an exclusion for controlled companies suggested that for purposes of the exclusion the definition of "controlled company" should be similar to the definition used by the national securities exchanges in connection with director independence requirements.[156] Some commenters suggested that if Rule 14a-11 excluded controlled companies using the same definition as the national securities exchanges in connection with director independence requirements, then the rule should contain an instruction providing that whether more than 50% of the voting power of a company is held by an individual, group, or other company would be determined by any schedules filed under Section 13(d) of the Exchange Act.[157]

After considering the issue further, we are persuaded that Rule 14a-11 should apply to controlled companies, as we proposed. As commenters noted, it is common for companies structured with dual classes of stock to allow shareholders of the non-controlling class to elect a set number of directors that is less than the full board. In that situation, it may be useful for non-controlling shareholders to be able to include shareholder nominations in company proxy materials with respect to the directors the non-controlling class is entitled to elect. In addition, though applying Rule 14a-11 to controlled companies would be unlikely to result in the election of shareholder-nominated directors in cases in which these are not directors elected exclusively by the non-controlling shareholders, we appreciate that shareholders at controlled companies may have other reasons for nominating candidates for director.[158]

---

156 See letters from ABA; AllianceBernstein; Cleary; Seven Law Firms; Duane Morris; Sidley Austin. See, e.g., New York Stock Exchange Rule 303A.00 and NASDAQ Stock Market LLC Rule 5615(c) (defining "controlled companies" as a company of which more than 50% of the voting power for the election of directors is held by an individual, group or another company).

157 See letters from AllianceBernstein; Duane Morris.

158 We note that controlled companies are not excluded from Rule 14a-8 despite the same improbability that a shareholder proposal will receive the approval of the majority of the votes cast at a controlled company.

d. "Debt only" companies

As proposed, Rule 14a-11 would allow eligible shareholders to submit director nominees at all companies subject to the Exchange Act proxy rules other than companies that are subject to the proxy rules solely because they have a class of debt securities registered under Section 12 of the Exchange Act. We sought comment on whether this exclusion from Rule 14a-11 was appropriate.

Commenters that specifically addressed this question agreed with our approach and stated generally that Rule 14a-11 should not apply to companies subject to the federal proxy rules solely because they have a class of debt securities registered under Exchange Act Section 12.[159] Most of these commenters stated that the ability to submit nominees for inclusion in a company's proxy materials should be limited to holders of equity securities registered under the Exchange Act.[160] One commenter warned that subjecting companies with a registered class of debt securities to Rule 14a-11 would deter private companies from accessing the public debt market and, in any case, private companies typically have shareholder agreements and other arrangements in place that address the election of directors.[161]

We are adopting this exclusion as proposed. We note that this approach was supported by investor and corporate commenters. We believe that Rule 14a-11 should not apply to

---

Shareholders may use Rule 14a-8 to submit a proposal to the board even though controlling shareholders may vote against the proposal and prevent it from being approved.

159 See letters from ABA; CII; Cleary; S&C.

160 See letters from ABA; Cleary; S&C.

161 See letter from S&C. This commenter also stated that Rule 14a-11 should not apply to those reporting companies who voluntarily continue to file Exchange Act reports while they are not required to do so under Exchange Act Section 13(a) or Section 15(d). It argued that these voluntary filers should be treated the same as companies with Exchange Act reporting obligations relating solely to debt securities. We note that Rule 14a-11 will not apply to a company filing Exchange Act reports when neither Exchange Act Section 13(a) nor Section 15(d) requires that it do so (for example, to comply with a covenant contained in an indenture relating to outstanding debt securities).

companies that are subject to the federal proxy rules solely because they have a class of debt securities registered under Section 12 of the Exchange Act.

e. Application of Exchange Act Rule 14a-11 to companies that voluntarily register a class of securities under Exchange Act Section 12(g)

In the Proposing Release, we noted that Rule 14a-11 would apply to companies that have voluntarily registered a class of equity securities pursuant to Exchange Act Section 12(g); however, we solicited comment on whether Rule 14a-11 should apply to these companies.[162] We also asked whether nominating shareholders of these companies should be subject to the same ownership eligibility thresholds as those shareholders of companies that were required to register a class of equity securities pursuant to Section 12, or whether we should adjust any other aspects of Rule 14a-11 for these companies.

Three commenters stated that Rule 14a-11 should apply to companies that voluntarily register a class of equity securities under Exchange Act Section 12(g).[163] One explained that investors in securities registered under Section 12 should be provided some assurance that the company is subject to various rules safeguarding their interests, such as the proposed rule, and expressed concern that less than uniform application could lead to investor confusion.[164] One commenter stated that nominating shareholders of voluntarily-registered companies should be subject to the same ownership thresholds as shareholders of companies that were required to

---

[162] A company must register a class of equity securities under Section 12(g) if, on the last day of its fiscal year, the class of equity securities is held by 500 or more record holders and the company has total assets of more than $10 million. An issuer may, however, register any class of equity securities under Section 12(g) even if these thresholds have not been met. Reporting after this form of voluntary registration is distinguished from a company that continues to file Exchange Act reports when neither Exchange Act Section 13(a) nor Section 15(d) requires that it do so. See footnote 161 above.

[163] See letters from ABA; CII; USPE.

[164] See letter from USPE.

register a class of securities under Exchange Act Section 12.[165]

We agree with the commenters that Rule 14a-11 generally should apply to those companies that choose to avail themselves of the obligations and benefits of Section 12(g) registration. As Section 12 registrants, these companies are subject to the full panoply of the Exchange Act, including Section 14(a), and their shareholders receive proxy materials in connection with annual and special meetings of shareholders in accordance with the proxy rules. We believe disparate treatment among these Section 12 registrants is unwarranted and shareholders of these companies should enjoy the same protections generally available to shareholders of other companies with a class of equity securities registered pursuant to Section 12. Accordingly, Rule 14a-11 will apply to companies that have voluntarily registered a class of equity securities pursuant to Exchange Act Section 12(g), with the same ownership eligibility thresholds as those of companies that were required to register a class of equity securities pursuant to Section 12.

f. Smaller reporting companies

Under the Proposal, Rule 14a-11 would apply to all companies subject to the proxy rules, other than companies that are subject to the proxy rules solely because they have a class of debt registered under Exchange Act Section 12. Thus, Rule 14a-11, as proposed, would apply to smaller reporting companies. We sought comment in the Proposal on what effect, if any, the application of Rule 14a-11 would have on any particular group of companies, and in particular, smaller reporting companies.[166]

---

165 See letter from ABA.

166 The Commission has considered this issue on prior occasions. See, e.g., 2003 Proposal; Division of Corporation Finance, Briefing Paper for Roundtable Discussion on the Proposed Security Holder Director Nominations Rules, February 25, 2004, available at http://www.sec.gov/spotlight/dir-nominations/dir-nom-briefing.htm.

A number of commenters stated generally that Rule 14a-11 should not apply to small businesses.[167] One commenter argued that Rule 14a-11 should be limited to accelerated filers and that there should possibly be a transition period where the rule was only applicable to large accelerated filers.[168] That commenter believed that smaller companies would have trouble recruiting directors because the pool of qualified directors is already small for smaller companies, and directors would not want to risk the exposure to a proxy contest. Another commenter argued that we should implement Rule 14a-11 on a pilot basis for large accelerated filers for two years and then revisit whether application of the rule would be appropriate for smaller companies.[169]

Other commenters stated that smaller reporting companies should not be excluded from the application of Rule 14a-11.[170] One commenter agreed with the Commission that exempting

---

167 See letters from ABA; American Mailing; All Cast; Always N Bloom; American Carpets; J. Arquilla; B. Armburst; Artistic Land Designs; C. Atkins; Book Celler; K. Bostwick; Brighter Day Painting; Colletti; Commercial Concepts; Complete Home Inspection; D. Courtney; S. Crawford; Crespin; Don's; T. Ebreo; M. Eng; eWareness; Evans; Fluharty; Flutterby; Fortuna Italian Restaurant; Future Form; Glaspell; C. Gregory; Healthcare Practice; B. Henderson; S. Henning; J. Herren; A. Iriarte; J. Jones; Juz Kidz; Kernan; LMS Wine; T. Luna; Mansfield Children's Center; D. McDonald; Meister; Merchants Terminal; Middendorf; Mingo; Moore Brothers; Mouton; D. Mozack; Ms. Dee; G. Napolitano; NK; H. Olson; PESC; Pioneer Heating & Air Conditioning; RC; RTW; D. Sapp; SBB; SGIA; P. Sicilia; Slycers Sandwich Shop; Southern Services; Steele Group; Sylvron; Theragenics; E. Tremaine; Wagner; Wagner Industries; Wellness; West End; Y.M.; J. Young.

168 See letter from ABA. A large accelerated filer is an issuer that, as of the end of its fiscal year, had an aggregate worldwide market value of voting and non-voting common equity held by its non-affiliates of $700 million or more, as of the last business day of the issuer's most recently completed second fiscal quarter; has been subject to the reporting requirements of Section 13(a) or 15(d) of the Exchange Act for at least 12 calendar months; has filed at least one annual report pursuant to Section 13(a) or 15(d) of the Act; and is not eligible to use the requirements for smaller reporting companies for its annual and quarterly reports. See Exchange Act Rule 12b-2(2).

169 See letter from Theragenics. See also letter from Alston & Bird, recommending that we consider adopting a phase-in approach, whereby companies would be permitted to follow a phase-in schedule for mandatory compliance based on their size, similar to the Commission's rules regarding internal controls reporting and XBRL. See Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, Release No. 33-8238; 34-47968 [69 FR 9722] (June 5, 2003) and Interactive Data to Improve Financial Reporting, Release No. 33-9002; 34-59324 [74 FR 6776] (Jan. 30, 2009).

170 See letters from AFSCME; CII; D. Nappier.

small entities would be inconsistent with the stated goals of the Proposal and the costs and burden for such entities would be minimal.[171] Other commenters believed that small companies are "just as likely" to have poorly functioning boards as their larger counterparts.[172] Another commenter argued that Rule 14a-11 would not impose a material burden on any company subject to the proxy rules because companies already have to distribute proxy cards and it would not be an imposition if they were required to add additional nominees to those cards.[173]

In the recently enacted Dodd-Frank Act, Congress confirmed our authority to require inclusion of shareholder nominees for director in company proxy materials.[174] In addition, in Section 971(c) of the Dodd-Frank Act Congress specifically provided the Commission with the authority to exempt an issuer or class of issuers from requirements adopted for the inclusion of shareholder director nominations in company proxy materials. In doing so, this provision instructs the Commission to take into account whether such requirement for the inclusion of shareholder nominees for director in company proxy materials disproportionately burdens small issuers.[175]

---

171 See letter from CII.

172 See letters from AFSCME; D. Nappier.

173 See letter from USPE.

174 Dodd-Frank Act §§ 971(a) and (b).

175 Dodd-Frank Act § 971(c). A comment letter on July 28, 2010 from the Society of Corporate Secretaries & Governance Professionals invoked this new legislation in support of a request to re-open the period for comment on the Proposal as it relates to small companies. As noted, we did specifically request comment in the Proposal on the rule's effect on smaller reporting companies, and we received and have considered numerous comments on this topic. Accordingly, we believe we have substantially achieved the objective stated in that letter, namely to identify and evaluate any "unique and significant challenges that access to the proxy will create for small and mid-sized companies." Moreover, our determination to delay implementation of Rule 14a-11 in respect of smaller companies will further allow us to evaluate the implementation of Rule 14a-11 by larger companies and provide us with the additional opportunity to consider whether adjustments to the rule would be appropriate for smaller reporting companies.

After considering the comments, amended Section 14(a), and Section 971(c) of the Dodd-Frank Act, we continue to believe that Rule 14a-11 should apply regardless of company size, as was proposed. As noted above, the purpose of Rule 14a-11 is to facilitate the exercise of shareholders' traditional state law rights to nominate and elect directors to company boards of directors and thereby enable shareholders to participate more meaningfully in the nomination and election of directors at the companies in which they invest. We are not persuaded that exempting smaller reporting companies would be consistent with these goals. As stated above, we expect the rule changes will further investor protection by facilitating shareholder rights to nominate and elect directors and providing shareholders a greater voice in the governance of the companies in which they invest. We believe shareholders of smaller reporting companies should be afforded these same protections.

Nonetheless, we recognize that smaller reporting companies may have had less experience with existing forms of shareholder involvement in the proxy process (e.g., Rule 14a-8 proposals), and thus may have less developed infrastructures for managing these matters. We believe that a delayed effective date for smaller reporting companies should allow those companies to observe how the rule operates for other companies and should allow them to better prepare for implementation of the rules. We also believe that delayed implementation for these companies will allow us to evaluate the implementation of Rule 14a-11 by larger companies and provide us with the additional opportunity to consider whether adjustments to the rule would be appropriate for smaller reporting companies before the rule becomes applicable to them. Therefore, we are delaying implementation for companies that meet the definition of smaller reporting company in Exchange Act Rule 12b-2.[176] New Rule 14a-11 will become effective for

176 See Exchange Act Rule 12b-2. A smaller reporting company is defined as "an issuer that is not an investment company, an asset-backed issuer, or a majority-owned subsidiary of a parent that is not a

these companies three years after the date that the rules become effective for companies other than smaller reporting companies. In addition, as discussed below, in an effort to limit the cost and burden on all companies subject to the rule, including smaller reporting companies, we have limited use of Rule 14a-11 to nominations by shareholders who have maintained significant continuous holdings in the company for an extended period of time. As discussed further below, we have extended the required holding period to at least three years at the time the notice of nomination is filed with the Commission and transmitted to the company. In addition, we have made modifications to the ownership threshold that, in combination with the three-year holding period, we believe should facilitate shareholders' ability to exercise their state law rights to nominate and elect directors without unduly burdening companies, including smaller reporting companies. We proposed a tiered ownership threshold that included a 5% ownership threshold for non-accelerated filers; however, we are adopting a 3% ownership threshold for all companies subject to the rule. In adopting the uniform 3% ownership threshold, we carefully considered, among other factors, the potential that the rule would have a disproportionate impact on small issuers. Despite identifying that concern in the Proposal, however, the comments we received did not substantiate that concern, and comments from companies overwhelmingly supported uniform ownership thresholds for all public companies. Moreover, the data we examined did not

smaller reporting company and that: had a public float of less than $75 million as of the last business day of its most recently completed second fiscal quarter, computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity; or in the case of an initial registration statement under the Securities Act or Exchange Act for shares of its common equity, had a public float of less than $75 million as of a date within 30 days of the date of the filing of the registration statement, computed by multiplying the aggregate worldwide number of such shares held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of such shares included in the registration statement by the estimated public offering price of the shares; or in the case of an issuer whose public float as calculated under paragraph (1) or (2) of this definition was zero, had annual revenues of less than $50 million during the most recently completed fiscal year for which audited financial statements are available." Whether or not an issuer is a smaller reporting company is determined on an annual basis.

indicate any substantial difference in share ownership concentrations between large accelerated filers and non-accelerated filers. Thus, we expect that the eligibility requirements will help achieve the stated objectives of the rule without disproportionately burdening any particular group of companies.

4. Who Can Use Exchange Act Rule 14a-11

a. General

In an effort to facilitate fair corporate suffrage, we could have proposed and adopted a rule pursuant to which the ability to use Rule 14a-11 would be conditioned solely on whether the shareholder lawfully could nominate a director, and not include any ownership thresholds or holding period. However, we believe it is appropriate to take a measured approach that balances competing interests and seeks to ensure investor protection. Accordingly, Rule 14a-11 will be available to shareholders that hold a significant, long-term interest in the company, have provided timely notice of their intent to include a nominee in the company's proxy materials, and provide specified disclosure concerning themselves and their nominees. More specifically, as described in detail in this section, a company will be required to include a shareholder nominee or nominees if the nominating shareholder or group:[177]

- Holds, as of the date of the shareholder notice on Schedule 14N,[178] either individually

[177] In some circumstances, the requirements of Rule 14a-11 applicable to a nominating shareholder group must be satisfied by each member of the group individually (e.g., no member of the group may be holding the company's securities with the purpose of, or with the effect, of changing control of the company or to gain more than the maximum number of nominees that the registrant would be required to include under the rule). See also Section II.B.4.

[178] Throughout this release, when we say "as of the date of the notice on Schedule 14N" we mean the date the nominating shareholder or group files the Schedule 14N with the Commission and transmits the notice to the company. See Section II.B.8.c.ii. below for a further discussion of the timing requirements for filing a Schedule 14N.

or in the aggregate,[179] at least 3% of the voting power (calculated as required under the rule)[180] of the company's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) or on a written consent in lieu of a meeting;[181]

- Has held the qualifying amount of securities used to satisfy the minimum ownership threshold continuously for at least three years as of the date of the shareholder notice on Schedule 14N (in the case of a shareholder group, each member of the group must have held the amount of securities that are used to satisfy the ownership threshold continuously for at least three years as of the date of the shareholder notice on Schedule 14N);[182]

---

179 The manner in which a nominating shareholder or group would establish its eligibility to use new Rule 14a-11 is discussed further in Section II.B.4.b.iv. below.

180 See Instruction 3 to new Rule 14a-11(b)(1).

181 See new Rule 14a-11(b)(1).

182 See new Rule 14a-11(b)(2). The three-year holding period requirement applies only to the amount of securities that are used for purposes of determining the ownership threshold.

- Continues to hold the required amount of securities used to satisfy the ownership threshold through the date of the shareholder meeting;[183]
- Is not holding any of the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11;[184]
- Does not have an agreement with the company regarding the nomination;[185]
- Provides a notice to the company on Schedule 14N, and files the notice with the Commission,[186] of the nominating shareholder's or group's intent to require that the company include that nominating shareholder's or group's nominee in the company's proxy materials no earlier than 150 calendar days, and no later than 120 calendar days, before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting;[187] and

183 See new Rule 14a-11(b)(2).

184 See new Rule 14a-11(b)(6).

185 See new Rule 14a-11(b)(7).

186 See Section II.B.8. for a discussion of new Schedule 14N and the disclosures required to be filed. The Schedule 14N may be filed by an individual shareholder that meets the ownership threshold, an individual shareholder that is a member of a nominating shareholder group that is aggregating the individual members' securities to meet the ownership threshold but is choosing to file the notice on Schedule 14N individually, or a nominating shareholder group through their authorized representative, as provided for in Rule 14n-1(b)(1).

187 The dates would be calculated by determining the release date disclosed in the previous year's proxy statement, increasing the year by one, and counting back 150 calendar days and 120 calendar days for the beginning and end of the window period, respectively. In this regard, we note that the deadline could fall on a Saturday, Sunday or holiday. In such cases, the deadline should be treated as the first business day following the Saturday, Sunday or holiday, similar to the treatment filing deadlines receive under Exchange Act Rule 0-3. See Instruction 1 to Rule 14a-11(b)(10). If the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 days from the prior year, then the nominating shareholder or group must provide notice pursuant to new Item 5.08 a reasonable time before the company mails its proxy materials, as specified by the company in a Form 8-K filed within four business days after the company determines the anticipated meeting date. See new Rule 14a-11(b)(10) and

- Includes the certifications required in the shareholder notice on Schedule 14N.[188]

b. Ownership threshold

As proposed, a nominating shareholder or group would have been required to beneficially own 1%, 3%, or 5% of the company's securities entitled to be voted on the election of directors at the shareholder meeting, depending on the company's accelerated filer status or, in the case of registered investment companies, depending on the net assets of the company. We received significant comment on this topic, which we discuss further below, and have made alterations to the final rule to reflect the concerns expressed by commenters.

As adopted, to rely on Rule 14a-11, a nominating shareholder or group will be required to hold, as of the date of the shareholder notice on Schedule 14N, either individually or in the aggregate, at least 3% of the voting power of the company's securities that are entitled to be voted on the election of directors at the annual (or a special meeting in lieu of the annual) meeting of shareholders or on a written consent in lieu of a meeting. The nominating shareholder or group or member of a nominating shareholder group will be required to hold both the power to dispose of and the power to vote the securities, as discussed below. The nominating shareholder or member of a nominating shareholder group also will be required to have held the qualifying amount of securities for at least three years as of the date of the notice on Schedule 14N, and to hold that amount through the date of the election of directors. Each aspect of the ownership requirement is discussed further below.

Instruction 2 to that paragraph. See further discussion in Section II.B.8.c.ii.

188 See new Rule 14a-11(b)(11) and Item 8 of new Schedule 14N. Pursuant to new Schedule 14N, the nominating shareholder or group would be required to include in its notice to the company a certification that the nominating shareholder or group satisfies the requirements in Rule 14a-11.

i. Percentage of securities

We proposed tiered ownership thresholds for large accelerated, accelerated, and non-accelerated filers in an effort to address the possibility that certain companies could be affected disproportionately based on their size.[189] Many commenters criticized the proposed ownership thresholds or recommended generally higher thresholds.[190] Of these, most commenters criticized the tiered ownership thresholds and recommended a uniform ownership threshold generally higher than the proposed thresholds.[191] Many of these commenters questioned whether the data on shareholdings discussed in the Proposal in relation to the proposed thresholds took into

---

189 Similarly, we proposed tiered ownership thresholds for registered investment companies with the tiers based on net assets.

190 See letters from 26 Corporate Secretaries; ABA; Australian Council of Superannuation Investors ("ACSI"); ADP; Advance Auto Parts; Aetna; Alaska Air; Alcoa Inc. ("Alcoa"); Allstate; American Express; Anadarko; Applied Materials; Association of Corporate Counsel; AT&T; Avis Budget; Barclays; Best Buy; J. Blanchard; Boeing; BorgWarner; BRT; Burlington Northern; R. Burt; Calvert Group; Ltd. ("Calvert"); Caterpillar; CFA Institute; Chevron; J. Chico; Committee on Investment of Employee Benefit Assets ("CIEBA"); CIGNA; Peter Clapman ("P. Clapman"); Cleary; CNH Global; Comcast; Con Edison; Capital Research and Management Company ("CRMC"); CSX; Cummins; Darden Restaurants; Davis Polk; Deere; Dewey; W. Brinkley Dickerson, Jr. ("W. B. Dickerson"); J. Dillon; DTE Energy; DuPont; Craig Dwight ("C. Dwight"); Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; eWareness; ExxonMobil; FedEx; Financial Services Roundtable; FMC Corp.; FPL Group; GE; General Mills; A. Goolsby; Home Depot; Honeywell; IBM; ICI; Intel; ITT; JPMorgan Chase; J. Kilts; Koppers; E.J. Kullman; N. Lautenbach; Leggett; Lionbridge Technologies, Inc. ("Lionbridge Technologies"); Lorsch et al.; M. Metz; McDonald's; MeadWestvaco; J. Miller; Motorola; Norfolk Southern; Northrop Grumman Corporation ("Northrop"); Office Depot; PepsiCo; Pfizer; P&G; Praxair, Inc. ("Praxair"); Protective; Stephen Lange Ranzini ("S. Ranzini"); Rosen; Ryder; Sara Lee; S&C; Seven Law Firms; Shearman & Sterling; Sherwin-Williams; SIFMA; Society of Corporate Secretaries; Southern Company; Tenet; Tesoro; Textron; TI; TIAA-CREF; Tidewater Inc. ("Tidewater"); Tompkins Financial Corporation ("Tompkins"); G. Tooker; T. Rowe Price; tw telecom; L. Tyson; UnitedHealth; U.S. Bancorp; ValueAct Capital; Vanguard; Verizon Communications Inc. ("Verizon"); Bruno de la Villarmois ("B. Villarmois"); Wachtell; Wells Fargo; Weyerhaeuser; Xerox.

191 See letters from ACSI; ADP; Advance Auto Parts; Allstate; American Express; Applied Materials; Association of Corporate Counsel; AT&T; Avis Budget; Barclays; Best Buy; J. Blanchard; Boeing; BRT; Burlington Northern; R. Burt; Calvert; Caterpillar; CFA Institute; J. Chico; CIGNA; CNH Global; Comcast; Con Edison; CSX; Darden Restaurants; Davis Polk; Deere; Dewey; W. B. Dickerson; J. Dillon; DTE Energy; DuPont; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; ExxonMobil; FedEx; Financial Services Roundtable; FMC Corp.; FPL Group; General Mills; Home Depot; IBM; Intel; ITT; JPMorgan Chase; J. Kilts; E.J. Kullman; Lorsch et al.; McDonald's; M. Metz; Motorola; N. Lautenbach; Office Depot; PepsiCo; Praxair; Protective; S. Ranzini; Sara Lee; S&C; Seven Law Firms; Shearman & Sterling; Sherwin-Williams; Society of Corporate Secretaries; Southern Company; Tesoro; Textron; TI; TIAA-CREF; Tompkins; G. Tooker; T. Rowe Price; tw telecom; L. Tyson; UnitedHealth; U.S. Bancorp; ValueAct Capital; Vanguard; Verizon; Weyerhaeuser; Xerox.

account the fact that shareholders could aggregate their holdings in order to use Rule 14a-11.[192] One of these commenters described formation of a nominating group as "the most likely scenario" to qualify for use of Rule 14a-11,[193] and another commenter submitted that with a significant ownership threshold an "inability to aggregate shareholders to reach the ownership threshold is unreasonable."[194]

A few commenters criticized generally the proposed thresholds as too high and recommended lower thresholds.[195] One commenter opposed the tiered ownership thresholds because a number of companies regularly move from one category of filer to another as the aggregate worldwide market value of their voting and non-voting common equity changes from fiscal year to fiscal year, which the commenter believed would lead to uncertainty under the Commission's tiered approach.[196] Commenters from the investment company industry noted that the proposed eligibility thresholds were based on data for non-investment companies and were not supported by empirical data analysis for investment companies.[197]

On the other hand, we also received comment generally supporting the proposed tiered ownership thresholds.[198] One commenter expressed general support for the proposed thresholds

---

192 See letters from ABA; ABA II; BRT; Business Roundtable (January 19, 2010) ("BRT II"); Cleary; Davis Polk; Honeywell; SIFMA.

193 Letter from BRT II.

194 Letter from California State Teachers' Retirement System (Nov. 18, 2009)("CalSTRS II").

195 See letters from Committee of Concerned Shareholders ("Concerned Shareholders"); L. Dallas; USPE.

196 See letter from Shearman & Sterling.

197 See, e.g., letters from ICI; S&C; T. Rowe Price.

198 See letters from AFL-CIO; AFSCME; British Insurers; CalPERS; CalSTRS; COPERA; CRMC; Florida State Board of Administration; Glass Lewis; IAM; ICGN; LACERA; Marco Consulting; D. Nappier; Nathan Cummings Foundation; P. Neuhauser; Norges Bank; OPERS; Pax World; RiskMetrics; David E. Romine ("D. Romine"); Shamrock; Sodali; Teamsters; WSIB.

and stated that the proposed thresholds would achieve the Commission's and commenter's shared objective of facilitating the exercise of shareholders' nomination rights.[199] Another commenter explained that the thresholds would "ensure[] that only those long-term shareholders who are seriously concerned about the governance of portfolio companies will have a seat at the table."[200]

With regard to an appropriate uniform ownership threshold, commenters recommended a number of different possibilities, including:

- at least 1% of the company's outstanding shares for an individual shareholder and 5% for a group of shareholders;[201]
- at least 2% of a company's voting securities;[202]
- 3% of a company's shares;[203]
- 5% of the company's voting securities for an individual shareholder and 10% for a group of shareholders;[204]

---

199 See letter from CII.

200 Letter from AFL-CIO.

201 See letter from Deere.

202 See letter from ADP.

203 See letters from CSI; Calvert; CFA Institute; Labour Union Co-operative Retirement Fund ("LUCRF"); S. Ranzini.

204 See letters from Advance Auto Parts; Alaska Air; American Express; Association of Corporate Counsel; Avis Budget; Best Buy; J. Blanchard; Boeing; BRT; Burlington Northern; Callaway; CIGNA; CNH Global; Comcast; Con Edison; Darden Restaurants; Dewey; J. Dillon; DTE Energy; DuPont; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; ExxonMobil; FedEx; FMC Corp.; FPL Group; General Mills; Home Depot; Intel Corporation ("Intel"); JPMorgan Chase; E.J. Kullman; McDonald's; N. Lautenbach; PepsiCo; Praxair; Protective (recommending this threshold if its proposed 35% withhold vote triggering event is not included; if included, it recommended a 3% threshold); Sara Lee; Seven Law Firms; Sherwin-Williams; Society of Corporate Secretaries; Textron; Tompkins; G. Tooker; Weyerhaeuser; Xerox.

- 5% of a company's outstanding shares;[205]
- 5% of a company's outstanding shares for an individual shareholder and a higher but unspecified threshold for a group of shareholders;[206]
- with regard to investment companies, a 5% threshold;[207]
- from 5% to 10% of a company's shares;[208]
- 10% of the company's shares;[209]
- 10% of the company's outstanding shares for an individual shareholder and 15% of the outstanding shares for a group of shareholders;[210]
- 5% to 15% of the company's outstanding shares;[211]
- 15% of the company's shares;[212] and
- 20% of a company's shares.[213]

Two of the commenters that criticized the proposed threshold as too high recommended that Rule 14a-11 have the same ownership threshold as Rule 14a-8,[214] with one of these

---

205 See letters from Applied Materials; R. Burt; CSX; Financial Services Roundtable; IBM (recommending 5% as one of the two acceptable thresholds); ITT; J. Kilts; Shearman & Sterling; Southern Company; Tesoro; TIAA-CREF; T. Rowe Price; tw telecom; UnitedHealth; U.S. Bancorp; Verizon.

206 See letters from Applied Materials; U.S. Bancorp.

207 See letters from S&C; TIAA-CREF.

208 See letters from Davis Polk; Lorsch et al.

209 See letters from Allstate; Caterpillar; J. Chico; W. B. Dickerson; IBM (recommending 10% as one of the two acceptable thresholds); ICI; M. Metz; Office Depot; L. Tyson; ValueAct Capital; Vanguard.

210 See letter from Motorola.

211 See letter from Barclays.

212 See letter from TI.

213 See letter from AT&T.

214 See letters from Concerned Shareholders; USPE.

commenters expressing the belief that the proposal, with its ownership thresholds, would enable only institutional shareholders to access the corporate ballot.[215] Another of the commenters opposing the proposed thresholds asserted that the threshold for non-accelerated filers is too high and cited figures indicating that a significant number of such filers do not have any shareholders that would satisfy the proposed threshold.[216] This commenter suggested that for an individual shareholder or a group of shareholders, the threshold should be based on the dollar value of the shares held (e.g., $250,000) or a lower percentage of shares (e.g., 0.25%).

After considering the comments, we believe that it is appropriate to apply a uniform 3% ownership threshold to all companies subject to the rule, regardless of whether they are classified as large accelerated, accelerated, or non-accelerated filers under the federal securities laws. As an initial matter, as we did at the time we issued the Proposing Release, we considered whether and why Rule 14a-11 should include any ownership threshold. Because the Commission's proxy rules seek to enable the corporate proxy process to function, as nearly as possible, as a replacement for in-person participation at a meeting of shareholders, some may argue that once a shareholder has satisfied any procedural requirements to a director nomination that a company is allowed to impose under state law, then that nomination should be included in the company's proxy materials. Each time we consider and adopt amendments to our rules, however, we balance competing interests.

Based on our consideration of these competing interests, including balancing and facilitating shareholders' ability to participate more fully in the nomination and election process against the potential cost and disruption of the amendments, we have determined that requiring a

---

215 See letter from Concerned Shareholders.

216 See letter from L. Dallas.

significant ownership threshold is appropriate to use Rule 14a-11. Indeed, we believe that the 3% ownership threshold – combined with the other requirements of the rule – properly addresses the potential practical difficulties of requiring inclusion of shareholder director nominations in a company's proxy materials, and some concerns that both company management and other shareholders may have about the application of Rule 14a-11. Providing this balanced, practical, and measured limitation in Rule 14a-11 is consistent with the approach we have taken in many of our other proxy rules[217] and reflects our desire to proceed cautiously with these new amendments to our rules.

We also considered whether the ownership threshold we adopt for Rule 14a-11 should be tiered based on the size and related filing status (or net assets) of the company, or uniform for all companies, and what percentage of ownership would be most appropriate. We have decided to adopt a uniform standard for all companies for several reasons. First, we determined that a uniform standard would reduce the complexities of Rule 14a-11. As noted by one commenter,[218] the potential for the filing status of a company to change would result in uncertainty about the availability of the provisions of Rule 14a-11 as a result of market fluctuations in share prices, acquisitions, or divestitures. A uniform standard avoids that uncertainty and the resulting potential for the costs and burdens of disputes over the selection of the appropriate tier. Elimination of that uncertainty, moreover, would make the availability of Rule 14a-11 more predictable and therefore more useful for shareholders in planning nominations in reliance on the

217 See, e.g., Exchange Act Rule 14a-8(b) (requiring shareholders to have "continuously held at least $2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting for at least one year by the date" they submit a shareholder proposal); Exchange Act Rule 14a-6(g) (requiring a soliciting person that "owns beneficially securities of the class which is the subject of the solicitation with a market value of over $5 million" to file a notice with the Commission); Regulation S-K, Item 404(a) (requiring disclosure of transactions with related parties that exceed $120,000).

218 See letter from Shearman & Sterling.

rule. A uniform standard also will avoid any ability on the part of management to structure corporate actions to modify the impact of Rule 14a-11 by placing the company in a different tier. The concern we expressed in the Proposal – that companies could be disproportionately affected by adoption of the rule based on their size – was not supported by comments of potentially affected companies; to the contrary, comments from companies overwhelmingly supported uniform ownership thresholds.[219] In addition, as discussed below, we are deferring implementation of Rule 14a-11 for smaller reporting companies.[220]

A comparison of the share ownership concentrations in large accelerated filers and non-accelerated filers produced relatively minor observable difference. The results, adjusted to give effect to a three-year holding period requirement, are summarized in the table below:[221]

---

219 See letters from General Mills; Tesoro; T. Rowe Price; ValueAct Capital; Verizon (explicitly opposing variation in percentage ownership requirement based on issuer size); and letters identified in footnotes 199-211 above (commenters supporting various uniform ownership thresholds).

220 As noted in Section II.B.3.f., we have adopted a three-year delay in implementation for smaller reporting companies.

221 The percentages in the table are derived from the data set described in the Proposing Release involving companies that have held meetings between January 1, 2008 and April 15, 2009 (the "Proposing Release data"). See Section III.B.3. of the Proposing Release. The percentages have been adjusted, however, because the Proposing Release data did not give effect to any holding period requirement, and we have attempted to estimate what those percentages would have been had they given effect to the three-year holding period we are adopting. By the calculation described below, we have estimated a reasonable adjustment to the reported percentages in the Proposing Release data by using the data presented in a November 24, 2009 memorandum based on the analysis of Schedule 13F filings, data which did give effect to holding period requirements. See Memorandum from the Division of Risk, Strategy, and Financial Innovation regarding the Share Ownership and Holding Period Patterns in 13F data (November 24, 2009), available at http://www.sec.gov/comments/s7-10-09/s71009-576.pdf (the "November 2009 Memorandum"). The two data sets have overlapping statistics that can be used for comparison and adjustment: both sets report percentages of a broad sample of public companies and identify percentages of companies having (i) at least one shareholder with holdings of 3% of more, (ii) at least two shareholders with holdings of 3% or more, (iii) at least one shareholder with holdings of 1% or more, and (iv) at least two shareholders with holdings of 1% or more. Comparing the percentages reflected in the November 2009 Memorandum (giving effect to a three-year holding period requirement) with the percentages in the Proposing Release data (not reflecting any holding period requirement), we observe that the percentages reported in the Proposing Release data exceed the percentages reported in the November 2009 memorandum by amounts ranging from 56% to 69%. In order to derive the approximate percentages in the table, we adjusted downward by 62.5% the percentages reported in the Proposing Release data, to account at least approximately for the application of the three-year holding period requirement.

	Non-Accelerated Filers (approximate percentages)	Large Accelerated Filers (approximate percentages)
Companies with at least one 1% shareholder	37%	37%
Companies with at least one 3% shareholder	33%	32%
Companies with at least one 5% shareholder	22%	16%
Companies with at least two 1% shareholders	36%	37%
Companies with at least two 1.5% shareholders	33%	33%
Companies with at least two 2.5% shareholders	27%	25%

Our further review of relevant data has persuaded us that applying different ownership thresholds to large accelerated filers and non-accelerated filers is not justified.[222]

As noted above, we have decided to adopt a uniform ownership threshold for all categories of public companies. We determined that a 3% ownership threshold is an appropriate standard for all such companies – not just accelerated filers. We believe that the 3% threshold, while higher for many companies and lower for others than the thresholds advanced in the Proposal, properly balances our belief that Rule 14a-11 should facilitate shareholders' traditional state law rights to nominate and elect directors with the potential costs and impact of the amendments on companies. The ownership threshold we are establishing should not expose issuers to excessively frequent and costly election contests conducted through use of Rule 14a-11, but it is also not so high as to make use of the rule unduly inaccessible as a practical matter.

We selected the uniform 3% threshold based upon comments received, our analysis of the data available to us, and the fact that the rule allows for shareholders to form groups to aggregate their holdings to meet the threshold. We also considered that our amendments to Rule 14a-8

222 See letter from P. Neuhauser (suggesting only two ownership eligibility tiers because data show "almost no difference in ownership characteristics between smaller accelerated filers and non-accelerated filers.").

remove barriers to the ability of shareholders to have proposals included in company proxy materials to establish a procedure under a company's governing documents for the inclusion of one or more nominees in the company's proxy materials. Because of these amendments, shareholders who believe the 3% threshold is too high can take steps to seek to establish a lower ownership threshold.[223]

We note that we considered a lower threshold, such as 1%, and a higher threshold, such as 5%, both of which were thresholds in the proposed tiers. Quite a few commenters, including a number who generally supported the adoption of Rule 14a-11, advocated for an ownership threshold higher than the 1% level we proposed for large accelerated filers.[224] One large institutional investor, for example, "strongly urg[ed] the adoption of proposed Rule 14a-11" and argued that "existing reforms are incomplete as long as boards retain the exclusive control of the proxy card and sole discretion over the mechanisms that govern their own elections," but also stated the belief that "in order to use company resources to nominate a director, a significant amount of capital must be represented and 5% is an acceptable threshold."[225] Similarly, the manager of a large family of investment companies stated its "support [for] the Commission's intent to facilitate shareholders' rights to participate in the governance process," yet commented that "a 1% threshold is too low, in our opinion, to maintain the critical balance between serving the interests of eligible nominating shareholders and serving the interests of a company's

223 As noted in Section II.C., we are adopting an amendment to Rule 14a-8(i)(8) to preclude companies from relying on that basis to exclude from their proxy materials shareholder proposals that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. Such a shareholder proposal would, of course, have to satisfy the other requirements of the rule, like other Rule 14a-8 shareholder proposals.

224 See letters from ACSI (advocating a uniform 3% threshold); Calvert (same); LUCRF (same); S. Ranzini (same); TIAA-CREF (advocating a uniform 5% threshold); T. Rowe Price (same).

225 Letter from TIAA-CREF.

shareholder base at large."[226] That commenter recommended a "flat 5% threshold for all companies" because it "represents significant economic stake." Other commenters recommended a uniform 3% ownership threshold in the interest of avoiding "frivolous or vexatious nominations,"[227] or because it "is not so small that it would allow a board nomination for only a de minimis investment in [a non-accelerated filer]," but "would not be so large as to prevent all but the largest institutional shareowners to submit nominees for [large accelerated filers]."[228]

In light of such comments we have determined not to adopt the 1% threshold we had proposed with respect to large accelerated filers. We also have determined not to adopt, as the uniform standard, the 5% threshold we had proposed for non-accelerated filers. Several commenters from the investor community explicitly opposed a 5% uniform threshold, maintaining that it would as a practical matter exclude all but the largest institutional investors.[229] On the other hand, although some companies supported a uniform 5% threshold,[230] most other companies urged the adoption of a substantially higher threshold, either for individual shareholders or for shareholder groups, or both. For example, companies and their counsel generally believed a higher threshold should apply to group nominations and overwhelmingly recommended a 10% minimum ownership requirement for nominations by shareholder groups.[231]

226 Letter from T. Rowe Price.

227 Letters from SCSI and LUCRF.

228 Letter from CFA Institute.

229 See letters from CFA Institute; P. Neuhauser; RiskMetrics.

230 See letters from CSX; ITT; Southern Company; Tesoro; tw telecom; UnitedHealth; Verizon.

231 See letters from Advance Auto Parts; Alaska Air; American Express; Association of Corporate Counsel; Avis Budget; Best Buy; J. Blanchard; Boeing; BRT; Burlington Northern; Callaway; CIGNA; CNH Global; Comcast; Con Edison; Darden Restaurants; Dewey; J. Dillon; DTE Energy; DuPont; Eaton; Edison Electric Institute; Eli Lilly; Emerson Electric; ExxonMobil; FedEx; FMC Corp.; FPL Group; General

We note, however, that at a 10% threshold for groups, the likelihood of forming a group sufficient to meet the minimum ownership requirement would likely be significantly reduced compared to a 3% threshold. Given a three-year holding period, the data in the November 2009 Memorandum identify combinations totaling 10% or more but involving five or fewer shareholders as achievable in as little as 7% of public companies, compared to at least 21% of public companies at a 5% threshold and at least 31% of public companies at a 3% threshold. In addition, the data suggest that it would be even more unlikely that a company would have an individual shareholder that would meet a 10% ownership threshold.[232] While some commenters suggested a 5% threshold was appropriate because that amount is consistent with other filing requirements such as Schedule 13D and 13G,[233] we ultimately were not persuaded because the underlying principles of such filing requirements[234] are quite different from those underlying the ownership condition to Rule 14a-11. After considering the comments and available data, we have decided that a 3% ownership threshold – including where shareholders form groups to

---

Mills; Home Depot; Intel; JPMorgan Chase; E.J. Kullman; McDonald's; N. Lautenbach; PepsiCo; Praxair; Protective (recommending this threshold if its proposed 35% withhold vote triggering event is not included; if included, it recommended a 3% threshold); Sara Lee; Seven Law Firms; Sherwin-Williams; Society of Corporate Secretaries; Textron; Tompkins; G. Tooker; Weyerhaeuser; Xerox.

232 The data in the November 2009 Memorandum suggest that just 4% of companies would have at least one shareholder with 10%.

233 See, e.g., letters from CSX; ITT; Shearman & Sterling; Tesoro; T. Rowe Price; tw telecom.

234 See, e.g., Release No. 34-26598, Reporting of Beneficial Ownership in Publicly-Held Companies (March 6, 1989)("The beneficial ownership reporting requirements embodied in Sections 13(d) and 13(g) of the [Exchange Act] and the regulations adopted thereunder are intended to provide to investors and to the subject issuer information about accumulations of securities that may have the ability to change or influence control of the issuer."). See also Release No. 34-50699 (proposing to require disclosure of persons holding 5% of an ownership interest in a securities exchange because the principles underlying such disclosure were similar to those underlying other filing requirements: "The 5% reporting threshold and the information proposed to be required to be disclosed about such ownership is modeled on the beneficial ownership reporting requirements of the Williams Act, embodied in Sections 13(d) and 13(g) of the Exchange Act and the rules and regulations thereunder. These Exchange Act provisions are intended to provide information to the issuer and the marketplace about accumulations of securities that may have the potential to change or influence control of an issuer."(footnotes omitted)).

satisfy the threshold – is an appropriate and workable approach for the rule.

In adopting a uniform 3% threshold for all companies, as opposed to a lower ownership threshold for all companies, we are mindful that the rule will allow shareholders to form a group by aggregating their holdings to meet the ownership threshold.[235] Indeed, as we assumed in the Proposing Release and as some commenters told us, in many cases shareholders will need to form groups to meet the ownership threshold for the purpose of submitting director nominations pursuant to Rule 14a-11.[236] Commenters also pointed to instances of coordinated shareholder activity in recent "vote no" campaigns as support for the ability of shareholders to form groups.[237] We have adopted a number of amendments to our rules that will facilitate the formation of groups for this purpose.[238] We understand the result of our ownership threshold determination may be that shareholders will need to convince other shareholders to support their attempt to use Rule 14a-11. We believe this outcome reduces the potential for excessive costs to be incurred by companies and their shareholders.

The data available to us also suggest that reaching the 3% ownership threshold we are adopting is possible for a significant number of shareholders either individually or by a number of shareholders aggregating their holdings in order to satisfy the ownership requirement. In particular, the data presented in the November 2009 Memorandum indicate that a sizeable

---

235 Some commenters suggested that the data on share ownership dispersion referred to in the Proposing Release were insufficient because we did not focus on the possibility that shareholders could form groups to satisfy the minimum ownership requirement. See letters from American Bar Association (January 19, 2010) ("ABA III"); BRT II.

236 See letters from AFL-CIO ("[I]t will be necessary to permit aggregation of holdings to prevent the Proposed Access Rule from being usable only by hedge funds."); Florida Board of Administration ("Public funds would need to form a nominating group in order to meet the hurdle in nearly all cases.").

237 See letter from BRT II.

238 See, e.g., Rule 14a-2(b)(7).

percentage (33%) of public companies have at least one institutional investor owning at least 3% of their securities for at least three years, and thus potentially qualified to meet the Rule 14a-11 ownership threshold individually. As noted, however, the data are based on Form 13F filings, which include holders that are custodians and may not be likely users of the rule. The data in the November 2009 Memorandum also suggest that forming nominating shareholder groups with holdings aggregating 3% is achievable at many companies by a relatively small number of shareholders. Even factoring in the requirement of continuous ownership for three years, 31% of public companies have three or more holders with at least 1% share ownership each; and 29% have two or more holders with at least 2% share ownership each.[239] Moreover, neither of these categories includes companies with one holder of 2% and another holder of at least 1%, and none of these percentages includes companies having a relatively small number (e.g. four to ten) of holders whose aggregate holdings exceed 3% but whose individual holdings do not bring the company within any of the categories identified in the data.

We are concerned, however, that use of Rule 14a-11 may not be consistently and realistically viable, even by shareholder groups, if the uniform ownership threshold were set at 5% or higher. At the 5% minimum ownership requirement for individuals as advocated by many of those same commenters, only 20% of public companies had even one shareholder satisfying that requirement. Finally, even applying a 5% threshold for shareholder groups, the data identify combinations involving five or fewer shareholders that add up to 5% or more as theoretically achievable in as few as 21% of public companies – at least 25% fewer than with a 3% threshold.[240]

---

239 We note that it is unlikely that the ownership test used in calculating the data tracks the definition that we are adopting for Rule 14a-11. As a result, the percentages in the data may be over- or under-inclusive.

240 At the 10% threshold for groups urged by many commenters, for example, the likelihood of forming a

All of these data thus suggest that a uniform 5% ownership requirement would be substantially more difficult to satisfy than the 3% requirement we are adopting. Moreover, our resulting concern about the viability of a 5% ownership threshold is exacerbated by several limitations on the data reported in the November 2009 Memorandum. While those data do account for the application of a three-year holding period requirement, they may overstate in several ways the potential to meet the ownership threshold. First, they may include controlling shareholders that may be unlikely to rely on Rule 14a-11. Second, the data are based on filings on Form 13F, in which ownership is defined differently than under Rule 14a-11, and thus may yield a higher number of larger shareholdings. Finally, the data include large shareholdings by institutions which report aggregated holdings of securities held for multiple beneficial owners.[241]

Nevertheless, and principally because they give effect to holding period requirements, we considered the data in the November 2009 Memorandum to be the most pertinent to our selection of a uniform minimum ownership percentage. We received additional data relating to large companies, however, that offer some additional indication about the number of shareholders potentially available to form a group to meet the 3% ownership threshold. One study indicated that in the top 50 companies by market capitalization as of March 31, 2009, the five largest institutional investors held from 9.1% to 33.5% of the shares, and an average of 18.4% of the

---

group sufficient to meet the minimum ownership requirement would be more sharply constrained: the data in the November 2009 Memorandum identify combinations totaling 10% or more but involving five or fewer shareholders as theoretically achievable in as little as 7% of public companies.

241 On the other hand, the data in the November 2009 Memorandum may understate the number of large shareholdings, because the data may exclude smaller holdings in multiple institutions that are subject to common voting control, and in any event, do not include holdings of less than 1% at all, even though such holdings could contribute to the formation of a group eligible to use Rule 14a-11. Likewise, those data do not include securities held by institutions holding less than $100 million in securities because Exchange Act Section 13(f) does not require such institutions to report their holdings. See letters from ABA III; BRT II.

shares.[242] That same study found that among a sample of 50 large accelerated filers, the median number of shareholders holding at least 1% of the shares for at least one year was 10.5, with 45 of the 50 companies in the sample having at least seven such shareholders.[243] Another study that was reported to us[244] similarly suggests relatively high concentration of share ownership. According to that analysis of S&P 500 companies, 14 institutional investors could satisfy a 1% threshold at more than 100 companies, eight could meet that threshold at over 200 companies, five could meet it at over 300 companies, and three could meet it at 499 of the 500. Information from specific large issuers likewise suggests the achievability of shareholder groups aggregating 3%.[245]

We realize these data likely overstate the number of eligible shareholders or shareholders whose holdings could be grouped to meet the ownership threshold, as these data generally do not appear to reflect any continuous holding requirement.

In any event, our assessment of the percentage of companies with various share ownership concentrations cannot be taken as an assurance that shareholder nominating groups will or will not be formed at any particular combination of percentage ownership and holding

---

242 See "Report on Effects of Proposed SEC Rule 14a-11 on Efficiency, Competitiveness and Capital Formation, in Support of Comments by Business Roundtable" by NERA Economic Consulting ("NERA Report"), Appendix Table 1, submitted with the letter from BRT.

243 Id. at 13-14, Figure 2.

244 See letter from JPMorgan Chase.

245 See letters from AT&T (eight shareholders owning 1% or more, although holding periods not identified); AGL Resources (same); CIGNA (20 1%+ shareholders, although holding periods not identified); Cummins (36 1+% shareholders, although holding periods not identified); General Mills (one 5%+ shareholder holding for at least 6 years, over 12 1%+ shareholders, and over 25 0.5%+ shareholders, although holding periods not identified); ITT (14 1%+ shareholders, although holding periods not identified); McDonald's (10 holders owning 1% or more, one shareholder owning 5%, although holding periods not identified); UnitedHealth (four 3%+ shareholders, six 2%+ shareholders, nine 1%+ shareholders, 20 0.5%+ shareholders, 32 0.25% shareholders, applying a 2-year holding period); Weyerhaeuser (three 5%+ shareholders, 20 1%+ shareholders, although holding periods not identified).

period requirements or of the likelihood that persons with large securities holdings would be inclined or disinclined to use Rule 14a-11.[246] Taking all of this information into account, overall we believe that our selection of a 3% ownership threshold strikes an appropriate balance between the benefits of facilitating shareholder participation in the process of electing directors of public companies and the costs and disruption associated with contested elections of directors conducted pursuant to new Rule 14a-11. We also believe, and as noted, many commenters supported, that a threshold tied to a significant commitment to the company is an important feature of our amendments. Of course, to the extent that shareholders believe the 3% threshold is too high our amendments to Rule 14a-8 will facilitate their ability to adopt a lower ownership percentage.[247]

We proposed to apply the same thresholds for registered investment companies and business development companies as for non-investment companies, except that the applicability of the particular thresholds for registered investment companies would have depended on the net assets of the company, rather than the company's accelerated filer status. No commenters recommended a higher threshold for investment companies than for non-investment companies. While some commenters noted the absence of data specifically relating to the impact of various ownership thresholds on investment companies,[248] no commenter supplied any data suggesting the need for an ownership threshold for investment companies different from that applicable to

---

246 See letter from Council of Institutional Investors (January 14, 2010) ("CII II"). This comment refers to research indicating that in a small sample of accelerated and non-accelerated filers, the holdings of the ten largest public pension funds, if aggregated, would not exceed 5% and would also be unlikely to meet a 3% threshold, while a 1% threshold could be met. Apart from the sample size, however, this research itself appears limited in that it apparently does not include other types of shareholders and is not adjusted for any holding period.

247 See footnote 223 above.

248 See, e.g., letters from ICI; S&C; T. Rowe Price.

non-investment companies.[249] Although two commenters suggested a 5% ownership threshold for investment companies, both of these commenters also suggested a 5% threshold for non-investment companies.[250]

We believe that it is appropriate to apply to registered investment companies and business development companies the same 3% ownership threshold that we are applying to other companies. We also believe that, similar to non-investment companies, our selection of a 3% ownership threshold strikes an appropriate balance between the benefits of facilitating shareholder participation in the process of electing directors of investment companies and the costs and disruption associated with contested elections of directors conducted pursuant to Rule 14a-11.

We are not adopting the suggestion of commenters that the eligibility thresholds for investment companies be based on the holdings for the fund complex in the case of unitary boards or the cluster in the case of cluster boards.[251] We believe that eligibility should be based on holdings for the investment company, not the entire fund complex or cluster, because under

---

249 One joint comment letter provided data regarding the net assets of investment companies and the dollar value of the shares that would be necessary to meet the proposed 1%, 3%, or 5% thresholds. See letter from ICI/IDC. The data provided by the commenters suggest that there are a limited number of small investment companies with net assets ranging from $50,000 to $351,000, where the 3% threshold could be met by an investment ranging from $1,500 to $10,530. However, the data also indicate that the vast majority of funds are significantly larger, and would therefore require a significantly larger investment to meet the 3% threshold (e.g., 90% of long-term mutual funds, money market funds, and closed-end funds have total net assets greater than $19 million, $100 million, and $57 million, respectively; the median long-term mutual fund, money market fund, and closed-end fund have total net assets of $216 million, $844 million, and $216 million, respectively).

250 See letters from S&C (recommending "with respect to the ownership thresholds applicable to shareholders of [registered investment companies], a minimum percentage of no less than the 5% threshold recommended in the Seven Law Firm Letter" (to which Sullivan & Cromwell was a party and which recommended that ownership thresholds of non-investment companies be adjusted upwards to 5% for individual shareholders and higher for groups of shareholders)); TIAA-CREF (recommending "that the Commission adopt a 5% ownership requirement across the board regardless of the company's size" and "[w]ith respect to investment companies, … that the 5% requirement be applied at the fund complex level rather than at the individual fund level").

251 See letters from Barclays; T. Rowe Price; TIAA-CREF.

state law, shareholder voting is determined based on the holdings in the investment company. Fund complexes have flexibility to organize their funds into one or more investment companies. Thereafter, state law governs which shareholders vote as a group for directors. Because Rule 14a-11 is intended to facilitate the exercise of traditional state law rights to nominate and elect directors, we believe that the rule should follow state law.

ii. Voting power

We proposed that the ownership threshold be determined as a percentage of the securities entitled to be voted on the election of directors. Some commenters sought clarification of how the ownership threshold would be calculated where companies have multiple classes of stock with varying voting rights.[252] These commenters observed that the proposed rule did not adequately address voting regimes where the voting rights have been separated from the economic rights of ownership.[253] One commenter explained that in situations where ownership of securities does not correlate with voting power,[254] shares will have voting rights disproportionate to the number of shares held, and that creates a disparity between the two classes in terms of the economic value of a single vote.[255] One commenter advised that further clarification was needed for companies with two or more outstanding classes of voting securities with disparate voting rights, including those companies with classes of voting securities and non-voting securities, so that those companies would be treated in a manner consistent with

---

252 See letters from ABA; Duane Morris; Media General; P. Neuhauser; New York Times. These letters illustrated a scenario where one publicly-issued class of stock is entitled to one vote per share, while the privately-held controlling class of stock is entitled to 10 votes per share and both classes vote together on the election of directors.

253 See letters from ABA; P. Neuhauser; Duane Morris; Media General.

254 See, e.g., discussion in footnote 252 of common ten-to-one voting provisions of a structure with Class A and Class B securities.

255 See letter from ABA.

companies that have one class of voting securities.[256]

In proposing that the ownership threshold be determined as a percentage of securities entitled to be voted on the election of directors, our goal was to have the requirement tie to the percentage of votes that could be cast for the director nominees. In response to these commenters, we have revised the rule text to clarify that the ownership threshold will be determined as a percentage of voting power of the securities entitled to be voted on the election of directors at the meeting, rather than as a percentage of securities entitled to be voted on the election of directors, as was proposed. Accordingly, where a company has multiple classes of stock with unequal voting rights and the classes vote together on the election of directors, then voting power would be calculated based on the collective voting power.[257] If a company has multiple classes of stock that do not vote together in the election of all directors (where, for example, each class elects a subset of directors), then voting power would be determined only on the basis of the voting power of the class or classes of stock that would be voting together on the election of the person or persons sought to be nominated by the nominating shareholder or group, rather than the voting power of all classes of stock.[258] We believe this approach properly bases the availability of Rule 14a-11 on the right to vote for the nominees that may be included in the company's proxy materials, which is both consistent with the intent of the provisions of a company's governing documents and in accord with the principle that class directors are elected by the votes of the holders of the class.

256 See letter from Duane Morris.

257 See Rule 14a-11(b)(1) and Instruction 3 and the discussion below.

258 See Instruction 3 to Rule 14a-11(b)(1).

iii. Ownership position

In the Proposing Release, we solicited comment about whether beneficial ownership is the appropriate standard of ownership to use for purposes of the minimum ownership threshold in the rule or whether another standard would be more appropriate. In this regard, we requested comment about whether a net long requirement should be used and, if so, what other modifications would be required. We received a number of comments addressing the appropriate standard of ownership and supporting the inclusion of a net long requirement.[259] Commenters suggested that we adopt an "ultimate" beneficial owner definition that included, among other things, a requirement that the nominating shareholder or group hold the entire bundle of voting and economic rights to any securities used to determine eligibility under the rule.[260] At least one of these commenters thought the ownership definition should be adopted this way in order to remove the possibility that multiple parties may count the same securities toward their individual securities ownership totals.[261] Moreover, many commenters were concerned that without requiring net long ownership, shareholders could engage in hedging strategies to obtain the requisite amount of ownership while eliminating or reducing their economic exposure.[262] Some commenters expressed the view that shares loaned to a third party should be taken into account when determining whether the nominating shareholder or group satisfies the relevant

---

259 See letters from 26 Corporate Secretaries; Advance Auto Parts; Aetna; Alaska Air; Alcoa; Alston & Bird; American Express; BorgWarner; BRT; Burlington Northern; CSX; L. Dallas; Dewey; DuPont; FPL Group; Florida State Board of Administration; GE; Honeywell; ICI; JPMorgan Chase; Kirkland & Ellis LLP ("Kirkland & Ellis"); Leggett; P. Neuhauser; PepsiCo; Protective; Seven Law Firms; SIFMA: Society of Corporate Secretaries; T. Rowe Price; tw telecom; UnitedHealth; ValueAct Capital; Xerox.

260 See letters from BRT; Devon; IBM; P. Neuhauser; Society of Corporate Secretaries.

261 See letter from ABA.

262 See letters from 26 Corporate Secretaries; ABA; Advance Auto Parts; Alaska Air; Allstate; Applied Materials; Association of Corporate Counsel; AT&T; J. Blanchard; Biogen; BRT; CIEBA; Cleary; Devon; Dewey; Headwaters; IBM; JPMorgan Chase; PepsiCo; Sara Lee; Seven Law Firms; Shearman & Sterling; Sidley Austin; Society of Corporate Secretaries; Verizon.

ownership threshold.[263] Commenters explained that institutional investors who hold shares for the long-term may lend their shares to others periodically while retaining the right to recall those shares to cast votes.[264] Commenters suggested several conditions for counting these shares: the shareholder has a legal right to recall the shares and cast votes;[265] the shareholder discloses in the Schedule 14N an intention to vote the shares;[266] the shareholder holds the shares through the date of the meeting;[267] and the shares are held past the date of the election.[268]

After considering the comments, we have modified in several respects the ownership requirement of Rule 14a-11 so that it is consistent with our intent to limit use of Rule 14a-11 to long-term shareholders with significant ownership interests. First, in order to satisfy the ownership requirement, the nominating shareholder or member of the nominating shareholder group must hold a class of securities subject to the proxy solicitation rules.[269] Limiting Rule 14a-11 nominations to holders of securities that are subject to the proxy rules appropriately excludes from the calculation private classes of voting securities held by persons that would have no expectation that our proxy rules would be available to facilitate their state law nomination rights. Further, if we included securities not covered by the proxy rules in the calculation, those securities could dilute the relative holdings of shareholders holding securities that our rules are

---

263 See letters from AFL-CIO; CalPERS; CII; COPERA; IAM, LIUNA; Marco Consulting; P. Neuhauser; D. Nappier; Sheet Metal Workers National Pension Fund ("Sheet Metal Workers"); SWIB.

264 See letters from AFL-CIO; Marco Consulting; Sheet Metal Workers; SWIB.

265 See letters from CalPERS; CII; COPERA; IAM; LIUNA; D. Nappier.

266 See letters from AFL-CIO; CalPERS; CII; IAM; D. Nappier.

267 See letters from CalPERS; CII; IAM; D. Nappier.

268 See letters from COPERA.

269 This would include securities registered pursuant to Section 12 of the Exchange Act or subject to Investment Company Act Rule 20a-1.

designed to protect. Second, the nominating shareholder or member of the nominating shareholder group must hold both investment and voting power, either directly or through any person acting on their behalf, of the securities. By requiring that a nominating shareholder or member of a nominating shareholder group hold investment and voting power of the securities that are used for purposes of determining whether the ownership requirement has been met, we are addressing the concerns raised by certain commenters that the provisions of Rule 14a-11 should only be available to shareholders that possess ultimate ownership rights over the shares.

Similar to the provisions in Exchange Act Rule 13d-3,[270] the definition of voting power for purposes of Rule 14a-11 includes the power to vote, or to direct the voting of, such securities and investment power for purposes of Rule 14a-11 includes the power to dispose, or to direct the disposition of, such securities.[271] Unlike the provisions in Rule 13d-3, however, the ownership requirement of Rule 14a-11 includes both voting and investment power – as opposed to just one or the other – and voting and investment power for purposes of Rule 14a-11 does not exist over securities that a nominating shareholder or member of a nominating shareholder group merely has the right to acquire. For example, a nominating shareholder or member of a nominating shareholder group will not be able to count securities that could be acquired, such as securities underlying options that are currently exercisable but have not yet been exercised.

For purposes of meeting the ownership threshold in Rule 14a-11, a nominating shareholder or group will include investment and voting power of the company's securities that is held "either directly or through any person acting on their behalf." We are adopting the

---

270 17 CFR § 240.13d-3. Like the approach under Rule 13d-3, we are including and excluding certain securities from the determination of who has voting power for policy reasons. Those inclusions and exceptions and the policy reasons underlying them are discussed throughout this section.

271 See Instruction 3.c. to Rule 14a-11(b)(1).

ownership provisions with this language to account for the common situation when financial intermediaries, such as banks or brokers, hold securities on behalf of their clients.[272] This additional language also covers relationships, such as parent and subsidiary, when for organizational or tax reasons, among others, investment and voting power is held by an entity that is controlled by another entity. This provision, however, would not include securities that are held in a pooled investment vehicle in which the nominating shareholder or member of a nominating shareholder group does not have voting and investment power over the securities held in the pooled investment vehicle.

Third, we have adopted a provision in the ownership requirement in Rule 14a-11 that, subject to specific conditions, allows for securities that have been loaned to a third party by or on behalf of the nominating shareholder or member of a nominating shareholder group to be considered in the calculation. We recognize that share lending is a common practice, and we believe that loaning securities to a third party is not inconsistent with a long-term investment in a company.[273] To capture only securities where voting power can ultimately be exercised by the nominating shareholder or member of a nominating shareholder group in the election of directors, however, securities that have been loaned by or on behalf of the nominating shareholder or any member of the nominating shareholder group to another person may be counted toward the ownership requirement only if the nominating shareholder or member of the nominating shareholder group:

- has the right to recall the loaned securities; and

---

272 The rule also clarifies that financial intermediaries, such as banks or brokers, that may hold securities on behalf of their clients could not use the provisions of Rule 14a-11. See Instruction 3.c. to Rule 14a-11(b)(1).

273 See letters from AFL-CIO; CalPERS; CII; COPERA; IAM; LIUNA; Marco Consulting; P. Neuhauser; D. Nappier; Sheet Metal Workers; SWIB.

- will recall the loaned securities upon being notified that any of the nominees will be included in the company's proxy materials.

Absent satisfaction of these conditions – in addition to holding the requisite investment power over the loaned securities – we believe it is appropriate to exclude securities that have been loaned to another person from the calculation of voting power because, generally, the person to whom the securities have been loaned has the ability to vote those securities.[274] If the rule were to allow loaned securities that either will not or cannot be recalled to be included for purposes of the ownership calculation, then the voting power of a nominating shareholder or member of a nominating shareholder group may potentially be inflated because the calculation could include votes that the nominating shareholder or member of a nominating shareholder group cannot actually cast.

In determining the total voting power of the company's securities held by or on behalf of the nominating shareholder or any member of the nominating shareholder group, the voting power would be reduced by the voting power of any of the company's securities that the nominating shareholder or any member of a nominating shareholder group has sold in a short sale during the relevant periods.[275] In addition, the rule text explicitly excludes borrowed shares because the rule is intended to be used by holders with a significant long-term commitment to the company, and including shares that are merely borrowed is inconsistent with that purpose. The

274 See letter from P. Neuhauser.

275 See Instruction 3.b.3 to Rule 14a-11(b)(1). We note that in a typical short sale the person selling the securities short would not have the power to vote the securities subject to the short sale. Nevertheless, the provisions of Rule 14a-11 require that the voting power of the securities subject to the short sale be deducted from the voting power held directly or on behalf of the nominating shareholder or member of the nominating shareholder group to address our concerns about limiting the application of Rule 14a-11 to shareholders that retain significant ownership interests in a company. Likewise, a person whose ownership of shares arises solely from borrowing them for purposes of short sale would be deemed to have no share ownership for purposes of the ownership requirement of Rule 14a-11(b)(1).

instruction makes clear that to the extent borrowed securities are not already excluded through the subtraction of securities sold short, borrowed securities would be subtracted in computing the relevant amount. We recognize that by requiring the voting power of securities sold short or borrowed for purposes other than a short sale to be subtracted from the ownership calculation, we are potentially reducing the eligibility of certain shareholders to rely on Rule 14a-11.[276] Nevertheless, as noted above, we believe that eligibility for Rule 14a-11 should be limited to those shareholders that have a significant interest in the company.[277] We agree with commenters who suggested that selling a company's securities short may divest that shareholder of the economic risks of ownership.[278]

For purposes of determining whether the nominating shareholder or any member of a nominating shareholder group has sold a company's securities short, the term "short sale" will

---

276 The ownership provisions related to short sales do not apply to securities that have been sold in a short sale where the nominating shareholder or member of the nominating shareholder group had no control over such transactions. See Instruction 3.b.3. to Rule 14a-11(b)(1) (covering short sales by "the nominating shareholder or any member of the nominating shareholder group, as the case may be, or any person acting on their behalf…"). For example, a nominating shareholder would not be required to exclude securities that have been sold short by a pooled investment vehicle in which the nominating shareholder or member of a nominating shareholder group has invested as long as the shareholder does not have the ability to direct the investments held in the pooled investment vehicle. Similarly, securities held by the pooled investment vehicle with respect to which the shareholder does not have the ability to direct the investments held in the pooled investment vehicle would not be included in the amount of holdings of the shareholder.

277 We recognize that selling a company's securities short is only one of a number of ways that a shareholder can hedge the economic risk of its investment. Indeed, a number of commenters suggested that we adopt a beneficial ownership definition for purposes of Rule 14a-11 that netted all hedging arrangements (derivatives, swaps, etc.). We believe, however, that it is appropriate at this time to adopt the ownership threshold for Rule 14a-11 with the provision only relating to short sales as it contributes significantly towards the goal of excluding votes from the ownership calculation securities where the voting and economic interests are separated and does not unduly complicate the rule. Further, by excluding securities that the holder merely has the right to acquire (such as securities underlying options) and securities that have been loaned and cannot be recalled, we have further narrowed the application of the rule to address concerns about separating economic interest and voting power.

278 See letters from 26 Corporate Secretaries; ABA; Advance Auto Parts; Alaska Air; Allstate; Applied Materials; Association of Corporate Counsel; AT&T; J. Blanchard; Biogen; BRT; CIEBA; Cleary; Devon; Dewey; Headwaters; IBM; JPMorgan Chase; PepsiCo; Sara Lee; Seven Law Firms; Shearman & Sterling; Sidley Austin; Society of Corporate Secretaries; Verizon.

have the meaning provided in Exchange Act Rule 200(a).[279] Under that rule, a short sale is "any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller."

In calculating the voting power required to satisfy the 3% voting power eligibility requirement described above, nominating shareholders or members of a nominating shareholder group must first determine the total number of votes that can be derived from their holdings of securities that are subject to the proxy rules. This determination is made as of the date the Schedule 14N is filed. The total number of votes can be increased by the number of votes attributable to securities which have been loaned (subject to the conditions previously noted) and must be reduced by the number of votes attributable to any securities that have been sold in a short sale that is not closed out as of that date or borrowed for purposes other than a short sale. This adjusted number of votes is the qualifying number of votes eligible to be used as the numerator in calculating the percentage held of the company's total voting power. The number of securities to which these qualifying votes are attributable is the amount of securities that must be used for evaluating compliance with the continuous holding period requirements specified in Rule 14a-11(b)(2), and discussed below.

In determining the total voting power of the company's securities, nominating shareholders and members of a nominating shareholder group will be entitled to rely on the most recent quarterly, annual or current report filed by the company unless the nominating shareholder or member of a nominating shareholder group knows or has reason to know that the information

[279] 17 CFR § 242.200(a). We note that certain of the provisions in Exchange Act Rule 200, including when a "person shall be deemed to own a security" as defined in Rule 200(b), differ from the provisions we have adopted for purposes of Rule 14a-11. For instance, Rule 200(b) extends ownership of a security to options that have been exercised. As noted above, however, we have not extended ownership for purposes of Rule 14a-11 to options. We believe that these different, but not conflicting, approaches are appropriate and reflect the policy objectives for adopting each rule.

in the reports is inaccurate.[280] We believe that a nominating shareholder or member of a nominating shareholder group should be able to rely on the filings made by the company in making the calculation of voting power for purposes of Rule 14a-11 even if the number of securities outstanding has changed since the last report so that a nominating shareholder or member of a nominating shareholder group can easily make a determination about the percentage of voting power that they hold.

iv. Demonstrating ownership

Under the Proposal, a nominating shareholder or member of a nominating shareholder group would be able to demonstrate ownership in several ways.[281] If the nominating shareholder or member of the nominating shareholder group is the registered holder of the shares, he or she could state as much. In this instance, the company would have the ability to independently verify the shareholder's ownership. Where the nominating shareholder or member of the nominating shareholder group is not the registered holder of the securities, the nominating shareholder or member of the nominating shareholder group would be required to demonstrate ownership by attaching to the Schedule 14N a written statement from the "record" holder of the nominating shareholder's shares (usually a broker or bank) verifying that, at the time of submitting the shareholder notice to the company on Schedule 14N, the nominating shareholder or member of the nominating shareholder group continuously held the securities being used to

280 See Instruction 1 to Rule 14a-11(b)(1). In the case of a registered investment company, in determining the total voting power of the securities that are entitled to be voted on the election of directors for purposes of establishing whether the 3% voting power threshold has been met, the nominating shareholder or group may rely on information set forth in the following documents, unless the nominating shareholder or group knows or has reason to know that the information contained therein is inaccurate: (1) in the case of a series company, a Form 8-K that will be required to be filed in connection with the meeting where directors are to be elected; or (2) in the case of other registered investment companies, the company's most recent annual or semi-annual report filed with the Commission on Form N-CSR. See Instruction 2 to Rule 14a-11(b)(1).

281 See Item 5 of proposed Schedule 14N.

satisfy the applicable ownership threshold for a period of at least one year.[282] In the alternative, if the nominating shareholder or member of the nominating shareholder group has filed a Schedule 13D, Schedule 13G, Form 3, Form 4, and/or Form 5, or amendments to those documents, the shareholder or group member may so state and attach a copy or incorporate that filing or amendment by reference.

Commenters generally did not object to the proposed methods of demonstrating ownership; however, they did suggest some revisions to the rule. Two commenters believed that the nominating shareholder or group, if requested by the company, should be required to provide evidence from its broker-dealer or custodian certifying that its ownership position meets the requisite threshold through a date that is within five days of the shareholders' meeting.[283] Another commenter recommended a revision to the proposed rule to allow the written statement to be dated no more than seven days prior to the date of submission of the nomination to the company.[284] The commenter explained that it may be difficult for a group of nominating shareholders to obtain letters from the "record" holders on the exact same date they submit the nomination to the company and file a Schedule 14N and cited similar problems in the context of the Rule 14a-8 process as an example. Another commenter recommended more generally that the written statement be dated a short period before the filing of the Schedule 14N.[285] Other commenters submitted various suggestions as to who should provide the required written statement.[286]

---

282 See the discussion below regarding the holding period we are adopting.

283 See letters from BorgWarner; Society of Corporate Secretaries.

284 See letter from CII.

285 See letter from P. Neuhauser.

286 See letters from ABA; CII; ICI; P. Neuhauser; Schulte Roth & Zabel; Seven Law Firms; S&C. Litigation

While we are adopting the requirements to demonstrate ownership as proposed, we agree with the commenters that additional clarity is needed with regard to how far in advance of the notice date the statement of the broker or bank may be dated, as well as what type of bank or broker may provide the written statement on behalf of the shareholder. We believe the date should be as close as practicable to the notice date, and believe that seven calendar days should provide a workable time frame that is still close in time to the notice date. Accordingly, we have revised the rule to clarify that the statement from the registered holder, broker, or bank may be dated within seven calendar days prior to the date the nominating shareholder or group submits the notice on Schedule 14N.[287]

Also, to provide additional clarity about these requirements, the final rule includes an example of a form of written statement verifying share ownership that may be used if the nominating shareholder or any member of the nominating shareholder group (i) is not the registered holder of the shares, (ii) is not proving ownership by providing previously filed Schedules 13D or 13G or Forms 3, 4, or 5, and (iii) holds the shares in an account with a broker or bank that is a participant in the Depository Trust Company ("DTC") or a similar clearing agency acting as a securities depository.[288] An instruction to Schedule 14N describes more fully

---

subsequent to the Proposal has underscored the utility of clarifying the source of verification of ownership by shareholders who are not themselves registered owners of the shares. See Apache Corp. v. Chevedden, 696 F.Supp.2d 723 (S.D.Tex. Mar. 10, 2010) (interpreting the proof of ownership requirement in Rule 14a-8(b)(2)).

287 We note that a nominating shareholder may have changed brokers or banks during the time period in which it has held the shares it is using to meet the ownership threshold. In such cases, the nominating shareholder would need to obtain a written statement from each broker or bank with respect to the shares held and specify the time period in which the shares were held.

288 This form of written statement from a bank or broker is a modification to the Proposal, and is provided as a non-exclusive example of an acceptable method of satisfying the requirement in Rule 14a-11(b)(3). See Instruction to Item 4 of new Schedule 14N. We note that the written statements would not reflect all aspects of the ownership requirement, such as the percentage of voting power held, and thus, would not be dispositive with regard to whether the nominating shareholder or group satisfied the ownership threshold. For purposes of complying with Rule 14a-11(b)(3), loaned securities may be included in the amount of

what information should be provided if a nominating shareholder or any member of the nominating shareholder group holds the securities through a broker or bank (e.g., in an omnibus account) that is not a participant in DTC or a similar clearing agency.[289]

We note that satisfying the requirement in Rule 14a-11(b)(3) to demonstrate ownership is different from satisfying the requirement in Rules 14a-11(b)(1) and 14a-11(b)(2) that a shareholder or shareholder group hold the requisite amount of the company's securities that are entitled to be voted on the election of directors for three years, as calculated pursuant to the Instruction to paragraph (b)(2). It is possible for a shareholder to be able to demonstrate ownership pursuant to Rule 14a-11(b)(3), and yet not satisfy the total voting power and holding period requirements in Rules 14a-11(b)(1) and (b)(2).

c. **Holding period**

With respect to duration of ownership, we proposed a one-year holding requirement for each nominating shareholder or member of a nominating shareholder group. Although many commenters supported the proposed one-year holding period,[290] the majority of commenters suggested a holding period longer than the proposed one-year period, with many recommending

---

securities set forth in the written statements. Consistent with the Proposal, a nominating shareholder or group proving ownership by using a previously filed Schedule 13D or 13G or Form 3, 4, or 5 could attach a copy of the filing to the Schedule 14N or incorporate it by reference into the Schedule. We note that the calculation of voting power of a company's securities for purposes of Rule 14a-11 differs from the determination of beneficial ownership for purposes of those schedules and forms. In addition, as adopted, we are clarifying that the schedules or forms used to provide proof of ownership must reflect ownership of the securities as of or before the date on which the three-year eligibility period begins.

289 See the Instruction to Item 4 of new Schedule 14N.

290 See letters from ADP; AFSCME; Callaway; CalPERS; CalSTRS; Calvert; CFA Institute; J. Chico; CII; Corporate Library; Dominican Sisters of Hope ("Dominican Sisters of Hope"); GovernanceMetrics International ("GovernanceMetrics"); ICGN; Lorsch et al.; LUCRF; Mercy Investment Program ("Mercy Investment Program"); Motorola; D. Nappier; Nathan Cummings Foundation; P. Neuhauser; Norges Bank; Pax World; RiskMetrics; Shamrock; Shearman & Sterling; Sisters of Mercy Regional Community of Detroit Charitable Trust ("Sisters of Mercy"); Social Investment Forum; Sodali; Tri-State Coalition for Responsible Investment ("Tri-State Coalition"); Trillium; T. Rowe Price; Ursuline Sisters of Tildonk ("Ursuline Sisters of Tildonk"); USPE; ValueAct Capital; Walden Asset Management ("Walden").

alternative holding periods ranging from 18 months to four years.[291] Some commenters, for example, expressed a belief that increasing the duration of the minimum holding period would ensure that use of Rule 14a-11 is limited to holders of a significant, long-term interest and would dissuade shareholders from using the rule to nominate and elect directors to make short-term gains at the expense of long-term shareholders.[292] A small number of commenters believed that Rule 14a-11 should not include a holding period requirement.[293] One commenter believed that all holders of the same securities should have the same rights under Rule 14a-11 regardless of how long the securities have been held.[294] Another commenter stated that a short-term shareholder has the same risk as long-term shareholders; thus their rights under Rule 14a-11 should be equal.[295]

After considering the comments, we have decided to adopt a three-year holding requirement, rather than the proposed one-year requirement. This decision is based on our belief that holding securities for at least a three-year period better demonstrates a shareholder's long-

291 See letters from 26 Corporate Secretaries; ABA; Advance Auto Parts; Aetna; AFL-CIO; Alaska Air; Alcoa; Allstate; Alston & Bird; Amalgamated Bank; American Express; Anadarko; Applied Materials; Association of Corporate Counsel; AT&T; Avis Budget; Biogen; J. Blanchard; Boeing; BorgWarner; BRT; Burlington Northern; Caterpillar; Chevron; CIEBA; CIGNA; CNH Global; P. Clapman; Comcast; Con Edison; CSX; CtW Investment Group; Cummins; L. Dallas; Darden Restaurants; E. Davis; Deere; Devon; Dewey; DTE Energy; DuPont; Eaton; Eli Lilly; ExxonMobil; FedEx; Fenwick; FMC Corp.; FPL Group; General Mills; Headwaters; Home Depot; Honeywell; IAM; IBM; ICI; Intel; ITT; JPMorgan Chase; Lionbridge Technologies; LIUNA; Marco Consulting; McDonald's; M. Metz; J. Miller; NACD; D. Nappier (expressing a willingness to accept a two-year holding period instead of the proposed one-year holding period); Northrop; Office Depot; OPERS; Pfizer; P&G; Praxair; Protective; RiskMetrics (accepting a two-year holding period as alternative to the proposed one-year holding period); Sara Lee; S&C; Sheet Metal Workers; Sidley Austin; SIFMA; Society of Corporate Secretaries; Southern Company; Teamsters; Tesoro; Textron; Theragenics; TI; TIAA-CREF; Tidewater; Time Warner Cable Inc. ("Time Warner Cable"); tw telecom; L. Tyson; UnitedHealth; U.S. Bancorp; Wells Fargo; Weyerhaeuser; Xerox; Vanguard; Verizon; B. Villiarmois.

292 See letters from BRT; CIEBA; IBM; McDonald's; Society of Corporate Secretaries.

293 See letters from 13D Monitor; ACSI; British Insurers; Ironfire Capital LLC ("Ironfire"); LUCRF.

294 See letter from British Insurers.

295 See letter from 13D Monitor.

term commitment and interest in the company.[296] We also based our decision to have a holding period longer than one year on the strong support of a variety of commenters. For instance, we received comments that advised that we should "adopt a more reasonable holding period of at least two years,"[297] and "a minimum holding period of at least two years is appropriate" because a "shorter holding period would allow shareholders with a short-term focus to nominate directors who, if elected, would be responsible for dealing with a company's long-term issues."[298] Another commenter stated that "three years would be a more reasonable test with respect to longevity of stock ownership."[299] Although two commenters suggested even longer holding periods,[300] we believe that a three year holding period reflects our goal of limiting use of the rule to significant, long-term holders and appropriately responds to commenters' suggestions regarding the length of the holding period. In this regard, as noted previously, some commenters suggested a two year holding period, but others stated it should be "at least" two years. Given the support expressed for a significant holding period, we believe a three year holding period, rather than one or two years, strikes the appropriate balance in providing shareholders with a significant, long-term interest with the ability to have their nominees included in a company's proxy materials while limiting the possibility of shareholders attempting to use Rule 14a-11 inappropriately, as discussed further below.

296 One commenter pointed to the Aspen Principles, available at http://www.aspeninstitute.org/sites/default/files/content/docs/pubs/Aspen_Principles_with_signers_April_09.pdf, suggesting that companies that are often forced to react to short-term investors are constrained from creating valuable goods and services, investing in innovations, and creating jobs. See also letter from AFL-CIO.

297 Letter from Teamsters.

298 Letter from BRT.

299 Letter from Tesoro.

300 See letters from E. Davis; Fenwick.

We also factored our desire to limit the use of Rule 14a-11 to shareholders who do not possess a change in control intent with regard to the company into our decision to extend the holding period. Although we have, as noted below, adopted specific requirements in Rule 14a-11 to address the control issue, we believe that a longer holding period is another safeguard against shareholders that may attempt to inappropriately use Rule 14a-11 as a means to quickly gain control of a company. Finally, we note that if shareholders believe that the three-year period should be shorter, the amendment that we decided to adopt to Rule 14a-8 will remove barriers to proposals that seek to establish a different procedure with a lesser (or no) holding period condition.

The requirement we are adopting is that shareholders seeking to use Rule 14a-11 to have a nominee or nominees included in a company's proxy materials must have held the minimum amount of securities used to satisfy the 3% ownership threshold continuously for at least three years.[301] Similar to the calculation of voting power discussed above, in order to satisfy the three-year holding requirement, the nominating shareholder or member of the nominating shareholder group must have investment and voting power over the amount of securities, and the amount of securities held during the period will have to be reduced by the amount of securities of the same class that are the subject of short positions or are borrowed for purposes other than a short sale

301 As proposed, a nominating shareholder or group would have been required to hold "the securities that are used for purposes of determining the applicable ownership threshold" and intend to continue to hold "those securities" through the date of the meeting. See proposed Rule 14a-11(b)(2). The Proposal also would have required the nominating shareholder or group to provide a statement that the nominating shareholder or group intends to continue to own the "requisite shares" through the date of the meeting. See proposed Rule 14a-18(f). As adopted, we are modifying Rule 14a-11 to require the nominating shareholder or each member of the nominating shareholder group to have held the "amount of securities" that are used for satisfying the ownership requirement and to continue to hold that amount of securities through the date of the meeting, rather than referring to the "requisite securities." In addition, even though the ownership requirement is based on the percentage of voting power held, the requirement refers to "amount" rather than "percentage" so that satisfaction of the ownership requirement can be accurately determined. We believe it would be unduly burdensome to require that a nominating shareholder or group determine whether its holdings exceeded 3% of the company's voting power continuously for a three-year period prior to the filing of the Schedule 14N.

during the period.[302] The rule also allows securities loaned to a third party to be considered held during the period, provided that the nominating shareholder or group has the right to recall the loaned securities during the period.[303] As discussed above, we do not believe that the common practice of lending securities is inconsistent with a long-term investment. While we believe it is important to include both of the recall provisions for purposes of allowing loaned securities to be used in the 3% ownership threshold calculation in Rule 14a-11(b)(1), we believe it is only necessary for the nominating shareholder or member of a nominating shareholder group to have the right to recall the loaned securities to satisfy the three-year holding period requirement.[304] Finally, the rule requires the amount of securities to be adjusted for stock splits, reclassifications or other similar adjustments made by the company during the period.[305]

A commenter suggested that we clarify that a nominating shareholder or each member of the group must have continuously held only the minimum number of shares used to satisfy the ownership requirement.[306] We agree that a nominating shareholder or member of a nominating shareholder group is not required to have continuously held shares in excess of the amount used to attain eligibility for purposes of Rule 14a-11. For example, under Rule 14a-11(b)(2), which requires continuous holding of "the amount of securities that are used for purposes of satisfying

---

302 See the Instruction to Rule 14a-11(b)(2). For purposes of this calculation, the amount of the short position or borrowed securities at any point in time during the three year holding period would be deducted from the amount of securities otherwise held at that point in time.

303 Id.

304 Id. The recall provisions are discussed in Section II.B.4.b.iii. above. We note that at the time the nominating shareholder or group calculates its ownership and submits a nominee or nominees, it may not be certain that its nominee or nominees will be included in the company's proxy materials. We do not believe it is necessary to require a nominating shareholder or group to recall loaned shares that it has the right to recall and vote prior to the time that the nominating shareholder or group is notified that its nominee or nominees will be included in the company's proxy materials.

305 See the Instruction to Rule 14a-11(b)(2).

306 See letter from AFSCME.

the minimum ownership required of paragraph (b)(1) …, " if a nominating shareholder owns 400,000 shares and those shares comprise 4% of the issuer's voting power as of the date of filing of the Schedule 14N, that shareholder is not required to have held 400,000 shares continuously during the preceding three years and through the date of election of directors. Rather, the nominating shareholder would be required to continuously hold the minimum amount of shares required to satisfy the 3% ownership threshold in paragraph (b)(1), assuming no adjustments (in this example, at least 300,000 shares).

We also believe that it is important that any shareholder or member of a nominating shareholder group that intends to submit a nominee to a company for inclusion in the company's proxy materials continue to maintain the qualified minimum amount of securities in the company needed to satisfy the ownership provisions in the rule through the date of the meeting at which the shareholder's or group's nominee is presented to a vote of shareholders. To meet the eligibility criteria in proposed Rule 14a-11(b)(2), a nominating shareholder or member of a nominating shareholder group would have been required to "intend to continue to hold" the securities used to meet the ownership threshold through the date of the meeting. Commenters on the Proposing Release generally supported a holding requirement through the date of the meeting,[307] and one commenter suggested that we clarify that shareholders would be required to hold the securities used for determining ownership through the election of directors.[308] We agree with the suggestion and are modifying the language in Rule 14a-11(b)(2) to clarify that a nominating shareholder or member of a nominating shareholder group "must continue to hold"

---

307 See letters from ABA; Advance Auto Parts; Alston & Bird; American Express; Association of Corporate Counsel; J. Blanchard; BorgWarner; CalPERS; CII; Cleary; Comcast; CSX; Dewey; W. B. Dickerson; Florida State Board of Administration; General Mills; Headwaters; JPMorgan Chase; Nathan Cummings Foundation; Protective; Schulte Roth & Zabel; Seven Law Firms; Shearman & Sterling; Society of Corporate Secretaries; tw telecom; ValueAct Capital.

308 See letter from ABA.

the requisite amount of securities through the date of the meeting.[309] If a nominating shareholder or member of a nominating shareholder group fails to continue to hold the requisite amount of securities as required by the rule, a company could exclude the nominee or nominees submitted by the nominating shareholder or group.[310]

We also are adopting, as proposed, the requirement that a nominating shareholder or member of a nominating shareholder group provide a statement as to the nominating shareholder's or group member's intent to continue to hold the qualifying minimum amount of securities through the date of the meeting.[311] In addition, we proposed that nominating shareholders or members of a nominating shareholder group disclose their intent with regard to continued ownership of their shares after the election (which may be contingent on the election's outcome). As noted above, commenters generally supported the requirement for the nominating shareholder or group to hold the requisite amount of securities through the date of the meeting, although some commenters expressed opposition to the proposed disclosure requirement or any requirement for the nominating shareholder or group to disclose their intent to hold the

309 For purposes of determining whether the requirement to hold the specified amount of securities from the date of the filing of the Schedule 14N through the date of the election of directors is satisfied, a nominating shareholder or group must hold (as determined pursuant to the instruction to the rule) the qualifying minimum amount of securities, which can include securities that are loaned to a third party if the nominating shareholder or group has the right to recall the securities, and will recall them upon being notified that any of the nominees will be included in the company's proxy materials. Of course, between the date of the filing of the Schedule 14N and the date of the election of directors previously loaned securities may be returned. Likewise, the amount of securities held during the period from the filing of the Schedule 14N through the date of the election of directors must be reduced by the amount of securities of the same class that are sold in a short sale.

310 See new Rule 14a-11(b)(2) and Rule 14a-11(g). The company would be required to provide notice to the staff in accordance with Rule 14a-11(g) and could seek a no-action letter from the staff with regard to the determination to exclude the nominee at that time if the company so wished. In the event that the nominating shareholder's or group's failure to continue to hold the securities comes to light after the company has printed its proxy materials, the company would be permitted to exclude the nominee or nominees and send a revised proxy card to its shareholders. For additional information about a company's obligations in the event a nominee withdraws or is disqualified, see Section II.B.7.b. below.

311 See new Rule 14a-11(b)(4) and proposed Rule 14a-18(f).

company's shares after the date of the election.[312] One commenter explained that the nominating shareholder or group may not know its intent at the time the Schedule 14N is filed and, depending on the outcome of the director election, the nominating shareholder or group may, in fact, purchase more stock or sell some stock.[313] Another commenter observed that it is impractical for shareholders to represent that they would hold their position beyond the election and instead favored disclosure in an amended Schedule 14N of any change in the ownership of more than 1% of the voting shares or net economic position during a period after the election (e.g., 60 days).[314] Other commenters supported the proposed disclosure requirement regarding the nominating shareholder's or group's intent to hold shares after the meeting, or recommended that the Commission require instead that the nominating shareholder or group hold the requisite amount of shares for a specific period after the date of the meeting.[315]

We believe that a requirement to hold the securities through the date of the election of directors is appropriate to demonstrate the nominating shareholder's or group member's commitment to the director nominee and the election process. In addition, we are adopting the disclosure requirement, as proposed, concerning the nominating shareholder's or group member's intent with respect to continued ownership of their shares after the election.[316] We are

312 See letters from Alston & Bird; Amalgamated Bank; Calvert; CII; Florida State Board of Administration; P. Neuhauser; Norges Bank; Schulte Roth & Zabel; TIAA-CREF; USPE; ValueAct Capital.

313 See letter from CII.

314 See letter from Cleary.

315 See letters from 26 Corporate Secretaries; ABA; Aetna; AGL; Alaska Air; Alcoa; Anadarko; Applied Materials; Association of Corporate Counsel; Avis Budget; BRT; Burlington Northern; Callaway; Caterpillar; Comcast; L. Dallas; Darden Restaurants; Devon; W. B. Dickerson; Dupont; Eli Lilly; FPL Group; General Mills; Home Depot; Honeywell; Intel; Lionbridge Technologies; Lorsch et al.; Keating Muething; Office Depot; PepsiCo; Pfizer; Protective; Sara Lee; SIFMA; Tesoro; Textron; TI; UnitedHealth; U.S. Bancorp; Verizon; Xerox.

316 See new Rule 14a-11(b)(5) and new Item 4(b) of Schedule 14N.

not, however, adopting a requirement for a nominating shareholder or member of a nominating shareholder group to continue to hold their shares for a certain period of time after the date of the election. We believe that disclosure of a nominating shareholder's or group member's intent with respect to continued ownership in a Schedule 14N or amended Schedule 14N will provide investors with the information they need for this purpose.

d. No change in control intent

Under the Proposal, to rely on Rule 14a-11, a nominating shareholder or member of a nominating shareholder group would have been required to provide a certification in the filed Schedule 14N that it did not hold the securities with the purpose, or with the effect, of changing the control of the company or gaining more than a limited number of seats on the board.[317] We noted that this certification, along with the other required disclosures, would assist shareholders in making an informed decision with regard to any nominee or nominees put forth by the nominating shareholder or group, in that the information would enable shareholders to gauge the nominating shareholder's or group's interest in the company, longevity of ownership, and intent with regard to continued ownership in the company.

Most commenters on this aspect of the Proposal agreed generally that Rule 14a-11 should not be available to shareholders seeking to effect a change in control of a company (or to obtain more than a specified number of board seats) and supported a certification requirement regarding the lack of change in control intent.[318] Some commenters, however, expressed concern about the

---

317 See Item 8 of proposed Schedule 14N.

318 See letters from ABA; Advance Auto Parts; American Bankers Association; American Express; Americans for Financial Reform ("Americans for Financial Reform"); BRT; CalSTRS; CII; Cleary; COPERA; Corporate Library; Dewey; Dominican Sisters of Hope; Eli Lilly; Emerson Electric; Florida State Board of Administration; A. Goolsby; GovernanceMetrics; ICI; JPMorgan Chase; Sen. Carl Levin ("C. Levin"); Mercy Investment Program; Metlife; Nathan Cummings Foundation; P. Neuhauser; Protective; RiskMetrics; Seven Law Firms; SIFMA; Sisters of Mercy; Social Investment Forum; Society of Corporate Secretaries; Sodali; SWIB; TIAA-CREF; Trillium; Tri-State Coalition; T. Rowe Price; tw telecom;

lack of a remedy when a certification regarding control intent proves to be false or when a nominating shareholder or group changes its intent.[319] Suggested remedies included excluding the nominee of any nominating shareholder or group that changes intent and barring the nominating shareholder or group from using the rule for the following two annual meetings,[320] requiring disclosure of a change of intent and resignation of the Rule 14a-11 director,[321] and imposing liability under Rule 14a-9.[322]

We are adopting this requirement with some modifications from the Proposal. To rely on Rule 14a-11, the nominating shareholder (or where there is a nominating shareholder group, any member of the nominating shareholder group) must not be holding any of the company's securities with the purpose, or with the effect, of changing control of the company[323] or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11 and must provide a certification to this effect in its filed Schedule 14N.[324]

The final requirement differs from the Proposal in three respects. First, in addition to

---

Ursuline Sisters of Tildonk; Wachtell; Walden; B. Villiarmois.

319 See letters from American Bankers Association; Dewey; Emerson Electric; A. Goolsby; Metlife; Protective; Seven Law Firms; SIFMA.

320 See letter from Seven Law Firms.

321 See letter from Protective.

322 See letter from P. Neuhauser.

323 Although Rule 14a-11 does not contain a requirement that the shareholder nominee or nominees do not have an intent to change the control of the company, a nominating shareholder's or group's ability to meet the requirement and certify that it does not have such an intent will be impacted by the intentions and actions of its nominee or nominees. For example, a nominating shareholder would not be able to certify that it does not hold the company's securities for the purpose, or with the effect, of changing the control of the company if its nominee is engaged in its own proxy contest or tender offer while the Rule 14a-11 nomination is pending.

324 See certifications in Item 8 of new Schedule 14N.

requiring the certification to address the absence of change in control intent or intent to gain more than the maximum number of seats provided under the rule, we also have added this condition as an explicit requirement to the rule.[325] We believe that this more directly achieves our intent – that the rule not be used by shareholders that have an intent to change the control of the company or gain more than the maximum number of seats specified in the rule.

Second, we have clarified the language of the requirements so that it provides that the rule is available only if the nominating shareholder or group members do not have an intent to change control of the company[326] or gain more seats on the board than the maximum provided for under Rule 14a-11. We slightly revised the language of the requirement to clarify our intended meaning. The Proposal used the language "gain more than a limited number of seats on the board," which was intended to refer to the limitations within the rule on the maximum number of nominees required to be included in the company's proxy materials. The final rule states this more explicitly.

Finally, we have added an instruction to clarify that in order to rely on Rule 14a-11 to include a nominee or nominees in a company's proxy materials, a nominating shareholder or a member of a nominating shareholder group may not be a member of any other group with persons engaged in solicitations or other nominating activities in connection with the subject election of directors; may not separately conduct a solicitation in connection with the subject election of directors other than a Rule 14a-2(b)(8) exempt solicitation in relation to those nominees it has nominated pursuant to Rule 14a-11 or for or against the company's nominees; and may not act as a participant in another person's solicitation in connection with the subject

325 See Rule 14a-11(b)(6).

326 A change in control includes, but is not limited to, an extraordinary corporate action, such as a merger or tender offer.

election of directors.[327]

We understand that companies have concerns that shareholders using Rule 14a-11 may inaccurately assert that they do not have a change in control intent, and that this can be a difficult factual issue. If a company determines that it can exclude a nominee based on this eligibility condition, it will be required to notify the nominating shareholder, members of the nominating shareholder group, or, where applicable, the nominating shareholder group's authorized representative, of a deficiency in its notice on Schedule 14N and provide the nominating shareholder or group the opportunity to respond. The company also would be required to submit a notice to the Commission stating its intent to exclude a nominee from its proxy materials (which would be required to include a description of the company's basis for exclusion) and, if it wished to, it could seek the staff's informal view with regard to its determination to exclude the nominee (commonly referred to as a "no-action" request).[328] In addition, a nominating shareholder and each member of a nominating shareholder group will have liability under Rule 14a-9 for a materially false or misleading certification in the Schedule 14N. Questions concerning the nomination also may be resolved by the parties outside the staff process provided in Rule 14a-11(g), including through private litigation where necessary, similar to the way they resolve issues arising in traditional proxy contests.[329] Finally, we note that the Commission also could take enforcement action with respect to companies that inappropriately exclude nominees under Rule 14a-11 or shareholders that provide false certifications in their Schedule 14N. We believe these measures should provide sufficient means to address situations in which a

---

327 See new Instruction to Rule 14a-11(b).

328 See Section II.B.9.b. below for further discussion of determinations to exclude a nominee or nominees.

329 See Sections II.B.8. and II.B.9. for an explanation of the disclosure requirements applicable to a nomination made pursuant to Rule 14a-11 and the process for excluding a nominee.

nominating shareholder or member of a nominating shareholder group provides a false certification regarding change in control intent.

e. Agreements with the company

In the Proposing Release, we noted that a shareholder nomination process that includes limits on the number of nominees that a company is required to include in its proxy materials presents the potential risk of nominating shareholders or groups acting merely as a surrogate for the company or its management in order to block usage of the rule by another nominating shareholder or group. We proposed to address this concern by providing that a nominating shareholder or group using Rule 14a-11 would be required to represent that no agreement between the nominating shareholder or group and the company and its management exists.[330] To avoid any uncertainty about the breadth of this requirement, the Proposal included an instruction noting that prohibited agreements would not include unsuccessful negotiations with the company to have the nominee included in the company's proxy materials as a management nominee, or negotiations that are limited to whether the company is required to include the shareholder nominee in the company's proxy materials under Rule 14a-11.

Commenters generally supported the proposed requirement, including the clarifying instruction regarding certain negotiations with the company.[331] One commenter specifically supported the portion of the proposed rule providing that unsuccessful negotiations or negotiations that were limited to whether the company is required to include a shareholder nominee under Rule 14a-11 would not be deemed to be a direct or indirect agreement.[332] One

---

330 In this regard, we also proposed to require a nominating shareholder or group to represent that no relationships or agreements between the nominee and the company and its management exist. This aspect of the rule is discussed in Section II.B.5.c. below.

331 See letters from ADP; BRT; Calvert; CFA Institute; CII; Seven Law Firms; TIAA-CREF; USPE.

332 See letter from CII.

commenter was concerned about possible manipulation by companies and supported a prohibition on agreements.[333] According to that commenter, negotiations that resulted in a nomination being included in the proxy statement should be treated as a company nominee and not a shareholder nominee under Rule 14a-11.

Some commenters encouraged us to allow negotiations that resulted in inclusion of shareholder nominees as management nominees and cautioned that the proposal could discourage constructive dialogue between companies and shareholders.[334] Three commenters opposed limits on some or all relationships between the company and the nominating shareholder, group, or shareholder nominee.[335] These commenters believed that the Commission should not prohibit agreements between a company and a nominating shareholder or group. They warned that restricting the ability of companies to reach agreements with a nominating shareholder or group would limit the dialogue between companies and investors. One commenter suggested that proposed Rule 14a-18(d) be revised to permit a company to agree not to contest the eligibility of a shareholder nominee.[336] The commenter also suggested that if a company settled a threatened election contest by placing a shareholder nominee on the board, additional shareholder nominees should not be permitted for a specified period of time.

After careful review of the comments, we continue to believe that it is appropriate to provide that a nominating shareholder or group will not be eligible to have a nominee or nominees included in a company's proxy materials under Rule 14a-11 if the nominating shareholder, group, or any member of the nominating shareholder group, has any agreement with

333 See letter from USPE.

334 See letters from BRT; Seven Law Firms; Society of Corporate Secretaries.

335 See letters from ABA; Steve Quinlivan ("S. Quinlivan"); Verizon.

336 See letter from S. Quinlivan.

the company with respect to the nomination. We have revised the rule to make it clearer that this is an eligibility condition by listing it as a condition in the rule, rather than only a representation required in Schedule 14N.[337] We have incorporated, as proposed, the instruction with respect to unsuccessful negotiations (i.e. negotiations that do not result in an agreement) regarding whether a company is required to include a nominee in order to make clear that those negotiations would not be disqualifying.

As described above, a nominating shareholder or group will not be eligible to use Rule 14a-11 if there is an agreement with the company regarding the nomination of the nominee.[338] When a nominating shareholder or group files its Schedule 14N, this requirement will apply, and the certification required by Schedule 14N will have the effect of confirming that there are no agreements. We believe this is an important safeguard to prevent actions that could undermine the purpose of the rule. If, after the Schedule 14N is filed, a nominating shareholder or group reached an agreement with the company for the nominee to be included in the company's proxy materials as a management nominee, the nominating shareholder or group would no longer be proceeding under Rule 14a-11. Consequently, there is no need to revise the "no agreements" requirement in Rule 14a-11 to address that fact pattern.

Although we are adopting the "no agreements" requirement largely as proposed, we are persuaded by commenters that we should revise our final rules so that they do not unnecessarily

---

337 We note that a nominating shareholder or members of a nominating shareholder group will be required to provide a certification in the Schedule 14N that the requirements of Rule 14a-11 are satisfied, which will include the "no agreements" requirement. A nominating shareholder or member of a nominating shareholder group will be liable, pursuant to Rule 14a-9(c), for a false or misleading certification provided in Schedule 14N.

338 See Rule 14a-11(b)(7). See also Rule 14a-11(d)(7) which clarifies that if a nominee, nominating shareholder or any member of a nominating group has an agreement with the company or an affiliate of the company regarding the nomination of a candidate for election, other than as specified in Rule 14a-11(d)(5) or (6), any nominee or nominees from such shareholder or group shall not be counted in calculating the number of shareholder nominees for purposes of Rule 14a-11(d).

discourage constructive dialogue between shareholders and companies. However, we believe this concern is more appropriately addressed in the method of calculation of the maximum number of permissible nominees, and the question of whether that number should include management nominees that were originally put forward as shareholder nominees under Rule 14a-11. Our revisions to that provision are discussed in Section II.B.6. below.

f. No requirement to attend the annual or special meeting

Under Rule 14a-11 as proposed, a nominating shareholder or group would have no obligation to attend the annual or special meeting at which its nominee or nominees is being presented to shareholders for a vote. We received comment on the Proposal, however, suggesting that we require a nominating shareholder or group, or a qualified representative of the nominating shareholder or group, to attend the company's shareholder meeting and nominate its director candidate(s) in person.[339] One commenter explained that this requirement would be consistent with state law requirements for nominations and many companies' advance notice bylaws.[340] Another commenter suggested that, as required under Rule 14a-8(h)(3) for shareholder proposals, if the nominating shareholder or group (or its qualified representative) fails, without good cause, to appear and nominate the candidate, the company should be permitted to exclude from its proxy materials for the following two years all nominees submitted by that nominating shareholder or members of the nominating group.[341]

We have decided not to include a requirement that the nominating shareholder or qualified representative appear at the meeting and present the nominee because we believe that

339 See letters from ABA; BRT.

340 See letter from ABA.

341 See letter from BRT.

shareholders will have sufficient incentive to take steps to assure that their nominees are voted on at the meeting, whether through attending the meeting or sending a qualified representative, or through other arrangements with the company, and we do not want to add unnecessary complexities and burdens to the rule. We note that state law will control what happens if a candidate is not nominated at the meeting because the person supporting the candidate does not attend the meeting or make other arrangements.[342]

g. No limit on resubmission

Under the Proposal, a nominating shareholder's or group's ability to use Rule 14a-11 would not be impacted by prior unsuccessful use of the rule. In response to our request for comment, a number of commenters supported a provision that would render a nominating shareholder or group ineligible to use Rule 14a-11 for a period of time (e.g., one, two, or three years) if the nominating shareholder or group presented a nominee who failed to receive significant shareholder support in a previous election (e.g., 10%, 15%, 25%, or 30%).[343] One commenter indicated that this resubmission threshold would have a dual purpose: (i) when the nominee failed to garner significant support from shareholders, it would be inappropriate to

---

342 While state statutes are largely silent on the subject of presentation of nominations, motions or other business at meetings of shareholders, the chairman of the meeting typically has broad discretionary authority over its conduct (see, e.g., Model Business Corporation Act § 7.08(b)). As we understand, it is prevailing practice for the chairman to invite nominations of directors from the meeting floor. See David A. Drexler, et al., Delaware Corporation Law and Practice, ¶ 24.05[3] (2009 supp.); Carroll R. Wetzel, Conduct of a Stockholders' Meeting, 22 BUS. LAW. 303, 313-314 (1967); American Bar Association Corporate Laws Committee and Corporate Governance Committee, Business Law Section, Handbook for the Conduct of Shareholders' Meetings (2d ed. 2010) at 151.

343 See letters from 26 Corporate Secretaries; ABA; ADP; Advance Auto Parts; Aetna; Alcoa; AllianceBernstein; Anadarko; Applied Materials; Avis Budget; Boeing; BorgWarner; BRT; Burlington Northern; Caterpillar; Chevron; CIGNA; Cleary; Comcast; CSX; Darden Restaurants; Deere; Dewey; DTE Energy; Dupont; Eaton; FedEx; Florida State Board of Administration; FMC Corp.; FPL Group; General Mills; Headwaters; Intel; ITT; JPMorgan Chase; Kirkland & Ellis; E.J. Kullman; Leggett; P. Neuhauser; Northrop; PepsiCo; Pfizer; Protective; RiskMetrics; Sara Lee; Seven Law Firms; SIFMA; Society of Corporate Secretaries; Southern Company; T. Rowe Price; tw telecom; U.S. Bancorp; Wells Fargo; Weyerhaeuser; Whirlpool; Xerox.

require the company to expend resources repeatedly to include the unsuccessful nominee;[344] and (ii) other shareholders would have an opportunity to submit their own nominations.[345] On the other hand, some commenters opposed a provision that would render a nominating shareholder or group ineligible to use Rule 14a-11 for a period of time if the nominating shareholder or group presented a nominee who failed to receive a specified percentage of shareholder votes at a previous election.[346] One commenter pointed out that management nominees are not subject to similar limits.[347] After consideration of the comments we do not believe it is necessary or appropriate to include a limitation on use of Rule 14a-11 by nominating shareholders or groups that have previously used the rule. We continue to believe that such a limitation would not facilitate shareholders' traditional state law rights and would add unnecessary complexity to the rule's operation.

5. Nominee Eligibility under Exchange Act Rule 14a-11

a. Consistent with applicable law and regulation

Under the Proposal, a company would have been able to exclude a nominee where the nominee's candidacy or, if elected, board membership would violate controlling state law, federal law, or rules of a national securities exchange or national securities association (other than rules of a national securities exchange or national securities association that set forth requirements regarding the independence of directors, which the rule addresses separately) and

344 See discussion in Section II.B.5.e. below with regard to resubmission of unsuccessful shareholder nominees.

345 See letter from Society of Corporate Secretaries.

346 See letters from CII; Norges Bank; Solutions; USPE; Walden.

347 See letter from CII.

such violation could not be cured.[348]

Commenters generally supported this requirement.[349] These commenters suggested that the rule require the nominating shareholder or group to provide any information necessary to ensure compliance with these laws or regulations. Some of these commenters noted that there are various federal and state laws that govern or affect the ability of a person to serve as a director, such as the Federal Power Act and related FERC regulations, federal maritime laws and regulations, Department of Defense security clearance requirements, Department of State export licensing requirements, bank holding company laws, FCC licensing requirements, state gaming licensing requirements, Federal Reserve regulations, FDIC regulations, U.S. government procurement regulations, Section 8 of the Clayton Act, Section 1 of the Sherman Act, and Section 5 of the Federal Trade Commission Act.[350] One commenter, for example, explained that banking laws and regulations impose their own eligibility standards for directors.[351] One commenter stated more generally that it does not oppose the proposed requirement that a company would not have to include a shareholder nominee in its proxy materials if the nominee's candidacy or election would violate federal law or state law and such violation could not be cured.[352] It noted, however, that "there is not a lot of law" that disqualifies a person from serving as a director and described concerns about state law barriers as a "red herring."

---

348 In the Proposing Release, we described an exception from the provision if the violation could be cured. We inadvertently did not include language for this provision in the proposed regulatory text.

349 See letters from 26 Corporate Secretaries; American Bankers Association; Association of Corporate Counsel; BRT; Dewey; Emerson Electric; Financial Services Roundtable; GE; Intel; JPMorgan Chase; O'Melveny & Myers; Protective; Sidley Austin; Tenet; Xerox.

350 See letters from American Bankers Association; BRT; Emerson Electric; GE; O'Melveny & Myers; Sidley Austin; Tenet.

351 See letter from American Bankers Association.

352 See letter from CII.

On the other hand, one commenter stated that a company should not be allowed to exclude a shareholder nominee from its proxy materials because the election of the nominee would result in the violation of state law or federal law.[353] The commenter explained that allowing such exclusion "would make it prohibitively expensive for most shareowners to submit nominations under the proposed rule. It would lead to many shareowner nominees being disqualified based on technicalities or invented legal theories."

After considering the comments, we continue to believe that Rule 14a-11 should address federal law, state law, and applicable exchange requirements (other than the requirements related to objective independence standards, which are addressed separately under the rule). Requiring compliance with basic legal requirements regarding nominees should encourage nominating shareholders to bring forward candidates that may be more likely to be able to be elected and serve as directors, and should reduce disruption and expense for companies of opposing a candidate who could not serve on the board if elected because their service would violate law.[354] Thus, under Rule 14a-11, a nominee will not be eligible to be included in a company's proxy materials if the nominee's candidacy, or if elected, board membership will violate federal law, state law, or applicable exchange requirements, if any,[355] other than those related to independence standards, and such violation could not be cured during the time period provided in the rule.[356]

---

353 See letter from USPE.

354 We note that this condition would not disqualify a nominee unless the violation could not be cured during the time period in which a nominating shareholder or group has to respond to a company's notice of deficiency.

355 We are not aware of other exchange requirements related to director qualifications, but should an exchange adopt new requirements, this provision would apply.

356 As discussed in Section II.B.9.b., a company that intends to exclude a shareholder nominee or nominees will be required to notify the nominating shareholder or group of the basis on which the company plans to exclude the nominee or nominees and the nominating shareholder or group will have 14 calendar days to cure the deficiency (where curable).

b. Independence requirements and other director qualifications

Under the Proposal, the nominating shareholder or each member of the nominating shareholder group would have been required to provide a representation that the shareholder nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the company, if any, or, in the case of a registrant that is an investment company, a representation that the nominee is not an "interested person" of the registrant, as defined in Section 2(a)(19) of the Investment Company Act.[357] For registrants other than investment companies, the representation would not have been required in instances where a company is not subject to the requirements of a national securities exchange or a national securities association. We also noted that exchange rules regarding director independence generally include some standards that depend on an objective determination of facts and other standards that depend on subjective determinations.[358] Under our Proposal, the representation would not cover subjective determinations. Also, the representation would not cover additional independence or director qualification requirements imposed by a board on its

---

357 Pursuant to proposed Rule 14a-18(c), a nominating shareholder or group would include a representation in its notice to the company that the nominee satisfies the existing independence or "interested person" standards.

358 See proposed Rule 14a-18(c) and the Instruction to paragraph (c). For example, the NYSE listing standards include both subjective and objective components in defining an "independent director." As an example of a subjective determination, Section 303A.02(a) of the NYSE Listed Company Manual provides that no director will qualify as "independent" unless the board of directors "affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company)." On the other hand, Section 303A.02(b) provides that a director is not independent if he or she has any of several specified relationships with the company that can be determined by a "bright-line" objective test. For example, a director is not independent if "the director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $120,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service)." Similar to the NYSE rules, the NASDAQ Listing Rules require a company's board to make an affirmative determination that individuals serving as independent directors do not have a relationship with the company that would impair their independence. The NASDAQ rules include certain objective criteria, similar to those provided in NYSE Section 303A.02(b), for making such a determination. See NASDAQ Rule 5605(a)(2) and IM-5605.

independent members, although we requested comment on whether it should.

Commenters generally supported the requirement regarding the objective independence standards.[359] Institutional and other investors agreed that nominating shareholders should not be required to represent that nominees satisfy the subjective independence standards of the relevant exchange or national securities association, and also agreed that they should not be subject to any director independence or qualification standards set by the board or the nominating committee.[360] One of these commenters expressed agreement with the Proposal that where a company is not subject to the independence standards of an exchange or national securities association, the nominating shareholder or group should not be required to provide disclosure concerning whether nominees would be independent.[361] To the extent that a company has independence standards that are more stringent than those of an exchange, then the commenter would not oppose the application of those standards to the shareholder nominee as long as the standards are objective. Two commenters expressed the view that the Section 2(a)(19) test is more appropriate for investment company directors than the independence standard applied to non-investment company directors,[362] with one noting that the Section 2(a)(19) test is tailored to the types of

---

359 See letters from ABA; ACSI; Advance Auto Parts; Aetna; Alaska Air; Alcoa; Anadarko; Avis Budget; Biogen; The Board Institute ("Board Institute"); BorgWarner; BRT; Burlington Northern; Callaway; CalSTRS; Caterpillar; CIGNA; Cleary; Comcast; Con Edison; CII; COPERA; CSX; Cummins; Darden Restaurants; Deere; Dewey; DTE Energy; Eaton; Edison Electric Institute; Einstein Noah Restaurant Group, Inc. ("Einstein Noah"); Emerson Electric; ExxonMobil; FedEx; FMC Corp.; FPL Group; General Mills; A. Goolsby; Headwaters; Home Depot; Honeywell; Horizon Lines, Inc. ("Horizon"); C. Horner; IBM; Intel; JPMorgan Chase; Keating Muething; E.J. Kullman; LUCRF; McDonald's; Merchants Terminal; Metlife; P. Neuhauser; Norfolk Southern; Northrop; Office Depot; O'Melveny & Myers; P&G; PepsiCo; Pfizer; Protective; S&C; Seven Law Firms; Sidley Austin; SIFMA; Society of Corporate Secretaries; Southern Company; Tenet; Tesoro; Theragenics; TI; TIAA-CREF; Tompkins; tw telecom; UnitedHealth; U.S. Bancorp; ValueAct Capital; Verizon; Wells Fargo; Weyerhaeuser.

360 See letters from ACSI; CalSTRS; CII; COPERA; LUCRF; P. Neuhauser; TIAA-CREF; ValueAct Capital.

361 See letter from CII.

362 See letters from ABA II; ICI.

conflicts of interest faced by investment company directors and that the Section 2(a)(19) provision is critical given that investment companies must have a specified percentage of independent directors to be able to comply with certain statutory and regulatory requirements.[363]

A significant number of commenters from the corporate community stated generally that shareholder nominees should satisfy not just the objective director independence standards of the relevant exchange or national securities associations, but all of the company's director qualifications and independence standards (including, if applicable, more stringent objective independence standards imposed by the board, subjective director independence standards, director qualification standards, board service guidelines, and code of conduct in the company's governance principles and committee charters) applicable to all directors and director nominees.[364] Many commenters warned that exempting shareholder nominees from a company's director independence and qualification standards could cause the company to be exposed to legal issues, lower the quality and diversity of the board, and create difficulties in recruiting qualified directors.[365] Other commenters also believed that exempting shareholder nominees from the subjective director independence standards of the relevant exchange or national securities association would put companies at risk of noncompliance with the exchange's or association's rules regarding independent directors, burden the remaining independent directors

363 See letter from ICI. One commenter stated that the application of the "interested person" standard of Section 2(a)(19) is unnecessary. See letter from Norges Bank.

364 See letters from ABA; Advance Auto Parts; Aetna; Alaska Air; Alcoa; Anadarko; Avis Budget; Biogen; Board Institute; BorgWarner; BRT; Burlington Northern; Callaway; Caterpillar; CIGNA; Cleary; Comcast; Con Edison; CSX; Cummins; Darden Restaurants; Deere; Dewey; DTE Energy; Eaton; Edison Electric Institute; Einstein Noah; Emerson Electric; ExxonMobil; FedEx; FMC Corp.; FPL Group; General Mills; A. Goolsby; Headwaters; Home Depot; Honeywell; Horizon; C. Horner; IBM; Intel; JPMorgan Chase; Keating Muething; E.J. Kullman; McDonald's; Merchants Terminal; Metlife; Norfolk Southern; Northrop; Office Depot; O'Melveny & Myers; P&G; PepsiCo; Pfizer; Protective; S&C; Seven Law Firms; Sidley Austin; SIFMA; Society of Corporate Secretaries; Southern Company; Tenet; Tesoro; Theragenics; TI; Tompkins; tw telecom; UnitedHealth; U.S. Bancorp; Verizon; Wells Fargo; Weyerhaeuser.

365 See letters from Board Institute; BRT; Con Edison; C. Horner; TI; Verizon.

with additional duties by forcing them to serve on more board committees, make it more difficult for companies to recruit the independent directors needed for the board committees, and force companies to increase the size of the board and conduct additional searches for directors qualifying as independent.[366]

After carefully considering the comments, we are adopting the requirement largely as proposed. We believe that the Rule 14a-11 process should be limited to nominations of board candidates who meet any objective independence standards of the relevant securities exchange. While we understand the concerns expressed by many commenters from the corporate community, particularly with respect to the risk of noncompliance with listing standards, we continue to believe that the rule should not extend to subjective independence standards. We note that Rule 14a-11 only addresses when a company must include a nominee in its proxy materials – it does not preclude a nominee from ultimately being subject to any subjective determination of independence for board committee positions. We believe the concerns regarding independent directors being forced to take on additional duties, companies needing to increase the size of the board or conducting additional searches for independent directors are best addressed through disclosure. A company could include disclosure in its proxy materials advising shareholders that the shareholder nominee would not meet the company's subjective criteria, as appropriate. This would provide shareholders with the opportunity to make an informed choice with regard to the candidates for director.

We believe that it is in both the company's and shareholders' interest for the company to continue to meet any applicable listing standards, and requiring that Rule 14a-11 nominees meet the objective independence standards will further that interest. It also should help reduce

366 See letters from Metlife; O'Melveny & Myers; Seven Law Firms; Wells Fargo.

disruption and expense for companies opposing a candidate it believes would cause it to violate applicable listing standards. To clarify that this is an affirmative requirement for Rule 14a-11 nominees, we have revised the rule to include this provision as an eligibility requirement rather than a representation.[367]

A nominating shareholder or group also will be required to provide a statement in Schedule 14N that the nominee or nominees meets the objective independence standards of the applicable exchange rules.[368] For this purpose, the nominee would be required to meet the definition of "independent" that is applicable to directors of the company generally and not any particular definition of independence applicable to members of the audit committee of the company's board of directors.[369] To the extent a rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board (for example, requiring that the board of directors or any group or committee of the board of directors make a determination that the nominee has no material relationship with the listed company), this element of an independence standard would not have to be satisfied.[370] Where a company (other than an investment company) is not subject to the standards of a national securities exchange or national securities association, the requirement would not apply.

While we acknowledge commenters' concerns about nominees not being subject to

---

367 See Rule 14a-11(b)(9).

368 See Item 5(f) of new Schedule 14N.

369 See new instruction to paragraph (b)(9) in Rule 14a-11.

370 The rule addresses only the requirements under Rule 14a-11 to be included in a company's proxy materials – it would not preclude a nominee from ultimately being subject to the subjective determination test of independence for board committee positions. A company could include disclosure in its proxy materials advising shareholders that the shareholder nominee for director would not meet the company's subjective criteria, as appropriate. If a shareholder nominee is elected and the board determines that the nominee is not independent, the board member presumably would be included in the group of non-independent directors for purposes of applicable listing standards.

subjective independence requirements, we believe that including such requirements would create undue uncertainty for shareholders seeking to nominate directors and make it difficult to evaluate the board's conclusion regarding independence. In addition, if a board believes a nominee would not be considered independent under its subjective independence evaluation, it could describe its reasons for that view in its proxy statement. In this regard, we note that in a traditional proxy contest an insurgent's nominee or nominees do not have to comply with any requirements, including the independence requirements applicable to the company.[371] We also agree with the commenter who noted that the "interested person" test under Section 2(a)(19) is tailored to the types of conflicts of interest faced by investment company directors and that the Section 2(a)(19) provision is critical given that investment companies must have a specified percentage of independent directors to be able to comply with certain statutory and regulatory requirements.[372] Accordingly, under the final rule, a company will be required to include a shareholder nominee in its proxy materials if the shareholder nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the company, if any, or, in the case of a company that is an investment company, the nominee is not an "interested person" of the registrant, as defined in Section 2(a)(19) of the Investment Company Act.[373]

As noted above, we did not propose to require a shareholder nominee submitted pursuant

371 If a shareholder nominee did not meet the independence requirements of a listed market, that listed market may provide for a cure period during which time the company may resolve this deficiency. See, e.g., NASDAQ Rule 5810(c)(3)(E) ("If a Company fails to meet the majority board independence requirement in Rule 5605(b)(1) due to one vacancy, or because one director ceases to be independent for reasons beyond his/her reasonable control, the Listing Qualifications Department will promptly notify the Company and inform it has until the earlier of its next annual shareholders meeting or one year from the event that caused the deficiency to cure the deficiency.").

372 See letter from ICI.

373 See new Rule 14a-11(b)(9).

to Rule 14a-11 to be subject to the company's director qualification standards. With regard to these standards, we believe that a nominee's compliance with a company's director qualifications is best addressed through disclosure. Under state law, shareholders generally are free to nominate and elect any person to the board of directors, regardless of whether the candidate satisfies a company's qualification requirement at the time of nomination and election.[374] Many commenters recommended a requirement that the shareholder nominee complete the company's standard director questionnaire or otherwise provide information required of other nominees.[375] While we do not believe nominees submitted pursuant to Rule 14a-11 should be required to complete a company's director questionnaire, we are persuaded that information should be provided regarding whether the nominee meets the company's director qualifications, if any. Accordingly, although we have not revised the rule to allow exclusion of nominees who do not meet any director qualification requirements, we have adopted a requirement that a nominating shareholder or group disclose under Item 5 of Schedule 14N whether, to the best of their knowledge, the nominating shareholder's or group's nominee meets the company's director qualifications, if any, as set forth in the company's governing documents.[376] The company also may choose to provide disclosure in its proxy statement about whether it believes a nominee satisfies the company's director qualifications, as is currently done in a traditional proxy contest. Where a company's governing documents establish certain

---

374 See, e.g., Triplex Shoe Co. v. Rice & Hutchins, Inc., 152 A. 342, 375 (Del. 1930). See also 1-13 David A. Drexler et al., Delaware Corporation Law and Practice §13.01 n. 42 (citing Triplex for the proposition that "a bylaw requiring a director to be a stockholder required a director to own stock prior to entering into the office of director, not prior to election").

375 See letters from 26 Corporate Secretaries; Advance Auto Parts; Alaska Air; Anadarko; Aetna; American Express; Association of Corporate Counsel; BorgWarner; BRT; Callaway; Caterpillar; Dewey; DTE Energy; Dupont; Emerson Electric; eWareness; ExxonMobil; Financial Services Roundtable; IBM; ICI; McDonald's; O'Melveny & Myers; PepsiCo; Praxair; Seven Law Firms; Society of Corporate Secretaries; Theragenics; UnitedHealth; U.S. Bancorp; Xerox.

376 See Item 5(e) of new Schedule 14N.

qualifications for director nominees that, consistent with state law, would preclude the company from seating a director who does not meet these qualifications, we believe this would be important disclosure for shareholders.

c. Agreements with the company

As discussed above with regard to the eligibility requirements for a nominating shareholder or group, we recognize that certain limitations of the rule create the potential risk of nominating shareholders or groups acting merely as a surrogate for the company or its management in order to block usage of the rule by another nominating shareholder or group.[377] Under the Proposal as it relates to nominee eligibility, a nominating shareholder or group would have been required to represent that no agreements between the nominee and the company and its management exist regarding the nomination of the nominee.[378] The Proposal included an instruction clarifying that negotiations between a nominating shareholder or group, nominee, and nominating committee or board of a company to have the nominee included in the company's proxy materials, where the negotiations were unsuccessful or were limited to whether the company was required to include the nominee in accordance with Rule 14a-11, would not represent a direct or indirect agreement with the company.[379]

Commenters generally supported this proposed requirement.[380] Most of the comments addressed negotiations or agreements between the nominating shareholder or group and the

---

377 See the discussion in Section II.B.4.e. above regarding relationships or agreements between the nominating shareholder or group and the company and its management.

378 In this regard, we also proposed to require a nominating shareholder or group to represent that no relationships or agreements between the nominee and the company and its management exist. This aspect of the rule is discussed in Section II.B.5.d. below.

379 See instruction to proposed Rule 14a-18(d).

380 See letters from ADP; BRT; Calvert; CFA Institute; CII; Seven Law Firms; TIAA-CREF; USPE.

company rather than the relationship or agreements between a nominee and the company.[381]

Consistent with our approach to agreements with nominating shareholders, we are adopting the requirement that there not be any agreements between the nominee and the company and its management regarding the nomination of the nominee largely as proposed. In this regard, we believe it would undermine the purpose of the rule to allow nominees under Rule 14a-11 to have such agreements with the company because of the potential risk of a nominating shareholder or group acting merely as a surrogate for a company. In order to clarify that this is an affirmative requirement of Rule 14a-11, we have revised the rule to make clear that this is an eligibility condition by listing it as a condition in the rule, rather than only in a representation required in Schedule 14N.

d. Relationship between the nominating shareholder or group and the nominee

We did not propose a requirement that the nominee must be independent or unaffiliated with the nominating shareholder or group, but we requested comment on whether we should include such a requirement.[382] A large number of commenters supported generally an independence requirement that would limit some or all relationships between the nominating shareholder or group and its nominee.[383] Commenters explained that an independence requirement would reduce the risk that a successful shareholder nominee would represent only

---

381 See Section II.B.4.e. above for a further discussion of the comments.

382 The 2003 Proposal included such a requirement. For a discussion of this aspect of the 2003 Proposal and the comments received, see the Proposing Release.

383 See letters from ABA; Advance Auto Parts; Aetna; Alaska Air; Association of Corporate Counsel; Avis Budget; Biogen; Boeing; BorgWarner; Brink's; BRT; Callaway; Caterpillar; CIGNA; Comcast; Cummins; Darden Restaurants; Deere; Dewey; Dupont; Eaton; Eli Lilly; ExxonMobil; FedEx; Financial Services Roundtable; FMC Corp.; FPL Group; General Mills; Headwaters; Honeywell; JPMorgan Chase; E.J. Kullman; Leggett; Norfolk Southern; Office Depot; O'Melveny & Myers; Pax World; Protective; Sara Lee; Seven Law Firms; SIFMA; Society of Corporate Secretaries; Southern Company; Tenet; U.S. Bancorp; Vinson & Elkins LLP ("Vinson & Elkins"); Wells Fargo; Weyerhaeuser.

the nominating shareholder or group, avoid potential disruptions and divisiveness from having "special interest" directors, ameliorate the issue of preserving confidentiality within the boardroom and avoiding misuse of material non-public information, and lessen the likelihood that Rule 14a-11 would be used for change in control attempts.[384]

With regard to the degree of independence needed and types of relationships that should be prohibited, numerous commenters recommended a prohibition on any affiliation between the nominating shareholder or group and the shareholder nominee.[385] Some commenters recommended that Rule 14a-11 prohibit a shareholder nominee from being (1) a nominating shareholder, (2) a member of the immediate family of any nominating shareholder, or (3) a partner, officer, director or employee of a nominating shareholder or any of its affiliates.[386] They noted that a similar limitation was included in the 2003 Proposal. Two commenters recommended that the Commission impose the same restrictions and disclosure requirements that were included in the 2003 Proposal.[387]

One commenter noted the Commission's assertion in the Proposing Release that "such limitations may not be appropriate or necessary" because, if elected, a director would be subject to state law fiduciary duties owed to the company.[388] The commenter, however, expressed skepticism that fiduciary obligations would adequately resolve the issue of "special interest"

384 See letters from ABA; Alaska Air; Eli Lilly; Leggett.

385 See letters from Advance Auto Parts; Aetna; Association of Corporate Counsel; Avis Budget; Boeing; Brink's; CIGNA; Cummins; Deere; Eaton; FedEx; FMC Corp.; FPL Group; General Mills; E.J. Kullman; Pax World; Protective; Sara Lee.

386 See letters from Alaska Air; BorgWarner; Caterpillar; JPMorgan Chase; O'Melveny & Myers; Society of Corporate Secretaries.

387 See letters from BRT; Intel.

388 Letter from BRT.

directors. One commenter would not require independence between the nominating shareholder or group and the nominee if the nominating shareholder or group could use Rule 14a-11 to nominate only one candidate; however, if the nominating shareholder or group is allowed to nominate more than one candidate using Rule 14a-11, then the commenter believed independence between the nominating shareholder or group and the nominees is needed.[389] The commenter asserted that a lack of an independence requirement between multiple nominees and the nominating shareholder could give rise to control issues because the nominees, if elected, could be beholden to a single nominating shareholder or group. In addition, the commenter claimed that a lack of independence could give rise to "single issue" or "special interest" directors, thereby causing balkanization of boards. According to this commenter, if independence is not required, then Schedule 14N should require detailed disclosure about the nature of relationships between the nominating shareholder or group and the nominees.[390]

A few commenters recommended requiring disclosure in the Schedule 14N of any direct or indirect relationships between the nominating shareholder or group and the nominee, including family or employment relationships, ownership interests, commercial relationships and any other arrangements or agreements.[391] One commenter recommended that a nominating shareholder or group provide "[d]isclosure about any agreements or relationships with the Rule 14a-11 nominee other than those relating to the nomination of the nominee."[392]

---

389 See letter from Seven Law Firms.

390 Id. The recommended disclosures included: familial relationships with a nominating shareholder or group member; ownership interests (or other participation) in a nominating shareholder, group member, or affiliates; employment history with a nominating shareholder, group member, or affiliates; prior advisory, consulting or other compensatory relationships with a nominating shareholder, group member, or affiliates; and agreements with a nominating shareholder, group member, or affiliates (other than relating to the nomination).

391 See letters from O'Melveny & Myers; SIFMA; UnitedHealth. See also letter from CII.

392 Letter from IBM.

Other commenters opposed generally any requirement that the nominating shareholder or group be independent from the shareholder nominee.[393] Of these, some commenters recommended the Commission require full disclosure of any affiliations and business relationships instead of an outright prohibition.[394] One commenter noted that no such restriction or prohibition applies to current director candidates, some of whom have various personal and professional links to the company and its executives.[395] Another commenter noted that the NYSE recognized the issue of share ownership when crafting its director independence rules and determined that even significant share ownership should not be dispositive as to a determination of a director's independence.[396] Two commenters opposed a prohibition on any affiliation between the nominating shareholder and its nominee because they believed that fears regarding the election of "special interest" directors are unfounded or exaggerated, as any nominee would have to gain the support of a broad array of shareholders to be elected.[397] One commenter asserted that existing fiduciary duties are an adequate safeguard against "special interest" directors.[398]

We continue to believe that such limitations are not appropriate or necessary. Rather, we believe that Rule 14a-11 should facilitate the exercise of shareholders' traditional state law rights and afford a shareholder or group meeting the requirements of the rule the ability to propose a

393. See letters from Amalgamated Bank; CalSTRS; CFA Institute; CII; COPERA; Nathan Cummings Foundation; P. Neuhauser; Norges Bank; Pershing Square; Relational; RiskMetrics; Solutions by Design ("Solutions"); TIAA-CREF; USPE; B. Villiarmois.

394 See letters from CFA Institute; CII; COPERA; P. Neuhauser; Pershing Square; Relational; USPE; B. Villiarmois.

395 See letter from CII.

396 See letter from Relational.

397 See letters from CII; Nathan Cummings Foundation.

398 See letter from TIAA-CREF.

nominee for director that, in the nominating shareholder's view, better represents the interests of shareholders than those put forward by the nominating committee or board. We note that once a nominee is elected to the board of directors, that director will be subject to state law fiduciary duties and owe the same duty to the corporation as any other director on the board.[399] To the extent a company board is concerned that a director nominee will not represent the views of shareholders, the board could address those points in the company's proxy materials opposing the candidate's election. In addition, we believe the disclosure requirements about the relationships between a nominating shareholder or group and the nominee that we are adopting, combined with the fact that any nominee elected will be subject to fiduciary duties, should help address any "special interest" concerns.

e. No limit on resubmission of shareholder director nominees

Under the Proposal, an individual would not be limited in their ability to stand as a nominee under the rule based on prior unsuccessful nominations under the rule. A number of commenters supported a provision under which a shareholder nominee who failed to receive a specified threshold (e.g., 10%, 15%, 25%, or 30%) of support at a previous election would be ineligible to be nominated again pursuant to Rule 14a-11 for a specified period (e.g., one, two, or three years).[400] One commenter reasoned that "[t]his would allow more shareholders to participate in the process and would motivate them to propose high quality candidates."[401] On the other hand, other commenters opposed a provision under which a shareholder nominee who

---

399 See E. Norman Veasey & Christine T. DiGuglielmo, How Many Masters Can a Director Serve? A Look at the Tensions Facing Constituency Directors, 63 BUS. LAW. 761 (2008).

400 See letters from 26 Corporate Secretaries; ABA; Aetna; Anadarko; BorgWarner; BRT; Burlington Northern; Caterpillar; Cummins; Dewey; Headwaters; JPMorgan Chase; Kirkland & Ellis; Leggett; P. Neuhauser; Northrop; PepsiCo; Pfizer; Protective; Sara Lee; SIFMA; Society of Corporate Secretaries; TIAA-CREF; T. Rowe Price; Xerox.

401 Letter from Northrop.

failed to receive significant support at a previous election would be ineligible to be nominated again pursuant to Rule 14a-11 for a specified period.[402] One commenter reasoned that "[s]imilar resubmission requirements aren't applicable to management's candidates, so they shouldn't apply to candidates suggested by shareowners."[403] We agree with those commenters who opposed a provision that would limit the ability of a shareholder nominee to be nominated based on the level of support received in a prior election. We do not believe that such a limitation would facilitate shareholders' traditional state law rights and would add undue complexity to the rule's operation.

6. Maximum Number of Shareholder Nominees to Be Included in Company Proxy Materials

a. General

Under the Proposal, a company would be required to include no more than one shareholder nominee or the number of nominees that represents 25% of the company's board of directors, whichever is greater.[404] Where the term of a director that was nominated pursuant to Rule 14a-11 continues past the meeting date, that director would continue to count for purposes of the 25% maximum.

As noted in the Proposing Release, we do not intend for Rule 14a-11 to be available for any shareholder or group that is seeking to change the control of the company or to gain more

---

402 See letters from CII; Corporate Library; Dominican Sisters of Hope; First Affirmative Financial Network LLC ("First Affirmative"); Mercy Investment Program; Sisters of Mercy; Social Investment Forum; Tri-State Coalition; Trillium; Ursuline Sisters of Tildonk; USPE.

403 Letter from CII.

404 See proposed Rule 14a-11(d)(1). According to information from RiskMetrics, based on a sample of 1,431 public companies, in 2007, the median board size was 9, with boards ranging in size from 4 to 23 members. Approximately 40% of the boards in the sample had 8 or fewer directors, approximately 60% had between 9 and 19 directors, and less than 1% had 20 or more directors.

than a limited number of seats on the board.[405] The existing procedures regarding contested elections of directors are intended to continue to fulfill that purpose.[406] We also noted that by allowing shareholder nominees to be included in a company's proxy materials, part of the cost of the solicitation is essentially shifted from the individual shareholder or group to the company and thus, all of the shareholders.[407] We do not believe that we should require that an election contest conducted by a shareholder to change the control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11 be funded out of corporate assets.

Some commenters supported generally the proposed limit on the number of shareholder nominees.[408] While agreeing that the Commission's proposed limit on the number of shareholder nominees is needed to ensure a more measured approach towards inclusion of shareholder nominees in company proxy materials, one commenter supported the general principle that shareholders should be entitled to nominate as many directors as necessary to focus the board's attention on optimizing company performance, profitability and sustainable returns.[409] On the other hand, many commenters disagreed with the proposed limit or recommended different limits.[410] Some commenters expressed a general concern that the proposed limit would affect a

405 The final rule clarifies the second part of this requirement by specifying that a nominating shareholder or group may not be seeking to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11.

406 See, e.g., Exchange Act Rule 14a-12(c).

407 In this regard, we anticipate that shareholders seeking election of nominees included in the company's proxy materials may need to engage in solicitation efforts for which they will incur expenses.

408 See letters from CalPERS; CalSTRS; CFA Institute; ICGN; Nathan Cummings Foundation; P. Neuhauser; Norges Bank; Protective; RiskMetrics; TIAA-CREF; T. Rowe Price; WSIB.

409 See letter from CalPERS.

410 See letters from 13D Monitor; ABA; ACSI; Advance Auto Parts; Aetna; Alcoa; Allstate; American Express; Americans for Financial Reform; Association of Corporate Counsel; Avis Budget; Best Buy; J.

significant portion of the board, disrupt the board, facilitate a change in control of the company, and possibly require companies to integrate numerous new directors into their boards each year.[411] Other commenters wanted more shareholder nominees to be allowed because they feared that a single shareholder-nominated director would be ineffective due to the lack of a second for motions at board meetings, hostile board members, possible exclusion from key committees, and being effectively cut out of key discussions.[412] Commenters' suggestions as to the appropriate limitation on the number of shareholder nominees ranged from a limit of one shareholder nominee, regardless of the size of the board,[413] to at least two nominees, but less than a majority of the board.[414] Other commenters recommended various limits ranging from 10% to 15% of the board.[415]

Blanchard; Boeing; BorgWarner; BRT; Burlington Northern; R. Burt; Callaway; CalPERS; Caterpillar; CIGNA; CII; Cleary; CNH Global; Comcast; Concerned Shareholders; COPERA; Cummins; L. Dallas; Darden Restaurants; Deere; Dupont; Eaton; Eli Lilly; Dale C. Eshelman ("D. Eshelman"); ExxonMobil; FedEx; FMC Corp.; FPL Group; Frontier; GE; General Mills; Headwaters; C. Holliday; Honeywell; IBM; ICI; ITT; JPMorgan Chase; J. Kilts; E. J. Kullman; N. Lautenbach; Leggett; C. Levin; Lionbridge Technologies; LUCRF; McDonald's; Motorola; Office Depot; O'Melveny & Myers; OPERS; P&G; Nathan Cummings Foundation; Northrop; Pax World; PepsiCo; Sara Lee; S&C; Schulte Roth & Zabel; Sherwin-Williams; Sidley Austin; SIFMA; Society of Corporate Secretaries; Solutions; SWIB; Teamsters; TI; G. Tooker; tw telecom; Universities Superannuation; U.S. Bancorp; Verizon; USPE; B. Villiarmois; Wachtell; Wells Fargo; Weyerhaeuser; WSIB.

411 See letters from BRT (citing a July 2009 survey showing many companies would have to integrate multiple new directors); CII; Eaton; N. Lautenbach; McDonald's; Sherwin-Williams; Sidley Austin; Society of Corporate Secretaries; G. Tooker; WSIB.

412 See letters from CII; L. Dallas; C. Levin; Nathan Cummings Foundation; Universities Superannuation.

413 See letters from Advance Auto Parts; Avis Budget; BRT; Caterpillar; CIGNA; CNH Global; Comcast; Cummins; Darden Restaurants; Deere; Eaton; Eli Lilly; FedEx; FMC Corp.; FPL Group; Frontier; General Mills; ICI; ITT; E. J. Kullman; N. Lautenbach; Leggett; McDonald's; Office Depot; O'Melveny & Myers; PepsiCo; Sherwin-Williams; TI; G. Tooker; tw telecom; Verizon; Wachtell; Weyerhaeuser.

414 See letters from ACSI; Americans for Financial Reform; CalPERS; CII (stating that while it supports the Commission's proposed limit, shareholders should be allowed to nominate two candidates in all cases); COPERA; C. Levin; LUCRF; Nathan Cummings Foundation; SWIB; Teamsters.

415 See, e.g., Aetna; Association of Corporate Counsel; Barclays; J. Blanchard; BorgWarner; Dewey; ExxonMobil; Headwaters; Honeywell; Lionbridge Technologies; Northrop; Sidley Austin; Society of Corporate Secretaries; U.S. Bancorp.

We carefully considered commenters' concerns regarding the limitation on the number of Rule 14a-11 nominees; however, we are adopting the limitation largely as proposed. We believe the rule we are adopting strikes the appropriate balance in allowing shareholders to more effectively exercise their rights to nominate and elect directors, but does not provide nominating shareholders or groups using the rule with the ability to change control of the company. The limitation on the number of Rule 14a-11 nominees that a company is required to include should also limit costs and disruption as compared to a rule without such a limit. We also believe that a lower threshold, such as 10% or 15%, may result in only one shareholder-nominated director at many companies. In addition, we note that our rule only addresses the inclusion of nominees in the company's proxy materials. After reviewing all of the disclosures provided by the company and the nominating shareholder or group, shareholders will be able to make an informed decision as to whether to vote for and elect a shareholder nominee. We believe that the modifications we are making to the rule, as described below, help to alleviate concerns that the election of shareholder nominees would unduly disrupt the board. As to concerns about the possibility that a single shareholder-nominated director would be ineffective due to actions of other members of the board, the rule is not intended to address the interactions of board members after the election of directors. In this respect, we note that any shareholder-nominated directors and board-nominated directors would be subject to fiduciary duties under state law.

As adopted, Rule 14a-11(d) will not require a company to include more than one shareholder nominee or the number of nominees that represents 25% of the company's board of directors, whichever is greater.[416] Consistent with the Proposal, where a company has a director (or directors) currently serving on its board of directors who was elected as a shareholder

[416] See new Rule 14a-11(d)(1).

nominee pursuant to Rule 14a-11, and the term of that director extends past the date of the meeting of shareholders for which the company is soliciting proxies for the election of directors, the company will not be required to include in its proxy materials more shareholder nominees than could result in the total number of directors serving on the board that were elected as shareholder nominees being greater than one shareholder nominee or 25% of the company's board of directors, whichever is greater.[417] We believe this limitation is appropriate to reduce the possibility of a nominating shareholder or group using Rule 14a-11 as a means to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11 or to effect a change in control of the company by repeatedly nominating additional candidates for director. One commenter requested that we explain how Rule 14a-11 would apply to different board structures, and in particular, classified boards.[418] In the case of a staggered board, the rule provides that the 25% limit will be calculated based on the total number of board seats,[419] not the lesser number that are being voted on because it is the size of the full board, not the number up for election, that would be relevant for considering the effect on control.

We note that in the 2003 Proposal, the Commission proposed to require companies to include a set number of nominees, rather than a percentage of the board.[420] We believe that using

---

417 See new Rule 14a-11(d)(2). This requirement is adopted as it was proposed in Rule 14a-11(d)(2). Depending on board size, 25% of the board may not result in a whole number. In those instances, the maximum number of shareholder nominees for director that a registrant will be required to include in its proxy materials will be the closest whole number below 25%. See the Instruction to paragraph (d)(1).

418 See letter from ABA.

419 See Rule 14a-11(d)(2).

420 Comments on the 2003 Proposal provided a range of views regarding the appropriate number of shareholder nominees. Commenters that supported the use of a percentage, or combination of a set number and a percentage, to determine the number of shareholder nominees suggested percentages ranging from 20% to 35%. See Comment File No. S7-19-03, available at http://www.sec.gov/rules/proposed/s71903.shtml.

a percentage in the rule will promote ease of use and alleviate any concerns that a company may increase its board size in an effort to reduce the effect of a shareholder nominee elected to the board.

We understand the concerns addressed by some commenters that this limitation could result in shareholder-nominated directors being less influential,[421] as well as the concerns of other commenters that the possibility of 25% of the board changing through the Rule 14a-11 process could present significant changes to the board.[422] For the reasons discussed above, we believe the limitation as adopted strikes an appropriate balance and is an appropriate safeguard to assure that the Rule 14a-11 process is not used as a means to effect a change in control.

Though we are adopting this requirement largely as proposed, we have added certain clarifications, which are described below, to address situations at companies where shareholders are able to elect only a subset of the board, revised the standard for determining which nominating shareholder or group will have their nominee or nominees included in the company's proxy materials where there is more than one eligible nominating shareholder or group, and made other modifications designed to facilitate negotiations between companies and nominating shareholders.

b. Different voting rights with regard to election of directors

Several commenters responded to the Commission's request for comment about how to calculate the maximum number of candidates a nominating shareholder or group could nominate under Rule 14a-11 when certain directors are not elected by all shareholders. Some commenters

---

421 See letters from CII; L. Dallas; C. Levin; Nathan Cummins Foundation; Universities Superannuation.

422 See letters from BRT (citing a July 2009 survey showing many companies would have to integrate multiple new directors); CII; Eaton; N. Lautenbach; McDonald's; Sherwin-Williams; Sidley Austin; Society of Corporate Secretaries; G. Tooker; WSIB.

noted that controlled companies are commonly structured with dual classes of stock which allow shareholders of the non-controlling class of stock to elect a set number of directors that is less than the full board.[423]

In the context of a company where shareholders are only entitled to elect a subset of the total number of directors, the rule as proposed potentially would have allowed shareholders to nominate more candidates than may be elected by the nominating shareholders. Two commenters argued that Rule 14a-11 should be modified so that the maximum number of shareholder nominees is based on the number of directors that may be elected by the class of securities held by the shareholders making the nomination, as opposed to the number of total directors.[424] Another commenter urged us to revise Rule 14a-11 so that it would be limited to a percentage of the number of directors that are elected by the public shareholders (rather than a percentage of all directors) and would not apply to directors that are elected by shareholders of a class of stock having a right to nominate and elect a specified number or percentage of directors, or preferred shareholders having such right as a result of the company's failure to pay dividends.[425] Another commenter argued that, as proposed, Rule 14a-11 would not allow companies with multiple classes of voting shares the ability to make choices about how to best implement access to the company's proxy to fit their capital structure.[426] One commenter suggested that Rule 14a-11 address how it would apply to companies with multiple classes of stock to prevent shareholders from using the rule to change control of the class of directors those

423 See letters from ABA; Duane Morris; Media General; New York Times.

424 See letters from Media General; New York Times.

425 See letter from Sidley Austin.

426 See letter from BRT.

shareholders have the right to elect.[427] Other commenters, by contrast, believed that the maximum number of nominees that companies should be required to include should be based on the total number of director seats, regardless of whether a class of shares only gets to elect a subset of the board.[428]

We also sought comment on how to calculate the maximum number of nominees where the company is contractually obligated to permit a certain shareholder or group to elect a set number of directors to the board. Commenters' views differed on how to calculate the maximum number of nominees a shareholder or shareholder group may nominate in that case. Some commenters believed that the maximum number of nominees should be based on the total board size, regardless of whether a company has granted rights to nominate.[429] One such commenter noted that if Rule 14a-11 contained an exception for board seats subject to contractual rights, companies would have an incentive to enter into contractual agreements in order to evade its application.[430] Other commenters, however, asserted that the maximum number of nominees that shareholders should be permitted to nominate under Rule 14a-11 should be limited to 25% of the "free" seats on the board – that is, only those board seats that are not subject to a contractual nomination right that existed as of the date of the submission and filing of a Schedule 14N.[431] These commenters suggested taking board seats subject to contractual nomination rights "off the table" and basing the 25% calculation on the number of nominees that the nominating committee is free to name. One such commenter remarked that unless board seats subject to contractual

---

427 See letter from Media General.

428 See letters from CII; P. Neuhauser.

429 Id.

430 See letter from P. Neuhauser.

431 See letters from Seven Law Firms; Sidley Austin; ValueAct Capital.

nomination rights are excluded, companies may be limited in their ability to offer contractual nominating rights to shareholders without running a heightened risk of change of control, which could result in increased costs of capital and a decrease in the number of strategic alternatives.[432]

We believe that the maximum number of candidates a shareholder can nominate using Rule 14a-11 at companies with multiple classes of stock should be based on the total board size, as is the case at other companies. Thus, we are adopting this requirement as proposed. We believe the changes we are adopting with regard to calculating ownership and voting power, as discussed above, should address concerns about the possibility that the rule could be used to change control of the company or to affect the rights of shareholders as established by a particular company's capital structure.[433] Where shareholders have the right to elect a subset of the full board, however, we believe it is appropriate to provide that the maximum number of nominees a company may be required to include under Rule 14a-11 may not exceed the number of director seats the class of shares held by the nominating shareholder is entitled to elect.[434] We believe the right to nominate is an integral part of the right to elect, therefore we are linking the ability under Rule 14a-11 for a shareholder to nominate directors to instances in which the shareholder can elect directors. Limiting the number of nominations to the number of director seats the class of shares held by the nominating shareholder is entitled to elect presumably would allow to be fully expressed the views of the shareholder about who should sit in the director seats in respect of which the shareholder has nomination rights.

The shareholder nomination provisions in Rule 14a-11 are available only for holders of

---

432 See letter from Seven Law Firms.

433 See Section II.B.4.b. above.

434 See new Rule 14a-11(d)(3).

classes of securities that are subject to the Exchange Act proxy rules, provided that a company is otherwise subject to the rule. If a company subject to Rule 14a-11 has multiple classes of eligible securities, however, the maximum number of candidates a shareholder can nominate will be determined based on the number of director seats the class of shares held by the nominating shareholder is entitled to elect.[435]

c. Inclusion of shareholder nominees in company proxy materials as company nominees

As discussed in Section II.B.4.e. above, commenters expressed concern that the rule, as proposed, might discourage constructive dialogue between shareholders and companies.[436] These commenters noted that companies would be discouraged from discussing potential board candidates with shareholders planning to use Rule 14a-11 and including them as management nominees because such nominees would not reduce the maximum number of shareholder nominees that the company would be required to include under Rule 14a-11. Subject to certain safeguards, we believe our rule should not discourage dialogue between nominating shareholders and companies and agree that the rule, as proposed, could have the effect of discouraging constructive dialogue if shareholder nominees nominated by a company as a result of that dialogue do not count toward the maximum number of shareholder nominees a company is required to include in its proxy materials. Consequently, under our final rule, where a company negotiates with the nominating shareholder or group that has filed a Schedule 14N before beginning any discussion with the company about the nomination and that otherwise would be eligible to have its nominees included in the company's proxy materials, and the company agrees to include the nominating shareholder's or group's nominees on the company's proxy card as

435 See new Rule 14a-11(d)(3).

436 See letters from BRT; Seven Law Firms; Society of Corporate Secretaries.

company nominees, those nominees will count toward the 25% maximum set forth in the rule.[437] As noted, this would only apply where the nominating shareholder or group has filed its notice on Schedule 14N before beginning discussions with the company. Although this limitation may reduce somewhat the utility of this provision, we believe limiting the treatment to situations in which the nominating shareholder or group has filed a Schedule 14N will reduce the possibility that this exception is used by a company to avoid having to include shareholder director nominees submitted by shareholders or groups of shareholders that are not affiliated with or not working on behalf of the company.

In the Proposing Release, we requested comment as to whether it would be appropriate for the rule to take into account incumbent directors who were nominated pursuant to Rule 14a-11 for purposes of determining the maximum number of shareholder nominees, or whether there should be a different means to account for such incumbent directors. One commenter argued that incumbent Rule 14a-11 directors should not count towards the 25% limit.[438] It reasoned that, once elected, the Rule 14a-11 director represents all shareholders and that future use of Rule 14a-11 by other shareholders should not be restricted. A number of commenters stated that incumbent Rule 14a-11 directors should count towards the maximum number of shareholder nominees allowed under the rule,[439] with some suggesting that this should be the case in limited circumstances, such as when a Rule 14a-11 director is re-nominated by the board or as long as

437 See new Rule 14a-11(d)(4). In this regard, we note that we would view such an agreement as a termination of a Rule 14a-11 nomination. Thus, the nominating shareholder or group would be required to file an amendment to Schedule 14N to disclose the termination of the nomination as a result of the agreement with the company regarding the inclusion of the nominee or nominees. See Item 7 of Schedule 14N and Rule 14n-2.

438 See letter from Florida State Board of Administration.

439 See letters from ABA; Aetna; American Express; BorgWarner; BRT; Chevron; Cleary; Davis Polk; DTE Energy; Dupont; Edison Electric Institute; Eli Lilly; ExxonMobil; FPL Group; Home Depot; ICI; JPMorgan Chase; Metlife; P. Neuhauser; Pfizer; Protective; RiskMetrics; S&C; Seven Law Firms; Sidley Austin; SIFMA; Society of Corporate Secretaries; Verizon; Vinson & Elkins; Wells Fargo.

the director continues on the board.[440] Commenters expressed concerns that the method of calculating the maximum number of directors subject to Rule 14a-11 nominations – which as proposed would not include directors previously elected following a Rule 14a-11 nomination unless they are nominated again by a shareholder using Rule 14a-11 – would not encourage boards to integrate these directors.[441] Some commenters asserted that failing to count such a director toward the 25% limit would cause boards to be disinclined to include these directors as company nominees in future elections.[442] They viewed this as counterproductive to efficient board integration and functioning.

While we appreciate commenters' views, we are not persuaded that it is appropriate to provide an exception to the general method of calculating the maximum number of Rule 14a-11 nominees in the case of a shareholder-nominated incumbent director that is re-nominated by the company. As noted previously, by adopting Rule 14a-11 we are seeking to facilitate shareholders' ability under state law to nominate and elect directors, not necessarily to enhance shareholder representation on the board. We do not believe that a Commission rule is needed to facilitate the working relationship between the shareholder-nominated director and the company-nominated directors, or to provide an incentive for the board to integrate the shareholder-nominated director into its activities. To the extent that a shareholder nominee is elected to the board, the company-nominated directors and the shareholder-nominated director will have a fiduciary duty to act in the best interests of the company and its shareholders.

---

440 See letters from P. Neuhauser; RiskMetrics.

441 See letters from ABA; BRT; Seven Law Firms.

442 See letters from Davis Polk; Society of Corporate Secretaries.

7. Priority of nominations received by a company

a. Priority when multiple shareholders submit nominees

Proposed Rule 14a-11(d)(3) addressed situations where more than one shareholder or group would be eligible to have its nominees included in the company's form of proxy and disclosed in its proxy statement pursuant to the proposed rule. In those situations, the company would have been required to include in its proxy materials the nominee or nominees of the first nominating shareholder or group from which it receives timely notice of intent to nominate a director pursuant to the rule, up to and including the total number of shareholder nominees required to be included by the company. We proposed this standard because we believed that there would be a benefit to enabling companies to begin preparing their proxy materials and coordinating with the nominating shareholder or group immediately upon receiving an eligible nomination rather than requiring companies to wait to see whether another nomination from a larger nominating shareholder or group was submitted before the notice deadline.

Commenters were almost uniformly opposed to the proposed "first-in" standard. A large number of commenters expressed general opposition to the proposed first-in approach, with many presenting their own recommendations.[443] Commenters expressed concern that the first-in

---

443 See letters from 13D Monitor; 26 Corporate Secretaries; ABA; ACSI; Advance Auto Parts; Aetna; AFL-CIO; AFSCME; Allstate; Alston & Bird; Amalgamated Bank; American Bankers Association; Anadarko; Applied Materials; Avis Budget; Blue Collar Investment Advisors ("BCIA"); Best Buy; Boeing; BorgWarner; Brink's; BRT; Burlington Northern; CalPERS; CalSTRS; Caterpillar; CFA Institute; Chevron; CIGNA; CII; Cleary; Con Edison; COPERA; Corporate Library; CSX; Cummins; Darden Restaurants; Deere; Devon; Dewey; T. DiNapoli; Dominican Sisters of Hope; DuPont; Eaton; Emerson Electric; ExxonMobil; FedEx; Financial Services Roundtable; First Affirmative; Florida State Board of Administration; FMC Corp.; FPL Group; Frontier; General Mills; A. Goolsby; Honeywell; IAM; IBM; ICI; Intel; JPMorgan Chase; Kirkland & Ellis; C. Levin; Leggett; LIUNA; LUCRF; Marco Consulting; J. McCoy; McDonald's; Joel M. McTague ("J. McTague"); MeadWestvaco; Mercy Investment Program; Metlife; Motorola; D. Nappier; Nathan Cummings Foundation; P. Neuhauser; Norfolk Southern; Norges Bank; Office Depot; OPERS; PACCAR Inc. ("PACCAR"); Pershing Square; PepsiCo; Pfizer; S. Quinlivan; RacetotheBottom; RiskMetrics; Ryder; Sara Lee; Social Investment Forum; Seven Law Firms; Shearman & Sterling; Sheet Metal Workers; Sidley Austin; SIFMA; Sisters of Mercy; Society of Corporate Secretaries; Sodali; Southern Company; SWIB; Teamsters; Tenet; TI; TIAA-CREF; Tri-State Coalition; Trillium; T. Rowe Price; Textron; tw telecom; Universities Superannuation; Ursuline Sisters of Tildonk;

approach would rush shareholders to submit nominations.[444] One commenter worried that even if the Commission included a window period for submission of shareholder nominees in the final rule, the first-in approach would encourage a race to file, discourage constructive dialogue between shareholders and management, and encourage a "gamesmanship" attitude among possible nominating shareholders or groups.[445] Another commenter argued that the first-in approach would undercut the Commission's stated objectives in proposing Rule 14a-11.[446] One commenter worried that the "first in" approach would favor large shareholders, who have greater resources to prepare their submission materials, over small shareholders who must aggregate to reach the ownership threshold and need to pool resources to prepare their submission materials.[447]

Some commenters expressed general concern about how companies should handle multiple nominations received on the same date.[448] Two commenters worried that it would be difficult for companies to determine which nomination was received first because nominations could be submitted by various methods (e.g., fax transmission, mail, hand delivery) or arrive on the same date.[449] Another commenter feared that a company that receives several nominations on the same date could choose the nomination submitted by shareholders friendly to management.[450]

U.S. Bancorp; USPE; ValueAct Capital; Verizon; Wachtell; Walden; Wells Fargo; Weyerhaeuser; Whirlpool; WSIB; Xerox.

444 See letters from ABA; BRT; Con Edison; First Affirmative; C. Levin; Verizon.

445 Letter from ABA.

446 See letter from BRT.

447 See letter from Con Edison.

448 See letters from IBM; S. Quinlivan; USPE; Verizon; Xerox.

449 See letters from IBM; Verizon.

450 See letter from USPE.

Many commenters that opposed the first-in approach suggested alternatives. Of these, the majority preferred to give priority to the largest shareholder or group that submits a nomination.[451] Noting that the 2003 Proposal included this standard and that it received the most support, one commenter argued that what matters most is not who is the fastest to nominate but which shareholder or group has the "greatest stake in the director election and, ultimately, the long-term performance of the company" (with the added benefits of avoiding "gamesmanship" and "administrative challenges").[452] Further, commenters believed that an approach based on the largest holdings would provide sufficient certainty because the number of shares of the largest shareholder or group could be determined from the Schedule 14N filing.[453]

Commenters presented a wide range of views or recommendations for determining priority. Some commenters suggested that when the largest shareholder or group nominates fewer than the maximum number of nominees allowed under Rule 14a-11, then the second largest shareholder or group should have the right to have its nominees included (up to the

451 See letters from 13D Monitor; 26 Corporate Secretaries; ABA (recommending this approach as one of several recommendations); ACSI; Advance Auto Parts; Aetna; AFL-CIO; AFSCME; Allstate; Amalgamated Bank; Anadarko; Applied Materials; Avis Budget; BCIA; Best Buy; Boeing; BorgWarner; Burlington Northern; CalPERS; CalSTRS; Caterpillar; CFA Institute; Chevron; CIGNA (recommending this approach as an alternative to another recommendation that the shareholder that held the shares the longest be given priority); CII; Cleary; Con Edison; COPERA; Corporate Library; Cummins; Darden Restaurants; Deere; Devon; Dominican Sisters of Hope; DuPont; Eaton; Emerson Electric; ExxonMobil; FedEx; Financial Services Roundtable; First Affirmative; Florida State Board of Administration (supporting this approach as an alternative to the first-in approach); FMC Corp.; Frontier; A. Goolsby; IAM; ICI; JPMorgan Chase; Kirkland & Ellis; C. Levin; Leggett; LIUNA; LUCRF; Marco Consulting; J. McCoy; McDonald's; J. McTague; Mercy Investment Program; Metlife; D. Nappier; Nathan Cummings Foundation; P. Neuhauser; Norfolk Southern; Office Depot; PACCAR; Pershing Square; PepsiCo; Pfizer; RiskMetrics; Ryder; Sara Lee; Shamrock; Social Investment Forum; Sodali; Seven Law Firms; Shearman & Sterling; Sheet Metal Workers; Sidley Austin; SIFMA; Sisters of Mercy; Society of Corporate Secretaries; Southern Company; SWIB; Teamsters; Tenet; TI; TIAA-CREF; Tri-State Coalition; Trillium; T. Rowe Price; Textron; tw telecom; Universities Superannuation; Ursuline Sisters of Tildonk; U.S. Bancorp; Verizon; Wachtell; Walden; Wells Fargo; Whirlpool; WSIB.

452 Letter from CII.

453 See letters from CII; Society of Corporate Secretaries.

maximum number allowable), and so on.[454] Commenters also suggested that a nominating shareholder or group be required to "rank" their nominees in the order of preference to facilitate any necessary "cutbacks."[455]

A few commenters stated that in the case of competing nominations submitted by shareholders with equally-sized holdings, the shareholder that held the shares for the longest period of time should be allowed to include its nominees.[456] Two commenters recommended that when determining the order of priority, an individual shareholder should have priority over a nominating group.[457]

One commenter recommended that nominees be ordered in accordance with the largest qualifying shareholdings, but subject to the qualification that the Commission impose a cap on either the permitted number of members in a nominating group or on the aggregate holdings of a nominating group and limit each nominating shareholder or group to only one Rule 14a-11 nomination at an annual meeting.[458] If shareholders are not limited to one nomination, then companies should be allowed to order the nominees based on the largest holdings. Alternatively, the commenter recommended awarding Rule 14a-11 nomination slots first to the nominating shareholder or group with the largest holdings, next to the nominating shareholder or group with the longest holding period, then to the next largest holder, and so on.

One commenter stated that priority should be given to the largest nominating shareholder

---

454 See letters from Amalgamated Bank; CII; COPERA; P. Neuhauser; Protective; T. Rowe Price.

455 See letters from Amalgamated Bank; CFA Institute; CII; COPERA; P. Neuhauser; Protective; T. Rowe Price.

456 See letters from Allstate; Boeing; Pfizer.

457 See letters from Honeywell; Sara Lee.

458 See letter from ABA.

or group based on the number of voting securities over which such shareholder or group has voting control (as opposed to beneficial ownership).[459] Another commenter stated that in the case of nominating groups, the determination of the largest holder should be based on the largest shareholder within the nominating group.[460]

Other commenters recommended that the shareholder or group holding a company's shares for the longest period be permitted to submit nominees under Rule 14a-11.[461] These commenters argued that this approach would be more consistent with the Commission's stated goal of making Rule 14a-11 available to shareholders with a long-term interest.

Some commenters preferred to give priority based on a combination of factors, such as length of ownership and size of ownership stake.[462] Several commenters preferred to let companies (e.g., the nominating committee) choose either the shareholder nominees or the method for deciding which shareholder nominees are included in the proxy materials when there are multiple nominations.[463] Under this approach, companies would disclose the method in the previous year's proxy statement or in a Form 8-K.

A small number of commenters supported the proposed first-in approach.[464] While understanding the concern about "a rush to the courthouse," one commenter indicated that this

---

459 See letter from Kirkland & Ellis.

460 See letter from Seven Law Firms.

461 See letters from BRT; CIGNA (recommending this approach as an alternative to its recommendation that the largest shareholder be given priority); Cummins; Darden Restaurants; FPL Group; General Mills; IBM (recommending this approach as an alternative to its recommendation that the largest shareholder be given priority); Motorola; TIAA-CREF; Xerox.

462 See letters from L. Dallas; T. DiNapoli; Nathan Cummings Foundation; OPERS; Southern Company.

463 See letters from Alston & Bird; CSX; Textron.

464 See letters from Calvert; Florida State Board of Administration; Hermes Equity Ownership Services Ltd. ("Hermes"); Protective.

concern may not necessarily be justified because the "'first' proponent may have sufficiently prepared beforehand for the nomination process."[465] Further, the commenter believed that "[a]llowing the largest shareholder group to essentially trump the first smaller, but no less committed or relevant, shareholder submission is not good governance." Another commenter believed that the first-in approach would best give effect to the proposed rule.[466] If the standard was based on the amount of securities held instead, the commenter would be concerned that long-term owners of companies with index-tracking portfolios might be frozen out of the process. One commenter believed the first-in approach would provide certainty, but companies should be required to set the dates in calendar form and announce the dates in Form 8-K filings at least 30 days prior to the date of effectiveness.[467]

After considering the comments, we have revised the manner in which the rule addresses multiple qualifying nominations. Rather than a first-in standard, as was proposed, a company will be required to include in its proxy materials the nominee or nominees of the nominating shareholder or group with the highest qualifying voting power percentage.[468] In this regard, in light of the comments received, we are concerned that a first-in standard would result in shareholders rushing to submit nominations, discourage constructive dialogue between shareholders and management, and encourage gamesmanship among possible nominating shareholders or groups. When there are multiple qualifying nominations, giving priority to the

---

465 Letter from Calvert.

466 See letter from Hermes.

467 See letter from Florida State Board of Administration.

468 See Rule 14a-11(e). Rule 14a-11(e)(4) prescribes a limited variation on this principle where the company has more than one class of voting shares subject to the proxy rules and eligible nominating shareholders or shareholder groups from more than one of those classes submit nominations that exceed the 25% maximum. In this circumstance, priority of nominations will be determined by reference to the relative voting power of the classes in question.

shareholder or group with the highest voting power percentage is consistent with our overall approach to facilitate director nominations by shareholders with significant commitments to companies. Finally, we seek to avoid the confusion that could result if multiple nominating shareholders or groups submitted their notices on the same day.

We believe that the standard we are adopting, under which the nominating shareholder or group with the highest qualifying voting power percentage will have its nominees included in the company's proxy materials, up to the maximum of 25% of the board, addresses these concerns. We are persuaded that this standard is more consistent with the other limitations of Rule 14a-11 that seek to balance facilitating shareholder rights to nominate directors with practical considerations.

As adopted, Rule 14a-11 addresses situations where more than one shareholder or group would be eligible to have its nominees included on the company's proxy card and disclosed in its proxy statement pursuant to the rule. Given that we are adopting a highest qualifying voting power percentage standard rather than a first-in standard, the company will determine which shareholders' nominees it must include in its proxy statement and on its proxy card by considering which eligible nominating shareholder or group has the highest qualifying voting power percentage, as opposed to which eligible nominating shareholder or group submitted a timely notice first. A company will be required to include in its proxy statement and on its proxy card the nominee or nominees of the nominating shareholder or group with the highest qualifying voting power percentage in the company's securities as of the date of filing the Schedule 14N, up to and including the total number of shareholder nominees required to be included by the company.[469] Where the nominating shareholder or group with highest qualifying voting power

469 See new Rule 14a-11(e) and proposed Rule 14a-11(d)(3).

percentage that is otherwise eligible to use the rule and that filed a timely notice does not nominate the maximum number of directors allowed under the rule, the nominee or nominees of the nominating shareholder or group with the next highest qualifying voting power percentage that is otherwise eligible to use the rule and that filed a timely notice of intent to nominate a director pursuant to the rule would be included in the company's proxy materials, up to and including the total number of shareholder nominees required to be included by the company. This process would continue until the company included the maximum number of nominees it is required to include in its proxy statement and on its proxy card or the company exhausts the list of eligible nominees. If the number of eligible nominees exceeds the maximum number required under Rule 14a-11 and the shareholder or group with the next highest qualifying voting power percentage submitted more nominees than there are remaining available director slots, the nominating shareholder would have the option to specify which of its nominees are to be included in the company's proxy materials.[470]

b. Priority when a nominating shareholder or group or a nominee withdraws or is disqualified

Under the Proposal, we did not address what would be expected of a company if a nominating shareholder or group or nominee withdraws or is disqualified after the company has provided notice to the nominating shareholder or group of its intent to include the nominee in the company's proxy materials. One commenter asked for guidance on how to handle such situations.[471] Another commenter stated that it opposed allowing a nominating shareholder group to change its composition to correct an identified deficiency, such as a failure of the group to

[470] See Instruction 2 to new Rule 14a-11(e).

[471] See letter from Best Buy.

meet the requisite ownership threshold.[472] Two commenters believed that if any member of a nominating shareholder group becomes ineligible due to a failure to own the requisite number of shares, then the entire group and its nominee also should be ineligible to use Rule 14a-11.[473] On the other hand, one commenter recommended that a nominating shareholder group should be allowed to change its composition to correct an identified deficiency, such as the failure of the group to meet the requisite threshold.[474] The commenter also addressed a situation in which a nominating shareholder group qualifies to use Rule 14a-11, provides the necessary notice, submits its nominees, but then becomes disqualified before the meeting at which its nominees would have been put to a shareholder vote. The commenter stated that while it "generally believe[s] that the nominating shareowner should have a short window within which to add a shareowner who would meet all eligibility requirements, a lapse that cannot be cured in that fashion should be remedied by going to the 'second' candidate(s)."

Consistent with the Proposal, under our final rules, neither the composition of the nominating shareholder group nor the shareholder nominee may be changed as a means to correct a deficiency identified in the company's notice to the nominating shareholder or nominating shareholder group – those matters must remain as they were described in the notice to the company.[475] We believe that to allow otherwise could serve to undermine the purpose of the notice deadline provided for in the rule. Thus, a nominating shareholder or group should be sure that it and its nominees meet the requirements of the rule – including the ownership and holding period requirements – before it files its Schedule 14N, as a nominating shareholder or

---

472 See letter from ABA.

473 See letters from CFA Institute; Verizon.

474 See letter from CII.

475 See Instruction 2 to Rule 14a-11(g) and proposed Rule 14a-11(f)(6).

group will not be permitted to add or substitute another shareholder or nominee in order to satisfy the requirements.[476]

In the Proposing Release, we solicited comment on how we should address situations where a nomination is submitted and the nominating shareholder subsequently becomes ineligible under the rule. We also sought comment as to the circumstances under which a second shareholder or group should be able to have its nominees included in a company's proxy materials. Some commenters stated that if a nominating shareholder or group does not remain eligible, the company should be allowed to withdraw the nominating shareholder's or group's candidate from its proxy materials.[477] Some commenters believed that a company should not be required to include a substitute shareholder nominee if the original shareholder nominee is excluded by a company after receiving a no-action letter from the Commission staff regarding the nomination, is withdrawn by the nominating shareholder or group, or otherwise becomes ineligible.[478] These commenters generally argued that a company would not have enough time to seek the exclusion of such a substitute nominee. Still other commenters argued that a nominating shareholder or group should be allowed to submit a new nominee if its original nominee is determined to be ineligible,[479] especially if the company sought and obtained a no-

476 In this regard, we note that if a member of a nominating shareholder group withdraws, the nominating shareholder group and its nominee or nominees would continue to be eligible so long as the group continues to meet the requirements of the rule. If the withdrawal of a member of the nominating shareholder group would result in the group failing to meet the ownership threshold, a company would no longer be required to include any nominees submitted by the nominating shareholder group. As another example, if after a nominating shareholder or group submits one nominee for inclusion in a company's proxy materials and the nominee subsequently withdraws or is disqualified, a company will not be required to include a substitute nominee from that nominating shareholder or group.

477 See letters from BorgWarner; Society of Corporate Secretaries.

478 See letters from 26 Corporate Secretaries; ABA; Allstate; American Express; BorgWarner; DTE Energy; Dupont; FPL Group; Honeywell; IBM; Pfizer; RiskMetrics; Seven Law Firms; Society of Corporate Secretaries; Xerox.

479 See letters from AFL-CIO; P. Neuhauser; USPE.

action letter from the staff concerning the company's determination to exclude the nominee.[480] One commenter worried that a prohibition on substitute shareholder nominees would encourage an unduly adversarial approach by both sides.[481] Another commenter recommended that if the first nominating shareholder or group becomes ineligible, then the nominating shareholder or group with the second-largest holdings should be allowed to submit their own nominees.[482]

Our final rule provides that if a nominating shareholder or group withdraws or is disqualified (e.g., because the nominating shareholder or a member of the group[483] failed to continue to hold the qualifying amount of securities) after the company provides notice to the nominating shareholder or group of the company's intent to include the nominee or nominees in its proxy materials, the company will be required to include in its proxy statement and form of proxy the nominee or nominees of the nominating shareholder or group with the next highest voting power percentage that is otherwise eligible to use the rule and that filed a timely notice in accordance with the rule, if any.[484] This process would continue until the company included the maximum number of nominees it is required to include in its proxy materials or the company exhausts the list of eligible nominees.

If a nominee withdraws or is disqualified after the company provides notice to the nominating shareholder or group of the company's intent to include the nominee in its proxy materials, the company will be required to include in its proxy materials any other eligible

480 See letter from P. Neuhauser.

481 See letter from Universities Superannuation.

482 See letter from CFA Institute.

483 If one member of a group becomes ineligible to use the rule but the group continues to qualify to use the rule without that member, the group would remain eligible overall.

484 See new Rule 14a-11(e)(2).

nominee submitted by that nominating shareholder or group.[485] If that nominating shareholder or group did not include any other nominees in its notice filed on Schedule 14N, then the company will be required to include the nominee or nominees of the nominating shareholder or group with the next highest voting power percentage that is otherwise eligible to use the rule and that filed a timely notice in accordance with the rule, if any, until the maximum number of nominees is included in the company's proxy materials or the list of eligible nominees is exhausted.

We believe that these requirements are appropriate in order to give effect to the intent of our rule – to facilitate shareholders' ability to nominate and elect directors. If the nominating shareholder or group with the highest voting power percentage used all available Rule 14a-11 nominations in a company's proxy materials and the nominating shareholder or group with the second highest voting power percentage had its nominees excluded even after one or more nominees from the nominating shareholder or group with the highest voting power percentage withdrew or was disqualified, we believe the purpose of our rule would be undermined. However, in order to address practical considerations, Rule 14a-11(e)(2) provides that once a company has commenced printing its proxy materials it will not be required to include a substitute nominee or nominees. We believe that at that point in the process it would be too difficult and costly for a company to change course to include a new nominee or nominees. If a nominating shareholder or group or nominee withdraws or is disqualified after the company has commenced printing its proxy materials, the company may determine whether it wishes to print (and furnish) additional materials and a proxy card, delete the disqualified or withdrawn nominee, or instead provide disclosure through additional soliciting materials informing shareholders about the change.[486]

---

485 See new Rule 14a-11(e)(3).

486 We note that pursuant to Exchange Act Rule 14a-4(c)(5) a completed proxy card containing a disqualified

8. Notice on Schedule 14N

a. Proposed notice requirements

As proposed, in order to submit a nominee for inclusion in the company's proxy statement and form of proxy, Rule 14a-11 would require that the nominating shareholder or group provide a notice on Schedule 14N to the company of its intent to require that the company include that shareholder's or group's nominee or nominees in the company's proxy materials.[487] The shareholder notice on Schedule 14N also would be required to be filed with the Commission on the date it is first sent to the company.

We proposed to require the notice to be provided to the company and filed with the Commission by the date specified in the company's advance notice bylaw provision, or where no such provision is in place, no later than 120 calendar days before the date the company mailed its proxy materials for the prior year's annual meeting. If the company did not hold an annual meeting during the prior year, or if the date of the meeting changes by more than 30 calendar days from the prior year, the nominating shareholder must provide notice a reasonable time before the company mails its proxy materials. The company would be required to disclose the date by which the shareholder must submit the required notice in a Form 8-K filed pursuant to proposed Item 5.07 within four business days after the company determines the anticipated meeting date.[488]

As proposed, the notice on Schedule 14N would include disclosures relating to the nominating shareholder's or group's interest in the company, length of ownership, and eligibility

---

or withdrawn nominee or nominees could, under certain circumstances, confer discretionary authority to vote on the election of a substitute director or directors.

487 See proposed Rule 14a-11(c), Rule 14a-18 and Rule 14n-1.

488 See proposed Instruction 2 to Rule 14a-11(a) and proposed Rule 14a-18.

to use Rule 14a-11. The notice on Schedule 14N also would include disclosure required by proposed Rule 14a-18 about the nominating shareholder or group and the nominee for director, as well as disclosure regarding the nature and extent of relationships between the nominating shareholder or group and nominee or nominees and the company. The disclosure provided by the nominating shareholder or group would be similar to the disclosure currently required in a contested election and would be included by the company in its proxy materials.

In addition, as proposed, the notice on Schedule 14N also would include the following representations by the nominating shareholder or group:

- the nominee's candidacy or, if elected, board membership, would not violate controlling state or federal law, or rules of a national securities exchange or national securities association other than rules relating to director independence;[489]
- the nominating shareholder or group satisfies the eligibility conditions in Rule 14a-11;[490]
- in the case of a company other than an investment company, the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the company, if any, or, in the case of a company that is an investment company, the nominee is not an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act of

489 See proposed Rule 14a-18(a). Proposed Rule 14a-11 also included this provision as a direct requirement. Thus, a company would not be required to include a shareholder nominee in its proxy materials if the nominee's candidacy or, if elected, board membership would violate controlling state law, federal law, or rules of a national securities exchange or national securities association (other than rules of a national securities exchange or national securities association that set forth requirements regarding the independence of directors).

490 See proposed Rule 14a-18(b) (which referred to the requirements in proposed Rule 14a-11(b)).

1940;[491] and

- neither the nominee nor the nominating shareholder (or any member of a nominating shareholder group) has an agreement with the company regarding the nomination of the nominee.[492]

Proposed Item 8 of Schedule 14N would have required a certification from the nominating shareholder or each member of the nominating shareholder group that the securities used for purposes of meeting the ownership threshold in Rule 14a-11 are not held for the purpose, or with the effect, of changing control of the company or to gain more than a limited number of seats on the board.

b. Comments on the proposed notice requirements

Commenters generally supported the proposed content requirements of Schedule 14N on the general principle that the Commission should impose disclosure requirements on nominating shareholders and their nominees.[493] Two of these commenters also stated that additional disclosures or representations are not needed.[494] In addition, some commenters recommended that all nominees be subject to any new disclosure rules adopted by the Commission as part of its proxy disclosure and solicitation enhancements rulemaking.[495] Four commenters asked that companies be allowed to require additional disclosure from a nominating shareholder or group

---

491 See proposed Rule 14a-18(c).

492 See proposed Rule 14a-18(d).

493 See letters from ABA; Alston & Bird; Americans for Financial Reform; CalSTRS; CFA Institute; CII; Corporate Library; Dominican Sisters of Hope; Florida State Board of Administration; GovernanceMetrics; ICI; Mercy Investment Program; Protective; RiskMetrics; Sisters of Mercy; Tri-State Coalition; Ursuline Sisters of Tildonk; USPE; Walden.

494 See letters from CII; USPE.

495 See letters from ABA; Alaska Air; Robert A. Bassett ("R. Bassett"); BorgWarner; Eli Lilly; NACD; O'Melveny & Myers; Pfizer; Society of Corporate Secretaries; UnitedHealth.

through, for example, the advance notice bylaws, as long as such requirements are consistent with state law.[496] One commenter argued that the nominating shareholder, group, or nominee should provide any disclosure required under a company's governing documents as long as such disclosure is required of all nominees.[497] One commenter asked that all content requirements be set forth in Schedule 14N itself, as it found the structure of the Schedule and the references to disclosure requirements to be unnecessarily complicated.[498] The commenter recommended that we include a requirement that the nominating shareholder or group disclose information about the nature and extent of the relationships between the nominating shareholder, group and the nominee and the company or its affiliates.[499] Another commenter recommended the rules include a representation that the nominee is not controlled by the nominating shareholder or group.[500]

We also sought comment on the proposed representations to be provided by the nominating shareholder or group in Schedule 14N. One commenter stated that the proposed representations are appropriate and no additional representations are needed.[501] This commenter opposed a requirement for a shareholder nominee to make any representation either in addition to, or instead of, those made by the nominating shareholder or group. One commenter stated simply that none of the proposed representations in Schedule 14N should be eliminated.[502] It also observed generally that the shareholder nominee should be required to make the representations

---

496 See letters from ABA; Chevron; Sidley Austin; SIFMA.

497 See letter from Cleary.

498 See letter from ABA.

499 Id.

500 See letter from IBM.

501 See letter from CII.

502 See letter from ABA.

(e.g., regarding independence) because he or she would know the facts relating to the representations and therefore should accept responsibility. One commenter opposed the requirement for a representation that a shareholder nomination (or election of the shareholder nominee) would not violate state law, federal law, or listing standards.[503] The commenter also believed it would be inappropriate to require a representation that the nomination complies with any independence requirement under federal law, state law, or listing standards.

c. Adopted notice requirements

We are adopting the notice requirements substantially as proposed, with differences noted below. In addition, we agree that the rules as proposed could be streamlined to reduce complexity. As adopted, Schedule 14N will contain the disclosure items that were included in the Schedule as proposed, as well as the disclosures proposed in Rule 14a-11, Rule 14a-18 and Rule 14a-19. We believe that the disclosure requirements we are adopting will provide transparency and facilitate shareholders' ability to make an informed voting decision on a shareholder director nominee or nominees without being unnecessarily burdensome on nominating shareholders or groups.

i. Disclosure

Schedule 14N will require a nominating shareholder or group to provide the following information about the nominating shareholder or group and the nominee:[504]

- The name and address of the nominating shareholder or each member of the nominating shareholder group;
- Information regarding the amount and percentage of securities held and entitled to

503 See letter from USPE.

504 The disclosure requirements proposed in Rule 14a-18(e) – (l) are now contained in new Item 4(b) and new Item 5 of Schedule 14N.

vote on the election of directors at the meeting and the voting power derived from securities that have been loaned or sold in a short sale that remains open, as specified in Instruction 3 to Rule 14a-11(b)(1);[505]

- A written statement from the registered holder of the shares held by the nominating shareholder or each member of the nominating shareholder group, or the brokers or banks through which such shares are held, verifying that, within seven calendar days prior to submitting the notice on Schedule 14N to the company, the shareholder continuously held the qualifying amount of securities for at least three years;[506]
- A written statement of the nominating shareholder's or group's intent to continue to hold the qualifying amount of securities through the shareholder meeting at which directors are elected. Additionally, the nominating shareholder or group would provide a written statement regarding the nominating shareholder's or group's intent with respect to continued ownership after the election;[507]
- A statement that the nominee consents to be named in the company's proxy statement and form of proxy and, if elected, to serve on the board of directors;[508]
- Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b), and (c) and, for investment companies,

505 See Item 3 of new Schedule 14N.

506 See Item 4(a) of new Schedule 14N. A nominating shareholder would not be required to provide this statement if the nominating shareholder is the registered holder of the shares or is attaching or incorporating by reference a previously filed Schedule 13D, Schedule 13G, Form 3, Form 4, and/or Form 5, or amendments to those documents to prove ownership.

507 See Item 4(b) of new Schedule 14N. These requirements were proposed in Rule 14a-18(f) and Item 5(b) of Schedule 14N.

508 See Item 5(a) of new Schedule 14N and proposed Rule 14a-18(e).

Item 22(b) of Schedule 14A, as applicable;[509]

- Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A, as applicable;[510]
- Disclosure about whether the nominating shareholder or any member of a nominating shareholder group has been involved in any legal proceeding during the past ten years, as specified in Item 401(f) of Regulation S-K;[511]
- Disclosure about whether, to the best of the nominating shareholder's or group's knowledge, the nominee meets the director qualifications set forth in the company's governing documents, if any;[512]
- A statement that, to the best of the nominating shareholder's or group's knowledge, in the case of a company other than an investment company, the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the company, if any, or, in the case of a company that is an investment company, the nominee is not an "interested person" of the company as defined in Section 2(a)(19) of the Investment Company Act of

---

509 See Item 5(b) of new Schedule 14N and proposed Rule 14a-18(g).

510 See Item 5(c) of new Schedule 14N and proposed Rule 14a-18(h). If a nominating shareholder is organized in a form other than a corporation or partnership, comparable disclosure with respect to persons in similar capacities would be required.

511 See Item 5(d) of new Schedule 14N and proposed Rule 14a-18(i). As proposed, the rule would have required disclosure regarding a nominating shareholder's involvement in any legal proceedings during the past five years. Recently, the Commission amended Item 401(f) of Regulation S-K to require disclosure regarding involvement in legal proceedings for the prior ten years. See Proxy Disclosure Enhancements, Release No. 33-9089; 34-61175 (Dec. 16, 2009) [74 FR 68334] ("Proxy Disclosure Enhancements Adopting Release"). Accordingly, as adopted, Item 5(d) will require disclosure about a nominating shareholder's involvement in legal proceedings during the past ten years.

512 See Item 5(e) of new Schedule 14N.

1940;[513]

- Disclosure about the nature and extent of the relationships between the nominating shareholder or group, the nominee, and/or the company or any affiliate of the company,[514] such as:
  - Any direct or indirect material interest in any contract or agreement between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the company or any affiliate of the company (including any employment agreement, collective bargaining agreement, or consulting agreement);
  - Any material pending or threatened litigation in which the nominating shareholder or any member of the nominating shareholder group and/or the nominee is a party or a material participant, and that involves the company, any of its officers or directors, or any affiliate of the company; and
  - Any other material relationship between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the company or any affiliate of the company not otherwise disclosed;[515]
- Disclosure of any Web site address on which the nominating shareholder or group may publish soliciting materials;[516] and
- If desired to be included in the company's proxy statement, a statement in support of

---

513 See Item 5(f) of new Schedule 14N.

514 We note that this disclosure requirement would apply to relationships between the nominating shareholder or group and the nominee, as well as the relationships between the nominating shareholder or group or the nominee and the company or its affiliates. See Item 5(g) of new Schedule 14N.

515 See Item 5(g) of new Schedule 14N and proposed Rule 14a-18(j).

516 See Item 5(h) of new Schedule 14N and proposed Rule 14a-18(k).

the shareholder nominee or nominees, which may not exceed 500 words per nominee.[517]

The disclosure provided by the nominating shareholder or group in Item 5 of Schedule 14N would be included by the company in its proxy materials,[518] along with the company's disclosure in response to Items 4(b) and 5(b) of Schedule 14A.[519]

In a traditional proxy contest, shareholders receive the disclosure required by Items 4(b), 5(b), 7, and 22, as applicable, of Schedule 14A from both the company and the insurgent when the contest relates to an annual election of directors. The new Schedule 14N disclosure requirements are somewhat more expansive in that they also include the disclosures concerning ownership amount, length of ownership, intent to continue to hold the shares through the date of the meeting and with respect to continued ownership after the meeting, and disclosure regarding the nature and extent of the relationships between the nominating shareholder or group and nominee and the company or any affiliate of the company. We believe that these disclosures will

---

517 See Item 5(i) of new Schedule 14N and proposed Rule 14a-18(l). This requirement is discussed in more detail in this section. If a nominating shareholder or group submits a statement in support that exceeds 500 words per nominee, a company will be required to include the nominee or nominees, provided that the eligibility requirements are met, but may exclude the statement in support from its proxy materials pursuant to Rule 14a-11(g). In this instance, the company would provide notice to the staff and could, if desired, seek a no-action letter from the staff. See new Rule 14a-11(c) and Rule 14a-11(g). The 500 words would be counted in the same manner as words are counted under Rule 14a-8. Any statements that are, in effect, arguments in support of the nomination would constitute part of the supporting statement. Accordingly, any "title" or "heading" that meets this test would be counted toward the 500-word limitation. Inclusion of a Web site address in the supporting statement would not violate the 500-word limitation; rather, the Web site address would be counted as one word for purposes of the 500-word limitation.

518 See Item 7(e) of Schedule 14A. Similarly, if a company receives a nominee for inclusion in its proxy materials pursuant to a procedure set forth under applicable state or foreign law, or the company's governing documents providing for the inclusion of shareholder director nominees in the company's proxy materials, the disclosure provided by the nominating shareholder or group in response to Item 6 of Schedule 14N would be included in the company's proxy materials. See Item 7(f) of Schedule 14A.

519 Instruction 3 to Rule 14a-12(c) clarifies that though inclusion of a nominee pursuant to Rule 14a-11 or solicitations by a nominating shareholder or nominating shareholder group that are made in connection with that nomination would constitute solicitations in opposition subject to Rule 14a-12(c), they would not be treated as such for purposes of Exchange Act Rule 14a-6(a).

assist shareholders in making an informed voting decision with regard to any nominee or nominees put forth by the nominating shareholder or group using Rule 14a-11, in that the disclosures will enable shareholders to gauge the nominating shareholder's or group's interest in the company, longevity of ownership, and intent with regard to continued ownership in the company. These disclosures also will be important to the company in determining whether the nominating shareholder or group is eligible to rely on Rule 14a-11 to require the company to include a nominee or nominees in the company's proxy materials.

In some cases, the requirements in new Schedule 14N are slightly different than we proposed. We have clarified that the nominating shareholder or group will be required to include disclosure in the Schedule 14N concerning specified relationships between the nominating shareholder or group and the nominee or nominees. As discussed in Section II.B.5.d. above, we received comment suggesting that, in the absence of a limitation on relationships between the nominating shareholder or group and their nominee or nominees, we should adopt a disclosure requirement concerning relationships between the parties.[520] Similarly, and as discussed in Section II.B.5.b., we have added a requirement that a nominating shareholder or group disclose whether, to the best of their knowledge, the nominating shareholder's or group's nominee meets the company's director qualifications, if any, as set forth in the company's governing documents.[521] We added this requirement because we believe that this information will be useful to shareholders in making a voting decision by enabling them to consider whether shareholder nominees would meet a company's director qualifications. Shareholders will provide this disclosure "to the best of their knowledge" to address the fact that the standards will be company

---

520 See letters from CII; IBM; O'Melveny & Myers; SIFMA; UnitedHealth.

521 See Item 5(e) of new Schedule 14N.

standards and thus could be subject to interpretation.

We also have added an instruction to Item 4 of Schedule 14N to provide a form of written statement that may be used for verifying the amount of securities held by the nominating shareholder, and that the qualifying amount of securities has been held continuously for at least three years.[522] A statement will be required from a nominating shareholder that is not the registered holder of the securities and is not proving ownership by providing previously filed Schedules 13D or 13G, or Forms 3, 4, or 5. We believe that providing a form of written statement will make it easier for nominating shareholders and the persons through which they hold their securities to comply with the requirement and reduce complexity for shareholders and companies in determining whether satisfactory proof of ownership has been provided.[523] In addition, as noted above, Item 5(d) will require disclosure about each nominating shareholder's involvement in legal proceedings during the past ten years rather than the past five years as proposed, consistent with the changes recently adopted by the Commission for board nominees in general.

In connection with our revisions to the rule concerning calculation of ownership, we also have added new Items 3(c) and (d) to the Schedule 14N to require disclosure of the voting power attributable to securities that have been loaned or sold in a short sale that is not closed out, or that have been borrowed for purposes other than a short sale, as specified in Instruction 3 to Rule 14a-11(b)(1).

Finally, as proposed, a nominating shareholder or group could provide a statement in

---

[522] See the Instruction to Item 4 of new Schedule 14N.

[523] In this regard, we note that providing proper proof of ownership has proved to be an area of confusion for some shareholder proponents using Rule 14a-8 who must obtain a written statement from the "record" holder of the proponent's securities. Thus, we believe that providing a form of written statement that may be used to provide proof of ownership for purposes of Rule 14a-11(b)(3) will alleviate any potential confusion that could arise in this context.

support of a shareholder nominee or nominees, which could not exceed 500 words if the nominating shareholder or group elects to have such a statement included in the company's proxy materials. Two commenters stated that a limit of 500 words would be appropriate,[524] five commenters recommended that a nominating shareholder or group be permitted to include a supporting statement of more than 500 words,[525] and four commenters proposed a limit of either 750 or 1000 words.[526] We believe it is appropriate to allow a nominating shareholder or group to provide a statement in support of the shareholder nominee or nominees which may not exceed 500 words for each nominee, rather than 500 words for all nominees in total,[527] if the nominating shareholder or group elects to have such a statement included in the company's proxy materials. We believe that a limitation of 500 words per nominee is sufficient for a nominating shareholder or group to express their support for a nominee. In this regard, we note that shareholders and companies are familiar with the 500 word limitation, as it is the limit on the number of words that may be used to support a shareholder proposal submitted under Rule 14a-8. While we believe it is appropriate to limit the length of the supporting statement that the company is required to include, we note that if a nominating shareholder or group wishes to provide additional information, it is free to do so in supplemental materials, provided it complies with the requirements of Rule 14a-2(b)(8). If a nominating shareholder or group submits a statement in support that exceeds 500 words per nominee, a company will be required to include the nominee or nominees, provided that the eligibility requirements are met, but the company may exclude the statement in support from its proxy materials provided it provides notice to the staff of its intent

524 See letters from CII; Florida State Board of Administration.

525 See letters from ACSI; AFSCME; Hermes; Pax World; USPE.

526 See letters from AFSCME; L. Dallas; P. Neuhauser; USPE.

527 We are adopting this modification in Item 5(i) of Schedule 14N.

to do so.[528]

As noted above, we proposed to require certain representations to be provided in the Schedule 14N, either in the form of representations or as certifications. As adopted, we are including the proposed representations and certifications as direct requirements in Rule 14a-11.[529] Consequently, we have simplified the requirements so that under the final rules a nominating shareholder or group will be required to certify, in its notice on Schedule 14N filed with the Commission, that it does not have a change in control intent or an intent to gain more than the maximum number of board seats provided for under Rule 14a-11 and that the nominating shareholder and the nominee satisfies the applicable requirements of Rule 14a-11.[530] We have retained the certification with regard to no change in control intent or intent to gain more than the maximum number of board seats provided for under Rule 14a-11, even though this is also a direct requirement in Rule 14a-11 as adopted, because we believe it is important to highlight this requirement for nominating shareholders or groups signing the certification. As was proposed, the nominating shareholder or each member of the nominating shareholder group (or authorized representative) will be required to certify when signing the Schedule 14N that, "after reasonable inquiry and to the best of my knowledge and belief," the information in the statement is "true, complete and correct." Though all disclosure in the Schedule 14N would be covered by this representation, we have specifically included it in the certifications concerning compliance with

528 See new Rule 14a-11(c) and Rule 14a-11(g).

529 See also Section II.B.4. and Section II.B.5. above, regarding nominating shareholder and nominee eligibility.

530 See new Rule 14a-11(b)(11) and Item 8(a) of new Schedule 14N. We note that in some cases, an authorized representative may file a Schedule 14N for each member of a nominating shareholder group and would provide the required disclosures and certifications. In such cases, each member of the nominating shareholder group represented by the authorized representative will be deemed to have provided the certifications.

the requirements of Rule 14a-11 as well.

We have revised the rule to delete the provision that had the effect of allowing exclusion of a nominee if any required representation or certification was materially false or misleading.[531] Rather than allowing companies to exclude Rule 14a-11 nominees on that basis, we believe companies should address any concerns regarding false or misleading disclosures through their own disclosures, as in traditional proxy contests. This change will limit the bases on which a company may exclude a nominee,[532] but we emphasize that the nominating shareholder or group will have Rule 14a-9 liability for any statement included in the Schedule 14N or which it causes to be included in a company's proxy materials which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact or that omits to state any material fact necessary to make the statements therein not false or misleading. In addition, as discussed in Section II.E. below, we have provided in the final rules that the company is not responsible for the information provided by the nominating shareholder or group in its Schedule 14N and included by the company in its proxy materials.

ii. Schedule 14N filing requirements

We proposed to require the notice to be provided to the company and filed with the Commission by the date specified in the company's advance notice bylaw provision, or where no such provision is in place, no later than 120 calendar days before the date the company mailed its proxy materials for the prior year's annual meeting. A significant number of commenters

---

531 See proposed Rule 14a-11(a)(5).

532 See Section II.B.9. below for a discussion of the requirements for a company receiving a nomination submitted pursuant to Rule 14a-11 and the process for seeking a staff no-action letter with respect to a company's decision to exclude a nominee. As noted below, assertions that a certification or disclosure provided by a nominating shareholder or group is false or misleading will not be a basis for excluding a nominee or nominees. A company seeking a no-action letter from the staff with regard to a determination to exclude a nominee or nominees would need to assert that a requirement of the rule has not been met.

suggested using a uniform deadline for all companies, as is the case in Rule 14a-8.[533] Many of these commenters believed that the proposed timing requirement would create difficulties for companies with advance notice bylaws providing a later deadline and, thus, would preclude those companies from engaging in the proposed staff process.[534] Some commenters supported the proposed default 120 calendar day deadline,[535] while others argued that the 120 calendar day deadline would provide too little time for companies.[536] Some commenters worried that the proposed deadline would not give sufficient time for companies to resolve any eligibility issues presented by potential nominees, including resolution through the Rule 14a-11 no-action process, Commission appeals, and litigation.[537]

We are adopting a uniform deadline of no later than 120 calendar days before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting for all companies subject to the rule.[538] We believe that a uniform deadline will benefit shareholders by providing them with one standard to comply with at all companies and should

533 See letters from 26 Corporate Secretaries; ABA; Alaska Air; American Express; Anadarko; Boeing; BorgWarner; BRT; Caterpillar; CIGNA; CII; Dewey; Florida State Board of Administration; FPL Group; Honeywell; JPMorgan Chase; Keating Muething; P. Neuhauser; PepsiCo; Pfizer; Praxair; Schulte Roth & Zabel; Seven Law Firms; Shearman & Sterling; Sidley Austin; Society of Corporate Securities; Thompson Hine LLP ("Thompson Hine"); TI; USPE; Wells Fargo; Xerox.

534 See letters from ABA; Alaska Air; BRT; Caterpillar; CIGNA; Dewey; Honeywell; JPMorgan Chase; Keating Muething; PepsiCo; Sidley Austin; Society of Corporate Securities; Thompson Hine; TI; Wells Fargo.

535 See letters from Alaska Air; Boeing; BorgWarner; CII; Dewey; JPMorgan Chase; P. Neuhauser; O'Melveny & Myers; PepsiCo; Praxair; Seven Law Firms; Shearman & Sterling; Society of Corporate Secretaries; Thompson Hine; USPE.

536 See letters from 26 Corporate Secretaries; ABA; Alcoa; Allstate; American Express; Boeing; BRT; Con Edison; Davis Polk; FPL Group; JPMorgan Chase; McDonald's; P. Neuhauser; Pfizer; Protective; RiskMetrics; Seven Law Firms; TI; Xerox.

537 See letters from ABA; BRT; Con Edison; TI.

538 See new Rule 14a-11(b)(10). The Schedule 14N would, of course, have to contain all required disclosure as of the date of filing.

address concerns of companies that an advance notice bylaw deadline would provide too little time. We also believe that a deadline of 120 calendar days will provide adequate time for companies to take the steps necessary to include or, where appropriate, to exclude a shareholder nominee for director that is submitted pursuant to Rule 14a-11.[539]

In the Proposing Release, we solicited comment as to whether a window period should be provided for the submission of the notice on Schedule 14N and the appropriate time period for the window. A number of commenters recommended a window period during which a nominating shareholder or group could submit its Rule 14a-11 nomination.[540] These commenters believed that including such a requirement would prevent a race to file among shareholders that could discourage dialogue with the board and force the board to address nominations throughout the year.[541] We agree and are adopting a window period for the submission of the notice to the

539 We note that as with Rule 14a-8, Rule 14a-11 requires a company to provide notice to the Commission if it intends to exclude a nominee. Also as with Rule 14a-8, if a company determines that it may exclude a nominee, the rule does not require the company to seek a no-action letter from the staff with regard to the determination to exclude the nominee. In this regard, we note that the 120-day deadline in Rule 14a-8 appears to provide companies with sufficient time in which to consider complex matters. For example, companies routinely consider whether a proposal submitted pursuant to Rule 14a-8 would cause the company to violate federal or state law and submit requests for no-action letters, along with detailed legal opinions, with respect to those proposals. We believe that a company will consider nominees submitted pursuant to Rule 14a-11 in a similar manner. Thus, we believe a deadline of 120 calendar days before the date that the company mailed it proxy materials the prior year is sufficient.

540 See letters from 26 Corporate Secretaries; Aetna; Allstate; Boeing; BorgWarner; L. Dallas; DuPont; Florida State Board of Administration; FPL Group; Kirkland & Ellis; Leggett; P. Neuhauser; PepsiCo; Pfizer; S. Quinlivan; RiskMetrics; Schulte Roth & Zabel; Shearman & Sterling; SIFMA; Society of Corporate Secretaries; Southern Company; TI; USPE; Wells Fargo; Xerox.

541 The commenters generally mentioned various 30 day ranges that we requested comment on (e.g., no earlier than 180 days and no later than 150 days before the date that the company mailed its proxy materials for the prior year's annual meeting; no earlier than 150 calendar days and no later than 120 calendar days before the date that the company mailed its proxy materials for the prior year's annual meeting; no earlier than 120 calendar days and no later than 90 calendar days prior to the anniversary of the company's last annual meeting). One commenter suggested that the Commission limit the nomination process to a 45-day window period commencing four months after the company's annual shareholder meeting. See letter from Aetna. Another commenter suggested that nominations be submitted within a 30-day period commencing five months after the company's annual meeting. See letter from SIFMA. We believe that starting the period for nominations earlier than 150 calendar days before the anniversary of the date the company mailed its proxy materials for the prior year's annual meeting would not provide the current board with sufficient opportunity to perform its duties and demonstrate its performance, nor would it provide

company. Limiting the time period during which Rule 14a-11 nominations could be made should help reduce disruptions that might occur when a company receives shareholder nominations for director submitted pursuant to Rule 14a-11. In this regard, as noted above, commenters generally supported a 30-day window period. We believe that a window of 30 days is sufficient for the submission of the notice on Schedule 14N because it provides shareholders with an opportunity to submit a nomination, as well as the opportunity to consider any nominations that have been submitted and whether the shareholder would like to submit a nomination, either individually or as a group. Therefore, we are adopting a requirement that the notice on Schedule 14N be transmitted to the company and filed with the Commission no earlier than 150 calendar days, and no later than 120 calendar days, before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting. As proposed, we are adopting a requirement that if the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, then the nominating shareholder must provide notice a reasonable time before the company mails its proxy materials.[542] In that case, the company will be required to disclose the date by which the shareholder must submit the required notice in a Form 8-K filed pursuant to new Item 5.08 within four business days after the company determines the anticipated meeting date.[543]

---

shareholders with enough time to evaluate the board's performance, to make an informed decision with respect to a potential nomination.

542 In addition, if a company is holding a special meeting in lieu of an annual meeting, the nominating shareholder must provide notice a reasonable time before the company mails its proxy materials.

543 See new Rule 14a-11(b)(10). See also proposed Instruction 2 to Rule 14a-11(a) and Rule 14a-18. This would be similar to the requirement currently included in Rule 14a-5(f), which specifies that, where the date of the next annual meeting is advanced or delayed by more than 30 calendar days from the date of the annual meeting to which the proxy statement relates, the company must disclose the new meeting date in the company's earliest possible quarterly report on Form 10-Q. Although registered investment companies

As noted, the notice on Schedule 14N must be transmitted to the company[544] and filed with the Commission on the same day.[545] Consistent with the Proposal, the Schedule 14N must be filed with the Commission on EDGAR. To file the Schedule 14N on EDGAR, a nominating shareholder or group and any nominee will need to have or obtain EDGAR filing codes and user identification numbers, which may be obtained by filing electronically a Form ID in advance of filing the Schedule 14N.[546] We encourage nominating shareholders and groups to take the steps necessary to obtain an EDGAR filing code and CIK code well in advance of the deadline for filing a notice on Schedule 14N.

The Schedule 14N will:

- Include a cover page in the form set forth in Schedule 14N with the appropriate box

---

generally are not required to file Form 8-K, we are requiring them to file a Form 8-K disclosing the date by which the shareholder notice must be provided if the company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year. For a further discussion of the Form 8-K filing requirement for registered investment companies, see Section II.D.1.

544 Rule 14n-3 specifies that the Schedule 14N must be transmitted to the company at its principal executive office.

545 See new Rule 14n-1. In this regard, we are adopting an amendment to Rule 13(a)(4) of Regulation S-T, as proposed, to provide that a Schedule 14N will be deemed to be filed on the same business day if it is filed on or before 10 p.m. Eastern Standard Time or Eastern Daylight Saving Time, whichever is currently in effect. This will allow nominating shareholders additional time to file the notice on Schedule 14N and transmit the notice to the company.

546 To file the Schedule 14N on EDGAR, a nominating shareholder or group and any nominee that does not already have EDGAR filing codes, and to which the Commission has not previously assigned a user identification number, which we call a "Central Index Key (CIK)" code, will need to obtain the codes by filing electronically a Form ID (17 CFR 293.63; 249.446; and 274.402) at https://www.filermanagement.edgarfiling.sec.gov. The applicant also will be required to submit a notarized authenticating document. If the authenticating document is prepared before the applicant makes the Form ID filing, the authenticating document may be uploaded as a Portable Document Format (PDF) attachment to the electronic filing. An applicant also may submit the authenticating document by faxing it to the Commission within two business days before or after electronically filing the Form ID. The authenticating document would need to be manually signed by the applicant over the applicant's typed signature, include the information contained in the Form ID, and confirm the authenticity of the Form ID. If the authenticating document is filed after electronically filing the Form ID, it would need to include the accession number assigned to the electronically filed Form ID as a result of its filing. See 17 CFR 232.10(b)(2).

on the cover page marked to specify that the filing relates to a Rule 14a-11 nomination;[547]

- Be made under the subject company's Exchange Act file number (or in the case of a registered investment company, under the subject company's Investment Company Act file number); and
- Be made on the date the notice is first transmitted to the company.

We are adopting, as proposed, a requirement that the Schedule 14N be amended promptly for any material change to the disclosure and certifications provided in the originally-filed Schedule 14N.[548] In this regard, we would view withdrawal of a nominating shareholder or group (or any member of the group), or of a director nominee, and the reasons for any such withdrawal, as a material change. For example, such a withdrawal could be material because it may result in a group no longer meeting the required ownership threshold under Rule 14a-11. We also would view as material entering into an agreement between the company and the nominating shareholder or group for the company to include a nominee in the company's proxy materials as a company nominee.[549] The nominating shareholder or group also will be required, as proposed, to file a final amendment to the Schedule 14N disclosing within 10 days of the final results of the election being announced by the company the nominating shareholder's or group's intention with regard to continued ownership of its shares.[550] As discussed above, the nominating

---

547 The Schedule 14N also would be used for disclosure concerning the inclusion of shareholder nominees in company proxy materials when made pursuant to an applicable state or foreign law provision or a company's governing documents. See new Rule 14a-18 and proposed Rule 14a-19, as discussed in Section II.C.5. below.

548 See new Rule 14n-2(a).

549 We note that if this occurs, the nominee would no longer be a Rule 14a-11 nominee. See Section II.B.6.c. for a discussion of how this would affect the calculation of the maximum number of Rule 14a-11 nominees.

550 See new Rule 14n-2(b).

shareholder or group would be required to disclose its intent with regard to continued ownership of the company's securities in its original notice on Schedule 14N.[551] Filing an amendment to the Schedule 14N within 10 days after the announcement of the final results of the election will provide shareholders with information as to whether the outcome of the election may have altered the intent of the nominating shareholder or group and what further plans the nominating shareholder or group may have with regard to the company.

As was proposed,[552] the Schedule 14N may be signed either by each person on whose behalf the statement is filed or his or her authorized representative. We assume that in many cases group members will choose to appoint an authorized representative from among the group. If the statement is signed on behalf of a person by his authorized representative other than an executive officer or general partner of the filing person, evidence of the representative's authority to sign on behalf of such person must be filed with the statement, provided, however, that a power of attorney for this purpose which is already on file with the Commission may be incorporated by reference.

The Schedule 14N, as filed with the Commission, as well as any amendments to the Schedule 14N, will be subject to the liability provisions of Exchange Act Rule 14a-9 pursuant to new paragraph (c) to the rule.[553]

9. Requirements for a Company That Receives a Notice from a Nominating Shareholder or Group

---

551 See Item 4(b) of new Schedule 14N.

552 While the proposed Schedule 14N included the instruction regarding the signing of the Schedule by an authorized representative, we did not discuss this aspect of the proposed rule text in the narrative portion of the release.

553 For further discussion, see Section II.E.

a. Procedure if company plans to include Rule 14a-11 nominee

In the Proposing Release, we proposed a process for a company to follow once it received a nomination submitted pursuant to Rule 14a-11. Upon receipt of a shareholder's or group's notice of its intent to require the company to include in its proxy materials a shareholder nominee or nominees pursuant to Rule 14a-11, the company would determine whether it would include the nominee or whether it believed it would be desirable to, and that the company had a basis upon which it could rely to, exclude a nominee. If a company determined it would include the nominee, the company would notify in writing the nominating shareholder or group no later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the Commission that it will include the nominee or nominees.[554] The company would be required to provide this notice in a manner that provides evidence of timely receipt by the nominating shareholder or group.

We are adopting this requirement as proposed, with a clarification regarding the timing of the company's transmission of the notice and receipt by the nominating shareholder or group.[555] As adopted, if a company will include a shareholder nominee, a company will be required to notify the nominating shareholder or group (or their authorized representative). Rather than including the proposed requirement that the company must provide the notice in a manner that evidences timely receipt by the shareholder, we are adopting a requirement that the notification must be postmarked or transmitted electronically no later than 30 calendar days before it files its definitive proxy materials with the Commission.[556] We believe this will provide for ease of use

---

554 See proposed Rule 14a-11(f)(2).

555 See new Rule 14a-11(g)(1) and Instruction 1 to Rule 14a-11(g).

556 This 30-day deadline for this notice should provide a nominating shareholder or group with sufficient time to engage in soliciting activities with respect to its nominee or nominees, if it has not done so already, or pursue any legal remedies that may be available if the company determines it will exclude the nominating

and administration because it should be clear when the notice was transmitted. We also note that it is consistent with the transmission standard we are adopting for submitting a notice of intent with respect to a nomination pursuant to Rule 14a-11(b)(10). We note that while we are not adopting a requirement regarding the evidence of timely receipt by the nominating shareholder or group, we believe it is in a company's interest to send the notice to the nominating shareholder or group in a manner that will allow the company to demonstrate that the nominating shareholder or group received the notice, as doing so may avoid potential disputes.

b. Procedure if company plans to exclude Rule 14a-11 nominee

The Proposal also included a process for a company to follow if it determined that it could exclude a nominee submitted pursuant to Rule 14a-11.[557] As proposed, a company could determine that it is not required under Rule 14a-11 to include a nominee from a nominating shareholder or group in its proxy materials if:

- Proposed Rule 14a-11 is not applicable to the company;
- The nominating shareholder or group has not complied with the requirements of Rule 14a-11;
- The nominee does not meet the requirements of Rule 14a-11;
- Any representation required to be included in the notice to the company is false or misleading in any material respect; or
- The company has received more nominees than it is required to include by proposed Rule 14a-11 and the nominating shareholder or group is not entitled to have its

shareholder's or group's nominee or nominees.

557 The process was modeled after the staff no-action process used in connection with shareholder proposals under Rule 14a-8.

nominee included under the criteria proposed in Rule 14a-11(d)(3).[558]

Under the Proposal, the nominating shareholder or group would need to be notified of the company's determination not to include the shareholder nominee in sufficient time to consider the validity of any determination to exclude the nominee and respond to such a notice.[559] In this regard, we noted the time-sensitive nature of Rule 14a-11 and the interpretive issues that may arise in applying the new rule. After the company provided such a notice to a nominating shareholder or group and afforded the nominating shareholder or group the opportunity to respond, the company would be required to provide a notice to the Commission regarding its intent not to include a shareholder nominee in its proxy materials. The company could seek a no-action letter from the staff with respect to its decision to exclude the nominee.[560]

The proposed process would have afforded a nominating shareholder or group the opportunity to remedy certain eligibility or procedural deficiencies in a nomination.[561] The various time deadlines set out in the proposed process were determined by considering the appropriate balance between companies' needs in meeting printing and filing deadlines for their shareholder meetings with shareholders' need for adequate time to satisfy the requirements of the

---

558 See proposed Rule 14a-11(a). More specifically, under the proposal a company would not be required to include a nominee where (1) applicable state law or the company's governing documents prohibit the company's shareholders from nominating a candidate for director; (2) the nominee's candidacy, or if elected, board membership, would violate controlling state law, federal law or rules of a national securities exchange or national securities association; (3) the nominating shareholder or group does not meet the rule's eligibility requirements; (4) the nominating shareholder's or group's notice is deficient; (5) any representation in the nominating shareholder's or group's notice is false in any material respect, or (6) the nominee is not required to be included in the company's proxy materials due to the proposed limitation on the number of nominees required to be included.

559 See proposed Rule 14a-11(f).

560 See proposed Rule 14a-11(f)(7) – (14).

561 See proposed Rule 14a-11(f)(3) – (6).

rule.[562] Specifically, as proposed, a company determining that the nominating shareholder or group or nominee or nominees has not satisfied the eligibility requirements could exclude the shareholder nominee or nominees, subject to the following requirements:

- The company would notify in writing the nominating shareholder or group of its determination. The notice would be required to be postmarked or transmitted electronically no later than 14 calendar days after the company receives the shareholder notice of intent to nominate. The company would have to provide the notice in a manner that provides evidence of receipt by the nominating shareholder or group;[563]
- The company's notice to the nominating shareholder or group that it determined that the company may exclude a shareholder nominee or nominees would be required to include an explanation of the company's basis for determining that it may exclude the nominee or nominees;[564]
- The nominating shareholder or group would have 14 calendar days after receipt of the written notice of deficiency to respond to the notice and correct any eligibility or procedural deficiencies identified in the notice. The nominating shareholder or group would have to provide the response in a manner that provides evidence of its receipt by the company;[565]

---

562 We considered the timing requirements and deadlines in Rule 14a-8 when crafting the proposed requirements and deadlines for Rule 14a-11; however, due to the potential complexity of the nomination process, we determined in the proposal that it would be appropriate to provide additional time for the process.

563 See proposed Rule 14a-11(f)(3).

564 See proposed Rule 14a-11(f)(4).

565 See proposed Rule 14a-11(f)(5).

- If, upon review of the nominating shareholder's or group's response, the company determines that the company still may exclude the shareholder nominee or nominees, after providing the requisite notice of and time for the nominating shareholder or group to remedy any eligibility or procedural deficiencies in the nomination, the company would be required to provide notice of the basis for its determination to the Commission no later than 80 calendar days before it files its definitive proxy statement and form of proxy with the Commission. The Commission staff could permit the company to make its submission later than 80 calendar days before the company files its definitive proxy statement and form of proxy if the company demonstrates good cause for missing the deadline;[566]
- The company's notice to the Commission would be required to include:
  - Identification of the nominating shareholder or each member of the nominating shareholder group, as applicable;
  - The name of the nominee or nominees;
  - An explanation of the company's basis for determining that it may exclude the nominee or nominees; and
  - A supporting opinion of counsel when the company's basis for excluding a nominee or nominees relies on a matter of state law;[567]
- The company would be required to file its notice of intent to exclude with the Commission and simultaneously provide a copy to the nominating shareholder or

566 See proposed Rule 14a-11(f)(7).

567 See proposed Rule 14a-11(f)(8).

each member of the nominating shareholder or group;[568]

- The nominating shareholder or group could submit a response to the company's notice to the Commission. The response would be required to be postmarked or transmitted electronically no later than 14 calendar days after the nominating shareholder's or group's receipt of the company's notice to the Commission. The nominating shareholder or group would be required to provide a copy of its response to the Commission simultaneously to the company;[569]
- If requested by the company, the Commission staff would, at its discretion, provide an informal statement of its views (commonly known as a no-action letter) to the company and the nominating shareholder or group;[570]
- The company would provide the nominating shareholder or group with notice, no later than 30 calendar days before it files its definitive proxy statement and form of proxy with the Commission, of whether it will include or exclude the shareholder nominee or nominees.[571]

Some commenters supported the proposed staff review process for handling disputes regarding a company's determination to exclude a shareholder nominee.[572] Other commenters expressed concerns about the staff's expertise and ability to handle disputes in a timely manner.[573] With respect to the timing requirements in the proposed process, two commenters

568 See proposed Rule 14a-11(f)(10).

569 See proposed Rule 14a-11(f)(11).

570 See proposed Rule 14a-11(f)(12).

571 See proposed Rule 14a-11(f)(13).

572 See letters from CFA Institute; CII; P. Neuhauser; Schulte Roth & Zabel; Universities Superannuation.

573 See letters from ABA; Anadarko; BRT; Cleary; Davis Polk; Delaware Bar; ExxonMobil; E.J. Kullman;

supported the proposed 14-day time period for the company to respond to a nominating shareholder's or group's notice.[574] A number of commenters criticized the proposed 14-day time period as too short or requested a longer time period for the company to respond.[575] Commenters explained that boards would need time to consider various issues, such as if the election of a shareholder nominee would trigger issues under the laws and regulations relevant to the company's business (e.g., antitrust laws, government procurement, security clearances and export control) as well as under listing standards and state law.[576] Two commenters supported the proposed 14-day time period for a nominating shareholder or group to respond to a company's notice of deficiency.[577] Two commenters worried the 14-day time period would give too little time for a response and recommended instead a 21-day time period.[578] One commenter warned that the Commission is underestimating the number of boards that would challenge shareholder nominees and the level of intensity of these challenges.[579] This commenter suggested that such challenges and possible litigation would demand significant time and resources from the Commission's staff.[580] Commenters also argued that challenges to Rule 14a-11 nominations likely would raise highly complex issues that fall outside the scope of the staff's

---

Protective; S. Quinlivan; Seven Law Firms; Weyerhaeuser.

574 See letters from CFA Institute; CII.

575 See letters from 26 Corporate Secretaries; Boeing; Con Edison; Honeywell; Kirkland & Ellis; Pfizer; Protective; UnitedHealth; USPE; Wells Fargo; Whirlpool.

576 See letters from Boeing; Honeywell.

577 See letters from CFA Institute; CII.

578 See letters from Protective; USPE.

579 See letter from BRT.

580 Id.

expertise (e.g., whether a candidacy would violate state law).[581] One commenter pointed to difficulties arising from the "dueling" legal opinions situation in the Rule 14a-8 no-action process.[582] A couple commenters believed that courts, rather than the staff, would be better able to resolve disputes regarding shareholder director nominations.[583]

After considering the comments, we believe that it is in shareholders' and companies' interest to have a process available for seeking to resolve certain disputes regarding nominations submitted pursuant to Rule 14a-11.[584] Therefore, the rules we are adopting set out the process by which a company would determine whether to include a shareholder nominee and notify the nominating shareholder or group (or their authorized representative) of its determination.[585] The rules also include a process by which a company would notify a nominating shareholder or group (or their authorized representative) of a deficiency in its notice on Schedule 14N, the nominating shareholder or group would have the opportunity to respond, and the company would send a notice to the Commission if the company intends to exclude a shareholder nominee from its proxy materials. Consistent with the Proposal, a company making the determination to exclude a shareholder nominee will be required to submit a notice to the Commission regarding its determination, and it may also choose to avail itself of the process to seek a no-action letter from

---

581 See letters from ABA; BRT.

582 See letter from ABA.

583 See letters from ABA; Delaware Bar.

584 In this regard, we note that the staff process for aiding in the resolution of disputes related to nominations made pursuant to Rule 14a-11 is non-exclusive. As discussed throughout this release, a company can seek the staff's view with regard to its determination to exclude a nominee from its proxy materials, but it is not required to do so. A company could engage in negotiations with a nominating shareholder or group and ultimately reach a resolution outside of the staff process, or the parties could avail themselves of other alternatives, such as litigation.

585 Other than the modifications to the standards relating to transmission and receipt of notices and responses, which are described below, we are adopting the process as proposed.

the staff with respect to its decision.[586] While we understand the concerns raised by commenters regarding the rule's timing requirements, we believe the requirements are appropriate in light of the need to facilitate the process between a company and its shareholders in time for an annual meeting.[587] In addition, the staff is committed to timely addressing these matters.

We are changing and clarifying the requirements related to the timing of sending and receiving notifications. As proposed, if a company determined that it could exclude a shareholder nominee, it would be required to notify the nominating shareholder or group and the notification would be required to be postmarked or transmitted electronically no later than 14 calendar days after the company received the notice on Schedule 14N. The proposed rule stated that the company would be responsible for providing the notice in a manner that evidences timely receipt by the nominating shareholder or group. The proposed rule also included similar requirements for a response to the notice by the nominating shareholder or group. As adopted, the rules will keep the deadlines as they were proposed but will use a transmission standard in determining the deadlines, similar to the standard discussed above for new Rule 14a-11(g)(1). We believe using such a uniform standard for all notification aspects of the rule will provide clarity and ease of use. Under the final rule, a company's notification must be postmarked or transmitted electronically no later than 14 calendar days after the close of the window period for submission of nominations pursuant to Rule 14a-11. We believe this change from the Proposal

586 We encourage companies and shareholders to attempt to resolve disputes independently. To the extent that a company and nominating shareholder or group are able to resolve an issue at any point during the staff process, the company should withdraw its request for a no-action letter from the staff.

587 The final rule does not include the proposed 30-calendar day notice requirement when a company determines to exclude a nominee. We believe this requirement is rendered unnecessary by the requirement in paragraph (g)(3) of Rule 14a-11 that the company provide notice to the Commission staff and nominating shareholder or group no later than 80 calendar days before the company files its definitive proxy statement and form of proxy. In addition, if a company seeks the staff's informal view with respect to the company's determination to exclude a nominee, promptly following receipt of the staff's response a company would be required to provide a notice to the nominating shareholder or group stating whether it will include or exclude the nominee.

is appropriate because it will allow shareholders to submit their nominations, and companies to receive all the nominations, before requiring a company to send a notice to the nominating shareholder or group (or their authorized representative) as to whether it will include or exclude a nominee. Thus, a company will be able to make an informed decision with respect to individual nominations because it will be able to evaluate and respond to all the nominations it has received at one time, rather than evaluating and responding to the nominations as they are received. This approach should help reduce the possibility of any confusion that could result from requiring a company to respond to each nomination no later than 14 days after it is transmitted.[588] A nominating shareholder's or group's response to the company's notice must be postmarked or transmitted electronically no later than 14 calendar days after receipt of the company's notification. We note that a timely transmission standard applies in both instances; however, we urge companies to send the notification, and nominating shareholders or groups to send a response, in a manner that will allow them to demonstrate when the communication is received, as doing so may avoid potential disputes.

Under new Rule 14a-11(g), a company may exclude a shareholder nominee because:

- Rule 14a-11 is not applicable to the company;
- the nominating shareholder or group or nominee failed to satisfy the eligibility

588 For example, suppose a company decided it did not have a reason to exclude a nominee submitted by a nominating shareholder during the first week of the window period. If we were to require that a company must respond to a nomination no later than 14 days after it was transmitted, the company would be required to respond to the nominating shareholder or group before the window period closed, and the company would inform the nominating shareholder that it intends to include the nominee. If, subsequent to the company sending a notice to the nominating shareholder of its intent to include the nominee, a nominating shareholder with a higher qualifying ownership percentage submits a nomination for the maximum number of nominees the company would be required to include under the rule, the company would be required to include those nominees assuming that the company determined that it did not have a reason to exclude the nominees. In that situation, confusion could result because, under the rule, the company would no longer be required to include the nominee submitted by the nominating shareholder during the first week of the window period, even though the company had informed the nominating shareholder it would include its nominee.

requirements in Rule 14a-11(b);[589] or

- including the nominee or nominees would result in the company exceeding the maximum number of nominees it is required to include in its proxy statement and form of proxy.[590]

In addition, a company would be permitted to exclude a statement in support of a nominee or nominees if the statement in support exceeds 500 words for each nominee.[591] In such cases, a company would be required to include the nominee or nominees, provided the eligibility requirements were satisfied, but would be permitted to exclude the statement in support. Although we did not propose to allow for exclusion of a supporting statement that exceeds the length specified in the rule, we believe that it is appropriate to provide the ability to do so in the final rule.[592]

We note that, in a change from the Proposal, under the final rule a company may not exclude a nominee or a statement in support on the basis that, in the company's view, the Schedule 14N (which will include the statement in support) contains materially false or misleading statements. Nominating shareholders and groups will have liability for any materially false or misleading information or for making a false or misleading certification in the

---

589 Specifically, the final rule provides that a company could exclude a shareholder nominee because the nominating shareholder or group, or the nominee, fails to satisfy the applicable eligibility requirements in Rule 14a-11(b). In this regard, we note that the nominating shareholder or each member of the nominating shareholder group (or authorized representative) would be required to certify that, after reasonable inquiry and to the best of its knowledge and belief, the nominating shareholder or member of the nominating shareholder or group and the nominee satisfied the applicable requirements of Rule 14a-11(b).

590 See new Rule 14a-11(d).

591 See new Rule 14a-11(c).

592 In this regard, we note that this is consistent with Rule 14a-8, which specifies that a company may exclude a proposal if the proposal, including any accompanying supporting statement, exceeds 500 words.

notice filed on Schedule 14N, and companies will not be responsible for this information.[593] We believe that such disputes concerning whether information is false or misleading should be handled through disclosure, and if necessary, through private litigation, rather than through exclusion of the nominee under our rule. A company and the nominating shareholder or group will be in possession of the facts and circumstances regarding any disputes that arise about the truthfulness or accuracy of information or representations made by a nominating shareholder or group; thus, they will be in a better position than the staff to resolve those disputes. In addition, we note that in traditional proxy contests, companies and insurgents regularly use disclosure to communicate with a company's shareholders about an insurgent's nominee(s) and provide related information, including disclosure disputing the information provided by the other party. We believe that it is appropriate for companies and nominating shareholders engaged in the Rule 14a-11 nomination process to work together to resolve these types of issues. While we encourage private parties to resolve disputes under this provision, the Commission could, of course, bring enforcement actions in appropriate instances. All filings associated with a nomination included in the company's proxy materials pursuant to Rule 14a-11, including the Schedule 14N, the company's proxy statement and any additional soliciting materials provided by the company or the nominating shareholder, will be subject to the staff's proxy contest review procedures and, as noted, will be subject to the Rule 14a-9 prohibition against materially false or misleading statements.

In the Proposing Release, we noted that:

- Unless otherwise provided in Rule 14a-11 (e.g., the nominating shareholder's or group's obligation to demonstrate that it responded to a company's notice of deficiency, where applicable, within 14 calendar days after receipt of the notice of

593 See new Rule 14a-9(c) and Rule 14a-11(f).

deficiency), the burden would be on the company to demonstrate that it may exclude a nominee or nominees; and

- All materials submitted to the Commission in relation to proposed Rule 14a-11(g) would be publicly available upon submission.

We are adopting these aspects of the rules as proposed. We did not receive significant comment on these aspects of the proposed rules, although two commenters requested that companies bear the burden of proof when objecting to a nominee.[594] The rule, as adopted and proposed, specifies that the burden is on the company to demonstrate that it may exclude a nominee or statement of support, unless otherwise specified.[595] In addition, as we discussed in the Proposing Release, the staff's responses to the submissions made pursuant to new Rule 14a-11(g) would reflect only informal views. The staff determinations reached in these responses would not, and cannot, adjudicate the merits of a company's position with respect to exclusion of a shareholder nominee under Rule 14a-11. Accordingly, a discretionary staff determination would not preclude an interested person from pursuing a judicial determination regarding the application of Rule 14a-11.

As noted above, if a nominee withdraws or is disqualified, a company will be required to include an otherwise eligible nominee submitted by the shareholder or group with the next highest qualifying ownership percentage, if any. The company would be required to continue replacing withdrawn or disqualified nominees until it included the maximum number of nominees it is required to include in its proxy materials or the list of shareholder nominees is exhausted. As described above, a company will be required to give notice that it plans to

---

594 See letters from CII; Universities Superannuation.

595 In the Proposal, we noted that the exclusion of a nominee or nominees where the exclusion was not permissible would result in a violation of the rule. We are adopting that provision as proposed.

exclude a nominee for any nominee that it intends to exclude, and the notice must include the reasons for the exclusion. If a company anticipates that it would seek a no-action letter from the staff with respect to its decision to exclude any Rule 14a-11 nominee or nominees, it should seek a no-action letter with regard to all nominees that it wishes to exclude at the outset and should assert all available bases for exclusion at that time. For example, if a company receives more nominees than it is required to include, its reasons for exclusion would note that basis. In addition, if the company believes it has other bases to exclude the nominee, it should note those other bases in its notice and include the other bases in its request for a no-action letter.

c. Timing of Process

The process generally would operate as follows:

Due Date	Action Required
No earlier than 150 calendar days, and no later than 120 calendar days, before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting	Nominating shareholder or group must provide notice on Schedule 14N to the company and file the Schedule 14N with the Commission
No later than 14 calendar days after the close of the window period for submission of nominations	Company must notify the nominating shareholder or group (or its authorized representative) of any determination not to include the nominee or nominees
No later than 14 calendar days after the nominating shareholder's or group's receipt of the company's deficiency notice	Nominating shareholder or group must respond to the company's deficiency notice and, where applicable, cure any defects in the nomination
No later than 80 calendar days before the company files its definitive proxy statement and form of proxy with the Commission	Company must provide notice of its intent to exclude the nominating shareholder's or group's nominee or nominees and the basis for its determination to the Commission and, if desired, seek a no-action letter from the staff with regard to its determination
No later than 14 calendar days after the nominating shareholder's or group's receipt of the company's notice to the Commission	Nominating shareholder or group may submit a response to the company's notice to the Commission staff
As soon as practicable	If requested by the company, Commission staff would, at its discretion, provide an informal statement of its views to the company and the nominating shareholder or group
Promptly following receipt of the staff's informal statement of its views	Company must provide notice to the nominating shareholder or group stating whether it will include or exclude the nominee

d. Information required in company proxy materials

i. Proxy statement

As discussed in Section II.B.8. above, we proposed and are adopting a requirement that a company that is including a shareholder director nominee in its proxy statement and form of proxy pursuant to Rule 14a-11 include certain disclosure about the nominating shareholder or group and the nominee in the company proxy statement. This disclosure will be provided by the nominating shareholder or group in its notice on Schedule 14N in response to Item 5 of that

Schedule and will be included in the company's proxy statement pursuant to Item 7(e) (and, in the case of investment companies, Item 22(b)(18)) of Schedule 14A.[596] As we proposed, the company will not be responsible for the disclosure; rather, the nominating shareholder or group will have liability for any materially false or misleading statements.[597]

As discussed in Section II.B.8., the disclosures to be included in the company's proxy statement include:

- A statement that the nominee consents to be named in the company's proxy statement and form of proxy and, if elected, to serve on the company's board of directors;
- Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A, as applicable;
- Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required of a participant in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A, as applicable;
- Disclosure about whether the nominating shareholder or any member of a nominating shareholder group has been involved in any legal proceeding during the past ten years, as specified in Item 401(f) of Regulation S-K;
- Disclosure about whether, to the best of the nominating shareholder's or group's knowledge, the nominee meets the director qualifications set forth in the company's governing documents, if any;

596 Refer to Section II.B.8. for a discussion of comments received on the proposed disclosure and changes made in response to these comments. We did not receive comment specifically on new Items 7(e) or 22(b)(18) of Schedule 14A.

597 See new Rule 14a-11(f).

- A statement that, to the best of the nominating shareholder's or group's knowledge, in the case of a registrant other than an investment company, the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the company, if any, or, in the case of a registrant that is an investment company, the nominee is not an "interested person" of the registrant as defined in Section 2(a)(19) of the Investment Company Act of 1940;
- The following information regarding the nature and extent of the relationships between the nominating shareholder or group, the nominee, and/or the company or any affiliate of the company:
    - Any direct or indirect material interest in any contract or agreement between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the company or any affiliate of the company (including any employment agreement, collective bargaining agreement, or consulting agreement);
    - Any material pending or threatened litigation in which the nominating shareholder or any member of the nominating shareholder group and/or the nominee is a party or a material participant, and that involves the company, any of its officers or directors, or any affiliate of the company;
    - Any other material relationship between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the company or any affiliate of the company not otherwise disclosed; and
    - The Web site address on which the nominating shareholder or nominating shareholder group may publish soliciting materials, if any.

The disclosures set out in Items 4(b) and 5(b) of Schedule 14A are specifically tailored to contested elections and currently are provided by both companies and insurgents in traditional proxy contests. The disclosures required pursuant to Item 4(b) include:

- Who is making the solicitation and the methods of solicitation;
- If employees of the soliciting party are engaged in the solicitation, what types of employees are engaged in the solicitation and the manner and nature of their employment;
- If specially engaged employees are engaged in the solicitation, the material features of the engagement, the cost, and the number of employees;
- The total amount estimated to be spent and the total expenditures to date for the solicitation;
- Who will bear the cost of the solicitation; and
- The terms of any settlement between the company and the soliciting parties, including the cost to the company.

The disclosures included pursuant to Item 5(b) include:

- Any substantial interest of the soliciting party in the matter to be voted on;
- Certain biographical information about the soliciting party, such as name and business address, principal occupation, and any criminal convictions in the past 10 years;
- The amount of company securities beneficially owned and owned of record;
- Dates and amounts of any securities purchased or sold within the past two years and the amount of funds borrowed and owed to purchase the securities;
- Whether the soliciting person is or was within the past year a party to any contracts,

arrangements or understandings with respect to the company's securities and the terms of the contract, arrangement or understanding;

- Beneficial ownership of company securities by any associate of the soliciting person;
- Beneficial ownership by the soliciting person of any parent or subsidiary of the company;
- Disclosure responsive to Item 404(a) of Regulation S-K with regard to the soliciting person and any associate;
- Disclosure of any arrangements concerning future employment or transactions with the company; and
- Any substantial interest in the vote, either by security holdings or otherwise, held by a party to an arrangement or understanding related to a director nominee.

The company also will include in its proxy statement disclosure about the management nominees responsive to Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A, as applicable, as well as disclosure concerning the persons making the solicitation for the management nominees responsive to Items 4(b) and 5(b) of Schedule 14A, as applicable. We did not amend the disclosure requirements in this regard, as companies are already required to make these disclosures in the context of a "solicitation in opposition," under Rule 14a-12(c).[598]

In addition, as discussed in Section II.B.8., we proposed and adopted a requirement that the company include in its proxy statement the nominating shareholder's or group's statement in

598 We have clarified in new Instruction 3 to Rule 14a-12 that inclusion of a shareholder director nominee pursuant to Rule 14a-11, an applicable state or foreign law provision, or a company's governing documents as they relate to the inclusion of shareholder director nominees in the company's proxy materials, or solicitations that are made in connection with that nomination, constitute solicitations subject to Rule 14a-12(c), except for purposes of the requirement for the company to file their proxy statement in preliminary form pursuant to Rule 14a-6(a).

support of the shareholder nominee or nominees, if the nominating shareholder or group elects to have such statement included in the company's proxy materials. As discussed in Section II.B.8., we had proposed that this statement not exceed 500 words total, but in response to commenters' concerns, we have revised this provision in the final rule to enable a nominating shareholder or group to include up to 500 words for each nominee. The company also would have the option to include a statement of support for the management nominees.[599]

ii. Form of proxy

Under the Proposal, a company that is required to include a shareholder nominee or nominees on its form of proxy could identify the shareholder nominees as such and recommend whether shareholders should vote for, against, or withhold votes on those nominees and management nominees on the form of proxy.[600] In addition, the company could determine the order in which its nominees and any shareholder nominees are listed in the form of proxy. The company would otherwise be required to present the nominees in an impartial manner in accordance with Rule 14a-4.

Under the current rules, a company may provide shareholders with the option to vote for or withhold authority to vote for the company's nominees as a group, provided that shareholders also are given a means to withhold authority for specific nominees in the group. In our view, as we stated in the Proposal, this option would not be appropriate where the company's form of

---

599 In the Proxy Disclosure Enhancements Adopting Release, we amended our rules to require disclosure about directors that will provide investors with more meaningful disclosure to enable them to determine whether and why a director or nominee is an appropriate choice for a particular company. The information is required in the company's proxy statement for each director nominee and each director who will continue to serve after the shareholder meeting. Under revised Item 401 of Regulation S-K, a nominating shareholder or group will be required to discuss the particular experience, qualifications, attributes or skills of the nominee or nominees that led the nominating shareholder or group to conclude that the person should be put forward as a candidate for director on the company's board of directors.

600 This would be similar to the current practice with regard to shareholder proposals submitted pursuant to Rule 14a-8 where companies identify the shareholder proposals and provide a recommendation to shareholders as to how they should vote on each of those proposals.

proxy includes shareholder nominees, as grouping the company's nominees may make it easier to vote for all of the company's nominees than to vote for the shareholder nominees in addition to some of the company nominees. Accordingly, when a shareholder nominee is included (either pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents), we proposed an amendment to Rule 14a-4 to provide that a company may not give shareholders the option of voting for or withholding authority to vote for the company nominees as a group, but instead must require that shareholders vote on each nominee separately.

Commenters were mixed on the appropriate presentation of nominees on the form of proxy. Several commenters supported the proposed amendments to Rule 14a-4 to prohibit the option of voting for management's slate as a whole,[601] with one of these commenters characterizing the current option of "elect all directors" as "a convenience in uncontested director elections" but warning that providing that option in contested elections "tilts the scales unduly in favor of management."[602] The commenter believed that shareholders would not have any difficulty in identifying the management nominees and disagreed with the argument that a form of proxy listing all nominees would be confusing. As a possible solution, the commenter suggested a legend such as "There are six candidates. Vote for no more than five." Another commenter argued that the advantage of voting for each individual nominee is the de facto plurality voting standard that would result.[603] Numerous commenters opposed the proposed amendments to Rule 14a-4 and argued that the form of proxy should allow shareholders to vote for the entire slate of management nominees.[604] Many of these commenters believed that such an

601 See letters from CII; COPERA; P. Neuhauser; RiskMetrics; USPE.

602 Letter from CII.

603 See letter from RiskMetrics.

604 See letters from 26 Corporate Secretaries; ABA; Aetna; Alcoa; American Express; Anadarko; Boeing;

option is needed to minimize shareholder confusion,[605] with several commenters justifying such an option on the basis that boards expend considerable efforts in selecting the complete slate of management nominees (e.g., considering issues as the independence of the board as whole).[606] One commenter stated that individual shareholders (unlike large institutional investors who have outsourced the actual proxy voting process for their portfolio) would be discouraged from voting if the proxy voting process becomes overly tedious as a result of the inability to vote for (or withhold votes for) a group of nominees.[607] The commenter analogized to the shareholders' voting options for shareholder proposals, where shareholders are allowed to vote on all matters as recommended by management through the exercise of discretionary voting authority. It noted that, under the existing proxy rules, companies often allow shareholders to vote "For All, except" and then allow them to identify the specific nominees for whom the proxy is not authorized to vote. The commenter recommended that companies be permitted to have this same option when there are shareholder nominees included in the proxy materials (with a clear statement in the form of proxy that the shareholder should indicate a vote for the shareholder nominee in the space provided for that nominee). One commenter argued that the ability to vote on the entire slate is essential in the event that the proposed rules are applied to investment companies, as such entities have a far higher proportion of retail shareholders than most operating companies and consequently have more difficulty in achieving a quorum.[608]

BorgWarner; BRT; ExxonMobil; Fenwick; Honeywell; ICI; Intel; JPMorgan Chase; Pfizer; Seven Law Firms; Society of Corporate Secretaries; Tenet; U.S. Bancorp.

605 See letters from Aetna; American Express; Boeing; BorgWarner; JPMorgan Chase; Seven Law Firms; Society of Corporate Secretaries; U.S. Bancorp.

606 See letters from BorgWarner; Pfizer; Society of Corporate Secretaries; Tenet.

607 See letter from ABA.

608 See letter from ICI.

We are adopting this aspect of the Proposal largely as proposed,[609] because we continue to believe that grouping the company's nominees and permitting them to be voted on as a group would make it easier to vote for all of the company's nominees than to vote for the shareholder nominees in addition to some of the company nominees. This would result in an advantage to the management nominees and would be inconsistent with an impartial approach and the goals of Rule 14a-11. The final rule clarifies that the change would apply not only when a nominee is included pursuant to Rule 14a-11, applicable state law, or a company's governing documents, but also where a nominee is included pursuant to a provision in foreign law.

We believe that potential confusion that may result from not providing the option to vote for the company's slate can be mitigated to the extent that companies provide clear voting instructions, particularly with respect to the number of candidates for which a shareholder can vote. In addition, we do not believe that requiring shareholders to vote for candidates individually, rather than as a group, creates a burden that will result in discouraging shareholders

609 See new Rule 14a-4(b)(2)(iv). We anticipate that companies would continue to be able to solicit discretionary authority to vote a shareholder's shares for the company nominees, as well as to cumulate votes for the company nominees in accordance with applicable state law, where such state law or the company's governing documents provide for cumulative voting.

from voting at all in director elections. In this regard, we note that a company could clearly designate the nominees on its form of proxy as company nominees or shareholder nominees.

e. No preliminary proxy statement

Under the Proposal, inclusion of a shareholder nominee in the company's proxy materials would not require the company to file a preliminary proxy statement provided that the company was otherwise qualified to file directly in definitive form. In this regard, the Proposal made clear that inclusion of a shareholder nominee would not be deemed a solicitation in opposition.[610] We did not receive a significant amount of comment on this aspect of the rule, although two commenters agreed that inclusion of a Rule 14a-11 shareholder nominee should not require the company to file preliminary proxy materials.[611] We are adopting this provision largely as proposed. As adopted, a company would not be required to file a preliminary proxy statement in connection with a nomination made pursuant to Rule 14a-11, an applicable state or foreign law provision, or a company's governing documents.[612]

10. Application of the Other Proxy Rules to Solicitations by the Nominating Shareholder or Group

a. Rule 14a-2(b)(7)

As noted in the Proposing Release, we anticipate that shareholders may engage in communications with other shareholders in an effort to form a nominating shareholder group to aggregate their holdings to meet the applicable minimum ownership threshold to nominate a director. While consistent with the purpose of Rule 14a-11, such communications would be deemed solicitations under the proxy rules. Accordingly, we proposed an exemption from the

610 See proposed revisions to Rule 14a-6(a)(4) and Note 3 to that rule.

611 See letters from ABA; CII.

612 See also discussion in footnote 598 above.

proxy rules for written communications made in connection with using proposed Rule 14a-11[613] that are limited in content and filed with the Commission.[614] As noted in the Proposal, we believed this limited exemption would facilitate shareholders' use of proposed Rule 14a-11 and remove concerns shareholders seeking to use the rule may have regarding certain communications with other shareholders regarding their intent to submit a nomination pursuant to the rule.

Some commenters supported the proposed exemption for soliciting activities by shareholders seeking to form a group for purposes of Rule 14a-11.[615] One of these commenters stated that because "many institutional investors lack incentives to invest actively in seeking governance benefits that would be shared by their fellow shareholders," the rule should avoid imposing unnecessary hurdles or costs on shareholders organizing or joining a nominating group.[616] Another supporter of the exemption stated that soliciting activities to form a group for the purpose of submitting nominations under Rule 14a-11, state law, or a company's governing documents generally should be exempt, with no filing requirement prior to giving the company notice and filing a Schedule 14N.[617] Another commenter also recommended that any exemption also cover solicitations for nominations submitted under state law or a company's governing documents.[618] Finally, one commenter expressed support for the proposed exemption so

613 Under the Proposal, the exemption would not apply to solicitations made when seeking to have a nominee included in a company's proxy materials pursuant to a procedure specified in the company's governing documents or pursuant to applicable state law (as opposed to pursuant to Rule 14a-11).

614 See proposed Rule 14a-2(b)(7)(i).

615 See letters from Group of 80 Professors of Law, Business, Economics and Finance ("Bebchuk, et al."); CalSTRS; CII; P. Neuhauser; RiskMetrics; Schulte Roth & Zabel; USPE.

616 Letter from Bebchuk, et al.

617 See letter from CII.

618 See letter from P. Neuhauser.

shareholders could communicate with other investors to explain their nominee's qualifications and the rationale for submitting their nominations as long as they file all materials with the Commission and do not solicit proxies on behalf of their nominees.[619]

On the other hand, several commenters opposed the creation of a new exemption for soliciting activities to form a nominating group.[620] Two of these commenters stated that the proposed exemption in Rule 14a-2(b)(7) is unnecessary, given the existing exemptions available to nominating shareholders (e.g., Rule 14a-2(b)(2) exemption for communications with up to 10 shareholders and Rule 14a-2(b)(6) for communications in an electronic shareholder forum).[621] One commenter indicated that a solicitation to form a "control" group could have significant implications affecting control of a company if there are no limits on the number of shareholders or aggregated holdings of a nominating group.[622] The commenter asserted that, absent these limits, a shareholder could build a nominating group with hundreds of shareholders owning far in excess of the ownership threshold needed to use Rule 14a-11. The commenter warned that the proposed exemption could facilitate avoidance of the proposed requirements of Rule 14a-11 because the exempt solicitations could be the first stage of a campaign against incumbent directors and in favor of shareholder nominees. This commenter also believed that the exemption should not apply to solicitations undertaken by shareholders to form a nominating shareholder group in order to submit nominees pursuant to state law or a company's governing documents.[623]

619 See letter from RiskMetrics.

620 See letters from ABA; Anadarko; BRT; Seven Law Firms.

621 See letters from ABA; Seven Law Firms.

622 See letter from ABA.

623 Id.

Commenters also suggested the following changes to the proposed exemption:

- The exemption should not be available if the shareholder or any member of the nominating group uses another available exemption for a nomination to be presented at the same shareholder meeting;[624]
- The exemption should not be available for a "data gathering strategy" in which a shareholder is "testing the waters" for other purposes, such as for a traditional proxy contest;[625]
- The shareholder should certify that it has a bona fide intent to present a Rule 14a-11 nomination and the shareholder should be prohibited from nominating directors at the same meeting through means other than Rule 14a-11;[626] and
- The exemption should not be available if the company or another shareholder has publicly announced that the company would be facing a traditional proxy contest.[627]

One commenter stated generally that allowing the "permitted activity among shareholders wishing to nominate a director" would "increase the need for the Commission to police group activity that may be undertaken with an undisclosed control intent."[628]

Two commenters agreed with the Commission that the Rule 14a-2(b)(7) exemption should not be available for solicitations conducted through oral communications.[629] These commenters warned that there would be no way to ensure that orally-communicated information

---

624 See letters from ABA; Seven Law Firms.

625 Id.

626 See letter from ABA.

627 See letters from ABA; Seven Law Firms.

628 Letter from Biogen.

629 See letters from ABA; Seven Law Firms.

is being provided to shareholders in a consistent manner and in accordance with the rule's requirements. One commenter recommended specific changes to the rule to clarify that the exemption is not available for oral communications.[630] On the other hand, several commenters believed that oral communications should be exempt.[631] Some commenters pointed out that such communications are exempt in other contexts and are difficult to monitor in any case.[632] To mitigate the risk of inappropriate communications, one commenter suggested that the Commission require that oral communications made in reliance on the exemption not be inconsistent with any communications previously filed by the shareholder in connection with the nomination.[633]

Two commenters expressed general support for the proposal requiring that a nominating shareholder or group file any soliciting materials published, sent or given to shareholders pursuant to the exemption no later than the date that the material is first published, sent, or given.[634] One commenter argued that if the Commission retains the requirement that solicitations be in writing, then it should relax the "date of first use" filing deadline (with a three business day deadline being its preference).[635] One commenter supported the filing requirement of Rule 14a-2(b)(7)(ii) for soliciting materials published, sent or given to shareholders solicited to become part of a nominating group,[636] while three commenters opposed the filing requirement.[637]

---

630 See letter from Seven Law Firms.

631 See letters from CII; Cleary; P. Neuhauser; Schulte Roth & Zabel; USPE.

632 See letters from CII; USPE.

633 See letter from Cleary.

634 See letters from ABA; CII.

635 See letter from Schulte Roth & Zabel.

636 See letter from ABA.

Of those opposing the requirement, one commenter noted that under the Williams Act, persons contemplating an actual change in control are not required to publicly disclose their activities until a group owning 5% of the company's shares has been formed.[638] One commenter stated that it is possible that a group of shareholders ultimately may decide not to submit a shareholder nominee.[639] Therefore, this commenter believed, any requirement for filings before the group submits a nominee would place an unfair disadvantage on the process of first determining if a nomination is the right course of action, and if so, who the nominee should be. Another commenter suggested that the filing requirement be triggered on the date the shareholder proposes a nominee, not on the date of solicitation.[640] The commenter believed that a shareholder should not be burdened with the filing requirement at the initial stages of determining the feasibility of forming a group.

Three commenters recommended that communications made for the purpose of forming a nominating shareholder group should be permitted to identify possible or proposed nominees,[641] with one commenter adding the condition that the nominee first agree to being named.[642] Two commenters recommended the following additional disclosure in any written soliciting materials used in reliance on the Rule 14a-2(b)(7) exemption:

- the period that the soliciting shareholder held the specified number of shares;
- a description of any short positions or other hedging arrangements through which the

[637] See letters from CalSTRS; COPERA; P. Neuhauser.

[638] See letter from P. Neuhauser.

[639] See letter from COPERA.

[640] See letter from CalSTRS.

[641] See letters from ABA; CII; USPE.

[642] See letter from ABA.

soliciting shareholder reduced or otherwise altered its economic stake in the company;

- a description of any contracts, arrangements, understandings or relationships between the soliciting shareholder and any other person with respect to any securities of the company; and
- a description of any plans or proposals of the shareholder or group with respect to the organization, business or operations of the company.[643]

One commenter added that the required disclosure should be consistent with that required by Items 4 and 6 of Schedule 13D,[644] while another commenter stated that shareholders should be permitted to include a brief statement of the reasons for the formation of the nominating group.[645]

After considering the comments, we are adopting the proposed exemption with certain modifications, including modifications to enable shareholders to communicate orally, to require the filing of a cover page in the form set forth in Schedule 14N (with the appropriate box on the cover page marked) no later than when the solicitation commences, and to clarify the circumstances under which the exemption will be available.[646] We believe that this limited exemption will facilitate shareholders' use of Rule 14a-11 and remove concerns shareholders

---

643 See letters from ABA; Seven Law Firms.

644 See letter from ABA.

645 See letter from Schulte Roth & Zabel.

646 Shareholders also would have the option to structure their solicitations in connection with the formation of a nominating shareholder group, whether written or oral, to comply with an existing exemption from the proxy rules, including the exemption for solicitations of no more than 10 shareholders (Exchange Act Rule 14a-2(b)(2)) and the exemption for certain communications that take place in an electronic shareholder forum (Exchange Act Rule 14a-2(b)(6)). For example, a shareholder could rely on Rule 14a-2(b)(2) to solicit no more than 10 shareholders in an effort to form a nominating shareholder group. If the shareholder's efforts did not result in the formation of a group large enough to meet the ownership thresholds, the shareholder could then rely on Rule 14a-2(b)(7) to continue its efforts to form a nominating shareholder group for the purpose of submitting a nomination pursuant to Rule 14a-11.

seeking to use the rule may have regarding certain communications with other shareholders regarding their intent to submit a nomination pursuant to the rule.

New Rule 14a-2(b)(7) provides an exemption from the generally applicable disclosure, filing, and other requirements of the proxy rules for solicitations by or on behalf of any shareholder in connection with the formation of a nominating shareholder group, provided that the shareholder is not holding the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11(d). In addition, any written communication may include no more than:

- A statement of the shareholder's intent to form a nominating shareholder group in order to nominate a director under Rule 14a-11;
- Identification of, and a brief statement regarding, the potential nominee or nominees or, where no nominee or nominees have been identified, the characteristics of the nominee or nominees that the shareholder intends to nominate, if any;
- The percentage of voting power of the company's securities that are entitled to be voted on the election of directors that each soliciting shareholder holds or the aggregate percentage held by any group to which the shareholder belongs; and
- The means by which shareholders may contact the soliciting party.

Any written soliciting material published, sent or given to shareholders in accordance with the terms of this provision must be filed with the Commission by the nominating shareholder or group, under the company's Exchange Act file number (or in the case of a registered investment company, under the company's Investment Company Act file number), no later than the date the material is first published, sent or given to shareholders. The soliciting material would be required to be filed with a cover page in the form set forth in Schedule 14N, with the appropriate box on the cover page marked to identify the filing as soliciting material pursuant to Rule 14a-2(b)(7).[647] This requirement is largely consistent with the Proposal; however, under the final rule, the solicitation will be filed on Schedule 14N rather than as definitive additional soliciting materials on Schedule 14A, as was proposed. We have made this change to avoid confusion between soliciting materials filed in connection with the formation of a nominating shareholder group under Rule 14a-11 (or in connection with a Rule 14a-11 nomination), as discussed further below, and other proxy materials that may be filed by companies or by participants in a traditional proxy contest.

We also have expanded the exemption to cover oral solicitations. As noted in the Proposal, we originally proposed to limit the exclusion to written communications to address our concern that oral communications could not easily satisfy the filing requirement (which would make it more difficult to monitor use of the exemption). However, after further consideration, we agree with commenters that oral communications should be included within the exemption because it is likely that shareholders will need to speak to each other in order to effectively form a nominating shareholder group. Oral communications will not be limited in content in the way that written communications are limited. In an effort to better monitor and avoid abuse under the exemption, however, a shareholder seeking to form a nominating shareholder group in reliance on the exemption in Rule 14a-2(b)(7) will be required to file a Schedule 14N notice of commencement of the oral solicitation. Because there are no limits on the number of holders that can be solicited in reliance on the new rule, or the contents of the oral communications, we

647 Materials filed in connection with the new solicitation exemptions will be filed under a cover page of Schedule 14N and will appear as a Schedule 14N-S on EDGAR. See new Rule 14a-2(b)(7)(ii). We note that written communications include electronic communications, such as e-mails and Web site postings, and scripts used in connection with oral solicitations.

believe it is important for our staff and the markets to be aware of the commencement of these activities.

The Schedule 14N filing for oral solicitations will consist of a cover page in the form set forth in Schedule 14N, with the appropriate box on the cover page marked to identify the filing as a notice of solicitation pursuant to Rule 14a-2(b)(7). This filing would be made under the company's Exchange Act file number (or in the case of a registered investment company, under the company's Investment Company Act file number), no later than the date of the first communication made in reliance on the rule.

As noted above, some commenters were opposed to the filing requirement for solicitations for various reasons. We have decided to adopt the filing requirement because we believe it is important to provide companies and shareholders with information about potential nominations under Rule 14a-11 when the new solicitation exemption is used to pursue such a nomination. We do not believe that the filing requirement is burdensome, particularly in light of the fact that we are providing shareholders with the opportunity to engage in activities for which they would otherwise need to file a proxy statement or have another exemption available.

More generally, we understand commenters' concerns regarding the solicitation exemptions, including the exemption for oral communications when seeking to form a group, being used as a means to engage in a contest for control, but we believe that requiring a nominating shareholder or group to file a Schedule 14N to provide notice of such communications, along with the other limitations in the rule we are adopting, should mitigate these concerns. In response to commenters' concerns, we have clarified in the rule that a shareholder or group that chooses to rely on new Rule 14a-2(b)(7) would lose that exemption if they subsequently engaged in a non-Rule 14a-11 nomination or solicitation in connection with the subject election of directors other than solicitations exempt under Rule 14a-2(b)(8), or if they become a member of a group, as determined under Section 13(d)(3) of the Exchange Act and Rule 13d-5(b)(1), or otherwise, with persons engaged in soliciting or other nominating activities in connection with the subject election of directors.[648] This could result in the shareholder or group being deemed to have engaged in a non-exempt solicitation in violation of the proxy rules. In addition, we have clarified that, consistent with Rule 14a-11, the exemption is available only where the shareholder is not holding the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11(d). Thus, we do not believe that it is likely that a shareholder or group will use the exemption as a means to engage in a contest for control.

Consistent with the Proposal, neither this exemption nor the exemption set forth in Rule 14a-2(b)(8) (discussed below) will apply to solicitations made when seeking to have a nominee included in a company's proxy materials pursuant to a procedure specified in the company's governing documents (as opposed to pursuant to Rule 14a-11). As we noted in the Proposal, in this instance, companies and/or shareholders would have determined the parameters of the shareholder's or group's access to the company's proxy materials. Given the range of possible criteria companies and/or shareholders could establish for nominations, we continue to believe it would not be appropriate to extend the exemption to those circumstances. Also consistent with the Proposal, we have not extended the exemption to nominations made pursuant to applicable state law provisions,[649] again because state law could establish any number of possible criteria for

---

648 See new Instruction to Rule 14a-2(b)(7).

649 Similarly, the exemption would not be available for solicitations in connection with nominations made pursuant to foreign law provisions.

nominations. A shareholder would need to determine whether one of the existing exemptions applies to their solicitation conducted in connection with a nomination made pursuant to a company's governing documents or state law.

b. Rule 14a-2(b)(8)

Both the nominating shareholder or group and the company may wish to solicit in favor of their nominees for director by various means, including orally, by U.S. mail, electronic mail, and Web site postings. While the company ultimately would file a proxy statement and therefore could rely on the existing proxy rules to solicit outside the proxy statement,[650] shareholders could be limited in their soliciting activities under the current proxy rules. Accordingly, our Proposal included a new exemption to the proxy rules for solicitations by or on behalf of a nominating shareholder or group in support of its nominee who is included in the company's proxy statement and form of proxy.

As proposed, the exemption would be available only where the shareholder is not seeking proxy authority. In addition, any written communications would be required to include specified disclosures, including:

- the identity of the nominating shareholder or group;
- a description of his or her direct or indirect interests, by security holdings or otherwise; and
- a legend advising shareholders that a shareholder nominee is or will be included in the company's proxy statement and that they should read the company's proxy statement when available and that the proxy statement, other soliciting material, and any other relevant documents are or will be available at no charge on the

650 See Exchange Act Rule 14a-12.

Commission's Web site.

Under the Proposal, written soliciting materials also would be required to be filed with the Commission under the company's Exchange Act file number no later than the date the material is first published, sent or given to shareholders.[651] The soliciting material would be required to include a cover page in the form set forth in Schedule 14A, with the appropriate box on the cover page marked.[652]

Three commenters supported the proposed Rule 14a-2(b)(8) exemption for soliciting activities by or on behalf of a nominating shareholder or group in support of the shareholder nominees included in a company's proxy materials, with soliciting materials filed no later than the date that the materials are first used.[653] Two of these commenters explained that because management would solicit votes against the shareholder nominees and for their own nominees, the nominating shareholder, group, and shareholder nominees should have the same ability to solicit, so long as they do not request proxy authority.[654] Another commenter stated that the exemption should apply to solicitations for nominations made pursuant to Rule 14a-11, state law, or a company's governing documents.[655] The commenter opposed any limitations on the soliciting activities by a nominating shareholder or group and viewed such soliciting activities as the same as a company's disclosure opposing a shareholder proposal. One commenter supported the Rule 14a-2(b)(8) exemption for solicitations by a nominating shareholder or group in favor of

---

651 For a registered investment company, the filing would be made under the company's Investment Company Act file number.

652 See proposed Rule 14a-2(b)(8)(iii).

653 See letters from CII; COPERA; P. Neuhauser.

654 See letters from COPERA; P. Neuhauser.

655 See letter from CII.

a shareholder nominee who is included in a company's proxy materials (or against a management nominee), but recommended that the rule specify that the exemption only applies to solicitations in favor of a shareholder nominee (or against a board nominee) that occur after the distribution of the company's proxy materials – this would help avoid confusion and misunderstandings about whether solicitation may occur before the company's proxy materials are available.[656] This commenter also recommended that the exemption not be available if the company or another shareholder has publicly announced that the company would be facing a traditional proxy contest, even from an unrelated shareholder. The commenter also believed that the exemption should be available for any written solicitation by or on behalf of a nominating shareholder or group in support of a nominee included in a company's proxy materials pursuant to state law or the company's governing documents, as long as the nominating shareholder or group does not use a form of proxy that differs from that of the company, does not furnish or otherwise request a form of revocation, abstention, consent or authorization, and files its solicitation material for its nominees (or against the management nominees) with the Commission on the date of first use.

To the extent that it is not included in either the company's proxy materials or Schedule 14N, the commenter also recommended that additional disclosure be required to be included in solicitations made pursuant to Rule 14a-2(b)(8).[657] Another commenter also stated that Rule 14a-2(b)(8) should apply only to solicitations in favor of a shareholder nominee that occur after the

---

656 See letter from ABA.

657 The recommended disclosures included: the period that the soliciting shareholder held the specified number of shares; a description of any short positions or other hedging arrangements through which the soliciting shareholder reduced or otherwise altered its economic stake in the company; a description of any contracts, arrangements, understandings or relationships between the soliciting shareholder and any other person with respect to any securities of the company; and a description of any plans or proposals of the shareholder or group with respect to the organization, business or operations of the company.

mailing of a company's proxy materials.[658] Further, the commenter explained that solicitations should not occur at a time when shareholders do not have access to the more complete and balanced disclosure about all of the nominees in a company's proxy materials.

As adopted, Rule 14a-2(b)(8) provides an exemption from the generally applicable disclosure, filing, and other requirements of the proxy rules for solicitations by or on behalf of a nominating shareholder or group, provided that:

- The soliciting party does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as proxy for a shareholder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization;[659]
- Each written communication includes:[660]
  - The identity of the nominating shareholder or group and a description of his or her direct or indirect interests, by security holdings or otherwise;
  - A prominent legend in clear, plain language advising shareholders that a shareholder nominee is or will be included in the company's proxy statement and that they should read the company's proxy statement when available because it includes important information. The legend also must explain to shareholders that

658 See letter from Seven Law Firms.

659 See new Rule 14a-2(b)(8)(i). The language in this provision generally follows the language in Rule 14a-2(b)(1) and, therefore, we interpret both provisions in the same manner. In this regard, we note the discussion in the Proxy Disclosure and Solicitation Enhancements proposing release of our view of the scope of the term "form of revocation" within the meaning of Rule 14a-2(b)(1) and the proposed amendment to that rule to clarify that the term does not include an unmarked copy of the company's proxy card that is requested to be returned directly to management. See Securities Act Release No. 33-9052; 34-60280 (July 10, 2009) [74 FR 35076]. If we act on the proposed amendments to Rule 14a-2(b)(1), we would expect to make conforming changes to Rule 14a-2(b)(8).

660 See new Rule 14a-2(b)(8)(ii).

they can find the proxy statement, other soliciting material, and any other relevant documents at no charge on the Commission's Web site; and

- Any soliciting material published, sent or given to shareholders in accordance with this exemption must be filed by the nominating shareholder or group with the Commission on Schedule 14N, under the company's Exchange Act file number or, in the case of an investment company registered under the Investment Company Act of 1940, under the company's Investment Company Act file number, no later than the date the material is first published, sent or given to shareholders. Three copies of the material would at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the company is listed and registered. The soliciting material would be required to include a cover page in the form set forth in Schedule 14N, with the appropriate box on the cover page marked.[661]

We are adopting certain modifications to Rule 14a-2(b)(8) from the Proposal to clarify when a party may begin to rely on the exemption and to require that all soliciting material be filed on new Schedule 14N.[662] The exemption is otherwise consistent with the Proposal.

We have added a new instruction to the exemption clarifying that a nominating shareholder or group may rely on the exemption provided in Rule 14a-2(b)(8) after receiving notice from the company in accordance with Rule 14a-11(g)(1) or (g)(3)(iv) that the company will include the nominating shareholder's or group's nominee or nominees.[663] As proposed, a nominating shareholder or group would not have been able to rely on the exemption until their

661 See new Rule 14a-2(b)(8)(iii).

662 As noted above, the soliciting material will be filed under cover of Schedule 14N and will appear as Schedule 14N-S on EDGAR.

663 See Instruction 1 to Rule 14a-2(b)(8).

nominee or nominees are actually included in the company's proxy materials. We received little comment on the appropriate timing for commencement of soliciting activities under the proposed exemption, with one commenter suggesting that Rule 14a-2(b)(8) apply only to solicitations that occur after the mailing of a company's proxy materials,[664] and another suggesting generally that there should be no limitations on soliciting activities by nominating shareholders or groups.[665]

After further consideration, we have determined that a nominating shareholder or group should be able to begin soliciting once there is certainty as to whether their nominees will be included in the company's proxy materials rather than being required to wait for the company to furnish its proxy materials. In this regard, we note that the exemption is consistent with the treatment of insurgent soliciting materials in a traditional proxy contest, as an insurgent may rely on Rule 14a-12(a) to engage in soliciting activities before furnishing shareholders with a proxy statement provided that the soliciting party provides certain disclosure and files a definitive proxy statement before or at the same time as the forms of proxy, consent or authorization are furnished to or requested from shareholders.[666] We have included the requirement that the nominating shareholder or group have received notice that their nominee or nominees will be included in the company's proxy materials before commencing solicitations to avoid confusion and potential abuse of the exemption.

We also have modified the filing requirements for written soliciting materials. Similar to the filing requirements for relying on Rule 14a-2(b)(7), any written soliciting material published, sent or given to shareholders in accordance with the terms of Rule 14a-2(b)(8) must be filed with

---

664 See letter from ABA.

665 See letter from CII.

666 See Exchange Act Rule 14a-12(a).

the Commission on a Schedule 14N, under the company's Exchange Act file number (or in the case of a registered investment company, under the company's Investment Company Act file number), no later than the date the material is first published, sent or given to shareholders. The soliciting material would be required to be filed with a cover page in the form set forth in Schedule 14N, with the appropriate box on the cover page marked to identify the filing as soliciting material pursuant to Rule 14a-2(b)(8). This requirement is largely consistent with the Proposal, however, under the final rule, the solicitation will be filed on Schedule 14N rather than as definitive additional soliciting materials on Schedule 14A, as was proposed. As noted above, we received comment supporting the filing of soliciting materials,[667] however, the commenters did not specifically address whether the filing should be made under cover of Schedule 14N or Schedule 14A. As discussed above with respect to filings made pursuant to Rule 14a-2(b)(7),we have made the change to Schedule 14N to avoid confusion between soliciting materials filed in connection with the formation of a nominating shareholder group under Rule 14a-11 (or in connection with a Rule 14a-11 nomination) and other proxy materials that may be filed by companies or by participants in a traditional proxy contest.

As described in Section II.B.2.e. above, the rules we are adopting today will not prohibit shareholders from submitting Rule 14a-11 nominations for inclusion in company proxy materials when a proxy contest is being conducted by another person concurrently. We are, however, adding a clarification to new Rule 14a-2(b)(8), similar to Rule 14a-2(b)(7), in response to commenters' concern that the exemptions could be used as the first stage of a contest for control. As adopted, the exemption will be lost if a shareholder or group subsequently engages in a non-Rule 14a-11 nomination or solicitation in connection with the subject election of directors or if

667 See letters from CII; COPERA; P. Neuhauser.

they become a member of a group, as determined under Section 13(d)(3) of the Exchange Act and Rule 13d-5(b)(1), or otherwise, with persons engaged in soliciting or other nominating activities in connection with the subject election of directors. The risk of losing the Rule 14a-2(b)(8) exemption and potential liability for engaging in non-exempt solicitations should prevent nominating shareholders or groups from soliciting in relation to any other person's nominees.[668] Further, as discussed in Sections II.B.2.e. and II.B.10.a. above, under Rule 14a-11 a company will not be required to include a nominee or nominees if the nominating shareholder or group is a member of any other group with persons engaged in solicitations in connection with the subject election of directors or other nominating activities; separately conducts a solicitation in connection with the subject election of directors other than a Rule 14a-2(b)(8) exempt solicitation in relation to those nominees it has nominated pursuant to Rule 14a-11 or for or against the company's nominees; or is acting as a participant in another person's solicitation in connection with the subject election of directors. All of these restrictions are designed to address commenters' concerns about collusion and potential abuse of the process. We also believe these restrictions are consistent with the desire to limit Rule 14a-11 to those shareholders or groups that do not have an intent to change the control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11. Finally, we have clarified in an instruction to Rule 14a-2(b)(8)[669] that Rule 14a-2(b)(8) is the only exemption upon which Rule 14a-11 nominating shareholders or groups may rely for their soliciting activities in support of nominees that are or will be included in the company's proxy materials or for or against company nominees. This will help ensure that these persons will not seek proxy authority and will file written

668 See Instruction 3 to Rule 14a-2(b)(8).

669 See Instruction 2 to Rule 14a-2(b)(8).

communications in connection with their soliciting efforts and, we believe, will help to address some of commenters' concerns with regard to confusion and potential abuse of the exemption.

Consistent with the Proposal and as discussed above with regard to Rule 14a-2(b)(7), the exemption will not apply to solicitations made when seeking to have a nominee included in a company's proxy materials pursuant to a procedure specified in the company's governing documents (as opposed to pursuant to Rule 14a-11). As we noted in the Proposal, in this instance, companies and/or shareholders would have determined the parameters of the shareholder's or group's access to the company's proxy materials. Given the range of possible criteria that companies and/or shareholders could establish for nominations, we continue to believe it would not be appropriate to extend the exemption to those circumstances. Also consistent with the Proposal, we have not extended the exemption to nominations made pursuant to applicable state law provisions, again because state law could establish any number of possible criteria for nominations.[670] A shareholder would need to determine whether one of the existing exemptions applies to their solicitation conducted in connection with a nomination made pursuant to a company's governing documents or state law.

11. 2011 Proxy Season Transition Issues

Rule 14a-11 contains a window period for submission of shareholder nominees for inclusion in company proxy materials of no earlier than 150 calendar days, and no later than 120 calendar days, before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting.[671] Shareholders seeking to use new Rule 14a-11 would be able to do so if the window period for submitting nominees for a particular company is open after the

---

670 Similarly, the exemption would not be available for solicitations in connection with nominations made pursuant to foreign law provisions.

671 See Rule 14a-11(b)(10) and discussion in Section II.B.8.c.ii. above.

effective date of the rules. For some companies, the window period may open and close before the effective date of the new rules. In those cases, shareholders would not be permitted to submit nominees pursuant to Rule 14a-11 for inclusion in the company's proxy materials for the 2011 proxy season. For other companies, the window period may open before the effective date of the rules, but close after the effective date. In those cases, shareholders would be able to submit a nominee between the effective date and the close of the window period.

C. Exchange Act Rule 14a-8(i)(8)

1. Background

Currently, Rule 14a-8(i)(8) allows a company to exclude from its proxy statement a shareholder proposal that relates to a nomination or an election for membership on the company's board of directors or a procedure for such nomination or election. This provision currently permits the exclusion of a proposal that would result in an immediate election contest 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.

When the Commission adopted the current language of Rule 14a-8(i)(8) in December 2007,[672] it noted that many disclosures are required for election contests that are not provided for in Rule 14a-8.[673] In this regard, several Commission rules, including Exchange Act Rule 14a-12, regulate contested proxy solicitations to assure that investors receive disclosure to enable them to make informed voting decisions in elections. The requirements to provide these disclosures to

---

672 See Election of Directors Adopting Release.

673 See Election of Directors Adopting Release.

shareholders from whom proxy authority is sought are grounded in Rule 14a-3, which requires that any party conducting a proxy solicitation file with the Commission, and furnish to each person solicited, a proxy statement containing the information in Schedule 14A. Items 4(b) and 5(b) of Schedule 14A require numerous specified disclosures if the solicitation is subject to Rule 14a-12(c), and Item 7 of Schedule 14A also requires important specified disclosures for any director nominee. Finally, all of these disclosures are covered by the prohibition on making a solicitation containing materially false or misleading statements or omissions that is found in Rule 14a-9.

2. Proposed Amendment

In the Proposal, we proposed an amendment to Rule 14a-8(i)(8), the election exclusion, to enable shareholders, under certain circumstances, to require companies to include in their proxy materials shareholder proposals that would amend, or that request an amendment to, a company's governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with proposed Rule 14a-11.[674] The purpose of the proposed amendment was to further facilitate shareholders' rights to nominate directors and promote fair corporate suffrage, while still providing appropriate disclosure and liability protections.

Under the proposed amendment, the shareholder proposal would have to meet the

[674] Under the Proposal, Rule 14a-8(i)(8) would allow shareholders to propose additional means, other than Rule 14a-11, for inclusion of shareholder nominees in company proxy materials. Therefore, under the Proposal, a shareholder proposal that sought to provide an additional means for including shareholder nominees in the company's proxy materials pursuant to the company's governing documents would not be deemed to conflict with Rule 14a-11 simply because it would establish different eligibility thresholds or require more extensive disclosures about a nominee or nominating shareholder than would be required under Rule 14a-11. A shareholder proposal would conflict with proposed Rule 14a-11, however, to the extent that the proposal would purport to prevent a shareholder or shareholder group that met the requirements of proposed Rule 14a-11 from having their nominee for director included in the company's proxy materials.

procedural requirements of Rule 14a-8 (e.g., the proposal could be excluded if the shareholder proponent did not meet the ownership threshold under Rule 14a-8) and not be subject to one of the other substantive bases for exclusion in the rule.[675] The proposed revision of Rule 14a-8(i)(8) would not restrict the types of amendments that a shareholder could propose to a company's governing documents to address the company's provisions regarding nomination procedures or disclosures related to shareholder nominations, although any such proposals that conflict with proposed Rule 14a-11 or state law could be excluded.[676]

In the Proposal, we stated that we continued to believe that, under certain circumstances, companies should have the right to exclude proposals related to particular elections and nominations for director from company proxy materials where those proposals could result in an election contest between company and shareholder nominees without the important protections provided for in the proxy rules. Therefore, while proposing the revision to Rule 14a-8(i)(8) as discussed above, we also proposed to codify certain prior staff interpretations with respect to the types of proposals that would continue to be excludable pursuant to Rule 14a-8(i)(8). As proposed, a company would be permitted to exclude a proposal under Rule 14a-8(i)(8) if it:

- Would disqualify a nominee who is standing for election;
- Would remove a director from office before his or her term expired;
- Questions the competence, business judgment, or character of one or more nominees or directors;
- Nominates a specific individual for election to the board of directors, other than

675 Currently, Rule 14a-8 requires that a shareholder proponent have continuously held at least $2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting for a period of at least one year by the date the proponent submits the proposal. See Rule 14a-8(b). These requirements would remain the same.

676 In this regard, the proposed revision to Rule 14a-8(i)(8) would not make a distinction between binding and non-binding proposals.

pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents; or

- Otherwise could affect the outcome of the upcoming election of directors.

The proposed codification was not intended to change the staff's prior interpretations or limit the application of the exclusion; it was intended to provide more clarity to companies and shareholders regarding the application of the exclusion.

3. Comments on the Proposal

The proposal to amend Rule 14a-8 to revise the election exclusion received widespread support. Numerous commenters expressed general support for the proposed amendments to Rule 14a-8(i)(8), with many of the commenters supporting the Commission's proposal as a whole[677]

[677] See letters from 13D Monitor; ACSI; AFL-CIO; AFSCME; Joseph Ahearn ("J. Ahearn"); Rahim Ali ("R. Ali"); AllianceBernstein; Amalgamated Bank; Americans for Financial Reform; Australian Reward Investment Alliance ("ARIA"); AUST(Q) Superannuation ("AUST(Q)"); W. Baker; Barclays; BCIA; Bebchuk, et al.; R. Blake; William B. Bledsoe ("W. Bledsoe"); Brigham and Associates, LLC ("Brigham"); British Insurers; Ethan S. Burger ("E. Burger"); J. Burke; CalPERS; CalSTRS; Calvert; Cbus ("Cbus"); CFA Institute; John P. Chaney ("J. Chaney"); The Christopher Reynolds Foundation of New York ("Christopher Reynolds Foundation"); CII; COPERA; Corporate Library; Central Pension Fund of the International Union of Operating Engineers ("CPF"); CRMC; L. Dallas; Mike G. Dill ("M. Dill"); T. DiNapoli; Dominican Sisters of Hope; Andrew H. Dral ("A. Dral"); D. Eshelman; First Affirmative; Florida State Board of Administration; Martin Fox ("M. Fox"); Raymond E. Frechette ("R. Frechette"); Glass Lewis; James J. Givens ("J. Givens"); Governance for Owners ("Governance for Owners"); GovernanceMetrics; Michael D. Grabowski ("M. Grabowski"); Greenlining Institute ("Greenlining"); Hermes; HESTA Super Fund ("HESTA"); Sheryl Hogan ("S. Hogan"); David G. Hood ("D. Hood"); IAM; ICGN; Frank Coleman Inman ("F. Inman"); Ironfire; Melinda Katz ("M. Katz"); Michael E. Kelley ("M. Kelley"); Peter C. Kelly ("P. Kelly"); Key Equity Investors, Inc. ("Key Equity Investors"); Victor Kimball ("V. Kimball"); Jeffery Kondracki ("J. Kondracki"); A. Krakovsky; Paul E. Kritzer ("P. Kritzer"); LACERA; C. Levin; Lanny D. Levin ("L. Levin"); LIUNA; LUCRF; Marco Consulting; Maine Securities Corporation ("Maine Securities"); B. McDonnell; James McRitchie ("J. McRitchie"); Mercy Investment Program; M. Metz; David B. Moore ("D. Moore"); Karen L. Morris ("K. Morris"); Robert Moulton-Ely ("R. Moulton-Ely"); Motor Trades Association of Australia Superannuation Fund Pty Limited ("MTAA"); Murray & Murray & Co., LPA ("Murray & Murray"); William J. Nassif ("W. Nassif"); Tom Nappi ("T. Nappi"); D. Nappier; Nathan Cummings Foundation; P. Neuhauser; Nine Law Firms; New Jersey State Investment Council ("NJSIC"); Norges Bank; Non-Government School Superannuation Fund ("Non-Government"); Ontario Teachers' Pension Plan Board ("Ontario Teachers"); OPERS; Thomas Paine ("T. Paine"); Pax World; Pershing Square; Karl Putnam ("K. Putnam"); S. Ranzini; RacetotheBottom; Joan Reekie ("J. Reekie"); Relational; RiskMetrics; D. Roberts; D. Romine; Joseph Rozbicki ("J. Rozbicki"); Schulte Roth & Zabel; Shamrock; Shareowners.org; Sheet Metal Workers; Sisters of Mercy; Social Investment Forum; Sodali; Solutions; Laszlo Sterbinszky (L. Sterbinszky"); Stringer Photography ("Stringer"); SWIB; J. Taub; Teamsters; Aleta Thielmeyer ("A. Thielmeyer"); TIAA-CREF; Trillium; TriState Coalition; T. Rowe Price; L. Tyson; Ursuline Sisters of Tildonk; Universities Supernnuation; USPE; ValueAct Capital; The Value Alliance and Corporate Governance Alliance ("Value Alliance"); R.

and other commenters supporting the amendments while opposing Rule 14a-11.[678] Some commenters expressly supported the adoption of both Rule 14a-11 and amendments to Rule 14a-8(i)(8).[679] Some commenters indicated that the adoption of only the proposed amendments to Rule 14a-8(i)(8), without Rule 14a-11, would not address current shortcomings in corporate governance and achieve the Commission's stated objectives.[680] Of the commenters that supported the Rule 14a-8 amendments but opposed Rule 14a-11, many believed the amendments to Rule 14a-8 would allow procedures for the inclusion of shareholder nominees in company proxy materials to evolve and private ordering under state law to continue, unfettered by the complexities of a federal standard that would apply uniformly to differently situated companies operating under diverse state law regimes.[681]

While supporting the amendments to Rule 14a-8(i)(8), some commenters expressed concerns about certain aspects of the amendments or recommended certain changes.[682] Two

---

VanEngelenhoven; Walden; B. Wilson; Leslie Wolfe ("L. Wolfe"); Steve Wolfe ("S. Wolfe"); Neil Wollman ("N. Wollman"); WSIB; Marcelo Zinn ("M. Zinn").

678 See letters from 26 Corporate Secretaries; 3M; ABA; Advance Auto Parts; Aetna; AGL; Alcoa; Allstate; Alston & Bird; Ameriprise; American Bankers Association; American Express; Anadarko; Applied Materials; Association of Corporate Counsel; Avis Budget; Best Buy; Boeing; Boston Scientific; Brink's; BRT; Burlington Northern; California Bar; Callaway; Caterpillar; Chevron; P. Clapman; Comcast; CSX; Cummins; Davis Polk; Deere; Devon; DTE Energy; DuPont; Eaton; Einstein Noah; Eli Lilly; ExxonMobil; FedEx; Financial Services Roundtable; FMC Corp.; FPL Group; Frontier; GE; General Mills; A. Goolsby; C. Holliday; Home Depot; Honeywell; IBM; ICI; Intel; JPMorgan Chase; E. J. Kullman; N. Lautenbach; MetLife; Microsoft; J. Miller; Motorola; NACD; NIRI; O'Melveny & Myers; Office Depot; P&G; PepsiCo; Pfizer; Piedmont; Praxair; Protective; Ryder; S&C; Safeway; Seven Law Firms; Shearman & Sterling; Sherwin-Williams; SIFMA; Simpson Thacher; Society of Corporate Secretaries; Southern Company; Tenet; Tesoro; Textron; Theragenics; Tidewater; Tompkins; G. Tooker; tw telecom; United Brotherhood of Carpenters; U.S. Bancorp; The Valspar Corporation ("Valspar"); Wachtell; Wells Fargo; Xerox.

679 See letters from AFL-CIO; CFA Institute; CII; Governance for Owners; C. Levin; Marco Consulting; SWIB.

680 See letters from CII; USPE.

681 See letters from American Express; Brink's; BRT; CSX; Davis Polk; DuPont; C. Holliday; GE; General Mills; MetLife; Safeway; Tenet; Verizon.

682 See letters from ABA; BorgWarner; CII; J. McRitchie; P. Neuhauser; O'Melveny & Myers; Seven Law

commenters expressed concerns about the codification of staff policies and interpretations under the current version of Rule 14a-8(i)(8).[683] One commenter expressed concerns that the proposed amendments to Rule 14a-8(i)(8) are broader than necessary to allow proposals seeking to establish access to a company's proxy materials and have the potential of significantly changing the administration of Rule 14a-8(i)(8) with respect to other types of proposals.[684] The commenter also noted that the fact that only four types of proposals have been addressed by the staff in the Rule 14a-8 process could be attributed to the fact that the current standard under Rule 14a-8(i)(8) operated to avoid other impermissible proposals from being presented in the first place. If the current standard is repealed, this commenter worried that the staff would have no basis upon which to assess proposals that attempt to circumvent or supplement the Commission's proxy solicitation rules. The commenter believed that eliminating the current standard would go beyond what is needed to permit shareholders to submit proposals seeking to amend, or request an amendment to, a company's governing documents to establish a procedure for including shareholder-nominated candidates for director in a company's proxy materials. The commenter suggested retaining the current standard in Rule 14a-8(i)(8) and amending the language only to specifically authorize proposals seeking to establish access to a company's proxy materials and require the disclosure provided in proposed Rule 14a-19.

4. Final Rule Amendment

As noted above in Section I.A., we do not believe that adopting changes to Rule 14a-8(i)(8) alone, without adopting Rule 14a-11, will achieve our goal of facilitating shareholders'

Firms.

683 See letters from ABA; Seven Law Firms.

684 See letter from ABA.

ability to exercise their traditional state law rights to nominate directors. We believe that revising Rule 14a-8 will provide an additional avenue for shareholders to indirectly exercise those rights; therefore, the final rules include a revision to Rule 14a-8(i)(8). As adopted, companies will no longer be able to rely on Rule 14a-8(i)(8) to exclude a proposal seeking to establish a procedure in a company's governing documents for the inclusion of one or more shareholder nominees for director in the company's proxy materials.[685]

In addition, we are adopting the proposed amendment to codify the prior staff interpretations largely as proposed. As adopted, companies will be permitted to exclude a shareholder proposal pursuant to Rule 14a-8(i)(8) if it:

- Would disqualify a nominee who is standing for election;
- Would remove a director from office before his or her term expired;
- Questions the competence, business judgment, or character of one or more nominees or directors;
- Seeks to include a specific individual in the company's proxy materials for election to the board of directors; or
- Otherwise could affect the outcome of the upcoming election of directors.[686]

---

685 As we stated in the Proposing Release, a proposal would continue to be subject to exclusion under other provisions of Rule 14a-8. For example, a proposal would be excludable under Rule 14a-8(i)(2) if its implementation would cause the company to violate any state, federal, or foreign law to which it is subject, or under Rule 14a-8(i)(3), if the proposal or supporting statement was contrary to any of the Commission's proxy rules.

686 We note that the rule text adopted differs slightly from the proposed rule text as a result of technical modifications we made to better reflect our intent with respect to the rule. We are adopting amended Rule 14a-8(i)(8) with the language "seeks to include a specific individual in the company's proxy materials for election to the board of directors" rather than "nominates a specific individual for election to the board of directors, other than pursuant to Rule 14a-11, an applicable state law provision, or a company's governing documents." The change in the language from "nominates" to "seeks to include" more accurately reflects the fact that Rule 14a-8 cannot be used as a means to nominate a candidate for election to the board of directors. We also deleted the language regarding Rule 14a-11, an applicable state law provision, or a company's governing documents because we believe it is unnecessary.

We believe that shareholders and companies will benefit from the enhanced clarity that the amended rule will provide concerning the application of the rule. We do not believe that the amendments will result in confusion with regard to the rule's application because the amendments do not change the manner in which Rule 14a-8(i)(8) has been, and will continue to be, interpreted by the staff with respect to other types of proposals.

The amendments to Rule 14a-8(i)(8) could result in shareholders proposing amendments to a company's governing documents that would establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees for director in company proxy materials. These proposals could seek to include a number of provisions relating to nominating directors for inclusion in company proxy materials, and disclosures related to such nominations, that require a different ownership threshold, holding period, or other qualifications or representations than those contained in Rule 14a-11. To the extent that shareholders are successful in adopting amendments to a company's governing documents to establish procedures for the inclusion of one or more shareholder nominees for director in the company's proxy materials, we note that the provision would be an additional avenue for shareholders to submit nominees for inclusion in company proxy materials, not a substitute for, or restriction on, Rule 14a-11. While such amendments proposed by shareholders through Rule 14a-8 would not be excludable under Rule 14a-8(i)(8) as amended, a company may seek to exclude such a proposal on another basis. For example, to the extent a proposal sought to limit the application of Rule 14a-11, a company could seek to exclude the proposal pursuant to Rule 14a-8(i)(3) on the basis that it is contrary to the proxy rules. We considered whether permitting proposals to allow additional means for shareholder director nominees to be included in company proxy materials would create confusion or lack of certainty for companies and their shareholders in light of the final provisions of Rule 14a-11. In the end, however, we have concluded that this possibility of confusion can be addressed through disclosure and is more than offset by the benefits of facilitating shareholders' ability to determine that their companies should have additional provisions allowing for inclusion of shareholder nominees in company proxy materials.

One commenter opposed the application of proposed Rule 14a-8(i)(8) to investment companies for the same reasons that it opposed the application of proposed Rule 14a-11 to investment companies.[687] We have decided to make amended Rule 14a-8(i)(8) applicable to investment companies for the same reasons that we are making Rule 14a-11 applicable to investment companies. Rule 14a-8(i)(8) is intended to further facilitate shareholders' traditional state law rights to nominate directors, which apply to the shareholders of investment companies. As discussed above, we do not believe that the regulatory protections offered by the Investment Company Act or the fact that open-end management investment companies are not required by state law to hold annual meetings serves to decrease the importance of the rights that are granted to shareholders under state law. For further discussion of our reasons for applying the rule to investment companies, see Section II.B.3.b.

5. Disclosure Requirements

We did not propose any new disclosure requirements for a shareholder that submits a proposal that would amend, or that requests an amendment to, a company's governing documents to address the company's nomination procedures for inclusion of shareholder nominees in company proxy materials or disclosures related to those shareholder provisions.[688]

---

687 See letter from ICI.

688 Shareholders submitting a proposal that seeks to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials would be subject to Rule 14a-8's current requirements. See footnote 685 above.

We solicited comment on whether additional disclosure from a shareholder submitting such a proposal would be appropriate. Three commenters opposed requiring disclosure from shareholders who submit such a proposal pursuant to Rule 14a-8 that differs from disclosure required of shareholders who submit other types of Rule 14a-8 proposals.[689] Three commenters recommended generally that a shareholder who submits a Rule 14a-8 proposal regarding a procedure to include shareholder nominees for director in a company's proxy materials should be required to provide additional disclosure (e.g., disclosure about its long-term interest in the company and intentions regarding the shareholder proposal) so that other shareholders could make a fully-informed voting decision.[690] They argued that disclosure at the time of a nomination pursuant to such a procedure would relate only to the election of specific nominees; it would not provide shareholders with enough information to make a voting decision on the proposed procedure and its effect.

As we stated in the Proposing Release, it is our view that disclosure at the time a nominee is submitted and an actual vote is taken on a shareholder nominee is sufficient. Therefore, we are not adopting any new disclosure requirements for a shareholder simply submitting such a proposal because we believe that a shareholder may simply want to amend the company's procedures for including shareholder nominees in company proxy materials, but may not intend to nominate any particular individual.[691]

In proposing amendments to Rule 14a-8(i)(8), we noted that the amendments could result

689 See letters from CII; Florida State Board of Administration; United Brotherhood of Carpenters.

690 See letters from ICI; Keating Muething; O'Melveny & Myers.

691 This approach is different from the disclosure requirements the Commission proposed in the Shareholder Proposals Release in 2007; however, it is consistent with the overall requirements relating to the submission of shareholder proposals – generally, shareholder proponents are not required to provide any specific type of disclosure along with their proposal.

in shareholder proposals that would establish procedures for nominating directors and disclosures related to such nominations that require a different ownership threshold, holding period, or other qualifications or representations than those proposed in Rule 14a-11. In addition, a state could set forth in its corporate code,[692] or a company may choose to amend its governing documents, to establish nomination or disclosure provisions in addition to those provided pursuant to Rule 14a-11 (e.g., a company could choose to allow shareholders to have their nominees included in the company's proxy materials regardless of ownership – in that instance, the company's provision would apply for certain shareholders who otherwise could not have their nominees included in the company's proxy materials pursuant to Rule 14a-11). Accordingly, we proposed amendments to our proxy rules to address the disclosure requirements when a nomination is made pursuant to such a provision.[693]

As proposed, Rule 14a-19 would apply to a shareholder nomination for director for inclusion in the company's proxy materials made pursuant to procedures established pursuant to state law or by a company's governing documents. The proposed rule would require a nominating shareholder or group to include in its shareholder notice on Schedule 14N (which, under the Proposal, also would be filed with the Commission on the date provided to the company) disclosures about the nominating shareholder or group and their nominee that are similar to what would be required in an election contest.[694]

Specifically, the notice on Schedule 14N, as proposed, would be required to include:

---

692 See North Dakota Publicly Traded Corporations Act, N.D. Cent. Code § 10-35-08 (2009). In 2007, North Dakota amended its corporate code to permit five percent shareholders to provide a company notice of intent to nominate directors and require the company to include each such shareholder nominee in its proxy statement and form of proxy. See N.D. Cent. Code § 10-35 et al (2007).

693 See proposed Rule 14a-19.

694 See proposed Rule 14a-19.

- A statement that the nominee consents to be named in the company's proxy statement and to serve on the board if elected, for inclusion in the company's proxy statement;[695]
- Disclosure about the nominee complying with the requirements of Item 4(b), Item 5(b), and Items 7(a), (b) and (c) and, for investment companies, Item 22(b) of Exchange Act Schedule 14A, as applicable, for inclusion in the company's proxy statement;[696]
- Disclosure about the nominating shareholder or members of a nominating shareholder group consistent with the disclosure currently required pursuant to Item 4(b) and Item 5(b) of Schedule 14A;[697]
- Disclosure about whether the nominating shareholder or any member of a nominating shareholder group has been involved in any legal proceeding during the past five years, as specified in Item 401(f) of Regulation S-K. Disclosure pursuant to this section need not be provided if provided in response to Items 4(b) and 5(b) of Schedule 14A;[698]
- The following disclosure regarding the nature and extent of the relationships between

695 See proposed Rule 14a-19(a).

696 See proposed Rule 14a-19(b). This information would identify the nominee, describe certain legal proceedings, if any, related to the nominee, and describe certain of the nominee's transactions and relationships with the company. See Items 7(a), (b), and (c) of Schedule 14A. This information also would include biographical information and information concerning interests of the nominee. See Item 5(b) of Schedule 14A. With respect to a nominee for director of an investment company, the disclosure would include certain basic information about the nominee and any arrangement or understanding between the nominee and any other person pursuant to which he was selected as a nominee; information about the positions, interests, and transactions and relationships of the nominee and his immediate family members with the company and persons related to the company; information about the amount of equity securities of funds in a fund complex owned by the nominee; and information describing certain legal proceedings related to the nominee, including legal proceedings in which the nominee is a party adverse to, or has a material interest adverse to, the company or any of its affiliated persons. See paragraph (b) of Item 22 of Schedule 14A.

697 See proposed Rule 14a-19(c).

698 See proposed Rule 14a-19(d).

the nominating shareholder or group and nominee and the company or any affiliate of the company:

- Any direct or indirect material interest in any contract or agreement between the nominating shareholder or group or the nominee and the company or any affiliate of the company (including any employment agreement, collective bargaining agreement, or consulting agreement);
- Any material pending or threatened litigation in which the nominating shareholder or group or nominee is a party or a material participant, and that involves the company, any of its officers or directors, or any affiliate of the company; and
- Any other material relationship between the nominating shareholder or group or the nominee and the company or any affiliate of the company not otherwise disclosed;[699] and

- Disclosure of any Web site address on which the nominating shareholder or group may publish soliciting materials.[700]

These disclosures would be included in the company's proxy materials pursuant to proposed new Item 7(f) of Schedule 14A, or in the case of investment companies, proposed Item 22(b)(19) of Schedule 14A.

In addition, under the Proposal, the nominating shareholder or group would be required to identify the shareholder or group making the nomination and the amount of their ownership in the company on Schedule 14N. The filing would be required to include, among other disclosures:

---

699 See proposed Rule 14a-19(e).

700 See proposed Rule 14a-19(f).

- The name and address of the nominating shareholder or each member of the nominating shareholder group; and
- Information regarding the aggregate number and percentage of the securities entitled to be voted, including the amount beneficially owned and the number of shares over which the nominating shareholder or each member of the nominating shareholder group has or shares voting or disposition power.

We did not receive a significant amount of comment specifically addressing proposed Rule 14a-19. One commenter believed that the disclosure requirements of Rules 14a-18 and 14a-19 should be virtually identical.[701] The commenter highlighted certain discrepancies, such as the intent to retain the requisite shares through, and subsequent to, the date of election. Another commenter saw no need for a separate rule to deal with nominations submitted under state law or a company's governing documents and therefore urged the Commission not to adopt Rule 14a-19.[702] The commenter believed there are no policy grounds to justify disparate treatment of nominations submitted under state law or a company's governing documents. It warned that a separate rule would only create confusion. Another commenter suggested that we extend the disclosure requirement to nominations submitted pursuant to a provision under foreign law.[703]

As we stated in the Proposing Release, we believe the proposed additional disclosure requirements are necessary to provide shareholders with full and fair disclosure of information that is material when a choice among directors to be elected is presented; thus, we are adopting the disclosure requirement largely as proposed.[704] As noted above, one commenter suggested

---

[701] See letter from P. Neuhauser.

[702] See letter from Cleary.

[703] See letter from Curtis.

[704] As noted in footnote 511 above, the applicable disclosure requirement in Item 401(f) of Regulation S-K

that the disclosure standard should apply to nominations made pursuant to foreign law. We agree that the disclosure is necessary regardless of the source of the ability to nominate candidates for director. We therefore have clarified that the disclosure requirement extends not only to nominations made pursuant to state law or a company's governing documents, but also pursuant to foreign law (in the case of a non-U.S. domiciled company that does not qualify as a foreign private issuer). We continue to believe that these disclosures will assist shareholders in making an informed voting decision with regard to any nominee or nominees put forth by the nominating shareholder or group, in that the disclosures would enable shareholders to gauge the nominating shareholder's or group's interest in the company. We understand the concern that a separate disclosure rule for nominations made pursuant to state or foreign law provisions, or a company's governing documents could create confusion. We note, however, that certain disclosure provisions or certifications applicable to Rule 14a-11 nominations may not be applicable to nominations made pursuant to other provisions. For example, state or foreign law provisions, or the company's governing documents may require different ownership thresholds or holding periods. Therefore, we believe it is necessary to have separate disclosure requirements for nominations made pursuant to state or foreign law, or a company's governing documents. As with disclosures made in connection with a Rule 14a-11 nomination, the nominating shareholder or group would be liable for any materially false or misleading statements in these disclosures pursuant to new paragraph (c) of Rule 14a-9.[705]

---

was amended in the Proxy Disclosure Enhancements Adopting Release to require disclosure regarding legal proceedings for the past 10 years as opposed to past five years. Thus, disclosure would be required about a nominee's or nominating shareholder's participation in legal proceedings during the past 10 years. We also are making clarifying changes to the disclosure required regarding the nature and extent of relationships between the nominating shareholder or group and/or nominee and/or the company or its affiliates. See footnote 514 and accompanying text in Section II.B.8.c.i. above.

705 See proposed Rule 14a-9(c).

As noted above, we have restructured Rule 14a-11, Rule 14a-18, and Schedule 14N. Similarly, while we are adopting the disclosure requirements largely as proposed in Rule 14a-19,[706] they are now included in Item 6 of Schedule 14N. In addition, because we moved the disclosure requirements for Rule 14a-11 from proposed Rule 14a-18 into Schedule 14N, the requirements for shareholders submitting nominations pursuant to a provision in state law or a company's governing documents are being adopted as new Rule 14a-18.

Under the Proposal, a shareholder submitting a nomination pursuant to a state law provision or a provision in a company's governing documents would be required to file a Schedule 14N (with the disclosures required by that Schedule) by the date specified in the advance notice provision, or where no such provision is in place, no later than 120 calendar days before the date the company mailed its proxy materials for the prior year's annual meeting.[707] We are adopting this requirement as proposed. We note that it is likely that a state or foreign law provision or a provision in a company's governing documents will provide a deadline for submission of nominations made pursuant to those provisions. While we believe that shareholders submitting nominations pursuant to those provisions should provide the disclosure required by Schedule 14N, we believe it is appropriate to defer to the deadline, if any, set forth in those provisions. In this regard, we note that timing concerns present in the Rule 14a-11 nomination context (e.g., timing requirements for engaging in the staff no-action process) are not present in this context.

706 As adopted, Item 6(d) of Schedule 14N will require disclosure about a nominating shareholder's involvement in legal proceedings during the past ten years, rather than five years as was proposed. This is due to the Commission's recent amendment of Item 401(f) of Regulation S-K. See footnotes 511 and 704 above.

707 If a company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, then the nominating shareholder or group must provide notice a reasonable time before the registrant mails its proxy materials.

D. Other Rule Changes

1. Disclosure of Dates and Voting Information

As proposed, if a company did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 days from the prior year, within four business days of determining the anticipated meeting date a company would be required to file a Form 8-K to disclose the date by which a nominating shareholder or group must submit notice to include a nominee in the company's proxy materials pursuant to Rule 14a-11.[708] The date disclosed as the deadline for such shareholder nominations for director would be required to be a reasonable time before the company mails its proxy materials for the meeting. We also proposed to require a registered investment company that is a series company to file a Form 8-K disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting and the total number of the company's shares that are outstanding and entitled to vote for the election of directors (or if votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating votes) at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.

We did not receive much comment on this aspect of the rule. One commenter urged the Commission not to require the Form 8-K filing for investment companies, which generally are not required to file Form 8-K.[709] The commenter favored instead a requirement for investment companies to inform shareholders through another method (or combination of methods) of disclosure reasonably designed to provide notice of the date, including via a press release or

---

708 See proposed Item 5.07 to Form 8-K.

709 See letter from ICI.

posting information on the company's Web site. One commenter supported the proposed instruction to Item 5.07 of Form 8-K.[710]

We are adopting this requirement substantially as proposed, although the requirement will be in new Item 5.08 of Form 8-K. A company will be required to file a Form 8-K, within four business days of determining the anticipated date of the meeting, disclosing the date by which a nominating shareholder or group must submit notice to include a nominee in the company's proxy materials pursuant to Rule 14a-11, which date shall be a reasonable time before the registrant mails its proxy materials for the meeting.[711] We also have clarified that where a company is required to include shareholder director nominees in the company's proxy materials pursuant to an applicable state or foreign law provision, or a provision in the company's governing documents then the company is required to disclose the date by which a nominating shareholder or nominating shareholder group must submit the Schedule 14N required pursuant to Rule 14a-18.

A registered investment company that is a series company also must disclose the total number of the company's shares that are outstanding and entitled to vote for the election of directors (or if votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) at the shareholder meeting as of the end of the most recent calendar quarter.[712] We believe it is important to provide

---

710 See letter from ABA.

711 See new Item 5.08 of Form 8-K and new General Instruction B.1. to Form 8-K. A late filing of such form would result in the registrant not being current or timely for purposes of rules and regulations related to form eligibility and the resale of securities. The company would be deemed current once the Form 8-K is filed.

712 See General Instruction B.1 and Item 5.08(b) of Form 8-K; Rules 13a-11(b)(3) and 15d-11(b)(3); and Instruction 2 to Rule 14a-11(b)(1). In the case of registered investment companies, nominating shareholders may rely on the information contained in the Form 8-K filed in connection with the meeting, unless the nominating shareholder or group knows or has reason to know that the information contained

shareholders with information regarding the deadline for submitting such nominations in the event that the date of the meeting at which the election of directors will take place changes significantly. Moreover, we have decided to require registered investment companies to make the disclosures on Form 8-K, as proposed, rather than through another method or combination of methods because we believe that the information that we are requiring is important information that should be filed with the Commission and accessible on EDGAR rather than merely disclosed on a Web site or in a press release.[713]

Exchange Act Rule 14a-5 requires registrants to disclose in a proxy statement the deadlines for submitting shareholder proposals and matters submitted pursuant to advance notice bylaws. We are amending Rule 14a-5 to also require companies to disclose the deadline for submitting nominees for inclusion in the company's proxy materials for the company's next annual meeting of shareholders. This provision will apply with respect to inclusion of nominations in a company's proxy materials pursuant to Rule 14a-11, an applicable state or foreign law provision, or a company's governing documents.[714] We believe that it is necessary to conform the existing requirements in Rule 14a-5, consistent with the proposal to give adequate notice to shareholders about their ability to submit a nominee or nominees for inclusion in a company's proxy materials pursuant to Rule 14a-11. The change should help to avoid any potential confusion regarding the date by which shareholders seeking to have a nominee included in a company's proxy materials would need to submit a Schedule 14N pursuant to Rule 14a-11

---

therein is inaccurate. See discussion in footnote 280.

713 We are not adopting the proposed requirement that a registered investment company that is a series company file a Form 8-K disclosing the company's net assets as of June 30 of the calendar year immediately preceding the calendar year of the meeting. We proposed this requirement in connection with our proposal to use tiered thresholds based on net assets to determine eligibility under Rule 14a-11. Since the rule we are adopting does not use tiered thresholds, the proposed requirement is no longer necessary.

714 See new Rule 14a-5(e)(3).

or Rule 14a-18.

2. Beneficial Ownership Reporting Requirements

As adopted, Rule 14a-11 requires that a nominating shareholder or group hold at least 3% of the voting power of the company's securities entitled to be voted on the election of directors. Although unnecessary to be able to use the rule, it is possible that in aggregating shares to meet the ownership requirement, a nominating shareholder or group will trigger the reporting requirements of Regulation 13D-G, which requires that a shareholder or group that beneficially owns more than 5% of a voting class of any equity security registered pursuant to Section 12 file beneficial ownership reports.[715] Therefore, nominating shareholders will need to consider whether they have formed a group under Exchange Act Section 13(d)(3) and Rule 13d-5(b)(1) that is required to file beneficial ownership reports. Any person (which includes a group as defined in Rule 13d-5(b)(1)) who is directly or indirectly the beneficial owner of more than 5% of a class of equity securities registered under Exchange Act Section 12 must report that ownership by filing an Exchange Act Schedule 13D with the Commission.[716] There are exceptions to this requirement, however, that permit such a person to report that ownership on Schedule 13G rather than Schedule 13D. One exception permits filings on Schedule 13G for a specified list of qualified institutional investors who have acquired the securities in the ordinary course of their business and with neither the purpose nor the effect of changing or influencing control of the company.[717] A second exception applies to persons who beneficially own more

---

715 The term equity security also includes any equity security of any insurance company which would have been required to be registered pursuant to Section 12 of the Exchange Act except for the exemption contained in Section 12(g)(2)(G) of the Act or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940. See Exchange Act Rule 13d-1(i).

716 See Exchange Act Rule 13d-1.

717 See Exchange Act Rule 13d-1(b).

than 5% of a subject class of securities if they acquired the securities with neither the purpose nor the effect of changing or influencing control of the company and they are not directly or indirectly the beneficial owner of 20% or more of the subject class of securities.[718]

Central to Schedule 13G eligibility under the exceptions discussed above is that the shareholder be a passive investor that has acquired the securities without the purpose, or the effect, of changing or influencing control of the company. In addition, shareholders who are filing as qualified institutional investors must have acquired the securities in the ordinary course of their business. Typically, persons who seek to nominate candidates for a company's board of directors would be unable to meet these eligibility requirements to file on Schedule 13G. As we stated in the Proposing Release, however, we believe that the formation of a shareholder group solely for the purpose of nominating one or more directors pursuant to proposed Rule 14a-11, the nomination of one or more directors pursuant to proposed Rule 14a-11, or soliciting activities in connection with such a nomination (including soliciting in opposition to a company's nominees) should not result in a nominating shareholder or nominating shareholder group losing its eligibility to file on Schedule 13G. As a result, we proposed to revise the requirement that the first and second categories of persons who may report their ownership on Schedule 13G must have acquired the securities without the purpose or effect of changing or influencing control of the company and, in the case of Rule 13d-1(b), in the ordinary course of business, to provide an exception for activities solely in connection with a nomination under Rule 14a-11.

Comments on the proposal were mixed. Some commenters generally supported the proposed exceptions from the Schedule 13D filing obligation for a nominating shareholder or group conducting activities solely in connection with a Rule 14a-11 nomination so that it would

[718] See Exchange Act Rule 13d-1(c).

be eligible to report on Schedule 13G rather than Schedule 13D.[719] One such commenter added that the exceptions also should be available to a nominating shareholder or group submitting nominees pursuant to state law or a company's governing documents.[720] One commenter predicted the amendment would encourage use of Rule 14a-11 by large shareholders who are knowledgeable about the company but may be reluctant to take action that may jeopardize their Schedule 13G filer status.[721] One commenter observed more generally that a Schedule 13D filing is unnecessary if the filing requirement of Rule 14a-2(b)(7) is retained because such filings would provide sufficient notice to the market.[722] Even if such filing requirement is not retained, the commenter believed that a Schedule 13D is unnecessary because the underlying assumption of Rule 14a-11 is that there is no control intent.

On the other hand, other commenters opposed generally the proposed exceptions from the Schedule 13D filing obligation.[723] Some of these commenters expressed reservations about creating a broad exemption or carve-out from Exchange Act Section 13(d) "control" concepts.[724] One commenter noted that Rules 13d-1(b), (c) and (e) track the use of the phrase "changing or

719 See letters from CalSTRS; CFA Institute; CII; Florida State Board of Administration; ICI; Schulte Roth & Zabel. Another commenter, ICGN, did not expressly address the proposed amendment but asked the Commission to clarify the definition of "group" so that shareholders would not be dissuaded from acting collectively to use Rule 14a-11 out of concern that a Schedule 13D filing obligation would arise.

720 See letter from CII. In contrast, two commenters stated that the proposed exceptions should not be extended outside the context of Rule 14a-11, and agreed that it would not be possible to address the eligibility standards in provisions of state law or a company's governing documents or ensure that there is no change in control attempt. See letters from ABA; Alston & Bird.

721 See letter from Schulte Roth & Zabel.

722 See letter from P. Neuhauser.

723 See letters from ABA; Alston & Bird; BRT; Cleary; Microsoft; Seven Law Firms; Shearman & Sterling; Society of Corporate Secretaries; Vinson & Elkins.

724 See letters from ABA; Cleary; Microsoft; Seven Law Firm; Shearman & Sterling.

influencing control of the issuer" from Exchange Act Section 13(d)(5).[725] This commenter did not believe there is a persuasive basis for the Commission to provide that, under all circumstances, a shareholder or group seeking to nominate a director, in opposition to the election of incumbent directors, is not seeking to "influence" control of the company. One commenter stated that most election contests would fall within the concept of "influencing the control of the issuer" because they focus on the governance, strategic direction and policy initiatives of the company.[726] Another commenter noted that the Schedule 14N certifications require only that a nominating shareholder has no intention of "changing control" of the company, but does not require the nominating shareholder to certify that it has no intention of "influencing control."[727] Several commenters expressed concerns about inadequate disclosures that would result from the proposed exceptions or pointed to the useful disclosure required by Schedule 13D.[728] One commenter observed that if a nominating shareholder or group has no plans regarding significant changes in the company or relationships with other parties regarding securities of the company, a Schedule 13D filing would not require significant information from a nominating shareholder or group beyond that required by Schedule 14N.[729] This commenter noted that if a nominating shareholder or group, however, has more complicated relationships or intentions relating to the company or its securities, the Schedule 13D filing would provide

---

725 See letter from ABA.

726 See letter from Seven Law Firms.

727 See letter from ABA.

728 See letters from ABA; Alston & Bird; BRT; Seven Law Firms; Society of Corporate Secretaries; Vinson & Elkins.

729 See letter from ABA.

additional information that shareholders would find useful.[730]

We continue to believe that it is appropriate to provide an exception for activities solely in connection with a nomination pursuant to Rule 14a-11 to allow a nominating shareholder or group to report on Schedule 13G. Accordingly, we are adopting, as proposed, the exception from the requirement to file a Schedule 13D (and therefore permitting filing on Schedule 13G) for activities undertaken solely in connection with a nomination under Rule 14a-11. In addition, we are adopting a change to the certifications in Schedule 13G to reflect this exception.[731]

It is important to note that any activity other than those provided for under Rule 14a-11 would make the exception inapplicable. For example, approaching a company's board and urging them to consider strategic alternatives (e.g., sale of non-core assets or a leveraged recapitalization) would constitute activities outside of the Rule 14a-11 nomination, and any nominating shareholder or group engaging in such activities most likely would be ineligible to file on Schedule 13G. The rule changes will not apply to nominating shareholders or groups that submit a nomination pursuant to an applicable state or foreign law provision, or a company's governing documents because in those instances the applicable provisions may not limit the number of board seats for which a shareholder or group could nominate candidates or include a requirement that the nominating shareholder or group lack intent to change the control of the issuer or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under Rule 14a-11 (as is the case under Rule 14a-11). Accordingly, we do not believe it would be appropriate to make a general determination by rule as to whether a nominating shareholder or group under an applicable state

[730] Id

[731] We did not propose the change to the certifications in Schedule 13G; however, we believe this conforming change is necessary to reflect the intent of the exception.

or foreign law provision, or a company's governing documents would be eligible to file on Schedule 13G. Instead, this would be a fact-specific inquiry.

We believe that the disclosures about the nominating shareholder or group required by Rule 14a-11 and Schedule 14N are adequate to allow shareholders to make an informed decision and to keep the market apprised of developments regarding board nomination activities, and do not believe that requiring the additional disclosures in Schedule 13D is necessary for activities solely in connection with a nomination under Rule 14a-11. Because this exception is only available for purposes of the nomination, a nominating shareholder or group would need to reassess its eligibility to continue to report on Schedule 13G as a passive or qualified institutional investor after the election. For example, if a nominating shareholder is also the nominee and is successfully elected to the board, then the shareholder would likely be ineligible to continue filing on Schedule 13G due to its ability as a director to directly or indirectly influence the management and policies of the company. We believe the limited scope of the exemption addresses commenters' concerns about nominating shareholders or groups influencing control of the issuer while reporting on Schedule 13G.

3. Exchange Act Section 16

Section 16[732] applies to every person who is the beneficial owner of more than 10% of any class of equity security registered under Exchange Act Section 12 ("10% owners"), and each officer and director (collectively with 10% owners, "insiders") of the issuer of such security. We did not propose an exemption from Section 16 for groups formed solely for the purpose of nominating a director pursuant to Rule 14a-11.[733] In the Proposal, we explained that we believed

---

[732] 15 U.S.C. 78p.

[733] As discussed in the Proposing Release, the Commission had previously proposed, in 2003, that a group formed solely for the purpose of nominating a director pursuant to Rule 14a-11, soliciting in connection

the existing analysis of whether a group has formed[734] and whether Section 16 applies[735] should continue to apply. We also explained that because the proposed ownership thresholds for Rule 14a-11 were significantly lower than 10%, we did not believe that the lack of an exclusion would have a deterrent effect on the formation of groups, and therefore did not believe it was necessary to propose an exclusion from Section 16.

We also noted in the Proposal that some shareholders, particularly institutions and other entities, may be concerned that successful use of Rule 14a-11 to include a director nominee in company proxy materials may result in the nominating person also being deemed a director under the "deputization" theory developed by courts in Section 16(b) short-swing profit recovery cases.[736] Under this theory it is possible for a person to be deemed a director subject to Section 16, even though the issuer has not formally elected or otherwise named that person a director. We did not propose standards for establishing the independence of the nominee from the nominating shareholder, or members of the nominating shareholder group.

Although we did not propose an exemption from Section 16, we requested comment on, among other things, whether a nominating shareholder group should be excluded from Section 16 and whether subjecting such groups to Section 16 would be a disincentive to using Rule 14a-

---

with the election of that nominee, or having that nominee elected as a director be exempted from Exchange Act Section 16 reporting.

734 See Exchange Act Rule 13d-5(b) [17 CFR 240.13d-5(b)].

735 See Exchange Act Rule 16a-1(a)(1) [17 CFR 240.16a-1(a)(1)].

736 See Feder v. Martin Marietta Corp., 406 F.2d 260 (2d Cir. 1969), cert. denied, 396 U.S. 1036 (1970); Blau v. Lehman, 368 U.S. 403 (1962); and Rattner v. Lehman, 193 F.2d 564 (2d Cir. 1952). The judicial decisions in which this theory was applied do not establish precise standards for determining when "deputization" may exist. However, the express purpose of Section 16(b) is to prevent the unfair use of information by insiders through their relationships to the issuer. Accordingly, one factor that courts may consider in determining if Section 16(b) liability applies is whether, by virtue of the "deputization" relationship, the "deputizing" entity's transactions in issuer securities may benefit from the deputized director's access to inside information.

11. A few commenters recommended that the Commission create an exemption from Section 16 for a group of shareholders that aggregated their holdings in order to submit a nominee pursuant to Rule 14a-11.[737] Commenters reasoned that members of a nominating group that owns more than 10% of the shares could not reasonably be considered company "insiders."[738] These commenters noted that the group would exist for the sole purpose of nominating a candidate and, absent special facts, would have no access to inside information about the company. Thus, these commenters argued that the statutory purpose of Section 16 – the prevention of insider trading – would not be relevant to such groups. Other commenters did not support an exemption from Section 16.[739] Some of these commenters further agreed that no standard should be adopted regarding application of the judicial doctrine concerning "deputized directors."[740]

After considering the comments, we continue to believe that an exclusion from Section 16 is not appropriate for groups formed solely for the purpose of nominating a director pursuant to Rule 14a-11, soliciting in connection with the election of that nominee, or having that nominee elected as director. We also believe that it is not necessary to change the existing analysis of whether a group has formed and whether Section 16 applies. Because the ownership threshold we are adopting for Rule 14a-11 eligibility is significantly less than 10%, shareholders will be able to form groups with holdings sufficient to meet the Rule 14a-11 threshold without reaching the 10% threshold in Section 16. Thus, we do not believe that Section 16 commonly will be a deterrent to use of Rule 14a-11. As such, we believe that shareholders forming a group to submit a nominee for director pursuant to Rule 14a-11 should be analyzed in the same way as

---

737 See letters from ICI; Schulte Roth & Zabel; ValueAct Capital.

738 See letters from ICI; Schulte Roth & Zabel.

739 See letters from ABA; Alston & Bird; CII; Seven Law Firms.

740 See letters from ABA; CII; Seven Law Firms.

any other group for purposes of determining whether group members are 10% owners subject to Section 16. Similarly, we are not adopting standards regarding application of the "deputized director" doctrine, which will be left to existing case law and courts.

4. Nominating Shareholder or Group Status as Affiliates of the Company

We proposed that Rule 14a-11(a) contain a safe harbor providing that a nominating shareholder would not be deemed an "affiliate" of the company under the Securities Act or the Exchange Act solely as a result of using Rule 14a-11.[741] Under the Proposal, this safe harbor would apply not only to the nomination of a candidate, but also where that candidate is elected, provided that the nominating shareholder or group does not have an agreement or relationship with that director otherwise than relating to the nomination. We were concerned that, without such a safe harbor, some nominating shareholders may be deterred from using Rule 14a-11.

We solicited comment on the appropriateness of the proposed safe harbor and posed some specific questions concerning its application. We also asked whether we should include a similar safe harbor provision for nominating shareholders that submit a nominee for inclusion in a company's proxy materials pursuant to an applicable state law provision or a company's governing documents rather than using the proposed rule.

Three commenters provided statements of general support for the proposed safe harbor.[742] One commenter believed that a safe harbor also would be warranted for shareholders submitting

[741] This safe harbor was set forth in Instruction 1 to proposed Rule 14a-11(a). The safe harbor was intended to operate such that the determination of whether a shareholder or group is an "affiliate" of the company would continue to be made based upon all of the facts and circumstances regarding the relationship of the shareholder or group to the company, but a shareholder or group would not be deemed an affiliate "solely" by virtue of having nominated that director.

[742] See letters from CII; Protective; Schulte Roth & Zabel.

nominees pursuant to state law or a company's governing documents.[743] Another commenter believed the safe harbor should not be available once the shareholder nominee is elected.[744] One commenter recommended that Instruction 1 to Rule 14a-11(a) clarify that the presence of agreements, other than those relating only to the nomination, between a nominating shareholder and a candidate or director would not necessarily confer affiliate status on the nominating shareholder, and that Rule 14a-11 is not intended to change the current law regarding affiliate status.[745]

Two commenters opposed the safe harbor.[746] One commenter believed that we should not adopt such a safe harbor without addressing the issue of affiliate status more broadly.[747] It argued that as long as the Commission follows the historical, facts-and-circumstances analysis for the determination of affiliate status in other contexts, it also should follow this practice in the context of Rule 14a-11. Both commenters opposing the safe harbor also did not believe that proposed Instruction 1 to Rule 14a-11(a) would significantly reduce the interpretive analysis needed to determine whether a nominating shareholder is an "affiliate."[748] They argued that it rarely would be clear whether a nominating shareholder's relationship with the company would consist "solely" of its nominating and soliciting activities, no matter how a safe harbor may be worded. They also expressed concern that the safe harbor would discourage nominating shareholders

---

743 See letter from CII.

744 See letter from Protective.

745 See letter from Schulte Roth & Zabel. The commenter explained that nominees often request agreements, such as indemnification agreements, that clearly relate only to their nomination. In other situations, however, nominees and nominating shareholders enter into other agreements, including compensation agreements, which may not relate exclusively to the nomination.

746 See letters from ABA; Seven Law Firms.

747 See letter from ABA.

748 See letters from ABA; Seven Law Firms.

from participating in potentially fruitful discussions with the company, for fear that such participation would go beyond "solely" nominating and soliciting for a director candidate.

After considering the comments, we do not believe that the proposed safe harbor would provide a level of certainty to nominating shareholders concerning their potential "affiliate" status sufficient to warrant a departure from the current application of the term. We believe it is more appropriate to conduct a facts-and-circumstances analysis in this regard, as would currently be the case in other situations. We agree with commenters' views on the limited utility of the safe harbor's application in practice, acknowledging that a nominating shareholder would be obligated to conduct a facts-and-circumstance analysis to determine affiliate status even if we were to adopt the safe harbor as proposed. We also recognize that some nominating shareholders or members of nominating shareholder groups may be reluctant to engage in certain activities that would further the general purpose of Rule 14a-11 due to concerns that such activities would jeopardize their ability to use the safe harbor.

In this light, it does not appear that the proposed safe harbor would meaningfully facilitate use of Rule 14a-11, if at all, and may, in fact, deter it because some nominating shareholders or members of nominating shareholder groups may limit their activities out of concern that their activities would jeopardize reliance on the safe harbor. Accordingly, we have decided neither to adopt a safe harbor under the rule nor to adopt a similar safe harbor for shareholders submitting nominees pursuant to state law or a company's governing instruments. Instead, as is currently the case in other contests, those who use the rule will need to analyze affiliate status on a case-by-case basis, taking into consideration all relevant facts and circumstances, including the circumstances surrounding a nomination and election of a shareholder nominee.

E. Application of the Liability Provisions in the Federal Securities Laws to Statements Made By a Nominating Shareholder or Nominating Shareholder Group

It is our intent that a nominating shareholder or group relying on Rule 14a-11, an applicable state or foreign law provision, or a company's governing documents to include a nominee in company proxy materials be liable for any statement included in the Schedule 14N or other related communications, or which it causes to be included in a company's proxy materials, which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact or omits to state any material fact necessary to make the statements therein not false or misleading. To this end, we proposed to add a new paragraph (c) to Rule 14a-9 to specifically address a nominating shareholder's or group's liability when providing information on a Schedule 14N to be included in a company's proxy materials pursuant to Rule 14a-11.

As proposed, new paragraph (c) stated that "no nominee, nominating shareholder or nominating shareholder group, or any member thereof, shall cause to be included in a registrant's proxy materials, either pursuant to the federal proxy rules, an applicable state law provision, or a registrant's governing documents as they relate to including shareholder nominees for director in registrant proxy materials, any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to a solicitation for the same meeting or subject matter which has become false or misleading."

Commenters generally supported the proposal to impose Rule 14a-9 liability on nominating shareholders or groups that caused false or misleading statements to be included in a company's proxy materials. One commenter supported the use of Rule 14a-9 as the standard for assigning liability, as the standards under that rule are well known and therefore would promote uniformity.[749] The commenter further stated that Rule 14a-9(c) makes sufficiently clear that a nominating shareholder or group would be liable for statements included in its Schedule 14N or notice to the company that is included in the company's proxy materials. As for the consequences of providing materially false information or representations in a Schedule 14N, the commenter stated that such a situation should be handled in the same way as materially false statements or omissions in a Schedule 14A or other soliciting material filed in connection with a proxy contest. Another commenter suggested that the disclosure provided to the company by the nominating shareholder or group and included in the company's proxy materials be treated as the shareholder's or group's soliciting materials.[750] The commenter did not believe that Rule 14a-9(c) makes clear that the nominating shareholder or group would be liable for any information included in its Schedule 14N or notice to the company that is included in the company's proxy materials. One commenter stated that members of a nominating group should be jointly and severally liable to the company for material misstatements or omissions provided to the company about the group or its members.[751] Another commenter, noting investors' concerns about exposure to joint liability from participating with other investors to nominate a candidate, requested that the Commission add additional commentary about the limits of joint liability for unapproved statements of other members of a nominating group.[752] One commenter suggested that a nominating shareholder or group should be required to indemnify the company for any

749 See letter from CII.

750 See letter from Protective.

751 See letter from Verizon.

752 See letter from Universities Superannuation.

costs incurred in connection with any misstatements or omissions in the information provided to the company for inclusion in the company's proxy materials.[753]

We are adopting Rule 14a-9(c) largely as proposed, but with specific references to statements made in the Schedule 14N and other related communications and a clarification that the rule would apply where a nominee is submitted pursuant to a foreign law provision in addition to a state law provision or the company's governing documents. New Rule 14a-9(c) provides that "no nominee, nominating shareholder or nominating shareholder group, or any member thereof, shall cause to be included in a registrant's proxy materials, either pursuant to the federal proxy rules, an applicable state or foreign law provision, or a registrant's governing documents as they relate to including shareholder nominees for director in registrant proxy materials, include in a notice on Schedule 14N, or include in any other related communication, any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to a solicitation for the same meeting or subject matter which has become false or misleading." The changes to the rule text are intended to clarify that a nominating shareholder or group would be liable for statements it makes regarding the nomination, regardless of whether those statements ultimately appear in the company's proxy statement, as we consider any statements that are made in the Schedule 14N or in other communications to be part of the solicitation by the nominating shareholder or group. Consistent with this view, the Schedule 14N filing (as well as any other related communications) would be considering soliciting materials for purposes of Section 14(a) liability.

---

753 See letter from Verizon.

Under the Proposal, the rule also included express language providing that the company would not be responsible for information that is provided by the nominating shareholder or group under Rule 14a-11 and then repeated by the company in its proxy statement, except where the company knows or has reason to know that the information is false or misleading.[754] A similar provision was proposed in Rule 14a-19 with regard to information provided by the nominating shareholder or group in connection with a nomination made pursuant to an applicable state law provision or a company's governing documents.[755]

A number of commenters opposed the "knows or has reason to know" standard.[756] Many commenters argued generally that because the Commission's Proposal would eliminate the board's involvement in selecting the shareholder nominees and prevent a company from excluding any information from its proxy materials, the company should not be liable for information provided by the nominating shareholder, group, or nominee.[757] Commenters further noted that companies would not have adequate time or sufficient means to investigate the statements made by the nominating shareholder, group, or nominee.[758] Therefore, these commenters argued that it would be inappropriate to shift onto companies any liability for statements made by a nominating shareholder, group, or nominee or impose a duty to investigate or otherwise confirm the accuracy of the information provided by a nominating shareholder,

754 See proposed Rule 14a-11(e).

755 See Note to proposed Rule 14a-19.

756 See letters from ABA; Alaska Air; American Bankers Association; Ameriprise; BorgWarner; BRT; Caterpillar; Cleary; DTE Energy; ExxonMobil; Honeywell; ICI; Protective; S. Quinlivan; Seven Law Firms; Sidley Austin; Society of Corporate Secretaries; Southern Company; UnitedHealth; Verizon.

757 See letters from American Bankers Association; Ameriprise; BorgWarner; BRT; Caterpillar; ExxonMobil; Honeywell; S. Quinlivan; UnitedHealth; Verizon.

758 See letters from Alaska Air; BorgWarner; BRT; DTE Energy; Protective; Seven Law Firms; Society of Corporate Secretaries.

group, or nominee.[759] One commenter predicted that if a company is liable for information provided by a nominating shareholder or group and included in a company's proxy materials pursuant to Rule 14a-11, an applicable state law provision, or a provision in a company's governing documents, it would challenge in court any information provided by a nominating shareholder, group, or nominee that it suspects is materially false or misleading.[760] The commenter asserted that this type of expensive and time-consuming litigation likely would undermine the Commission's goals for the rule. Some commenters believed that the appropriate standard would be the standard in Rule 14a-8(l)(2) and Rule 14a-7(a)(2)(i): "the company is not responsible for the contents of [the shareholder proponent's] proposal or supporting statement."[761] Other commenters recommended generally that the Commission allow companies to provide certain disclaimers in their proxy materials regarding the statements provided by the nominating shareholder or group,[762] with one commenter suggesting that companies also should be able to set the nominating shareholder's or group's statements apart from their own statements by using different fonts, colors, graphics or other visual devices.[763]

Two commenters addressed the issue of a company's liability for disclosure provided by a nominating shareholder or group that is determined to be materially false or misleading after the proxy materials have been sent.[764] One commenter stated that companies should not have

759 See letters from Alaska Air; BorgWarner; BRT; DTE Energy; Protective; Seven Law Firms; Sidley Austin; Society of Corporate Secretaries; Southern Company; United Health; Verizon.

760 See letter from ABA.

761 See letters from ABA; BorgWarner; BRT; Caterpillar; Society of Corporate Secretaries; Southern Company.

762 See letters from Alaska Air; BorgWarner; BRT; ICI; Protective.

763 See letter from BRT.

764 See letters from ABA; Sidley Austin.

liability for failing to correct or recirculate proxy materials if, after the company mails its proxy materials, it is notified (or learns) that the information provided by a nominating shareholder or group is (or has become) materially false or misleading.[765] The commenter noted that the burden of updating and correcting information provided by a nominating shareholder or group should be solely the obligation of that shareholder or group. Another commenter provided similar views, noting that "[i]n situations where the registrant's changes have not been permitted, and certainly after the proxy materials have been published, we think the burden [of correcting or recirculating proxy materials] should be on the nominating shareholder and that the exception imposing liability on the registrant should not apply."[766] One commenter recommended that if Rule 14a-11 is adopted, the rule should state that liability is only attached when "the company knows or is grossly negligent in not knowing that the information is false or misleading."[767] Another commenter asked that the company be liable for false and misleading information provided by a nominating shareholder or group only if it knew the information was false or misleading.[768]

After considering the comments, we are adopting the proposed provision stating that companies will not be responsible for information that is provided by the nominating shareholder or group under Rule 14a-11 and then repeated by the company in its proxy statement. This is the same standard used in Rule 14a-8. We modified the proposed provision in response to commenters to remove the reference to information that the company knows or has reason to know is false or misleading. We believe that the standard that currently is used in Rule 14a-8 is well understood and that it would add unnecessary confusion and create significant uncertainty

---

765 See letter from ABA.

766 Letter from Sidley Austin.

767 See letter from Ameriprise.

768 See letter from ICI.

for companies to alter the standard in the context of Rule 14a-11. Using the Rule 14a-8 standard also is consistent with our revision to Rule 14a-11 to remove as a basis for exclusion of a nominee that information in the Schedule 14N is false or misleading. Accordingly, the final rule contains express language providing that the company will not be responsible for information that is provided by the nominating shareholder or group under Rule 14a-11 and then reproduced by the company in its proxy statement.[769] A similar provision is included in an instruction to new Rule 14a-18 with regard to information that is provided by the nominating shareholder or group in connection with a nomination made pursuant to an applicable state or foreign law provision, or the company's governing documents.[770]

As noted above, commenters raised concerns about correcting or recirculating proxy materials and potential liability for failing to correct or recirculate proxy materials after learning that material a nominating shareholder or group provided is false or misleading. As discussed above, under the rules as adopted, a company will not be responsible for any information that is provided by the nominating shareholder or group under Rule 14a-11 and then reproduced by the company in its proxy statement – the nominating shareholder or group will have liability for that information. Accordingly, a company will not be required to recirculate or correct proxy materials if it learns that the materials provided to shareholders included false or misleading information from the nominating shareholder or group.

Under the Proposal, any information provided to the company in the notice from the nominating shareholder or group under Rule 14a-11 (and, as required, filed with the Commission by the nominating shareholder or group) and then included in the company's proxy materials

---

769 See Rule 14a-11(f).

770 See Instruction to new Rule 14a-18. See also Note to proposed Rule 14a-19.

would not be incorporated by reference into any filing under the Securities Act, the Exchange Act, or the Investment Company Act unless the company determines to incorporate that information by reference specifically into that filing.[771] A similar provision was proposed regarding information provided by the nominating shareholder or group in connection with a nomination made pursuant to an applicable state law provision or a company's governing documents.[772]

Those commenting on this provision stated that information provided by a nominating shareholder, group, or nominee should not be deemed to be incorporated by reference into Securities Act, Exchange Act or Investment Company Act filings,[773] but if it is, it should be treated as the responsibility of the nominating shareholder, group, or nominee rather than the company.[774]

We are adopting this provision as proposed.[775] To the extent the company does specifically incorporate the information by reference or otherwise adopt the information as its own, however, we will consider the company's disclosure of that information as the company's own statements for purposes of the anti-fraud and civil liability provisions of the Securities Act, the Exchange Act, or the Investment Company Act, as applicable.

---

771 See the Instruction to proposed Item 7(e) of Schedule 14A; Instruction to proposed Item 22(b)(18) of Schedule 14A.

772 See the Instruction to proposed Item 7(f) of Schedule 14A; Instruction to proposed Item 22(b)(19) of Schedule 14A.

773 See letters from ABA; CII; Protective.

774 See letters from ABA; Protective.

775 See the Instruction to Item 7(e) of Schedule 14A and Instruction to Item 22(b)(18) of Schedule 14A with regard to information provided in connection with a Rule 14a-11 nomination. See the Instruction to Item 7(f) of Schedule 14A and Instruction to Item 22(b)(19) of Schedule 14A with regard to information provided in connection with a nomination made pursuant to applicable state law or a company's governing documents.

III. PAPERWORK REDUCTION ACT

A. Background

Certain provisions of the final rules contain "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995.[776] We published a notice requesting comment on the collection of information requirements in the Proposing Release for the rules, and we submitted these requirements to the Office of Management and Budget for review in accordance with the PRA.[777] The titles for the collections of information are:

(1) "Proxy Statements – Regulation 14A and Schedule 14A" (OMB Control No. 3235-0059);

(2) "Information Statements – Regulation 14C and Schedule 14C" (OMB Control No. 3235-0057);

(3) "Form ID" (OMB Control No. 3235-0328);

(4) "Schedule 14N";

(5) "Securities Ownership – Regulation 13D and 13G (Commission Rules 13d-1 through 13d-7 and Schedules 13D and 13G)" (OMB Control No. 3235-0145);

(6) "Form 8-K" (OMB Control No. 3235-0060); and

(7) "Rule 20a-1 under the Investment Company Act of 1940, Solicitations of Proxies, Consents, and Authorizations" (OMB Control No. 3235-0158).

These regulations, rules and forms were adopted pursuant to the Exchange Act and the Investment Company Act, among other statutes, and set forth the disclosure requirements for securities ownership reports filed by investors, proxy and information statements,[778] and current

---

776 44 U.S.C. 3501 et seq.

777 44 U.S.C. 3507(d) and 5 CFR 1320.11.

778 The proxy rules apply only to domestic companies with securities registered under Section 12 of the Exchange Act and to investment companies registered under the Investment Company Act. The number of annual reports by reporting companies may differ from the number of proxy and information statements

reports filed by companies to provide investors with the information they need to make informed voting or investing decisions. The hours and costs associated with preparing, filing, and sending these schedules and forms constitute reporting and cost burdens imposed by each collection of information. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. Compliance with the rules is mandatory. Responses to the information collection will not be kept confidential and there is no mandatory retention period for the information disclosed.

B. Summary of the Final Rules and Amendments

As discussed above in more detail, the final rules provide shareholders with two ways to more fully exercise their traditional state law rights to nominate and elect directors. First, new Exchange Act Rule 14a-11 will, under certain circumstances, require companies to include in their proxy materials shareholder nominees for director submitted by long-term shareholders or groups of shareholders with significant holdings. Rule 14a-11 will apply to all reporting companies subject to the Exchange Act proxy rules, with a few exceptions. Rule 14a-11 will apply only when applicable state or foreign law or a company's governing documents do not prohibit shareholders from nominating a candidate for election as a director. Further, Rule 14a-11 will not apply to companies subject to the proxy rules solely because they have a class of debt securities registered under Section 12 of the Exchange Act. Rule 14a-11 will apply to smaller reporting companies, but on a delayed basis. Consistent with the Proposal, companies are not able to "opt out" of the rule in favor of a different framework for including shareholder director

filed with the Commission in any given year. This is because some companies are subject to reporting requirements by virtue of Section 15(d) of the Exchange Act, and therefore are not covered by the proxy rules. Also, some companies are subject to the proxy rules only because they have a class of debt registered under Section 12. These companies generally are not required to hold annual meetings for the election of directors. In addition, companies that are not listed on a national securities exchange or national securities association may not hold annual meetings and therefore would not be required to file a proxy or information statement.

nominees in company proxy materials. In addition, as was proposed, the rule will apply regardless of whether any specified event has occurred to trigger the rule and regardless of whether the company is subject to a concurrent proxy contest.

A nominating shareholder or group seeking to use Rule 14a-11 to require a company to include a nominee or nominees in the company's proxy materials will be required to meet certain conditions, including an ownership threshold and holding period and filing a Schedule 14N to provide required disclosures and certifications. Under the rule, a company will not be required to include a shareholder nominee or nominees for director in the company's proxy materials where the nominating shareholder or group holds the securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11. A company also will not be required to include a nominee submitted pursuant to Rule 14a-11 who does not meet the requirements of the rule. For example, a company would not be required to include a nominee if that nominee's candidacy, or if elected, board membership, would violate applicable federal law, state law, foreign law, or the rules of a national securities exchange or a national securities association (other than the rules related to director independence) and such violation could not be cured during the time period provided in the rule.[779]

Second, the new amendment to Exchange Act Rule 14a-8(i)(8)[780] will preclude a company from relying on Rule 14a-8(i)(8) to exclude from its proxy materials shareholder

---

779 For an additional discussion of the Rule 14a-11 eligibility requirements, see Section II.B.4 above.

780 Exchange Act Rule 14a-8 requires a company to include a shareholder proposal in its Schedule 14A unless the shareholder has not complied with the procedural requirements in Rule 14a-8 or the proposal falls within one of the 13 substantive bases for exclusion in Rule 14a-8, including Rule 14a-8(i)(8).

proposals by qualifying shareholders seeking to establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees in a company's proxy materials including, for example, proposals to allow lower ownership thresholds or higher numbers of shareholder director nominees.[781]

In connection with Rule 14a-11 and the amendment to Rule 14a-8(i)(8), we also are adopting new rules that will require a notice to be filed with the Commission on new Schedule 14N, and transmitted to the company, when a shareholder seeks to submit a nomination to a company pursuant to Rule 14a-11 or pursuant to applicable state or foreign law provision or the company's governing documents.[782] The Schedule 14N will require a nominating shareholder or group to provide disclosure similar to the disclosure currently required in a contested election. The company will be required to include the disclosure provided by the nominating shareholder or group in its proxy materials. Thus, the new rules will require a company to provide additional disclosure on Schedules 14A and 14C,[783] as well as Form 8-K, and a nominating shareholder or group to provide disclosure on new Schedule 14N.

---

781 In this regard, we note that to the extent that a shareholder proposal seeks to establish a procedure for the inclusion of shareholder nominees for director in a company's proxy materials, generally any such proposal adopted by shareholders would not affect the availability of Rule 14a-11. To the extent that a proposal seeks to restrict shareholder reliance on Rule 14a-11, the proposal would be subject to exclusion pursuant to Rule 14a-8(i)(2) because it would cause the company to violate federal law or pursuant to Rule 14a-8(i)(3) because the proposal would be contrary to the proxy rules.

782 See Sections II.B.8 and II.C.5 above.

783 Schedule 14A prescribes the information that a company with a class of securities registered under Exchange Act Section 12, or a person soliciting shareholders of such a company, must include in its proxy statement to provide shareholders with material information relating to voting decisions.

Schedule 14C prescribes the information that a company with a class of securities registered under Exchange Act Section 12 must include in its information statement in advance of a shareholders' meeting when it is not soliciting proxies from its shareholders, including when it takes corporate action by written authorization or consent of shareholders.

Investment Company Act Rule 20a-1 requires registered investment companies to comply with Exchange Act Regulation 14A or 14C, as applicable. The annual responses to Investment Company Act Rule 20a-1 reflect the number of proxy and information statements that are filed by registered investment companies.

When filed in connection with Rule 14a-11, Schedule 14N requires disclosure about the amount and percentage of securities entitled to be voted on the election of directors by the nominating shareholder or group and the length of ownership of such securities. Schedule 14N also requires disclosure similar to the disclosure currently required for a contested election and disclosure of whether the nominee satisfies the company's director qualifications.[784] Schedule 14N also requires a certification that the nominating shareholder or group is not holding any of the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11. A nominating shareholder or group also will be required to certify that the nominating shareholder or group and the nominee satisfy the applicable requirements of Rule 14a-11.

When a Schedule 14N is filed in connection with a nomination pursuant to an applicable state or foreign law provision or a company's governing documents providing for the inclusion of one or more shareholder director nominees in company proxy materials, the Schedule 14N requires similar, but more limited, disclosures than a Schedule 14N filed in connection with a nomination pursuant to Rule 14a-11.[785] In addition, a nominating shareholder or group filing a Schedule 14N in connection with a nomination submitted for inclusion in a company's proxy materials pursuant to applicable state or foreign law or a company's governing documents will be required to provide a more limited certification than is required for a nomination pursuant to Rule 14a-11.[786]

---

784 See Item 5 of Schedule 14N.

785 See Item 6 of Schedule 14N.

786 See Item 8(b) of Schedule 14N.

We also are adopting two new exemptions from the proxy rules for solicitations by a shareholder or group in connection with a nomination pursuant to Rule 14a-11.[787] The first exemption addresses written and oral solicitations by shareholders that are seeking to form a nominating shareholder group, provided that certain requirements are met.[788] The second new exemption will apply to written and oral solicitations by or on behalf of a nominating shareholder or group that has met the requirements of Rule 14a-11 in favor of shareholder nominees or for or against company nominees.[789] Each of these new exemptions requires the shareholder or group soliciting in connection with a nomination pursuant to Rule 14a-11 to file under cover of Schedule 14N any written materials published, sent or given to shareholders no later than the date such materials are first published, sent or given to shareholders. In addition, persons relying on Rule 14a-2(b)(7) to commence oral solicitations must file a notice of such solicitation under cover of Schedule 14N.

C. Summary of Comment Letters and Revisions to Proposal

We requested comment on the PRA analysis in the Proposing Release. Three commenters addressed our estimate of 30 burden hours for a company that is associated with including a nominee in its proxy materials.[790] According to a survey that BRT conducted, two commenters noted that if a company determines that it will include a shareholder nominee, the costs of preparing a written notice to the nominating shareholder or group, as well as including in the company's proxy materials the name of, and other disclosures concerning, the nominee, and

---

787 For further discussion of these exemptions, see Section II.B.10 above.

788 See new Rule 14a-2(b)(7).

789 See new Rule 14a-2(b)(8).

790 See letters from BRT; S&C; Society of Corporate Secretaries. In response to these comments, we have increased some of our burden estimates. See footnotes 815 and 817 below.

preparing the company's own statement regarding the shareholder nominee would require a total of an average of 99 hours of company personnel time and outside costs of $1,159,073 per company for each shareholder nominee.[791] One commenter asserted that we underestimated the burden associated with these three actions because our estimate did not account for the fact that a company or its corporate governance committee is likely to undertake a lengthy process before determining whether to support the candidate.[792] This commenter asserted that our estimate began only once a company has already determined to include the nominee, and did not account for the amount of time necessary for a company to fully and completely evaluate shareholder nominees. This would include, for example, determinations about the nominee's eligibility, investigation and verification of information provided by the nominee, research into the nominee's background, analysis of the relative merits of the shareholder nominee as compared to management's own nominees, multiple meetings of the relevant board committees, and analysis of whether a nomination would conflict with any federal law, state law or director qualification standards.

The commenter asserted that our burden estimate of 65 hours for a company that determines not to include a nominee in its proxy materials does not account for "significant" costs and the "enormous" amount of time that management and the board will likely spend on the proxy contest itself.[793] The commenter also indicated that our estimates did not account for the burdens on registered investment companies as a result of their unique circumstances. The commenter noted that subjecting registered investment companies to Rule 14a-11 will result in

---

791 See letters from BRT; Society of Corporate Secretaries.

792 See letter from S&C.

793 Id.

significant administrative burdens on open-end funds and fund complexes, and increased costs. This commenter, however, did not provide alternative cost estimates. Another commenter questioned our assumption that the cost of submitting a no-action request pursuant to Rule 14a-11 is comparable to that of a no-action request submitted pursuant to Rule 14a-8.[794] This commenter argued that due to the fundamental issues at stake, boards will likely expend significantly more resources to challenge shareholder nominees and elect their own nominees than they will to oppose a shareholder proposal submitted pursuant to Rule 14a-8.

One commenter submitted the results of a survey it conducted in which the participants predicted that, on average, 15% of companies listed on U.S. exchanges could expect to face a shareholder director nomination under Rule 14a-11 in 2011.[795] As explained in greater detail below, we believe the actual number of shareholders or groups of shareholders that will seek to use Rule 14a-11 may be much smaller. While we note that there are inherent uncertainties involved in providing this estimate, we estimate for purposes of the PRA requirements, based on available data on the number of contested elections, that 45 companies other than registered investment companies and six registered investment companies with shareholders eligible to submit nominees pursuant to Rule 14a-11 will receive such a nomination each year.

D. Revisions to PRA Reporting and Cost Burden Estimates

As discussed above, the rules we are adopting include several substantive modifications to the Proposal; however, the Schedule 14N disclosure requirements we are adopting are substantially similar to the proposed disclosure requirements. In addition to the disclosure we proposed to be included in Schedule 14N, the schedule also will require disclosure of whether

---

794 See letter from BRT.

795 See letter from Altman. The survey had 47 participants that were primarily issuers. The median forecast of this survey was 10%. The survey was based on the eligibility criteria contained in the Proposing Release.

the shareholder nominee satisfies the company's director qualifications.[796] As discussed more fully below, we are revising our estimates in response to commenters' suggestions and the modifications to the Proposal that we are adopting in the final rules. The burden estimates discussed below relate to the hours and costs associated with preparing, filing and sending the above schedules and forms, and constitute estimates of reporting and cost burdens imposed by each collection of information.

For purposes of the PRA, we estimate the total annual incremental paperwork burden resulting from new Rule 14a-11 and the related rule changes for reporting companies (other than registered investment companies) and registered investment companies to be approximately 4,113 hours of internal company or management time and a cost of approximately $548,200 for the services of outside professionals.[797] For purposes of the PRA, we estimate the total annual incremental paperwork burden to nominating shareholders and groups from Schedule 14N to be approximately 7,870 hours of shareholder personnel time, and $1,049,300 for services of outside professionals. As discussed further below, these total costs include all additional disclosure burdens associated with the final rules, including burdens related to the notice and disclosure requirements. The total costs described above also include the burden hours resulting from the new exemptions for solicitations by nominating shareholders or groups in connection with a nomination pursuant to Rule 14a-11.[798] As noted above, smaller reporting companies will not be subject to Rule 14a-11 until three years after the effective date of the rule. For purposes of the

---

796 See Item 5(e) of Schedule 14N.

797 For convenience, the estimated PRA hour burdens have been rounded to the nearest whole number. We estimate an hourly cost of $400 for the service of outside professionals based on our consultations with several registrants and law firms and other persons who regularly assist registrants in preparing and filing proxy statements and related disclosures with the Commission.

798 See new Rules 14a-2(b)(7) and 14a-2(b)(8).

PRA, we have calculated the burden estimates as if the rule has been fully phased in for all companies.

As amended, Rule 14a-8(i)(8) will no longer permit companies to exclude, under that basis, shareholder proposals that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. For purposes of the PRA, we estimate the total annual incremental paperwork burden resulting from the amendment to Rule 14a-8(i)(8) and the related rule changes for reporting companies (other than registered investment companies), registered investment companies, and shareholders to be approximately 17,994 hours of internal company or shareholder time and a cost of approximately $2,399,200 for the services of outside professionals.[799]

1. Rule 14a-11

New Rule 14a-11 will require any company subject to the rule to include disclosure about a nominating shareholder's or group's nominee or nominees for election as director in the company's proxy statement, and the name of the nominee or nominees on the company's proxy card, when the conditions of the rule are met. The rule will not apply if the company is subject to the proxy rules solely as a result of having a class of debt registered under Section 12 of the Exchange Act or if state law, foreign law or a company's governing documents prohibit shareholders from nominating a candidate or candidates for election as director. A nominating shareholder or group will be required to file Schedule 14N to disclose information about the nominating shareholder or group and the nominee or nominees, and the company will be

[799] This corresponds to 6,510 hours of shareholder time and $868,000 for the shareholders' use of outside professionals and 11,484 hours of company time and $1,531,200 for the company's use of outside professionals.

required to include certain information regarding the nominating shareholder or group and nominee or nominees in the company's proxy statement unless the company determines that it is not required to include the nominee or nominees in its proxy materials.[800] A nominating shareholder or group also will be afforded the opportunity to include in the company's proxy statement a statement of support for its nominee or nominees not to exceed 500 words per nominee. The nominee or nominees also will be included on the company's form of proxy in accordance with Exchange Act Rule 14a-4.

Under the final rule, shareholders or groups owning at least 3% of the voting power of a company's securities entitled to be voted on the election of directors for at least three years as of the date of filing their notice on Schedule 14N with the Commission, and transmitting the notice to the company, will be eligible to submit a nominee for election as director to be included in the company's proxy materials,[801] provided certain other eligibility requirements are met[802] and subject to certain limitations on the overall number of shareholder nominees for director.

In the Proposing Release, we estimated that 208 companies with eligible shareholders would receive nominations pursuant to Rule 14a-11. That number was based in part on data, which we used to estimate that approximately 4,163 reporting companies (other than registered investment companies) would have at least one shareholder who met the eligibility criteria set forth in the Proposing Release. We then estimated that 5% of those companies would receive a

---

800 The burdens associated with Schedule 14N are discussed below.

801 See Section II.B.4.b. above for a discussion of how voting power is determined.

802 The eligibility requirements are provided in Rule 14a-11(b). As discussed in more detail in Section II.B.4., a nominating shareholder or group must not be holding the securities used to meet the ownership threshold with the purpose, or with the effect, of changing the control of the company or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11. A nominating shareholder or group also must provide certain statements and disclosure regarding its ownership and the nominee or nominees must meet the applicable eligibility requirements.

nomination from an eligible shareholder or group of shareholders, resulting in 208 companies receiving nominations pursuant to Rule 14a-11 annually.[803] In the Proposing Release, we also estimated that 61, or 5%, of 1,225 registered investment companies responding to Rule 20a-1 each year would receive shareholder nominations for inclusion in their proxy materials. After further consideration, we believe that a better indicator of how many shareholders might submit a nomination is the number of contested elections and board-related shareholder proposals that have been submitted to companies.[804] We believe starting with this number is better because it indicates shareholders or groups of shareholders who have shown an interest in using currently available means under our rules to influence governance matters. The number of contested elections and board-related shareholder proposals, however, does not reflect the additional eligibility requirements that are being adopted in new Rule 14a-11. For example, Rule 14a-11 requires that a shareholder or group of shareholders satisfy an ownership threshold of at least 3% of the company's voting power; that amount of securities must have been held continuously for at least three years as of the date the nominating shareholder or group submits notice of its intent to use Rule 14a-11; and the nominating shareholder or group must execute a certification that it is not holding the securities with the purpose, or with the effect, of changing control of the

[803] If we used the same data for estimating the number of nominees that would be submitted pursuant to the final rules as adopted, there would be approximately 2,117 companies with at least one shareholder eligible to submit a nomination. If we were to assume that 5% of those companies with at least one shareholder eligible to submit a nomination would receive a nomination, then we would estimate that 106 companies would receive a nomination each year.

[804] In this regard, we note that it is estimated that there were 57 contested solicitations in 2009. See Georgeson, 2009 Annual Corporate Governance Review Executive Summary (available at http://www.georgeson.com/usa/acgr09.php) and footnote 828 below. In addition, approximately 118 Rule 14a-8 shareholder proposals related to board issues were submitted to shareholders for a vote in the 2008-2009 proxy season. Board related proposals include proposals to have an independent chairman of the board, proposals to allow for cumulative voting and proposals to require a majority vote to elect directors. See RiskMetrics 2009 Proxy Season Scorecard, May 15, 2009. We believe these actions related to contested solicitations or board issues, 175 in total, provide useful information about the degree of interest in using Rule 14a-11.

company or to gain a number of board seats that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11. As a result of the additional eligibility requirements and certifications required by Rule 14a-11, we believe it is reasonable to significantly reduce the number of contested elections and board-related shareholder proposals for purposes of estimating the number of shareholders or groups of shareholders who may submit a nomination pursuant to Rule 14a-11. For purposes of this analysis, we estimate that 45 companies other than registered investment companies will receive nominees from shareholders[805] for inclusion in their proxy materials.[806] We further estimate that six registered investment companies will receive nominees from shareholders pursuant to Rule 14a-11 annually.[807]

We estimate for PRA purposes that each company that receives nominees pursuant to

---

805 We further estimate that 75% of the 45 submissions, or 34, will be made by groups of shareholders, and the remaining 11 will be made by individuals. See the discussion below regarding the estimated increase in Schedule 13G filings.

806 For the reasons noted above, we discounted the 175 contested elections and board-related shareholder proposals by approximately 75% to reflect the much more stringent eligibility requirements under new Rule 14a-11 as compared to Rule 14a-8. The 45 filings that we estimate for purposes of the PRA are equal to 2.1% of the 2,117 companies we estimate to have at least one eligible shareholder meeting the ownership requirements of the rule.

807 In this regard, we estimate that there were 11 contested elections in 2009, based on the number of EDGAR filings on form-type PREC14A with respect to unique investment companies in 2009. In addition, the average number of no-action letters issued by the staff regarding proposals seeking to amend a registered investment company's bylaws to provide for shareholder director nominations received in calendar years 2007, 2008 and 2009, rounded to the nearest whole number greater than zero, is one. We estimate that investment companies currently receive as many proposals regarding nomination procedures or disclosures as there are contested elections and no-action letters issued by the staff, resulting in a total of 24 contested elections and board-related shareholder proposals per year. For reasons similar to those articulated above for non-investment companies, we believe these actions related to contested solicitation or board issues, 24 in total, provide useful information about the degree of interest in using Rule 14a-11. However, as discussed above, Rule 14a-11 contains different eligibility requirements than our current rules that will likely result in fewer companies receiving nominations submitted pursuant to the rule. Similar to non-investment companies, we believe it is reasonable to discount the 24 contested elections and board-related shareholder proposals by approximately 75%, resulting in six investment companies receiving nominations pursuant to Rule 14a-11. We further estimate that 75% of the submissions, or five, will be made by groups of shareholders and the remaining one will be made by an individual. See the discussion below regarding the estimated increase in Schedule 13G filings.

Rule 14a-11 will receive two nominees from one shareholder or group. The median board size based on a 2007 sample of public companies was nine.[808] Approximately 60% of the boards sampled had between nine and 19 directors. In the case of registered investment companies, we estimate that the median board size is eight.[809] Thus, although some shareholders or groups could seek to include fewer than two nominees and others would be permitted to include more than two nominees, depending on the size of the board, we assume for purposes of the PRA that each shareholder or group would submit two nominees. As a result, for reporting companies, we estimate up to 211 total company burden hours per company (which is the sum of the bullets below doubled where appropriate to reflect two nominees) which corresponds to 158 hours (211 x 0.75) of company time, and a cost of approximately $21,100 (211 x 0.25 x $400) for the services of outside professionals. In each case, this estimate includes:

- if the company determines that it will include a shareholder nominee, the company's preparation of a written notice to the nominating shareholder or group (five burden hours per notice);
- the company's inclusion in its proxy statement and form of proxy of the name of, and other related disclosures concerning, a person or persons nominated by a shareholder or shareholder group (five burden hours per nominee);[810]
- the company's preparation of its own statement regarding the shareholder nominee or

808 According to information from RiskMetrics, based on a sample of 1,431 public companies the median board size in 2007 was 9, with boards ranging in size from 4 to 23 members. Approximately 40% of the boards in the sample had 8 or fewer directors, approximately 60% had between 9 and 19 directors, and less than 1% had 20 or more directors.

809 See Investment Company Institute and Independent Directors Council, Overview of Fund Governance Practices 1994-2006, at 6-7 (November 2007), available at http://www.ici.org/pdf/rpt_07_fund_gov_practices.pdf (noting that the median number of independent directors per fund complex in 2006 was six and that independent directors held 75% or more of board seats in 88% of fund complexes).

810 The requirement is in amended Rule 14a-4.

nominees (40 burden hours per nominee); and

- if a company determines that it may exclude a shareholder nominee submitted pursuant to the new rule, the company's preparation of a written notice to the nominating shareholder or group followed by written notice of the basis for its determination to exclude the nominee to the Commission staff (116 burden hours per notice).[811]

For purposes of this PRA analysis, we assume that approximately 41 (or 90% of 45) reporting companies (other than registered investment companies) and 5 (or 90% of 6) registered investment companies that receive a shareholder nominee for director will be required to include the nominee in their proxy materials. In the other 10% of cases, we assume that the company will be able to exclude the shareholder nominee (after providing notice of its reasons to the Commission). If a company determines to include a shareholder nominee, it must provide written notice to the nominating shareholder or group. We estimate the burden associated with preparing this notice to be five hours. For reporting companies (other than registered investment companies), this will result in 205 aggregate burden hours (41 companies x 5 hours/company), which corresponds to 154 burden hours of company time (41 companies x 5 hours/company x 0.75) and $20,500 in services of outside professionals (41 companies x 5 hours/company x 0.25 x $400). For registered investment companies, this will result in 25 aggregate burden hours (5 companies x 5 hours/company), which corresponds to 19 burden hours of company time (5 companies x 5 hours/company x 0.75), and $2,500 for services of outside professionals (5 companies x 5 hours/company x 0.25 x $400).

We estimate the annual disclosure burden for companies to include nominees and related

811 As discussed below, for companies that exclude a nominee but do not request no-action relief, we estimate this burden to be 100 hours.

disclosure in their proxy statements and on their form of proxy to be 5 burden hours per nominee, for a total of 410 aggregate burden hours (41 responses x 5 hours/response x 2 nominees) for reporting companies (other than registered investment companies), and 50 aggregate burden hours (5 responses x 5 hours/response x 2 nominees) for registered investment companies. For reporting companies (other than registered investment companies), this corresponds to 308 burden hours of company time, and $41,000 for services of outside professionals.[812] For registered investment companies, this corresponds to 38 hours of company time, and $5,000 for services of outside professionals.[813]

We estimate that 41 reporting companies (other than registered investment companies) and 5 registered investment companies will include a statement with regard to the shareholder nominees.[814] We anticipate that the burden to include a statement will include time spent to research the nominee's background, determinations about the nominee's eligibility, investigation and verification of information provided by the nominee, analysis of the relative merits of the shareholder nominee as compared to management's own nominees, multiple meetings of the relevant board committees, analysis of whether a nomination will conflict with any federal law, state law or director qualification standards, preparation of the statement, and company time for review of the statement by, among others, the nominating committee and legal counsel. In the Proposing Release we estimated that this burden will be approximately 20 hours per nominee. Based on comments received, however, we believe it is appropriate to increase this estimate to

812 The calculations for these numbers are: 410 burden hours x 0.75 = 308 burden hours of company time and 410 burden hours x 0.25 x $400 = $41,000 for services of outside professionals.

813 The calculations for these numbers are: 50 burden hours x 0.75 = 38 hours of company time and 50 burden hours x 0.25 x $400 = $5,000 for services of outside professionals.

814 We assume that each company that includes a shareholder nominee in its proxy materials would include such a statement.

40 hours per nominee.[815] For reporting companies (other than registered investment companies), this will result in 3,280 aggregate burden hours (41 statements x 40 hours/statement x 2 nominees). This corresponds to 2,460 hours of company time (41 statements x 40 hours/statement x 2 nominees x 0.75) and $328,000 for services of outside professionals (41 statements x 40 hours/statement x 2 nominees x 0.25 x $400) for reporting companies (other than registered investment companies). For registered investment companies, this will result in 400 aggregate burden hours (5 statements x 40 hours/statement x 2 nominees). This corresponds to 300 hours of company time (5 statements x 40 hours/statement x 2 nominees x 0.75) and $40,000 for services of outside professionals (5 statements x 40 hours/statement x 2 nominees x 0.25 x $400).

Further, for purposes of this analysis, we assume that approximately 9 (or 20% of 45) reporting companies (other than registered investment companies) and 1 (or 20% of 6) registered investment companies that receive a shareholder nominee for director for inclusion in their proxy materials will make a determination that they are not required to include a nominee in their proxy materials because the requirements of Rule 14a-11 are not met and will file a notice of intent to exclude that nominee.[816] We further estimate that 3 (or 33% of 9) of those reporting companies

---

815 In its comment letter and based on its survey of its members, BRT estimated that the preparation of a notice to the nominating shareholder, inclusion of related disclosure in the company's proxy materials, and preparation of its own statement regarding the shareholder nominee will require an average of 99 hours of personnel time. In the Proposing Release, we estimated the burden for these three actions to be 30 hours. We note that the survey conducted by the BRT provides useful information regarding the amount of personnel time that a company will spend responding to a Rule 14a-11 nomination, however, the survey represents a limited number of companies. While we are persuaded that the burden to companies of preparing a statement with regard to the shareholder nominee may require more than the 20 hours we estimated in the Proposing Release, we believe that 99 hours may represent the high end of the range. In light of this information, we believe it is appropriate to increase our estimate and we believe it is adequate to double our estimate of this component from 20 to 40 hours to reflect the average burden across all companies. Thus, we estimate that the internal burden associated with these three actions would be 50 hours.

816 With respect to companies other than registered investment companies, we assume that 6 of these submissions ultimately would be excludable under the rule.

(other than registered investment companies) will not seek no-action relief from the Commission and will only provide the required notice to the nominating shareholder or group and the Commission. We estimate that the remaining 6 reporting companies other than registered investment companies and the one registered investment company that makes a determination that it is not required to include a nominee in its proxy materials will seek no-action relief in order to exclude the nomination. We estimate that the burden hours associated with preparing and submitting the company's notice to the nominating shareholder or group and the Commission regarding its intent to exclude a shareholder nominee that includes a request for no-action relief would be 116 hours per notice.[817] We estimate that the burden hours associated with preparing and submitting the company's notice to the nominating shareholder or group and the Commission regarding its intent to exclude a shareholder nominee and its reasons for doing so would be 100 hours.[818] One commenter questioned our assumption that submitting a request to

---

817 This estimate is based on data provided by the BRT in its comment letter dated August 17, 2009. In its letter, the BRT provided data from a survey of its own members indicating that the average burden associated with preparing and submitting a single no-action request to the Commission staff in connection with a shareholder proposal is approximately 47 hours and associated costs of $47,784. Although the letter did not specify as much, assuming these costs correspond to legal fees, which we estimate at an hourly cost of $400, we estimate that this cost is equivalent to approximately 120 hours ($47,784/$400). We note that this estimate is higher than the 65 hours we estimated in the Proposing Release, where we relied on 2003 data provided by the American Society of Corporate Secretaries indicating 30 hours and associated costs of $13,896, or 35 hours ($13,896/$400). The BRT survey also indicated that if a company opposes a shareholder nominee, it would incur an additional average of 302 hours of company time. This would be in addition to its estimate of 99 hours for the actions described above. As noted above, the survey conducted by the BRT provides useful estimates for us to consider, but the survey represents a limited number of companies. In addition, it is unclear whether the 302 hours is inclusive of the no-action process. We believe this estimate is high and believe the revised number discussed below is a better estimate because it attempts to reflect the burden across all companies. For purposes of the PRA, we assume that submitting the notice and reasons for excluding a shareholder nominee to the staff will be comparable to preparing a no-action request to exclude a proposal under Rule 14a-8. While it appears, based on commenters' estimates, that associated costs may have increased since 2003, based on estimates provided by other commenters on the costs of preparing and submitting a no-action request (see, e.g., letter from S&C), we believe an average of the two estimates provides a more representative estimate of the spectrum of reporting companies, as opposed to those who participated in the BRT survey. Thus, we estimate that the burden to submit the notice and reasons for excluding a shareholder nominee and request no-action relief would be approximately 116 hours ([167 hrs + 65 hrs] / 2).

818 We believe that even if a company is not seeking no-action relief the company will still spend significant time preparing its notice to exclude the nominee. Because the notice will be required to include the reasons

the staff to exclude a shareholder nominee will be comparable to preparing a no-action request to exclude a proposal under Rule 14a-8.[819] This commenter argued that due to the fundamental issues at stake, boards are likely to expend significant resources to challenge shareholder nominees and elect their own nominees. We recognize the possibility that companies might expend greater resources in opposing a shareholder nominee than a shareholder proposal. We believe, however, that some of the resources to oppose a shareholder nominee will be allocated to the use of other means outside of the required disclosure in the proxy statement (e.g., "fight letters") so we have not factored that into our collection of information estimate. We believe that a portion of the burden associated with this will be reflected in the company's preparation of its own statement regarding the shareholder nominee, rather than in the preparation of a no-action request, and accordingly, as discussed above, we have increased our estimate of the associated burden from 20 to 40 hours. Although we have increased the burden to the company associated with preparing its own statement, we are not persuaded that also increasing the burden associated with preparing a request to exclude the nominee will be an accurate estimate. We are, however, as discussed above, increasing to 116 hours our estimate for preparing a notice of intent to exclude the nominee and request no-action relief based on 2009 data received from commenters.[820]

In the case of reporting companies (other than registered investment companies) that have determined they may exclude a nominee and seek no-action relief from the staff, we estimate that this will result in an aggregate burden of 696 hours (6 notices x 116 hours/notice), corresponding

---

that the nominee is being excluded, we believe that the burden will be similar to, though not quite as extensive as, preparing a request for no-action relief.

819 See letter from BRT.

820 Our prior estimate of 65 hours in the Proposing Release was based on 2003 data.

to 522 hours of company time (6 notices x 116 hours/notice x 0.75) and $69,600 for the services of outside professionals (6 notices x 116 hours/notice x 0.25 x $400). In the case of registered investment companies that have determined they may exclude a nominee and seeking no-action relief from the staff, we estimate that this will result in 116 aggregate burden hours (1 notice x 116 hours/notice), which will correspond to 87 hours of company time (1 notice x 116 hours/notice x 0.75) and $11,600 for the services of outside professionals (1 notice x 116 hours/notice x 0.25 x $400). For companies (other than registered investment companies) that have determined they may exclude a nomination but not to seek no-action relief from the staff, we estimate that this will result in an aggregate burden of 300 hours (3 notices x 100 hours/notice), corresponding to 225 hours of company time (3 notices x 100 hours/notice x 0.75) and $30,000 for the services of outside professionals (3 notices x 100 hours/notice x 0.25 x $400).[821] These burdens would be added to the PRA burdens of Schedules 14A and 14C or, in the case of registered investment companies, Rule 20a-1.

We also estimate that the annual burden for the nominating shareholder's or group's participation in the no-action process[822] available pursuant to Rule 14a-11 would average 60 hours per nomination.[823] For nominating shareholders or groups of reporting companies (other

821 As discussed above, we estimate that only one registered investment company will make a determination that it is not required to include a nominee in its proxy material and that this company will seek no-action relief.

822 There is no corresponding burden for shareholders or groups whose nomination is excluded by the company, and the company does not seek no-action relief. If the shareholder objects to the exclusion, there is no requirement that the shareholder seek redress from the staff or the Commission. As a result, we have not provided an estimated burden.

823 As noted in footnote 817, we estimate that the average burden to a company associated with preparing and submitting a no-action request to the staff is approximately 116 burden hours. We believe that the average burden for a shareholder proponent to respond to a company's no-action request is likely to be less than a company's burden to prepare the request; therefore, we estimate it will take approximately half the time (or 60 burden hours) for a nominating shareholder or group to respond to a company's notice to the Commission of its intent to exclude.

than registered investment companies), this will result in 360 total burden hours (6 responses x 60 hours/response). This will correspond to 270 hours of shareholder time (6 responses x 60 hours/response x 0.75) and $36,000 for services of outside professionals (6 responses x 60 hours/response x 0.25 x $400). For nominating shareholders or groups of registered investment companies, this will result in 60 total burden hours (1 response x 60 hours/response). This will correspond to 45 hours of shareholder time (1 response x 60 hours/response x 0.75) and $6,000 for services of outside professionals (1 response x 60 hours/response x 0.25 x $400). This burden would be added to the PRA burden of Schedule 14N.

We also are adopting two new exemptions from the proxy rules for solicitations by shareholders or groups in connection with a nomination pursuant to Rule 14a-11. The first exemption addresses written and oral solicitations by shareholders that are seeking to form a nominating shareholder group, provided that certain requirements are met.[824] Solicitations made in reliance on this exemption would be required to be filed under cover of Schedule 14N with the appropriate box marked on the cover page. As discussed above, we estimate that 34 of the submissions made to companies (other than registered investment companies) pursuant to Rule 14a-11 will be by groups of shareholders formed for purposes of satisfying the eligibility requirements of the rule. We estimate that 31 (90% of 34) of these groups will avail themselves of Rule 14a-2(b)(7). In the case of reporting companies (other than registered investment companies), this will result in an aggregate burden of 31 hours (31 solicitations x 1 hour/solicitation), which corresponds to 23 hours of shareholder time (31 solicitations x 1 hour/solicitation x 0.75) and $3,100 for the services of outside professionals (31 solicitations x 1 hour/solicitation x 0.25 x $400). In the case of registered investment companies, we estimate

824 See new Rule 14a-2(b)(7).

that five of the submissions made pursuant to Rule 14a-11 will be by groups of shareholders formed for purposes of satisfying the eligibility requirements of the rule. We estimate that all of these groups will avail themselves of Rule 14a-2(b)(7) (90% of 5 rounds up to 5). This will result in an aggregate burden of 5 hours (5 solicitations x 1 hour/solicitation), which corresponds to 4 hours of shareholder time (5 solicitations x 1 hour/solicitation x 0.75) and \$500 for the services of outside professionals (5 solicitations x 1 hour/solicitation x 0.25 x \$400). These burden hours would be added to the PRA burden of Schedule 14N.

The second new exemption will apply to written and oral solicitations by or on behalf of a nominating shareholder or group that has met the requirements of Rule 14a-11 in favor of shareholder nominees or for or against company nominees.[825] Although nominating shareholders or groups will not be required to engage in written solicitations, if the nominating shareholder or group does so, the exemption will require inclusion in any written soliciting materials filed under cover of Schedule 14N of a legend advising shareholders to look at the company's proxy statement when available and advising shareholders how to find the company's proxy statement. For purposes of this analysis, we assume that 50% of nominating shareholders or groups ultimately included in a company's proxy statement will solicit in favor of their nominee or nominees outside the company's proxy statement. In the case of reporting companies (other than registered investment companies), this will result in an aggregate burden of 20 hours (20 solicitations x 1 hour/solicitation), which corresponds to 15 hours of shareholder time (20 solicitations x 1 hour/solicitation x 0.75) and \$2,000 for services of outside professionals (20 solicitations x 1 hour/solicitation x 0.25 x \$400). These burden hours would be added to the PRA burden of Schedule 14N. In the case of registered investment companies, this will result in

[825] See new Rule 14a-2(b)(8).

an aggregate burden of 3 hours (3 solicitations x 1 hour/solicitation), which corresponds to 2 hours of shareholder time (3 solicitations x 1 hour/solicitation x 0.75) and $300 for services of outside professionals (3 solicitations x 1 hour/solicitation x 0.25 x $400). These burden hours would be added to the PRA burden of Schedule 14N.

2. Amendment to Rule 14a-8(i)(8)

Under our amendment to Rule 14a-8(i)(8), the election exclusion, a company will no longer be able to rely on this basis to exclude a shareholder proposal that seeks to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. The shareholder proposal will have to meet the procedural requirements of Rule 14a-8 and not be subject to one of the substantive exclusions other than the election exclusion (e.g., the proposal could be excluded if the shareholder proponent did not meet the ownership threshold under Rule 14a-8).

Historically, shareholders have made relatively few proposals relating to shareholder access to a company's proxy materials. The staff received 368 no-action requests from companies seeking to exclude shareholder proposals during the 2006-2007 fiscal year. Of these requests, only three (or approximately one percent) related to proposals for bylaw amendments providing for shareholder nominees to appear in the company's proxy materials. During the 2007-2008 fiscal year, the staff received 423 no-action requests to exclude shareholder proposals pursuant to Rule 14a-8. Of these no-action requests, six (or approximately two percent) related to proposals for bylaw amendments providing for shareholder nominees to appear in the company's proxy materials. During the 2008-2009 fiscal year, the staff received 365 no-action requests to exclude shareholder proposals pursuant to Rule 14a-8. Of these requests, seven related to shareholders' ability to have their nominee included in a company's proxy materials.

One such request sought to exclude a proposal to directly amend a company's governing documents to permit shareholder director nominations; the remaining six no-action requests related to proposals requesting that the company reincorporate in North Dakota where the relevant state corporate law gives qualified shareholders the right to submit director nominees for inclusion in the company's proxy materials.[826] Although these reincorporation proposals did not seek to amend the companies' bylaws, by seeking reincorporation into North Dakota it appears they sought the ability for shareholders to have nominees included in a company's proxy materials. As of July 23, 2010, during the 2009-2010 fiscal year, the staff has received 353 no-action requests to exclude shareholder proposals pursuant to Rule 14a-8, none of which related to shareholders' ability to have their nominee included in a company's proxy materials. While we believe that these proposals are helpful in gauging the level of shareholder interest in nominating directors, because our amendment to Rule 14a-8(i)(8) narrows the scope of the exclusion and no longer permits companies to exclude certain proposals that are excludable under current Rule 14a-8(i)(8), and Rule 14a-11 as adopted includes meaningful eligibility standards, we believe there may be an increase in the number of shareholder proposals seeking to establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees in a company's proxy materials to allow, for example, lower ownership thresholds or higher numbers of shareholder director nominees.

While the number of no-action requests the staff has received in the past is a useful starting point for the PRA analysis, other data also is helpful to gauge shareholder interest in nominating directors and to predict the anticipated impact on the number of proposals submitted pursuant to Rule 14a-8 that seek to establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees in a company's proxy

826 See North Dakota Publicly Traded Corporations Act, N.D. Cent. Code § 10-35-08 (2009).

materials that otherwise would be excludable under current Rule 14a-8(i)(8). For example, based on publicly available information, from 2001 to 2005, there were, on average, 14 contested elections per year.[827] It is estimated that in 2009 there were at least 57 contested elections,[828] and in 2008 it is estimated that there were at least 50 contested elections.[829] For purposes of the PRA, we believe that as a result of the amendment to Rule 14a-8(i)(8), shareholders may submit at least as many shareholder proposals to establish procedures under a company's governing documents for the inclusion of shareholder nominees for director in company proxy materials as there are contested elections. We believe that if shareholders are willing under the current proxy rules to put forth the expense and effort to wage a contest to put forth their own nominees in 57 instances, there may be a similar number of proposals submitted to companies pursuant to Rule 14a-8, as amended, because companies will no longer be permitted to exclude some proposals that currently are excludable under Rule 14a-8(i)(8). We also believe that some shareholders that have submitted proposals in the past with regard to other board issues will submit proposals seeking to establish procedures under a company's governing documents for the inclusion of shareholder nominees for director in company proxy materials. As noted in the Proposing Release, according to information from RiskMetrics, approximately 118 Rule 14a-8 shareholder proposals regarding board issues were submitted to shareholders for a vote in the 2008-2009

---

827 See Lucian A. Bebchuk, The Myth of the Shareholder Franchise, 93 VA. L. REV. 675, 683 (2007) ("Bebchuk (2007)")(citing data from proxy solicitation firm Georgeson Shareholder). See footnote 314 in the Proposing Release.

828 See Georgeson, 2009 Annual Corporate Governance Review (stating that as of the end of September 2009 it had tracked 57 formal proxy contests); see also RiskMetrics Group, 2009 Postseason Report Summary, A New Voice in Governance: Global Policymakers Shape the Road to Reform, October 2009, available at http://www.riskmetrics.com/docs/2009-postseason-report (noting that during the 2009 proxy season there were at least 39 proxy contests, and 36 negotiated settlements prior to a shareholder vote).

829 See letter from BRT (citing data from Georgeson, "2008 Annual Corporate Governance Review"). See also RiskMetrics Group, 2008 Postseason Report Summary, Weathering the Storm: Investors Respond to the Global Credit Crisis, October 2008, available at http://www.riskmetrics.com/docs/2008postseason_review_summary.

proxy season.[830] For purposes of the PRA, we estimate that approximately half of these shareholders may submit a proposal regarding procedures for the inclusion of shareholder nominees for director in company proxy materials, resulting in up to 59 proposals in lieu of proposals related to other board issues.[831]

In the case of reporting companies (other than registered investment companies), we believe that the amendment to Rule 14a-8(i)(8) may result in an increase of up to 64 (57 + 7 2009 shareholder proposals) proposals annually from 2009, and a total of 123 proposals (59 proposals + 57 + 7) to companies per year regarding procedures for the inclusion of shareholder nominees for director in company proxy materials.[832] We estimate the annual incremental burden for the shareholder to prepare the proposal to be 10 burden hours per proposal, for a total of 640 burden hours (64 proposals x 10 hours/proposal). This will correspond to 480 hours of shareholder time (64 proposals x 10 hours/proposal x 0.75) and \$64,000 for the services of outside professionals (64 proposals x 10 hours/proposal x 0.25 x \$400).[833]

We recognize that a company that receives a shareholder proposal has no obligation to submit a no-action request to the staff under Rule 14a-8. We anticipate that because the

---

830 See footnote 804 above.

831 We note that we used this estimate in the Proposing Release and did not receive comment on it. See Section IV.C.2. of the Proposing Release. We acknowledge the possibility that the number of Rule 14a-8 proposals relating to director nomination procedures may decrease with shareholders' ability to submit a nominee for inclusion in company proxy materials pursuant to Rule 14a-11, but we believe that any decrease may be countered by an increase in shareholder proposals to establish company-specific requirements that are different than Rule 14a-11.

832 The increase is calculated by adding the number of proxy contests in 2009 (57) plus the number of no-action requests received in 2009 regarding proposals seeking to amend a company's bylaws to provide for shareholder director nominations (seven). We have not included an estimated 59 proposals in this increase because we believe they will be submitted in lieu of other types of proposals (a shareholder is limited to submitting one shareholder proposal to each company).

833 We note that this calculation is for incremental, not total, costs. One commenter estimated that the average approximate total cost for shareholders to include a Rule 14a-8 proposal was \$30,000. See letter from CalPERS. Assuming these costs correspond to legal fees, which we estimate at an hourly cost of \$400, we estimate that this cost will be equivalent to approximately 75 hours.

proposals that would be submitted pursuant to amended Rule 14a-8 could affect the composition of the company's board of directors, nearly all companies receiving such proposals would submit a written statement of its reasons for excluding the proposal to the staff. We estimate that there will be a total of 123 proposals per year regarding procedures for the inclusion of shareholder nominees in the company's proxy statement. This number includes the 64 (57 + 7) new proposals plus the 59 proposals submitted in lieu of other proposals. Thus, we estimate that 90% of the estimated 123 companies receiving proposals seeking to establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees in a company's proxy materials will submit a written statement of their reasons for excluding the proposal to the staff and would seek no-action relief.

We estimate that companies would determine that they could exclude, and would seek staff concurrence through the no-action letter process for, 110 proposals (123 proposals x 90%) per proxy season. We estimate that the annual burden for the company's submission of a notice of its intent to exclude the proposal and its reasons for doing so would average 116 hours per proposal, for a total of 12,760 burden hours (110 proposals x 116 hours/proposal) for reporting companies (other than registered investment companies). This will correspond to 9,570 hours of company time (110 proposals x 116 hours/proposal x 0.75) and $1,276,000 for the services of outside professionals (110 proposals x 116 hours/proposal x 0.25 x $400).

We also estimate that the annual burden for the proponent's participation in the Rule 14a-8 no-action process would average 60 hours per proposal, for a total of 6,600 burden hours (110 proposals x 60 hours/proposal).[834] This will correspond to 4,950 hours of shareholder time (110

[834] As noted in footnote 817 above, we estimate that the average burden to a company associated with preparing and submitting a no-action request to the staff was approximately 116 burden hours. As noted above in footnote 823, we estimate 60 burden hours for a shareholder proponent to respond to a company's notice of intent to exclude and request for no-action relief to the Commission. In this regard, we also

proposals x 60 hours/proposal x 0.75) and $660,000 for services of outside professionals (110 proposals x 60 hours/proposal x 0.25 x $400). These burdens would be added to the PRA burden of Schedules 14A and 14C.

In the case of registered investment companies, we anticipate that the amendment to Rule 14a-8(i)(8) will result in an increase of 12 proposals annually, and a total of 24 proposals regarding procedures for the inclusion of shareholder nominees for director in company proxy materials to companies per year.[835] We estimate the annual incremental burden for the shareholder proponent to prepare the proposal to be 10 hours per proposal, for a total of 120 burden hours (12 proposals x 10 hours/proposal). This would correspond to 90 hours of shareholder time (12 proposals x 10 hours/proposal x 0.75) and $12,000 for the services of outside professionals (12 proposals x 10 hours/proposal x 0.25 x $400).

Similar to reporting companies other than investment companies, we assume that 90% of registered investment companies that receive a shareholder proposal seeking to establish procedures under a company's governing documents for the inclusion of one or more shareholder nominees in a company's proxy materials will determine that they may exclude the proposal from their proxy materials and request concurrence through the no-action letter process

---

estimate that the average incremental burden for a shareholder proponent to submit a shareholder proposal would be 10 hours. We note that one commenter estimated that the average approximate cost to shareholders of submitting a proposal is $30,000. See letter from CalPERS. We note that this commenter's estimate corresponds to the burden to shareholders of submitting a proposal, whereas our estimate of 60 burden hours corresponds to the burden to shareholders in responding to a company's no-action request.

835 The increase is estimated based on the number of registered investment company proxy contests in calendar year 2009 (11) plus the average number of no-action letters issued by the staff regarding proposals seeking to amend a registered investment company's bylaws to provide for shareholder director nominations received in calendar years 2007, 2008, and 2009 rounded to the nearest whole number greater than zero (1). In addition, we estimate that investment companies currently receive as many proposals regarding nomination procedures or disclosures as there are contested elections and no-action letters issued by the staff, resulting in a total of an estimated 24 proposals regarding nomination procedures or disclosures related to director nominations to companies per year.

(so registered investment companies will seek to exclude 22 such proposals per proxy season). Also similar to reporting companies other than registered investment companies, we assume that the annual burden for the company's submission of a notice of its intent to exclude the proposal and its reasons for doing so would average 116 hours per proposal, for a total of 2,552 burden hours for registered investment companies (22 proposals x 116 hours/proposal). This corresponds to 1,914 hours of company time (22 proposals x 116 hours/proposal x 0.75) and $255,200 for the services of outside professionals (22 proposals x 116 hours/proposal x 0.25 x $400). We also estimate that the annual burden for the proponent's participation in the Rule 14a-8 no-action process would average 60 hours per proposal, for a total of 1,320 burden hours (22 proposals x 60 hours/proposal). This corresponds to 990 hours of shareholder time (22 proposals x 60 hours/proposal x 0.75) and $132,000 for the services of outside professionals (22 proposals x 60 hours/proposal x 0.25 x $400). These burdens would be added to the PRA burden of Rule 20a-1.

3. Schedule 14N and Exchange Act Rule 14a-18

Rule 14n-1 establishes a new filing requirement for the nominating shareholder or group, under which the nominating shareholder or group will be required to file notice of its intent to include a shareholder nominee or nominees for director pursuant to Rule 14a-11, applicable state law provisions, or a company's governing documents, as well as disclosure about the nominating shareholder or group and nominee or nominees on new Schedule 14N. New Schedule 14N was modeled after Schedule 13G, but with more extensive disclosure requirements than Schedule 13G. Schedule 14N will require, among other items, disclosure about the amount and percentage of securities owned by the nominating shareholder or group, the length of ownership of such amount, and a written statement that the nominating shareholder or group will continue to hold the securities through the date of the meeting.

In addition, Schedule 14N will contain the disclosure required to be included in the nominating shareholder's or group's notice to the company of its intent to require that the company include the shareholder's or group's nominee in the company's proxy materials pursuant to Rule 14a-11 or pursuant to applicable state or foreign law provisions or a company's governing documents. With regard to the latter, we are seeking to assure that nominating shareholders or groups that submit a shareholder nomination for inclusion in a company's proxy materials pursuant to applicable state or foreign law provisions or the company's governing documents also provide disclosure similar to the disclosure required in a contested election to give shareholders the information needed to make an informed voting decision.

Schedule 14N will require disclosures regarding the nature and extent of the relationships between the nominating shareholder or group, the nominee and the company or any affiliate of the company. Pursuant to Items 7(e)-(f) of Schedule 14A and, in the case of an investment company, Items 22(b)(18)-(19) of Schedule 14A, the company will be required to include certain information set forth in the shareholder's notice on Schedule 14N in its proxy materials. A nominating shareholder or group filing a Schedule 14N to provide disclosure when submitting a nominee for inclusion in a company's proxy materials pursuant to applicable state or foreign law provisions or the company's governing documents will not be required to provide certain statements and certifications required for nominating shareholders or groups using Rule 14a-11.

We estimate that compliance with the Schedule 14N requirements will result in a burden greater than Schedule 13G[836] but less than a Schedule 14A.[837] Therefore, we estimate that

[836] We currently estimate the burden per response for preparing a Schedule 13G filing to be 12.4 hours.

[837] We currently estimate the burden per response for preparing a Schedule 14A filing to be 101.5 hours and a Schedule 14C to be 102.62 hours.

compliance with Schedule 14N will result in 47 hours per response per nominee submitted pursuant to Rule 14a-11.[838] We also note that the burden associated with filing a Schedule 14N in connection with a nomination made pursuant to an applicable state or foreign law provision or the company's governing documents may be slightly less than a nomination made pursuant to Rule 14a-11 because certain disclosures, statements, and certifications will not be required (including a statement that the nominating shareholder will continue to own the amount of securities through the date of the meeting, disclosure about the nominating shareholder's or group's intent with respect to continued ownership of the securities after the election, the certifications that will be required to use Rule 14a-11 (such as the certification concerning lack of intent to change control or to gain a number of seats on the board that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11, or the certifications that the nominating shareholder or group and the nominee satisfy the requirements of Rule 14a-11), and a supporting statement from the nominating shareholder or group. Therefore, we estimate that compliance with Schedule 14N when a shareholder or group submits a nominee or nominees to a company pursuant to an applicable state or foreign law provision or the company's governing documents will result in 40 hours per response per nominee.

For purposes of the PRA, we estimate the total annual incremental burden for nominating shareholders or groups to prepare the disclosure that will be required under this portion of the final rules to be approximately 7,870 hours of shareholder time, and $1,049,300 for the services

838 We estimate that the burden of preparing the information in Schedule 14N for a nominating shareholder or group would be 1/3 of the disclosures typically required by a Schedule 14A filing, which results in approximately 34 burden hours. For purposes of this analysis, we estimate that the 34 burden hours will be added to the 12.4 hours associated with filing a Schedule 13G, resulting in a total of approximately 47 burden hours. We estimate that 75% of the burden of preparation of Schedule 14N will be borne internally by the nominating shareholder or group, and that 25% will be carried by outside professionals. We believe the nominating shareholder or group will work with their nominee to prepare the disclosure and then have it reviewed by outside professionals.

of outside professionals.[839] This estimate includes the nominating shareholder's or group's preparation and filing of the notice and required disclosure and, as applicable, certifications on Schedule 14N and filings related to new Rules 14a-2(b)(7) and 14a-2(b)(8).

We do not expect that every shareholder that meets the eligibility threshold to submit a nominee for inclusion in a company's proxy materials pursuant to Rule 14a-11, an applicable state or foreign law provision, or a company's governing documents will do so. As discussed above, we estimate that 45 reporting companies (other than registered investment companies) and 6 registered investment companies will receive notices of intent to submit nominees pursuant to Rule 14a-11. We anticipate that some companies will receive nominees from more than one shareholder or group, though, as discussed above, for purposes of PRA estimates, we assume companies with an eligible shareholder would receive two nominees from only one shareholder or group.

We estimate that compliance with the requirements of Schedule 14N submitted pursuant to Rule 14a-11 will require 4,230 burden hours (45 notices x 47 hours/notice x 2 nominees/shareholder) in aggregate each year for nominating shareholders or groups of reporting companies (other than registered investment companies), which corresponds to 3,173 hours of shareholder time (45 notices x 47 hours/notice x 2 nominees/shareholder x 0.75) and costs of $423,000 (45 notices x 47 hours/notice x 2 nominees/shareholder x 0.25 x $400) for the services of outside professionals. In the case of registered investment companies, we estimate that a nominating shareholder's or group's compliance with the requirements of Schedule 14N will require 564 burden hours (6 responses x 47 hours/response x 2 nominees) in aggregate each year,

839 This figure represents the aggregate burden hours attributed to Schedule 14N and is the sum of the burden associated with Schedules 14N submitted pursuant to Rule 14a-11, applicable state or foreign law provisions, and a company's governing documents.

which corresponds to 423 hours of shareholder time (6 responses x 47 hours/response x 2 nominees x 0.75) and costs of $56,400 for the services of outside professionals (6 responses x 47 hours/response x 2 nominees x 0.25 x $400). Therefore, we estimate a total of 4,794 burden hours for all reporting companies, including investment companies, broken down into 3,596 hours of shareholder time and $479,400 for services of outside professionals.

We assume that all nominating shareholders or groups will prepare a statement of support for the nominee or nominees, and we estimate the disclosure burden for the nominating shareholder or group to prepare a statement of support for its nominee or nominees to be approximately 10 burden hours per nominee. In the case of companies other than registered investment companies, this results in an aggregate burden of 900 (45 statements x 10 hours/statement x 2 nominees/shareholder), which corresponds to 675 hours of shareholder time (45 statements x 10 hours/statement x 2 nominees/shareholder x 0.75) and $90,000 for services of outside professionals (45 statements x 10 hours/statement x 2 nominees/shareholder x 0.25 x $400) for shareholders of reporting companies (other than registered investment companies). For registered investment companies, this will result in an aggregate burden of 120 (6 statements x 10 hours/statement x 2 nominees/shareholder), which corresponds to 90 hours of shareholder time (6 statements x 10 hours/statement x 2 nominees/shareholder x 0.75) and $12,000 for services of outside professionals (6 statements x 10 hours/statement x 2 nominees/shareholder x 0.25 x $400). Therefore, we estimate a total of 1,020 burden hours for all reporting companies, including investment companies, broken down into 765 hours of shareholder time and $102,000 for services of outside professionals.

When a nominating shareholder or group submits a nominee or nominees to a company pursuant to an applicable state or foreign law provision or the company's governing documents, the nominating shareholder or group will be required to file a Schedule 14N to provide disclosure about the nominating shareholder or group and the nominee or nominees. As discussed, a company will be required to include certain disclosures about the nominating shareholder or group and the nominee or nominees in its proxy statement. As noted above, we estimate that the burden associated with filing a Schedule 14N in connection with a nomination made pursuant to an applicable state or foreign law provision or a company's governing documents is 40 hours per nominee. We also estimate that approximately 30 nominating shareholders or groups of reporting companies (other than registered investment companies) will submit a nomination pursuant to an applicable state or foreign law provision or a company's governing documents.[840] Thus, we estimate compliance with the requirements of Schedule 14N for nominating shareholders or groups submitting nominations pursuant to an applicable state or foreign law provision or the company's governing documents would result in 2,400 aggregate burden hours (30 notices x 40 hours/notice x 2 nominees/shareholder) each year for nominating shareholders or groups of reporting companies (other than registered investment companies), broken down into 1,800 hours of shareholder time (30 notices x 40 hours/notice x 2 nominees/shareholder x 0.75) and costs of $240,000 for the services of outside professionals (30 notices x 40 hours/notice x 2 nominees/shareholder x 0.25 x $400). In the case of registered investment companies, we estimate that approximately 12 nominating shareholders or groups

---

840 As discussed above, according to information from RiskMetrics, approximately 118 Rule 14a-8 shareholder proposals regarding board issues were submitted to shareholders for a vote in the 2008-2009 proxy season. See footnote 804. We believe this data is a useful starting point for estimating the number of shareholders who may avail themselves of our new rules, including the use of Schedule 14N. Also as discussed above, we estimate that approximately half of these shareholders may submit a proposal pursuant to Rule 14a-8 regarding procedures for the inclusion of shareholder nominees for director in company proxy materials, resulting in 59 proposals. We believe the number of shareholders submitting nominees pursuant to a state or foreign law provision will be lower than the number of shareholders submitting proposals pursuant to Rule 14a-8. As a result, we estimate that approximately 30 shareholder proponents will submit nominations pursuant to applicable state or foreign law provisions or a company's governing documents.

will submit a nomination pursuant to an applicable state or foreign law provision or a company's governing documents.[841] We estimate that a nominating shareholder's or group's compliance with the requirements of Schedule 14N would result in 960 aggregate burden hours (12 notices x 40 hours/notice x 2 nominees/shareholder) each year, which corresponds to 720 hours of shareholder time (12 notices x 40 hours/notice x 2 nominees/shareholder x 0.75) and costs of $96,000 for the services of outside professionals (12 notices x 40 hours/notice x 2 nominees/shareholder x 0.25 x $400). Therefore, we estimate that the total burden hours would be 3,360 for all reporting companies, including investment companies, broken down into 2,520 hours of shareholder time and $336,000 for services of outside professionals.

We assume that all nominating shareholders or groups that submit a nominee or nominees pursuant to an applicable state or foreign law provision or a company's governing documents will prepare a statement of support for the nominee or nominees,[842] and we estimate the disclosure burden for the nominating shareholder or group to prepare a statement of support for its nominee or nominees to be approximately 10 burden hours per nominee. This results in an aggregate burden of 600 hours (30 statements x 10 hours/statement x 2 nominees/shareholder) for shareholders of reporting companies (other than registered investment companies), which corresponds to 450 hours of shareholder time (30 statements x 10 hours/statement x 2 nominees/shareholder x 0.75) and $60,000 for services of outside professionals (30 statements x 10 hours/statement x 2 nominees/shareholder x 0.25 x $400). For registered investment

841 We estimate that approximately half of the 24 shareholders submitting proposals to registered investment companies regarding the inclusion of one or more shareholder nominees for director in company proxy materials will make submissions pursuant to applicable state or foreign law provisions or a company's governing documents. As a result, we estimate that approximately 12 shareholder proponents will submit to registered investment companies nominations pursuant to applicable state or foreign law provisions or a company's governing documents.

842 We are assuming for PRA purposes that any applicable state or foreign law provision or company's governing documents will allow for inclusion of such a statement by the nominating shareholder or group.

companies, this results in an aggregate burden of 240 hours (12 statements x 10 hours/statement x 2 nominees/shareholder), which corresponds to 180 hours of shareholder time (12 statements x 10 hours/statement x 2 nominees/shareholder x 0.75) and $24,000 for services of outside professionals (12 statements x 10 hours/statement x 2 nominees/shareholder x 0.25 x $400). This results in a total of 840 burden hours, broken down into 630 hours of shareholder time and $84,000 for the services of outside professionals.

4. Amendments to Exchange Act Form 8-K

Under Rule 14a-11, a nominating shareholder or group will be required to file with the Commission, and transmit to the company, a notice on Schedule 14N of its intent to require the company to include the nominating shareholder's or group's nominee in the company's proxy materials. The nominating shareholder or group must file and transmit the notice on Schedule 14N no earlier than 150, and no later than 120, calendar days before the anniversary of the date that the company mailed its proxy materials for the prior year's annual meeting. If the 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, then the nominating shareholder or group will be required to provide notice a reasonable time before the company mails its proxy materials, as specified by the company in a Form 8-K filed pursuant to new Item 5.08 of Form 8-K. The final rules also require a registered investment company that is a series company to file a Form 8-K disclosing the total number of the company's shares that are entitled to vote for the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.[843]

[843] The amendment to Rule 14a-8(i)(8) is not expected to impact Form 8-K, so the burden estimates solely reflect the burden changes resulting from new Item 5.08, including when a nomination is submitted pursuant to a company's governing documents or pursuant to applicable state law.

For purposes of the PRA, we estimate that approximately 4% of reporting companies (other than registered investment companies) will be required to file a Form 8-K because the company did not hold an annual meeting during the prior year, or the date of the meeting has changed by more than 30 days from the prior year.[844] Based on our estimate that there are approximately 11,000 reporting companies (other than registered investment companies), this corresponds to 440 companies that will be required to file a Form 8-K. In accordance with our current estimate of the burden of preparing a Form 8-K, we estimate 5 burden hours to prepare, review and file the Form 8-K, for a total burden of 2,200 hours (440 filings x 5 hours/filing). This total burden corresponds to 1,650 hours of company time (440 filings x 5 hours/filing x 0.75) and $220,000 for services of outside professionals (440 filings x 5 hours/filing x 0.25 x $400).

In the case of registered investment companies, we estimate that, similar to reporting companies other than registered investment companies, 4% of registered closed-end management investment companies subject to Rule 14a-11 that are traded on an exchange would be required to file a Form 8-K because the company did not hold an annual meeting during the prior year or the date of the meeting has changed by more than 30 days from the prior year.[845] We estimate that approximately 625 of the 1,225 registered investment companies responding to Investment Company Act Rule 20a-1 are closed-end funds that are traded on an exchange, resulting in 25 closed-end funds that will be required to file Form 8-K for these purposes (625 registered closed-

844 Based on information obtained in 2003 from the Investor Responsibility Research Center, 3.75% of companies (other than registered investment companies) did not hold an annual meeting during the prior year or the date of the meeting changed by more than 30 days from the prior year. See also footnote 195 in the 2003 Proposal.

845 We believe that the percentage for registered closed-end investment companies will be similar to other reporting companies because such investment companies are traded on an exchange and are required to hold annual meetings of shareholders.

end management investment companies x 0.04).[846] However, we estimate that few, if any, registered open-end management investment companies regularly hold annual meetings. Therefore, we estimate that 600 registered investment companies are not closed-end investment companies and will be required to file Form 8-K. This results in a total of 625 registered investment companies required to file Form 8-K (25 closed-end management investment companies + 600 other registered investment companies) and 3,125 burden hours (625 filings x 5 hours/filing). This total burden corresponds to 2,344 hours of company time (625 filings x 5 hours/filing x 0.75) and $312,500 for services of outside professionals (625 filings x 5 hours/filing x 0.25 x $400).[847] Adding the totals for reporting companies (other than registered investment companies) and registered investment companies results in a total burden of 5,325, which corresponds to 3,994 hours of company time and $532,500 for services of outside professionals. This includes the requirement for a registered investment company that is a series company to file a Form 8-K disclosing the total number of the company's shares that are entitled to vote for the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) as of the end of the most recent calendar quarter.

5. Schedule 13G Filings

Shareholders will be permitted to aggregate holdings for purposes of meeting the eligibility threshold in Rule 14a-11 and therefore we anticipate that some groups of shareholders

846 We estimate that 1,225 registered investment companies hold annual meetings each year based on the number of responses to Rule 20a-1. Based on data provided by Lipper, the Commission estimates that approximately 625 registered closed-end management investment companies are traded on an exchange.

847 Consistent with the current estimates for Form 8-K, we estimate that that 75% of the burden of preparation of Form 8-K is carried by the company and that 25% of the burden of preparation of Form 8-K is carried by outside professionals at an average cost of $400 per hour. The burden includes disclosure of the date by which a nominating shareholder or group must submit the notice required by Rule 14a-11(c) as well as disclosure of net assets, outstanding shares, and voting.

may beneficially own in the aggregate more than 5% of a voting class of an equity security registered pursuant to Section 12. In these circumstances, nominating shareholders will need to consider whether they have formed a group under Exchange Act Section 13(d)(3) and Rule 13d-5(b)(1) that is required to file beneficial ownership reports.[848] To the extent nominating shareholder groups exceed the 5% threshold and file a Schedule 13G, this will result in an increased number of Schedule 13G filings. With respect to reporting companies other than registered investment companies, we estimate that 25% (11) of the nominees submitted pursuant to Rule 14a-11 will be from shareholders who individually meet the eligibility thresholds (25% of 45), and 75% (34) will be from shareholder groups (75% of 45). We estimate that 75% of the 34 groups formed will exceed the 5% threshold and will file a Schedule 13G. As a result, we estimate that an additional 26 Schedule 13G filings will be made annually. The total burden associated with this increase in the number of filings is 322 burden hours (26 additional Schedule 13Gs x 12.4 hours/schedule). This burden corresponds to 81 hours of shareholder time (26 additional Schedule 13Gs x 12.4 hours/Schedule x 0.25) and $96,720 for services of outside professionals (26 additional Schedule 13Gs x 12.4 hours/Schedule x 0.75 x $400).

With respect to registered investment companies, we estimate that approximately 3 (50% of 6) of the shareholder nominees will be submitted by shareholders of closed-end funds whose shareholders are required to file beneficial ownership reports under the Exchange Act.[849] We

848 We recognize that each shareholder group will need to analyze its own facts and circumstances in order to determine whether it is required to file a Schedule 13G; however, we expect that most groups will file a Schedule 13G.

849 Under Section 13(d) of the Exchange Act, only holders of equity securities of closed-end funds are required to file beneficial ownership reports with the Commission. Holders of open-end funds are not subject to this requirement. Previously, we estimated that approximately 625 (or slightly over 50%) of the 1,225 registered investment companies responding to Investment Company Act Rule 20a-1 are closed-end funds that are traded on an exchange. We estimate that the percentage of the shareholder nominees that will be submitted by shareholders of closed-end funds will be approximately equal to the percentage of closed-end funds that are traded on an exchange.

estimate that 25% (1) of the nominees for director of closed-end funds submitted pursuant to Rule 14a-11 will be from shareholders who individually meet the eligibility thresholds (25% of 3), and 75% (2) will be from shareholder groups (75% of 3). We estimate that 75% of the two groups formed to nominate directors of closed-end funds will exceed the 5% threshold and file a Schedule 13G. As a result, we estimate that an additional 2 Schedule 13G filings will be made annually (75% of two groups rounds up to two). The total burden associated with this increase in the number of filings is approximately 25 burden hours (2 additional Schedule 13Gs x 12.4 hours/schedule). This burden corresponds to 6 hours of shareholder time (2 additional Schedule 13Gs x 12.4 hours/schedule x 0.25) and $7,440 for services of outside professionals (2 additional Schedule 13Gs x 12.4 hours/schedule x 0.75 x $400).

Adding the totals for reporting companies (other than registered investment companies) and registered investment companies results in a total burden of 347 hours, which corresponds to 87 hours of shareholder time and $104,160 for services of outside professionals.

6. Form ID Filings

Under Rule 14n-1 and Rule 14a-11, a shareholder who submits a nominee or nominees for inclusion in the company's proxy statement must provide notice on Schedule 14N to the company of its intent to require that the company include the nominee or nominees in the company's proxy materials. The notice on Schedule 14N must be filed with the Commission on the date the notice is transmitted to the company. We anticipate that some shareholders who submit a nominee or nominees for inclusion in a company's proxy materials will not previously have filed an electronic submission with the Commission and will file a Form ID. Form ID is the application form for access codes to permit filing on EDGAR. The final rules are not changing the form itself, but we anticipate that the number of Form ID filings may increase due to shareholders filing Schedule 14N when submitting a nominee or nominees to a company for inclusion in its proxy materials pursuant to Rule 14a-11, applicable state or foreign law provisions, or a company's governing documents. We estimate that 90% of the shareholders who submit a nominee or nominees for inclusion in a company's proxy materials will not have filed previously an electronic submission with the Commission and will be required to file a Form ID. As noted above, we estimate that approximately 45 reporting companies (other than registered investment companies) and 6 registered investment companies will receive shareholder nominations submitted pursuant to Rule 14a-11. This corresponds to 46 additional Form ID filings (90% of 51). In addition, as noted above, we estimate that approximately 30 reporting companies (other than registered investment companies) and 12 registered investment companies will receive shareholder nominations submitted pursuant to an applicable state or foreign law provision or a company's governing documents. This corresponds to an additional 38 Form ID filings (90% of 42). As a result, the additional annual burden would be 13 hours (84 filings x 0.15 hours/filing).[850] For purposes of the PRA, we estimate that the additional burden cost resulting from the new rules will be zero because we estimate that 100% of the burden will be borne internally by the nominating shareholder or group.

E. Revisions to PRA Reporting and Cost Burden Estimates

Table 1 below illustrates the incremental annual compliance burden of the collection of information in hours and in cost for securities ownership reports filed by investors, proxy and information statements, and current reports under the Exchange Act. The burden was calculated by multiplying the estimated number of responses by the estimated average number of hours each entity spends completing the form. We estimate that 75% of the burden of preparation of

850 We currently estimate the burden associated with Form ID is 0.15 hours per response.

the proxy and information statement and current reports is carried by the company internally, while 25% of the burden of preparation is carried by outside professionals at an average cost of $400 per hour. We estimate that 75% of the burden of preparation of Schedule 14N, any soliciting materials with regard to formation of a nominating shareholder group, and any soliciting materials regarding the nomination will be carried by the nominating shareholder or group internally and that 25% of the burden of preparation will be carried by outside professionals retained by the nominating shareholder or group. We estimate that 25% of the burden of preparation of Schedule 13G (for nominating shareholder groups that beneficially own more than 5% of a voting class of any equity security registered pursuant to Section 12) will be carried by the nominating shareholder or group internally and that 75% of the burden of preparation will be carried by outside professionals retained by the nominating shareholder or group. The portion of the burden carried by outside professionals is reflected as a cost, while the portion of the burden carried internally by the company and nominating shareholder or group is reflected in hours.

Table 1: Calculation of Incremental PRA Burden Estimates*

	Current Annual Responses (A)	Proposed Annual Responses (B)	Current Burden Hours (C)	Increase in Burden Hours (D)	Proposed Burden Hours (E) =C+D	Current Professional Costs (F)	Increase in Professional Costs (G)	Proposed Professional Costs =F+G
Sch 14A	7,300	7,300	671,970	16,370	688,340	$79,214,887	$2,182,590	$81,397,477
Sch 14C	680	680	631,152	1,819	632,971	$7,393,639	$242,510	$7,636,149
Sch 14N	0	162	0	7,870	7,870	$0	$1,049,300	$1,049,300
Form 8-K	115,795	116,860	493,436	3,994	497,430	$65,791,500	$532,500	$66,324,000
Form ID	65,700	65,784	9,855	13	9,868	$0	$0	$0
Sch 13G	12,500	12,528	35,577	87	35,664	$42,694,200	$104,160	$42,798,360
Rule 20a-1	1,225	1,225	142,958	3,438	146,396	$20,090,000	$458,300	$20,548,300
Total				33,591			$4,569,360	

* The incremental burden estimate for Rule 20a-1 includes the disclosure that would be required on Schedule 14A and

14C, discussed above, with respect to funds.

IV. COST-BENEFIT ANALYSIS

A. Background

The Commission is adopting new rules that, under certain circumstances, will require companies to include in their proxy materials shareholder nominees for director, as well as other disclosure regarding those nominees and the nominating shareholder or group. In addition, the new rules will require companies, under certain circumstances, to include in their proxy materials a shareholder proposal that seeks to establish a procedure in the company's governing documents for the inclusion of shareholder director nominees in the company's proxy materials. As a result, a company's proxy materials may be required, under certain circumstances, to provide shareholders with information about, and the ability to vote for, a shareholder nominee for director. The new rules will therefore facilitate shareholders' ability to exercise their traditional state law rights to nominate and elect directors by improving the disclosure provided in connection with corporate proxy solicitations and communication between shareholders in the proxy process.

We requested comment on all aspects of the cost-benefit analysis contained in the Proposing Release, including identification of any additional costs and benefits. We have considered these comments carefully and made responsive changes to the rules in order to minimize the potential costs. Below we consider the benefits and costs of the economic effects of the new rules and discuss the comments we received, as applicable.

B. Summary of Rules

Rule 14a-11 will require companies to include shareholder nominations for director and disclosure about the nominating shareholder or group and the nominee in a company's proxy materials if, among other things, the nominating shareholder or group held, as of the date of the shareholder notice on Schedule 14N, either individually or in the aggregate, at least 3% of the voting power of the company's securities that are entitled to be voted on the election of directors at the annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) or on a written consent in lieu of such meeting and has held the qualifying amount of securities used to satisfy the ownership threshold continuously for at least three years as of the date of the shareholder notice on Schedule 14N (in the case of a shareholder group, each member of the group must have held the amount of securities that are used to satisfy the ownership threshold for at least three years as of the date of the shareholder notice on Schedule 14N). The nominating shareholder or group also will be required to hold the shares through the date of the meeting. A nominating shareholder or group that includes a nominee or nominees in a company's proxy materials pursuant to Rule 14a-11 will be required to provide in its notice on Schedule 14N filed with the Commission and transmitted to the company disclosures similar to the disclosures required in a traditional contested election. Pursuant to Item 7(e) of Schedule 14A (and, in the case of registered investment companies and business development companies, Item 22(b)(18) of Schedule 14A), the company will be required to include in its proxy materials certain disclosure provided by the nominating shareholder or group in its notice on Schedule 14N. In addition, the new rules will enable shareholders to engage in limited solicitations to form nominating shareholder groups and engage in solicitations in support of their nominee or nominees without disseminating a proxy statement.[851]

The Commission also is adopting an amendment to Rule 14a-8 to narrow the exclusion in paragraph (i)(8) of the rule, which addresses director elections. Under the amendment, a

[851] See Rules 14a-2(b)(7) and 14a-2(b)(8).

company will not be permitted to rely on Rule 14a-8(i)(8) to omit from its proxy materials a shareholder proposal that seeks to establish a procedure in the company's governing documents for the inclusion of shareholder nominees for director in the company's proxy materials. The current procedural requirements for submitting a shareholder proposal pursuant to Rule 14a-8 will remain the same. No additional disclosures will be required from any shareholder that submits such a proposal; however, a nominating shareholder or group that includes a nominee or nominees in a company's proxy materials pursuant to an applicable state or foreign law provision or the company's governing documents will be required to file with the Commission and transmit to the company, in its notice on Schedule 14N, disclosures similar to the disclosures required in a traditional contested election. Pursuant to Item 7(f) of Schedule 14A (and, in the case of registered investment companies and business development companies, Item 22(b)(19) of Schedule 14A), the company will be required to include in its proxy materials certain disclosures provided by the nominating shareholder or group in its notice on Schedule 14N.

C. Factors Affecting Scope of the New Rules

Our discussion of the economic effects of the new rules takes into account various factors, such as the incentives and actions of certain parties, that will affect the rules' scope and influence.

Any future actions of the states and their legislatures could affect the applicability of the new rules. Rule 14a-11, for instance, will not apply to companies incorporated in states or other jurisdictions that prohibit nominations of directors by shareholders or permit companies to prohibit such nominations and where the company's governing documents do so.[852] Under Rule 14a-8, shareholder proposals must be proper subjects for action by shareholders under the laws

[852] As noted above, we are not aware of any states that currently prohibit shareholder nominations for director.

of the jurisdiction of the company's organization. To the extent that states or other jurisdictions change their laws, for example, to prohibit the nomination of directors by shareholders, Rule 14a-11 and Rule 14a-8 would apply less broadly.

Future actions of boards may affect the applicability of the new rules. In the case of Rule 14a-11, we believe that the applicability of the rule is not likely to be affected by future actions of a board because companies generally may not prohibit shareholders from nominating directors under existing state law.[853] In addition, a company will not be permitted to exclude pursuant to amended Rule 14a-8(i)(8) a shareholder proposal that would establish a procedure under a company's governing documents for the inclusion of one or more shareholder nominees for director in the company's proxy materials. It is reasonable to expect that some shareholders will submit this type of proposal, particularly shareholders who perceive that the current board does not represent, or possibly may come to not represent, their interests and are not otherwise able to use Rule 14a-11 (such as if the shareholder does not qualify to submit a nominee or if larger shareholders have exhausted the nomination slots available pursuant to Rule 14a-11). Finally, boards seeking to limit the effect of shareholder-nominated candidates submitted pursuant to Rule 14a-11 and elected as directors may, in some instances, choose to expand the board size to dilute, to an extent, the influence of those directors.[854]

The actions and intentions of shareholders also may affect the applicability of the new rules. To rely on Rule 14a-11, the nominating shareholder (or where there is a nominating

---

853 Several commenters also stated that they were unaware of any law in any state or in the District of Columbia that prohibits shareholders from nominating directors. See letters from ABA; BRT; CII; Eaton.

854 As an example, a board of eight directors, with two new shareholder-nominated directors, may expand to up to 11 directors. Such an expansion would dilute the influence of the shareholder-nominated directors without increasing the number of director slots for shareholder nominees for director in the proxy materials because Rule 14a-11 includes a provision allowing companies to round down the number of nominees that must be included when calculating the 25% maximum.

shareholder group, each member of the nominating shareholder group) must not be holding any of the company's securities with the purpose, or with the effect, of changing control of the company[855] or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11 and must provide a certification to this effect in its filed Schedule 14N.[856] The effect of the rule also is affected by the limitation on the number of shareholder director nominees that a company is required to include in its proxy materials. Under Rule 14a-11, a company will not be required to include shareholder nominations for more than a maximum of one director or 25% of the existing board, whichever is greater. If one shareholder or group that is eligible to use Rule 14a-11 nominates the maximum allowable number of candidates, a company will be permitted to exclude any other shareholder's or group's nominees from the company's proxy materials.[857] Further, if the maximum allowable number of existing shareholder director nominees is currently in place on the board, additional shareholder director nominees are not required to be disclosed in the proxy materials pursuant to the rule.[858]

855 Although Rule 14a-11 does not contain a requirement that the shareholder nominee or nominees do not have an intent to change the control of the company, a nominating shareholder's or group's ability to meet the requirement and certify that it does not have such an intent will be impacted by the intentions and actions of its nominee or nominees. For example, a nominating shareholder will not be able to certify that it does not hold the company's securities for the purpose, or with the effect, of changing the control of the company if its nominee launches its own proxy contest or tender offer. For further discussion, see Section II.B.4.d. above.

856 See certifications in Item 8 of new Schedule 14N.

857 Prior to the time a company has commenced printing its proxy statement and a form of proxy, if a nominating shareholder or group withdraws its shareholder director nominee or the nominee becomes disqualified, the company will be required to include in its proxy materials the director nominee or nominees of the nominating shareholder or group with the next highest voting power percentage that is otherwise eligible to use the rule and that filed a timely notice in accordance with the rule, if any. This process will continue until the company includes the maximum number of nominees that it is required to include in its proxy materials or the company exhausts the list of eligible nominees. For further discussion, see Section II.B.7.b above.

858 This could be the case when shareholder-nominated candidates for director are elected at a company with a classified board or when a company decides to nominate previously-elected shareholder-nominated

Shareholders seeking to establish a procedure in a company's governing documents and submit nominees for director using such a provision will need to initiate a two-step process to have their nominees included in a company's proxy materials.[859] Unlike the use of Rule 14a-11, this two-step process depends on both the likelihood that a shareholder will initiate such a process and on its success at each step of the process (e.g., the successful inclusion of the shareholder proposal in the company's proxy materials and adoption of the proposal by the appropriate shareholder vote). The likelihood that a shareholder will initiate the two-step process could be limited by the costs arising from the time needed to complete the process (e.g., including opportunity costs of holding securities where the shareholder may consider the company's board composition to be sub-optimal) and the added risk of failure due to the need to complete two separate steps to include its director nominees in the proxy materials. The likelihood that a shareholder will initiate this process is also affected by the existence of Rule 14a-11, which some eligible shareholders may seek to use instead.

Lastly, the scope of the effects of Rule 14a-11, including the expected benefits and costs described below, is affected by the size of the eligible population of shareholder groups and companies. Consequently, the scope of the direct effects of Rule 14a-11 will narrow to the extent that the rule's eligibility criteria reduce the number of shareholders eligible to take advantage of the rule. According to the data from Form 13F filings, 33% of the 6,416 public issuers included in the sample would have one or more shareholders that, on its own, satisfies the

---

directors after their first term in office.

859 The first step of this two-step process would be the submission of a shareholder proposal pursuant to Rule 14a-8 seeking to establish a procedure in a company's governing documents for the inclusion of shareholder nominees for director in the company's proxy materials and shareholder approval of the proposal. The second step would be the submission and inclusion of shareholder director nominees in the company's proxy materials pursuant to the nomination procedures adopted by shareholders.

3% ownership threshold and three-year holding period requirement of Rule 14a-11.[860] Our extension of the holding period from a one-year period, as proposed, to the three-year period in the final rule, as well as the increase in the ownership threshold from that proposed for large accelerated filers, limit the number of shareholders eligible to use the rule and the number of companies directly affected by the rule. For non-accelerated filers, the uniform 3% ownership threshold is lower than the 5% ownership threshold that we proposed for that class of filers. This may result in an increase in the number of shareholders eligible to use Rule 14a-11 and the number of companies directly affected by the rule as compared to those shareholders and companies affected under the proposed one year and 5% minimum standards; however, we believe that the extension of the holding period from one to three years may limit any increase in the number of shareholders eligible to use the rule at smaller reporting companies. The comments we received on the Proposal did not substantiate the concern that the rule would have a disproportionate impact on small issuers, and comments from companies overwhelmingly supported uniform ownership thresholds for all public companies.

D. Benefits

We believe that Rule 14a-11 and the amendment to Rule 14a-8(i)(8), where applicable, will (1) facilitate shareholders' ability to exercise their traditional state law rights to nominate and elect directors; (2) establish a minimum uniform procedure pursuant to which shareholders will be able to include their director nominees in a company's proxy materials and enhance shareholders' ability to propose alternative procedures that further shareholders' rights to nominate and elect directors; (3) potentially improve overall board and company performance; and (4) result in more informed voting decisions in director elections due to improved disclosure

860 November 2009 Memorandum. <u>See</u> Section II.B.4.b. above for a discussion of the data, including its limitations.

of shareholder director nominations and enhanced communications between shareholders regarding director nominations.

1. Facilitating Shareholders' Ability to Exercise Their State Law Rights to Nominate and Elect Directors

Facilitating shareholders' ability to exercise their traditional state law rights to nominate and elect directors is a direct benefit of the new rules for shareholders. The new rules do so by requiring the company proxy materials to include shareholder nominees under certain conditions and, as a result, providing alternative means for shareholders to nominate and elect director candidates other than through a traditional proxy contest. Some eligible shareholders may view the new rules as more advantageous than traditional proxy contests and, hence, the new rules may influence their behavior. In addition, eligible shareholders who would have considered launching a proxy contest for purposes other than to change control of the company may prefer to use the new rules instead. The availability of the new rules also may encourage shareholders who would not have previously considered conducting a proxy contest to take a greater role in the governance of their company by using the new rules to have their nominees for director included in a company's proxy materials.

The precise level of the direct benefits to shareholders will depend on a number of other factors. The benefits may be enhanced to the extent that companies' governing documents are modified to require inclusion of shareholder nominees for director in the company's proxy materials from a broader spectrum of shareholders (for example, by lowering the ownership threshold required to have a nominee included in the company's proxy materials or shortening the holding period).[861] The instances of such changes to provisions in governing documents may

861 As adopted, Rule 14a-11 requires the nominating shareholder individually, or the nominating group in the aggregate, to hold at least 3% of the total voting power of the company's securities that are entitled to be voted on the election of directors at the annual (or a special meeting in lieu of the annual) meeting of

increase as a result of the amendment to Rule 14a-8(i)(8).[862] We also recognize the possibility that certain quantifiable benefits for shareholders, such as a nominating shareholder's or group's savings in the direct costs of printing and mailing proxy materials, may be less than the quantifiable costs for a company subject to the new rules. We note, however, that the benefits of the new rules are not limited to those that are quantifiable (such as the direct savings in printing and mailing costs) and instead include benefits that are not as easily quantifiable (such as the possibility of greater shareholder participation and communication in the director nomination process), as discussed below. We believe that these benefits, collectively, justify the costs of the new rules.

We discuss below the ways in which the new rules will facilitate shareholders' exercise of their traditional state law rights and the benefits for shareholders (particularly as compared to a traditional proxy contest). We discuss specific monetary cost savings, both direct and indirect, as well as other changes and the resulting benefits for shareholders.

Shareholders generally have the right under state law to nominate and elect their own director candidates – a right that many shareholders believe they should be able to exercise.[863] Currently, however, a shareholder or group that wishes to present its director nominations for a shareholder vote must generally conduct a proxy contest, which is a costly endeavor. The nominating shareholder or group would have to incur costs involved with preparing proxy

---

shareholders, or on a written consent in lieu of such meeting, on the date the nominating shareholder or nominating group provides notice to the company on Schedule 14N.

862 As amended, companies will no longer be able to rely on Rule 14a-8(i)(8) to exclude a shareholder proposal that seeks to establish a procedure in the company's governing documents for the inclusion of shareholder nominees for director in the company's proxy materials.

863 See letters from AFSCME; Sodali; Universities Superannuation (citing a June 2009 survey conducted by ShareOwners.org showing that 82% of the respondents believed that shareholders should be able to "nominate and elect directors of their own choosing to the boards of the companies they own," while 16% of the respondents stated that "shareholders should not be able to propose directors to sit on the boards of the companies they own.").

materials with the required disclosures regarding the director nominations and mailing the proxy materials to each shareholder solicited.[864] Several commenters stated that the costs of traditional proxy contests have made them prohibitively expensive for shareholders wishing to exercise their traditional state law rights to nominate and elect directors.[865]

Further, the concern about the costs of conducting a traditional proxy contest is not limited to the fact that the nominating shareholder or group must incur these costs directly. A collective action problem also exists. The time and effort spent by a shareholder in nominating and advocating for new directors are not shared by other shareholders. This unequal cost sharing may serve to discourage any one shareholder from assuming the costs of running a traditional proxy contest on its own, even though a successful contest could result in a greater aggregate benefit for all shareholders.[866] As a result, there is the added economic cost of foregone opportunities where a qualified director candidate fails to be nominated because no one shareholder or group wishes to bear alone the costs of an election contest for the benefit of all shareholders.

We believe Rule 14a-11 will further our stated goal of facilitating shareholders' ability to

---

864 Proxy contests waged in connection with efforts to obtain control may involve costs related to not only preparing proxy materials and engaging in solicitation efforts, but to the purchase or lock-up of a significant amount of the voting securities of the target company. Such costs could be high.

865 See letters from Americans for Financial Reform; CalPERS; CII; Florida State Board of Administration; M. Katz; J. McRitchie; S. Ranzini; Teamsters.

866 See, e.g., letters from Bebchuk, et al. ("In evaluating eligibility and procedural requirements, the SEC should also keep in mind that many institutional investors lack incentives to invest actively in seeking governance benefits that would be shared by their fellow shareholders."); Lucian A. Bebchuk and Scott Hirst ("Bebchuk/Hirst") (submitting the article by Lucian A. Bebchuk and Scott Hirst, Private Ordering and the Proxy Access Debate, 65 BUS. LAW. 329 (2010)("Bebchuk and Hirst (2010)"), in which the authors state: "Thus, challengers who might be able to improve the management of the company may be discouraged from running because they will bear all of the costs but capture only a fraction of the benefits from any improvement in governance." See also Lynn A. Stout, The Mythical Benefit of Shareholder Control, 93 VA. L. REV. 789, 789 (2007)("Stout (2007)")("In a public company with widely dispersed share ownership, it is difficult and expensive for shareholders to overcome obstacles to collective action and wage a proxy battle to oust an incumbent board.")(cited in the Proposing Release, Section V.B.1.).

nominate and elect their own director candidates by allowing shareholders to avoid certain direct costs of conducting a traditional proxy contest and reducing the overall costs to shareholders for nominating and electing directors – a belief shared by several commenters.[867] The new rules also will mitigate collective action and free-rider concerns that may have otherwise deterred many shareholders from exercising their rights under state law to nominate directors.

Direct cost savings, particularly as compared to the cost of a traditional proxy contest, come from two sources. First, a nominating shareholder or group may see direct cost savings due to reduced printing and postage costs. Based on the information available,[868] we calculate that a shareholder using Rule 14a-11 to submit a director nominee or nominees to be included in a company's proxy materials will save at least $18,000 on average in printing and postage costs.

Second, and significantly, a nominating shareholder or group may see direct cost savings related to reduced expenditures for advertising and promotion of its candidates as a result of its

---

867 See letters from CII; Key Equity Investors; Pershing Square. The benefit of a reduction in the cost of a proxy solicitation exists only to the extent that the nominating shareholder or group views Rule 14a-11 as a substitute for a traditional proxy contest. Even with the adoption of Rule 14a-11, some shareholders may prefer to conduct a traditional proxy contest due to the various restrictions on the use of the rule. For example, the rule restricts the number of shareholder director nominees that a company will be required to include in its proxy materials. The rule also will be available only to shareholders that do not hold the securities in the company with the purpose, or with the effect, of changing control of the company. These elements of Rule 14a-11 impose restrictions that are not present in a traditional proxy contest. Some shareholders also may prefer a traditional proxy contest over Rule 14a-11 for reasons related to their strategy for the conduct of the election contest, such as having greater control over the mailing schedule and contents of their proxy materials. See, e.g., letter from Carl T. Hagberg ("C. Hagberg")(stating that "most truly serious nominators of director candidates will surely produce their own proxy materials, and take control of their own 'electioneering' with materials and proxy cards of their own, if they want to stand a reasonable chance to win."). Therefore, while Rule 14a-11 may encourage some shareholders seeking to nominate and elect their candidates to use the rule instead of conducting a traditional proxy contest, other shareholders may continue to prefer a traditional contest. For such shareholders, the expected reduction in a shareholder's proxy solicitation costs will not materialize.

868 According to a study of proxy contests conducted during 2003, 2004, and 2005, the average cost of a proxy contest to a soliciting shareholder was $368,000. See letter from Automatic Data Processing, Inc. (April 20, 2006) regarding Internet Availability of Proxy Materials, Exchange Act Release No. 34-52926 (December 8, 2005)(File No. S7-10-05). The costs included those associated with proxy advisors and solicitors, processing fees, legal fees, public relations, advertising, and printing and mailing of proxy materials. Approximately 95% of the costs were unrelated to printing and postage. The cost of printing and postage averaged approximately $18,000.

ability to use the company's proxy materials to directly solicit other shareholders. To the extent that the nominating shareholder or group decides to reduce its public relations and advertising expenditures to promote its candidates, or to engage proxy solicitors, the cost savings will be greater. These reductions in costs may remove a disincentive for shareholders to submit their own director nominations, mitigate the collective action concern, and serve the goal of facilitating shareholders' ability to exercise their traditional state law rights to nominate and elect directors.

We received significant comment questioning the need for the new rules to reduce the costs described above or the degree to which the reduction in costs will actually facilitate shareholder director nominations.[869] One commenter characterized the direct printing and mailing cost savings as the sole benefit of the new rules for shareholders and one that is not justified by the costs and disruption that would result from the rules.[870] The commenter observed that the average of $18,000 in estimated savings identified in the Proposing Release represented less than 5% of the cost of a traditional proxy contest and did not include costs that would be incurred by a shareholder actively seeking the election of its nominee, such as costs related to legal counsel, proxy solicitors, public relations advisers and advertising.

We recognize that the adoption of the new rules may not relieve a nominating shareholder or group of all expenditures that could be incurred for an active campaign that may be more successful to support the election of its candidate to the company's board of directors. The new rules, however, are not intended to serve that purpose. Instead, the new rules' goal is to

---

869 See letters from 26 Corporate Secretaries; 3M; Ameriprise; Association of Corporate Counsel; BRT; Cummins; DuPont; ExxonMobil; FMC Corp.; Frontier; GE; General Mills; Honeywell; IBM; Keating Muething; Motorola; Schneider; Sidley Austin; Simpson Thacher; Time Warner Cable; Wachtell; Wells Fargo; Xerox.

870 See letter from BRT.

facilitate shareholders' ability to present their own director nominees for a vote at a shareholder meeting by eliminating or reducing barriers in the proxy solicitation process – one of which is the direct cost of printing and mailing proxy materials – that have contributed to frustrating shareholder director nominations.[871]

We also recognize that the direct printing and mailing cost savings of $18,000, on their own, may not be viewed by some to be significant enough to drive the behavior of large shareholders of public companies. The comments that we received regarding the likely increase in the number of election contests resulting from the new rules, however, seem to undercut this view and suggest instead that shareholders' behavior may indeed be influenced by the rules.[872] The extent to which election contests are predicted to increase as a result of shareholders nominating their own director candidates for inclusion in the company's proxy materials strongly indicates that the benefits of the new rules cannot be fairly characterized as a "mere $18,000 in estimated savings"[873] – a characterization that we believe obfuscates the significance of this benefit of our new rules.

We received comment that while certain shareholders may be relieved of certain costs to run a traditional proxy contest as a result of the new rules, the rules may simply shift those costs onto the company and, indirectly, all shareholders.[874] Therefore, while the rules may reduce the

---

871 We recognize that other factors may have similarly frustrated the effective exercise of this state law right. We discuss below these factors and how the new rules will reduce or eliminate these factors.

872 See, e.g., letters from Altman (stating that participants in its survey predicted that, on average, 15% of companies listed on U.S. exchanges could expect to face a shareholder director nomination submitted under Rule 14a-11 in 2011, based on the eligibility criteria of the Proposal); BRT (stating that the new rules "will increase the frequency of contested elections…"); Chamber of Commerce/CCMC (noting that if the new rules are adopted, "it is likely that proxy contests (in which the company is required to solicit proxies on behalf of shareholders) will increase greatly and may become customary.").

873 See letter from BRT.

874 See letter from ABA. We recognized this possibility in the Proposing Release as well, noting that the rule "may result in a decrease in costs to shareholders that would have to conduct proxy contests in the absence

direct costs of solicitation by a particular shareholder for its director nominees, it may result in an increase in the overall cost of a company's proxy solicitation for a director election (e.g., additional printing and mailing costs arising from the disclosure of the shareholder director nominations) and indirectly the cost to all shareholders, particularly if the new rules lead to an increase in the number of shareholder director nominations. We have some reason to believe, however, that the increased costs for the company may not be as much as would otherwise result if that shareholder engaged in a traditional proxy contest.[875] We also note that, to the extent that the new rules help to address the collective action concern, it could remove disincentives that previously deterred shareholders from submitting director nominations that may have ultimately benefited all shareholders.

Other commenters observed that savings in printing and mailing costs could be obtained through our notice and access model for electronic delivery of proxy materials[876] or stated that the notice and access model has already reduced the costs for shareholders to effect changes in the membership of a board.[877] We note that this observation applies only to the direct

---

of [proposed] Rule 14a-11, but may increase the costs for companies." See Proposing Release, Section V.C.3.

875 One commenter on the 2003 Proposal estimated that a Rule 14a-11 contest would cost a company approximately one-third what a full proxy contest costs. See letter from Stephen M. Bainbridge submitted in connection with the 2003 Proposal (File No. S7-19-03)("Bainbridge 2003 Letter"). Based on this assumption and relying on data from a late 1980s survey, this commenter estimated that the costs of such a contest to a public company would be $500,000. This commenter also cited data estimating companies' annual expenditures on Rule 14a-8 shareholder proposals to be $90 million. While this commenter noted the belief that it is unlikely that there will be as many Rule 14a-11 election contests as Rule 14a-8 shareholder proposals, the commenter asserted that incumbent boards are likely to spend considerably more on opposing each Rule 14a-11 contest than on opposing a Rule 14a-8 shareholder proposal. This commenter estimated that $100 million may be an appropriate estimate for the lower boundary of the range within which Rule 14a-11's direct costs will fall. Commenters did not provide any data during the comment period for the Proposal that compared these costs for a company.

876 See, e.g., letters from 26 Corporate Secretaries; Ameriprise; BRT.

877 See letters from 26 Corporate Secretaries; 3M; Ameriprise; Association of Corporate Counsel; BRT; Cummins; DuPont; ExxonMobil; FMC Corp.; Frontier; GE; General Mills; Honeywell; IBM; Keating Muething; Motorola; Schneider; Sidley Austin; Simpson Thacher; Time Warner Cable; Wachtell; Wells

printing and mailing costs, rather than all of the other monetary cost savings discussed throughout this section. We agree that the notice and access model may decrease significantly the printing and mailing costs associated with a proxy solicitation. To the extent that a shareholder chooses to nominate and elect its director candidates through a traditional proxy contest using the notice and access model, the expected benefit of a reduction in printing and mailing costs will be somewhat lower. The notice and access model, however, may not necessarily provide a soliciting shareholder with the same cost savings possible under Rule 14a-11. Under the model, a soliciting shareholder will still incur the costs of printing and mailing notices of availability of proxy materials to shareholders from whom the person is soliciting proxy authority.[878] Further, as we recognized at the time we created the notice and access model, additional printing and mailing costs will be incurred to the extent that a solicited shareholder requests paper copies of the proxy materials.[879] A soliciting shareholder also may prefer using the new rules over a traditional proxy contest conducted through the notice and access model for reasons related to its strategy for the conduct of the election contest, such as avoiding the need and cost to use Exchange Act Rule 14a-7 to obtain a shareholder list from the company (or have

---

Fargo; Xerox.

878 Exchange Act Rule 14a-16(l)(2). A soliciting person other than the company could limit the cost of a solicitation by soliciting proxies only from a select group of shareholders, such as those with large holdings, without furnishing other shareholders with any information. This flexibility would allow a soliciting person other than the company to reduce even further its printing and mailing costs by soliciting only those persons who have not previously requested paper copies of the proxy materials. Certain practical reasons, however, may deter a soliciting person other than the company from taking full advantage of this flexibility, such as the fact that institutional investors may prefer receiving paper copies of proxy materials. See Jeffrey N. Gordon, Proxy Contests in an Era of Increasing Shareholder Power: Forget Issuer Proxy Access and Focus on E-Proxy, 61 VAND. L. REV. 476, 488 (2008)(noting that institutional investors "generally may request paper delivery to minimize their own printing costs.")(cited in the letters from BRT and Simpson Thacher).

879 See Internet Availability of Proxy Materials, Release No. 34-55146 (January 22, 2007)("Internet Proxy Availability Release")(noting that "to the extent that some shareholders request paper copies of the proxy materials, the benefits of the amendments in terms of savings in printing and mailing costs will be reduced.").

the company send proxy materials on its behalf)[880] as well as the requirement to file preliminary proxy materials at least ten calendar days before definitive materials are first sent to shareholders.[881]

The new rules will do more than reduce the direct monetary costs described above. We recognize that shareholders today are widely dispersed and the corporate proxy is the principal means through which state law voting rights are exercised. The dispersed nature of ownership creates certain intangible disincentives to the effective exercise of shareholders' ability to nominate and elect their own director candidates, as discussed below. As we stated in the Proposing Release, the proxy process provides the only practical means for shareholders to solicit votes from other shareholders in favor of the election of their nominees. The current inability of many shareholders to utilize the proxy process for this purpose means that shareholder director nominees do not have a realistic prospect of being elected because most, if not all, shareholders would have cast their votes well in advance of the shareholder meeting. Shareholders are deprived of not only the ability to exercise a traditional state law right, but the opportunity to assess and vote on qualified candidates who could have been presented for a vote

880 Exchange Act Rule 14a-7 sets forth the obligation of companies either to provide a shareholder list to a requesting shareholder or to send the shareholder's proxy materials on the shareholder's behalf. The rule provides that the company has the option to provide the list or send the shareholder's materials, except when the company is soliciting proxies in connection with a going-private transaction or a roll-up transaction. Under Rule 14a-7(e), the shareholder must reimburse the company for "reasonable expenses" incurred by the company in providing the shareholder list or sending the shareholder's proxy materials.

881 Exchange Act Rule 14a-6 requires that preliminary copies of the proxy statement and form of proxy be filed with the Commission at least ten calendar days prior to the date that definitive copies of such materials are first sent or given to security holders, except if the solicitation relates to certain matters to be acted upon at the meeting of security holders. Accordingly, the proxy statement and form of proxy for a traditional proxy contest must be filed in preliminary form. By contrast, under the amendments to Rule 14a-6 that we are adopting today, the inclusion of a shareholder director nominee in the company's proxy materials will not require the company to file preliminary proxy materials, provided that the company is otherwise qualified to file directly in definitive form. In this regard, the inclusion of a shareholder director nominee will not be deemed a solicitation in opposition for purposes of the exclusion from filing preliminary proxy materials.

if the proxy process functioned as intended. As with the direct monetary costs, reducing the costs arising from the dispersed nature of ownership discussed below will help address any related collective action concerns.

Some commenters observed that a shareholder seeking to nominate and elect its own director candidates through a traditional proxy contest is disadvantaged by the fact that its candidates are presented to shareholders through a separate set of proxy materials.[882] A nominating shareholder or group may encounter difficulties in having its nominees evaluated in the same manner as those of management by shareholders who are used to receiving only the company's proxy materials and who may react differently, and perhaps negatively, to the shareholder's nominees simply because the nominees are presented in a separate, unfamiliar set of proxy materials.

As we stated throughout this release, the federal proxy rules should not frustrate the exercise of a shareholder's traditional state law right to present its own director candidates for a shareholder vote. To the extent that the exercise of this right is hindered simply because of a

---

882 See letters from Bebchuk/Hirst (submitting the Bebchuk and Hirst (2010) study, which noted the ability of shareholders to include their nominees in the company's proxy materials would "avoid intangible disadvantages that may result from being on a separate card."); Pershing Square (stating that "the absence of universal ballots, on which shareholders can vote from among all nominees regardless of who proposed them, is glaring and clearly anti-choice" and that "[o]ur hope is that, outside the control context, selection of the best nominees in a contest will be based more on character, competency, and relevancy of their experience rather than the identity of the person nominating the candidate.").

At the October 7, 2009 "Proxy Access Roundtable" held by the Harvard Law School Program on Corporate Governance (the transcript of which was submitted as part of a comment letter from S. Hirst), Roy Katzovicz, the Chief Legal Officer of Pershing Square Capital Management, L.P. explained:

> As a cultural matter, there are two sub-points. First and foremost, having the decision of choosing two people, one next to the other, invites, we think, a more intelligent analysis on the part of shareholders generally. In particular, we think that if the basis for election for a nominee is their merit as an individual, a fund or an investor of any type that can identify the deadweight on the board, and in place of that deadweight find ideal candidates from a skills perspective to round out the board, they're going to have an easier time getting shareholder support for their nominee. Their ability to vote among all the nominees and from all proponents, I think, facilitates that kind of person-by-person analysis, versus slate-by-slate analysis.

nominating shareholder's or group's need to deliver a separate set of proxy materials and potentially negative reaction by shareholders to the appearance of this set of materials, we believe that our new rules will help address that concern. With the new rules, a shareholder will have the ability to include its director nominees in the company's proxy materials, provided that the rules' requirements are met. The fact that a nominating shareholder or group could have its director nominees included in a company's proxy materials – as opposed to being included in its own proxy materials – pursuant to the new rules may be viewed by the shareholder or group as a significant improvement in its ability to have its nominees evaluated by shareholders in the same manner as they evaluate management's nominees. Shareholders who are interested in effecting a change in the company's leadership or direction may be less likely to be deterred by the prospect that their director nominees will not be assessed on their merit. Nominating shareholders also may see less need for additional soliciting efforts, such as the hiring of proxy solicitors, public relations advisors, or advertising, if their director nominees are presented alongside those of management in a set of company proxy materials with which the company's shareholders are familiar.[883]

Shareholders also may be hindered in making their voting decisions in a traditional proxy contest due to the fact that they have to evaluate more than one set of proxy materials – one sent by a company and another sent by an insurgent shareholder – when evaluating whether and how to grant authority to vote their shares by proxy.[884] Presenting the competing director nominees

---

883 As discussed in Section II.B.9.d.ii. above, we have adopted the proposed amendments to Exchange Act Rule 14a-4 out of a similar desire to avoid giving management's director nominees an advantage over those of a nominating shareholder or group and to create an impartial presentation of the nominees for whom a shareholder may vote.

884 One commenter stated that if enabling shareholders to evaluate a board more efficiently and make more informed voting decisions is the goal of the Proposal, then enhancing proxy disclosure, rather than facilitating proxy contests, will better achieve that goal. See letter from Davis Polk. We recognize the importance of enhancing the disclosure provided in connection with proxy solicitations and recently

on one proxy card, with the related disclosure contained in one proxy statement, may simplify the shareholder's decision-making process and reduce the potential for any confusion on the part of shareholders.[885] The result may be a greater degree of participation by shareholders through the proxy process in the governance of their companies.

2. Minimum Uniform Procedure for Inclusion of Shareholder Director Nominations and Enhanced Ability for Shareholders to Adopt Director Nomination Procedures

Rule 14a-11, as adopted, will provide shareholders of companies subject to the federal proxy rules the ability to include their director nominees in the company's proxy materials, provided that the rule's requirements are met.[886] Further, with our adoption of the amendment to Rule 14a-8(i)(8), shareholders will be able to present in the company's proxy materials a proposal that would seek to establish a procedure in the company's governing documents for the inclusion of shareholder nominees for director in the company's proxy materials.[887] Shareholders will have a greater ability to present for a shareholder vote a director nomination procedure with requirements, such as the requisite ownership threshold or holding period, that differ from those

---

adopted new rules to better enable shareholders to evaluate the leadership of public companies. See Proxy Disclosure Enhancements Adopting Release. These rules, however, do not dispense with the need for Rule 14a-11 and the amendment to Rule 14a-8(i)(8). The new rules we are adopting will complement the recently-adopted proxy disclosure enhancement rules by enabling shareholders to submit their own director nominees if, after evaluating a company's public disclosures and performance, they are displeased with that company's current leadership or direction.

885 As discussed in Section IV.D.4. below, the new disclosure requirements that we are adopting for shareholder director nominations submitted pursuant to Rule 14a-11, a state or foreign law provision, or a provision in the company's governing documents also will facilitate more informed voting decisions by providing shareholders with important disclosures and enhancing their ability to communicate with each other regarding director nominations.

886 For a discussion of the companies that are subject to Rule 14a-11, see Section II.B.3. above. As discussed in that section, foreign private issuers and companies that are subject to the federal proxy rules solely because they have a class of debt securities registered under Exchange Act Section 12 will not be subject to Rule 14a-11. For smaller reporting companies, Rule 14a-11 will become effective three years after the date that the rule becomes effective for all other companies.

887 As previously discussed, a shareholder proposal seeking to establish such a procedure will continue to be subject to exclusion under other provisions of Rule 14a-8.

of Rule 14a-11.[888]

We received significant comment regarding the uniform applicability of Rule 14a-11 and the amendment to Rule 14a-8(i)(8).[889] While there was widespread support for the amendment to Rule 14a-8(i)(8), commenters were divided on the extent to which companies and shareholders should be permitted to use Rule 14a-8 to propose alternative requirements for shareholder director nominations and on the related issue of whether shareholders and companies should be able to opt out of Rule 14a-11 entirely. Some commenters believed that the amendment to Rule 14a-8(i)(8) should facilitate private ordering under state law by enabling shareholders to include in the company's proxy materials a Rule 14a-8 proposal that would impose more restrictive eligibility criteria than those of Rule 14a-11.[890] A number of commenters also believed that shareholders should be able to elect to have their companies opt out of Rule 14a-11, including through the submission of a Rule 14a-8 proposal.[891] To facilitate private ordering, a significant number of commenters supported the adoption of the amendment to Rule 14a-8(i)(8) while opposing adoption of Rule 14a-11.[892]

By contrast, other commenters supported an amendment enabling shareholders to include

---

888 As discussed in Section II.C. above, a provision in a company's governing documents establishing a procedure for the inclusion of shareholder director nominees in a company's proxy materials will not affect the operation of Rule 14a-11, regardless of whether the company's shareholders have approved the provision.

889 For further discussion of the comments regarding the uniform applicability of Rule 14a-11 and the amendment to Rule 14a-8(i)(8), see Sections II.B.2. and II.C. above.

890 See letters from American Express; BorgWarner; Brink's; BRT; CIGNA; P. Clapman; Con Edison; CSX; Davis Polk; DTE Energy; DuPont; GE; General Mills; C. Holliday; JPMorgan Chase; Metlife; P&G; Pfizer; Safeway; Seven Law Firms; Society of Corporate Secretaries; Southern Company; Tenet; U.S. Bancorp; Verizon.

891 See letters from DTE Energy; JPMorgan Chase; P&G; Seven Law Firms; Society of Corporate Secretaries; U.S. Bancorp.

892 See, e.g., letters from ABA; BRT; Society of Corporate Secretaries.

in a company's proxy materials a Rule 14a-8 proposal that establishes a shareholder director nomination procedure but only if the procedure would provide shareholders with a greater ability to include their director nominees in the company's proxy materials.[893] A number of commenters also opposed any provision that would permit companies to opt out of Rule 14a-11[894] and preferred the uniform applicability of Rule 14a-11 to all companies.[895]

We considered these comments carefully. As discussed above, and noted in the Proposal, the purpose of the rules is to facilitate shareholders' traditional state law rights to nominate and elect their own director candidates. As such, we believe that a uniform application of Rule 14a-11 to companies subject to the federal proxy rules is the best way to enable shareholders of these companies to do so without having to incur the types of costs and other disadvantages that shareholders traditionally have encountered. A single, uniform rule will provide shareholders of any company subject to the rule with the ability to meaningfully exercise their traditional state law rights to present their own director candidates for a vote at a shareholder meeting may be invoked through the proxy process. With the adoption of the amendment to Rule 14a-8(i)(8), shareholders will be able to establish procedures that can further facilitate this ability, if they wish.

By contrast, we believe that exclusive reliance on private ordering under state law would not be as effective and efficient in facilitating the exercise of these rights. Commenters identified procedural and legal difficulties that they believe would hinder the establishment of a

---

893 See letters from CII; Governance for Owners; D. Nappier.

894 See letters from AFL-CIO; Amalgamated Bank; W. Baker; Florida State Board of Administration; IAM; Marco Consulting; P. Neuhauser; Nine Law Firms; Norges Bank; Relational; Shamrock; TIAA-CREF; USPE; ValueAct Capital.

895 See letters from AFSCME; CalPERS; CalSTRS; CII; COPERA; Florida State Board of Administration; John C. Liu ("J. Liu"); D. Nappier; Nathan Cummings Foundation; Phil Nicholas ("P. Nicholas"); OPERS; State Universities Retirement System of Illinois ("SURSI"); SWIB; WSIB.

shareholder director nomination procedure under private ordering, including: a supermajority voting standard for approval of the proposal;[896] the constraints imposed by the 500-word limit for a Rule 14a-8 proposal;[897] the significant percentage of companies that restrict shareholders' ability to amend or propose bylaws;[898] and the potential ability of a board to repeal or amend a shareholder-adopted bylaw procedure.[899] Some commenters also expressed a general concern that under private ordering, the provisions in a company's governing documents regarding shareholder director nominations may be so restrictive that it would be impossible for shareholders to have candidates included in company proxy materials.[900] Other commenters, however, disagreed that these difficulties would actually interfere with the establishment of a procedure under a private ordering approach.[901]

As previously discussed, we believe that our rules should provide shareholders with the ability to include director nominees in a company's proxy materials without the need for

---

896 See B. Young, footnote 52, above ("Data on bylaw amendment limitations show that at between 38 and 43% of companies, depending on the index, shareholders are either unable to amend the bylaws or face significant challenges in the form of supermajority vote requirements."); see also letters from AFSCME; Bebchuk/Hirst; Florida State Board of Administration; J. Liu.

897 See letters from Bebchuk/Hirst; CII; Florida State Board of Administration.

898 See letters from AFSCME; Florida State Board of Administration; Nathan Cummings Foundation; SWIB.

899 See letters from AFSCME; Corporate Library; Sodali. See also Michael E. Murphy, The Nominating Process for Corporate Boards of Directors: A Decision-Making Analysis, 5 BERKELEY BUS. L.J. 131, 144 (2008)(discussing how a company's management defeated a shareholder proposal regarding shareholder director nominations through the use of a bylaw requiring a super-majority shareholder vote in favor of such a shareholder proposal and noting that "[t]he super-majority requirement was one of several potential defenses that management might have employed; it might also have imposed inconvenient notice requirements, stringent shareholder qualification rules, or restrictions mirroring the conditions of SEC rule 14a-8. If these barriers proved insufficient, management might have considered counter-initiatives; it is an open question in Delaware and certain other states whether the board of directors has the power to repeal a shareholder-initiated bylaw by adopting a superseding bylaw amendment.")

900 See letters from Florida State Board of Administration; P. Neuhauser; Shamrock.

901 See letters from AT&T; ABA; BRT; J. Grundfest; Keller Group; Lemonjuice.biz ("Lemonjuice"); Seven Law Firms.

shareholders to bear the burdens of overcoming substantial obstacles to creating that ability on a company-by-company basis.[902] Private ordering based on an opt-in approach would require shareholders to incur significant costs, regardless of the presence of the difficulties described above. Shareholders would need to expend both time and funds to draft and submit a proposal, such as a Rule 14a-8 proposal, establishing a shareholder director nomination procedure on a company-by-company basis.[903] These costs may be higher if the company opposes and solicits against adoption of the proposal – a possibility that is very likely at companies where disagreements between incumbent directors and a nominating shareholder or group already exist.[904] Further, shareholders may be disinclined to undergo a two-step process to submit their own nominees – first, to establish a nomination procedure through a Rule 14a-8 shareholder proposal and, second, to submit their director candidates for inclusion in the company's proxy materials – given the length of time that they will have to hold the requisite amount of securities and, perhaps more importantly, the risk of failure at each step of the process.

Different but equally significant issues would arise under an opt-out approach. Shareholders who wish to retain their ability to include their director nominees in the company's proxy materials pursuant to Rule 14a-11 may find it difficult to successfully oppose an opt-out proposal due to management's ability to draw on the company's resources to promote the

---

902 See Section II.B.2. above, for additional discussion of our consideration of a private ordering approach.

903 See letters from CalPERS; Florida State Board of Administration; D. Nappier; P. Neuhauser. One of these commenters estimated that the approximate cost for shareholders of "running a proposal" is $30,000. See letter from CalPERS. The commenter estimated that it would cost $351,000,000 to attempt to establish the right of shareholders of Russell 3000 companies to include their director nominees in a company's proxy materials.

904 The reluctance of companies to support the establishment of a shareholder director nomination procedure was noted in an article submitted by a commenter. See letter from Bebchuk/Hirst (referring to Bebchuk and Hirst (2010)). In their article, the authors observed that while the establishment of such a procedure is permissible under the existing laws of some states, including Delaware, only three companies have in fact established a shareholder director nomination procedure.

adoption of the proposal.[905] We also believe that if we were to allow an opt-out approach, even one in which only shareholders could approve an opt out, there is a high likelihood that the effort to procure such approval could be supported by management and funded by company assets, while opposing views could not be advanced effectively. Shareholders of these companies would find themselves, once again, left without an effective or efficient ability to nominate and elect their own director candidates. Further, as some commenters observed, both the opt-in and opt-out approaches may impose unnecessary complexity and administrative burdens for shareholders with diversified holdings in numerous companies and may hinder their exercise of a traditional state law right.[906]

3. Potential Improved Board Performance and Company Performance

As discussed throughout this release, we are adopting the new rules with the goal of facilitating shareholders' ability under state law to nominate and elect directors for election to the board. Because state law provides shareholders with the right to nominate and elect directors to ensure that boards remain accountable to shareholders and to mitigate the agency problems associated with the separation of ownership from control, facilitating shareholders' exercise of

905 In this regard, we note that a survey that one commenter conducted showed that, if available, a large majority of its member companies – approximately two-thirds – would seek to implement an opt-out from Rule 14a-11. See letter from Society of Corporate Secretaries. This survey suggests that shareholders of many companies may, once again, be limited in their ability to have their director candidates included in the companies' proxy materials.

906 See letters from CFA Institute; CII; COPERA; D. Nappier; OPERS. One commenter countered that most long-term institutional shareholders are unlikely to submit director candidates at a large number of companies simultaneously and predicted that private ordering will lead to "some degree of standardization" in the types of shareholder director nomination procedures. See letter from Society of Corporate Secretaries. While we appreciate these points, we believe that adoption of Rule 14a-11, in fact, provides such "standardization." The amendment to Rule 14a-8(i)(8) complements Rule 14a-11 by enabling shareholders to consider and vote on proposals that provide shareholders with an even greater ability to present their own director candidates for a shareholder vote. Lastly, we recognize that the amendment to Rule 14a-8(i)(8) could result in some complexity as well, in that shareholders could establish director nomination procedures that require, for example, a different ownership threshold or holding period than those contained in Rule 14a-11. We believe, however, that such complexity is justified because it furthers our goal of facilitating, as much as possible, the effective exercise of shareholders' traditional state law right of shareholders to nominate their own director candidates for a vote at a shareholder meeting.

these rights may have the potential of improving board accountability and efficiency and increasing shareholder value. In the Proposing Release, we requested comment on the assertion that the Proposal could improve board performance and, hence, company performance – both for boards that include shareholder-nominated directors elected pursuant to the new rules and for boards that may be more attentive and responsive to shareholder concerns to avoid the submission of shareholder director nominations pursuant to the new rules.[907]

We received significant comment regarding this assertion. Many commenters agreed that the new rules may result in the benefit of more accountable, more responsive, and generally better-performing boards.[908] Other commenters, however, questioned whether the new rules would in fact promote board accountability,[909] warned of the costs of distracting and expensive election contests,[910] and disputed the conclusions of a study regarding the benefits enjoyed by companies with "hybrid boards" that was cited in the Proposing Release.[911] Commenters also

---

907 See Proposing Release, Section V.B.3.

908 See letters from AFSCME; Bebchuk, et al.; Brigham; CalPERS; CII; L. Dallas; T. DiNapoli; A. Dral; GovernanceMetrics; Governance for Owners; Hermes; M. Katz; LUCRF; J. McRitchie; R. Moulton-Ely; D. Nappier; P. Neuhauser; NJSIC; OPERS; Pax World; Pershing Square; Relational; RiskMetrics; D. Romine; Shareowners.org; Social Investment Forum; Teamsters; TIAA-CREF; Universities Superannuation; USPE; Walden. One commenter added that the benefits of the right to include shareholder director nominees in the company's proxy materials, including enhanced shareholder value from hybrid boards and directors becoming "more alert to their duties," are "less easy to quantify." See letter from P. Neuhauser.

909 See, e.g., letters from Alaska Air; Ameriprise; Brink's; Comcast; CSX; General Mills; Piedmont; Praxair; William H. Steinbrink ("W. Steinbrink"); Time Warner Cable; United Brotherhood of Carpenters.

910 See letters from ABA; Atlas; AT&T; Book Celler; Carlson; Carolina Mills; Chamber of Commerce/CCMC; Chevron; Crespin; M. Eng; Erickson; ExxonMobil; Fenwick; GE; General Mills; Glass Lewis; Glaspell; Intelect; R. Clark King; Koppers; MCO; MeadWestvaco; MedFaxx; Medical Insurance; Merchants Terminal; D. Merilatt; NAM; NIRI; NK; O3 Strategies; Roppe; Rosen; Safeway; Sara Lee; Schneider; Southland; Style Crest; Tenet; TI; tw telecom; R. VanEngelenhoven; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

911 See, e.g., letters from IBM; Simpson Thacher. These commenters questioned the conclusions of the study by Chris Cernich, et al., "Effectiveness of Hybrid Boards," IRRC Institute for Corporate Responsibility (May 2009)("Cernich (2009)"), available at http://www.irrcinstitute.org/pdf/IRRC_05_09_EffectiveHybridBoards.pdf (cited in the Proposing Release, Section V.B.3.). For example, one of these commenters stated that the study "demonstrates that the

challenged the basis for any suggestions in the Proposing Release that the recent economic crisis was somehow linked to the inability of shareholders to include their director nominees in the company's proxy materials, pointing out that we have contemplated similar regulatory efforts several times before the recent crisis occurred.[912]

The comments reflect the sharp divide on the question of whether facilitating shareholders' ability to exercise their rights to nominate and elect directors would lead to the benefit of improved board and company performance. We have considered these comments carefully and appreciate both the fact that the empirical evidence may appear mixed and the potential for negative effects due to management distraction and discord on the board that some

---

objectives of successful dissidents were often short-term in nature" and "suggests that companies with dissidents on their board perform better than their peers over a one-year period, but that they perform worse over a three-year period." See letter from Simpson Thacher. The other commenter stated that "the only conclusion that could fairly be drawn from the data is that some companies perform better, and many perform worse, under such circumstances" and "of the companies with dissident directors studied for three years after the contest period, share performance averaged just 0.7%, which is 6.6% less than peer companies."

We recognize the limitations of the Cernich (2009) study as well. While it provides useful documentation of patterns of behavior of activist investors, its long-term findings on shareholder value creation are difficult to interpret. Return estimates are presented without standard errors. For long-term returns in particular, this shortcoming makes it difficult to infer whether results arise because returns are different than peers in expectation, or because of random chance. Other studies cited in this release do use standard statistical inference techniques to approach similar questions. See, e.g., J. Harold Mulherin and Annette B. Poulsen, Proxy Contests and Corporate Change: Implications For Shareholder Wealth, J. FIN. ECON. (March 1998)("Mulherin and Poulsen (1998)")(cited in the NERA Report submitted as part of the letter from BRT).

912 See letters from 3M; ACE; Ameriprise; American Bankers Association; BRT; Devon; Dewey; GE; A. Goolsby; C. Holliday; Honeywell; IBM; Jones Day; Norfolk Southern; Pfizer; Sidley Austin; Simpson Thacher; TI; tw telecom; Unitrin; Wachtell. See also letters from BRT (submitting the study by Andrea Beltratti and René M. Stulz, Why Did Some Banks Perform Better During the Credit Crisis? A Cross-Country Study of the Impact of Governance and Regulation (July 2009)("Beltratti and Stulz (2009)"), in which the authors found "no consistent evidence that better governance led to better performance during the crisis" but found "strong evidence that banks with more shareholder-friendly boards performed worse."); Chamber of Commerce/CCMC (submitting an article by Brian R. Cheffins, Did Corporate Governance "Fail" During the 2008 Stock Market Meltdown? The Case of the S&P 500 ("Cheffins (2010)"), which stated that because "corporate governance functioned tolerably well in companies removed from the S&P 500 and that a combination of regulation and market forces will likely prompt financial firms to scale back the free-wheeling business activities that arguably helped to precipitate the stock market meltdown, the case is not yet made for fundamental reform of current corporate governance arrangements.").

commenters identified. After assessing the costs and benefits identified by commenters, and for reasons discussed below, we believe that the totality of the evidence and economic theory supports the view that facilitating shareholders' ability to include their director nominees in a company's proxy materials has the potential of creating the benefit of improved board performance and enhanced shareholder value – both in companies with the actual election of shareholder-nominated directors and in companies that react to shareholders' concerns because of the possibility of such directors being elected. Thus, as discussed below, it is our conclusion that the potential benefits of improved board and company performance and shareholder value justify the potential costs.

By facilitating shareholders' exercise of their traditional state law rights to nominate and elect directors, we believe that eligible shareholders may prefer to use the new rules over a costly traditional proxy contest, making election contests a more plausible avenue for shareholders to participate in the governance of their company. This may have two beneficial effects on the governance of a company. First, the board and management of a company may be increasingly responsive to shareholders' concerns, even when contested elections do not occur, because of shareholders' ability to present their director nominees more easily. Second, new shareholder-nominated directors may be more inclined to exercise judgment independent of the company's incumbent directors and management.

The new rules will remove or reduce some of the current disincentives to shareholders' exercise of their traditional state law rights to nominate director candidates. Once the rules become effective, boards' responsiveness to concerns expressed by shareholders may increase because shareholders could more easily nominate their own directors to run against incumbent directors.[913] In response to the Proposal, commenters submitted studies regarding the effects of reducing incumbent directors' insulation from removal, which showed measures that make incumbent directors more vulnerable to replacement by shareholder action have salutary deterrent effects against board complacency and improve corporate governance and shareholder value.[914] Further, by creating a new threat of removal, the new rules could lead to greater accountability on the part of incumbent directors to the extent they see a close link between their performance and the prospect of removal.[915] In response to the Proposal, one commenter also

---

913 The Supreme Court's recent opinion in Citizens United v. FEC, 130 S.Ct. 876 (2010) underscores the importance of board responsiveness to shareholder concerns. In Citizens United, the government asserted an interest in limiting independent expenditures by corporations in political campaigns in order to prevent dissenting shareholders from being compelled to fund corporate political speech with which they disagreed. Citizens United, 130 S.Ct. at 911. The Court, however, stated that any such coercion could be addressed "through the procedures of corporate democracy." Id., quotation omitted.

914 See letter from L. Bebchuk (noting the article by Lucian A. Bebchuk and Alma Cohen, The Costs of Entrenched Boards, J. FIN. ECON. (November 2005)("Bebchuk and Cohen (2005)"), in which the authors stated: "Staggered boards are associated with an economically meaningful reduction in firm value…[w]e also provide suggestive evidence that staggered boards bring about, and not merely reflect, an economically significant reduction in firm value…[f]inally, the correlation with reduced firm value is stronger for staggered boards that are established in the corporate charter (which shareholders cannot amend) than for staggered boards established in the company's bylaws (which shareholders can amend).").

Commenters also submitted empirical studies indicating that facilitating shareholders' rights and voice may result in better company performance. See letters from L. Bebchuk; CalSTRS; Nathan Cummings Foundation (noting the study by Paul Gompers, Joy Ishii and Andrew Metrick, Corporate Governance and Equity Prices, 118 Q.J. ECON. 107 (2003), in which the authors found that "firms with stronger shareholder rights had higher firm value, higher profits, higher sales growth, lower capital expenditures, and made fewer corporate acquisitions."); letters from CalSTRS; Nathan Cummings Foundation (noting the study by B. Lawrence Brown and Marcus Caylor, The Correlation Between Corporate Governance and Company Performance, Research Commissioned Institutional Shareholder Services (2004), in which the authors found that "firms with weaker governance perform more poorly, are less profitable, more risky, and have lower dividends than firms with better governance."). See also letter from T. Yang (noting the study by Bonnie Buchanan, Jeffry M. Netter, and Tina Yang, Proxy Rules and Proxy Practice: An Empirical Study of US and UK Shareholder Proposals (September 2009)("Buchanan, Netter, and Yang (2009)"), in which the authors found that "after receiving a shareholder proposal, [U.S.] firms exhibit higher stock returns and the improvement is greater [] when the proposal is likely to be wealth maximizing or sponsored by a shareholder owning a relatively large equity stake in the target firm.").

915 As we noted in the Proposing Release, economists have put forth theory and evidence on the link between incentives that are associated with accountability and performance. See, e.g., Benjamin E. Hermalin and Michael S. Weisbach, Endogenously Chosen Board of Directors and Their Monitoring of the Board, 88 AM. ECON. REV. 96 (1998)(cited in the Proposing Release, Section V.B.3); Milton Harris and Artur Raviv, Control of Corporate Decisions: Shareholders vs. Management (May 29, 2008), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=965559 (cited in the Proposing Release, Section V.B.3.).

submitted studies that showed that anti-takeover provisions protecting incumbent management are associated with economically significant reductions in firm valuation, returns and performance, and share prices increase when activists prompt elimination of provisions such as staggered boards.[916] Conversely, the creation of a staggered board structure was found to be associated with a reduction in firm value.[917] Because our new rules may make director elections more competitive by facilitating shareholders' ability to nominate and elect their own director candidates and, hence, also make some incumbent directors less secure in their positions, we believe that the rules may have analogous salutary effects.

As we noted in the Proposing Release, the presence of directors nominated by shareholders may have an effect on company performance and shareholder value.[918] We also noted in the Proposing Release that academic literature indicates the benefit to shareholders of

---

916 See Bebchuk and Hirst (2010)(noting the "substantial empirical evidence indicating that director insulation from removal is associated with lower firm value and worse performance."). See also letter from L. Bebchuk (noting the following articles: Lucian A. Bebchuk, Alma Cohen and Allen Ferrell, What Matters in Corporate Governance?, 22 REV. FIN. STUDS. 783 (2009)("Bebchuk, Cohen, and Ferrell (2009)")("We put forward an entrenchment index based on six provisions: staggered boards, limits to shareholder bylaw amendments, poison pills, golden parachutes, and supermajority requirements for mergers and charter amendments…[w]e find that increases in the index level are monotonically associated with economically significant reductions in firm valuation as well as large negative abnormal returns during the 1990-2003 period."); Re-Jin Guo, Timothy A. Kruse and Tom Nohel, Undoing the Powerful Anti-Takeover Force of Staggered Boards, J. CORP. FIN. (June 2008)("Guo, Kruse and Nohel (2008)")("We find that de-staggering the board creates wealth and that shareholder activism is an important catalyst for pushing through this change."); Olubunmi Faleye, Classified Boards, Firm Value, and Managerial Entrenchment, J. FIN. ECON. (February 2007)("Faleye (2007)")(noting that "classified boards significantly insulate management from market discipline, thus suggesting that the observed reduction in value is due to managerial entrenchment and diminished board accountability.")).

917 See Bebchuk and Hirst (2010); Bebchuk and Cohen (2005).

918 See Proposing Release, Section V.B.3. (citing Cernich (2009)). Moreover, as we noted in the same section of the Proposing Release, empirical evidence has indicated that the ability of significant shareholders to hold corporate managers accountable for activity that does not benefit investors may reduce agency costs and increase shareholder value. See, e.g., Brad M. Barber, "Monitoring the Monitor: Evaluating CalPERS' Activism" (November 2006), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=890321 (cited in the Proposing Release, Section V.B.3.). See also Deutsche Bank, Global Equity Research, "Beyond the Numbers: Corporate Governance in Europe," (March 5, 2005)(cited in the Proposing Release, Section V.B.3).

having an independent, active and committed board of directors.[919] Directors are charged under state law to act as disinterested fiduciaries on behalf of all shareholders, but it has been recognized that the difficult agency problem created by the separation in public companies of ownership from control creates conflicts not completely addressed by state law. We received comment expressing concern regarding the close relationships between directors and a company's management and the degree to which the nomination process is dominated by management.[920] Directors nominated by shareholders pursuant to the new rules will owe their presence on the board to their nomination by one or more significant shareholders and therefore may be independent in a way that is fundamentally different from directors nominated by the incumbent directors. We found to be relevant the empirical evidence cited in our Proposing Release and by commenters regarding the effect on shareholder value of so-called "hybrid boards" (i.e., boards composed of a majority of incumbent directors and a minority of dissident directors).[921] Such boards are a close, but not perfect, analog to the results from an election in

---

919 See Proposing Release, Section V.B.3. (citing Fitch Ratings, "Evaluating Corporate Governance" (December 12, 2007), available at http://www.fitchratings.com/corporate/reports/report_frame.cfm?rpt_id=363502).

920 See, e.g., letters from CII (noting that "some boards are dominated by the chief executive officer, who often plays the key role in selecting and nominating directors" and quoting a view expressed by a prominent investor that "[t]hese people [chief executive officers] aren't looking for Dobermans . . . . They're looking for cocker spaniels."); J. McRitchie ("It is well known that until recently the vast majority of board vacancies were filled via recommendations from CEOs who also are typically chairmen of the boards…Recent requirements for an 'independent' nominating committee provide little assurance against continued management domination. These 'independent' board members serve at the pleasure of the CEOs and the other board members; they have no independent base of power.").

921 Cernich (2009). See also letters from D. Romine; GovernanceMetrics; P. Neuhauser; Social Investment Forum; TIAA-CREF; Universities Superannuation.

As we previously noted, the Cernich (2009) study cites long-term return results, relative to peers, which are positive over the subsequent year but negative over the subsequent three years. However, these results are not reported with standard errors, making it difficult to determine whether the expected returns following contests are different from peers, or whether the realized long-term returns during the sample period are merely the result of random chance. Other research, such as Mulherin and Poulsen (1998), is consistent with these findings, but investigates the impact of proxy contests generally, rather than hybrid boards.

which shareholder nominees submitted pursuant to the new rules are elected and typically result when the shareholder's nominees join the board through an actual or threatened proxy contest, but without a change of control. In the study cited in the Proposing Release, ongoing businesses with a minority of dissident directors posted increases in shareholder value of 9.1%, relative to peers, during the contest period, indicating that the market viewed the contest as having a positive effect on shareholder value.[922] Other commenters adduce evidence that boards with a minority of dissident directors produce positive changes in corporate governance structures and strategy and result in increased shareholder value measured in both absolute returns and relative to peers.[923] Amending our proxy rules to facilitate the operation of state laws permitting shareholder nominations of directors may allow shareholders to elect directors who, without obtaining control, can exercise similar influence over decisions critical to shareholder value.

We recognize the existence of studies that reached conclusions contrary to those discussed above.[924] Other commenters warn that the new rules will lead to election contests that

---

922 Cernich (2009).

923 See letters from D. Romine; GovernanceMetrics; P. Neuhauser; Social Investment Forum; TIAA-CREF; Universities Superannuation. See also Mulherin and Poulsen (1998); James F. Cotter, Anil Shivdasani, and Marc Zenner, Do Independent Directors Enhance Target Shareholder Wealth During Tender Offers?, J. FIN. ECON. (February 1997)(finding, after examining a sample of 169 tender offers conducted from 1989 through 1992, that target shareholder gains from tender offers were approximately 20% greater when the board was independent).

924 See letter from BRT (referring to the "Report on Effects of Proposed SEC Rule 14a-11 on Efficiency, Competitiveness and Capital Formation, in Support of Comments by Business Roundtable" by NERA Economic Consulting ("NERA Report")); David Ikenberry and Josef Lakonishok, Corporate Governance Through the Proxy Contest: Evidence and Implications, 66 J. BUS. 420 (1993)("Ikenberry and Lakonishok (1993))(claiming that "companies with dissident board members substantially underperform compared to their peers.")(cited in the NERA Report); Lisa Borstadt and Thomas Zwirlein, The Efficient Monitoring Role of Proxy Contests: An Empirical Analysis of Post-Contest Control Changes and Firm Performance, FIN. MGM'T (1992)("Borstadt and Zwirlein (1992)")(asserting that, in the long run, proxy contests destroy shareholder value)(cited in NERA Report); Beltratti and Stulz (2009)(submitted as part of the letter from BRT and cited in letters from AT&T, BRT, and Seven Law Firms); Cheffins (2010)(examining thirty-seven companies removed from the S&P 500 index during 2008 and concluding that corporate governance functioned "tolerably well" in these companies to negate the need for fundamental reform of the current corporate governance arrangements)(submitted as part of the letter from Chamber of Commerce/CCMC); Ali C. Akyol, Wei Fen Lim and Patrick Verwijmeren, Shareholders in the Boardroom: Wealth Effects of

will be distracting, time-consuming, and inefficient for companies, boards, and management.[925]

We have reviewed these studies and have reason to question some of their conclusions either because of questions raised by subsequent studies,[926] limitations acknowledged by the studies' authors,[927] or our own concerns about the studies' methodology or scope.[928] While we

---

the SEC's Rule to Facilitate Director Nominations (December 14, 2009)("Akyol, Lim, and Verwijmeren (2009)")(documenting negative stock price reactions to the announcements of regulatory activities related to shareholders' right to include director nominees in the company's proxy materials, including the Proposal)(submitted as part of the letter from J. Grundfest); David F. Larcker, Gaizka Ormazabal and Daniel J. Taylor, The Regulation of Corporate Governance (January 16, 2010))("Larcker, Ormazabal, and Taylor (2010)")(submitted as part of the letter from David F. Larcker ("D. Larcker")).

925 See letters from ABA; Atlas; AT&T; Book Celler; Carlson; Carolina Mills; Chamber of Commerce/CCMC; Chevron; Crespin; M. Eng; Erickson; ExxonMobil; Fenwick; GE; General Mills; Glass Lewis; Glaspell; Intelect; R. Clark King; Koppers; MCO; MeadWestvaco; MedFaxx; Medical Insurance; Merchants Terminal; D. Merilatt; NAM; NIRI; NK; O3 Strategies; Roppe; Rosen; Safeway; Sara Lee; Schneider; Southland; Style Crest; Tenet; TI; tw telecom; R. VanEngelenhoven; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

926 For example, we note that a study highlighted a methodological flaw in the Ikenberry and Lakonishok (1993) study. Mulherin and Poulsen (1998) noted that this study had required that companies exist as the same entity in the COMPUSTAT database subsequent to the contest, eliminating some of the most favorable outcomes of proxy contests from consideration and biasing the estimate of long-term returns downward. After making corrections for this statistical bias and examining a sample of 270 proxy contests for board seats conducted from 1979 to 1994, the authors found that the market had a favorable response to the initiation of the proxy contest with an average abnormal return of 8.04% in the initiation period, followed by long-run returns statistically indistinguishable from those of comparable stocks. Their analysis showed that the wealth gains during proxy contests stemmed mainly from firms that were acquired. Overall, the authors concluded that proxy contests generally create value, and for companies that were not acquired, "the occurrence of management turnover [had] a significant, positive effect on shareholder wealth relative to the firms that do not replace senior management." In the Borstadt and Zwirlein (1992) study, the finding of a negative risk-adjusted return, conditional on dissidents winning, was based on a sample of 32 firms. Borstadt and Zwirlein note that, overall, "dissident activity leads to gains for shareholders and is often followed by corporate reforms... such that the realized gains over the contest period appear to be permanent." A survey article on corporate governance confirmed that this is the current academic consensus, stating that "[t]he latest evidence suggests that proxy fights provide a degree of managerial disciplining and enhance shareholder value." See Marco Becht, Patrick Bolton and Ailsa Roell, Corporate Governance and Control, HANDBOOK OF THE ECONOMICS OF FINANCE (2003)("Becht, Bolton and Roell (2003)").

927 For example, we believe that attempts to draw sharp inferences from the Beltratti and Stulz (2009) study may not be warranted because, as the authors themselves noted, the evidence leaves much to interpretation. The authors concluded that negative conclusions about board effectiveness may be unwarranted because it is unfair to evaluate ex-ante decisions using hind-sight. In particular, they explained that:

> Such a result does not mean that good governance is bad. Rather it is consistent with the view that banks that were pushed by their boards to maximize shareholder wealth before the crisis took risks that were understood to create shareholder wealth, but were costly ex post because of outcomes that were not expected when the risks were taken.

recognize that there are strongly-held views on every side of this debate, we believe that, as discussed throughout this release and supported by commenters' views and empirical data, we have a reasonable basis for expecting the benefits described above.

We are aware, of course, that the new rules are additive to many existing means of monitoring and "disciplining" a company's board and management,[929] which include: hostile takeovers; stockholders "voting with their feet" by selling their shares; board members being replaced by other means when the company's stock performance is poor; and management turnover following poor performance or wrongdoing.[930]

We acknowledge these alternatives, but believe that, for the reasons noted above, directors nominated pursuant to the new rules will have a degree of independence that is not present in the existing means of "disciplining" a company's board and management. Moreover, the ability of shareholders to "vote with their feet" or submit to a takeover bid may be unattractive from a shareholder's perspective if those transactions occur after a period of weak management that has depressed the company's share price. Further, shareholders who invest in

---

Beltratti and Stulz (2009) at 3.

928 For example, the relatively short timeframe and small number of companies examined in Cheffins (2010) study alone justify some caution in attempting to draw any sharp inferences from the study. As for the Akyol, Lim, and Verwijmeren (2009) and Larcker, Ormazabal, and Taylor (2010) studies, we note that, even if facilitating shareholders' ability to include their nominees in a company's proxy materials enhances shareholder value, it may be possible to observe negative stock price reactions for a particular set of public announcement dates. The problem lies in ascertaining the first time investors learned about the regulatory efforts to facilitate this shareholder right. On that initial date, investors may have adjusted share prices for both the capitalized value of the benefits (or costs) associated with the regulatory effort and the probability of the effort's success. Subsequent public announcements may simply cause investors to update these initial assessments of the valuation impact and the probability of success. Consequently, it is difficult to infer whether the price reactions are independent of past announcements or simply a revision of the investors' prior expectations. It is important, therefore, to disentangle investor expectations about the probability of the success of the regulatory effort from the associated valuation implications. It appears that the Akyol, Lim, and Verwijmeren (2009) and Larcker, Ormazabal, and Taylor (2010) studies did not focus on this distinction.

929 See NERA Report.

930 Id.

indices may not be readily able to sell securities of a particular company that is part of the index, making it difficult for them to "vote with their feet." The high costs involved with other existing mechanisms for "management discipline," such as a traditional proxy contest, often mean that the prospect of replacing incumbent directors is remote unless the company's performance falls below a very low threshold. By that time, a significant amount of shareholder value will have, by hypothesis, already been lost and will require additional time to recoup. We believe that the new rules will help shareholders exert "management discipline" by reducing the cost of, and otherwise making more plausible, shareholder nominations.

We also acknowledge concerns expressed by commenters that the Proposal would encourage boards to make decisions to improve results in the short-term at the expense of long-term shareholder value creation.[931] For the reasons described above, we believe the new rules have the potential to lead to improved company performance and enhanced shareholder value for both short-term and long-term shareholders. Evidence suggests that, historically, proxy contests have created value in both the short-run and long-run for shareholders.[932] The possible inclusion and potential election of shareholder director nominees in company proxy materials would not negate the board's fiduciary obligations, which are to all shareholders. Finally, shareholder director nominees are subject to election by both long-term and short-term shareholders, who will express their interest through their vote. In sum, we do not expect that the prospect that such holders would nominate directors should lead boards to take short-term actions that would detract from long-term value in order to avoid nominations.

A number of commenters expressed special concerns with respect to the Proposal's effect on investment companies, asserting that the election of a shareholder director nominee may, in

931 See, e.g., letters from BRT; GE; General Mills; IBM; Metlife; Office Depot; Safeway; Wachtell.

932 See Mulherin and Poulsen (1998) and discussion in footnote 926 above.

some circumstances, increase costs and potentially decrease the effectiveness and efficiency of a unitary or cluster board utilized by a fund complex.[933] Some of these commenters noted their belief that investment company governance presents a special case, arguing that the rules should not be extended to them absent empirical evidence specifically related to boards in this industry.[934] Commenters also argued that investment companies are subject to a unique regulatory regime under the Investment Company Act that provides additional protection to investors, such as the requirement to obtain shareholder approval to engage in certain transactions or activities, and that investment companies and their boards have very different functions from non-investment companies and their boards.[935] We understand these concerns, but we also note that some commenters have raised governance concerns regarding the relationship between boards and investment advisers.[936] Moreover, although investment companies and their boards may have different functions from non-investment companies and their boards, investment company boards, like the boards of other companies, have significant responsibilities in protecting shareholder interests, such as the approval of advisory contracts and fees.[937] We also do not believe that the regulatory protections offered by the Investment Company Act (including requirements to obtain shareholder approval to engage in certain transactions and activities) serve to decrease the importance of the rights that are granted to

933 See, e.g., letters from ABA; ICI; ICI/IDC; IDC; MFDF; S&C; T. Rowe Price; Vanguard.

934 See letters from ICI; ICI/IDC; S&C; T. Rowe Price.

935 See letters from ABA; Barclays; ICI; ICI/IDC; IDC; T. Rowe Price; S&C; Vanguard.

936 See letters from J. Reid; J. Taub.

937 See Jones v. Harris Assocs., 130 S.Ct. 1418, 1423, 176 L. Ed. 2d 265, 273-274 (2010). See also S. Rep. No. 91-184; 91st Congress 1st Session; S. 2224 (1969) ("This section is not intended to authorize a court to substitute its business judgment for that of the mutual fund's board of directors in the area of management fees. . . . The directors of a mutual fund, like directors of any other corporation will continue to have . . . overall fiduciary duties as directors for the supervision of all of the affairs of the fund.").

shareholders under state law. In fact, the separate regulatory regime to which investment companies are subject emphasizes the importance of investment company directors in dealing with the conflicts of interest created by the external management structure of most investment companies.[938]

Lastly, improved board performance may result from the possible increase in the pool of qualified director candidates. When a company does not include shareholder nominees for director in its proxy materials, it loses the opportunity to increase the pool of qualified nominees. Further, it deprives shareholders of the opportunity to consider and assess all qualified candidates if asked to make an informed voting decision in director elections. As we stated in the Proposing Release, facilitating shareholders' ability to include director nominations in a company's proxy materials may result in a larger pool of qualified director nominees from which to choose.[939] By allowing shareholders to submit their own director nominees for inclusion in the company's proxy materials, the demand for qualified individuals who may be willing to serve as shareholder-nominated directors also may increase. This increased demand may, in turn, encourage more individuals to present themselves as potential shareholder director nominees, resulting in a large pool of potential candidates. We recognize, however, this benefit may be offset by the possibility that some qualified individuals may be less willing to be nominated to serve on a board if faced with a contested election.[940]

4. More Informed Voting Decisions in Director Elections Due to Improved Disclosure of Shareholder Director Nominations and Enhanced Shareholder Communications

---

938 See footnote 142 above.

939 See Proposing Release, Section V.B.3.

940 For a more detailed discussion, see Section IV.E.1. below.

There was widespread support among commenters for the principle that the Commission should require disclosures regarding nominating shareholders and their nominees.[941] The new requirements in Rule 14a-11, Rule 14n-1, and Schedule 14N will require certain disclosures and certifications to be provided on Schedule 14N by shareholders who submit a nominee under Rule 14a-11. A nominating shareholder or group will be required to provide disclosure of the information similar to that currently required in a proxy contest regarding the nominating shareholder and nominee[942] as well as certain certifications required for use of Rule 14a-11.[943] Rule 14a-18, Rule 14n-1 and Schedule 14N will require similar disclosures when a shareholder or group uses an applicable state or foreign law provision or company's governing documents to include shareholder nominees for director in the company's proxy materials. The information provided by the disclosures and certifications will help provide transparency to shareholders when voting on shareholder nominees for director and therefore may lead to better informed voting decisions.

With respect to Rule 14a-8(i)(8), companies previously have been permitted to exclude shareholder proposals to establish procedures for including shareholder director nominees in the

---

941 See letters from ABA; Alston & Bird; Americans for Financial Reform; CalSTRS; CFA Institute; CII; Corporate Library; Dominican Sisters of Hope; Florida State Board of Administration; GovernanceMetrics; ICI; Mercy Investment Program; Protective; RiskMetrics; Sisters of Mercy; Tri-State Coalition; Ursuline Sisters of Tildonk; USPE; Walden.

942 Among the information included in Schedule 14N is the disclosure required by Items 4(b), 5(b), 7 and, for investment companies, Item 22(b) of Schedule 14A. This disclosure is the same disclosure required for a solicitation subject to Exchange Act Rule 14a-12(c).

943 Item 8 of Schedule 14N. These certifications include: a certification that the nominating shareholder (or where there is a nominating shareholder group, each member of the nominating shareholder group) is not holding any of the company's securities with the purpose, or with the effect, of changing control of the company or to gain a number of seats on the board that exceeds the maximum number of nominees that the company could be required to include under Rule 14a-11; a certification that the nominating shareholder or group satisfies the applicable eligibility requirements of Rule 14a-11; a certification that the shareholder director nominee satisfies the applicable eligibility requirements of Rule 14a-11; and a certification that the information set forth in the notice on Schedule 14N is true, complete, and correct.

company's proxy materials. This exclusion arose out of the concern that allowing such proposals would result in the occurrence of contested elections without the disclosure that otherwise would be required in a traditional proxy contest.[944] The new disclosure requirements applicable to nominations made pursuant to state or foreign law or a company's governing documents address that concern by mandating disclosure that is similar to that required in a traditional proxy contest.[945]

In addition to improved disclosure, our new rules will enhance shareholders' ability to communicate with each other regarding director nominations and elections through the proxy process. Shareholders eligible to use Rule 14a-11 will be able to utilize the company's proxy materials to present their own director nominees for a vote by other shareholders. They will be able to include in the company's proxy materials a statement supporting their director nominees.[946] Shareholders who are dissatisfied with the company's existing board or the company's director nominees will be able to communicate this view and their preference for alternative candidates through the votes they cast under the proxy process.

The new solicitation exemptions also will facilitate communications between shareholders.[947] Shareholders interested in forming a nominating group to use Rule 14a-11 can contact other shareholders – through both oral and written communications – for that purpose without fear that their communications would be viewed as solicitations under the proxy rules, as

---

944 See Shareholder Proposal Proposing Release (proposing amendments to Rule 14a-8 to "make clear that director nominations made pursuant to [bylaw amendments concerning shareholder nominations of directors] would be subject to the disclosure requirements currently applicable to proxy contests" and noting that such disclosure is of "great importance" to an informed voting decision by shareholders).

945 See Rule 14a-18, Rule 14n-1, and Schedule 14N.

946 See Item 7(e) of Schedule 14A and Item 5(i) of Schedule 14N.

947 See Rules 14a-2(b)(7) and 14a-2(b)(8).

long as the exemption's conditions are satisfied.[948] If its director nominees are included in the company's proxy materials pursuant to Rule 14a-11, the nominating shareholder or group can solicit other shareholders to vote in favor of its nominees, or against the company's own nominees, as long as the exemption's conditions are satisfied.[949]

With the new amendment to Rule 14a-8(i)(8), shareholders will benefit from a greater ability to present a proposal to establish an alternative procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. Thus, shareholders will be able to present for consideration by other shareholders a director nomination procedure that they believe is appropriate for their company. Through their votes on the proposal, shareholders will then have an opportunity to communicate their views on this proposal to other shareholders and the company's management.

E. Costs

We anticipate that the new rules, where applicable, may result in costs related to (1) potential adverse effects on company and board performance; (2) additional complexity in the proxy process; and (3) preparing the required disclosures, printing and mailing, and costs of additional solicitations.

1. Costs Related to Potential Adverse Effects on Company and Board Performance

Rule 14a-11 and the amendment to Rule 14a-8(i)(8) may result in potential adverse effects on the performance of a company and its board of directors.

First, we received significant comment stating that election contests are distracting and

948 See Rule 14a-2(b)(7).

949 See Rule 14a-2(b)(8).

time-consuming for companies, boards, and management.[950] Further, to the extent that a more competitive nomination and election process motivates incumbent directors to be more responsive to shareholders' concerns, the board may incur costs in attempting to institute policies and procedures it believes will address shareholder concerns. It is possible that the time a board spends on shareholder relations could reduce the time that it otherwise would spend on strategic and long-term thinking and overseeing management, which, in turn, may negatively affect shareholder value.[951]

We considered these comments and appreciate commenters' concerns regarding these costs. We believe it is important to note that these costs are associated with the traditional state law right to nominate and elect directors, and are not costs incurred for including shareholder nominees for director in the company's proxy materials. Further, the ownership threshold and holding period that we adopted in response to commenters' concerns should limit the use of Rule 14a-11 to only holders who demonstrate a long-term, significant commitment to the company.

---

950 See letters from ABA; Atlas; AT&T; Book Celler; BRT; Carlson; Carolina Mills; Chamber of Commerce/CCMC; Chevron; Crespin; M. Eng; Erickson; ExxonMobil; Fenwick; GE; General Mills; Glass Lewis; Glaspell; Intelect; R. Clark King; Koppers; MCO; MeadWestvaco; MedFaxx; Medical Insurance; Merchants Terminal; D. Merilatt; NAM; NIRI; NK; O3 Strategies; Roppe; Rosen; Safeway; Sara Lee; Schneider; Southland; Style Crest; Tenet; TI; tw telecom; R. VanEngelenhoven; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

951 See, e.g., Akyol, Lim, and Verwijmeren (2009)(finding that, based on the market response of a sample of 1,315 firms, "the proposed rule is perceived as costly by shareholders," "that increasing shareholder rights, specifically by facilitating director nominations by shareholders, may actually be detrimental to shareholder wealth," and that "empowering shareholders is not necessarily perceived as a good thing by most shareholders."); Stout (2007)("Perhaps the most obvious [economic function of board governance] is promoting more efficient and informed business decisionmaking. It is difficult and expensive to arrange for thousands of dispersed shareholders to express their often-differing views on the best way to run the firm."); see generally Stephen M. Bainbridge, Response to Increasing Shareholder Power: Director Primacy and Shareholder Disempowerment, 119 HARV. L. REV. 1735 (2006)(discussing how concern for accountability may undermine decision-making discretion and authority)(cited in the Proposing Release, Section V.C.1.). But see Lucian Arye Bebchuk, The Case for Increasing Shareholder Power, 118 HARV. L. REV. 833, 883 (2005) ("[M]ere recognition that back-seat driving might sometimes be counter-productive is hardly sufficient to mandate general deference to management. Such mandated deference would follow only if one assumes that shareholders are so irrational or undisciplined that they cannot be trusted to decide for themselves whether deference would best serve their interests.")(cited in the Proposing Release, Section V.C.1.).

To encourage constructive dialogue between a company and a nominating shareholder or group regarding the director nominees to be presented to shareholders for a vote, we revised the rule so that if a company negotiates with the nominating shareholder or group that otherwise would be eligible to have its nominees included in the company's proxy materials after the nominating shareholder or group has submitted its nomination on Schedule 14N, and the company agrees to include the nominating shareholder's or group's nominees on the company's proxy card as company nominees, those nominees will count toward the 25% maximum set forth in the rule.[952] We believe that the cost described above may be offset by other factors as well. The additional communication between a board and the company's shareholders may lead to enhanced transparency into the board's decision-making process, more effective monitoring of this process by shareholders, and, ultimately, a better decision-making process by the board. The cost also may be offset to the extent that shareholders understand that the board's time and other resources are in scarce supply and will take these considerations into account in deciding to nominate directors, recognizing that the cost of a distracted board may not justify pursuing their own specific concerns.

Second, the new rules may lead some companies to re-examine their current procedures for shareholders to submit their own director nominees for consideration by either the company's board or nominating committee, especially if the company is subject to, or thinks it likely will be subject to, shareholder-nominated director candidates submitted pursuant to Rule 14a-11. These companies may incur costs associated with such a re-examination and any resulting adjustments to their procedures.[953] These costs may be limited, however, to the extent that the new rules

[952] See new Rule 14a-11(d)(5). For a discussion of this modification, see Section II.B.6.c. above.

[953] See, e.g., letters from Biogen; GE.

improve the overall efficiency of the director nomination process and lead to improvements in the existing procedures for director nominations.

Third, the new rules could, in some cases, result in lower quality boards.[954] The quality of a company's board may decrease if, as some commenters predicted, unqualified individuals are elected to the board.[955] Commenters worried, in particular, that a shareholder director nominee will be elected without undergoing the same extensive vetting process or having to comply with the same independence or director qualification standards applicable to other director nominees.[956] The presence of directors who lack the proper qualifications may result in a lower quality board and represent a cost to companies and shareholders. It is important to recognize that Rule 14a-11 provides for only the inclusion of a shareholder director nominee in the company's proxy materials, not the election of that nominee. Further, the new disclosure requirements contained in the Proposal will provide shareholders with information for them to assess whether a shareholder nominee possesses the necessary qualifications and experience to

---

954 See letters from 3M; ABA; American Electric Power; Atlantic Bingo; AT&T; Avis Budget; Biogen; Boeing; BRT; Burlington Northern; Callaway; Carlson; Chamber of Commerce/CCMC; CIGNA; Columbine; Cummins; CSX; J. Dillon; Emerson Electric; Erickson; ExxonMobil; FedEx; Headwaters; C. Holliday; IBM; Intelect; R. Clark King; Lange; Louisiana Agencies; Metlife; NIRI; O3 Strategies; V. Pelson; PepsiCo; Pfizer; Roppe; Rosen; Ryder; Sara Lee; Sidley Austin; tw telecom; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo. See also Stephen M. Bainbridge, A Comment on the SEC Shareholder Access Proposal (November 14, 2003) at 17, available at http://ssrn.com/abstract=470121 ("The likely effects of electing a shareholder representative therefore will not be better governance. It will be an increase in affectional conflict . . . . It will be a reduction in the trust-based relationships that causes horizontal monitoring within the board to provide effective constraints on agency costs.")(cited in the Proposing Release, Section V.C.1.).

955 See letters from AGL; Air Tite, Inc. ("Air Tite"); All Cast; John C. Astle ("J. Astle"); Astrum Solar ("Astrum"); Atlantic Bingo; Burlington Northern; Glen Burton ("G. Burton"); R. Chicko; Columbine; Darden Restaurants; Erickson; Fluharty; Horizon; Lange; Mama's; Massey Services; NIRI; O3 Strategies; P&G; PepsiCo; W. Steinbrink; Stringer; Theragenics; VCG; Wachtell; and Wells Fargo.

956 See letters from AGL; Astrum; Boeing; R. Burt; G. Burton; S. Campbell; Carolina Mills; Columbine; W. Cornwell; Erickson; Fenwick; FPL Group; Intelect; Little; McDonald's; MedFaxx; Norfolk Southern; P&G, Rosen; UnitedHealth; VCG; Wells Fargo; Xerox; Yahoo.

serve as a director.[957] Accordingly, as other commenters have noted, an unqualified individual, even if nominated, will still need to receive the support of a significant number of shareholders in order to be elected to the board.[958] Therefore, the cost arising from unqualified directors may be limited to the extent that shareholders understand that experience and competence are important director qualifications and cast their votes for the most-qualified candidates. Moreover, as adopted, the rule will require a company to include in its proxy materials no more than one shareholder director nominee or a number of nominees that represent 25% of the company's board, whichever is greater.[959] We believe that this provision will limit the effect of any potential decrease in the overall quality of a board. Lastly, to the extent that there is a risk of unqualified individuals being elected as directors, it is a risk that arises because shareholders are given the right under state or foreign law to determine who sits on the board of directors.

The quality of a board also may decrease if, as some commenters warned, the increased likelihood of a contested election discourages experienced and capable individuals from serving on boards, making it more difficult for companies to recruit qualified directors or create a board with the proper mix of experience, skills, and characteristics.[960] Some commenters noted that it is already difficult to recruit qualified independent directors.[961] Other commenters, however, did

---

957 See Rules 14a-11, 14a-18 and 14n-1, and Schedule 14N.

958 See letters from BCI; Bebchuk, et al.; CII; T. DiNapoli; Florida State Board of Administration; Governance for Owners; A. Krakovsky; P. Neuhauser; NJSIC; Relational; Shamrock; Social Investment Forum.

959 See Rule 14a-11(d)(1).

960 See letters from 3M; ABA; American Electric Power; Atlantic Bingo; AT&T; Avis Budget; Biogen; Boeing; BRT; Burlington Northern; Callaway; Carlson; Chamber of Commerce/CCMC; CIGNA; Columbine; Cummins; CSX; J. Dillon; Emerson Electric; Erickson; ExxonMobil; FedEx; Headwaters; C. Holliday; IBM; Intelect; R. Clark King; Lange; Louisiana Agencies; Metlife; NIRI; O3 Strategies; V. Pelson; PepsiCo; Pfizer; Roppe; Rosen; Ryder; Sara Lee; Sidley Austin; tw telecom; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

961 See, e.g., letters from Ameriprise; BRT; Chamber of Commerce/CCMC.

not believe that Rule 14a-11 will discourage experienced, capable directors from serving,[962] with one commenter stating that it encountered no difficulty in finding executives willing to serve on a shareholder-nominated slate.[963] To the extent that the prospect of a contested election deters an otherwise qualified individual from considering a board seat, this will represent a cost to both the company and its shareholders. This cost may be mitigated, however, by the ability of other individuals – those who would not have been considered or nominated by the incumbent directors – to be nominated and presented for a shareholder vote pursuant to Rule 14a-11 or a procedure in the company's governing documents established through Rule 14a-8. The cost may be further mitigated to the extent that the new rules lead to the election of individuals who will present a greater diversity of views for the board's consideration, thereby leading to a better decision-making process, and, ultimately, greater shareholder value.[964] Lastly, as we stated in the Proposing Release,[965] the possibility of qualified candidates being discouraged from running for a board seat may be limited by shareholders' understanding that board dynamics can be important, and that changing them may not always be beneficial.

Fourth, potential disruptions in boardroom deliberations represent another possible cost to shareholders and companies. If a shareholder director nominee is elected and disruptions or polarization in boardroom dynamics occur as a result, the disruptions may delay or impair the

---

962 See letters from Florida State Board of Administration; Pershing Square.

963 See letter from Pershing Square.

964 See letters from L. Dallas (citing Jerry Goodstein et al., The Effects of Board Size and Diversity on Strategic Change, 15 STRATEGIC MGMT. J. 241 (1994) and Lynne L. Dallas, The New Managerialism and Diversity on Corporate Boards of Directors, 76 TULANE L. REV. 1363 (2002)); LIUNA; RiskMetrics (noting that it tracked over a four-year period the returns of a portfolio of companies where activists gained board seats in 2005, found that the portfolio outperformed the S&P 500 index even during the recent market turmoil, and saw no indication that the presence of dissident directors on boards had a detrimental impact on shareholder value); Teamsters.

965 See Proposing Release, Section V.C.1.

board's decision-making process. Such boardroom disruption may occur when one or more directors seek to promote an agenda that conflicts with that of the rest of the board. We received significant comment that the presence of shareholder-nominated directors could disrupt the collegiality and efficiency of boards.[966] We recognize the view that for companies whose boards are already well-functioning, such disruption could be counterproductive and could delay the board's decision-making process and a delay or impairment in the decision-making process could constitute an indirect economic cost to shareholder value. For the reasons discussed above, however, we believe that boards with directors who were not nominated by the incumbent directors would, on balance, improve company performance and increase shareholder value.[967]

In addition, it may be possible for an investor to submit director nominees through the new rules with the intention of having the nominees, if elected, advocate for board decisions that maximize the investor's private gains but at the expense of other shareholders.[968] In the case of Rule 14a-11, the cost may be limited to the extent that the ownership threshold and holding requirement allow the use of the rule by only holders who demonstrated a significant, long-term commitment to the company. This cost may be limited to the extent that a director nominee with

---

966 See, e.g., letters from Association of Corporate Counsel; BRT; Chamber of Commerce/CCMC; GE; IBM; McDonald's; O'Melveny & Myers; P&G; PepsiCo; Seven Law Firms; Society of Corporate Secretaries (also presenting data that the average hedge fund ownership is 7.15%, the number of S&P 500 companies with hedge fund ownership at or above 5% is 273, and the number of S&P 500 companies with hedge fund ownership at or above 10% is 104); Vinson & Elkins; Wachtell; Xerox; Yahoo. See also Larcker, Ormazabal, and Taylor (2010)(stating that "the evidence suggests shareholders react negatively to regulation of proxy access, and that the reaction is decreasing in the number of large blockholders and increasing in the number of small institutional investors," and that "the market perceives that shareholders of firms with many large blockholders are harmed by proxy access and is consistent with critics' claims that large blockholders will use the privileges afforded them by proxy access regulation to manipulate the governance process to make themselves better off at the expense of other shareholders.").

967 See Section IV.D.3. above.

968 See, e.g., letters from BRT; Eaton; IBM; McDonald's; Seven Law Firms; Society of Corporate Secretaries; UnitedHealth. See also Stout (2007) at 794 ("[B]y making it easier for large shareholders in public firms to threaten directors, a more effective shareholder franchise might increase the risk of intershareholder 'rent-seeking' in public companies.").

narrow interests must still gain the support of a significant number of shareholders to be elected.[969] The disclosure requirements that we are adopting also may alert shareholders to the narrow interests of the nominating shareholder or group in advance of the election so that they can cast their votes in favor of the candidate who will best serve the interests of all shareholders.[970] The cost may be further limited to the extent that a shareholder director nominee, once elected to the board, will be subject to the same fiduciary duties applicable to all other directors.[971] The possibility of a director seeking to promote private gain at the expense of shareholders generally – and the related costs to the board's overall performance and dynamics – should be limited to the extent that such a director recognizes these duties and strives to fulfill these legal obligations. The cost also may be limited to the extent that shareholders recognize the potential harm from misuse of the board's decision-making process and therefore do not vote for the nominee if they view the cost as sufficiently high.

Fifth, to the extent that the need to comply with the new rules makes the U.S. public equity markets less attractive,[972] discourages private companies from conducting public offerings in the U.S.,[973] or encourages U.S. reporting companies to become non-reporting companies, this would be a cost of the new rules because investors' investment opportunities could be limited. This cost may be mitigated to the extent that the new rules help improve board accountability

---

969 See letters from BCIA; Bebchuk, et al.; CII; T. DiNapoli; Florida State Board of Administration; Governance for Owners; A. Krakovsky; P. Neuhauser; NJSIC; Relational; Shamrock; Social Investment Forum.

970 See Rule 14a-11, Rule 14a-18, Rule 14n-1, and Schedule 14N.

971 See letter from CII. See also Veasey & DiGuglielmo, above.

972 See letter from BRT.

973 See letters from Altman (stating that its survey of 36 public companies showed that 80.85% of respondents believe the new rules "will deter some U.S. private companies from going public and some foreign companies from listing on U.S. exchanges."); BRT; Richard Tullo ("R. Tullo").

and corporate governance, generate stronger company performance, and increase shareholder value. Investors may be more willing to invest or continue to invest in companies in which they have the ability to present their own shareholder director nominees in the company's proxy materials if they are displeased with the company's performance. We also note that shareholders in many foreign countries already have the ability to include their director nominees in the company's proxy materials.[974] We therefore believe that the new rules may bring the U.S. capital markets closer in line with international practice by giving shareholders of U.S. companies an ability that may already be enjoyed by shareholders of many non-U.S. companies.

Lastly, with respect to investment companies, a number of commenters expressed concern that the election of a shareholder director nominee may, in some circumstances, increase costs and burdens (e.g., the shareholder-nominated director would have to leave during discussions that pertain to the other investment companies in the complex, board materials would have to be customized for the director, and the fund complex would face challenges in preserving the status of privileged information) and potentially decrease the efficiency of a unitary or cluster board utilized by a fund complex.[975] We recognize that for fund complexes that utilize unitary or cluster boards, the election of a shareholder director nominee may, in some circumstances, increase costs and potentially decrease the efficiency of the boards.[976] We note, however, that these costs are associated with the traditional state law right to nominate and elect directors, and are not costs incurred for including shareholder nominees in the company's proxy materials. We also note that any increased costs and decreased efficiency of an investment company's board as

---

974 See letters from ACSI; CalPERS; ICGN; LUCRF; Pax World; RiskMetrics; Social Investment Forum; SWIB.

975 See, e.g., letters from ABA; ICI; ICI/IDC; IDC; MFDF; S&C; T. Rowe Price; Vanguard.

976 See, e.g., letters from ICI; ICI/IDC; IDC; MFDF; Vanguard.

a result of the fund complex no longer having a unitary or cluster board would occur, if at all, only in the event that the investment company shareholders elect the shareholder nominee. Investment companies may include information in the proxy materials making investors aware of the company's views on the perceived benefits of a unitary or cluster board and the potential for increased costs and decreased efficiency if the shareholder nominees are elected. Moreover, we note that a fund complex can take steps to minimize the cost and burden of a shareholder-nominated director who is elected by, for example, entering into a confidentiality agreement in order to preserve the status of confidential information regarding the fund complex.

Two commenters in a joint comment letter argued that there are a number of practical and legal issues that prevent confidentiality agreements from being sufficient to protect the interests of fund shareholders, and included a memorandum from a law firm discussing concerns about Regulation FD, enforceability of confidentiality agreements, whether shareholder-nominated directors would sign confidentiality agreements, compliance, and loss of attorney-client privilege.[977] We considered the issues raised by the joint comment letter. To the extent that material non-public information is discussed by boards in a fund complex, we emphasize that entering into a confidentiality agreement is only one method of preserving the confidentiality of information revealed in board meetings attended by the shareholder-nominated director. The fund complex can have separate meetings and board materials for the board with the shareholder-nominated director, especially if particularly sensitive legal or other matters will be discussed or to protect attorney-client privilege. Finally, we believe the concerns expressed in the memorandum about confidentiality agreements were either not compelling or speculative in nature.

---

977 See letter from ICI/IDC (including attached legal memorandum).

Although commenters argued that the election of a shareholder-nominated director to a unitary or cluster board will necessarily result in decreased effectiveness of the board, we disagree. In this regard, one commenter argued that competition in the board nomination process may improve efficiency by providing additional leverage for boards in negotiations with the investment adviser.[978] In any event, we believe that investment company shareholders should have the opportunity to exercise their traditional state law rights to elect a non-unitary or non-cluster board if they so choose.

2. Costs Related to Additional Complexity of Proxy Process

The new rules that we are adopting will, for the first time, require that company proxy materials include information about, and the ability to vote for, director nominees submitted by shareholders. The rules will facilitate shareholders' ability to exercise their traditional state law rights to nominate and elect their own director candidates. One of the costs of this newly-enhanced ability, however, is the additional complexity in the proxy process as both companies and shareholders may have to consider and address the issue of shareholder director nominations more frequently than in the past.

Several commenters expressed concern that the inability of companies and shareholders to opt out of Rule 14a-11, or establish a shareholder director nomination procedure with criteria different than those of Rule 14a-11, may create workability and implementation issues for companies, as they struggle to comply with a rule that does not fit their specific capital and governance structures.[979] One commenter, for example, identified several of these issues, such

978 See letter from J. Taub.

979 See, e.g., letters from ABA ("Workability requires that the rule or bylaw be easily understandable, be able to be readily administered, address all relevant issues, operate in a time frame that permits proper conduct of shareholder meetings and action by a fully informed shareholder body, recognize the role and fiduciary responsibility of the board of directors, comply with the requirements of the Commission's rules and other applicable law and allow the company and its shareholders sufficient flexibility to respond to changed

as: the operation of the rule in a company with multiple classes of stock, a cumulative voting standard, or a majority voting standard; the treatment of derivatives and other synthetic ownership under the rule; the need for adequate protection against use of the rule for change of control attempts; and the consequences of false certifications by a nominating shareholder or group.[980] We recognize the possibility that attempting to comply with a highly-complex rule without the necessary flexibility to adapt the rule to a company's specific situation may create certain costs for companies, such as the cost of legal advice and possible litigation if uncertainties must be resolved in courts. We also recognize the possibility that shareholders may have to incur similar costs if they attempt to use a highly-complex and unclear rule.

The requirements of Rule 14a-11, such as the eligibility criteria, may add a certain degree of complexity in the proxy process. For example, the process of determining which shareholder director nominee will be in the company's proxy materials and the limitations on the number of shareholder nominees for director that a company is required to include in its proxy materials may add complexity. If several shareholders or groups desire (and qualify) to nominate the maximum number of directors they are allowed to place in the company's proxy materials, only the shareholder or group holding the largest qualifying ownership interest will succeed. Another potential source of complexity under Rule 14a-11 is the number of shareholder director nominees that a nominating shareholder or group may submit to a company during a particular proxy season. For example, if the maximum allowable number of shareholder director nominees currently serves on the board, a company will not be required to include additional shareholder director nominees in the company's proxy materials. These sources of complexity and any

---

circumstances in a timely manner."); Keller Group; Wachtell.

980 See letter from Wachtell.

uncertainty that may arise in implementing the new rules could result in costs to companies, shareholders seeking to have their nominees included in the companies' proxy materials, and shareholder director nominees. For example, both companies and shareholders could incur costs to seek legal advice in connection with shareholder nominations submitted pursuant to Rule 14a-11, the inclusion of shareholder director nominees in a company's proxy materials, submission of a notice of intent to exclude a nominee or nominees, and the process set forth in the rule for seeking an informal statement of the staff's views with respect to the company's determination to exclude a shareholder director nominee. Companies and shareholders also could incur costs to seek legal advice in connection with shareholder proposals submitted pursuant to Rule 14a-8 and the process for submission of a no-action request to exclude the proposal. To the extent disputes on whether to include particular nominees or proposals are not resolved between the company and shareholders, companies and/or shareholders may seek recourse in courts, which will increase costs.

As discussed throughout the release, the rules we are adopting include modifications to the proposed rules. We believe that the modifications will help minimize the complexity of the new rules and clarify uncertainties as much as possible. For example, our decision to adopt a uniform ownership threshold instead of the proposed tiered approach simplifies this particular eligibility requirement and should reduce some of the uncertainties identified by a commenter.[981] We also clarified the availability of Rule 14a-11 when there is a concurrent proxy contest,[982] provided standards for the order of priority of shareholder director nominees upon the

[981] See letter from Shearman & Sterling (opposing the tiered ownership thresholds because a number of companies regularly move from one category of filer to another as the aggregate worldwide market value of their voting and non-voting common equity changes from fiscal year to fiscal year, which it believed would lead to uncertainty).

[982] See Section II.B.2.e. above.

withdrawal or disqualification of another shareholder director nominee,[983] addressed issues regarding the application of Rule 14a-11 to certain corporate structures (such as staggered boards and different classes of voting securities),[984] and adopted a uniform deadline for the submission of shareholder director nominations pursuant to Rule 14a-11 that is generally applicable to companies subject to the rule.[985] The costs arising from any complexity or uncertainty arising from the new rules may be mitigated to the extent that companies and shareholders gain greater familiarity with the new rules over time,[986] additional guidance is provided by the Commission or its staff,[987] and, if necessary, uncertain legal issues are resolved by courts.

Lastly, as discussed above, we believe the overall proxy solicitation process for contested director elections may be less confusing for shareholders as a result of our new rules.[988] Presenting the competing director nominees on one proxy card, with the related disclosure contained in one proxy statement, may simplify the shareholder's decision-making process, reduce the potential for any confusion on the part of shareholders, and address any reluctance on the part of shareholders to consider an insurgent shareholder's nominee solely because the nominee was not presented in the company's proxy materials.

3. Costs Related to Preparing Disclosure, Printing and Mailing and Costs of Additional Solicitations and Shareholder Proposals

---

983 See Section II.B.7.b. above.

984 See Sections II.B.4.b. and II.B.6.a. above.

985 See Section II.B.8.c.ii. above.

986 See letter from CII.

987 For example, we are adopting, as proposed, a procedure by which companies could send a notice to the Commission where the company intends not to include a shareholder director nominee in its proxy materials and could seek informal staff views – through a no-action request – with respect to that determination.

988 See Section IV.D.1. above.

The new rules will impose additional direct costs on companies and shareholders related to the preparation of required disclosure, printing and mailing costs, and costs of additional solicitations that may be undertaken as a result of including one or more shareholder nominees for director in the company's proxy materials pursuant to Rule 14a-11, a company's governing documents, or an applicable state or foreign law provision.[989]

First, the new rules will impose direct costs onto companies and shareholders due to the rules' disclosure and procedural requirements. For example, companies that determine that they may exclude a shareholder director nominee pursuant to Rule 14a-11 will be required to provide a notice to the nominating shareholder or group regarding any eligibility or procedural deficiencies in the nomination and provide to the Commission notice of the basis for its determination.[990] Companies also may incur costs in preparing any statements regarding the shareholder director nominees that they wish to include in their proxy materials. Nominating shareholders or groups and the nominees also will be required to disclose information about themselves, which may be costly.[991] Most of this disclosure will be provided by the nominating shareholder or group in the notice to the company, which would be filed on new Schedule 14N. The Schedule 14N also will include information regarding the length of ownership, certifications, and other information. Companies could incur additional costs to investigate or verify the information regarding shareholder director nominees provided by nominating shareholders or groups, determine whether nominations will conflict with any laws, and analyze

---

989 We note that these increased costs may be less for companies using the notice and access model. See Internet Proxy Availability Release.

990 For purposes of the PRA analysis, we estimate these disclosure requirements would result in 225 burden hours of company time, and $30,000 for the services of outside professionals.

991 For purposes of the PRA analysis, we estimate the total burden for Schedule 14N for shareholders submitting nominees pursuant to Rule 14a-11 would result in a total of 7,870 hours of shareholder time and $1,049,300 for the services of outside professionals.

the relative merits of the shareholder director nominees and the companies' own director nominees.[992] For purposes of the PRA analysis, we estimate that the disclosure burden of Rule 14a-11 on reporting companies (other than registered investment companies) and registered investment companies is 4,113 hours of personnel time and $548,200 for the services of outside professionals. We also estimate for purposes of the PRA analysis that the disclosure burden to shareholders of Schedule 14N will be 7,870 hours of shareholder time and $1,049,300 for the services of outside professionals. We also received estimates from commenters regarding the costs described above.[993] These estimates are described in the PRA analysis above.[994]

Companies also could incur costs due to the potential increase in the number of shareholder proposals submitted to companies as a result of the expansion in the types of proposals permitted under Rule 14a-8. Under the amendment to Rule 14a-8(i)(8), companies will no longer be able to rely on this basis to exclude from their proxy materials shareholder proposals that seek to establish a procedure in the company's governing documents for the inclusion of shareholder nominees for director in the company's proxy materials. This will likely result in increased costs to companies related to reviewing and processing such proposals to determine matters such as shareholder eligibility and whether there is another basis for excluding these proposals under Rule 14a-8. If a company decides to exclude the shareholder proposal, it will have to incur the costs, such as legal fees, needed to prepare and submit a notice to the Commission regarding its basis for excluding the proposal. In this regard, we received several estimates from commenters regarding the costs related to a Rule 14a-8 shareholder

---

992 See, e.g., letter from S&C.

993 See letters from BRT; Society of Corporate Secretaries.

994 See Section III.C. above, for discussion of the estimates included in the letters from BRT and Society of Corporate Secretaries.

proposal. Based on its July 2009 survey of its member companies, one commenter stated that companies spend an estimated 47 hours and associated costs of $47,784 to prepare and submit a notice of intent to exclude a shareholder proposal.[995] An investment company estimated that its costs for including a shareholder proposal in its complex-wide proxy materials exceeded $3 million in "tabulation expenses."[996] One commenter, however, described the costs to companies resulting from the amendment to Rule 14a-8(i)(8) as "negligible" (with such costs confined to any additional costs of printing and distributing the proposal in the company's proxy materials).[997] For purposes of the PRA analysis, we estimate that shareholders will submit a total of 147 proposals regarding procedures for the inclusion of shareholder nominees in company proxy materials per year to reporting companies, including registered investment companies. Assuming that 90% of reporting companies (including registered investment companies), or 132 companies, prepare and submit a notice of intent to exclude these proposals, the resulting costs to companies will result in approximately 11,484 hours and $1,531,200 for the services of outside professionals.[998] These costs could decrease to the extent that the Rule 14a-8 no-action process

---

995 See letter from BRT.

996 See letter from Vanguard. The commenter did not elaborate on the nature of these "tabulation expenses." It also noted that this figure does not include "incremental printing and mailing costs because the proposal was included in the proxy statement and did not require a separate mailing."

997 See letter from CII.

998 This estimate is based on the assumption that shareholders of reporting companies (other than registered investment companies) will submit approximately 123 proposals per year regarding procedures for inclusion of shareholder nominees for director in company's proxy materials, and that 90% of companies that receive such a shareholder proposal will seek to exclude the proposal from their proxy materials. Thus, we estimate that companies will seek to exclude 110 such proposals (123 proposals x 90%) per proxy season. We estimate that the annual burden for the company's submission of a notice of its intent to exclude the proposal and its reasons for doing so would average 116 hours per proposal, for a total of 12,760 burden hours (110 proposals x 116 hours/proposal) for reporting companies (other than registered investment companies). This will correspond to 9,570 hours of company time (110 proposals x 116 hours/proposal x 0.75) and $1,276,000 for the services of outside professionals (110 proposals x 116 hours/proposal x 0.25 x $400). For registered investment companies, we estimate for purposes of the PRA that the total burden hours will be 2,552 hours, which corresponds to 1,914 hours of company time and $255,200 for the services of outside professionals. See Section III.D.2. above.

provides guidance from the staff on which types of proposals are excludable. Further, because a company that receives a shareholder proposal has no obligation to make a submission under Rule 14a-8 unless it intends to exclude the proposal from its proxy materials, these costs also may decrease to the extent that the company does not seek to exclude the proposal. Lastly, the costs may be limited to the extent that shareholders do not submit proposals related to director nomination procedures due to the uniform applicability of Rule 14a-11 to all companies subject to the rule and availability of the rule for eligible shareholders.[999]

Second, the new rules may increase the incremental costs of printing and mailing a company's proxy materials due to the need to include additional names and background information of shareholder director nominees in the proxy materials and the increased weight of these materials. These costs may increase as the number of shareholder director nominees to be included in the company's proxy materials increases. Thus, this may result in a decrease in the costs to shareholders that would have had to conduct traditional proxy contests in the absence of Rule 14a-11, but may increase the costs for companies.[1000]

Companies also will incur additional printing and mailing costs with respect to the inclusion of a shareholder proposal related to changes to a company's governing documents regarding inclusion of shareholder director nominees in the company's proxy materials. We have two sources of information estimating such costs. Based on its July 2009 survey of its member companies, one commenter stated that companies spend an estimated 20 hours and associated costs of $18,982 to print and mail one shareholder proposal.[1001] The responses to a

---

999 As discussed in Section II.B.3. above, Rule 14a-11 will not apply to certain types of companies.

1000 However, as explained in footnote 875 above, the increased costs for the company may not be as much as would otherwise result if the shareholders engaged in a traditional proxy contest.

1001 See letter from BRT. This cost is in addition to the estimated 47 hours and associated costs of $47,784 that companies spend to prepare and submit a notice of intent to exclude a shareholder proposal.

questionnaire that the Commission made available in 1997 relating to 1998 amendments to Rule 14a-8 suggest such costs to the responding companies averaged $50,000.[1002] As noted above, for purposes of the PRA, we estimate that the amendment to Rule 14a-8(i)(8) could result in the annual submission of 147 shareholder proposals regarding procedures for the inclusion of shareholder director nominees in company proxy materials. Based on this information, for purposes of our analysis, we assume printing and mailing costs of one shareholder proposal in a company's proxy materials could be in the range of approximately $18,000 to $50,000. Assuming each of these proposals were included in company proxy materials, it could result in a total cost of approximately $2,646,00 to $7,350,00 for the affected companies.

Finally, the new rules may lead to an increase in soliciting activities by both companies and shareholders. Companies may increase solicitations to vote for their slate of directors, to vote against shareholder director nominees, or to vote against shareholder proposals. Shareholders may increase solicitations to vote for shareholder proposals, to withhold votes for a company's nominees for director, or to vote for the shareholder director nominees. This increase in soliciting activities by both companies and shareholders will result in an increase in costs as well. These solicitation costs are not, however, required under our rules.

We received a significant amount of comment regarding the extent to which companies will solicit against the election of a shareholder director nominee. One commenter predicted that boards will take "extraordinary efforts" to campaign against the shareholder director nominees, including significant media and public relations efforts, advertising in a number of forums, mass

1002 In the adopting release for the amendments to Rule 14a-8 in 1998, we noted that responses to a questionnaire we made available in February 1997 suggested the average cost spent on printing costs (plus any directly related costs, such as additional postage and tabulation expenses) to include shareholder proposals in company proxy materials was approximately $50,000. The responses received may have accounted for the printing of more than one proposal.

mailings, and other communication efforts, as well as the hiring of outside advisors and the expenditure of significant time and effort by the company's employees.[1003] As examples of these costs, the commenter pointed to the costs of recent proxy contests, which ranged from $14 million to $4 million, as well as the costs of contests at smaller companies, which ranged from $3 million to $800,000. Another commenter conducted a survey of its member companies and indicated that an average total of 302 hours of company personnel and director time will be needed if a company opposes a shareholder director nominee.[1004] One commenter estimated its own annual costs for defending against a shareholder director nominee to be approximately $330,000 and 275 hours of management's time.[1005] Another commenter noted that it had direct costs of approximately $11 million in 2008 and more than $9 million in 2009 – in addition to the substantial indirect costs in management time and attention – as a result of the proxy contests that it faced.[1006]

We understand that company boards may be motivated by the issues at stake to expend significant resources to challenge shareholder director nominees, elect their own nominees, or solicit votes against a shareholder proposal. We therefore recognize that, as a practical matter, it can reasonably be expected that the boards of some companies likely would oppose the election of shareholder director nominees. If the incumbent board members incur large expenditures to defeat shareholder director nominees, those expenditures will represent a cost to the company and, indirectly, all shareholders. It is also possible that some shareholders may perceive the use of corporate funds to oppose the election of nominees submitted by shareholders as having a

---

1003 See letter from Chamber of Commerce/CCMC.

1004 See letter from BRT.

1005 See letter from Ryder.

1006 See letter from Biogen.

negative effect on the value of their investments.

These costs, however, may be limited by two factors. They may be limited to the extent that the directors' fiduciary duties prevent them from using corporate funds to resist shareholder director nominations for no good-faith corporate purpose.[1007] Some commenters, in fact, characterized the costs incurred by incumbent directors to defeat shareholder director nominees as discretionary because Rule 14a-11 itself does not require such efforts.[1008] Other commenters disagreed with this characterization, asserting that the directors' fiduciary duties may compel them to expend company resources to oppose a shareholder director nominee.[1009] We recognize that, under certain circumstances, company directors likely would oppose a particular shareholder director nominee and expend company resources in that effort, which would increase the costs to the company resulting from Rule 14a-11.[1010] However, the costs for companies may be less to the extent that directors determine not to expend such resources to oppose the election of the shareholder director nominees and simply include the shareholder director nominees and the related disclosure in the company's proxy materials.[1011] The requisite ownership threshold

1007 See Hall v. Trans-Lux Daylight Picture Screen Corp., 171 A. 226, 228 (Del. Ch. 1934)("where reasonable expenditures are in the interest of an intelligent exercise of judgment on the part of the stockholders upon policies to be pursued, the expenditures are proper; but where the expenditures are solely in the personal interest of the directors to maintain themselves in office, expenditures made in their campaign for proxies are not proper.").

1008 See letters from CalSTRS; CII; Florida State Board of Administration.

1009 See letters from ABA; BRT.

1010 The Commission is not expressing a view as to the scope of directors' state law fiduciary duties in responding to shareholder director nominations or expressing a view as to what conduct would be consistent with these duties.

1011 For example, the costs that are incurred only if the incumbent directors choose to challenge or solicit against a shareholder director nominee (e.g., the legal fees arising from the company's efforts to exclude the nominee from its proxy materials) are distinguishable from the costs that must be incurred irrespective of whether the directors oppose the shareholder director nomination (e.g., the increased printing costs caused by the inclusion of the shareholder director nominees and related disclosures in the company's proxy materials).

and holding period of Rule 14a-11 may also limit the number of shareholder director nominations that a board may receive, consider, and possibly contest.

4. Other Costs

The new rules may result in additional costs, as described below.

With respect to investment companies, one commenter stated that if a shareholder nomination causes an election to be "contested" under rules of the New York Stock Exchange, brokers would not be able to vote client shares on a discretionary basis, making it difficult and more expensive for investment companies to achieve a quorum for a meeting.[1012] We recognize that it may be more costly for investment companies to achieve a quorum at shareholder meetings if a shareholder director nomination causes an election to be "contested" under the rules of the New York Stock Exchange and brokers cannot vote shares on a discretionary basis. We believe, however, that the costs imposed on investment companies will be limited for three reasons. First, to the extent investment companies do not hold annual meetings as permitted by state law, investment company shareholders will have less opportunity to take advantage of the new rules.[1013] Second, even when investment company shareholders do have the opportunity to take advantage of the new rules, the disproportionately large and generally passive retail shareholder base of investment companies suggests that the new rules will be used less frequently than will be the case with non-investment companies.[1014] Third, because we have sought to limit the cost and burden on all companies, including investment companies, by limiting Rule 14a-11 to nominations by shareholders who have maintained significant

---

1012 See letter from S&C. NYSE Rule 452 provides that, with respect to registered investment companies, brokers may not vote uninstructed shares in contested elections.

1013 See letters from ABA; MFDF.

1014 See letter from J. Taub.

continuous holdings in the company for at least three years, and because, as suggested by one commenter, many funds, such as money market funds, are held by shareholders on a short-term basis,[1015] we believe that the situations where shareholders will meet the eligibility requirements will be limited.

Our decision to adopt, as proposed, the revisions to Rule 14a-6(a)(4) and Note 3 to the rule[1016] means that the inclusion of a shareholder director nominee in the company's proxy materials will not require the company to file preliminary proxy materials, provided that the company was otherwise qualified to file directly in definitive form. Because the proxy materials will not be filed in preliminary form, the Commission staff may not have the opportunity to review these proxy materials before companies make definitive copies available to shareholders. Staff review of preliminary materials can benefit shareholders by helping to assure that companies comply with the federal proxy rules and provide appropriate disclosure to shareholders. We believe, however, that any cost related to the staff's inability to review preliminary proxy materials is mitigated by the staff's ability to review the disclosure contained in the Schedule 14N as well as in any additional soliciting materials filed by either the company or the nominating shareholder or group. Further, as we recently stated, the staff retains the right to comment on proxy materials filed in definitive form if the staff deems that to be appropriate under the circumstances.[1017]

V. CONSIDERATION OF BURDEN ON COMPETITION AND PROMOTION OF

1015 See letter from ABA.

1016 The revisions make clear that inclusion of a shareholder director nominee would not be deemed a solicitation in opposition for purposes of the exclusion from filing preliminary proxy materials.

1017 See Shareholder Approval of Executive Compensation of TARP Recipients, Exchange Act Release No. 34-61335 (Jan. 12, 2010)(adopting an amendment to Exchange Act Rule 14a-6(a) to add the shareholder advisory vote on executive compensation required for participants in the Troubled Asset Relief Program ("TARP") to the list of items that do not trigger a preliminary filing requirement).

EFFICIENCY, COMPETITION AND CAPITAL FORMATION

Section 23(a)(2) of the Exchange Act[1018] requires us, when adopting rules under the Exchange Act, to consider the impact that any new rule would have on competition. In addition, Section 23(a)(2) prohibits us from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act. Section 3(f) of the Exchange Act[1019] and Section 2(c) of the Investment Company Act[1020] require us, when engaging in rulemaking that requires us to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation.

We are adopting new rules that will, under certain circumstances, require that company proxy materials include information about, and the ability to vote for, director nominees submitted by shareholders. The rules will facilitate the exercise of shareholders' rights to nominate and elect directors and provide shareholders with information about a nominating shareholder or group and its nominees for director. Rule 14a-11 will provide for the inclusion of shareholder nominees for director in the company's proxy materials under certain circumstances and disclosure regarding the nominating shareholder or group and nominees submitted pursuant to the rule. The amendment to Rule 14a-8(i)(8) will provide an avenue for shareholders to submit proposals that would seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. No longer permitting companies to exclude these types of proposals pursuant to

---

1018 15 U.S.C. 78w(a)(2).

1019 15 U.S.C. 78c(f).

1020 15 U.S.C. 80a-2(c).

Rule 14a-8(i)(8) should enable shareholders to better reflect their preferences for director nomination procedures that would further facilitate their ability to nominate and elect their own director candidates. In addition, the new rules require disclosure of information regarding nominating shareholders or groups and any nominees submitted pursuant to an applicable state or foreign law provision or a company's governing documents, which provides shareholders a more informed basis for deciding how to vote for nominees for election to the board of directors.

We requested comment on whether the new rules will promote efficiency, competition and capital formation or have an impact or burden on competition. We received a number of comments that addressed this section. The comments we received, and our consideration of those comments, are discussed below.

The analysis below is based on our understanding that while no state currently prohibits shareholders from nominating candidates for the board of directors,[1021] shareholders generally do not have a right under existing state law to require a company to include their director nominees in the company's proxy materials.[1022]

We expect that the new rules will promote efficiency in the capital markets in a number of ways. First, we have already considered extensively the expected costs and benefits of the new rules in the Cost-Benefit Analysis and throughout the release. As we believe the benefits (including the possible benefit of improved board accountability and company performance) justify the costs, we expect the new rules to promote efficiency of the economy on the whole.

1021 We are not aware of any law in any state or in the District of Columbia that prohibits shareholders from nominating directors. For further discussion, see Section II.B.2.a. above.

1022 One notable exception exists under the North Dakota Publicly Traded Corporations Act, which permits holders of at least five percent of the outstanding shares of a company subject to the statute to submit a notice of intent to nominate directors and requires the company to include each such shareholder nominee in its proxy statement and form of proxy. See North Dakota Publicly Traded Corporations Act, N.D. Cent. Code §10-35-08 (2009).

We believe the new rules will promote efficiency by reducing several different types of costs that previously discouraged potentially beneficial actions. The new rules will reduce the cost of shareholders' exercise of their rights to nominate and elect directors.[1023] To the extent that facilitating shareholders' ability to nominate and elect directors of their own choosing is expected to produce the economic benefits for investors described elsewhere in this release, the new rules will bring about these benefits at a reduced cost and thereby promote efficiency. Some commenters asserted that although the new rules may relieve certain shareholders of costs that they are unwilling to incur to run a traditional short-slate election contest, those costs will simply be shifted onto the company and indirectly borne by all shareholders.[1024] This burden may be justified, however, because these costs may not be as much as would otherwise result if that shareholder engaged in a traditional proxy contest,[1025] resulting in a reduction in the overall cost of changing a limited percentage of a board's membership. The burden may be further justified because the new rules may mitigate any collective action concerns.[1026]

The new rules also will promote efficiency by reducing the cost of administering informed shareholder voting – to the extent that a shareholder director nominee is submitted for inclusion in a company's proxy materials pursuant to Rule 14a-11, a company's governing

1023 Many commenters noted the general ineffectiveness or prohibitive cost of the existing means to effect a change in the membership of a board, such as a traditional proxy contest, Rule 14a-8 shareholder proposals, and communications with a company's nominating committee or board. See letters from Americans for Financial Reform; Brigham; CalPERS; CII; Florida State Board of Administration; Ironfire; M. Katz; J. McRitchie; Nathan Cummings Foundation; P. Neuhauser; Pax World; S. Ranzini; Teamsters; TIAA-CREF; USPE. Moreover, only a traditional proxy contest was viewed by some commenters to be a realistic method of effecting change in the board's membership. See letters from Americans for Financial Reform; CalPERS; CII; Florida State Board of Administration; M. Katz; J. McRitchie; S. Ranzini; Teamsters. Yet, according to these commenters, the high costs of such a proxy contest hinder shareholders' ability to nominate and elect directors. For further discussion of these costs, see Section IV.C.1. above.

1024 See letter from ABA.

1025 See Bainbridge 2003 Letter.

1026 See Section IV.D.1. above.

documents, or a state or foreign law provision – by providing for director nominees to be included on one proxy card with clear disclosure[1027] for shareholders to evaluate when deciding whether and how to grant authority to vote their shares by proxy, as opposed to having to evaluate more than one set of proxy materials sent by a company and an insurgent shareholder.[1028] Presenting the competing director nominees on one proxy card, with the related disclosure contained in one proxy statement, may simplify the shareholder's decision-making process, reduce the potential for any confusion on the part of shareholders, and address any reluctance on the part of shareholders to consider an insurgent shareholder's nominee solely because the nominee was not presented in the company's proxy materials.[1029]

The new rules could promote efficiency by reducing the cost of effective communication between shareholders and directors, potentially resulting in enhanced board responsiveness and accountability as described elsewhere in the release.[1030] Such communications may, in some cases, address the concerns that prompted the shareholders to submit their own director nominations and help avert any distracting election contests.[1031] Enhanced communication with shareholders also may result in better decision-making by the board as shareholders may provide

---

[1027] It is assumed here that the private cost of making the required disclosure and the cost to the company for including the disclosure in the company's proxy materials is lower than the total information cost for voting shareholders.

[1028] As discussed in footnote 884 above, we do not believe that our recent adoption of rules enhancing proxy solicitation disclosure dispenses with the need for Rule 14a-11 and the amendment to Rule 14a-8(i)(8).

[1029] See Section IV.D.1. above.

[1030] See letters from AFSCME; Bebchuk, et al.; Brigham; CalPERS; CII; L. Dallas; T. DiNapoli; A. Dral; GovernanceMetrics; Governance for Owners; Hermes; M. Katz; LUCRF; J. McRitchie; R. Moulton-Ely; D. Nappier; P. Neuhauser; NJSIC; OPERS; Pax World; Pershing Square; Relational; RiskMetrics; D. Romine; Shareowners.org; Social Investment Forum; Teamsters; TIAA-CREF; Universities Superannuation; USPE; Walden. According to these commenters, the prospect of an election contest may create greater incentives for incumbent directors to communicate with shareholders, address their concerns, and consider shareholders' preferences regarding nominations for director.

[1031] We have changed certain provisions of Rule 14a-11 from their proposed form to further encourage communication between boards and shareholders. See, e.g., Rule 14a-11(d)(5).

the board with new ideas or information that the board has not considered.

We considered potential negative effects of the new rules on the efficiency of U.S. public companies, as discussed below.

As discussed elsewhere in the release, if the number of election contests increases as a result of the new rules, boards may end up devoting less time to overseeing their companies' business operations. Election contests have been described by many commenters as distracting, time-consuming, and inefficient for companies, boards, and management.[1032] To the extent that a board's attention is drawn away by the demands of election contests or shareholders, the new rules may impair companies' ability to compete efficiently. To limit the use of Rule 14a-11 to only holders who demonstrate a significant, long-term commitment to the company, we adopted a uniform 3% ownership threshold and three-year holding period. We also continue to believe that this concern may be mitigated to the extent that shareholders, while voicing their concerns and seeking the board's attention, understand the board's time may be in scarce supply and take this factor into consideration when deciding to nominate director candidates.[1033]

The efficiency of U.S. public companies could be negatively affected if shareholders use the new rules to promote their narrow interests at the expense of other shareholders.[1034] If the

---

1032 See, e.g., letters from ABA; Atlas; AT&T; Book Celler; Carlson; Carolina Mills; Chamber of Commerce/CCMC; Chevron; Crespin; M. Eng; Erickson; ExxonMobil; Fenwick; GE; General Mills; Glass Lewis; Glaspell; Intelect; R. Clark King; Koppers; MCO; MeadWestvaco; MedFaxx; Medical Insurance; Merchants Terminal; D. Merilatt; NAM; NIRI; NK; O3 Strategies; Roppe; Rosen; Safeway; Sara Lee; Schneider; Southland; Style Crest; Tenet; TI; tw telecom; R. VanEngelenhoven; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

1033 See Proposing Release, Section V.C.1.

1034 See, e.g., letters from 3M; ACE; AGL; Alaska Air; Alcoa; Allstate; American Bankers Association; American Business Conference; American Express; Ameriprise; Artistic Land Designs; Association of Corporate Counsel; J. Astle; Astrum; Atlantic Bingo; Avis Budget; J. Blanchard, Board Institute; Boeing; Boston Scientific; Brink's; BRT; Burlington Northern; Callaway; S. Campbell; Cargill; Carpet and Tile ("Carpet and Tile"); Caterpillar; Chamber of Commerce/CCMC; Kevin F. Clune ("K. Clune"); P. Clapman; Chevron; J. Chico; CIGNA; CNH Global; Columbine; Competitive Enterprise Institute; A. Conte; W. Cornwell; Crown Battery; Cummins; Darden Restaurants; Data Forms, Inc. ("Data Forms");

new rules facilitate the ability of shareholders with narrow interests to place directors on the board, the new rules may impair efficiency by increasing the cost of board deliberations and resulting in companies taking actions that benefit only a few shareholders. This negative effect, however, could be limited to the extent that the disclosure requirements related to Rule 14a-11 alert shareholders to the narrow interests of the nominating shareholder or group in advance of the election so that they can cast their votes in favor of the candidate who will best serve the interests of all shareholders.[1035] Directors with potentially narrow interests also will be subject to the same fiduciary duties as directors nominated by the company.[1036]

The increased likelihood of a contested election may discourage some qualified candidates from running for a board seat, making it more difficult for companies to recruit qualified directors and negatively affecting the efficiency of U.S. public companies.[1037]

Deere; T. Dermody; Dewey; A. Dickerson; W. B. Dickerson; J. Dillon; Eaton; Emerson Electric; A. England; Engledow; Mike Emis ("M. Emis"); FedEx; FMC Corp.; FPL Group; Frontier; GE; General Mills; Healthcare Practice; Home Depot; Honeywell; Horizon; Karen L. Hubbard ("K. Hubbard"); IBM; ICI; Instrument Piping Tech; Theodore S. Jablonski ("T. Jablonski"); Keating Muething; Koppers; C. Leadbetter; Leggett; Little; Louisiana Agencies; ITT; Leggett; Brittany D. Lunceford ("B. Lunceford"); Melvin Maltz ("M. Maltz"); Massey Services; J. McCoy; McDonald's; D. McDonald; MCO; McTague; MeadWestvaco; MedFaxx; D. Merilatt; Metlife; M. Metz; J. Miller; E. Mitchell; Moore Brothers; Motorola; MT Glass; NAM; NIRI; Norfolk Southern; O'Melveny & Myers; Office Depot; Omaha Door; P&G; V. Pelson; PepsiCo; Pinch a Penny ("Pinch a Penny"); Protective; Realogy; J. Rosen; RTW; Ryder; S&C; Safeway; Sara Lee; R. Saul; Schneider; Seven Law Firms; Sidley Austin; Southern Company; Southern Services; M. Sposato; Ralph Strangis ("R. Strangis"); Tenet; Tesoro; E. Tremaine; tw telecom; L. Tyson; UnitedHealth; U.S. Bancorp; VCG; Vinson & Elkins; Wachtell; Wagner Industries; Wells Fargo; Weyerhaeuser; Xerox; Yahoo. One commenter added that many recent election contests were directed towards achieving short-term financial objectives, including proposals to sell the company or effect a buyback or special dividend. See letter from Simpson Thacher.

1035 See Rule 14a-11, Rule 14a-18, Rule 14n-1, and Schedule 14N.

1036 Veasey & DiGuglielmo, at 774 ("Directors will generally be responsible for protecting the best interests of the corporation and all its stockholders, despite the directors' designation by some particular constituency, because fiduciary duties generally will trump contractual expectations in the corporate context."). See also letters from ACSI; LUCRF (indicating that they are unaware of any breaches of fiduciary or statutory duties, including Regulation FD, by shareholder-nominated directors in jurisdictions that allow shareholder director nominations in the company's proxy materials).

1037 See letters from 3M; ABA; American Electric Power; Atlantic Bingo; AT&T; Avis Budget; Biogen; Boeing; BRT; Burlington Northern; Callaway; Carlson; Chamber of Commerce/CCMC; CIGNA; Columbine; Cummins; CSX; J. Dillon; Emerson Electric; Erickson; ExxonMobil; FedEx; Headwaters; C.

Nevertheless, as discussed elsewhere in the release, a countervailing effect that the new rules may have is the impact on the labor market for director candidates and potential increase in the demand for individuals who can serve as shareholder director nominees.[1038]

Finally, compliance with the new rules may impose additional financial costs on companies, such as for legal services, printing and mailing of proxy materials, and additional proxy solicitation efforts.[1039] The workability and implementation issues identified by commenters, in particular, may force companies to incur significant time and funds to resolve.[1040] Increased litigation costs also represent a possible negative effect of the new rules, as companies and nominating shareholders or groups expend resources to resolve legal disputes in federal and state courts. Incurring such costs could negatively affect the efficiency of the capital markets. As discussed throughout the release, we have modified several aspects of the rules we proposed to clarify any uncertainties identified by commenters and to address workability issues. We also have taken steps to address commenters' concerns regarding a company's liability for misrepresentations or omissions in the nominating shareholder's or group's information that is repeated in the company's proxy materials.[1041] As described above, we have made modifications

---

Holliday; IBM; Intelect; R. Clark King; Lange; Louisiana Agencies; Metlife; NIRI; O3 Strategies; V. Pelson; PepsiCo; Pfizer; Roppe; Rosen; Ryder; Sara Lee; Sidley Austin; tw telecom; Wachtell; Wells Fargo; Weyerhaeuser; Yahoo.

1038 See Section IV.D.3. above.

1039 For a discussion of these costs, see Section IV.E.3. above.

1040 See, e.g., letters from ABA; Wachtell.

1041 See letters from ABA; Alaska Air; American Bankers Association; Ameriprise; BorgWarner; BRT; Caterpillar; Cleary; DTE Energy; ExxonMobil; Honeywell; ICI; Protective; S. Quinlivan; Seven Law Firms; Sidley Austin; Society of Corporate Secretaries; Southern Company; UnitedHealth; Verizon.

As originally proposed, under Rule 14a-11(e) and Note to Rule 14a-19, a company would not be responsible for information that is provided by the nominating shareholder or group under Rule 14a-11, an applicable state law provision, or the company's governing documents and then repeated by the company in its proxy statement, except where the company "knows or has reason to know that the information is to clarify that a company will not be liable for materially false or misleading information provided by the nominating shareholder or group.[1042] Finally, additional guidance from the Commission, its staff, or courts should further resolve any uncertainties regarding the new rules' implementation and may reduce the need for parties to resort to litigation.

With respect to investment companies, a number of commenters expressed concern that the election of a shareholder director nominee may, in some circumstances, decrease the effectiveness and efficiency of a unitary or cluster board utilized by a fund complex.[1043] In addition, one commenter noted that small investment companies are likely to be particularly affected by the Proposal and its attendant costs, including the loss of the benefits of a cluster or unitary board.[1044] According to the commenter, "the expected smaller rate of return on capital may dissuade some entrepreneurs from entering the investment company industry, and force the exit of some fund advisers with thin profit margins," negatively affecting both efficiency and competition.

We recognize that for fund complexes that utilize unitary or cluster boards, the election of a shareholder director nominee may, in some circumstances, increase costs and potentially decrease the efficiency of the boards.[1045] We note, however, that any decrease in efficiency and competition is associated with the state law right to nominate and elect directors, and not from including shareholder nominees in the company's proxy materials. We also note that any decreased efficiency of an investment company's board, or any decrease in competition, as a

false or misleading."

1042 For further discussion, see Section II.E. above.

1043 See, e.g., letters from ABA; ICI; ICI/IDC; IDC; MFDF; S&C; T. Rowe Price; Vanguard.

1044 See letter from ICI.

1045 See, e.g., letters from ICI; ICI/IDC; IDC; MFDF; Vanguard.

result of the fund complex no longer having a unitary or cluster board would occur, if at all, only in the event that investment company shareholders elect the shareholder nominee. Investment companies may include information in the proxy materials making investors aware of the company's views on the perceived benefits of a unitary or cluster board and the potential for increased costs and decreased efficiency if the shareholder nominees are elected. Furthermore, we believe that exempting small investment companies from the new rules would not be appropriate because doing so would interfere with achieving the goal of facilitating shareholders' ability to participate more meaningfully in the nomination and election of directors and to promote the exercise of shareholders' traditional state law rights to nominate and elect directors.[1046] Although commenters argued that the election of a shareholder-nominated director to a unitary or cluster board will necessarily result in decreased effectiveness of the board, we disagree. In this regard, one commenter argued that competition in the board nomination process may improve efficiency by providing additional leverage for boards in negotiations with the investment adviser.[1047] In any event, we believe that investment company shareholders should have the opportunity to exercise their traditional state law rights to elect a non-unitary or non-cluster board if they so choose.

We considered the possible effects that the new rules may have on competition, as discussed below.

With the possible effect of improved board accountability and corporate governance, the new rules may ultimately increase shareholder value, generate stronger company performance, and increase competition. Investors also may be more willing to invest in companies in which

1046 For a specific discussion of the impact of the rule on small companies and the alternatives we considered in lieu of applying the rule to such entities, see Section VI. below.

1047 See letter from J. Taub.

they have the ability to present their own shareholder director nominees in the company's proxy materials if they become displeased with the company's performance. Nevertheless, it is possible that some companies may be more reluctant to conduct public offerings in the U.S. or may wish to avoid being a reporting company due to the need to comply with new rules, making the U.S. public equity markets less attractive.[1048] Companies may instead attempt to raise capital through private placements or in foreign equity markets instead of through public offerings in the U.S. equity markets. We note that shareholders in many foreign countries already have the ability to include their director nominees in the company's proxy materials.[1049] We therefore believe that the new rules may bring the U.S. capital markets closer in line with international practice by giving shareholders of U.S. companies an ability that may already be enjoyed by shareholders of many non-U.S. companies. Lastly, we note that the new rules will not apply to foreign private issuers because they are exempt from the Commission's proxy rules.[1050] Therefore, we do not believe that the new rules will affect the willingness of such issuers to raise capital in the U.S. capital markets.

We also believe that directors nominated by shareholders pursuant to the new rules and elected to the board may be more inclined to exercise independent judgment in the boardroom due to the fact that they were nominated by shareholders, not the incumbent directors. The impact of these shareholder-nominated directors may lead to greater competition when the board considers strategic alternatives, including in the market for corporate control. Board members

---

1048 See letters from Altman (stating that its survey of 36 public companies showed that 80.85% of respondents believe the new rules "will deter some U.S. private companies from going public and some foreign companies from listing on U.S. exchanges."); BRT; R. Tullo.

1049 See letters from ACSI; CalPERS; ICGN; LUCRF; Pax World; RiskMetrics; Social Investment Forum; SWIB.

1050 Exchange Act Rule 3a12-3 exempts securities of certain foreign issuers from Section 14(a) of the Exchange Act.

play a key role in evaluating corporate control transactions and, while the new rules are not intended to facilitate a change in control, shareholder-nominated directors may not share the same bias as incumbent directors regarding a transaction that may be contrary to their interests but beneficial for shareholders. The presence of these directors, therefore, may lead to increased competition in the market for corporate control. We recognize that since the number of shareholder director nominees that a company is required to include in its proxy materials pursuant to Rule 14a-11 is limited, the potential effect on competition for corporate control may also be limited.

Lastly, the requirement that a nominating shareholder or member of the nominating shareholder group using Rule 14a-11 provide proof of ownership in the form of written statements with respect to securities held on deposit with a clearing agency acting as a securities depository may affect the competitive position of brokers or banks that are not securities depository participants.[1051] Due to the need for a nominating shareholder or member of a nominating shareholder group to obtain a separate written statement from a broker or bank that is not a clearing agency participant (e.g., when a broker or bank of the nominating shareholder or member of the nominating shareholder group holds shares of the shareholder or member in an omnibus account at another broker or bank), it is possible that some shareholders may prefer to hold their securities directly through a clearing agency participant to avoid having to obtain more than one written statement to prove their ownership of the requisite amount of securities. If so, the competitive positions of clearing agency participants and clearing agencies themselves in the marketplace may be enhanced. Their competitive position also may be enhanced if a nominating shareholder is reluctant to change its broker or bank because it would need to obtain a written statement from each broker or bank with respect to the shares that it is using to meet the

1051 See Instruction 4 to new Schedule 14N.

ownership threshold and specify the time period during which the shares were held.

We considered the possible effects that the new rules may have on capital formation, as discussed below.

We expect that potential investors may be more willing to invest in a company if they have greater confidence in the abilities of the company's board members. The new rules allow for a more competitive election process – one in which shareholders will have the opportunity to evaluate qualified alternatives to the board's own nominees and select the person that they feel is most qualified. To the extent that the overall quality of a company's board increases as a result of a more competitive election, the company's ability to attract the necessary capital in the marketplace may be enhanced as well.

Further, potential investors may be more willing to invest in a company if they know that they have a meaningful way to nominate directors for election. The new rules will facilitate investors' ability to nominate and elect director candidates, and may thereby have the effect of holding boards more accountable. Investors may also be attracted to the potential increase in shareholder value that may result from an increased ability to replace directors and enhancement of shareholders' rights.[1052] Lastly, potential investors could prefer to invest in companies with boards that they feel are more open and responsive to their views.

By enabling greater board accountability to shareholders, the new rules also may contribute to restoring investor confidence in the U.S. markets and address any reluctance to invest in U.S. companies.[1053] Companies attempting to raise capital in the U.S. markets may

---

1052 See Section IV.D.3. above.

1053 See, e.g., letters from AFSCME and Sodali (noting a June 2009 survey of investors conducted by ShareOwners.org that indicated 57% of the respondents feel strong federal action would "restore their lost confidence in the fairness of the markets" and 81% of the respondents identified "overpaid CEOs and/or unresponsive management and boards" as the top reason for the loss of investor confidence in the markets); letter from Universities Superannuation (noting that "Governance Metrics International now ranks the therefore encounter greater willingness on the part of potential investors to participate in their securities offerings.[1054]

As part of our rulemaking process, we considered possible alternatives to the new rules that may serve the same function – and to the same degree – of promoting efficiency, competition, and capital formation. In this regard, we received significant comment that the rules are unnecessary in light of recent corporate governance reforms that already increased the accountability of boards to shareholders.[1055] While each of these reforms may enhance to some degree the boards' accountability and responsiveness to shareholders or shareholders' ability to effect change in the board's membership, we believe they may not be as efficient, effective, or optimal as the new rules. Our consideration of recent corporate governance reforms and suggested alternatives are discussed throughout the release.

We recognize the passage of recent amendments to state corporation laws to enable companies to provide in their governing documents an ability for shareholders to include their director nominees in the company's proxy materials, and that private ordering is an alternative to

---

United States behind Britain, Australia, Canada, and Ireland in corporate governance quality" and that "the CFA Institute 2009 Financial Market Integrity Index survey of investment professionals found a marked decline over the past year in global sentiment of investment professionals toward the United States, with only 43 percent of non-U.S. respondents reporting they would recommend investing in the United States (based solely on ethical behavior and regulation of capital market systems), down from 67 percent a year earlier.").

1054 See letter from Universities Superannuation.

1055 See letters from 26 Corporate Secretaries; 3M; Advance Auto Parts; Allstate; Avis Budget; American Express; Anadarko; Association of Corporate Counsel; AT&T; L. Behr; Best Buy; Boeing; BRT; R. Burt; California Bar; S. Campbell; Carlson; Caterpillar; Chamber of Commerce/CCMC; Chevron; CIGNA; W. Cornwell; CSX; Cummins; Davis Polk; Dewey; DuPont; Eaton; M. Eng; FedEx; FMC Corp.; FPL Group; Frontier; GE; General Mills; C. Holliday; Honeywell; C. Horner; IBM; Jones Day; Keating Muething; J. Kilts; R. Clark King; N. Lautenbach; MeadWestvaco; Metlife; Motorola; O'Melveny & Myers; Office Depot; Pfizer; Protective; S&C; Safeway; Sara Lee; Shearman & Sterling; Sherwin-Williams; Sidley Austin; Simpson Thacher; Tesoro; Textron; TI; G. Tooker; UnitedHealth; Unitrin; U.S. Bancorp; Wachtell; Wells Fargo; West Chicago Chamber; Weyerhaeuser; Xerox; Yahoo.

our new rules.[1056] However, as discussed throughout the release, we have reason to believe that reliance on private ordering under state law would be insufficient to meet our goal of facilitating the exercise of shareholders' traditional state law rights to nominate and elect directors.[1057] For example, companies, particularly those that have performed poorly or have activist shareholders, may be reluctant to amend their governing documents to provide for an ability of shareholders to include director nominees in the company's proxy materials, even if permitted by state corporation law.[1058] In that regard, one commenter observed that most of the companies currently able to provide such an ability in their governing documents under state law have, in fact, not done so.[1059] Further, as previously discussed, establishing such an ability on a company-by-company basis may be more costly and inefficient than under our new rules.[1060] For shareholders with a diverse portfolio of securities, the administrative burden of tracking each company's requirements for including a director nominee in the company's proxy materials may add another degree of inefficiency.[1061] Some commenters also expressed concerns about the ability of

---

1056 For example, Delaware recently amended the Delaware General Corporation Law to add new Section 112 clarifying that the bylaws of a Delaware corporation may provide that, if the corporation solicits proxies with respect to an election of directors, the corporation may be required to include in its solicitation materials one or more individuals nominated by a shareholder in addition to the individuals nominated by the board of directors. The obligation of the corporation to include such shareholder nominees will be subject to the procedures and conditions set forth in the bylaw adopted under Section 112. In addition, the American Bar Association's Committee on Corporate Laws has adopted similar changes to the Model Business Corporation Act. See American Bar Association, Section of Business Law, Committee on Corporate Laws Amendments to The Model Business Corporation Act Approved on Third Reading at the Committee's Meeting on December 12, 2009 (available at http://www.abanet.org/media/docs/Amendments_to_MCBA_121709.pdf).

1057 See Sections II.B.2. and IV.D.2. above.

1058 See letters from CalPERS; D. Nappier; P. Neuhauser; Pershing Square; Schulte Roth & Zabel.

1059 See letter from TIAA-CREF. Further, based on its survey of its member companies, one commenter stated that a large majority – approximately two-thirds – would seek to opt out of Rule 14a-11, if possible. See letter from Society of Corporate Secretaries.

1060 See letters from CalPERS; D. Nappier; P. Neuhauser.

1061 See letter from CII.

shareholders to adopt a provision in a company's governing documents for the inclusion of shareholder director nominees through the Rule 14a-8 process due to the rule's requirements (such as the 500-word limit on shareholder proposals)[1062] or procedural requirements for shareholder-proposed bylaw amendments, such as a super-majority voting requirement for adoption of amendments.[1063]

We considered the recent amendments to state corporation laws to enable a company to include in its governing documents a provision for reimbursement of a shareholder's proxy solicitation costs.[1064] We note, however, that poorly-performing companies may be reluctant to include such a provision, forcing shareholders to undergo the potentially costly and time-consuming process of establishing such a provision themselves (for example, through a Rule 14a-8 shareholder proposal). Even if reimbursement arrangements were to exist at all public companies, we believe that the ability of shareholders to be reimbursed for their proxy solicitation costs may be less efficient in facilitating changes in the board or increasing board accountability or responsiveness because shareholders would still need funds to maintain an election contest.[1065] This may create a disparity among shareholders as shareholders with greater resources are able to take advantage of the right and conduct a proxy contest (with the knowledge they will be reimbursed) while those who lack such resources are unable to do so.

1062 Id.

1063 See letter from CII (stating that, based on a November 2009 white paper commissioned by the CII and ShareOwners.org, many companies have supermajority voting requirements to amend the bylaws, thereby "making shareholder-proposed bylaw amendments nearly impossible to implement").

1064 Delaware also added new Section 113 of the Delaware General Corporation Law, which allows a Delaware corporation's bylaws to include a provision that the corporation, under certain circumstances, will reimburse a shareholder for the expenses incurred in soliciting proxies in connection with an election of directors.

1065 See letter from Florida State Board of Administration.

We also considered the trend towards adopting a majority voting standard in director elections, which gives shareholders a greater voice in director elections and the company's corporate governance. It is important to note, however, that a majority voting standard in director elections, while increasingly common, is not yet used by all companies.[1066] Further, commenters pointed out that even with a majority voting standard, some boards have disregarded the outcome of the elections by, for example, refusing to accept the resignations of directors who failed to receive a majority vote.[1067] Further, while a majority voting standard facilitates shareholders' ability to elect candidates put forth by a company's management, it does not facilitate shareholders' ability to exercise their right to nominate candidates for director.

We considered the growing effectiveness of "withhold" or "vote no" campaigns in director elections, particularly at companies with a majority voting standard for director elections. "Withhold" or "vote no" campaigns have long been available but appear only occasionally to have resulted in a change in composition of the board or senior management.[1068] By definition, however, such campaigns lack what Rule 14a-11 facilitates, namely a direct means to include shareholder-nominated candidates for election as directors, rather than merely express disapproval of incumbent directors.[1069]

1066 See letters from CalPERS (noting that the standard has "only been adopted by 294 companies in the S&P 500 and just 734 companies out of the 3,369 companies according to the Corporate Library Board Analyst database."); TIAA-CREF (noting that "[o]nly about half of S&P 500 companies and a small minority of Russell 3000 companies have adopted this reform.").

1067 See letters from CalPERS; RiskMetrics; TIAA-CREF (noting that "[t]here are currently over 40 directors at U.S. companies who continue to serve without having received majority support."). See also City of Westland Police & Fire Ret. Sys. v. Axcelis Technologies, Inc., 2009 Del. Ch. LEXIS 173 (September 28, 2009), aff'd, 2010 Del. LEXIS 382 (Del., August 11, 2010) (finding "no credible basis" to infer wrongdoing by directors who refused to accept resignations by other directors who failed to achieve the majority vote required by board policy).

1068 See J.W. Verret, Pandora's Ballot Box, Or a Proxy with Moxie? Majority Voting, Corporate Ballot Access, and the Legend of Martin Lipton Re-Examined, 62 BUS. LAW. 1007, 1014 (2007) (reporting on one replacement of a board chairman following a withhold campaign resulting in a 43% withhold vote).

1069 See letter from AFSCME.

We considered the effect of adoption of our notice and access model for electronic delivery of proxy materials, which reduces the printing and mailing costs for shareholders' proxy solicitations. As discussed above, the notice and access model, while reducing the printing and mailing costs, does not necessarily provide the same cost savings as Rule 14a-11.[1070] Further, a shareholder may find the use of the model to be unattractive for the reasons related to its strategy for the conduct of the election contest.[1071]

Lastly, one commenter pointed out that the market already provides multiple means of "management discipline."[1072] Shareholders could express their displeasure with current management by selling their securities in the company, board members could be replaced, and managers could be removed for wrongdoing. In addition, the commenter stated that the threat of takeover attempts that management faces and higher levels of board independence suggest the success of existing means of "management discipline."

While we are aware of these means of "management discipline," we believe the relevant issue is whether investors will benefit from our new rules. Shareholders' ability to express their displeasure with current management through the sale of securities may be limited if the market for the securities is illiquid or the shareholder is constrained by its policies to invest in all companies within a given index. Replacing board members or removing managers under the current regulatory scheme is expensive and often requires considerable time during which significant shareholder value may be lost. By providing a more efficient means for shareholders

---

1070 See Section IV.D.1. above.

1071 Id.

1072 See letter from BRT (referring to the NERA Report).

with a significant, long-term stake to nominate directors, the new rules will promote competition and enable shareholders to nominate and elect directors.

Commenters also argued that it was not necessary to make investment companies subject to the new rules because they are subject to a unique regulatory regime under the Investment Company Act that provides additional protection to investors, such as the requirement to obtain shareholder approval to engage in certain transactions or activities.[1073] However, we do not believe that the regulatory protections offered by the Investment Company Act (including requirements to obtain shareholder approval to engage in certain transactions and activities) serve to decrease the importance of the rights that are granted to shareholders under state law. In fact, the separate regulatory regime to which investment companies are subject emphasizes the importance of investment company directors in dealing with the conflicts of interest created by the external management structure of most investment companies.[1074]

VI. FINAL REGULATORY FLEXIBILITY ANALYSIS

This Final Regulatory Flexibility Analysis ("FRFA") has been prepared in accordance with the Regulatory Flexibility Act.[1075] It relates to amendments to the rules and forms under the Exchange Act and the Investment Company Act that would, under certain limited circumstances, require companies to include in their proxy materials shareholder nominees for election as director. It also relates to the amendments to the rules that will prohibit companies from excluding shareholder proposals pursuant to Rule 14a-8(i)(8) that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director

---

1073 ABA; Barclays; ICI; IDC; T. Rowe Price; S&C; Vanguard.

1074 See footnote 142 above.

1075 5 U.S.C. 601.

nominees in the company's proxy materials. The amendments will require, under certain circumstances, a company's proxy materials to provide shareholders with information about, and the ability to vote for, a shareholder's, or group of shareholders', nominees for director. The amendments will facilitate the exercise of shareholders' traditional state law rights to nominate and elect directors to boards of directors and thereby enable shareholders to participate more meaningfully in the nomination and election of directors at the companies in which they invest.

A. Need for the Amendments

As described in this release and the Proposing Release, the final rules include features from the proposals on this topic in 2003 and 2007, and reflect much of what we learned through the public comment that the Commission has received concerning this topic over the past seven years. The final rules are intended to facilitate shareholders' ability to participate more meaningfully in the nomination and election of directors, to promote the exercise of shareholders' traditional state law rights to nominate and elect directors, to open up communication between a company and its shareholders, and to provide shareholders with more information to make an informed voting decision by requiring disclosure about a nominating shareholder or group and its nominee or nominees. In particular, the final rules will enable long-term shareholders, or groups of long-term shareholders, with significant holdings to have their nominees for director included in company proxy materials. In addition, the amendment to Rule 14a-8(i)(8) will narrow the exclusion and will not permit companies to exclude, under Rule 14a-8(i)(8), shareholder proposals that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials.

The final rules are intended to achieve the stated objectives without unduly burdening companies. We sought to limit the cost and burden on companies by limiting Rule 14a-11 to nominations by shareholders who have maintained a significant continuous ownership interest in the company for at least three years at the time the notice of nomination is submitted, and by limiting the number of nominees a company is required to include in its proxy materials under Rule 14a-11. These aspects of the final rules will limit the number of nominees a company will be required to consider for inclusion in its proxy materials and thus will lower the cost to companies while facilitating the exercise of shareholders' traditional state law rights to nominate and elect directors to boards of directors, thereby enabling shareholders to participate more meaningfully in the nomination and election of directors at the companies in which they invest. We believe the new rules will benefit shareholders by improving corporate suffrage, the disclosure provided in connection with proxy solicitations, and communication between shareholders through the proxy process.

The final rules include a phase-in period that delays the compliance date for Rule 14a-11 for smaller reporting companies, which include most small entities, for three years from the effective date of the rule for other companies.[1076] We believe the delayed compliance date will allow those companies to observe how the rule operates for other companies and may allow them to better prepare for the implementation of the rules. We also believe that delayed implementation for these companies will provide us with the opportunity to evaluate the implementation of Rule 14a-11 by larger companies and to consider whether adjustments to the rule would be appropriate for smaller reporting companies before the rule becomes applicable to

---

1076 For purposes of this FRFA, we are required to consider the impact of our rules on small entities, including "small business." See footnote 1088 and the related discussion. The new rules will have a delayed effective date for smaller reporting companies as defined in Exchange Act Rule 12b-2. Whether a company is a small business is determined based on a company's assets while the determination of whether a company is a smaller reporting company is generally based on a company's public float. We expect that most small businesses that would be subject to the new rules also would qualify as smaller reporting companies.

them.[1077] In addition, in an effort to limit the cost and burden on all companies subject to the rule, including smaller reporting companies, we have limited use of Rule 14a-11 to nominations by shareholders who have maintained significant continuous holdings in the company, and we have extended the required holding period to at least three years at the time the notice of nomination is filed with the Commission and transmitted to the company. We expect that these eligibility requirements will help achieve the stated objective without unduly burdening any particular group of companies.

B. Significant Issues Raised by Public Comments

In the Proposing Release, we requested comment on any aspect of the Initial Regulatory Flexibility Act Analysis ("IRFA"), including the number of small entities that would be affected by the proposed rules, the nature of the impact, how to quantify the number of small entities that would be affected, and how to quantify the impact of the proposed rules. We also considered, and sought comment on, excluding from operation of the rule smaller reporting companies either permanently or on a temporary basis through staggered compliance dates based on company size. We did not receive comments specifically addressing the IRFA. Several commenters, however, addressed aspects of the proposed rules that could potentially affect small entities.

In particular, many commenters stated generally that Rule 14a-11 should not apply to small businesses.[1078] Some commenters argued that the Proposal, if adopted, would hurt their

[1077] As discussed in Section II.B.3. above, the recent Dodd-Frank Wall Street Reform and Consumer Protection Act provided the Commission with exemptive authority with respect to rules permitting the inclusion of shareholder director nominations in company proxy materials. In doing so, Congress noted that the Commission shall take into account whether any such requirement to permit inclusion of shareholder nominees for director in company proxy materials would disproportionately burden small issuers.

[1078] See letters from ABA; American Mailing; All Cast; Always N Bloom; American Carpets; J. Arquilla; B. Armburst; Artistic Land Designs; C. Atkins; Book Celler; K. Bostwick; Brighter Day Painting; Colletti; Commercial Concepts; Complete Home Inspection; D. Courtney; S. Crawford; Crespin; Don's; T. Ebreo; M. Eng; eWareness; Evans; Fluharty; Flutterby; Fortuna Italian Restaurant; Future Form; Glaspell; C.

larger corporate suppliers which would, in turn, increase their own costs of doing business.[1079] Two commenters recommended that Rule 14a-11 exclude companies that are not at least accelerated filers and be limited, at least initially, to large accelerated filers.[1080] These commenters expressed concern about the burden Rule 14a-11 would place on smaller companies, including difficulty in recruiting qualified directors and costs of conducting due diligence on shareholder nominees.[1081] One commenter noted that small investment companies, which may operate with thin profit margins, would be particularly affected by the Proposal and its attendant costs, including the loss of the benefits of a cluster or unitary board.[1082] By contrast, some commenters stated that Rule 14a-11 should apply to small businesses.[1083] At least one commenter argued that Rule 14a-11 would not impose a material burden on any company subject to the proxy rules because companies already have to distribute proxy cards and it would not be

---

Gregory; Healthcare Practice; B. Henderson; S. Henning; J. Herren; A. Iriarte; J. Jones; Juz Kidz; Kernan; LMS Wine; T. Luna; Mansfield Children's Center; D. McDonald; Meister; Merchants Terminal; Middendorf; Mingo; Moore Brothers; Mouton; D. Mozack; Ms. Dee; G. Napolitano; NK; H. Olson; PESC; Pioneer Heating & Air Conditioning; RC; RTW; D. Sapp; SBB; SGIA; P. Sicilia; Slycers Sandwich Shop; Southern Services; Steele Group; Sylvron; Theragenics; E. Tremaine; Wagner; Wagner Industries; Wellness; West End; Y.M.; J. Young.

1079 See letters from Always N Bloom; Brighter Day Painting; Caswells; Complete Home Inspection; Darrell's Automotive; Data Forms; Fluharty; E. Garcia; S. Henning; T. Luna; Magnolia; American Mailing; H. Olson; T. Roper; Solar Systems; E. Sprenkle; Steele Group; R. Trummel; T. Trummel; V. Trummel; Wagner; T. White.

1080 See letters from ABA; Theragenics.

1081 In this regard, one commenter suggested that our estimate of the burden to companies of evaluating a shareholder nominee's background to determine eligibility, investigation and verification of information provided by the nominee, research into the nominee's background, analysis of the relative merits of the shareholder nominee as compared to management's own nominee, meetings of the relevant board committees, and analysis of whether a nomination would conflict with any federal or state law, or director qualification standards was too low. This commenter estimated that the burden hours associated with the above actions would be 99 hours of company personnel time. See letter from S&C (citing results of a survey conducted by BRT). For a discussion of burden estimates, see Section III. above.

1082 See letter from ICI.

1083 See letters from AFSCME; CII; D. Nappier.

an imposition if they were required to add additional nominees to those cards.[1084] Another commenter argued that exempting small entities would be inconsistent with the stated goals of the Proposal and the costs and burden to such entities would be minimal.[1085]

We believe that exempting small companies, including small investment companies, from the new rules would not be appropriate because doing so would interfere with achieving the goal of facilitating shareholders' ability to participate more meaningfully in the nomination and election of directors, to promote the exercise of shareholders' rights to nominate and elect directors, to open up communication between a company and its shareholders and to provide shareholders with better information from which to make an informed voting decision. Some commenters noted that small companies are "just as likely" to have dysfunctional boards as their larger counterparts.[1086] Also, one commenter agreed that exempting small entities would be inconsistent with the stated goals of the Proposal and the costs and burdens to these entities would be minimal.[1087] However, we are cognizant of the fact that the new rules will increase the burden on all companies and therefore the potential burden on smaller reporting companies as defined in Rule 12b-2 under the Exchange Act. To address concerns about the potential impact on smaller reporting companies, the final rule delays the compliance date for Rule 14a-11 for smaller reporting companies for a period of three years from the effective date of the rule for other companies so that smaller reporting companies can observe how the rule operates and allow them to better prepare for the implementation of the rules. We also believe that delayed implementation for these companies will allow us to evaluate the implementation of Rule 14a-11

1084 See letter from USPE.

1085 See letter from CII.

1086 See letters from AFSCME; D. Nappier.

1087 See letter from CII.

by larger companies and provide us with the additional opportunity to consider whether adjustments to the rule would be appropriate for smaller reporting companies before the rule becomes applicable to them. In addition, in an effort to limit the cost and burden on all companies subject to the rule, including smaller reporting companies, we have limited use of Rule 14a-11 to nominations by shareholders who have maintained significant continuous holdings in the company, and we have extended the required holding period to at least three years at the time the notice of nomination is filed with the Commission and transmitted to the company. We expect that these eligibility requirements will help achieve the stated objective without unduly burdening any particular group of companies.

C. Small Entities Subject to the Rules

The final rules will affect some companies that are small entities. The Regulatory Flexibility Act defines "small entity" to mean "small business," "small organization," or "small governmental jurisdiction."[1088] The Commission's rules define "small business" and "small organization" for purposes of the Regulatory Flexibility Act for each of the types of entities regulated by the Commission. Securities Act Rule 157[1089] and Exchange Act Rule 0-10(a)[1090] define a company, other than an investment company, to be a "small business" or "small organization" if it had total assets of $5 million or less on the last day of its most recent fiscal year. We estimate that there are approximately 1,209 issuers that may be considered small entities.[1091]

1088 5 U.S.C. 601(6).

1089 17 CFR 230.157.

1090 17 CFR 240.0-10(a).

1091 The estimated number of reporting small entities is based on 2009 data, including the Commission's EDGAR database and Standard & Poor's.

For purposes of the Regulatory Flexibility Act, an investment company is a small entity if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.[1092] We estimate that approximately 168 registered investment companies and 33 business development companies meet this definition. The new rules may affect each of the approximately 201 issuers that may be considered small entities, to the extent companies and shareholders take advantage of the rules.

D. Reporting, Recordkeeping and Other Compliance Requirements

The final rules are designed to require, under certain circumstances, Exchange Act reporting companies (other than debt-only companies and companies whose applicable state or foreign law provisions or governing documents prohibit shareholder nominations) subject to the federal proxy rules, including small entities, to include shareholder nominees for director in the company's proxy materials. Nominating shareholders or groups, including nominating shareholders that are small entities, will be required to meet certain eligibility requirements and to provide disclosure in Schedule 14N about the nominating shareholders and the nominee, and companies will be required to include the disclosure provided by the nominating shareholder or group in the company's proxy materials.

The final rules also will enable shareholders to include proposals in the company's proxy materials that seek to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. A nominating shareholder or group, including a nominating shareholder or group that is a small entity, using an applicable state or foreign law provision or a provision in the company's

---

1092 17 CFR 270.0-10(a).

governing documents to submit a nomination for director to be included in a company's proxy materials will be required to provide disclosure in new Schedule 14N about the nominating shareholder or group and the nominee. Companies also will be required to include disclosure about the nominating shareholder or group and the nominee in the company's proxy materials when a shareholder submits a nomination for director for inclusion in the company's proxy materials pursuant to an applicable state or foreign law provision or a company's governing documents.

We have no reason to expect that the amendment to Rule 14a-8(i)(8) will substantially increase the number of shareholder proposals to smaller companies and likely will have little impact on small entities. With respect to Rule 14a-11, there is some data indicating that smaller companies are subject to more proxy contests as a group than larger companies,[1093] but the data do not demonstrate that the frequency is disproportionately larger at smaller companies relative to other companies. In addition, we did not receive data substantiating a disproportionate impact on smaller companies.

With respect to investment companies, we assume that small investment companies, which may operate with thin profit margins, would be particularly affected by the rules and the attendant costs, including the loss of the benefits of a cluster or unitary board.[1094] However, the costs resulting from the loss of the benefits of a cluster or unitary board are costs associated with the traditional state law rights to nominate and elect directors, and are not costs incurred for including shareholder nominees in the company's proxy materials. We also note that any increased costs and decreased efficiency of an investment company's board as a result of the

1093 See, e.g., Bebchuk (2007).

1094 See letter from ICI.

fund complex no longer having a unitary or cluster board would occur, if at all, only in the event that investment company shareholders elect the shareholder nominee. Investment companies may include information in the proxy materials making investors aware of the company's views on the perceived benefits of a unitary or cluster board and the potential for increased costs and decreased efficiency if the shareholder nominees are elected.

E. Agency Action to Minimize Effect on Small Entities

The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish the stated objective, while minimizing any significant adverse impact on small entities. In connection with the new rules, we considered the following alternatives:

- the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities;
- the clarification, consolidation or simplification of the rule's compliance and reporting requirements for small entities;
- the use of performance rather than design standards; and
- an exemption for small entities from coverage under the proposals.

As noted in the Proposing Release, the Commission has considered a variety of reforms to achieve its regulatory objectives while minimizing the impact on small entities. As one possible approach, we considered in 2003 requiring companies to include shareholder nominees for director in a company's proxy materials only upon the occurrence of certain events so that the rule would apply only in situations where there was a demonstrated failure in the proxy process related to director nominations and elections. We sought comment in the Proposing Release on this approach, with commenters arguing both for[1095] and against[1096] the approach. We have not

[1095] See letters from ADP; Alaska Air; Allstate; American Electric Power; Anadarko; AT&T; Avis Budget; Barclays; Biogen; Boeing; BRT; Burlington Northern; R. Burt; Callaway; Chevron; CIGNA; CNH Global;

taken this approach in the final rules because we do not believe it is appropriate to limit the rule to companies where specified events have occurred. Moreover, we are not aware of data suggesting that such specified events are less likely to occur at smaller companies than at larger companies.

We considered changes to Rule 14a-8(i)(8) in 2007 that would enable shareholders to have their proposals for bylaw amendments regarding the procedures for nominating directors included in the company's proxy materials provided the shareholder submitting the proposal made certain disclosures and beneficially owned more than 5% of the company's shares. Although this approach could potentially reduce the number of shareholder proposals submitted to smaller entities by establishing a minimum threshold for having such proposals included in the company's proxy statement, we have not taken this approach because, as noted above, we do not expect the final rule to substantially increase the number of shareholder proposals to smaller companies. In addition, we have not relied exclusively on an amendment to Rule 14a-8(i)(8) to achieve our regulatory goals because we seek to provide shareholders with a more immediate and direct means of effecting change in the boards of directors of the companies in which they invest. For these reasons, as well as the reasons discussed throughout the release, we believe that these final rules may better achieve the Commission's objectives.

We also sought comment on whether the proposed tiered approach – under which shareholders or shareholder groups at larger companies would have to satisfy a lower ownership

---

Comcast; Cummins; Deere; Eaton; ExxonMobil; FedEx; FMC Corp.; FPL Group; Frontier; General Mills; C. Holliday; IBM; ITT; J. Kilts; E.J. Kullman; N. Lautenbach; McDonald's; J. Miller; Motorola; Office Depot; O'Melveny & Myers; P&G; PepsiCo; Pfizer; Protective; Ryder; Sara Lee; Sherwin Williams; Theragenics; TI; TW Telecom; G. Tooker; UnitedHealth; Xerox.

1096 See letters from ABA; AFSCME; CalSTRS; CFA Institute; CII; COPERA; T. DiNapoli; Florida State Board of Administration; ICGN; N. Lautenbach; LIUNA; D. Nappier; Nathan Cummings Foundation; OPERS; Pax World; Relational; Sodali; SWIB; TIAA-CREF; G. Tooker; USPE; ValueAct Capital.

threshold than shareholders or shareholder groups at smaller companies in order to rely on Rule 14a-11 – is appropriate and workable. We considered whether the effect of the tiered approach may make it less likely that shareholders at smaller companies will nominate directors under Rule 14a-11, but determined not to adopt this approach because the data available to us did not indicate a meaningful difference between small entities and entities generally in regard to concentration of long-term share ownership.[1097]

We considered whether a delayed compliance date for Rule 14a-11 for smaller reporting companies, which would include most small entities, would reduce the burden on these entities. After considering the comments discussed above, we have determined to delay the compliance date of Rule 14a-11 for smaller reporting companies for a period of three years from the effective date for other companies. We believe that a delayed compliance date for smaller reporting companies will allow those companies to observe how Rule 14a-11 operates for other companies and may allow them to better prepare for the implementation of the rules and, as noted, will give us a further opportunity to consider adjustments for smaller reporting companies. In addition, in an effort to limit the cost and burden on all companies subject to the rule, including smaller reporting companies, we have limited use of Rule 14a-11 to nominations by shareholders who have maintained significant continuous holdings in the company, and we have extended the required holding period to at least three years at the time the notice of nomination is filed with the Commission and transmitted to the company. We expect that these eligibility requirements will help achieve the stated objective without unduly burdening any particular group of companies.

We are not adopting different disclosure standards based on the size of the issuer. We believe uniform disclosure will be helpful to voting decisions on shareholder-nominated

1097 For further discussion, see Section II.B.4. above.

directors at companies of all sizes. Because we are delaying the compliance date of Rule 14a-11 for smaller reporting companies, we believe this will allow them additional time to prepare to comply with the new rule and observe the rule's impact on larger companies, which should allow smaller reporting companies to be able to comply with the same disclosure standards when the rule becomes applicable to them.

We considered the use of performance standards rather than design standards in the final rules. The final rule contains both performance standards and design standards. We proposed design standards to the extent that we believe compliance with particular requirements are necessary. However, to the extent possible, our rules impose performance standards. For example, under Rule 14a-11, a nominating shareholder or group can provide a 500-word statement of support concerning each of its nominee or nominees for director, but we do not specify the content. Similarly, shareholders can submit a proposal that seeks to establish a procedure under a company's governing documents for the inclusion of one or more shareholder director nominees in the company's proxy materials. By allowing shareholders to submit such proposals, we seek to provide shareholders and companies with a measure of flexibility to tailor the means through which they can comply with the standards. Even though Rule 14a-11 provides a procedure from which companies may not opt out, companies and shareholders are not prohibited from adopting nominating procedures that could further facilitate shareholders' ability to include their own director nominees in company proxy materials. Amended Rule 14a-8(i)(8) facilitates this process. In that respect, the rules provide both design and performance standards, as appropriate.

Lastly, as discussed above, we believe that the final rules should apply regardless of company size, as was proposed.[1098] The purpose of the rules is to facilitate the exercise of shareholders' traditional state law rights to nominate and elect directors to company boards of directors and thereby enable shareholders to participate more meaningfully in the nomination and election of directors at the companies in which they invest. We believe that shareholders of smaller reporting companies should be able to exercise these rights to the same extent as shareholders of larger reporting companies. Therefore, we are not persuaded that exempting smaller reporting companies from the final rules would be consistent with this goal.

Nonetheless, as discussed above, we recognize that smaller reporting companies may have had less experience with existing forms of shareholder involvement in the proxy process and may have less-developed infrastructures for managing these matters. The final rules therefore include a phase-in period that delays the compliance date of Rule 14a-11 for smaller reporting companies for three years from the effective date of the rule.

VII. STATUTORY AUTHORITY AND TEXT OF THE AMENDMENTS

The amendments are made pursuant to Sections 3(b), 13, 14, 15, 23(a) and 36 of the Securities Exchange Act of 1934, as amended, Sections 10, 20(a) and 38 of the Investment Company Act of 1940, as amended, and Sections 971 (a) and (b) of the Dodd-Frank Act.

List of Subjects

17 CFR Parts 200

Freedom of information, Reporting and recordkeeping requirements, Securities.

17 CFR Parts 232, 240, and 249

Reporting and recordkeeping requirements, Securities.

In accordance with the foregoing, the Securities and Exchange Commission is amending Title 17, chapter II of the Code of Federal Regulations as follows:

1098 See Section II.B.3.f. above.

PART 200 – ORGANIZATION; CONDUCT AND ETHICS; AND INFORMATION AND REQUESTS

Subpart D – Information and Requests

1. The authority citation for Part 200, Subpart D, continues to read, in part, as follows:

Authority: 5 U.S.C. 552, as amended, 15 U.S.C. 77f(d), 77s, 77ggg(a), 77sss, 78m(F)(3), 78w, 80a-37, 80a-44(a), 80a-44(b), 80b-10(a), and 80b-11.

* * * * *

2. Add § 200.82a to read as follows:

§ 200.82a Public availability of materials filed pursuant to § 240.14a-11(g) and related materials.

Materials filed with the Commission pursuant to Rule 14a-11(g) under the Securities Exchange Act of 1934 (17 CFR 240.14a-11(g)), written communications related thereto received from interested persons, and each related no-action letter or other written communication issued by the staff of the Commission, shall be made available to any person upon request for inspection or copying.

PART 232 – REGULATION S-T – GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS

3. The authority citation for Part 232 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s(a), 77z-3, 77sss(a), 78c(b), 78l, 78m, 78n, 78o(d), 78w(a), 78ll, 80a-6(c), 80a-8, 80a-29, 80a-30, 80a-37, and 7201 et seq.; and 18 U.S.C. 1350.

* * * * *

4. Amend § 232.13 by revising paragraph (a)(4) (the note remains unchanged) to read as follows:

§ 232.13 Date of filing; adjustment of filing date.

(a) * * *

(4) Notwithstanding paragraph (a)(2) of this section, a Form 3, 4 or 5 (§§ 249.103, 249.104, and 249.105 of this chapter) or a Schedule 14N (§ 240.14n-101 of this chapter) submitted by direct transmission on or before 10 p.m. Eastern Standard Time or Eastern Daylight Saving Time, whichever is currently in effect, shall be deemed filed on the same business day.

* * * * *

PART 240 – GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

5. The authority citation for Part 240 continues to read, in part, as follows:

<u>Authority</u>: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, and 7201, <u>et seq</u>.; and 18 U.S.C. 1350 and 12 U.S.C. 5221(e)(3), unless otherwise noted.

* * * * *

6. Amend § 240.13a-11 by revising paragraph (b) to read as follows:

§ 240.13a-11 Current reports on Form 8-K (§ 249.308 of this chapter).

* * * * *

(b) This section shall not apply to foreign governments, foreign private issuers required to make reports on Form 6-K (17 CFR 249.306) pursuant to § 240.13a-16, issuers of American Depositary Receipts for securities of any foreign issuer, or investment companies required to file reports pursuant to § 270.30b1-1 of this chapter under the Investment Company Act of 1940, except where such an investment company is required to file:

(1) Notice of a blackout period pursuant to § 245.104 of this chapter;

(2) Disclosure pursuant to Instruction 2 to § 240.14a-11(b)(1) of information concerning outstanding shares and voting; or

(3) Disclosure pursuant to Instruction 2 to § 240.14a-11(b)(10) of the date by which a nominating shareholder or nominating shareholder group must submit the notice required pursuant to § 240.14a-11(b)(10).

* * * * *

7. Amend § 240.13d-1 by revising paragraphs (b)(1)(i) and (c)(1) and adding Instruction 1 to paragraph (b)(1) and Instruction 1 to paragraph (c)(1) to read as follows:

§ 240.13d-1 Filing of Schedules 13D and 13G.

* * * * *

(b)(1) * * *

(i) Such person has acquired such securities in the ordinary course of his business and not with the purpose nor with the effect of changing or influencing the control of the issuer, nor in connection with or as a participant in any transaction having such purpose or effect, including any transaction subject to § 240.13d-3(b), other than activities solely in connection with a nomination under § 240.14a-11; and

* * * * *

<u>Instruction 1 to paragraph (b)(1)</u>. For purposes of paragraph (b)(1)(i) of this section, the exception for activities solely in connection with a nomination under § 240.14a-11 will not be available after the election of directors.

* * * * *

(c) * * *

(1) Has not acquired the securities with any purpose, or with the effect, of changing or

influencing the control of the issuer, or in connection with or as a participant in any transaction having that purpose or effect, including any transaction subject to § 240.13d-3(b), other than activities solely in connection with a nomination under § 240.14a-11;

* * * * *

Instruction 1 to paragraph (c)(1). For purposes of paragraph (c)(1) of this section, the exception for activities solely in connection with a nomination under § 240.14a-11 will not be available after the election of directors.

* * * * *

8. Amend § 240.13d-102 by revising the sentences following the introductory text in Items 10(a) and (c) as follows:

§ 240.13d-102 Schedule 13G – Information to be included in statements filed pursuant to § 240.13d-1(b), (c), and (d) and amendments thereto filed pursuant to § 240.13d-2.

* * * * *

Item 10. Certifications

(a) * * *

By signing below I certify that, to the best of my knowledge and belief, the securities referred to above were acquired and are held in the ordinary course of business and were not acquired and are not held for the purpose of or with the effect of changing or influencing the control of the issuer of the securities and were not acquired and are not held in connection with or as a participant in any transaction having that purpose or effect, other than activities solely in connection with a nomination under § 240.14a-11.

* * * * *

(c) * * *

By signing below I certify that, to the best of my knowledge and belief, the securities referred to above were not acquired and are not held for the purpose of or with the effect of changing or influencing the control of the issuer of the securities and were not acquired and are not held in connection with or as a participant in any transaction having that purpose or effect, other than activities solely in connection with a nomination under § 240.14a-11.

* * * * *

9. Amend § 240.14a-2 by:

a. Revising paragraph (b) introductory text; and

b. Adding paragraphs (b)(7) and (b)(8) and Instructions to those paragraphs.

The revision and additions read as follows:

§ 240.14a-2 Solicitations to which § 240.14a-3 to § 240.14a-15 apply.

* * * * *

(b) Sections 240.14a-3 to 240.14a-6 (other than paragraphs 14a-6(g) and 14a-6(p)), § 240.14a-8, § 240.14a-10, and §§ 240.14a-12 to 240.14a-15 do not apply to the following:

* * * * *

(7) Any solicitation by or on behalf of any shareholder in connection with the formation of a nominating shareholder group pursuant to § 240.14a-11, provided that:

(i) The soliciting shareholder is not holding the registrant's securities with the purpose, or with the effect, of changing control of the registrant or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under § 240.14a-11(d);

(ii) Each written communication includes no more than:

(A) A statement of each soliciting shareholder's intent to form a nominating shareholder group in order to nominate one or more directors under § 240.14a-11;

(B) Identification of, and a brief statement regarding, the potential nominee or nominees or, where no nominee or nominees have been identified, the characteristics of the nominee or nominees that the shareholder intends to nominate, if any;

(C) The percentage of voting power of the registrant's securities that are entitled to be voted on the election of directors that each soliciting shareholder holds or the aggregate percentage held by any group to which the shareholder belongs; and

(D) The means by which shareholders may contact the soliciting party.

(iii) Any written soliciting material published, sent or given to shareholders in accordance with this paragraph must be filed by the shareholder with the Commission, under the registrant's Exchange Act file number, or, in the case of a registrant that is an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), under the registrant's Investment Company Act file number, no later than the date the material is first published, sent or given to shareholders. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered. The soliciting material must include a cover page in the form set forth in Schedule 14N (§ 240.14n-101) and the appropriate box on the cover page must be marked.

(iv) In the case of an oral solicitation made in accordance with the terms of this section, the nominating shareholder must file a cover page in the form set forth in Schedule 14N (§ 240.14n-101), with the appropriate box on the cover page marked, under the registrant's Exchange Act file number (or in the case of an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), under the registrant's Investment Company Act file number), no later than the date of the first such communication.

Instruction to paragraph (b)(7). The exemption provided in paragraph (b)(7) of this section shall not apply to a shareholder that subsequently engages in soliciting or other nominating activities outside the scope of § 240.14a-2(b)(8) and § 240.14a-11 in connection with the subject election of directors or is or becomes a member of any other group, as determined under section 13(d)(3) of the Act (15 U.S.C. 78m(d)(3) and § 240.13d-5(b)), or otherwise, with persons engaged in soliciting or other nominating activities in connection with the subject election of directors.

(8) Any solicitation by or on behalf of a nominating shareholder or nominating shareholder group in support of its nominee that is included or that will be included on the registrant's form of proxy in accordance with § 240.14a-11 or for or against the registrant's nominee or nominees, provided that:

(i) The soliciting party does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as proxy for a shareholder and does not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention, consent or authorization;

(ii) Any written communication includes:

(A) The identity of each nominating shareholder and a description of his or her direct or indirect interests, by security holdings or otherwise;

(B) A prominent legend in clear, plain language advising shareholders that a shareholder nominee is or will be included in the registrant's proxy statement and that they should read the registrant's proxy statement when available because it includes important information (or, if the registrant's proxy statement is publicly available, advising shareholders of that fact and encouraging shareholders to read the registrant's proxy statement because it includes important information). The legend also must explain to shareholders that they can find the registrant's proxy statement, other soliciting material, and any other relevant documents at no charge on the Commission's Web site; and

(iii) Any written soliciting material published, sent or given to shareholders in accordance with this paragraph must be filed by the nominating shareholder or nominating shareholder group with the Commission, under the registrant's Exchange Act file number, or, in the case of a registrant that is an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), under the registrant's Investment Company Act file number, no later than the date the material is first published, sent or given to shareholders. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered. The soliciting material must include a cover page in the form set forth in Schedule 14N (§ 240.14n-101) and the appropriate box on the cover page must be marked.

Instruction 1 to paragraph (b)(8). A nominating shareholder or nominating shareholder group may rely on the exemption provided in paragraph (b)(8) of this section only after receiving notice from the registrant in accordance with § 240.14a-11(g)(1) or § 240.14a-11(g)(3)(iv) that the registrant will include the nominating shareholder's or nominating shareholder group's nominee or nominees in its form of proxy.

Instruction 2 to paragraph (b)(8). Any solicitation by or on behalf of a nominating shareholder or nominating shareholder group in support of its nominee included or to be included on the registrant's form of proxy in accordance with § 240.14a-11 or for or against the registrant's nominee or nominees must be made in reliance on the exemption provided in paragraph (b)(8) of this section and not on any other exemption.

Instruction 3 to paragraph (b)(8). The exemption provided in paragraph (b)(8) of this section shall not apply to a person that subsequently engages in soliciting or other nominating activities outside the scope of § 240.14a-11 in connection with the subject election of directors or is or becomes a member of any other group, as determined under section 13(d)(3) of the Act (15 U.S.C. 78m(d)(3) and § 240.13d-5(b)), or otherwise, with persons engaged in soliciting or other nominating activities in connection with the subject election of directors.

* * * * *

10. Amend § 240.14a-4 by:

a. Revising the first sentence of paragraph (b)(2) introductory text; and

b. Adding a sentence to the end of the undesignated paragraph following paragraph (b)(2)(iv).

The revision and addition read as follows:

§ 240.14a-4 Requirements as to proxy.

* * * * *

(b) * * *

(2) A form of proxy that provides for the election of directors shall set forth the names of persons nominated for election as directors, including any person whose nomination by a shareholder or shareholder group satisfies the requirements of § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials. * * *

* * * * *

(iv) * * *

* * * Means to grant authority to vote for any nominees as a group or to withhold

authority for any nominees as a group may not be provided if the form of proxy includes one or more shareholder nominees in accordance with § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials.

* * * * *

11. Amend § 240.14a-5 by:

a. Revising paragraph (e)(1) to remove "and" at the end of the paragraph;

b. Revising paragraph (e)(2) to remove the period at the end of the paragraph and add in its place "; and"; and

c. Adding paragraph (e)(3) to read as follows:

§ 240.14a-5 Presentation of information in proxy statement.

* * * * *

(e) * * *

(3) The deadline for submitting nominees for inclusion in the registrant's proxy statement and form of proxy pursuant to § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials for the registrant's next annual meeting of shareholders.

* * * * *

12. Amend § 240.14a-6 by:

a. Redesignating paragraphs (a)(4), (a)(5), (a)(6), and (a)(7) as paragraphs (a)(5), (a)(6), (a)(7), and (a)(8) respectively;

b. Adding new paragraph (a)(4);

c. Adding a sentence at the end of Note 3; and

d. Adding paragraph (p).

The revisions and additions read as follows:

§ 240.14a-6 Filing requirements.

(a) * * *

(4) A shareholder nominee for director included pursuant to § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials.

* * * * *

Note 3. * * * The inclusion of a shareholder nominee in the registrant's proxy materials pursuant to § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials does not constitute a "solicitation in opposition" for purposes of Rule 14a-6(a) (§ 240.14a-6(a)), even if the registrant opposes the shareholder nominee and solicits against the shareholder nominee and in favor of a registrant nominee.

* * * * *

(p) <u>Solicitations subject to § 240.14a-11</u>. Any soliciting material that is published, sent or given to shareholders in connection with § 240.14a-2(b)(7) or (b)(8) must be filed with the Commission as specified in that section.

13. Amend § 240.14a-8 by revising paragraph (i)(8) as follows:

§ 240.14a-8 Shareholder proposals.

* * * * *

(i) * * *

(8) Director elections: If the proposal:

(i) Would disqualify a nominee who is standing for election;

(ii) Would remove a director from office before his or her term expired;

(iii) Questions the competence, business judgment, or character of one or more nominees or directors;

(iv) Seeks to include a specific individual in the company's proxy materials for election to the board of directors; or

(v) Otherwise could affect the outcome of the upcoming election of directors.

* * * * *

14. Amend § 240.14a-9 by adding a paragraph (c), removing the authority citation following the section, and redesignating notes (a), (b), (c), and (d) as a., b., c., and d.

The addition reads as follows:

§ 240.14a-9 False or misleading statements.

* * * * *

(c) No nominee, nominating shareholder or nominating shareholder group, or any member thereof, shall cause to be included in a registrant's proxy materials, either pursuant to the federal proxy rules, an applicable state or foreign law provision, or a registrant's governing documents as they relate to including shareholder nominees for director in a registrant's proxy materials, include in a notice on Schedule 14N (§ 240.14n-101), or include in any other related communication, any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to a solicitation for the same meeting or subject matter which has become false or misleading.

* * * * *

15. Add § 240.14a-11 to read as follows:

§ 240.14a-11 Shareholder nominations.

(a) Applicability. In connection with an annual (or a special meeting in lieu of an annual) meeting of shareholders, or a written consent in lieu of such meeting, at which directors are elected, a registrant will be required to include in its proxy statement and form of proxy the name of a person or persons nominated by a shareholder or group of shareholders for election to the board of directors and include in its proxy statement the disclosure about such nominee or nominees and the nominating shareholder or members of the nominating shareholder group as specified in Item 5 of Schedule 14N (§ 240.14n-101), provided that the conditions set forth in paragraph (b) of this section are satisfied. This rule will not apply to a registrant if:

(1) The registrant is subject to the proxy rules solely because it has a class of debt securities registered under section 12 of the Exchange Act (15 U.S.C. 78l); or

(2) Applicable state or foreign law or a registrant's governing documents prohibit the registrant's shareholders from nominating a candidate or candidates for election as director.

(b) Eligibility. A shareholder nominee or nominees shall be included in a registrant's proxy statement and form of proxy if the following requirements are satisfied:

(1) The nominating shareholder individually, or the nominating shareholder group in the aggregate, holds at least 3% of the total voting power of the registrant's securities that are entitled to be voted on the election of directors at the annual (or a special meeting in lieu of the annual) meeting of shareholders or on a written consent in lieu of such meeting, on the date the nominating shareholder or nominating shareholder group files the notice on Schedule 14N (§

240.14n-101) with the Commission and transmits the notice to the registrant;

(2) The nominating shareholder or each member of the nominating shareholder group has held the amount of securities that are used for purposes of satisfying the minimum ownership requirement of paragraph (b)(1) of this section continuously for at least three years as of the date the notice on Schedule 14N (§ 240.14n-101) is filed with the Commission and transmitted to the registrant and must continue to hold that amount of securities through the date of the subject election of directors;

(3) The nominating shareholder or each member of the nominating shareholder group provides proof of ownership of the amount of securities that are used for purposes of satisfying the ownership and holding period requirements of paragraphs (b)(1) and (b)(2) of this section. If the nominating shareholder or each member of the nominating shareholder group is not the registered holder of the securities, the nominating shareholder or each member of the nominating shareholder group must provide proof of ownership in the form of one or more written statements from the registered holder of the nominating shareholder's securities (or the brokers or banks through which those securities are held) verifying that, as of a date within seven calendar days prior to filing the notice on Schedule 14N (§ 240.14n-101) with the Commission and transmitting the notice to the registrant, the nominating shareholder or each member of the nominating shareholder group, continuously held the amount of securities being used to satisfy the ownership threshold for a period of at least three years. The written statement or statements proving ownership must be attached as an appendix to Schedule 14N on the date the notice is filed with the Commission and transmitted to the registrant, and provide the information specified in Item 4 of Schedule 14N. In the alternative, if the nominating shareholder or member of the nominating shareholder group has filed a Schedule 13D (§ 240.13d-101), Schedule 13G (§

240.13d-102), Form 3 (§ 249.103 of this chapter), Form 4 (§ 249.104 of this chapter), and/or Form 5 (§ 249.105 of this chapter), or amendments to those documents, reflecting ownership of the securities as of or before the date on which the three-year eligibility period begins, the nominating shareholder or member of the nominating shareholder group may attach the filing as an appendix to the Schedule 14N or incorporate the filing by reference into the Schedule 14N;

(4) The nominating shareholder or each member of the nominating shareholder group provides a statement, as specified in Item 4(b) of Schedule 14N (§ 240.14n-101), on the date the notice on Schedule 14N is filed with the Commission and transmitted to the registrant, that the nominating shareholder or each member of the nominating shareholder group intends to continue to hold the amount of securities that are used for purposes of satisfying the minimum ownership requirement of paragraph (b)(1) of this section through the date of the meeting;

(5) The nominating shareholder or each member of the nominating shareholder group provides a statement, as specified in Item 4(b) of Schedule 14N (§ 240.14n-101), on the date the notice on Schedule 14N is filed with the Commission and transmitted to the registrant, regarding the nominating shareholder's or group's intent with respect to continued ownership of the registrant's securities after the election;

(6) The nominating shareholder (or where there is a nominating shareholder group, each member of the nominating shareholder group) is not holding any of the registrant's securities with the purpose, or with the effect, of changing control of the registrant or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under paragraph (d) of this section;

(7) Neither the nominee nor the nominating shareholder (or where there is a nominating shareholder group, any member of the nominating shareholder group) has an agreement with the registrant regarding the nomination of the nominee;

(8) The nominee's candidacy or, if elected, board membership would not violate controlling federal law, state law, foreign law, or rules of a national securities exchange or national securities association (other than rules regarding director independence) or, in the case that the nominee's candidacy or, if elected, board membership would violate such laws or rules, such violation could not be cured by the time provided in paragraph (g)(2) of this section;

(9) In the case of a registrant other than an investment company, the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the registrant, if any, or, in the case of a registrant that is an investment company, the nominee is not an "interested person" of the registrant as defined in section 2(a)(19) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(19));

(10) The nominating shareholder or nominating shareholder group provides notice to the registrant on Schedule 14N (§ 240.14n-101), as specified by § 240.14n-1, of its intent to require that the registrant include that shareholder's or group's nominee in the registrant's proxy statement and form of proxy. This notice must be transmitted to the registrant on the date it is filed with the Commission. The notice must be filed with the Commission and transmitted to the registrant no earlier than 150 calendar days, and no later than 120 calendar days, before the anniversary of the date that the registrant mailed its proxy materials for the prior year's annual meeting, except that, if the registrant did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, or if the registrant is holding a special meeting or conducting an election of directors by written consent,

then the nominating shareholder or nominating shareholder group must transmit the notice to the registrant and file its notice with the Commission a reasonable time before the registrant mails its proxy materials, as specified by the registrant in a Form 8-K (§ 249.308 of this chapter) filed pursuant to Item 5.08 of Form 8-K; and

(11) The nominating shareholder or nominating shareholder group provides the certifications required by Schedule 14N (§ 240.14n-101) on the date the notice on Schedule 14N is filed with the Commission and transmitted to the registrant.

Instruction to paragraph (b). A registrant will not be required to include a nominee or nominees submitted by a nominating shareholder or nominating shareholder group pursuant to this section if the nominating shareholder or any member of the nominating shareholder group also submits any other nomination to that registrant and/or is participating in more than one nominating shareholder group for that registrant. In addition, a registrant will not be required to include a nominee or nominees if a nominating shareholder or member of a nominating shareholder group:

a. Is or becomes a member of any other group, as determined under section 13(d)(3) of the Act (15 U.S.C. 78m(d)(3) and § 240.13d-5(b)), or otherwise, with persons engaged in soliciting or other nominating activities in connection with the subject election of directors;

b. Is separately conducting a solicitation in connection with the subject election of directors other than a solicitation subject to § 240.14a-2(b)(8) in relation to those nominees it has nominated pursuant to this section or for or against the registrant's nominees; or

c. Is acting as a participant in another person's solicitation in connection with the subject election of directors.

Instruction 1 to paragraph (b)(1). In the case of a registrant other than an investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), for purposes of (b)(1) of this section, in determining the total voting power of the registrant's securities that are entitled to be voted on the election of directors, the nominating shareholder or nominating shareholder group may rely on information set forth in the registrant's most recent quarterly or annual report, and any current report subsequent thereto, filed with the Commission pursuant to this Act, unless the nominating shareholder or nominating shareholder group knows or has reason to know that the information contained therein is inaccurate. In the case of a registrant that is an investment company registered under the Investment Company Act of 1940, for purposes of (b)(1) of this section, in determining the total voting power of the registrant's securities that are entitled to be voted on the election of directors, the nominating shareholder or nominating shareholder group may rely on information set forth in the following documents, unless the nominating shareholder or nominating shareholder group knows or has reason to know that the information contained therein is inaccurate:

a. In the case of a registrant that is a series company as defined in Rule 18f-2(a) under the Investment Company Act of 1940 (§ 270.18f-2(a) of this chapter), the Form 8-K (§ 249.308 of this chapter) described in Instruction 2 to paragraph (b)(1) of this section; or

b. In the case of other investment companies, the registrant's most recent annual or semi-annual report filed with the Commission on Form N-CSR (§ 249.331 and § 274.128 of this chapter).

Instruction 2 to paragraph (b)(1). If the registrant is an investment company that is a series company (as defined in § 270.18f-2(a) of this chapter), the registrant must disclose pursuant to Item 5.08 of Form 8-K (§ 249.308 of this chapter) the total number of shares of the registrant outstanding and entitled to be voted (or if the votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) on the election of directors as of the end of the most recent calendar quarter.

Instruction 3 to paragraph (b)(1).

a. When determining the total voting power of the registrant's securities, which is the denominator in the calculation of the percentage of voting power held by the nominating shareholder individually or the nominating shareholder group in the aggregate, calculate the aggregate number of votes derived from all classes of securities of the registrant that are entitled to vote on the election of directors regardless of whether solicitation of a proxy with respect to those securities would require compliance with Exchange Act Regulation 14A (§240.14a-1 et seq.).

b. When determining the total voting power of the registrant's securities held by the nominating shareholder or any member of the nominating shareholder group, which is the numerator in the calculation of the percentage:

1. Calculate the number of votes derived only from securities with respect to which solicitation of a proxy would require compliance with Exchange Act Regulation 14A (§ 240.14a-1 et seq.) and over which the nominating shareholder or any the member of the nominating shareholder group, as the case may be, has voting power and investment power, either directly or through any person acting on their behalf;

2. Notwithstanding the voting power calculation specified in paragraph b.1. of this instruction, add to the result of the calculation specified in paragraph b.1. of this instruction any votes attributable to securities with respect to which solicitation of a proxy would require compliance with Exchange Act Regulation 14A (§ 240.14a-1 et seq.) that have been loaned by or on behalf of the nominating shareholder or any member of the nominating shareholder group to

another person, if the nominating shareholder or member of the nominating shareholder group, as the case may be, or any person acting on their behalf, has the right to recall the loaned securities, and will recall the loaned securities upon being notified that any of the nominating shareholder's or group's nominees will be included in the registrant's proxy statement and proxy card; and

3. Subtract from the result of the calculation specified in paragraphs b.1. and b.2. of this instruction the number of votes attributable to securities of the registrant entitled to vote on the election of directors, regardless of whether solicitation of a proxy with respect to those securities would require compliance Exchange Act Regulation 14A (§ 240.14a-1 et seq.), that the nominating shareholder or any member of the nominating shareholder group, as the case may be, or any person acting on their behalf, has sold in a short sale, as defined in 17 CFR 242.200(a), that is not closed out, or has borrowed for purposes other than a short sale.

c. For purposes of the voting power calculation in paragraph b.1. of this instruction:

1. A shareholder has voting power directly only when the shareholder has the power to vote or direct the voting, and investment power directly only when the shareholder has the power to dispose or direct the disposition, of the securities; and

2. A securities intermediary (as defined in § 240.17Ad-20(b)) shall not have voting power or investment power over securities for purposes of paragraph b.1. of this instruction solely because such intermediary holds such securities by or on behalf of another person, notwithstanding that pursuant to the rules of a national securities exchange such intermediary may vote or direct the voting of such securities without instruction.

Instruction 4 to paragraph (b)(1). If a registrant has more than one class of outstanding securities entitled to vote on the election of directors and those classes do not vote together in the election of all directors, then the voting power of the registrant's securities for purposes of the calculation of both the numerator and denominator specified in Instruction 3 to paragraph (b)(1) should be determined only on the basis of the voting power of the class or classes of securities that would be voting together on the election of the person or persons sought to be nominated by the nominating shareholder or the nominating shareholder group.

Instruction to paragraph (b)(2). To determine whether the amount of securities that are used for purposes of satisfying the minimum ownership requirement of paragraph (b)(1) has been held continuously during the three year period prior to the date the Schedule 14N (§ 240.14n-101) is filed and during the period after the Schedule 14N is filed through the date of the subject election of directors, and with respect to all points in time during those periods:

a. Include only the amount of securities with respect to which a solicitation of a proxy would require compliance with Exchange Act Regulation 14A (§ 240.14a-1 et seq.) and over which the nominating shareholder or the member of the nominating shareholder group, as the case may be, has voting power and investment power, either directly or through any person acting on their behalf;

b. Notwithstanding the voting power determination specified in paragraph a. of this instruction, include the amount of securities that have been loaned by or on behalf of the nominating shareholder or any member of the nominating shareholder group to another person, if the nominating shareholder or member of the nominating shareholder group, as the case may be, or any person acting on their behalf:

1. Has the right to recall the loaned securities; and

2. With respect to the period from the date the Schedule 14N (§ 240.14n-101) is filed through the date of the subject election of directors, will recall the loaned securities upon being

notified that any of the person's nominees will be included in the registrant's proxy statement and proxy card;

c. Reduce the amount of securities held by the amount of securities, on a class basis, that the nominating shareholder or any member of the nominating shareholder group, as the case may be, or any person acting on their behalf, sold in a short sale, as defined in 17 CFR 242.200(a), during the periods, or borrowed for purposes other than a short sale; and

d. Adjust the amount of securities held to give effect to any changes in the amount of securities during the periods resulting from stock splits, reclassifications or other similar adjustments by the registrant.

Instruction to paragraph (b)(3). If the nominating shareholder or member of the nominating shareholder group must provide proof of ownership in the form of a written statement with respect to securities held through a broker or bank that is a participant in the Depository Trust Company or other clearing agency acting as a securities depository, then a statement from such broker or bank will satisfy the requirements of paragraph (b)(3) of this section. If the securities are held through a broker or bank (e.g., in an omnibus account) that is not a participant in a clearing agency acting as a securities depository, the nominating shareholder or member of the nominating shareholder group must also obtain and submit a separate written statement specified in the Instruction to Item 4 of Schedule 14N (§ 240.14n-101).

Instruction to paragraph (b)(7). Negotiations between the nominee, the nominating shareholder or nominating shareholder group and the nominating committee or board of the registrant to have the nominee included in the registrant's proxy statement and form of proxy as a registrant nominee, where those negotiations are unsuccessful, or negotiations that are limited to whether the registrant is required to include the shareholder nominee in the registrant's proxy statement and form of proxy in accordance with this section, will not represent a direct or indirect agreement with the registrant.

Instruction to paragraph (b)(9). For purposes of this provision, the nominee would be required to meet the definition of "independence" that is generally applicable to directors of the registrant and not any particular definition of independence applicable to members of the audit committee of the registrant's board of directors. To the extent a national securities exchange or national securities association rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board (for example, requiring that the board of directors or any group or committee of the board of directors make a determination regarding the existence of factors material to a determination of a nominee's independence), the nominee would not be required to meet the subjective determination of independence as part of the shareholder nomination process.

Instruction 1 to paragraph (b)(10). If the registrant held a meeting the previous year and the date of the current year's annual meeting has not changed by more than 30 calendar days from the date of the previous year's annual meeting, the window period for filing a notice on Schedule 14N (§ 240.14n-101) with the Commission and transmitting that notice to the registrant should be calculated by determining the release date disclosed in the registrant's previous year's proxy statement, increasing the year by one, and counting back 150 calendar days and 120 calendar days for the beginning and end of the window period, respectively. Where the 120 calendar day deadline falls on a Saturday, Sunday or holiday, the deadline will be treated as the first business day following the Saturday, Sunday or holiday.

Instruction 2 to paragraph (b)(10). If the registrant did not hold an annual meeting the previous year, or if the date of the current year's annual meeting has been changed by more than 30 calendar days from the date of the previous year's annual meeting, or if the registrant is holding a special meeting or conducting the election of directors by written consent, the registrant must disclose pursuant to Item 5.08 of Form 8-K (§ 249.308 of this chapter) the date by which a shareholder or group must submit the notice required pursuant to paragraph (b)(10) of this section, which date shall be a reasonable time prior to the date the registrant mails its proxy materials for the meeting.

(c) Statement of support. A registrant will be required to include a statement of support submitted by a nominating shareholder or nominating shareholder group in Item 5(i) of the notice on Schedule 14N (§ 240.14n-101), provided that the statement of support does not exceed 500 words per nominee. If a statement of support submitted by a nominating shareholder or nominating shareholder group exceeds 500 words per nominee, the registrant will be required to include the nominee or nominees, provided that the eligibility requirements and other conditions of the rule are satisfied, but the registrant may exclude the supporting statement(s).

(d) Maximum number of shareholder nominees. (1) A registrant will be required to include in its proxy statement and form of proxy one shareholder nominee or the number of nominees that represents 25% of the total number of the registrant's board of directors, whichever is greater, submitted by a nominating shareholder or nominating shareholder group pursuant to this section, subject to the limitations in paragraphs (d)(2), (d)(3), (d)(4), and (d)(5) of this section. A registrant may exclude a nominee or nominees if including the nominee or nominees would result in the registrant exceeding the maximum number of nominees it is required to include in its proxy statement and form of proxy pursuant to this provision.

(2) Where the registrant has one or more directors currently serving on its board of directors who were elected as a shareholder nominee pursuant to this section, and the term of that director or directors extends past the election of directors for which it is soliciting proxies, the registrant will not be required to include in the proxy statement and form of proxy more shareholder nominees than could result in the total number of directors who were elected as shareholder nominees pursuant to this section and serving on the board being more than one shareholder nominee or 25% of the total number of the registrant's board of directors, whichever is greater.

(3) Where the registrant has multiple classes of securities and each class is entitled to elect a specified number of directors, the registrant will be required to include the lesser of the number of nominees that the nominating shareholder's or group's class is entitled to elect or 25% of the registrant's board of directors, but in no case less than one nominee.

(4) Where the registrant agrees to include in its proxy statement and form of proxy, as an unopposed registrant nominee, the nominee or nominees of the nominating shareholder or nominating shareholder group that otherwise would be eligible under this section to have its nominees included in the registrant's proxy materials, the nominee will be considered a shareholder nominee for purposes of calculating the maximum number of shareholder nominees that must be included in the registrant's proxy statement and form of proxy, provided that the nominating shareholder or nominating shareholder group filed its notice on Schedule 14N (§ 240.14n-101) before beginning communications with the registrant about the nomination.

(5) A nominee included in a registrant's proxy statement and form of proxy as a result of an agreement between the nominee or nominating shareholder (or where there is a nominating shareholder group, any member of the nominating shareholder group) and the registrant, other

than as specified in paragraph (d)(4) of this section, will not be counted as a shareholder nominee for purposes of calculating the maximum number of shareholder nominees that the registrant is required to include in its proxy statement and form of proxy.

Instruction to paragraph (d)(1). Depending on board size, 25% of the board may not result in a whole number. In those instances, the registrant will round down to the closest whole number below 25% to determine the maximum number of shareholder nominees for director that the registrant is required to include in its proxy statement and form of proxy.

Instruction to paragraph (d)(5). Negotiations between the nominee, the nominating shareholder or nominating shareholder group and the nominating committee or board of the registrant to have the nominee included in the registrant's proxy statement and form of proxy as a registrant nominee, where those negotiations are unsuccessful, or negotiations that are limited to whether the registrant is required to include the shareholder nominee in the registrant's proxy statement and form of proxy in accordance with this section, will not represent a direct or indirect agreement with the registrant.

(e) Order of priority for shareholder nominees. (1) In the event that more than one eligible shareholder or group of shareholders submits a nominee or nominees for inclusion in the registrant's proxy materials pursuant to this section, the registrant shall include in the proxy statement and form of proxy the nominee or nominees of the nominating shareholder or nominating shareholder group with the highest qualifying voting power percentage disclosed as of the date of filing the Schedule 14N (§ 240.14n-101) (as determined in calculating ownership to satisfy the requirement as specified in paragraph (b)(1) of this section) from which the registrant received a notice filed and transmitted as specified in paragraph (b)(10) of this section, up to and including the total number of nominees required to be included by the registrant pursuant to this section. Where the nominating shareholder or nominating shareholder group with the highest qualifying voting power percentage that is otherwise eligible to rely on this section and that filed and transmitted the notice as specified in paragraph (b)(10) of this section does not nominate the maximum number of individuals required to be included by the registrant, the nominee or nominees of the nominating shareholder or nominating shareholder group with the next highest qualifying voting power percentage from which the registrant received the notice filed and transmitted as specified in paragraph (b)(10) of this section would be included in the registrant's proxy statement and form of proxy, if any, up to and including the total number required to be included by the registrant. This process would continue until the registrant has included the maximum number of nominees it is required to include in its proxy statement and form of proxy pursuant to paragraph (d) of this section or the registrant exhausts the list of eligible nominees.

(2) Prior to the time a registrant has commenced printing its proxy statement and form of proxy, if a nominating shareholder or nominating shareholder group withdraws or is disqualified, a registrant will be required to include in its proxy statement and form of proxy the nominee or nominees of the nominating shareholder or nominating shareholder group with the next highest qualifying voting power percentage, disclosed as of the date of filing the Schedule 14N (§ 240.14n-101) (as determined in calculating ownership to satisfy the requirement as specified in paragraph (b)(1) of this section), from which the registrant received a notice filed and transmitted as specified in paragraph (b)(10) of this section, if any, up to and including the total number required to be included by the registrant. This process would continue until the registrant included the maximum number of nominees it is required to include in its proxy statement and form of proxy pursuant to paragraph (d) of this section or the registrant exhausts the list of

eligible nominees. If the registrant has commenced printing its proxy statement and form of proxy, the registrant will not be required to include a nominee or nominees in its proxy statement and form of proxy in place of a nominee or nominees that has withdrawn or has been disqualified.

(3) If a nominee or nominees withdraws or is disqualified after the registrant provides notice to the nominating shareholder or nominating shareholder group of the registrant's intent to include the nominee or nominees in its proxy statement and form of proxy, the registrant will be required to include in its proxy statement and form of proxy any other eligible nominee submitted by that nominating shareholder or nominating shareholder group. If that nominating shareholder or nominating shareholder group did not include any other eligible nominees in its notice filed on Schedule 14N (§ 240.14n-101), then the registrant will be required to include the nominee or nominees of the nominating shareholder or nominating shareholder group with the next highest voting power percentage, disclosed as of the date of filing the Schedule 14N (§ 240.14n-101) (as determined in calculating ownership to satisfy the requirement as specified in paragraph (b)(1) of this section), from which the registrant received a notice filed and transmitted as specified in paragraph (b)(10) of this section, if any, up to and including the total number required to be included by the registrant. This process would continue until the registrant included the maximum number of nominees it is required to include in its proxy statement and form of proxy pursuant to paragraph (d) of this section or the registrant exhausts the list of eligible nominees. If the registrant has commenced printing its proxy statement and form of proxy, the registrant will not be required to include a nominee or nominees in its proxy statement and form of proxy in place of a nominee or nominees that has withdrawn or has been disqualified.

(4) Notwithstanding the other provisions of this paragraph, if a registrant has multiple classes of securities and each class is entitled to elect a specified number of directors, and nominating shareholders or groups of nominating shareholders of more than one of those classes submit a number of eligible nominees for inclusion in the registrant's proxy materials pursuant to this section that is greater than 25% of the total number of the registrant's board of directors, the registrant shall include in the proxy statement and form of proxy the nominee or nominees of the nominating shareholders or groups on the basis of the proportion of total voting power in the election of directors attributable to each class, rounding to the closest whole number, if necessary, and otherwise in accordance with paragraph (e) of this section.

Instruction 1 to paragraph (e). In determining the priority of the nominee or nominees to be included in the registrant's proxy materials, the registrant will be required to consider only the nominee or nominees that would otherwise be required to be included under the provisions of this section.

Instruction 2 to paragraph (e). If the registrant is including shareholder director nominees from more than one nominating shareholder or nominating shareholder group, as described in this paragraph, and including all of the shareholder director nominees of the nominating shareholder or nominating shareholder group that is last in priority would result in exceeding the maximum number required under paragraph (d) of this section, the nominating shareholder or nominating shareholder group that is last in priority may specify which of its nominees are to be included in the registrant's proxy materials.

(f) False or misleading statements. The registrant is not responsible for any information in the notice from the nominating shareholder or nominating shareholder group submitted as required by paragraph (b)(10) of this section or otherwise provided by the nominating shareholder or nominating shareholder group that is included in the registrant's proxy materials.

(g) Determinations regarding eligibility. (1) If the registrant determines that it will include a shareholder nominee, it must notify the nominating shareholder or nominating shareholder group (or their authorized representative) upon making this determination. In no event should the notification be postmarked or transmitted electronically later than 30 calendar days before it files its definitive proxy statement and form of proxy with the Commission.

(2) If the registrant determines that it may exclude a shareholder nominee pursuant to a provision in paragraph (a), (b), (d), or (e) of this section, or exclude a statement of support pursuant to paragraph (c) of this section, the registrant must notify in writing the nominating shareholder or nominating shareholder group (or their authorized representative) of this determination. This notice must be postmarked or transmitted electronically to the nominating shareholder or nominating shareholder group (or their authorized representative) no later than 14 calendar days after the close of the period for submission specified in paragraph (b)(10) of this section.

(i) The registrant's notice to the nominating shareholder or nominating shareholder group (or their authorized representative) that it has determined that it may exclude a shareholder nominee or statement of support must include an explanation of the registrant's basis for determining that it may exclude the nominee or statement of support.

(ii) The nominating shareholder or nominating shareholder group shall have 14 calendar days after receipt of the registrant's notice pursuant to paragraph (g)(2)(i) of this section to respond to the registrant's notice and correct any eligibility or procedural deficiencies identified in that notice. The nominating shareholder's or nominating shareholder group's response must be postmarked or transmitted electronically to the registrant no later than 14 calendar days after receipt of the registrant's notice.

(3) If the registrant intends to exclude a shareholder nominee or statement of support, after providing the requisite notice of and time for the nominating shareholder or nominating shareholder group to remedy any eligibility or procedural deficiencies in the nomination or statement, the registrant must provide notice of the basis for its determination to the Commission no later than 80 calendar days before it files its definitive proxy statement and form of proxy with the Commission. The Commission staff may permit the registrant to make its submission later than 80 calendar days before the registrant files its definitive proxy statement and form of proxy if the registrant demonstrates good cause for missing the deadline.

(i) The registrant's notice to the Commission shall include:

(A) Identification of the nominating shareholder or each member of the nominating shareholder group, as applicable;

(B) The name of the nominee or nominees;

(C) An explanation of the registrant's basis for determining that the registrant may exclude the nominee or nominees or a statement of support; and

(D) A supporting opinion of counsel when the registrant's basis for excluding a nominee or nominees relies on a matter of state or foreign law.

(ii) The registrant must file its notice to the Commission and simultaneously provide a copy to the nominating shareholder or each member of the nominating shareholder group (or their authorized representative). At the time the registrant files its notice, the registrant also may seek an informal statement of the Commission staff's views with regard to its determination to exclude from its proxy materials a nominee or nominees or a statement of support. The

Commission staff may provide an informal statement of its views to the registrant along with a copy to the nominating shareholder or nominating shareholder group (or their authorized representative);

(iii) The nominating shareholder or nominating shareholder group may submit a response to the registrant's notice to the Commission. This response must be postmarked or transmitted electronically to the Commission no later than 14 calendar days after the nominating shareholder's or nominating shareholder group's receipt of the registrant's notice to the Commission. The nominating shareholder or nominating shareholder group must simultaneously provide to the registrant a copy of its response to the Commission.

(iv) If the registrant seeks an informal statement of the Commission staff's views with regard to its determination to exclude a shareholder nominee or nominees, the registrant shall provide the nominating shareholder or nominating shareholder group (or their authorized representative) with notice, either postmarked or transmitted electronically, promptly following receipt of the staff's response, of whether it will include or exclude the shareholder nominee; and

(v) The exclusion of a shareholder nominee or a statement of support by a registrant where that exclusion is not permissible under paragraph (a), (b), (c), (d), or (e) of this section shall be a violation of this section.

Instruction 1 to paragraph (g). When a registrant must provide a notice to a nominating shareholder, member of a nominating shareholder group, or authorized representative of a nominating shareholder group, the registrant is responsible for providing the notice in a manner that evidences timely transmission. Where a nominating shareholder, member of a nominating shareholder group, or authorized representative of a nominating shareholder group responds to a notice, the nominating shareholder, member of a nominating shareholder group, or authorized representative of a nominating shareholder group is responsible for providing the response in a manner that evidences timely transmission.

Instruction 2 to paragraph (g). Neither the composition of the nominating shareholder group nor the shareholder nominee may be changed as a means to correct a deficiency identified in the registrant's notice to the nominating shareholder or nominating shareholder group under paragraph (g)(2) of this section; however, where a nominating shareholder or nominating shareholder group submits a number of nominees that exceeds the maximum number required to be included by the registrant under the circumstances set forth in paragraph (d) of this section, the nominating shareholder or nominating shareholder group may specify which nominee or nominees are not to be included in the registrant's proxy materials.

Instruction 3 to paragraph (g). Unless otherwise indicated in this section, the burden is on the registrant to demonstrate that it may exclude a nominee or statement of support.

16. Amend § 240.14a-12 by removing the heading following paragraph (c)(2)(iii) "Instructions to § 240.14a-12"; by removing the numbers 1. and 2. of instructions 1 and 2 to § 240.14a-12 and adding in their places the phrases "Instruction 1 to § 240.14a-12." and "Instruction 2 to § 240.14a-12.", respectively; and adding Instruction 3 to § 240.14a-12 to read as follows:

§ 240.14a-12 Solicitation before furnishing a proxy statement.

* * * * *

Instruction 3 to § 240.14a-12. Inclusion of a nominee pursuant to § 240.14a-11, an applicable state or foreign law provision, or a registrant's governing documents as they relate to the inclusion of shareholder director nominees in the registrant's proxy materials, or solicitations by a nominating shareholder or nominating shareholder group that are made in connection with that nomination constitute solicitations in opposition subject to § 240.14a-12(c), except for purposes of § 240.14a-6(a).

17. Add § 240.14a-18 to read as follows:

§ 240.14a-18 Disclosure regarding nominating shareholders and nominees submitted for inclusion in a registrant's proxy materials pursuant to applicable state or foreign law, or a registrant's governing documents.

To have a nominee included in a registrant's proxy materials pursuant to a procedure set forth under applicable state or foreign law, or the registrant's governing documents addressing the inclusion of shareholder director nominees in the registrant's proxy materials, the nominating shareholder or nominating shareholder group must provide notice to the registrant of its intent to do so on a Schedule 14N (§ 240.14n-101) and file that notice, including the required disclosure, with the Commission on the date first transmitted to the registrant. This notice shall be postmarked or transmitted electronically to the registrant by the date specified by the registrant's advance notice provision or, where no such provision is in place, no later than 120 calendar days before the anniversary of the date that the registrant mailed its proxy materials for the prior year's annual meeting, except that, if the registrant did not hold an annual meeting during the prior year, or if the date of the meeting has changed by more than 30 calendar days from the prior year, then the nominating shareholder or nominating shareholder group must provide notice a reasonable time before the registrant mails its proxy materials, as specified by the registrant in a Form 8-K (§ 249.308 of this chapter) filed pursuant to Item 5.08 of Form 8-K.

Instruction to § 240.14a-18. The registrant is not responsible for any information provided in the Schedule 14N (§ 240.14n-101) by the nominating shareholder or nominating shareholder group, which is submitted as required by this section or otherwise provided by the nominating shareholder or nominating shareholder group that is included in the registrant's proxy materials.

18. Amend § 240.14a-101 by:

a. Revising Item 7 as follows:

i. Redesignating paragraph (e) as paragraph (g); and

ii. Adding new paragraph (e) and paragraph (f); and

b. Adding paragraphs (18) and (19) to Item 22(b).

The additions read as follows:

§ 240.14a-101 – Schedule 14A. Information required in proxy statement.

SCHEDULE 14A INFORMATION

* * * * *

Item 7. * * *

* * * * *

(e) If a shareholder nominee or nominees are submitted to the registrant for inclusion in the registrant's proxy materials pursuant to § 240.14a-11 and the registrant is not permitted to exclude the nominee or nominees pursuant to the provisions of § 240.14a-11, the registrant must include in its proxy statement the disclosure required from the nominating shareholder or nominating shareholder group under Item 5 of § 240.14n-101 with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to Item 7(e). The information disclosed pursuant to paragraph (e) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933 (15 U.S.C. 77a et seq.), the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), or the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), except to the extent that the registrant specifically incorporates that information by reference.

(f) If a registrant is required to include a shareholder nominee or nominees submitted to the registrant for inclusion in the registrant's proxy materials pursuant to a procedure set forth under applicable state or foreign law, or the registrant's governing documents providing for the inclusion of shareholder director nominees in the registrant's proxy materials, the registrant must include in its proxy statement the disclosure required from the nominating shareholder or nominating shareholder group under Item 6 of § 240.14n-101 with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to Item 7(f). The information disclosed pursuant to paragraph (f) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933 (15 U.S.C. 77a et seq.), the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), or the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), except to the extent that the registrant specifically incorporates that information by reference.

* * * * *

Item 22. Information required in investment company proxy statement.

* * * * *

(b) * * *

(18) If a shareholder nominee or nominees are submitted to the Fund for inclusion in the Fund's proxy materials pursuant to § 240.14a-11 and the Fund is not permitted to exclude the nominee or nominees pursuant to the provisions of § 240.14a-11, the Fund must include in its proxy statement the disclosure required from the nominating shareholder or nominating shareholder group under Item 5 of § 240.14n-101 with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to paragraph (b)(18). The information disclosed pursuant to paragraph (b)(18) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933 (15 U.S.C. 77a et seq.), the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), or the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), except to the extent that the Fund specifically incorporates that information by reference.

(19) If a Fund is required to include a shareholder nominee or nominees submitted to the Fund for inclusion in the Fund's proxy materials pursuant to a procedure set forth under applicable state or foreign law or the Fund's governing documents providing for the inclusion of shareholder director nominees in the Fund's proxy materials, the Fund must include in its proxy statement the disclosure required from the nominating shareholder or nominating shareholder group under Item 6 of § 240.14n-101 with regard to the nominee or nominees and the nominating shareholder or nominating shareholder group.

Instruction to paragraph (b)(19). The information disclosed pursuant to paragraph (b)(19) of this Item will not be deemed incorporated by reference into any filing under the Securities Act of 1933 (15 U.S.C. 77a et seq.), the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.), or the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.), except to the extent that the Fund specifically incorporates that information by reference.

* * * * *

19. Amend Part 240 by adding an undesignated center heading and §§ 240.14n-1 through 240.14n-3 and § 240.14n-101 to read as follows:

REGULATION 14N: FILINGS REQUIRED BY CERTAIN NOMINATING SHAREHOLDERS

§ 240.14n-1 Filing of Schedule 14N.

(a) A shareholder or group of shareholders that submits a nominee or nominees in accordance with § 240.14a-11 or a procedure set forth under applicable state or foreign law, or a registrant's governing documents providing for the inclusion of shareholder director nominees in the registrant's proxy materials shall file with the Commission a statement containing the information required by Schedule 14N (§ 240.14n-101) and simultaneously provide the notice on Schedule 14N to the registrant.

(b)(1) Whenever two or more persons are required to file a statement containing the information required by Schedule 14N (§ 240.14n-101), only one statement need be filed. The statement must identify all such persons, contain the required information with regard to each such person, indicate that the statement is filed on behalf of all such persons, and include, as an appendix, their agreement in writing that the statement is filed on behalf of each of them. Each person on whose behalf the statement is filed is responsible for the timely filing of that statement and any amendments thereto, and for the completeness and accuracy of the information concerning such person contained therein; such person is not responsible for the completeness or accuracy of the information concerning the other persons making the filing.

(2) If the group's members elect to make their own filings, each filing should identify all members of the group but the information provided concerning the other persons making the filing need only reflect information which the filing person knows or has reason to know.

§ 240.14n-2 Filing of amendments to Schedule 14N.

(a) If any material change occurs with respect to the nomination, or in the disclosure or certifications set forth in the Schedule 14N (§ 240.14n-101) required by § 240.14n-1(a), the person or persons who were required to file the statement shall promptly file or cause to be filed with the Commission an amendment disclosing that change.

(b) An amendment shall be filed within 10 calendar days of the final results of the election being announced by the registrant stating the nominating shareholder's or the nominating shareholder group's intention with regard to continued ownership of their shares.

§ 240.14n-3 Dissemination.

One copy of Schedule 14N (§ 240.14n-101) filed pursuant to §§ 240.14n-1 and 240.14n-2 shall be mailed by registered or certified mail or electronically transmitted to the registrant at its principal executive office. Three copies of the material must at the same time be filed with, or mailed for filing to, each national securities exchange upon which any class of securities of the registrant is listed and registered.

§ 240.14n-101 Schedule 14N – Information to be included in statements filed pursuant to § 240.14n-1 and amendments thereto filed pursuant to § 240.14n-2.

Securities and Exchange Commission, Washington, D.C. 20549

Schedule 14N

Under the Securities Exchange Act of 1934

(Amendment No._)*

____

(Name of Issuer)

____

(Title of Class of Securities)

____

(CUSIP Number)

____

[ ] Solicitation pursuant to § 240.14a-2(b)(7)

[ ] Solicitation pursuant to § 240.14a-2(b)(8)

[ ] Notice of Submission of a Nominee or Nominees in Accordance with § 240.14a-11

[ ] Notice of Submission of a Nominee or Nominees in Accordance with Procedures Set Forth Under Applicable State or Foreign Law, or the Registrant's Governing Documents

*The remainder of this cover page shall be filled out for a reporting person's initial filing on this form, and for any subsequent amendment containing information which would alter the disclosures provided in a prior cover page.

The information required in the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act but shall be subject to all other provisions of the Act.

(1) Names of reporting persons: ___________________

(2) Mailing address and phone number of each reporting person (or, where applicable, the authorized representative): ___________________

(3) Amount of securities held that are entitled to be voted on the election of directors held by each reporting person (and, where applicable, amount of securities held in the aggregate by the nominating shareholder group), but including loaned securities and net of securities sold short or borrowed for purposes other than a short sale: ___________________

(4) Number of votes attributable to the securities entitled to be voted on the election of directors represented by amount in Row (3) (and, where applicable, aggregate number of votes attributable to the securities entitled to be voted on the election of directors held by group):

____

<u>Instructions for Cover Page</u>:

(1) Names of Reporting Persons – Furnish the full legal name of each person for whom the report is filed – i.e., each person required to sign the schedule itself – including each member of a group. Do not include the name of a person required to be identified in the report but who is not a reporting person.

(3) and (4) Amount Held by Each Reporting Person – Rows (3) and (4) are to be completed in accordance with the provisions of Item 3 of Schedule 14N.

Notes: Attach as many copies of parts one through three of the cover page as are needed, one reporting person per copy.

Filing persons may, in order to avoid unnecessary duplication, answer items on Schedule 14N by appropriate cross references to an item or items on the cover page(s). This approach may only be used where the cover page item or items provide all the disclosure required by the schedule item. Moreover, such a use of a cover page item will result in the item becoming a part of the schedule and accordingly being considered as "filed" for purposes of Section 18 of the Act or otherwise subject to the liabilities of that section of the Act.

SPECIAL INSTRUCTIONS FOR COMPLYING WITH SCHEDULE 14N

Under Sections 14 and 23 of the Securities Exchange Act of 1934 and the rules and regulations thereunder, the Commission is authorized to solicit the information required to be supplied by this Schedule. The information will be used for the primary purpose of determining and disclosing the holdings and interests of a nominating shareholder or nominating shareholder group. This statement will be made a matter of public record. Therefore, any information given will be available for inspection by any member of the public.

Because of the public nature of the information, the Commission can use it for a variety of purposes, including referral to other governmental authorities or securities self-regulatory organizations for investigatory purposes or in connection with litigation involving the Federal securities laws or other civil, criminal or regulatory statutes or provisions. Failure to disclose the information requested by this schedule may result in civil or criminal action against the persons involved for violation of the Federal securities laws and rules promulgated thereunder, or in some cases, exclusion of the nominee from the registrant's proxy materials.

General instructions to item requirements

The item numbers and captions of the items shall be included but the text of the items is to be omitted. The answers to the items shall be prepared so as to indicate clearly the coverage of the items without referring to the text of the items. Answer every item. If an item is inapplicable or the answer is in the negative, so state.

Item 1(a). **Name of registrant**

Item 1(b). **Address of registrant's principal executive offices**

Item 2(a). **Name of person filing**

Item 2(b). **Address or principal business office or, if none, residence**

Item 2(c). **Title of class of securities**

Item 2(d). **CUSIP No.**

Item 3. **Ownership**

Provide the following information, in accordance with Instruction 3 to § 240.14a-11(b)(1):

(a) Amount of securities held and entitled to be voted on the election of directors (and, where applicable, amount of securities held in the aggregate by the nominating shareholder group): ________.

(b) The number of votes attributable to the securities referred to in paragraph (a) of this Item: ________.

(c) The number of votes attributable to securities that have been loaned but which the reporting person:

(i) has the right to recall; and

(ii) will recall upon being notified that any of the nominees will be included in the registrant's proxy statement and proxy card: ________.

(d) The number of votes attributable to securities that have been sold in a short sale that is not closed out, or that have been borrowed for purposes other than a short sale: _______.

(e) The sum of paragraphs (b) and (c), minus paragraph (d) of this Item, divided by the aggregate number of votes derived from all classes of securities of the registrant that are entitled to vote on the election of directors, and expressed as a percentage: _______.

Item 4. Statement of Ownership from a Nominating Shareholder or Each Member of a Nominating Shareholder Group Submitting this Notice Pursuant to § 240.14a-11

(a) If the nominating shareholder, or each member of the nominating shareholder group, is the registered holder of the shares, please so state. Otherwise, attach to the Schedule 14N one or more written statements from the persons (usually brokers or banks) through which the nominating shareholder's securities are held, verifying that, within seven calendar days prior to filing the shareholder notice on Schedule 14N with the Commission and transmitting the notice to the registrant, the nominating shareholder continuously held the amount of securities being used to satisfy the ownership threshold for a period of at least three years. In the alternative, if the nominating shareholder has filed a Schedule 13D (§ 240.13d-101), Schedule 13G (§ 240.13d-102), Form 3 (§ 249.103 of this chapter), Form 4 (§ 249.104 of this chapter), and/or Form 5 (§

249.105 of this chapter), or amendments to those documents, reflecting ownership of the securities as of or before the date on which the three-year eligibility period begins, so state and incorporate that filing or amendment by reference.

(b) Provide a written statement that the nominating shareholder, or each member of the nominating shareholder group, intends to continue to hold the amount of securities that are used for purposes of satisfying the minimum ownership requirement of § 240.14a-11(b)(1) through the date of the meeting of shareholders, as required by § 240.14a-11(b)(4). Additionally, provide a written statement from the nominating shareholder or each member of the nominating shareholder group regarding the nominating shareholder's or nominating shareholder group member's intent with respect to continued ownership after the election of directors, as required by § 240.14a-11(b)(5).

Instruction to Item 4. If the nominating shareholder or any member of the nominating shareholder group is not the registered holder of the securities and is not proving ownership for purposes of § 240.14a-11(b)(3) by providing previously filed Schedules 13D or 13G or Forms 3, 4, or 5, and the securities are held in an account with a broker or bank that is a participant in the Depository Trust Company ("DTC") or other clearing agency acting as a securities depository, a written statement or statements from that participant or participants in the following form will satisfy § 240.14a-11(b)(3):

As of [date of this statement], [name of nominating shareholder or member of the nominating shareholder group] held at least [number of securities owned continuously for at least three years] of the [registrant's] [class of securities], and has held at least this amount of such securities continuously for [at least three years]. [Name of clearing agency participant] is a participant in [name of clearing agency] whose nominee name is [nominee name].

[name of clearing agency participant]

By: [name and title of representative]

Date:

If the securities are held through a broker or bank (e.g. in an omnibus account) that is not a participant in a clearing agency acting as a securities depository, the nominating shareholder or member of the nominating shareholder group must (a) obtain and submit a written statement or statements (the "initial broker statement") from the broker or bank with which the nominating shareholder or member of the nominating shareholder group maintains an account that provides the information about securities ownership set forth above and (b) obtain and submit a separate written statement from the clearing agency participant through which the securities of the nominating shareholder or member of the nominating shareholder group are held, that (i) identifies the broker or bank for whom the clearing agency participant holds the securities, and (ii) states that the account of such broker or bank has held, as of the date of the separate written statement, at least the number of securities specified in the initial broker statement, and (iii) states that this account has held at least that amount of securities continuously for at least three years.

If the securities have been held for less than three years at the relevant entity, provide written statements covering a continuous period of three years and modify the language set forth above as appropriate.

For purposes of complying with § 240.14a-11(b)(3), loaned securities may be included in the amount of securities set forth in the written statements.

Item 5. Disclosure Required for Shareholder Nominations Submitted Pursuant to § 240.14a-11

If a nominating shareholder or nominating shareholder group is submitting this notice in connection with the inclusion of a shareholder nominee or nominees for director in the registrant's proxy materials pursuant to § 240.14a-11, provide the following information:

(a) A statement that the nominee consents to be named in the registrant's proxy statement and form of proxy and, if elected, to serve on the registrant's board of directors;

(b) Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A (§ 240.14a-101), as applicable;

(c) Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required of a participant in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A (§ 240.14a-101), as applicable;

(d) Disclosure about whether the nominating shareholder or any member of a nominating shareholder group has been involved in any legal proceeding during the past ten years, as specified in Item 401(f) of Regulation S-K (§ 229.10 of this chapter). Disclosure pursuant to this paragraph need not be provided if provided in response to Item 5(c) of this section;

Instruction 1 to Item 5 (c) and (d). Where the nominating shareholder is a general or limited partnership, syndicate or other group, the information called for in paragraphs (c) and (d) of this Item must be given with respect to:

a. Each partner of the general partnership;

b. Each partner who is, or functions as, a general partner of the limited partnership;

c. Each member of the syndicate or group; and

d. Each person controlling the partner or member.

Instruction 2 to Item 5 (c) and (d). If the nominating shareholder is a corporation or if a person referred to in a., b., c. or d. of Instruction 1 to paragraphs (c) and (d) of this Item is a corporation, the information called for in paragraphs (c) and (d) of this Item must be given with respect to:

a. Each executive officer and director of the corporation;

b. Each person controlling the corporation; and

c. Each executive officer and director of any corporation or other person ultimately in control of the corporation.

(e) Disclosure about whether, to the best of the nominating shareholder's or group's knowledge, the nominee meets the director qualifications, if any, set forth in the registrant's governing documents;

(f) A statement that, to the best of the nominating shareholder's or group's knowledge, in the case of a registrant other than an investment company, the nominee meets the objective criteria for "independence" of the national securities exchange or national securities association rules applicable to the registrant, if any, or, in the case of a registrant that is an investment company, the nominee is not an "interested person" of the registrant as defined in section 2(a)(19) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(19)).

Instruction to Item 5(f). For this purpose, the nominee would be required to meet the definition of "independence" that is generally applicable to directors of the registrant and not any particular definition of independence applicable to members of the audit committee of the registrant's board of directors. To the extent a national securities exchange or national securities association rule imposes a standard regarding independence that requires a subjective determination by the board or a group or committee of the board (for example, requiring that the board of directors or any group or committee of the board of directors make a determination regarding the existence of factors material to a determination of a nominee's independence), the nominee would not be required to meet the subjective determination of independence as part of the shareholder nomination process.

(g) The following information regarding the nature and extent of the relationships between the nominating shareholder or nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant:

(1) Any direct or indirect material interest in any contract or agreement between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant (including any employment agreement, collective bargaining agreement, or consulting agreement);

(2) Any material pending or threatened legal proceeding in which the nominating shareholder or any member of the nominating shareholder group and/or the nominee is a party or a material participant, and that involves the registrant, any of its executive officers or directors, or any affiliate of the registrant; and

(3) Any other material relationship between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant not otherwise disclosed;

Note to Item 5(g)(3). Any other material relationship of the nominating shareholder or any member of the nominating shareholder group or nominee with the registrant or any affiliate of the registrant may include, but is not limited to, whether the nominating shareholder or any member of the nominating shareholder group currently has, or has had in the past, an employment relationship with the registrant or any affiliate of the registrant (including consulting arrangements).

(h) The Web site address on which the nominating shareholder or nominating shareholder group may publish soliciting materials, if any; and

(i) Any statement in support of the shareholder nominee or nominees, which may not exceed 500 words for each nominee, if the nominating shareholder or nominating shareholder group elects to have such statement included in the registrant's proxy materials.

Item 6. Disclosure Required by § 240.14a-18

If a nominating shareholder or nominating shareholder group is submitting this notice in connection with the inclusion of a shareholder nominee or nominees for director in the registrant's proxy materials pursuant to a procedure set forth under applicable state or foreign law, or the registrant's governing documents provide the following disclosure:

(a) A statement that the nominee consents to be named in the registrant's proxy statement and form of proxy and, if elected, to serve on the registrant's board of directors;

(b) Disclosure about the nominee as would be provided in response to the disclosure requirements of Items 4(b), 5(b), 7(a), (b) and (c) and, for investment companies, Item 22(b) of Schedule 14A (§ 240.14a-101), as applicable;

(c) Disclosure about the nominating shareholder or each member of a nominating shareholder group as would be required in response to the disclosure requirements of Items 4(b) and 5(b) of Schedule 14A (§ 240.14a-101), as applicable;

(d) Disclosure about whether the nominating shareholder or any member of a nominating shareholder group has been involved in any legal proceeding during the past ten years, as specified in Item 401(f) of Regulation S-K (§ 229.10 of this chapter). Disclosure pursuant to this paragraph need not be provided if provided in response to Item 6(c) of this section;

Instruction 1 to Item 6(c) and (d). Where the nominating shareholder is a general or limited partnership, syndicate or other group, the information called for in paragraphs (c) and (d) of this Item must be given with respect to:

a. Each partner of the general partnership;

b. Each partner who is, or functions as, a general partner of the limited partnership;

c. Each member of the syndicate or group; and

d. Each person controlling the partner or member.

Instruction 2 to Item 6(c) and (d). If the nominating shareholder is a corporation or if a person referred to in a., b., c. or d. of Instruction 1 to paragraphs (c) and (d) of this Item is a corporation, the information called for in paragraphs (c) and (d) of this Item must be given with respect to:

a. Each executive officer and director of the corporation;

b. Each person controlling the corporation; and

c. Each executive officer and director of any corporation or other person ultimately in control of the corporation.

(e) The following information regarding the nature and extent of the relationships between the nominating shareholder or nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant:

(1) Any direct or indirect material interest in any contract or agreement between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant (including any employment agreement, collective bargaining agreement, or consulting agreement);

(2) Any material pending or threatened legal proceeding in which the nominating shareholder or any member of the nominating shareholder group and/or nominee is a party or a material participant, involving the registrant, any of its executive officers or directors, or any

affiliate of the registrant; and

(3) Any other material relationship between the nominating shareholder or any member of the nominating shareholder group, the nominee, and/or the registrant or any affiliate of the registrant not otherwise disclosed; and

Instruction to Item 6(e)(3). Any other material relationship of the nominating shareholder or any member of the nominating shareholder group with the registrant or any affiliate of the registrant may include, but is not limited to, whether the nominating shareholder or any member of the nominating shareholder group currently has, or has had in the past, an employment relationship with the registrant or any affiliate of the registrant (including consulting arrangements).

(f) The Web site address on which the nominating shareholder or nominating shareholder group may publish soliciting materials, if any.

Item 7. Notice of Dissolution of Group or Termination of Shareholder Nomination

Notice of dissolution of a nominating shareholder group or the termination of a shareholder nomination shall state the date of the dissolution or termination.

Item 8. Signatures

(a) The following certifications shall be provided by the filing person submitting this notice pursuant to § 240.14a-11, or in the case of a group, each filing person whose securities are being aggregated for purposes of meeting the ownership threshold set out in § 240.14a-11(b)(1) exactly as set forth below:

I, [identify the certifying individual], after reasonable inquiry and to the best of my knowledge and belief, certify that:

(1) I [or if signed by an authorized representative, the name of the nominating

shareholder or each member of the nominating shareholder group, as appropriate] am [is] not holding any of the registrant's securities with the purpose, or with the effect, of changing control of the registrant or to gain a number of seats on the board of directors that exceeds the maximum number of nominees that the registrant could be required to include under § 240.14a-11(d);

(2) I [or if signed by an authorized representative, the name of the nominating shareholder or each member of the nominating shareholder group, as appropriate] otherwise satisfy [satisfies] the requirements of § 240.14a-11(b), as applicable;

(3) The nominee or nominees satisfies the requirements of § 240.14a-11(b), as applicable; and

(4) The information set forth in this notice on Schedule 14N is true, complete and correct.

(b) The following certification shall be provided by the filing person or persons submitting this notice in connection with the submission of a nominee or nominees in accordance with procedures set forth under applicable state or foreign law or the registrant's governing documents:

I, [identify the certifying individual], after reasonable inquiry and to the best of my knowledge and belief, certify that the information set forth in this notice on Schedule 14N is true, complete and correct.

Dated: ___________

Signature: ___________________

Name/Title: ______________________

The original statement shall be signed by each person on whose behalf the statement is filed or his authorized representative. If the statement is signed on behalf of a person by his authorized representative other than an executive officer or general partner of the filing person, evidence of the representative's authority to sign on behalf of such person shall be filed with the statement, provided, however, that a power of attorney for this purpose which is already on file with the Commission may be incorporated by reference. The name and any title of each person who signs the statement shall be typed or printed beneath his signature.

Attention: Intentional misstatements or omissions of fact constitute Federal criminal violations (see 18 U.S.C. 1001).

20. Amend § 240.15d-11 by revising paragraph (b) to read as follows:

§ 240.15d-11 Current reports on Form 8-K (§ 249.308 of this chapter).

* * * * *

(b) This section shall not apply to foreign governments, foreign private issuers required to make reports on Form 6-K (17 CFR 249.306) pursuant to § 240.15d-16, issuers of American Depositary Receipts for securities of any foreign issuer, or investment companies required to file reports pursuant to § 270.30b1-1 of this chapter under the Investment Company Act of 1940, except where such an investment company is required to file:

(1) Notice of a blackout period pursuant to § 245.104 of this chapter;

(2) Disclosure pursuant to Instruction 2 to § 240.14a-11(b)(1) of information concerning outstanding shares and voting; or

(3) Disclosure pursuant to Instruction 2 to § 240.14a-11(b)(10) of the date by which a nominating shareholder or nominating shareholder group must submit the notice required pursuant to § 240.14a-11(b)(10).

* * * * *

PART 249 – FORMS, SECURITIES EXCHANGE ACT OF 1934

21. The authority citation for Part 249 continues to read, in part, as follows:

Authority: 15 U.S.C. 78a et seq. and 7201 et seq.; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

22. Amend Form 8-K (referenced in § 249.308) by:

a. Adding a sentence at the end of General Instruction B.1;

b. Removing the phrase "Section 5.06" in the heading and adding in its place "Item 5.06"; and

c. Adding Item 5.08.

The additions read as follows:

Note: The text of Form 8-K does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 8-K

* * * * *

GENERAL INSTRUCTIONS

* * * * *

B. Events to be Reported and Time for Filing Reports

1. * * * A report pursuant to Item 5.08 is to be filed within four business days after the registrant determines the anticipated meeting date.

* * * * *

Item 5.08 Shareholder Director Nominations

(a) If the registrant did not hold an annual meeting the previous year, or if the date of this year's annual meeting has been changed by more than 30 calendar days from the date of the previous year's meeting, then the registrant is required to disclose the date by which a nominating shareholder or nominating shareholder group must submit the notice on Schedule 14N (§ 240.14n-101) required pursuant to § 240.14a-11(b)(10), which date shall be a reasonable time before the registrant mails its proxy materials for the meeting. Where a registrant is required to include shareholder director nominees in the registrant's proxy materials pursuant to either an applicable state or foreign law provision, or a provision in the registrant's governing documents, then the registrant is required to disclose the date by which a nominating shareholder or nominating shareholder group must submit the notice on Schedule 14N required pursuant to § 240.14a-18.

(b) If the registrant is a series company as defined in Rule 18f-2(a) under the Investment Company Act of 1940 (§ 270.18f-2 of this chapter), then the registrant is required to disclose in connection with the election of directors at an annual meeting of shareholders (or, in lieu of such an annual meeting, a special meeting of shareholders) the total number of shares of the registrant outstanding and entitled to be voted (or if the votes are to be cast on a basis other than one vote per share, then the total number of votes entitled to be voted and the basis for allocating such votes) on the election of directors at such meeting of shareholders as of the end of the most recent calendar quarter.

* * * * *

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Date: August 25, 2010

Commissioner Walter and Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3075 / August 25, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14021

In the Matter of

KYLE J. THOMPSON,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against Kyle J. Thompson ("Thompson" or the "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(f) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. Thompson is a resident of Salt Lake City, Utah, and is licensed with the State of Utah as an investment adviser representative. Thompson is president, chief compliance officer and a director of Thompson Consulting Inc. ("TCI") and was the principal trader of Apex Equity Options Fund, LP's ("Apex") and Premier Portfolio, LP's ("Premier") accounts.

2. On August 17, 2010, a final judgment was entered by consent against Thompson, permanently enjoining him from future violations of Sections 17(a)(2) and (3) of the Securities Act of 1933 in the civil action entitled Securities and Exchange Commission v. Thompson Consulting, Inc., et al., Civil Action Number 2:08-CV-171, in the United States District Court for the District of Utah.

3. The Commission's complaint alleged that TCI, a registered investment adviser, managed seven accounts including the Apex and Premier hedge funds. The Complaint further alleged that during the month of August 2007, Apex and Premier collapsed as a result of a high risk trading strategy implemented by TCI and its president and principal trader Kyle J. Thompson. The Complaint also alleged that the investment strategy TCI utilized during July and August 2007 was contrary to the much more conservative trading strategy TCI had presented to investors through Thompson. The Complaint further alleged that the trading strategy employed by Thompson involved a significantly higher degree of risk than the strategy presented to investors. According to the allegations in the Complaint, in August 2007, Apex and Premier lost virtually all value, declining from an aggregate net asset value of $53.8 million on July 31 to barely $200,000 by the end of August, resulting in an almost complete loss of the more than $50 million invested in the funds.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act, that Respondent Kyle J. Thompson be, and hereby is, barred from association with any investment adviser.

Any reapplication for association by Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Walter and
Commissioner Aguilar
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3074 / August 25, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14020

In the Matter of **E. SHERMAN WARNER,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against E. Sherman Warner ("Warner" or the "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose +of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(f) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. Warner is a resident of South Jordan, Utah, and, at the times relevant to the Complaint, was affiliated with Thompson Consulting, Inc. ("TCI") as an investment adviser. Warner participated in the solicitation of investors on behalf of Apex Equity Options Fund, LP ("Apex"). Warner was a trader of Apex's and Premier Portfolio, LP's ("Premier") account.

2. On August 17, 2010, a final judgment was entered by consent against Warner, permanently enjoining him from future violations of Sections 17(a)(2) and (3) of the Securities Act of 1933 in the civil action entitled Securities and Exchange Commission v. Thompson Consulting, Inc., et al., Civil Action Number 2:08-CV-171, in the United States District Court for the District of Utah.

3. The Commission's Complaint alleged that TCI, a registered investment adviser, managed seven accounts including the Apex and Premier hedge funds. During the month of August 2007, Apex and Premier collapsed as a result of a high risk trading strategy implemented by TCI and its president and principal trader Kyle Thompson ("Thompson") and in which Warner participated. The investment strategy TCI utilized during July and August 2007 was contrary to the much more conservative trading strategy TCI had presented to investors through Thompson and Warner. The Complaint further alleged that the trading strategy employed by Warner and Thompson involved a significantly higher degree of risk than the strategy presented to investors. In August 2007, Apex and Premier lost virtually all value, declining from an aggregate net asset value of $53.8 million on July 31 to barely $200,000 by the end of August, resulting in an almost complete loss of the more than $50 million invested in the funds.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act, that Respondent be, and hereby is barred from association with any investment adviser.

Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Walter and
Commissioner Aguilar
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3073 / August 25, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14019

In the Matter of

THOMPSON CONSULTING, INC.,

Respondent.

ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(e) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(e) of the Investment Advisers Act of 1940 ("Advisers Act") against Thompson Consulting, Inc. ("TCI" or the "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(e) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. TCI is a Utah corporation that has been registered with the Commission since May 2006 as an investment adviser. TCI manages the Apex Equity Options Fund, LP ("Apex") and the Premier Portfolio, LP ("Premier") fund, and charged both a performance fee of 25% of gain in the net asset value over the quarter, and a maintenance fee of 2% of assets under management for Apex and Premier.

2. On August 17, 2010, a final judgment was entered by consent against TCI, permanently enjoining it from future violations of Sections 17(a)(2) and (3) of the Securities Act of 1933 and Section 206(2) of the Advisers Act, in the civil action entitled Securities and Exchange Commission v. Thompson Consulting, Inc., et al., Civil Action Number 2:08-CV-171, in the United States District Court for the District of Utah.

3. The Commission's Complaint alleged that TCI, a registered investment adviser, managed seven accounts including the Apex and Premier hedge funds. The Complaint also alleged that during the month of August 2007, Apex and Premier collapsed as a result of a high risk trading strategy implemented by TCI and its president and principal trader Kyle J. Thompson. The Complaint also alleged that the investment strategy TCI utilized during July and August 2007 was contrary to the much more conservative trading strategy TCI had represented to investors and therefore operated as a fraud or deceit upon TCI's clients or prospective clients. According to the Complaint's allegations, as a consequence of the high risk trading strategy, Apex and Premier lost virtually all value, declining from an aggregate net asset value of $53.8 million on July 31 to barely $200,000 by the end of August 2007, resulting in an almost complete loss of the more than $50 million invested in the funds.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(e) of the Advisers Act, that the registration of Respondent Thompson Consulting, Inc. be, and here is, revoked.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Commissioner Walter and Commissioner Aguilar not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT ADVISERS ACT OF 1940
Release No. 3076 / August 25, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14022

In the Matter of **DAVID C. CONDIE,** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted pursuant to Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against David C. Condie ("Condie" or the "Respondent").

II.

In anticipation of the institution of these proceedings, Respondent submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Section 203(f) of the Investment Advisers Act of 1940, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. Condie is a resident of Salt Lake City, Utah, and, at the times relevant to the Complaint, was not licensed with the State of Utah as an investment adviser representative. Condie is an attorney and acted as in-house counsel to Thompson Consulting, Inc. ("TCI"). Condie conducted trades in Apex Equity Options Fund's ("Apex") and Premier Portfolio, LP's ("Premier") accounts.

2. On August 17, 2010, a final judgment was entered by consent against Condie, permanently enjoining him from future violations of Sections 17(a)(2) and (3) of the Securities Act of 1933 in the civil action entitled Securities and Exchange Commission v. Thompson Consulting, Inc., et al., Civil Action Number 2:08-CV-171, in the United States District Court for the District of Utah.

3. The Commission's Complaint alleged that TCI, a registered investment adviser, managed seven accounts including the Apex and Premier hedge funds. During the month of August 2007, Apex and Premier collapsed as a result of a high risk trading strategy implemented by TCI and its president and principal trader Kyle J. Thompson ("Thompson") and in which Condie participated. The investment strategy TCI utilized during July and August 2007 was contrary to the much more conservative trading strategy TCI had presented to investors through Thompson and Condie. The Complaint further alleged that the trading strategy employed by Condie and Thompson involved a significantly higher degree of risk than the strategy presented to investors. In August 2007, Apex and Premier lost virtually all value, declining from an aggregate net asset value of $53.8 million on July 31 to barely $200,000 by the end of August, resulting in an almost complete loss of the more than $50 million invested in the funds.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED:

Pursuant to Section 203(f) of the Advisers Act, that Respondent be, and hereby is barred from association with any investment adviser.

Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Schapiro and Commissioner Walter not participating

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION

INVESTMENT COMPANY ACT OF 1940
Release No. 29385 / August 25, 2010

In the Matter of	)
GE ASSET MANAGEMENT INCORPORATED GE INVESTMENT DISTRIBUTORS, INC. 3001 Summer Street Stamford, CT 06904-7900	)
File No. 812-13807	)

ORDER PURSUANT TO SECTION 9(c) OF THE INVESTMENT COMPANY ACT OF 1940 GRANTING A PERMANENT EXEMPTION FROM SECTION 9(a) OF THE ACT

GE Asset Management Incorporated ("GEAM") and GE Investment Distributors, Inc. ("GEID," collectively with GEAM, "Applicants") filed an application on July 27, 2010 and an amendment on July 30, 2010 requesting temporary and permanent orders under section 9(c) of the Investment Company Act of 1940 ("Act") exempting Applicants and any other company of which General Electric Company, Ionics, Inc., or Amersham plc is or hereafter becomes an affiliated person (together with Applicants, "Covered Persons") from section 9(a) of the Act with respect to an injunction entered by the United States District Court for the District of Columbia on July 30, 2010.

On July 30, 2010, the Commission simultaneously issued a notice of the filing of the application and a temporary conditional order exempting the Covered Persons from section 9(a) of the Act from July 30, 2010 until the Commission takes final action on the application for a permanent order (Investment Company Act Release No. 29374). The notice gave interested persons an opportunity to request a hearing and stated that an order disposing of the application would be issued unless a hearing was ordered. No request for a hearing has been filed, and the Commission has not ordered a hearing.

The matter has been considered and it is found that the prohibitions of section 9(a) as applied to the Applicants would be unduly and disproportionately severe and the conduct of the Applicants has been such as not to make it against the public interest or protection of investors to grant the permanent exemption from the provisions of section 9(a) of the Act.

Accordingly,

IT IS ORDERED, pursuant to section 9(c) of the Act, on the basis of the representations contained in the application filed by GEAM and GEID (File No. 812-13807), as amended, that Covered Persons be and hereby are permanently exempted from the provisions of section 9(a) of the Act, operative solely as a result of an injunction, described in the application, entered by the United States District Court for the District of Columbia on July 30, 2010.

By the Commission.

Elizabeth M. Murphy
Secretary

Florence E Harmon

By: Florence E. Harmon
Deputy Secretary

Commissioner Aguilar not participating

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62769 / August 26, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14023

In the Matter of **James E. Gansman** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against James E. Gansman ("Gansman" or "Respondent") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

> The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . attorney . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.2 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that

1. Gansman, age 49, resides in Butner, North Carolina, and is not currently employed. By 2006 and through at least 2007, he was an attorney licensed in the State of New York.

2. On May 29, 2008, the Commission filed a complaint against Gansman in SEC v. James E. Gansman, et al. (Civil Action No. 08-cv-4918). On August 16 , 2010, the court entered an order permanently enjoining Gansman, by consent, from future violations of Sections 10(b) and 14(e) of the Securities Exchange Act of 1934 and Rules 10b-5 and 14e-3 thereunder. Gansman was also ordered to pay $233,385 in disgorgement and $16,470 in prejudgment interest.

3. The Commission's complaint alleged, among other things, that from at least the summer of 2006 through the fall of 2007, Gansman, then a partner in Ernst and Young's Transactional Advisory Services Department, tipped a friend concerning the identities of at least seven different acquisition targets of clients who sought valuation services from his firm in connection with those acquisitions. Knowing the confidential nature of this information, the friend used the information to trade in the securities of the target companies.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent Gansmans's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

Gansman is suspended from appearing or practicing before the Commission as an attorney.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

UNITED STATES OF AMERICA
before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62773 / August 26, 2010

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3176 / August 26, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-14025

In the Matter of **STEPHEN D. CHANSLOR (CPA),** **Respondent.**	**ORDER INSTITUTING ADMINISTRATIVE PROCEEDINGS PURSUANT TO RULE 102(e) OF THE COMMISSION'S RULES OF PRACTICE, MAKING FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

I.

The Securities and Exchange Commission ("Commission") deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against Stephen D. Chanslor ("Respondent" or "Chanslor") pursuant to Rule 102(e)(3)(i) of the Commission's Rules of Practice.[1]

[1] Rule 102(e)(3)(i) provides, in relevant part, that:

The Commission, with due regard to the public interest and without preliminary hearing, may, by order, . . . suspend from appearing or practicing before it any . . . accountant . . . who has been by name . . . permanently enjoined by any court of competent jurisdiction, by reason of his or her misconduct in an action brought by the Commission, from violating or aiding and abetting the violation of any provision of the Federal securities laws or of the rules and regulations thereunder.

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, and the findings contained in Section III.3 below, which are admitted, Respondent consents to the entry of this Order Instituting Administrative Proceedings Pursuant to Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds that:

1. Chanslor, age 59, was a certified public accountant licensed to practice in the State of Texas until his license expired in June 1996. In January 1997, the Texas State Board of Public Accountancy issued an order suspending Chanslor's license based on his failure to fulfill continuing professional education requirements, and in January 2000, Chanslor's license was statutorily revoked. He served as Chief Financial Officer of Geotec, Inc. from April 2005 until October 2005.

2. Geotec was, at all relevant times, headquartered in Delray Beach, Florida. At all relevant times, Geotec's common stock was registered with the Commission and quoted in the Pink Sheets operated by Pink OTC Markets Inc.

3. In June 2009, the Commission filed a complaint against Chanslor in SEC v. Geotec, Inc., et al. (Civil Action No. 09-CV-80986). On July 28, 2010, the Court entered an order permanently enjoining Chanslor, by consent, from future violations of Sections 10(b) and 13(b)(5) of the Exchange Act and Rules 10b-5, 13a-14 and 13b2-1 thereunder, and aiding and abetting violations of Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder. The Court also imposed an officer-and-director bar and a civil penalty of $25,000 against Chanslor.

4. The Commission's complaint alleged, among other things, that Chanslor engaged in a fraudulent scheme which resulted in Geotec falsely reporting in its Commission filings that it had acquired millions of tons of coal. Chanslor signed Geotec's Form 10-QSB for the quarter ended March 31, 2005 and Form 10-QSB for the quarter ended June 30, 2005. In both filings, Geotec falsely represented it had acquired 3.7 million tons of coal and a permit had been obtained for the coal, and improperly recorded the coal as an $18.9 million asset. Geotec omitted to disclose that the coal was under a state receivership, rendering its claimed ownership tenuous at best, and Chanslor signed these filings, knowing they falsely stated there was a permit.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanction agreed to in Respondent Chanslor's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Chanslor is suspended from appearing or practicing before the Commission as an accountant.

B. After three years from the date of this order, Respondent may request that the Commission consider his reinstatement by submitting an application to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such an application must satisfy the Commission that Respondent's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; andor

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Respondent, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Respondent, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in the respondent's or the firm's quality control system that would indicate that the respondent will not receive appropriate supervision;

(c) Respondent has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Respondent acknowledges his responsibility, as long as Respondent appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Respondent to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Respondent's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-62784]

Notice Regarding the Requirement to Use eXtensible Business Reporting Language Format to Make Publicly Available the Information Required Pursuant to Rule 17g-2(d) of the Exchange Act

AGENCY: Securities and Exchange Commission ("Commission").

ACTION: Notice.

SUMMARY: The Commission is providing notice that the List of XBRL Tags for NRSRO's ("List of XBRL Tags") to be used for the ratings history disclosure requirements in paragraph (d) of Rule 17g-2 has been published on the Commission's Internet Web site. An NRSRO subject to the disclosure provisions of paragraph (d) of Rule 17g-2 shall make this information available in an interactive data file on its corporate Internet Web site in XBRL format using the List of XBRL Tags beginning no later than 60 days after the publication of this Notice in the Federal Register.

DATES: The date an NRSRO is required to begin using an XBRL format and the List of XBRL Tags for the purpose of Rule 17g-2(d) is [insert date that is 60 days after publication].

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, at (202) 551-5525; Thomas K. McGowan, Deputy Associate Director, at (202) 551-5521; Randall W. Roy, Assistant Director, at (202) 551-5522; Raymond A. Lombardo, Branch Chief, at (202) 551-5755; or Rebekah E. Goshorn, Attorney, at (202), 551-5514; Division of Trading and Markets, Securities and Exchange Commission; 100 F Street, NE, Washington, DC 20549-7010.

SUPPLEMENTARY INFORMATION:

The Credit Rating Agency Reform Act of 2006 ("Rating Agency Act")[1] defined the term "nationally recognized statistical rating organization" ("NRSRO") and provided authority for the Securities and Exchange Commission ("Commission") to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies. The regulations implemented by the Commission pursuant to this mandate include Securities Exchange Act of 1934 ("Exchange Act") Rule 17g-2,[2] which requires an NRSRO to make and retain certain records relating to its business and to retain certain other business records made in the normal course of business operations. The Commission adopted Rule 17g-2 and the amendments thereto, in part, under authority to require NRSROs to make and keep for specified periods such records as the Commission prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.[3]

On February 2, 2009, the Commission adopted amendments to its NRSRO rules imposing additional requirements on NRSROs in order to address concerns about the integrity of their credit rating procedures and methodologies.[4] Among other things, the rule amendments added new paragraph (a)(8) and paragraph (d) (now paragraph (d)(2)) to Rule 17g-2. Paragraph (a)(8) of Rule 17g-2 requires an NRSRO to make and retain a record for each outstanding credit rating it maintains showing all rating actions (initial rating, upgrades, downgrades, placements on watch for upgrade or downgrade, and withdrawals) and the date of such actions identified by the name of the security or obligor rated and, if applicable, the CUSIP for the rated security or

---

1 Public Law 109-291 (2006).

2 17 CFR 240.17g-2.

3 See Section 17(a)(1) of the Exchange Act (15 U.S.C. 78q(a)(1))

4 See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 59342 (February 2, 2009), 74 FR 6456 ("February 2009 Adopting Release").

the Central Index Key (CIK) number for the rated obligor.[5] Paragraph (d)(2) of Rule 17g-2 requires an NRSRO to make publicly available, on a six-month delayed basis, the ratings histories for a random sample of 10% of the credit ratings paid for by the obligor being rated or by the issuer, underwriter, or sponsor of the security being rated ("issuer-paid credit ratings") pursuant to paragraph (a)(8) of Rule 17g-2 for each class of credit rating for which the NRSRO is registered and has issued 500 or more issuer-paid credit ratings.[6]

Paragraph (d)(2) of Rule 17g-2 further requires that this information be made public on the NRSRO's corporate Internet Web site in eXtensible Business Reporting Language ("XBRL") format.[7] The rule provides that in preparing the XBRL disclosure, an NRSRO must use the List of XBRL Tags as specified on the Commission's Internet Web site.[8] The Commission established a compliance date of August 10, 2009 for this provision. On August 5, 2009, the Commission provided notice that an NRSRO subject to the disclosure provisions of paragraph (d) (now paragraph (d)(2)) of Rule 17g-2 could satisfy the requirement to make publicly available ratings history information in an XBRL format by using an XBRL format or any other machine-readable format, until such time as the Commission provides further notice.[9] The Commission today is providing notice that a List of XBRL Tags has been published on the Commission's Internet web site and that NRSROs shall commence publishing the information required by Rule 17g-2(d)(2) in XBRL format using the List of the XBRL Tags beginning no later than [insert date that is 60 days after publication].

---

5 17 CFR 240.17g-2(a)(8).

6 17 CFR 240.17g-2(d).

7 Id.

8 Id. The February 2009 Adopting Release specified a compliance date of 180 days after publication in the Federal Register.

9 See Securities Exchange Release No. 60451 (August 5, 2009) 74 FR 40246 (August 11, 2009) ("August 5, 2009 Notice").

On November 23, 2009, the Commission further amended Rule 17g-2 to add paragraph (d)(3), which requires that an NRSRO must make publicly available on its corporate Internet Web site ratings action histories for all credit ratings initially determined on or after June 26, 2007 in an interactive data file that uses a machine-readable format.[10] In the case of issuer-paid credit ratings, each new ratings action is required to be reflected in such publicly disclosed histories no later than twelve months after it is taken; in the case of ratings actions that are not issuer-paid, each new ratings action is required to be reflected no later than twenty-four months after it is taken.[11] Rule 17g-2(d)(3) provides that an NRSRO may use any machine-readable format to make this data publicly available until 60 days after the date on which the Commission publishes a List of XBRL Tags for NRSROs on its Internet Web site, at which point the NRSRO is required to make the information available in XBRL format using the List of XBRL Tags for NRSROs as published by the Commission on its Internet Web site.[12] Today, the Commission is providing notice that the List of XBRL Tags has been published on the Commission's Internet Web site.[13]

The publication of the List of XBRL Tags on the Commission's Internet Web site automatically triggers the 60 day time frame for compliance with Rule 17(g)(2)(d)(3) using an XBRL format. However, for purposes of establishing a uniform compliance date for Rule 17g-2(d)(2) and Rule 17g-2(d)(3), the Commission will require that NRSROs make the information

10 See Securities Exchange Release No. 61050 (November 23, 2009) 74 FR 63831 (December 4, 2009) ("November 2009 Adopting Release").

11 See November 2009 Adopting Release at 63834.

12 See November 2009 Adopting Release at 63834.

13 See List of XBRL Tags available at [website url].

required under Rule 17g-2(d)(3) available on its corporate website in XBRL format using the List of XBRL Tags beginning no later than [insert date that is 60 days after publication].

The relief provided by the August 5, 2009 Notice is superseded by this Notice.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

Date: August 27, 2010

Commissioner Aguilar
not participating

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62786 / August 27, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13862

In the Matter of **APOGEE TECHNOLOGY, INC.** **Respondent.**	**ORDER TERMINATING ADMINSTRATIVE PROCEEDINGS PURSUANT TO SECTION 12(j) OF THE SECURITIES EXCHANGE ACT OF 1934**

For good cause shown

It is hereby ORDERED that this administrative proceeding is terminated and that final judgment shall enter without the imposition of a remedy pursuant to Section 12(j) of the Exchange Act.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary

Chairman Schapiro not participating

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62798; File No. SR-FINRA-2010-032)

August 30, 2010

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Designation of a Longer Period for Commission Action on Proposed Rule Change Relating to Clearly Erroneous Transactions

On June 17, 2010, the Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 ("Act"),[2] and Rule 19b-4 thereunder,[3] a proposed rule change to amend its rules to set forth clearer standards and curtail its discretion with respect to breaking erroneous trades.

Section 19(b)(2) of the Act[4] provides that within thirty-five days of the publication of notice of the filing of a proposed rule change, or within such longer period as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, the Commission shall either approve the proposed rule change or institute proceedings to determine whether the proposed rule change should be disapproved. The 35th day for this filing was August 2, 2010.[5] The Commission had received an

1 15 U.S.C. 78s(b)(1).

2 15 U.S.C. 78a.

3 17 CFR 240.19b-4.

4 15 U.S.C. 78s(b)(2).

5 See Securities Exchange Act Release No. 62341 (June 21, 2010), 75 FR 36756 (June 28, 2010).

extension of time from FINRA until August 16, 2010.[6] The Commission extended this time period until August 30, 2010.[7] The Commission is again extending this time period.

The Commission finds it appropriate to designate a longer period within which to take action on the proposed rule change so that it has sufficient time to consider this proposed rule change, relating to the amendment of clearly erroneous execution rules to provide greater transparency and certainty to the process of breaking trades, and the comment letters that have been submitted in connection with the filing.

Accordingly, the Commission, pursuant to Section 19(b)(2) of the Act,[8] designates September 10, 2010, as the date by which the Commission should either approve or institute proceedings to determine whether to disapprove the proposed rule change.

By the Commission.

Florence E. Harmon

Florence E. Harmon
Deputy Secretary

---

6 FINRA submitted through the Commission's Electronic Form 19b-4 Filing System an extension of time period for Commission action through August 16, 2010.

7 See Securities Exchange Act Release No. 62729 (August 16, 2010), 75 FR 52384 (August 25, 2010).

8 15 U.S.C. 78s(b)(2).

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62797; File Nos. SR-BATS-2010-016; SR-BX-2010-040; SR-CBOE-2010-056; SR-CHX-2010-13; SR-EDGA-2010-03; SR-EDGX-2010-03; SR-ISE-2010-62; SR-NASDAQ-2010-076; SR-NSX-2010-07; SR-NYSE-2010-47; SR-NYSEAmex-2010-60; SR-NYSEArca-2010-58)

August 30, 2010

Self-Regulatory Organizations; BATS Exchange, Inc.; NASDAQ OMX BX, Inc.; Chicago Board Options Exchange, Incorporated; Chicago Stock Exchange, Inc.; EDGA Exchange, Inc.; EDGX Exchange, Inc.; International Securities Exchange LLC; The NASDAQ Stock Market LLC; National Stock Exchange, Inc.; New York Stock Exchange LLC; NYSE Amex LLC; NYSE Arca, Inc.; Notice of Designation of a Longer Period for Commission Action on Proposed Rule Changes Relating to Clearly Erroneous Transactions

On June 17, 2010, each of BATS Exchange, Inc. ("BATS"), NASDAQ OMX BX, Inc. ("BX"), Chicago Board Options Exchange, Incorporated ("CBOE"), Chicago Stock Exchange, Inc. ("CHX"), EDGA Exchange, Inc. ("EDGA"), EDGX Exchange, Inc. ("EDGX"), International Securities Exchange LLC ("ISE"), The NASDAQ Stock Market LLC ("Nasdaq"), National Stock Exchange, Inc. ("NSX"), New York Stock Exchange LLC ("NYSE"), NYSE Amex LLC ("NYSE Amex"), and NYSE Arca, Inc. ("NYSE Arca") (collectively, the "Exchanges") filed with the Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 ("Act"),[2] and Rule 19b-4 thereunder,[3] proposed rule changes to amend certain of their respective rules to set forth clearer standards and curtail their discretion with respect to breaking erroneous trades.

Section 19(b)(2) of the Act[4] provides that within thirty-five days of the publication of notice of the filing of a proposed rule change, or within such longer period as the Commission may designate up to ninety days of such date if it finds such longer period to be appropriate and

1 15 U.S.C. 78s(b)(1).

2 15 U.S.C. 78a.

3 17 CFR 240.19b-4.

4 15 U.S.C. 78s(b)(2).

publishes its reasons for so finding, the Commission shall either approve the proposed rule change or institute proceedings to determine whether the proposed rule change should be disapproved. The 35th day for the filings submitted by BATS, BX, CBOE, CHX, EDGA, EDGX, ISE, Nasdaq, NSX, NYSE, and NYSE Amex, was August 2, 2010.[5] The 35th day for the filing submitted by NYSE Arca was August 3, 2010.[6] The Commission had received an extension of time from the Exchanges until August 16, 2010.[7] The Commission extended this time period until August 30, 2010.[8] The Commission is again extending this time period.

The Commission finds it appropriate to designate a longer period within which to take action on the proposed rule changes so that it has sufficient time to consider these proposed rule changes, relating to the amendment of clearly erroneous execution rules to provide greater transparency and certainty to the process of breaking trades, and the comment letters that have been submitted in connection with these filings.

---

5 See Securities Exchange Act Release Nos. 62330 (June 21, 2010), 75 FR 36725 (June 28, 2010); 62331 (June 21, 2010), 75 FR 36746 (June 28, 2010); 62332 (June 21, 2010), 75 FR 36749 (June 28, 2010); 62333 (June 21, 2010), 75 FR 36759 (June 28, 2010); 62334 (June 21, 2010), 75 FR 36732 (June 28, 2010); 62336 (June 21, 2010), 75 FR 36743 (June 28, 2010); 62337 (June 21, 2010), 75 FR 36739 (June 28, 2010); 62338 (June 21, 2010), 75 FR 36762 (June 28, 2010); 62339 (June 21, 2010), 75 FR 36765 (June 28, 2010); 62340 (June 21, 2010), 75 FR 36768 (June 28, 2010); and 62342 (June 21, 2010), 75 FR 36752 (June 28, 2010).

6 See Securities Exchange Act Release No. 62335 (June 21, 2010), 75 FR 37494 (June 29, 2010).

7 The Exchanges submitted through the Commission's Electronic Form 19b-4 Filing System extensions of the time period for Commission action through August 16, 2010.

8 See Securities Exchange Act Release No. 62730 (August 16, 2010), 75 FR 52383 (August 25, 2010).

Accordingly, the Commission, pursuant to Section 19(b)(2) of the Act,[9] designates September 10, 2010, as the date by which the Commission should either approve or institute proceedings to determine whether to disapprove the proposed rule changes.

By the Commission.

Florence E. Harmon
Florence E. Harmon
Deputy Secretary

9 15 U.S.C. 78s(b)(2).

SECURITIES AND EXCHANGE COMMISSION

17 CFR PART 232

[RELEASE NO. 33-9137; File No. S7-18-10]

RIN 3235-AK70

EXTENSION OF FILING ACCOMMODATION FOR STATIC POOL INFORMATION IN FILINGS WITH RESPECT TO ASSET-BACKED SECURITIES

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Commission proposes to further extend the temporary filing accommodation in Rule 312 of Regulation S-T that allows static pool information required to be disclosed in a prospectus of an asset-backed issuer to be provided on an Internet Web site under certain conditions. Under this rule, such information is deemed to be included in the prospectus included in the registration statement for the asset-backed securities. This rule currently applies to filings with respect to asset-backed securities filed on or before December 31, 2010. We propose to amend this rule to extend its application for an additional eighteen months. Under the proposed extension, the rule would apply to filings with respect to asset-backed securities filed on or before June 30, 2012.

DATES: Comments should be received on or before [insert date 30 days after publication in the Federal Register].

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/proposed.shtml);
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-18-10 on the subject line; or
- Use the Federal Rulemaking Portal (http://www.regulations.gov). Follow the instructions for submitting comments.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-18-10. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (http://www.sec.gov/rules/proposed.shtml). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Jay Knight, Attorney-Adviser, Division of Corporation Finance, at (202) 551-3370, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-3720.

SUPPLEMENTARY INFORMATION: We are proposing an amendment to Rule 312[1] of Regulation S-T.[2]

I. BACKGROUND

In December 2004, we adopted new and amended rules and forms to address the registration, disclosure and reporting requirements for asset-backed securities ("ABS") under the Securities Act of 1933[3] (the "Securities Act") and the Securities Exchange Act of 1934[4] (the "Exchange Act").[5] As part of this rulemaking, we adopted Regulation AB,[6] a new principles-based set of disclosure items forming the basis for disclosure with respect to ABS in both Securities Act registration statements and Exchange Act reports. Compliance with the revised rules was phased in; full compliance with the revised rules became effective January 1, 2006. One of the significant features of Regulation AB is Item 1105, which requires, to the extent material, static pool information to be provided in the prospectus included in registration statements for ABS offerings.[7] While the disclosure required by Item 1105 depends on factors such as the type of underlying asset and materiality, the information required to be disclosed can be extensive. For example, a registrant may be required to disclose multiple performance

---

1 17 CFR 232.312.

2 17 CFR 232.10 et seq.

3 15 U.S.C. 77a et seq.

4 15 U.S.C. 78a et seq.

5 See Asset-Backed Securities, Release No. 33-8518 (Dec. 22, 2004) [70 FR 1506] (adopting release related to Regulation AB and other new rules and forms related to asset-backed securities) (hereinafter, the "2004 Adopting Release").

6 17 CFR 229.1100 et seq.

7 See Form S-1 (17 CFR 239.11) and Form S-3 (17 CFR 239.13) under the Securities Act. Static pool information indicates how groups, or static pools, of assets, such as those originated at different intervals, are performing over time. By presenting comparisons between originations at similar points in the assets' lives, the data allows the detection of patterns that may not be evident from overall portfolio numbers and thus may reveal a more informative picture of material elements of portfolio performance and risk.

metrics in periodic increments for prior securitized pools of the sponsor for the same asset type in the last five years.[8]

As described in the 2004 Adopting Release, in response to the Commission's proposal to require material static pool information in prospectuses for ABS offerings, many commentators representing both asset-backed issuers and investors requested flexibility in the presentation of such information. In particular, commentators noted that the required static pool information could include a significant amount of statistical information that would be difficult to file electronically on EDGAR as it existed at that time and difficult for investors to use in that format. Commentators accordingly requested the flexibility for asset-backed issuers to provide static pool information on an Internet Web site rather than as part of an EDGAR filing.[9] In response to these comments, we adopted Rule 312 of Regulation S-T, which permits, but does not require, the posting of the static pool information required by Item 1105 on an Internet Web site under the conditions set forth in the rule.[10] We recognized at the time that a Web-based approach might allow for the provision of the required information in a more efficient, dynamic and useful format than was currently feasible on the EDGAR system. At the same time, we explained that we continued to believe at some point for future transactions the information should also be submitted with the Commission in some fashion, provided investors continue to receive the information in the form they have requested. Accordingly, we adopted Rule 312 as a temporary filing accommodation applicable to filings filed on or before December 31, 2009.[11] We explained that we were directing our staff to consult with the EDGAR contractor, EDGAR

---

8 17 CFR 229.1105.

9 See 2004 Adopting Release, Section III.B.4.b.

10 17 CFR 232.312(a). Instead of relying on Rule 312, an issuer can include information required by Item 1105 of Regulation AB physically in the prospectus or, if permitted, through incorporation by reference from an Exchange Act report.

11 17 CFR 232.312(a); see also 2004 Adopting Release, Section III.B.4.b.

filing agents, issuers, investors and other market participants to consider how static pool information could be filed with the Commission in a cost-effective manner without undue burden or expense that still allows issuers to provide the information in a desirable format. We also noted, however, that it might be necessary, among other things, to extend the accommodation.[12]

On October 19, 2009, we proposed to extend the temporary filing accommodation until December 31, 2010.[13] We received four comment letters that addressed the proposed extension.[14] Two commentators expressed support for the Rule 312 filing accommodation and the proposed extension.[15] The ASF cited the strong preference among both its issuer and investor members for Web-based presentation of static pool information due to its efficiency, utility and effectiveness and the current lack of an adequate filing alternative.[16] The ABA Committees expressed their belief that the accommodation has been highly successful and of great value to investors.[17] Neither the ASF nor the ABA Committees was aware of any difficulties that investors or other market participants had locating, accessing, viewing or analyzing static pool information disclosed on a Web site.[18] For these reasons, among others, both the ASF and the ABA Committees requested that the filing accommodation be made

12 2004 Adopting Release, Section III.B.4.b.

13 Extension of Filing Accommodation for Static Pool Information in Filings With Respect to Asset-Backed Securities, Release No. 33-9074 (Oct. 19, 2009) [74 FR 54767] (the "2009 Static Pool Extension Proposing Release").

14 The public comments we received are available online at http://www.sec.gov/comments/s7-23-09/s72309.shtml.

15 See letters from the American Securitization Forum (the "ASF") and the Committee on Federal Regulation of Securities and the Committee on Securitization and Structured Finance of the Section of Business Law of the American Bar Association (the "ABA Committees").

16 See letter from ASF.

17 See letter from ABA Committees.

18 See letters from ASF and ABA Committees.

permanent or, in the alternative, extended for a longer period of time.[19] Two commentators, in contrast, did not support the extension and suggested the Commission should require structured disclosure using an industry standard computer language.[20]

On December 15, 2009, we adopted the proposed one-year extension of the filing accommodation.[21] In the adopting release for the extension ("2009 Static Pool Extension Adopting Release"), we noted the staff's experience with the rule and that a vast majority of residential mortgage-backed security issuers and a significant portion of ABS issuers in other asset classes have relied on the accommodation provided by the rule to disclose static pool information on an Internet Web site. We also noted that the staff of the Division of Corporation Finance was, at the time, engaged in a broad review of the Commission's regulation of ABS including disclosure, offering process, and reporting of ABS issuers and that along with this review, the staff of the Division of Corporation Finance was continuing to explore whether it was feasible to provide a filing mechanism for static pool information that fulfills the Commission's objectives. We also stated our belief that a proposal for a longer-term solution for providing static pool disclosure would be better considered together with other proposals on the regulations relating to the offer and sale of ABS.

---

19 Id. The ASF requested a five-year extension if the rule could not be made permanent and the ABA Committees requested an 18 to 24 month extension in such a case. Both the ASF and the ABA Committees expressed the belief that a permanent or longer extension would encourage continued use of the Web-based presentation by providing more of an incentive for issuers to make investments in developing and innovating Web sites for static pool disclosure. A longer extension would also, the ASF noted, give the Commission adequate time to consider alternatives.

20 See letters from Paul Wilkinson and EDGAR Online (noting they prefer immediately requiring static pool data be required in eXtensible Business Reporting Language (XBRL)). Subsequent to the 2009 Static Pool Extension Adopting Release (as defined below), we issued a comprehensive ABS proposal that included a proposed requirement to include asset-level information according to proposed standards and in a tagged data format using eXtensible Markup Language (XML). Additionally, we requested comment in the release as to whether static pool data should be required in an offering if there is an ongoing reporting requirement of asset-level data applicable to other pools of the sponsor of the same asset class.

21 Extension of Filing Accommodation for Static Pool Information in Filings With Respect to Asset-Backed Securities, Release No. 33-9087 (Dec. 15, 2009) [74 FR 67812] (the "2009 Static Pool Extension Adopting Release"); see also 2009 Static Pool Extension Proposing Release.

On April 7, 2010, we proposed significant revisions to Regulation AB and other rules regarding the offering process, disclosure and reporting for asset-backed securities (the "2010 ABS Proposals").[22] In that release, we proposed to revise Rule 312 to remove the temporary accommodation set to expire on December 31, 2010 for asset-backed securities to post the static pool information required by Item 1105 on an Internet Web site under conditions set forth in Regulation AB. In lieu thereof, under the proposal, ABS issuers would be required to file all static pool information on EDGAR; however, we proposed to allow that such information be filed in Portable Document Format (PDF).[23] Also, in lieu of providing the static pool information in the prospectus, we proposed to allow issuers to file the disclosure on Form 8-K and incorporate it by reference. The comment period for the 2010 ABS Proposals expired on August 2, 2010.

II. DISCUSSION OF PROPOSED AMENDMENT

We believe it is appropriate to further extend the filing accommodation provided by Rule 312, which is currently set to expire on December 31, 2010. As we stated in the 2009 Static Pool Extension Adopting Release, we believe a proposal for a long-term solution for providing static pool disclosure would be better considered together with other proposals to revise the regulations governing the offer and sale of ABS. On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act").[24] Among other things, the Act mandates a number of significant changes to the regulation of ABS offerings. In order to

---

22 Asset-Backed Securities, Release No. 33-9117 (Apr. 7, 2010) [75 FR 23328] (the "2010 ABS Proposing Release").

23 Portable Document Format (PDF) is a file format created by Adobe Systems in 1993 for document exchange. PDF captures formatting information from a variety of desktop publishing applications, making it possible to send formatted documents and have them appear on the recipient's monitor or printer for free as they were intended. To view a file in PDF format, you need Adobe Reader, an application distributed by Adobe Systems.

24 Pub. L. No. 111-203, 124 Stat. 1376 (July 21, 2010).

provide ample time for the Commission and its staff to give proper consideration to comments received on the 2010 ABS Proposals and in light of the changes to the regulations of ABS offerings that are mandated by the Act, we are proposing to extend the temporary filing accommodation set forth in Rule 312 of Regulation S-T for an additional eighteen months so that it would apply to filings with respect to ABS filed on or before June 30, 2012. Although we are proposing an eighteen-month extension of Rule 312, we may take action on the 2010 ABS Proposals, including the static pool proposal, at any time before the expiration of the proposed extension.

Under our proposed extension, the temporary filing accommodation set forth in Rule 312 of Regulation S-T would apply to filings with respect to ABS filed on or before June 30, 2012. During the proposed extension, the existing requirements of Rule 312 would continue to apply. Pursuant to these requirements, the registrant must disclose its intention to provide static pool information through a Web site in the prospectus included in the registration statement at the time of effectiveness and provide the specific Internet address where the static pool information is posted in the prospectus filed pursuant to Rule 424.[25] The registrant must maintain such information on the Web site unrestricted and free of charge for a period of not less than five years, indicate the date of any updates or changes to the information, undertake to provide any person without charge, upon request, a copy of the information as of the date of the prospectus if a subsequent update or change is made to the information and retain all versions of the information provided on the Web site for a period of not less than five years in a form that permits delivery to an investor or the Commission. In addition, the registration statement for the

[25] 17 CFR 230.424.

ABS must contain an undertaking pursuant to Item 512(l) of Regulation S-K[26] that the information provided on the Web site pursuant to Rule 312 is deemed to be part of the prospectus included in the registration statement.[27]

Request for Comment:

We request and encourage any interested person to submit comments regarding the proposed amendment described above. In particular, we solicit comment on the following questions:

- Is a further extension of the filing accommodation appropriate? What would be the consequences if the accommodation lapsed on December 31, 2010 and static pool information was required in an EDGAR filing beginning January 1, 2011?
- Should we consider proposed changes to static pool disclosure together with the other proposals outlined in the 2010 ABS Proposing Release? If not, why should we separate the static pool disclosure proposal from the rest of the ABS related proposals?
- Would the proposed eighteen-month extension present particular problems for investors? Would a shorter or more narrowly tailored extension address those concerns?
- Is an eighteen-month extension the appropriate length for an extension? Are there reasons for a shorter (12 month) or longer (24 month) extension?

III. PAPERWORK REDUCTION ACT

Rule 312 of Regulation S-T was adopted along with other new and amended rules and forms to address the registration, disclosure and reporting requirements for ABS under the

---

26 17 CFR 229.512(l).

27 17 CFR 232.312. As we indicated in the 2004 Adopting Release, if the conditions of Rule 312 are satisfied, then the information will be deemed to be part of the prospectus included in the registration statement and thus subject to all liability provisions applicable to prospectuses and registration statements, including Section 11 of the Securities Act [15 U.S.C. 77k]. 2004 Adopting Release, Section III.B.4.b.

Securities Act and the Exchange Act. In connection with this prior rulemaking, we submitted a request for approval of the "collection of information" requirements contained in the amendments and rules to the Office of Management and Budget ("OMB") in accordance with the Paperwork Reduction Act of 1995 ("PRA").[28] OMB approved these requirements.[29]

Item 1105 of Regulation AB[30] requires certain static pool information, to the extent material, to be provided in prospectuses included in registration statements for ABS offerings.[31] Rule 312 is a temporary filing accommodation that permits the posting of the static pool information required by Item 1105 on an Internet Web site under the conditions set forth in the rule.[32] The proposed amendment to Rule 312 further extends the existing temporary filing accommodation provided by the rule for an additional eighteen months. As is the case today, issuers may choose whether or not to take advantage of the accommodation. The conditions of Rule 312 remain otherwise unchanged. The disclosure requirements themselves, which are contained in Forms S-1 and S-3 under the Securities Act and require the provision of the information set forth in Item 1105 of Regulation AB, also remain unchanged. Therefore, the proposed amendment, if adopted, will not result in an increase or decrease in the costs and burdens imposed by the "collection of information" requirements previously approved by the OMB.

---

28 44 U.S.C. 3501 et seq.

29 The collections of information to which Rule 312 of Regulation S-T relates are "Form S-1" (OMB Control No. 3235-0065) and "Form S-3" (OMB Control No. 3235-0073).

30 17 CFR 229.1105.

31 See Form S-1 and Form S-3 under the Securities Act.

32 17 CFR 232.312(a).

IV. BENEFIT-COST ANALYSIS

In this section, we examine the benefits and costs of our proposed amendment. We request that commentators provide views and supporting information as to the benefits and costs associated with the proposal. We seek estimates of these costs and benefits, as well as any costs and benefits not already identified.

A. Benefits

We adopted the filing accommodation provided by Rule 312 of Regulation S-T because commentators requested flexibility in the presentation of required static pool information. Given the large amount of statistical information involved, commentators argued for a Web-based approach that would allow issuers to present the information in an efficient manner and with greater functionality and utility than might have been available if an EDGAR filing was required. We believe this greater functionality and utility has enhanced an investor's ability to access and analyze the static pool information because investors have been able to access static pool information in more user-friendly formats than was initially capable with filings on EDGAR and also removed the burden on issuers of duplicating the information in each prospectus as well as easing the burdens of updating such information.[33] As we discussed in the 2004 Adopting Release, since the information is deemed to be part of the prospectus included in the registration statement, the rule is designed to give investors access to accurate and reliable information.

By further extending the accommodation provided by Rule 312, these benefits to both issuers and investors would continue to apply. As noted in the 2009 Static Pool Extension Adopting Release, based on the staff's experience since Rule 312 became effective in 2006, the vast majority of residential mortgage-backed security issuers and a significant portion of ABS

[33] See Section I above and 2004 Adopting Release, Section V.D.

issuers in other asset classes have relied on the accommodation provided by the rule to disclose static pool information on an Internet Web site.[34] If we do not further extend the accommodation provided by Rule 312, static pool information would be required in EDGAR filings beginning on January 1, 2011. We believe this would result in costs for issuers as they attempt to adjust their procedures in a short period of time in order to present the information in a format acceptable to the EDGAR system and could result in costs to investors if the information filed on EDGAR was presented in a less useful format.

As indicated above, on April 7, 2010, we issued a release proposing to require the filing of static pool information on EDGAR at the same time we proposed other amendments addressing the disclosure, offering process and reporting of asset-backed issuers.[35] We believe that the proposed eighteen-month extension to the temporary filing accommodation contained in Rule 312 will benefit both investors and issuers by maintaining a consistent approach to the filing of static pool information while we and our staff consider comments received on the proposed amendment to static pool filing together with our other proposals regarding the offering and sale of asset-backed securities and in light of the changes to the regulations of ABS offerings that are mandated by the Dodd-Frank Act.

B. Costs

We do not believe an eighteen-month extension of the Rule 312 accommodation would impose any new or increased costs on issuers. In the Cost-Benefit Analysis section of the 2004 Adopting Release, we noted that asset-backed issuers electing the Web-based accommodation provided by Rule 312 would incur costs related to the maintenance and retention of static pool

---

[34] See Section I of the 2009 Static Pool Extension Adopting Release.

[35] See 2010 ABS Proposing Release.

information posted on a Web site and might also incur start-up costs.[36] While it is likely that certain of those costs would continue to impact asset-backed issuers that elect the Web-based approach during the extension period, we do not believe our proposed amendment would impose any new or increased costs for asset-backed issuers because it does not change any other conditions to the accommodation or the underlying filing and disclosure obligations. As a result of the proposed extension of the accommodation, asset-backed issuers would be able to continue their current practices for an additional eighteen months.

For investors, there may be costs associated with the static pool information not being electronically filed with the Commission. For example, when information is electronically filed with the Commission, investors and staff can access the information from a single, permanent, and centralized location, the EDGAR Web site. We think these costs are mitigated by the fact that ABS issuers relying on the Rule 312 accommodation must ensure that the prospectus for the offering contains the Internet Web site address where the static pool information is posted, the Web site must be unrestricted and free of charge, such information must remain on the Internet Web site for five years with any changes clearly indicated and the issuer must undertake to provide the information to any person free of charge, upon request, if a subsequent update or change is made. Furthermore, because the information is deemed included in the prospectus under Rule 312, it is subject to all liability provisions applicable to prospectuses and registration statements.

Investors and issuers may have incurred costs to adjust their processes in anticipation of the lapse of the Rule 312 accommodation and potential reversion to a requirement to file static pool information on EDGAR. In this case, benefits to investors or issuers of not having to

[36] See 2004 Adopting Release, Section V.D.

change their procedures regarding static pool reporting in a short time frame would be diminished by any costs already incurred in anticipation of the change. We believe such anticipatory action and any associated costs are minimal.

We request comment on the amount of any additional costs issuers or investors may incur as a result of the proposed amendment.

V. SMALL BUSINESS REGULATORY ENFORCEMENT FAIRNESS ACT

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"[37] we solicit data to determine whether the proposal constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in:

- An annual effect on the economy of $100 million or more (either in the form of an increase or a decrease);
- A major increase in costs or prices for consumers or individual industries; or
- Significant adverse effects on competition, investment or innovation.

We request comment on the potential impact of the proposed amendment on the U.S. economy on an annual basis, any potential increase in costs or prices for consumers or individual industries, and any potential effect on competition, investment or innovation. Commentators are requested to provide empirical data and other factual support for their views if possible.

VI. CONSIDERATION OF IMPACT ON THE ECONOMY, BURDEN ON COMPETITION AND PROMOTION OF EFFICIENCY, COMPETITION AND CAPITAL FORMATION

Section 2(b) of the Securities Act requires us, when engaging in rulemaking where we are required to consider or determine whether an action is necessary or appropriate in the public

[37] 5 U.S.C. 603.

interest, to also consider whether the action will promote efficiency, competition, and capital formation.

As discussed in greater detail above, Rule 312 of Regulation S-T was adopted as a temporary filing accommodation so that issuers of ABS could present static pool information on an Internet Web site. The proposed amendment to Rule 312 of Regulation S-T further extends its application for eighteen months. We are not proposing changes to the conditions of Rule 312 or to the disclosure obligations to which it applies. We do not believe that an eighteen-month extension would impose a burden on competition. We also believe the extension of the filing accommodation would continue to promote efficiency and capital formation by permitting ABS issuers to disclose static pool information in a format that is more useful to investors and cost-effective and not unduly burdensome for asset-backed issuers.

We request comment on whether the proposed amendment, if adopted, would promote efficiency, competition, and capital formation. Commentators are requested to provide empirical data and other factual support for their view to the extent possible.

VII. REGULATORY FLEXIBILITY ACT CERTIFICATION

The Commission hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed amendment contained in this release, if adopted, would not have a significant economic impact on a substantial number of small entities. The proposal relates to the disclosure requirements for ABS in Securities Act registration statements. Securities Act Rule 157[38] defines an issuer, other than an investment company, to be a "small business" or "small organization" if it had total assets of $5 million or less on the last day of its most recent fiscal year. As the depositor and issuing entity are most often limited purpose entities in an ABS transaction, we focused on the

[38] 17 CFR 230.157.

sponsor in analyzing the potential impact of the proposal under the Regulatory Flexibility Act. Based on our data, we only found one sponsor that could meet the definition of a small broker-dealer for purposes of the Regulatory Flexibility Act.[39] In addition, even if additional sponsors are small entities, the proposed amendment to Rule 312 would not have a significant economic impact on any such entities because it only extends a temporary filing accommodation that is currently in effect. Accordingly, the Commission does not believe that the extension, if adopted, would have a significant economic impact on a substantial number of small entities.

We encourage written comments on the Certification. Commentators are asked to describe the nature of any impact on small entities and provide empirical data to support the extent of the impact.

VIII. STATUTORY AUTHORITY AND TEXT OF THE PROPOSED AMENDMENT

The amendment described is being proposed under the authority set forth in Sections 6, 7, 10, 19 and 28 of the Securities Act of 1933 (15 U.S.C. 77f, 77g, 77j, 77s and 77z-3).

List of Subjects

17 CFR Part 232

Reporting and recordkeeping requirements, Securities.

TEXT OF THE PROPOSED AMENDMENT

For the reasons set out in the preamble, the Commission proposes to amend title 17, chapter II, of the Code of Federal Regulations as follows:

PART 232 – REGULATION S-T – GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS

1. The authority citation for part 232 continues to read, in part, as follows:

[39] This is based on data from Asset-Backed Alert. See Section IX of the 2010 ABS Proposing Release.

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s(a), 77z–3, 77sss(a), 78c(b), 78l, 78m, 78n, 78o(d), 78w(a), 78ll, 80a–6(c), 80a–8, 80a–29, 80a–30, 80a–37, and 7201 et seq.; and 18 U.S.C. 1350.

* * * * *

2. Amend §232.312 paragraph (a) introductory text by removing "December 31, 2010" and in its place adding "June 30, 2012" in the first sentence.

By the Commission.

Elizabeth M. Murphy

Elizabeth M. Murphy
Secretary

August 30, 2010

SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62802 / August 31, 2010

Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Moody's Investors Service, Inc.

I. Introduction

The Division of Enforcement has investigated whether Moody's Investors Service, Inc. ("MIS"), the credit rating business segment of Moody's Corporation ("Moody's"), violated the nationally recognized statistical rating organization ("NRSRO") registration provisions or the antifraud provisions of the federal securities laws.

In early 2007, an MIS rating committee meeting in Europe determined not to take rating action with respect to credit ratings that MIS previously had issued for certain constant proportion debt obligation ("CPDO") notes. Those ratings had been determined based in part on output from a model that contained an inadvertent coding error, the impact of which was 1.5 to 3.5 notches upward. The European rating committee refrained from taking responsive rating action in part because of concerns that doing so would negatively impact MIS's business reputation. In June 2007, MIS applied to be registered with the Commission as an NRSRO, pursuant to Section 15E(a)(1) of the Securities Exchange Act of 1934 ("Exchange Act") and Exchange Act Rule 17g-1(a). Accordingly, MIS furnished an NRSRO registration application that contained requisite information concerning the procedures and methodologies it used to determine credit ratings. The European rating committee's self-serving consideration of non-credit related factors in support of the decision to maintain the credit ratings constituted conduct that was contrary to MIS's procedures and policies used to determine credit ratings, described in the MIS application.

The Commission deems it appropriate and in the public interest to issue this Report of Investigation ("Report") pursuant to Section 21(a) of the Exchange Act.[1] This Report cautions NRSROs that deceptive conduct in connection with the issuance of credit ratings may violate the antifraud provisions of the federal securities laws. Further, recent legislative provisions expressly provide that federal district courts have jurisdiction over Commission enforcement actions alleging antifraud violations when conduct includes significant steps within the United States or has a foreseeable substantial effect within the United States. The Report also cautions NRSROs that they should take reasonable steps to assure themselves that statements made in their applications and reports submitted to the Commission are accurate and complete and that they are required to establish, maintain, and enforce effective internal controls over their procedures and methodologies for determining credit ratings.

[1] Section 21(a) of the Exchange Act authorizes the Commission to investigate violations of the federal securities laws and, in its discretion, "to publish information concerning any such violations." This Report does not constitute an adjudication of any fact or issue addressed herein.

II. Facts

A. Coding Error

In the summer of 2006, MIS began developing a methodology for rating notes issued by a newly created CPDO. CPDO issuers are special purpose vehicles that sell unfunded credit default swaps on corporate debt indices such as the iTraxx index in Europe and the CDX index in the United States. CPDO issuers use the proceeds of notes they sell to investors to purchase highly liquid instruments which, upon the occurrence of a contractually defined credit event, can be sold to pay the CPDO issuers' obligations under the unfunded credit default swaps. The indices referenced by the credit default swaps typically are re-balanced every six months to remove any issuers that have been downgraded below investment grade and replace them with investment grade issuers. Consequently, the unfunded credit default swaps typically are closed out and new transactions are entered into (i.e., the portfolio of credit default swaps is "rolled over") when the indices are rebalanced. When the unfunded credit default swaps are rolled over, the difference in the spread from the last roll over is multiplied by the amount of the CPDO issuer's leverage and is either a gain or a loss for the note holders. The structure relevant here was designed to pay a high fixed return over a ten-year lifespan, paying out a two percentage point spread above London Interbank Offered Rate or the purported risk-free rate.

Because CPDO notes were new instruments, MIS had no existing model for use in rating them. MIS created a model and in September 2006 gave the notes issued by the newly created CPDO issuer an Aaa credit rating. By the end of 2006, MIS had issued credit ratings for notes issued by an additional eleven CPDO issuers. The notes of all twelve CPDO issuers were marketed in Europe.

In January 2007, an MIS analyst in New York, assisting on a CPDO deal with a United States investment bank, was asked to determine why the MIS CPDO model was not generating the same output as the investment bank's model. Upon examination, the analyst discovered a coding error in the MIS model. The coding error upwardly impacted by 1.5 to 3.5 notches the model output used to determine MIS credit ratings for notes issued by eleven CPDO issuers. (The twelfth CPDO issuer was structured in such a way that the coding error did not affect the credit rating of its notes.) The CPDO notes with affected credit ratings had a combined notional value of just under $1 billion.

B. Rating Committee Conduct

MIS subsequently held several internal rating committee meetings in France and the United Kingdom to address the coding error. MIS corrected the coding error on February 12, 2007, but made no changes to the outstanding credit ratings for CPDO notes at that time. Internal e-mails show that committee members were concerned about the impact on MIS's reputation if it revealed an error in the rating model. A January 24, 2007, e-mail from a rating committee member to the Team Managing Director chairing the committee stated:

> In this particular case we seem to face an important reputation risk issue. To be fully honest this latter issue is so important that I would feel inclined at this stage to minimize ratings impact and accept unstressed parameters that are within

possible ranges rather than even allow for the possibility of a hint that the model has a bug.

On April 27, 2007, after additional analysis, the rating committee voted not to downgrade the affected credit ratings for the CPDO notes. The committee members felt that because the CPDO notes were generally performing well there would be no ostensible justification for downgrading the credit ratings, absent announcing the coding error. In declining to downgrade the credit ratings, the committee considered the following inappropriate non-credit related factors: (i) that downgrades could negatively affect Moody's reputation in light of ongoing negative media focus in Europe on Moody's Joint Default Analysis; (ii) that downgrades could impact investors who relied on the original ratings; and (iii) the desire not to validate the criticisms of Moody's ratings of CPDOs that had been made by a competitor and covered in the local media. The committee was comprised of senior level staff, including two Team Managing Directors, two Vice President-Senior Credit Officers, and a Vice President-Senior Analyst.

C. MIS Application

On September 29, 2006, the Credit Rating Agency Reform Act of 2006 was enacted. That Act, in relevant part, created Section 15E and amended Section 17 of the Exchange Act. Pursuant to Section 15E(a)(1), a credit rating agency that elects to be treated as an NRSRO "shall furnish to the Commission an application for registration . . . containing . . . the procedures and methodologies that the applicant uses in determining credit ratings." Exchange Act Rule 17g-1(a) requires an applicant to "furnish the Commission with an initial application on Form NRSRO . . . that follows all applicable instructions for the Form." Form NRSRO instructs an applicant to include an Exhibit 2, which must be "[a] description of the procedures and methodologies used in determining credit ratings."

Accordingly, Exhibit 2 to the MIS application provided the procedures and methodologies used by MIS to determine credit ratings and, among other things, stated therein that the "Relevant Credit Rating Process Policies" included the MIS "Core Principles for the Conduct of Rating Committees." The actions of the rating committee that evaluated the affected credit ratings for the CPDO notes did not comply with these Core Principles. Most notably, the Core Principles stated that "Moody's will not forbear or refrain from taking a rating action based on the potential effect (economic, political or otherwise) of the action on Moody's, an issuer, an investor, or any other market participant." The Core Principles also stated that "[i]n arriving at a Credit Rating, the [rating committee] will only consider analytical factors relevant to the rating opinion." Because the committee allowed concerns regarding the potential reputational impact on Moody's to influence decisions not to downgrade the affected CPDOs, the process did not comply with the procedures listed in the MIS application.

When MIS submitted its NRSRO application, the MIS Executive Vice President, Global Regulatory Affairs & Compliance certified the application, representing that "the information and statements in [the] Form . . . are accurate in all significant respects." At the time, the Executive Vice President was not aware of the European rating committee conduct that was contrary to the credit rating procedures listed in the MIS application.

On September 24, 2007, the Commission issued an Order granting registration of MIS as an NRSRO. Shortly thereafter, MIS made its Form NRSRO publicly available on its Web site.

D. Subsequent Actions

In January 2008, the European rating committee finally voted to begin downgrading the affected CPDO note credit ratings, citing factors such as widening spread movements and volatility of the iTraxx and CDX indices. By citing conditions that arose subsequent to its failure to downgrade the credit ratings, the committee effectively concealed its prior failure to downgrade. The committee did not reference or disclose the coding error.

Late in the day on May 20, 2008, the *Financial Times* published on its Web site an article that disclosed the coding error, citing internal Moody's documents that showed the error had been discovered by MIS almost a year earlier, and alleged that MIS had incorrectly awarded Aaa credit ratings to CPDO notes because of the error. When Moody's was contacted by reporters gathering information for the story, the company began an internal investigation into the coding error and the CPDO rating committee conduct. On July 1, 2008, a year and a half after the coding error had been discovered, and over a year after the European rating committee had declined to downgrade the credit ratings, Moody's issued a press release discussing the investigation results and stating that "some committee members considered factors inappropriate to the rating process when reviewing CPDO ratings following the discovery of the model error." Thereafter, MIS took personnel action with respect to management of the CPDO group and members of the committee, including termination of the Group Managing Director and two Team Managing Directors.

III. Discussion

The rating committee responsible for the credit ratings of the CPDO notes met in France and the United Kingdom. The CPDO notes were arranged by European banks and marketed in Europe. Members of the rating committee involved in the monitoring of CPDO ratings allowed concerns regarding Moody's reputation and other non-credit related considerations to influence decisions not to downgrade the affected CPDOs. The Commission cautions NRSROs that deceptive ratings conduct is unlawful under the antifraud provisions of the federal securities laws. Because of uncertainty regarding a jurisdictional nexus to the United States in this matter, the Commission declined to pursue a fraud enforcement action. The Commission notes that, in recently enacted legislation, Congress has provided expressly that federal district courts have jurisdiction over Commission enforcement actions alleging violations of the antifraud provisions of the Securities Act of 1933 or the Exchange Act involving "conduct within the United States that constitutes significant steps in furtherance of the violation, even if the securities transaction occurs outside the United States and involves only foreign investors" or "conduct occurring outside the United States that has a foreseeable substantial effect within the United States." Dodd-Frank Wall Street Reform and Consumer Protection (Dodd-Frank) Act, Pub. L. No 111-203, § 929P(b)(1), (2) (2010) (to be codified at 15 U.S.C. §§ 77v(c), 78aa(b)). NRSROs should expect that the Commission, where appropriate, will pursue antifraud enforcement actions, including pursuant to such jurisdiction.

Further, we conclude that, in early 2007, members of the European rating committee believed they could violate MIS's procedures without detection, and in fact the conduct did not come to light until the *Financial Times* contacted MIS about the error in the CPDO model and an investigation ensued. The Commission notes that recently enacted legislation amended the Exchange Act to require NRSROs to "establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings." Dodd-Frank Act, § 932(a)(2)(B) (to be codified at 15 U.S.C. § 78o-7(c)(3)). The legislation also provides that the Board of Directors of an NRSRO "shall oversee," among other things, "the establishment, maintenance, and enforcement of policies and procedures for determining credit ratings" and "the effectiveness of the internal control system with respect to policies and procedures for determining credit ratings." Dodd-Frank Act, § 932(a)(8) (to be codified at 15 U.S.C. § 78o-7(t)(3)).[2] The Commission further cautions NRSROs that they must implement and follow appropriate internal controls and procedures governing their determination of credit ratings, and must also take reasonable steps to ensure the accuracy of statements in applications or reports submitted to the Commission.

IV. Conclusion

This report serves to caution NRSROs that, where appropriate, the Commission will utilize recent legislative provisions granting jurisdiction for enforcement actions alleging otherwise extraterritorial fraudulent misconduct that involves significant steps or foreseeable effects within the United States. The Commission also cautions NRSROs that they should implement sufficient and requisite internal controls over policies, procedures, and methodologies used to determine credit ratings.

By the Commission.

[2] The Commission also notes that the legislation requires an annual examination by the Commission staff, which shall include a review, among other things, of whether an NRSRO "conducts business in accordance with [its] policies, procedures, and rating methodologies." Dodd-Frank Act, § 932(a)(8) (to be codified at 15 U.S.C. § 78o-7(p)(3)). Moreover, the legislation directs the Commission to require, by rule, that each NRSRO "include an attestation with any credit rating it issues affirming," among other things, "that the rating was based solely on the merits of the instruments being rated." Dodd-Frank Act, § 932(a)(8) (to be codified at 15 U.S.C. § 78o-7(q)(2)(F)).

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 62803 / August 31, 2010

INVESTMENT ADVISERS ACT OF 1940
Release No. 3077 / August 31, 2010

ADMINISTRATIVE PROCEEDING
File No. 3-13787

In the Matter of DAVID V. SIEGEL, Respondent.	ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS PURSUANT TO SECTION 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934 AND SECTION 203(f) OF THE INVESTMENT ADVISERS ACT OF 1940

I.

On February 22, 2010, the Securities and Exchange Commission ("Commission") instituted public administrative proceedings pursuant to Section 15(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") against David V. Siegel ("Respondent").

II.

In connection with these proceedings, Respondent Siegel has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except for the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Making Findings and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Section 203(f) of the Investment Advisers Act of 1940 ("Order"), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds[1] that:

Summary

Respondent failed reasonably to supervise Gary J. Gross with a view to preventing and detecting Gross's violations of the federal securities laws from approximately January 2004 through at least September 2006 while Respondent and Gross were associated with broker-dealer Axiom Capital Management, Inc. ("Axiom"). During this time period, Gross violated Section 17(a) of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by, among other things, making unsuitable investment recommendations, engaging in unauthorized transactions and churning customer accounts.

Respondent

1. **Siegel**, 52, is a resident of Parkland, Florida who was associated with Axiom Capital Management, Inc. ("Axiom"), a broker-dealer registered with the Commission, from May 2003 through January 2007 ("the relevant period"). During the relevant period, Siegel was Axiom registered representative Gary J. Gross' ("Gross") immediate supervisor. Siegel has Series 3, 4, 7, 15, 24, and 30 licenses.

Other Relevant Entity and Individual

2. **Axiom**, a Delaware corporation with its principal place of business in New York, New York, has been registered with the Commission since June 1990 as a broker-dealer and as an investment adviser from June 2004 through October 2006.

3. **Gross**, 57, is a resident of Boca Raton, Florida. Gross lived in Boca Raton while associated with Axiom from December 2002 until his termination in January 2007 as a result of the misconduct discussed below. During the relevant period, Gross held Series 7, 63 and 65 licenses.[2]

Background

4. Axiom hired Gross in December 2002 and established its first branch office in Boca Raton, Florida, mainly for Gross' use as an Axiom registered representative. Gross, Siegel, and a sales assistant ultimately comprised the office staff.

5. In May 2003, Axiom hired Siegel to manage its Boca Raton branch office and supervise Gross. During the relevant period, Siegel's compensation came from commissions he

[1] The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

[2] In September 2008, the Commission filed an action against Gross. SEC v. Gary J. Gross, Case No. 0881039-CIV-Marra/Johnson (S.D. Fla. September 22, 2008), Litigation Release No. 20732 (September 22, 2008).

generated from his own customers and a two percent override he received of the branch office's net commissions.

6. Due to customer complaints about Gross from his work at previous firms, the State of Florida required, among other things, that Axiom place Gross on strict supervision. During the relevant period, Gross remained subject to strict supervision until Axiom terminated him in January 2007.

7. While under Siegel's supervision, from early 2004 through at least September 2006, Gross implemented several abusive sales practices, including, among others, unauthorized trading for customers, churning customer investments, and making unsuitable investment recommendations to customers.

8. Beginning in early 2005 through at least April 2006, Gross sold millions of dollars worth of private placements and private issuances of public entities, commonly known as "PIPE" transactions (collectively "private placements") to his customers. The private placements were unsuitable recommendations for a portion of Gross' customers, who were elderly, retired with limited annual income, and risk-averse. Gross touted the purported profitability of private placements to some of his customers, but never disclosed the substantial risks, namely that these were illiquid investments in start-up ventures that greatly needed funding. Instead, Gross fraudulently described the private placements as riskless investments offered by high-quality companies. Given the customers' ages, financial circumstances, investment objectives and lack of prior experience in private placements, these investment recommendations and other subsequent investment recommendations Gross made between approximately January 2005 and September 2006 were unsuitable.

9. During the relevant period, Siegel was Gross' direct supervisor, but failed reasonably to supervise Gross with a view to preventing and detecting his violations of the federal securities laws.

10. Siegel failed to follow both Axiom's written supervisory procedures manual and an internal Axiom memorandum entitled "Heightened Supervision of Gary Gross" in relation to his supervision of Gross.

11. Siegel did not reasonably monitor Gross' orders for unauthorized transactions, failed to ensure that Gross' customers' margin use was suitable, and failed to review Gross' customers' private placement transactions and subsequent investments for suitability. Because he failed to follow firm procedures, Siegel failed to notice on numerous occasions when several of Gross' customers entered unsolicited orders to purchase or sell the same obscure securities, often on the same day. Siegel also failed to regularly use the firm's monthly Active Account Report, review monthly customer account statements, or take other reasonable action to monitor for churning by Gross.

12. Siegel profited from Gross' violations of the federal securities laws in the form of commissions he received based on Gross' commissions.

Violations

13. As a result of the conduct described above, Gross violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

14. As a result of the conduct described above, Siegel failed reasonably to supervise Gross within the meaning of Section 15(b)(4)(E), as incorporated by reference in Section 15(b)(6) of the Exchange Act, and Section 203(e)(6) of the Advisers Act with a view to preventing and detecting Gross' violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent Siegel's Offer.

Accordingly, pursuant to Section 15(b) of the Exchange Act and Section 203(f) of the Advisers Act, it is hereby ORDERED that:

A. Respondent Siegel be, and hereby is, barred from association in a supervisory capacity with any broker, dealer, or investment adviser.

B. Any reapplication for association by the Respondent will be subject to the applicable laws and regulations governing the reentry process, and reentry may be conditioned upon a number of factors, including, but not limited to, the satisfaction of any or all of the following: (a) any disgorgement ordered against the Respondent, whether or not the Commission has fully or partially waived payment of such disgorgement; (b) any arbitration award related to the conduct that served as the basis for the Commission order; (c) any self-regulatory organization arbitration award to a customer, whether or not related to the conduct that served as the basis for the Commission order; and (d) any restitution order by a self-regulatory organization, whether or not related to the conduct that served as the basis for the Commission order.

C. Respondent shall, within thirty (30) days of the entry of this Order, pay disgorgement of $10,600 and prejudgment interest of $35.33 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies David V. Siegel as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Glenn S. Gordon, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, 801 Brickell Avenue, Suite 1800, Miami, Florida 33131.

D. Respondent shall, within thirty (30) days of the entry of this Order, pay a civil money penalty in the amount of $15,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Such payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22312; and (D) submitted under cover letter that identifies David V. Siegel as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Glenn S. Gordon, Associate Regional Director, Division of Enforcement, Securities and Exchange Commission, 801 Brickell Avenue, Suite 1800, Miami, Florida 33131.

By the Commission.

Elizabeth M. Murphy
Secretary

Jill M. Peterson

By: Jill M. Peterson
Assistant Secretary