

Authored by Sarah A. Mussetter

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SEC ELIMINATES BROKER NON-VOTES FOR DIRECTOR ELECTIONS; PROPOSES NEW CORPORATE GOVERNANCE RULES

On July 1, 2009, the SEC approved (in a party line 3-2 vote) the NYSE's proposed rule change that eliminates broker discretionary voting in uncontested director elections.¹ This proposal was first advanced in October 2006 and resubmitted in February 2009.² The proposal regained momentum following the recent changes in leadership at the SEC and in response to criticism by institutional shareholders and shareholder activist groups directed at broker discretionary voting in director elections.

The effect of the rule change is that brokers will not be able to cast "uninstructed" votes in any director election. The amended rule will apply to proxy voting for stockholder meetings held on or after January 1, 2010. Because NYSE Rule 452 applies to brokers, the amendment applies not only to issuers listed on the NYSE, but also to issuers listed on other exchanges such as NASDAQ or NYSE Amex.

Previously, brokers delivering proxy materials to beneficial owners in advance of a stockholder meeting were required to request instruction from each beneficial owner on how to vote such owner's shares at the upcoming meeting. If no voting instructions had been received by the broker by the 10th day preceding the stockholder meeting, brokers were permitted to exercise discretionary voting authority with respect to those "uninstructed shares" on matters that the NYSE considers "routine." Prior to this amendment, that list of routine matters included uncontested director elections.

The rule change is intended to promote "better corporate governance and transparency of the election process," in line with many of the SEC's current initiatives. The cumulative effect of this rule change, taken together with the other ongoing SEC proxy access initiatives, remains to be seen; however, it appears to be substantial. With respect to the elimination of broker non-votes:

- This change will likely increase the cost of uncontested director elections while companies spend more resources on stockholder communication to successfully reach stockholders who may not be aware of the change in voting procedures and the effect of not returning their proxy.
- The loss of the broker discretionary vote in uncontested elections will likely make achieving a quorum more difficult where companies do not have at least one routine item on their ballot, such as ratification of the company's auditors.
- The rule change is expected to make it more difficult for companies with "majority voting" provisions to achieve a successful election, particularly for companies with a large retail investor base.
- The rule change can also be expected to increase the influence of institutional shareholders and shareholder activist groups in director elections.

HRO CONTACTS Commercial Law & Securities

Garth B. Jensen
Partner
garth.jensen@hro.com
303-866-0368

Mashenka Lundberg
Partner
mashenka.lundberg@hro.com
303-866-0616

Charles D. Maguire Jr.
Partner
charles.maguire@hro.com
303-866-0550

Richard R. Plumridge
Partner
rich.plumridge@hro.com
303-417-8504

Martha D. Rehm
Partner
martha.rehm@hro.com
303-866-0464

W. Dean Salter
Partner
dean.salter@hro.com
303-866-0245

Jennifer A. D'Alessandro
Senior Counsel
jennifer.d'alessandro@hro.com
303-866-0635

Sarah A. Mussetter
Associate
sarah.mussetter@hro.com
303-866-0623



Holme Roberts & Owen LLP.
Attorneys at Law

In addition to the approval of the NYSE Rule 452 amendments, the SEC proposed other rules relating to voting and corporate governance at its July 1, 2009 open meeting. One SEC proposal would require expedited disclosure of annual meeting voting results on a Form 8-K within four business days after the end of the meeting. In addition, the SEC proposed enhanced disclosure requirements relating to directors' experience, skills and background, as well as requirements to disclose more information regarding the selection of a particular management or leadership structure, such as the combination or separation of the board chair and chief executive officer positions. The SEC is currently soliciting comments on these proposals.

¹ See SEC Release No. 34-60215 (July 1, 2009) available at <http://www.sec.gov/rules/sro/nyse/2009/34-60215.pdf>.

² See SEC Release No. 34-59464 (Feb. 26, 2009) available at <http://www.sec.gov/rules/sro/nyse/2009/34-59464.pdf>.

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