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SEC's New Proxy Access: Practical Implications for Public Companies and Investors

September 15, 2010

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Today's Presenters



- **Phillip M. Goldberg**
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- **Patrick G. Quick**
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- **John K. Wilson**
Partner
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- **Richard H. Grubaugh**
Senior Vice President
D.F. King & Co., Inc.

Today's Presenters



- **Seth W. Hamot**
Managing Member
Roark, Rearden & Hamot Capital Management



- **Gail L. Hanson**
Deputy Executive Director
State of Wisconsin Investment Board



- **Steven H. Shapiro**
General Counsel and Corporate Secretary
Taylor Capital Group, Inc.

Agenda

- Overview of Key Provisions of the New Rules
- Panel Discussion on the Implications of the New Rules

Overview of Key Provisions of the New Rules

Proxy Access - Overview

- “Proxy access” - ability of shareholders to include their director nominees in the company’s proxy materials
- Dodd-Frank Act expressly authorized the SEC to issue rules to require public companies to provide proxy access
- SEC adopted final proxy access rules on August 25, 2010

When Proxy Access Will Apply

- SEC proxy access rules will be effective 60 days after their publication in the Federal Register (November __, 2010)
 - Not yet published
- Qualified shareholders seeking to include a nominee in a company's proxy materials must notify the company during a 30-day "window period" that generally runs from 150 to 120 calendar days before the anniversary of the date the company mailed its prior year's proxy materials
 - 120 days is the same as the Rule 14a-8 deadline
 - Companies that mailed their 2010 proxy materials on March __, 2010 or later will be subject to the rules for their 2011 annual meetings

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Companies Subject to Proxy Access

- Applies generally to all companies subject to the SEC's proxy rules, except:
 - Companies subject to the SEC's proxy rules solely because they have a class of debt registered under the Exchange Act
 - Companies subject to state or foreign laws or governing documents that prohibit their shareholders from nominating candidates for director
- Smaller reporting companies (generally, companies with a public float of less than \$75 million) will not be subject to the proxy access rules until 2014 annual meetings
- Compliance is mandatory for companies subject to the rules, regardless of any state or foreign law or provision in a company's governing documents that is more restrictive than SEC access rules
- Inclusion of a proxy access nominee alone will not constitute a proxy contest for purposes of the SEC's rules on contested proxy solicitations and will not require filing a preliminary proxy statement
 - For a company with a majority voting standard in uncontested director elections, inclusion of a proxy access nominee will likely trigger the application of a plurality voting standard to that election

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Eligible Shareholder or Group

- As of the date it provides notice of the nomination to the company, either individually or in the aggregate, holds at least 3% of the voting power of the company's securities entitled to vote for directors
- Has held the required amount of securities continuously for at least three years as of the date of notice of the nomination to the company
- Provides proof of ownership of the required amount
- Continues to hold the required amount used to satisfy the ownership threshold through the date of the shareholders meeting

Eligible Shareholder or Group

- Not holding securities with the purpose or effect of changing control or gaining a number of board seats that exceeds the maximum number of nominees that the company could be required to include under the proxy access rules
- Not part of another effort to elect directors, whether pursuant to another proxy access rule nomination or a solicitation or nomination effort outside of the proxy access rules, for the same election
- Does not have an agreement with the company regarding the nomination
- Provides notice to the company on a required form, Schedule 14N, and files the form with the SEC, during the 30-day window
- Includes the certifications required in the notice on Schedule 14N

Calculation of 3% Ownership Threshold

- Only securities as to which a shareholder holds both investment and voting power will count
- Securities that a shareholder merely has a right to acquire (e.g., through exercisable options or warrants) will not count
- Securities that have been loaned to a third party may be counted only if the shareholder has the right to recall the loaned securities and will do so upon being notified that any of its nominees will be included in the company's proxy materials
- Securities sold in a short sale that is not closed out during the relevant period and securities borrowed for purposes other than a short sale will not count
- Only securities subject to the proxy solicitation rules will be counted
- For companies with multiple classes of stock with unequal voting rights that vote together on the election of directors, voting power will be calculated based on the aggregate of all voting power
- For companies with multiple classes of stock that do not vote together in the election of all directors, voting power will be calculated on the basis of the voting power of the classes of stock that will vote together on the election of the person sought to be nominated

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Determination of Continuously Held

- Securities are treated as having been held continuously if a shareholder has held investment and voting power over the amount of securities continuously or, if the securities were loaned to a third party, the shareholder has had the right to recall the loaned securities and will do so upon being notified that any of their nominees will be included in the company's proxy materials
- Securities sold in a short sale during the period or borrowed for purposes other than a short sale will not be treated as continuously held

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Director Nominee Eligibility

- A nominee is eligible only if his/her candidacy and board membership will not violate federal or state law or national securities exchange requirements or if any violation may be cured in the time required
- A nominee also must meet the objective criteria for director independence of the applicable national securities exchange
- Nominees will not be required to meet:
 - A subjective independence determination by the board
 - Heightened independence standards applicable to audit committees members
 - Company independence requirements in addition to applicable national securities exchange requirements
- Nominees must not be party to any agreements with the company or its management regarding their nomination
- Nominees need not be independent from nominating shareholder
- But, a company need not seat an elected nominee who does not meet valid director qualifications

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Maximum Number of Nominees

- Limited to the greater of one or 25% of the total board seats, rounded down to the next whole number
 - Proxy access nominees elected by shareholders will continue to count against the 25% limit until the meeting at or after which their terms expire
 - Proxy access nominees included as company nominees under a compromise agreement will count against the 25% limit **only** if the nominating shareholder had provided notice of the nomination and filed it with the SEC before the company started communicating with the shareholder
 - Incumbent directors who were originally elected as proxy access nominees and are re-nominated by the company upon the expiration of their initial term will not count against the 25% limit

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Priority of Competing Nominations

- If more eligible proxy access nominees are submitted than the number of proxy access nominees that a company is required to include in its proxy materials, then:
 - Companies are required to include the nominee(s) of the nominating shareholder with the highest qualifying voting power percentage
 - If such nominating shareholder does not nominate the maximum number of directors allowed under the proxy access rules, the nominee(s) of the shareholder with the next highest qualifying voting power percentage will be included
 - Selection method continues until the company includes the maximum number of proxy access nominees or exhausts the list of eligible proxy access nominees

Notice on Schedule 14N

- Nominating shareholder or group must notify the company of its intent to submit a proxy access nominee by sending a Schedule 14N to the company and filing it with the SEC
- Schedule 14N requires, among other things, the following information that will also be included in the company's proxy materials:
 - 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
 - Disclosure about the shareholder or each member of the group and the nominee that would be required under the current rules for contested proxy solicitations
 - Whether the shareholder or any member of the group has been involved in certain legal proceedings during the past ten years

Notice on Schedule 14N

- Whether, to the best of the shareholder's or group's knowledge, the nominee meets the director qualifications set forth in the company's governing documents
- A statement that, to the best of the shareholder's or group's knowledge, the nominee meets the objective criteria for "independence" of the applicable national securities exchange
- The nature and extent of the relationships between the shareholder or group, the nominee, or the company or its affiliates
- Disclosure of any Web site address on which the shareholder or group may publish soliciting materials
- If the shareholder or group desires to include such a statement in the company's proxy statement, a statement in support of the proxy access nominee or nominees, which may not exceed 500 words per nominee

Application of Other Rules

- Proxy rule exemption for solicitations in connection with formation of a nominating group, presumably to reach the 3%
 - Schedule 14N filing required for written or oral
 - Restrictions on written communications
- Another exemption facilitates nominating shareholder/group solicitation activities to support their access nominees (or oppose company nominees) without filing and circulating more complete proxy materials
 - Some restrictions apply
 - Filing required for written materials
- Schedule 13D filing exception for activities solely in connection with a proxy access rules nomination to allow a shareholder/group to report on Schedule 13G

Requirements for Companies Receiving Schedule 14N Notice

- If a company determines that it may exclude the nominee(s) or supporting statement on technical grounds, it must so notify the nominating shareholder/group no later than 14 calendar days after the close of the nomination window period
 - A company must act at the outset as to all potential nominees
- Following the response of the shareholder/group and attempt to cure any deficiencies, if the company still intends to exclude the nominee(s) or statement of support, it must notify the SEC by at least 80 calendar days before it files its definitive proxy statement
 - There is a “no action” process to request SEC signoff
- If the company intends to include a proxy access nominee, it must notify the nominating shareholder or group no later than 30 calendar days before it files its definitive proxy statement

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Liability for Nominating Shareholders and Groups

- Nominating shareholders and groups, as well as proxy access nominees, will be subject to liability under the federal securities laws for materially misleading statements or omissions made in filings (including Schedule 14N) relating to proxy access nominations
 - A company will not be responsible for the accuracy of information that the nominating shareholder or group provides under the proxy access rules and that the company repeats in its proxy statement
 - Such information will also not be incorporated by reference into a company’s other securities filings unless the company specifically incorporates the information

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Expansion of Shareholder Proposals on Director Elections

- Rule 14a-8(i)(8) now allows shareholder proposals seeking to make proxy access more available by, for example, reducing required ownership threshold or the holding period or eliminating other required qualifications and representations
- Modified Rule 14a-8(i)(8) also clarifies that companies may exclude shareholder proposals if they do any of the following, which is now an exclusive list relating to the subject of director elections:
 - Disqualify a nominee who is standing for election;
 - Remove a director from office before the expiration of his or her term;
 - Question the competence, business judgment or character of a nominee or director;
 - Seek 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

Action Steps for Public Companies

- Be proactive with large shareholders
- Assess vulnerability
- Establish a response team
- Revise advance notice, majority voting and director qualification bylaws
- Revise director nomination procedures
- Review appropriate Board size
- Update proxy statement process timetable

Panel Discussion on the Implications of the New Rules

Questions & Answers

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