

another mechanism for determining that a proposal had been implemented would be necessary.

In addition to the issues regarding "implementation" discussed above, a nomination procedure triggering event premised upon the implementation of a security holder proposal would need to provide a means to inform security holders regarding the date by which implementation would be necessary and a discussion of the manner in which a proposal would be deemed to have been implemented. We believe that the most appropriate means for informing investors of a potential triggering event and its impact upon the proposed nomination procedure would be in the periodic report in which the company discloses the results regarding any matter that has been put to a vote of security holders.<sup>87</sup> Similarly, the most appropriate manner for determining implementation likely would be to have the board of directors of the company provide a representation on Exchange Act Form 8-K to the effect that it is the good faith judgment of those directors that the board has implemented the security holder resolution.

We are concerned that the inclusion of this third possible triggering event may affect a board's determination of how to react to or implement a security holder proposal or how to evaluate that proposal under state law. We believe, however, that an argument can be made that where a majority of votes cast by security holders favor a proposal and the board exercises its judgment not to implement it, there is an indication of ineffectiveness in, or dissatisfaction with, the proxy process. On the other hand, we are concerned that the link between the possible ineffectiveness of, or dissatisfaction with, a company's proxy process and this possible nomination procedure triggering event is more indirect than in the case of the two nominating process triggering events proposed today. A disagreement between a company's security holders and the board regarding its judgment on a proposal is a less directly linked indication of ineffectiveness relating to the director nomination and election process than a withhold vote on a director or a direct vote by security holders to provide for compliance with

the nomination procedure. This is particularly the case in light of the possible diversity of subjects that can be addressed in a security holder proposal. We also are concerned about the complexity and potential for dispute regarding whether proposals are implemented.

If we decide to adopt a nomination procedure that includes this third triggering event, non-implementation of a security holder proposal submitted as described above and adopted subsequent to January 1, 2004 could be a nominating procedure triggering event. Therefore, security holders and groups should be aware that, should we adopt a nomination procedure that includes a "non-implementation" trigger, they should provide evidence to the company that they satisfy the more than 1% and one-year thresholds when they submit their proposals.<sup>88</sup> As discussed above, we are proposing to amend Exchange Act Rule 14a-5 to require that a company identify in its proxy materials any proposal that would, if adopted, be a nominating process triggering event. We recommend that, pending final action on that proposal, companies make such an identification, both in their interest and in the interest of their security holders. Companies also should consider whether failure to make such an identification has any implications under Exchange Act Rule 14a-9.

#### c. Questions

C.1. As proposed, the new procedure would require a triggering event for security holders to be able to use the security holder nomination procedure. Is this appropriate? If so, are the proposed nomination procedure triggering events appropriate? Are there other events that should trigger the procedure? For example, should the following trigger the procedure: lagging a peer index for a specified number of consecutive years; being delisted by a market; being sanctioned by the Commission; being indicted on criminal charges; or having to restate earnings once or restate earnings more than once in a specified period? Should the election of a security holder nominee as a member of a company's board of directors be deemed a triggering event in itself that would extend the process by another year or longer period of time?

C.2. How long after a nomination procedure triggering event should security holders be able to use the

nomination procedure, if not two years, as is proposed (e.g., one year, three years, or longer)? Should there be other ways for the operation of the procedure to terminate at a company? If so, what other means would be appropriate? For example, should companies be able to take specified actions that would terminate operation of the nomination procedure? If so, what such actions would be appropriate?

C.3. As proposed, the nomination procedure could be triggered by withhold votes for one or more directors of more than 35% of the votes cast. Is 35% the correct percentage? If not, what would be a more appropriate percentage and why? Is it appropriate to base this trigger on votes cast rather than votes outstanding? If not, please provide a basis for the recommendation, including numeric data, where available. Is the percentage of withhold votes the appropriate standard in all cases? For example, what standard is appropriate for companies that do not use plurality voting? If your comments are based upon data with regard to withhold votes for individual directors, please provide such data in your response.

C.4. Should the nomination procedure triggering event related to direct access security holder proposals trigger the procedure only where a more than 1% holder or group submits the proposal? If not, what would be a more appropriate threshold, if any? For example, should the standards otherwise applicable for inclusion of a proposal under Exchange Act Rule 14a-8 apply? Should the required holding period for the securities used to calculate the security holder's ownership be longer than one year? If so, what is the appropriate holding period? Should that holding period be shorter than one year? If so, what is the appropriate holding period?

C.5. Are the existing methods under Exchange Act Rule 14a-8 sufficient to demonstrate that a proposal was submitted by a more than 1% security holder? If not, what other methods would be appropriate?

C.6. As proposed, a direct access security holder proposal could result in a nomination procedure triggering event if it receives more than 50% of the votes cast with regard to that proposal. Is this the proper standard? Should the standard be higher (e.g., 55%, 60%, or 65%)? Should the standard be based on votes cast for the proposal as a percentage of the outstanding securities that are eligible to vote on the proposal (e.g., 50% of the outstanding securities)?

C.7. Should direct access security holder proposals be subject to a higher resubmission standard than other Exchange Act Rule 14a-8 proposals? If

<sup>87</sup> For example, the company could describe the proposal in that Exchange Act report and discuss the operation of the proposed security holder nomination procedure in that situation, including the topic of the security holder proposal, the date by which the company would become subject to the security holder nomination procedure if it has not yet implemented the proposal, and any obligation of the company to continue to inform security holders regarding the implementation of the proposal.

<sup>88</sup> Security holders should use existing Exchange Act Rule 14a-8 procedures to provide evidence of ownership.