Final copy as sent

New York, N. Y.
October 12, 1942

Hon. Ganson Purcell
Chairman, Securities and Exchange Commission
Philadelphia, Pennsylvania

My dear Mr. Purcell:

At your invitation extended through Mr. Edgar Scott, President of the Philadelphia Stock Exchange, the undersigned met with you and members of your staff on October 7 and discussed the revision of proxy rules which has been proposed by the staff of the Securities and Exchange Commission. At the conclusion of that discussion you asked that we furnish the Commission with a memorandum of our views. This letter and the accompanying memorandum are in response to that request.

The proposed revision, dated August 19 last, was, it is understood, widely circulated to members of industry with a request for expressions of opinion. The impression was gained at the meeting in your office that there was a very wide response to that inquiry, and that a large percentage of the replies expressed disapproval of the proposed changes. This committee has not had the benefit of this general background of information, but, as an aid to the formulation of our views and the preparation of our memorandum, we have consulted many who submitted such opinions as well as other informed persons. In consequence, although we have acted solely at your request and therefore in no representative capacity, we know that the views herein expressed are those of a considerable number of persons in industry and we believe that they are those of a very large majority of such persons.

It is natural first to inquire whether there is a demand from stockholders for changes of the character proposed. The Commission's staff seems to imply that there is. Our relationship with stockholders should qualify us to answer this question. We believe that there is not and never has been any demand by stockholders that would warrant this action.

Of far greater moment, however, is the effect upon one of the main purposes of the Securities Exchange Act. This purpose is to encourage the dissemination of information to stockholders. The proposed revision would impair the character of the information which will be disseminated and decrease the number of companies which accept the obligation of dissemination.

An increasing number of companies are producing reports which laymen can read and understand and are thus encouraging the interest of stockholders in corporate affairs. Should the statutory liabilities be applied to the annual report, there is great danger that corporate officials will be constrained to turn the draftsmanship over to lawyers and technical men. What the report gains in technical compliance with rules, it will lose in readability. Should it thus become a dry and legalistic document, the revision will have impaired the very purpose which is ascribed to it. It would be far better to permit and encourage the natural evolution which corporate reports are now undergoing.

Of equal concern is the danger that adoption of these proposed rules would discourage companies from listing their securities on the exchanges of the nation and, perhaps, induce some companies, already so listed, to take their securities off the exchanges. Such a condition would, of course, tend to thwart the broad purposes of the Act. This would

be an unfortunate step backward.

Immediately, the adoption of the proposed proxy rule changes would be a great disservice to the best interests of a nation now engaged in an all-out struggle for its existence.

Industrial management, by its own choice and at the urging of its government, must now have but one primary test in passing judgment on all problems confronting it: Will it help to win the war?

Ignoring all other considerations in regard to the proposed new rules, we ask - How can these revisions possibly help to win the war?

We believe emphatically that adoption of the rules at this time cannot help, but must hinder production by an industry approaching total war effort; an industry in which swiftly dwindling manpower already is taxing its ability to perform its essential tasks.

Finally, it is our opinion that imposition of these new rules would be an assumption by the Securities and Exchange Commission of authority that has not been granted to it by Congress. If such regulations are considered necessary and desirable by the Commission, they are of such basic importance to the listed industrial corporations and to the millions of stockholding citizens of the nation that they should be promulgated only after hearings before the proper committee of Congress, and after legislation by Congress.

Detailed analysis of particular proposals would undoubtedly be mere reiteration of objections already expressed to the Commission by industry and others. However, in deference to your request, the statement of general objections is followed in the memorandum by a statement regarding certain of the rules which would have particularly unfortunate results.

In the light of all these considerations it is our earnest belief that none of the changes in the proxy rules as proposed by the Commission's staff should be made. It is our conviction that the Commissioners, devoted to the purposes of the Securities Exchange Act, can take no action which might risk the defeat of any of those purposes; nor, as patriotic administrators of an important department of our government, raise at this critical time a single barrier against the utmost utilization of the facilities of American industry.

Yours very truly,

LEWIS H. BROWN
President,
Johns-Manville Corporation

CHARLES S. GARLAND
Partner,
Alex. Brown & Sons

EDWARD HOPKINSON, JR.
Senior Partner, Drexel and Co. and
Chairman, Executive Committee
Baldwin Locomotive Works

EMIL SCHRAM
President,
New York Stock Exchange

ROBERT W. WHITE
Vice President,
Union Carbide & Carbon Company

MEMORANDUM REGARDING THE REVISION OF PROXY RULES PROPOSED BY THE STAFF OF THE SECURITIES AND EXCHANGE COMMISSION

Accompanying letter of October 12, 1942 by

Lewis H. Brown,
President, Johns-Manville Corporation

Charles S. Garland,
Partner, Alex. Brown & Sons, Baltimore

Edward Hopkinson, Jr.
Senior Partner, Drexel & Co.; and
Chairman, Executive Committee
Baldwin Locomotive Works

Emil Schram,
President, New York Stock Exchange

Robert W. White,
Vice President,
Union Carbide and Carbon Company

I

There are considerations of great gravity, general in their nature, which make the proposed revision of the proxy rules unwarranted and undesirable (or at the very least, ill-timed). To deal with these general objections seems much more important than to deal with the proposed revision in detail.

Part I of this memorandum, therefore, presents these general considerations under five main heads.

A. THERE IS NO DEMAND FROM STOCKHOLDERS THAT WOULD WARRANT THE PROPOSED CHANGES.

Information is entirely lacking of any significant demand from corporate stockholders for changes of the character proposed. Were there such a demand, one would expect to find it expressed in the pages of newspapers and magazines, in the letters of stockholders, on the floors of Congress, and in the other customary forms of public expression. It is apparent that no such demand exists.

Before the Commission could properly take action of so revolutionary a nature, it is suggested, there should be a positive showing that a substantial proportion of stockholders believe that the present rules are ineffective for their protection and that the proposed revision will make them effective.

B. THE PROPOSED CHANGES MIGHT NULLIFY THE EFFORTS OF AN INCREASING NUMBER OF COMPANIES TO PRODUCE MORE READABLE AND INFORMATIVE REPORTS AND TO ENCOURAGE THE INTEREST OF STOCKHOLDERS IN CORPORATE AFFAIRS

An increasing number of corporations have, especially during the

past decade, sought to give stockholders better information and to encourage a greater interest in corporate affairs. Thus, many annual reports have been made more readable and informative and show evidence of having been prepared by business men rather than by lawyers. Many companies have adopted a simplified form of financial statement. Not a few companies have set up departments which afford stockholders a readier means of inquiry through personal and sympathetic contact. Some companies have made especial effort to ascertain the wishes and attitudes of stockholders. Other companies have held regional meetings for the convenience of stockholders who are unable to attend the annual meeting.

It must be evident from these actions that corporations in general have no disagreement with the desire of the Securities and Exchange Commission that stockholders be better informed and have full opportunity to be articulate with respect to the affairs of their companies.

For the same reason, any proposal which would tend to defeat this good purpose cannot fail to alarm them. The proposed revision of the proxy rules, while not so intended, cannot avoid having this result.

The proposed revision would apparently extend the statutory liabilities to the annual report. Desirous though corporate officials may be to make reports more understandable by the use of simple language, this exposure cannot be ignored. Confronted by the possibility of penalty for inexact statement, they will be constrained to give the responsibility for draftsmanship over to lawyers and technical persons. These will be concerned more with literal compliance with the requirements of rules than with the need of stockholder understanding. The annual report, it is greatly to be feared, will thus become a dry and legalistic document.

In the face of possible penalties, managements are likely also to hesitate to include any matter which is not required by law. Since no rule applicable to corporations generally can be expected to evoke all the information which stockholders should have, both corporations and their stockholders would suffer.

Knowledge by a stockholder of the affairs of his company will be promoted, not so much by the quantity of information which is given him, as by its character and readability. Rules will never procure the latter qualities. They are being procured in increasing measure by natural evolution. It would be extremely unfortunate to interrupt that evolution, and no one could wish it less than the Commission.

C. ADOPTION OF THE REVISION WOULD PROVIDE A STRONG INCENTIVE TO CORPORATIONS TO TERMINATE THE LISTING OF THEIR SECURITIES.

A principal purpose of the Securities Exchange Act was to encourage the disclosure of essential information by as many corporations as possible. To this end, it is desirable that an ever greater number of corporate issues be listed on exchanges. Anything which tends to deter such listings, or to induce the termination of present listing, tends therefore to defeat one of the principal purposes of the Act.

The unlisted field is large. The number of listed companies is reported to be not much over 2,000. As compared with this, Moody's manual includes over 6,000 companies and it has been estimated that there are

30,000 issues traded in the over-the-counter market.

The onerous requirement of additional information and the added difficulty of obtaining stockholder representation at meetings would be important deterrents to listing. Beyond question, there is a point at which the obligations attached to listing can become so heavy as to start a migration away from listing. That point may be reached if the present proposals are adopted.

The advent of security regulation has been attended by many birth pangs. It would indeed be regrettable if some defeat of the broad purpose of the Act should prove them to have been in vain.

D. MOST OF THE CORPORATIONS AFFECTED BY THE PROPOSED REVISION ARE ENGAGED IN WAR WORK WHICH WOULD BE SERIOUSLY IMPEDED BY THE ONEROUS NATURE OF THE CHANGES. EVEN IF THE COMMISSION SHOULD THINK THE REVISION DESIRABLE, THE PARAMOUNT CONSIDERATIONS OF WAR WOULD REQUIRE THAT IT BE DEFERRED.

Corporations engaged in the war effort--and most of the listed corporations are so engaged--are finding their personnel problems tremendously complicated. This is true, not only of the production and operating end, but also of the clerical staffs--the accountants, the statisticians, the secretarial force--and the executives. As affected by matters such as proxy rules, this is principally in three ways:

(1) The greatly increased volume of clerical work, entailed both by increased production and by the multiplied requirements of government regulations and reporting, falls

upon clerical staffs whose level of competence is constantly being lowered by the demands of military service.

(2) The demands of military service have been particularly severe in depriving industrial concerns of the capable younger men upon whom executives have been accustomed to rely for the dispatch of a large portion of administrative detail.

(3) The demands upon the executives themselves have been increased manifoldly by the two foregoing results of the war; and also by the strict requirements of dealings with government, the production of new products, the changes in existing products made necessary by material shortages, the training of labor to new jobs, the reduced tolerances of time in production schedules, difficulties of purchase and transportation, the renegotiation of war contracts, and many other problems of equal import. In addition, many companies have permitted executives to devote full or part time to government service.

The overloaded staffs of industrial concerns are able even now to contribute less to the war effort than could be desired. This capacity for service may be decreased as drafts for military service grow greater and the demands for production heavier. The unavoidable effect is to delay matters which, though they may be of vital concern, are less immediately pressing, in favor of those which carry some immediate urgency, however superficial. It is unthinkable that such occasions of delay should be increased unless they are of truly significant import.

Yet this would be exactly the effect of approval of the proposed revision. Many of the matters thereby required can be dealt with only by the higher executives of a corporation, especially as neglect or error can lead to the imposition of serious penalties. These are the men most engrossed in the war effort. Many are so engrossed that they have been unable to study the proposed revision. Entirely apart from any regard for their individual comfort or convenience, the effect upon the war effort ought to give serious pause to any advocate of the revision.

This is scarcely the place to discuss the gravity of this war; but, accepting the statements of those most highly charged with its conduct, it presents so grave an aspect that even the smallest deterrents can mount up to serious impediments. As pointed out by our leaders, there is no smallest deviation from duty, no smallest neglect of responsibility, no slightest self-indulgence which can be tolerated in the face of our national peril. How, then, can any addition to the work of organizations which themselves are the machinery of war be justified except upon grounds of overwhelming necessity?

Such necessity does not appear in these proposals; and, in our opinion, the justification does not exist.

E. THE PROPOSED REVISION GOES BEYOND THE SCOPE OF THE AUTHORITY GRANTED BY CONGRESS. IF SUCH REGULATIONS ARE NECESSARY AND DESIRABLE, THEY SHOULD BE ESTABLISHED ONLY AFTER HEARINGS AND LEGISLATION BY CONGRESS.

Proposed Rules are not Limited to Disclosure

It has always been assumed that Section 14 of the Securities Exchange Act gave the Commission power to require disclosure in connection with the solicitation of proxies. Many of the new proposals have no relationship to disclosure, however, and are clearly designed to introduce new concepts into the conduct of corporate affairs.

One of the most alarming rules proposed to be grafted onto the principle of disclosure is the prohibition of solicitation of discretionary proxies* in connection with any proposed action. The purpose is to require (instead of permit) absentee voting by ballot. Clearly such a rule would regulate corporate voting rather than require any standard of disclosure.

Can the Commission properly adopt rules under Section 14 which are not confined to the disclosure principle?

Scope of Authority Granted by Congress

It seems clear that the abuse at which Section 14(a) was directed was the inadequacy of information given by those soliciting proxies. The Chairman of the Commission was quoted recently as testifying before the House Interstate and Foreign Commerce Committee as follows:

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*This subject is more fully discussed under "A" in Part II.

> "The Act also required corporations having Securities listed on national securities exchanges as well as those wishing to obtain such listing to file with the Commission and with the exchanges basic information and current corporate information with respect to their companies. They were also required under Section 14 to use adequate and truthful information in solicitation of proxies."

We are advised that the legislative history of Section 14(a) shows that an early draft included a brief description of the type of information which the Commission would be authorized to require. Although the section as enacted was very general in form, it is believed that this was due to the difficulty of prescribing precise standards rather than to any intent of Congress to give unlimited power to the Commission.

With so much doubt as to whether Congress intended to grant the scope of authority which is embraced in the proposed revision, there should be no action at least until hearings have been held by the proper committee of Congress and appropriate legislation enacted.

II

Part I of this memorandum has stated the general reasons why, in the opinion of the undersigned, the rules should not be changed as proposed. The objections to change appear sufficiently broad and compelling to dispel any necessity for detailed comment upon the individual proposals. However, in deference to the request of the Commission's Chairman, six of the principal proposals are discussed in this Part. Omission to comment upon other proposals is not to be taken as implication that they are considered unobjectionable. As to such, the authors feel obliged to repeat that the objections to the changes as a whole appear so weighty as to

indicate the doubtful propriety of adopting any of the proposals.

A. PROPOSAL THAT DISCRETIONARY PROXY CAN NOT BE SOLICITED IN CONNECTION WITH ANY PROPOSAL SUBMITTED TO STOCKHOLDERS FOR ACTION

Situation under Present Rules

Under the present rules the person solicited must be afforded an opportunity to specify in the form of proxy the action which such person desires to be taken on each matter intended to be acted upon, other than elections to office. It is usual for the proxy or proxy statement to contain a statement to the effect that, unless the shareholder otherwise indicates, the proxy will be voted as recommended by those making the solicitation. An examination of a great number of proxy forms and proxy statements shows that it is almost the universal, if not the universal, practice to provide for this discretion in voting if the shareholder does not desire to instruct the proxy holders.

Substance of Proposal

It is now proposed that each person solicited be "afforded an opportunity to specify by ballot a choice between approval or disapproval of each matter, or each group of related matters as a whole, which is intended to be acted upon pursuant to the proxy and the authority conferred as to each such matter or group of matters shall be limited to voting in accordance with the specification so made." (Emphasis supplied.)

Reason given by Commission's Staff for Suggested Change

> "The present form of proxy rules requires a ballot vote on all proposals submitted to stockholders for action. While the ballot form has become familiar to stockholders during a period of approximately four years, some managements have failed to follow the general practice, and have adopted procedures which encourage signature in blank rather than execution of the ballot. Under the present rules, a number of managements have drafted proxies so that the failure of a security holder to indicate how he desired his vote cast on a particular proposal vested authority in the management to vote the proxy in support of its position on the proposal. Many investors have commented that management should be permitted to vote only those proxies specifically marked. It is proposed that this suggestion be adopted as part of the amended rules."

Objections to the Proposal

1. Legal objection

This proposed change does not relate to the disclosure of information but is an effort to effect a substantial change in the method of conducting corporate affairs. If adopted, the proxy would be converted, as to all matters to be acted on at the meeting other than the election of directors, into a final ballot. The proxy (as it has always been known in the past) is an instrument executed by a shareholder, giving another person or persons authority to represent him at a shareholders' meeting. The persons vested with such authority are those in whom the shareholder has confidence and to whom he may be, not merely willing, but anxious to entrust discretion. Definitive action on corporate affairs has hitherto been taken at the meeting. By the proposal the proxy would be changed so that the authority of the proxy holders would cease and they would merely submit the proxy form to be counted by the tellers at the meeting. The vote itself would already have been taken.

We wonder whether Congress intended to delegate to the Commission power to make a rule of this nature. In any event, it would seem to a

layman that no change such as this one, which, in effect, requires a ballot by mail, should be undertaken by the Commission in the absence of clear Congressional authority.

2. The Proposed Change would make it Impossible for Corporations to bring about Necessary Changes in their Corporate Structure.

Under State statutes, and under charter and by-law provisions, the consent of a certain number or percentage of shareholders (often two-thirds or three-fourths) is necessary in order to mortgage the property of a corporation, issue convertible obligations, increase the amount of capital stock, change provisions of the charter, change provisions of the by-laws, etc. Even with the use of proxies in the present form it has been difficult for corporations to get the requisite proxies to effect such actions, and it is the almost unanimous opinion of corporate executives that it would be impossible to do so under the proposed revision. Under the existing rules which permit a shareholder to instruct his proxy holder with respect to matters to be acted upon at the meeting, corporations have found that a large proportion of shareholders do not exercise this right. This is partly because many of the matters submitted to shareholders are of a legal or highly technical nature, partly because shareholders expressly wish to vest discretion in the proxy holders, and partly because of carelessness or inattention in filling out proxies. As an example of the effect of this proposal, companies with charter restrictions upon mortgaging property will find it difficult if not impossible to do the financing which may be needed to increase war production.

It is even to be feared that the cumulative effect of this proposal, of the difficulties in communicating with shareholders whose affairs have been disrupted by service in the armed forces and otherwise, and of

the numerous other proposals which would increase the difficulty of obtaining valid proxies*, would be to make it impossible for many corporations to meet the bare quorum requirements for holding meetings, and to persuade managements of the futility of even attempting to hold meetings.

3. Reason given by Commission's Staff Not Valid

The reason given for the proposal is that, although the present rules require corporations to give shareholders an opportunity to indicate their wishes, "some managements have failed to follow the general practice and have adopted procedures which encourage signature in blank rather than execution of the ballot". It is further stated that a "number of managements have drafted proxies so that the failure of a security holder to indicate how he desired his vote cast on a particular proposal vested authority in the management to vote the proxy in support of its position on the proposal". The implication is that some managements have been violating the spirit of the existing rules. The fact is that all managements provide for a discretionary proxy in the absence of expression of desire, and that this violates neither the letter nor the spirit of the present rules. The granting of a discretionary proxy is a right and privilege which shareholders themselves want, since the past has shown that only thus can their corporations operate effectively.

Recommendation

Under the existing rules management must call the attention of

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*Examples are the requirement that shareholders must in effect be invited to write comments on their proxies, which, if done, will largely result in invalidating them; the requirement of furnishing a voluminous report of matters that can be outlined only in legalistic and unreadable language; and the requirement that the proxy, if attached to the proxy statement, must appear at the end of such material, so that only those who complete the arduous task of reading will find the proxy.

stockholders to matters to be taken up at the meeting and must give the shareholder an opportunity to indicate the manner in which he wishes to have his shares voted on such matters. The Commission can, under its existing rules, compel a clear statement of facts. If, with all the facts before him, the shareholder wishes to vest discretionary authority in his attorneys, he should not be prohibited from doing so.

It is strongly recommended that this proposed change not be incorporated into the proxy rules. If adopted it would greatly interfere with the effective functioning of corporations, and seriously prejudice the war effort.

B. PROPOSAL THAT COMMISSION ASSUME JURISDICTION OVER FORM OF ANNUAL REPORT

Substance of Proposal

Ten days prior to the solicitation of proxies for a meeting at which directors are to be elected, the corporation would be required to submit to the Commission, and subsequently send to shareholders, a statement containing the following information:

> "(1) Outline the business activities of the issuer and its subsidiaries during the last fiscal year, including: a description of material changes in the character of the business; material acquisitions and dispositions of subsidiaries and other interests and property; material acquisitions and dispositions of securities of the issuer and its subsidiaries; material changes in charters, indentures, or other instruments affecting the rights of security holders; transactions involving the granting or exercise of options, the operation of bonus, profit sharing, pension, retirement and other remuneration plans; material litigation involving the issuer or its

subsidiaries or any director or officer of the issuer or its subsidiaries; actions taken by the management regarding increases and decreases of management compensation, and the actions taken with respect to labor relations with employees.

"(2) Furnish such consolidated or unconsolidated financial statements of the issuer and its subsidiaries, on a comparative basis, as will clearly disclose the financial condition of the issuer and its subsidiaries as of the end of the last two fiscal years of the issuer and the results of the operations of the issuer and its subsidiaries for such years. Such financial statements shall be certified by an independent public or independent certified public accountant unless it is impracticable to obtain such a certification because of the time and expense involved or unless the issuer is not required to file regular annual certified statements with the Commission."

Situation under Present Rules

The information required by this proposal is not required under the existing rules.

Reason given by Commission's Staff for Making Proposal

The reason given for proposing this rule is that "The substantial nature of the changes which have occurred in the business of listed corporations during the period of adjustment to war production makes it essential that stockholders be informed of such changes."

Objections to Proposed Changes

1. Reason given by Commission's Staff for requiring change not valid

It would seem that the reasons given for this proposal have no relevancy to most of the detail to be required, and that that portion of the information which does relate to "adjustment to war production" would get no further than the censors.

2. The inclusion of this material would result in the proxy statement material not being read.

Corporate managements have found that, if a large body of material is submitted to shareholders, little if any of it is read. Managements which have studied the desires of shareholders find that they want brief statements which can easily be read and comprehended. Much of the material which corporations would have to furnish by this proposal would necessarily be technical in nature and not informative to many stockholders. This would constitute a step backward in proper shareholder relations and would defeat one of the principal purposes of the Securities Exchange Act.

3. Preparation and mailing of material would involve unjustifiable expense and burden to already over-burdened personnel

The additional time and expense consumed in the preparation of material of the nature required by this proposal would be large. Apparently the material would approach the amount required in prospectuses used in connection with public offerings. The greatest burden would fall on corporations which had converted their plants to war production; and the burden would be twofold: upon the already depleted and overworked personnel and upon executives compelled to leave war duties, become acquainted with the new rules, and attempt to prepare statements complying with them. The serious import of the proposals may not be realized by many executives until they find themselves compelled to divert weeks of time from war effort in order to assemble and prepare, in form which will protect them from the criminal penalties to which any violation of the rules subjects them, the maze of information required by the proposed revision.

4. Many corporations could not prepare financial statements within time permitted

Many corporations hold annual meetings within a short time after the close of the fiscal year. It would be impossible for many such companies to assemble the necessary information and prepare financial statements within the time required by the proposed revision.

Recommendation

If an administrative agency is to have authority over the form and content of annual reports, such authority should arise only from express Congressional grant after detailed study of its nature and the provision of adequate safeguards.

C. PROPOSAL THAT COMPENSATION OF OFFICERS AND DIRECTORS BE SET FORTH IN PROXY STATEMENT

Substance of Proposal

The proposed revision would require disclosure of compensation of all directors, officers, and nominees for director; and of all increases received during the preceding fiscal year by any such person whose compensation exceeds $25,000.

Situation under Present Rule

The proxy rules now require disclosure only of the salary of any nominee for director who receives one of the three highest salaries paid to any director, officer, or employee.

Reason given by Commission's Staff for Making Proposal

> "The disclosures by various Congressional investigating committees of practices involving disproportionately high compensation paid to management and employees of corporations engaged in war work have resulted in widespread investor demand for more information concerning the salaries of officers and directors.***"

Objections to the Proposal

(1) Some corporations have found that publication of salaries of officers and employees of competitors has resulted in a demand for salary increases to the level of the competitor. In a highly competitive business field, the disclosure of salaries of all officers of a corporation might lead competitors to proselyte important key executives by offering higher salaries. The statement of salary increases might also create jealousies between officers of a corporation. Many corporation heads feel strongly on these matters.

(2) Under the recent Act of Congress providing for control of price levels, and the effect given it in the President's order, it seems unlikely that unduly high salaries will be permitted. If there was ever justification for the proposed rule, there is no reason for it now.

(3) It is to be feared that adoption of this proposal would result in withdrawal of listings and would be a substantial deterrent to future listings.

D. PROPOSAL FOR LISTING NOMINATIONS FOR DIRECTORS BY SECURITY HOLDERS

Substance of Proposal

Under this proposal a security holder, upon notifying the management of the corporation and supplying the required information, may require the name of a nominee designated by him to be listed in the proxy statement and in the proxy form to be mailed to stockholders. The proposal also states that "in the event that security holders notify the management of an intention to nominate and support more than twice as many nominees as there are directors of the issuer, the management may select, on any equitable basis, name and furnish the required information concerning only twice as many nominees as there are directors."

Situation under Present Rule

The proposal is new. Under the present rules the management must circulate proxy solicitation material in behalf of nominees of stockholders, but at the expense of such stockholders.

Reason given by Commission's Staff for Proposal

None is given.

Objections

(1) This proposal, so far as it compels the listing of names of all nominees on the proxy in ballot form, has nothing to do with the principle of disclosure but is designed to change the form of the proxy by making it a ballot for the election of directors. As pointed out above, the Commission's authority to change the proxy into a ballot is open to question.

(2) Names of persons not only unfitted but unqualified for office might be proposed and submitted to stockholders for consideration and vote. For example, a corporation organized under State laws requiring a specified number of directors to be stockholders or residents of that State might be required to include persons who could not qualify as directors.

(3) The requirement that opposition candidates, if the number exceeds twice the number of directors, shall be reduced to that number "on any equitable basis" is probably unworkable and dangerous. The corporation, in peril of the severe penalties of the Act, might be at a loss how to select a basis which would stand court test.

(4) In some cases the number of opposition candidates might be many times the number of directors up for election. For example, if the board of directors has 16 members, it would be necessary to list 32 candidates even though only 4 directors might be up for election.

(5) The listing of numerous candidates in the proxy would undoubtedly result in invalidation of many proxies because of improper marking.

Recommendation

This proposal should not be adopted. Where security holders desire to propose opposition directors, they can solicit stockholders directly under the present proxy rules.

E. PROPOSAL REQUIRING A BRIEF DESCRIPTION OF ANY MATERIAL TRANSACTION IN WHICH A DIRECTOR MAY HAVE AN INTEREST

Substance of Proposal

The proposed proxy rules would require a brief description of "any interest, direct or indirect, of each person who has acted as a director of the issuer during the past year and each person nominated for election as a director and any associates of such director or nominee in any material transaction during the past year or in any proposed material transaction to which the issuer or any subsidiary was or is to be a party." The definition of "associate" has been enlarged to read as follows:

> "(e) The term "associate", used to indicate a relationship with any person, means (1) any corporation or organization (other than the issuer) of which such person is an officer or partner or directly or indirectly the beneficial owner of 10% or more of any class of equity securities, (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity, and (3) any relative or spouse of such person having the same home as such person;"

Situation under Present Rules

The present rules require a description of any substantial interest of a nominee for director and any associate of such nominee in any property acquired within two years or proposed to be acquired by the issuer or any of its subsidiaries, other than property acquired in the ordinary course of business or on the basis of bona fide competitive bidding. An "associate" is defined under the present rules as:

> "* * * (1) any corporation or organization (other than the issuer) of which such person owns of record or beneficially 10% or more of any class of voting securities, (2) any firm of

which such person is a partner, and (3) any relative or spouse of such person having the same home as such person;"

Reasons given by Commission's Staff for Making Proposal

No reason is given.

Objections to the Proposal

(1) In view of the fact that the proposal does not define or indicate what shall constitute "a material transaction" it probably would be necessary for a corporation, in order to avoid controversy, to include a description of the multitude of transactions which might possibly be regarded by some persons as "material". A large part of such transactions would be of no real interest to stockholders. It would be necessary to include not only transactions now covered by the rules but also, because of the broadened definition of the term "associate", transactions between the corporation and its subsidiaries and (a) other corporations of which the director or nominee is an officer including even subsidiary and affiliated companies; (b) any trust or other estate in which the director or nominee has a substantial beneficial interest; and (c) any trust in which the director or nominee serves as a trustee. In the case of corporations having many subsidiaries, the task might be stupendous.

(2) The proposal is so broad that a corporation might be required to report transactions of which it had no knowledge or means of knowledge. For example, if a railroad corporation should have on its board an individual who is an officer of a bank, such bank would become an "associate". If this individual be the trustee of an estate which has dealings with the railroad corporation or a subsidiary, there is apparently a duty to report such dealings. In the ordinary course of business banks have many such relationships of which the management of a railroad or other corporation

would have no knowledge.

(3) The effect of including information of the character called for by the proposal would be to divert attention of stockholders from matters which are to be taken up at the annual meeting. As a result, stockholders might overlook matters which are of vital interest to them and the corporation.

Recommendation

The present rules are adequate with respect to the matter.

F. PROPOSAL THAT ANY STATEMENT ABOUT ANY PROPOSAL SUBMITTED BY ANY STOCKHOLDER MUST BE INCLUDED IN PROXY STATEMENT

Substance of Proposal

The proposed proxy rules would give to any stockholder the right to have included in the proxy statement a hundred-word statement concerning any proposal which he desired to be submitted to stockholders for consideration and action. The management would also be required to include in the proxy material the name of such security holder.

Situation under Present Rules

At the present time, if a stockholder informs the management of his intention to submit a proposal for consideration and action at a stockholders' meeting, the management is required to include a summary of the proposal in the proxy material and to provide for appropriate opportunity in the proxy itself for stockholders to indicate their wishes; but is not

required to include a statement as prepared by the stockholder or to advertise the name of the stockholder.

Reasons given by Commission's Staff for Making Proposal

It is stated that the proposed change is to effect "an extension of the rights of stockholders not connected with the management."

Objections to the Proposal

(1) Since there has been no effort on the part of the Commission to impose restrictions upon statements to be supplied by shareholders, managements, in peril of participating in an illegal solicitation, would be required to submit such statements without discrimination. This would open the door wide to libelous, malicious, scurrilous, or abusive matter supplied by notoriety-seeking persons who need buy only a single share of stock for the purpose. Other statements might have no bearing on the matter proposed or on any other matter that could validly come before the meeting.

(2) If a large number of proposals and statements were submitted by shareholders (and there is no limit on the number which a single shareholder could submit), the volume which would be printed under this single requirement might be so formidable that all of the proxy material would be disregarded by shareholders.

Recommendation

The present rules are adequate.