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NYSE Ends Broker Discretionary Voting in Director Elections

Over two and a half years after its initial introduction, the SEC has approved, in a split 3-2 vote, the NYSE's proposal to amend Rule 452 and its corollary Rule 402.08 in the NYSE Listed Company Manual to eliminate broker discretionary voting in director elections for all issuers except registered investment companies. Starting with shareholder meetings on or after January 1, 2010 (other than meetings that were scheduled before such date but properly adjourned until after such date), brokers will no longer be able to vote uninstructed shares in director elections even if uncontested.

NYSE Rule 452 allows brokers to vote on certain "routine" proposals, including ratification of auditors and (before the recent amendment) uncontested director elections, if the beneficial owner has not provided voting instructions at least 10 days before the scheduled meeting. Until recently, brokers often voted uninstructed shares in accordance with the recommendations of the issuer's board. Activist shareholders criticized the rule's effect on corporate governance as thwarting shareholder rights, including masking the impact of "just vote no" campaigns. Opponents of the amendment argued that eliminating discretionary broker voting could make it more difficult and costly to establish a quorum at annual meetings, unless one other "routine" matter (such as auditor ratification) is included on the agenda. Some commentators have estimated that the number of companies that fail to achieve quorum could double under the new rule.

As the 2009 proxy season winds down, we urge companies to evaluate their election results and annual meeting processes to anticipate how the new rule may affect director elections in the coming 2010 season. To avoid a quorum failure, companies should work closely with their proxy solicitors to evaluate the historical voting patterns of their shareholders and develop a company-specific strategy to increase voting response. The new rule could have the effect of strengthening "no" or "withhold" vote campaigns at companies with majority voting standards, especially if one believes that brokers have historically voted uninstructed shares for management directors. This amendment may result in a longer, more aggressive proxy solicitation effort and entail higher proxy solicitation expenses.

This NYSE rule amendment is just one part of a series of regulatory and state law changes that may have a significant impact on director elections in 2010. The SEC's notice-and-access model of proxy statement distributions (which was mandated for large accelerated filers other than registered investment companies in January 2008 and all other issuers in January 2009) may continue to have the effect of reducing voting among retail investors. Delaware has also

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adopted a series of amendments to its General Corporation Law that would permit companies to adopt new procedures to allow, among other things, shareholders to submit director nominees for inclusion in a company's proxy materials, reimbursement of proxy contest expenses and the setting of different record dates for notice of, and voting at, shareholder meetings. Finally, the SEC has proposed proxy access amendments that would, among other things, allow shareholders who satisfy specified share ownership thresholds to submit a minority slate of directors via the company's proxy materials for election to the board. The proposal does not specify an anticipated effectiveness date for these amendments, if adopted, although Commissioner Casey suggested at today's open meeting that the SEC's current timeline would see these changes in effect for the 2010 proxy season. For our memorandum on this development, see http://www.paulweiss.com/resources/pubs/detail.aspx?publication=2399

We note that the SEC also voted today to propose amendments to its rules to enhance the disclosures that all U.S. public companies are required to make in their proxy statements about compensation and other corporate governance matters. In addition, the SEC voted to propose requirements for participants in the Troubled Asset Relief Program (TARP) to include advisory shareholder "say-on-pay" votes on executive compensation in their proxy materials. We will be covering these developments in separate client memoranda.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Any questions concerning the issues addressed in this memorandum may be directed to Kelley D. Parker (212-373-3136), James H. Schwab (212-373-3174) or Frances F. Mi (212-373-3185).