

## SEC Proposes Rules to Increase Shareholder Access to Proxies

The SEC approved today for public comment a proposal that would give investors greater power to nominate directors on corporate boards. (<http://www.sec.gov/news/press/2003-133.htm>)

The proposal would require executives to include shareholder nominations for director candidates in the proxy statement, to the extent shareholder nominations are permitted by state law, if one of two "trigger" events happens:

- 35% or more of votes cast on one or more director nominees are "withhold" votes; or
- At least 50% of shareholders approve a proposal, which can only be submitted by 1% or greater shareholders, to permit shareholder nominations in future years.

If one of these "triggers" occurs, the company would be required to include the shareholder nominee(s) in its next proxy statement. Only nominations from shareholders who have owned more than 5% of the company's outstanding shares for at least two years and intend to maintain such ownership through the next annual meeting can submit a nomination. The number of shareholder nominees would be limited to one if the board consists of eight or fewer members, two if the board has nine to 19 directors, and three for a company with 20 or more directors.

This proposal has caused much controversy, with opponents arguing that it will bring chaos into the boardroom and give special interests power over company policy, while advocates for investors say the proposal does not go far enough in preventing boards from "rubber-stamping" executive decisions. **Companies should be aware of these potential changes that may have an effect on their proxy statements in the future.**

### ■ ENRON WORKERS MAY SUE EXECUTIVES OVER LOST SAVINGS

A Federal District Court judge has ruled that employees may sue Kenneth Lay, the former Enron Chairman, and Northern Trust Corp., the trustee of Enron's 401(k) retirement plan, for breach of fiduciary duty. The lawsuit accuses Mr. Lay and others of misleading company employees by encouraging and sometimes requiring them to hold Enron stock in their retirement accounts. (<http://www.txs.uscourts.gov/notablecases/tittle.pdf>)

A key aspect of the ruling is that senior executives and directors could be treated as fiduciaries under ERISA. Persons or entities with a fiduciary duty must act in the best interests of the plan participants, rather than their own or the company's best interests. This ruling confirms existing law that persons who exercise "any discretionary authority or discretionary control" in the management of the plan can be considered fiduciaries even though they may not be the named trustees. **Company executives should not assume that only those people who are specifically named as fiduciaries have a general fiduciary duty to a retirement plan and its beneficiaries. You may wish to consult with counsel for further information about potential liability.**

### ■ INVESTMENT BANK SETTLES WITH SEC REGARDING ALLEGED VIOLATION OF REGULATION M

J.P. Morgan Chase & Co. recently settled with the SEC regarding allegations that buyers of initial public offering shares were induced to make aftermarket purchases of the same shares. (<http://www.sec.gov/news/press/2003-129.htm>)

The SEC alleged violations of Rule 101 to Regulation M, instead of the more widely used Exchange Act Rule 10b-5, which involves higher fines.

Rule 10b-5 is generally invoked in cases of fraud or market manipulation, such as if IPO allocations were given to investors only if they would place aftermarket orders. In contrast, Rule 101 to Regulation M provides that, in connection with a distribution of shares, it is unlawful for distribution participants to attempt directly or indirectly to induce any person to bid for or purchase the subject shares until the distribution has been completed. In Staff Legal Bulletin No. 10 (August 25, 2000), the SEC explained that the following practices are prohibited by Rules 101 and 102 of Regulation M:

- Soliciting customers to make additional purchases of shares during the distribution; and
- Requiring customers to purchase additional shares in the aftermarket as a condition to being allocated shares in the distribution.

The above actions may also violate other anti-fraud and anti-manipulation provisions of the federal securities laws. **Companies should be aware that there are several different securities regulations that may be utilized to punish improper sales of shares.**

## ■ CRIMINAL CHARGES LEVIED FOR DOCUMENT DESTRUCTION

A former Ernst and Young audit partner was criminally charged in federal court late last month with obstructing the examination of a financial institution and obstructing justice by falsifying and destroying audit workpapers during a federal investigation of NextCard, Inc. (<http://www.sec.gov/news/press/2003-123.htm>) The SEC separately brought administrative charges against the former partner for unethical and improper professional conduct because of these activities.

The falsification of records charge is the first of its kind brought under Section 802 of the Sarbanes-Oxley Act, which imposes criminal penalties of up to 20 years in prison for anyone who “knowingly alters, destroys, mutilates, conceals, covers up, [or] falsifies...any record, document, or tangible object” with the intent to obstruct a federal investigation or the activities of a federal agency. Section 802, enacted in reaction to the document shredding at Enron, also provides for penalties of up to ten years in prison for failing to maintain corporate audit records of public companies.

**Company executives should be aware that Sarbanes-Oxley has broadened the reach of criminal penalties to cover corporate misconduct by any individuals associated with a company. Also, the new statute covers any federal investigation at any company, whether public or private.**

Kutak Rock LLP is a national law firm with more than 325 attorneys located in 16 offices throughout the United States practicing in the areas of corporate, banking and securities law, public and corporate finance and complex commercial litigation matters.

For more information on these or other related topics, please contact any of the following attorneys:

**Steven P. Amen** ..... 402-231-8721  
steven.amen@kutakrock.com

**Mark A. Ellis** ..... 402-231-8744  
mark.ellis@kutakrock.com

**Joseph O. Kavan** ..... 402-231-8808  
joseph.kavan@kutakrock.com

**Lisa A. Sarver** ..... 402-231-8347  
lisa.sarver@kutakrock.com

This newsletter is a publication of Kutak Rock LLP and is intended for general information only. It may be considered advertising under applicable court rules. It is not intended and should not be construed as legal advice. With regard to specific circumstances, each person should seek the advice of his or her attorney. The material in this publication may only be reproduced, in whole or in part, with acknowledgement of its source and copyright.

Copyright © 2003 Kutak Rock LLP. All rights reserved.