NEW YORK STOCK EXCHANGE
Department of Stock List
11 Wall Street

September 17, 1942.

Mr. Milton V. Freeman
Assistant to the General Counsel
Securities and Exchange Commission
18th and Locust Streets
Philadelphia, Pennsylvania.

Dear Mr. Freeman:

We appreciate the opportunity you have afforded us to comment upon the proposed revisions of the proxy rules enclosed with your letter of August 19, 1942.

It seems to us apparent that any device for corporate regulation as distinguished from market regulation which rests upon the listing or non-listing of a security rests upon a very narrow and insecure foundation. Anything which tends to drive securities away from the regulated exchange markets must necessarily further narrow the field in which effective market regulation can operate. Where government finds a particular corporate regulation necessary, it does not seem to us appropriate that the application of such regulation should depend upon the listing of a security. We invite your attention to the fact that the proposed new proxy rules depart still further from market regulation and admittedly enter the field of corporate regulation. The evils which the Commission believes exist are certainly not peculiar to companies whose securities are listed on a national securities exchange and we do not believe that it is appropriate to use machinery established for market regulation to attempt to correct evils which are unrelated to the markets. If there are widespread evils which need correction, we believe that the government should adopt a direct approach which will apply wherever that evil may exist.

There are other factors which would seem to make the proposed changes in the proxy rules particularly inopportune at this time. The armed forces have already taken many office employees. Trained office personnel cannot be replaced. The increase in business activity has added a considerable burden to the presently undermanned office staffs and in addition the agencies of the Federal government which are concerned with the war effort require many detailed applications and reports in connection with priorities, allocations, foreign fund control, production control, price control, etc. It would seem that time and effort essential to the war effort should not be diverted to the preparation and clearance of complicated proxy statements.

We have no way of knowing the number of long-distance telephone calls or trips to Philadelphia which are necessary in clearing proxy statements under the present rules. Under the proposed rules not only is the proxy statement itself greatly expanded both as to scope and

detail but in addition the annual reports to stockholders may have to be cleared with the Commission. The new rules undoubtedly will add greatly to the load carried by the already over-taxed telephone and transportation facilities. The increased drain on manpower raises the question of whether it will be physically possible for the Commission's staff to handle the increased burden of proxy examination and war censorship. Under Rule X-6 it is necessary for the Commission to authorize or direct the filing under separate confidential cover of information which would contravene the Code of Wartime Practices or regulations of war agencies. The censoring of the Form 10-K reports has taken several months. This process as applied to a proxy statement will have to be completed in less than ten days.

The comments of the Department of Stock List on the proposed revisions of the proxy rules are contained in the annexed memorandum.

The New York Stock Exchange respectfully requests the opportunity of appearing before the Securities and Exchange Commission to present its objections to the proposed rules.

Yours very truly,

P. L. West,
Acting Director.

Enc.
PLW:hm

MEMORANDUM September 17, 1942.

Comments of the Department of Stock List of the New York Stock Exchange on the Proposed Revisions of the Proxy Rules of the Securities and Exchange Commission.

RULE X-14A-1

This rule, together with the subsequent rules, links the annual report to stockholders with proxy material; the apparent purpose being to extend statutory liabilities under the Act to the annual report. The imposition of this liability may check the present trend toward more readable and informative annual reports and turn them into dry and legalistic documents. If stockholders are to be informed, they must not only be given information, but that information must be in a form which they will read and comprehend. If the information is to be of value it is essential that it be current. We fear that these rules may further delay the transmission of annual reports to stockholders. This problem is further discussed under Item 5A of Schedule 14-A.

RULE X-14A-2(a)

This rule is intended to prohibit the voting of an undesignated proxy. Though the Commission's power to prescribe a form of proxy as distinguished from information which must be given by a person soliciting a proxy is not free from doubt, we have thought well of the practice of giving stockholders the opportunity to vote for or against a proposal. However, to deprive a stockholder of his right to be represented at a meeting if he fails to make a designation is an entirely different matter.

Apparently the intention is that an undesignated proxy cannot even be used for quorum purposes. It seems reasonable to suppose that there are many among the millions of men in the armed forces who are owners of listed securities and that they will not be able to return

their proxies in time for meetings. To add to the burden of obtaining a quorum may result in real detriment to the stockholders themselves as effective stockholder action may be prevented. Many state statutes prescribe the percentage of stockholder approval necessary for various kinds of corporate action. A company may have to amend its charter in order to participate in the war effort. Prompt stockholder action would be essential and anything which would tend to hinder such action would not be in the public interest.

Under the present rules stockholders are given the opportunity of directing their proxies to vote for or against a proposal. If a stockholder wishes to vest discretion in a management in which he has confidence, it is difficult to see why he should not be permitted to do so. We understand that the courts have long recognized that a proxy holder has authority, in the absence of specific instructions to the contrary, to use his discretion in acting at a stockholders' meeting.

There have been instances in the past where discretionary proxies have been of great advantage to the stockholders by reason of a change in conditions arising between the time the proxies were solicited and the holding of the meeting. If the proposed rules require the proxy holder to vote as directed, regardless of any change in circumstance, they may operate to the detriment of the stockholders.

The proposed rule raises certain problems:

1. If two proposals are to come before a stockholders' meeting and a stockholder votes for or against only one of the proposals, may his proxy be counted in determining whether or not a quorum is present?

2. If in the example given above the proxy is used in determining a quorum, that quorum will not be broken by the failure of the proxy holder to vote on the undesignated

proposal and a minority group of stockholders holding properly marked proxies may carry a proposal which is contrary to the wishes of the majority of the stockholders.

RULE X-14A-2(b)

It would appear that this rule would require the issuer to place the name of a nominee in its proxy if requested to do so by the holder of a single share of stock even though the stockholder had just acquired the stock for that purpose and no other. The consent of the nominee to serve does not appear to be required. This may result in the naming of individuals who would not serve if elected. A stockholder might, for his own selfish purposes, create the appearance of dissension within a particular company by nominating an opposition slate.

As the proxy rules stand today any security holder or group of security holders can solicit proxies for any purpose. The individual or individuals making such separate solicitation are made responsible for their own acts. Their statements appear in a separate document. The proxy rules governing the use of separate proxy material have appeared sufficient to prevent abuse.

We believe that this type of proxy rule should embody safeguards at least equivalent to those provided by the Congress in dealing with a similar problem under the Trust Indenture Act of 1939.

Several questions arise under this proposal.

1. What would happen if a management nominee were to die before the stockholders' meeting? Would the management then have to vote for the stockholder nominee, or could the management proxies vote for a substitute chosen by them?

2. What would happen if a proxy were marked for a minority stockholder's nominee and the minority stockholder did not attend the meeting and nominate his candidate?

3. If there are more than twice as many nominees as there are directors of the issuer, may the management retain all of its own nominees on the proxy or does the "equitable basis" of selection contemplate the elimination of some of the management's nominees?

We understand that the right of nomination given to stockholders does not include the right to have a one-hundred word statement inserted in the management proxy material with respect to such nominee.

The proposal to permit stockholders to nominate auditors would apply only in the comparatively few cases where the auditors have to be elected by the stockholders. Even in those cases it would seem that the management would be in a better position to judge the qualifications of a particular auditor than would an ordinary stockholder. No satisfactory method of having the stockholders select the auditors has been devised.

RULE X-14A-2(c)

Many companies today find it economical to use post card proxies. There are about 19 1/4 square inches on an ordinary post card. Almost 1/6 of this space would, under the proposal, have to be left blank. It does not appear that the three square inches provided by the rule would be sufficient for a reasoned comment and the value of a one or two-line comment would not appear to be worthwhile. A problem would be raised in those cases where the comments made by a stockholder cast doubt on his instructions. This would still further complicate the quorum problem which we have discussed above.

RULE X-14A-3(a)

This rule requires that information included in proxy soliciting material shall be presented in an order and form which will be clear to the person solicited. Many companies listed on this Exchange have thousands of stockholders. Information which may be clear to one individual certainly would not be clear to another. Approximately 20% of the outstanding stock of International Telephone & Telegraph Corporation is in foreign share certificates and the remainder in domestic share certificates. It is certain that the same proxy statement will not be clear to all stockholders.

If financial statements were a part of the proxy soliciting material, undoubtedly there would be many to whom such statements would not be clear, regardless of their order or form. No person soliciting a proxy may know beforehand or have any way of telling whether or not his material will be "clear to the person solicited." This proposal would inject a purely subjective standard. It seems reasonable to assume that what one person would think clear to a stockholder another person would think confusing.

One certain and easy way of proving that each stockholder who sends in a proxy has received the proxy statement is to attach physically the proxy to the proxy statement. Under the proposed new rule the proxy if attached must appear at the end of the proxy statement. Under the proposed rules the security holder will receive a sizeable document. Many stockholders may postpone examination of this voluminous material until after the meeting is held or discard it without reading it through. It does not seem improbable that the proxy itself may be overlooked. Here again the effect of this rule may be to make stockholder action more difficult.

RULE X-14A-3(b)

Under the present proxy rules it is not necessary to furnish information required to be included in the proxy statement if that information is not known and is "not reasonably available to the persons making the solicitation." The proposed new rules change this to "not reasonably within the power of such persons to ascertain or procure." This may well mean that proxy statements will have to be held up almost indefinitely in order to get information which, though "not available," would be reasonably "within the power" of the solicitor to obtain, regardless of the expense involved.

RULE X-14A-3(c)

No comment.

RULE X-14A-3(d)

Some companies have tried to explain technical accounting terms appearing in their financial statements by adding a small parenthetical clause immediately below a particular item. Through this device an otherwise technical term may be made clear to the average stockholder. It may not be practicable to use 8 point leaded type for these parenthetical notes. To require this type of notation to be printed in 8 point leaded type would, we fear, result in its omission.

RULE X-14A-4(a)

It is not clear whether a company which includes the material called for by paragraph 5A(1) in its ordinary annual report which precedes the filing of the proxy solicitation

material has to file a copy of the annual report at the time that the report is mailed to the stockholders or whether it merely has to file a copy of such report with the proxy material. The problems raised by the information required under item 5A(1) and (2) are discussed under item 5A below.

RULE X-14A-4(b) and (c)

No comment.

RULE X-14A-5

The present rules prohibit any solicitation "by means of any form of proxy, notice of meeting, or other communication containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact or omission to state any material fact necessary in order to make the statements therein not false or misleading."

The proposed rule drops out the phrase "at the time of and in the light of the circumstances under which it is made." The comments state, "No substantial change" in this rule is intended. It is not clear to us that the dropping of the clause referred to above may not make a substantial change. We see no reason for its deletion as it follows the liability language contained in Section 18(a) of the Act.

If the one-hundred word statement submitted by a stockholder were found to be misleading, would it be necessary for the management, to avoid a violation of this rule, to send out a corrected statement?

RULE X-14A-6(a)

Under the present rules it is the duty of the issuer to furnish certain material on the request of "any record owner" of a security of the issuer. The proposed rule extends the duty so that the issuer has to comply with the request made by "any owner" whether or not a record owner. This proposed change raises many troublesome problems:

1. Would a record owner be an "owner" within the meaning of the proposed rule unless he were also the beneficial owner?

2. If the word "owner" includes a beneficial owner, must such owner be the sole beneficial owner or is a partial beneficial ownership sufficient?

3. Under the proposed rule the owner of any security (whether or not a voting security) is entitled to ask for the information, even though he is not entitled to attend the meeting.

It seems to us advisable to limit the provisions of this paragraph to record owners, except, possibly, in the case of bond issues where the great majority of the bonds are unregistered. In such case a special clause should be inserted covering them. In the case of bearer securities, it would seem appropriate to require that the security be exhibited by the "owner" as a condition precedent to the making of the requests permitted under this paragraph.

RULE X-14A-6(b)

Under this proposed rule the management would be compelled to mail proxy material for a stockholder even though that proxy material did not comply with the proxy rules and had not been cleared with the Commission. It would seem that a proxy solicitor requesting an issuer to mail his proxy material should be compelled to furnish satisfactory evidence to the

issuer that the proxy material had been filed with the Securities and Exchange Commission; that the ten-day period had elapsed; and that neither the Commission nor its staff had raised any objection thereto.

RULE X-14A-7

Under this proposed rule the management would apparently be required to insert a one-hundred word statement in its proxy material at the request of any security holder whether or not that security holder were a holder of record and whether or not he was entitled to attend and vote at the meeting. Furthermore, the one-hundred word statement would apparently have to be included in the management's proxy statement even though the subject matter of the proposal was one which did not require stockholder action.

It is not clear whether the management must insert the one-hundred word statement as prepared by the security holder or whether the management must assume the burden of preparing the stockholder's statement. In either event the management may be liable for any misstatements or inaccuracies and there is nothing in the rules which would appear to impose liability on the stockholder supplying the statement.

It seems to us that here again the safeguards which Congress established in dealing with a comparable problem under the Trust Indenture Act might well be adapted by the Commission to proxy solicitation.

RULE X-14A-8(a)

The present rules exempt any solicitation made otherwise than by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national

securities exchange. The proposed rule removes the intrastate exemption and there would seem to be substantial doubt as to the constitutional power to regulate such solicitation under the rule.

RULE X-14A-8(b) (c) (d) (e) (f) (g) (h)

No comment.

RULE X-14A-9(a)

No comment.

RULE X-14A-9(b)

While we are sympathetic with what we understand to be the purpose of the Commission in expanding the definition of the term "solicitation of a proxy," to include any request to revoke a proxy or not to execute a proxy, there may be situations in which this may operate to the detriment of stockholders generally. Under many corporate laws only ten days notice of a stockholders' meeting is required. A corporation might call a meeting and solicit proxies for action which a minority group may think detrimental to the corporation. If this proposed revision is adopted the minority group could not advise the stockholders that they were opposed to the action and could not ask the stockholders not to execute the management's proxies without preparing, filing and clearing a proxy statement. It might be impossible for this minority group to prepare a proxy statement in the form required under the rules, file that proxy statement with the Commission in Philadelphia, clear with the Commission and have the statement accelerated in time to combat the management proposal.

Similarly, a minority group might call a meeting and rush through a proposal before the majority had a chance to effectively combat it.

RULE X-14A-9(c) and (d)

No comment.

RULE X-14A-9(e)

The broadening of the term "associate" will require the disclosure under item 5(I) of a description of all intercompany transactions with subsidiaries, if a director of the issuer happens to be an officer of the subsidiaries.

RULE X-14A-9(f), (g) and (h)

No comment.

SCHEDULE 14A, Item 1

It is not clear what is intended by "the reasons for the assertion" that the right of revocation of a proxy is limited. It would appear that the wording of the present rule which requires the summarizing of conditions of revocation would be better since the word "reasons" might indicate the necessity of a legal opinion to support the statements made.

SCHEDULE 14A, Item 2

No comment.

SCHEDULE 14A, Item 3

No comment.

SCHEDULE 14A, Item 4(a)

It might be well to require a statement of the record ownership as well as the beneficial ownership in order that a check may be made of such an amount.

SCHEDULE 14A, Item 4(b)

No comment.

SCHEDULE 14A, Item 4(c)

There is no time limit on this requirement and presumably a director could give notice to the management the day before the proxy material was to go out and thereby compel the management to prepare a new proxy statement. It appears that there should be some time limitation such as at least two days prior to the preliminary filing of the proxy material with the Commission.

SCHEDULE 14A, Item 5(A)

It seems to us that the result of the new 5(A) will necessarily be to either bring the ordinary annual report within the liability of the 1934 Act or to cause companies to send out two annual reports. In recent years the annual reports to stockholders made by corporations listed on the New York Stock Exchange have been made more readable and informative. They are documents prepared by business men rather than by lawyers. If the stockholder is to be informed

about his company he must not only be given information but this information must be in a form which he will read and comprehend. We fear that the imposition of statutory liability on the annual reports may reverse the present trend toward more informative reports and turn them into dry and legalistic documents. Liability may be incurred under the 1934 Act by understatement as well as overstatement and suit may be brought against the company by any person, whether or not a stockholder, who may buy or sell a security relying upon that report.

With these broad liability provisions applicable to an annual report, it seems to us that management will hesitate to include in these reports anything that is not required by law and we do not believe that any rule applicable to all listed companies can cover information which may be of vital importance in a particular case but of no importance in the great majority of cases.

If there are any companies whose annual reports to stockholders are misleading, it would seem to us more appropriate to have the exchanges themselves deal with the problem than to run the risk of having stereotyped reports.

There is another factor which we believe to be important. If an annual report is to be of value to a stockholder he ought to receive it as promptly as possible after the close of the company's fiscal year. We have for years required our companies to send out their annual reports as promptly as possible after the close of the fiscal year and in any event within three months. Over 80% of our listed companies have fiscal years ending December 31st. It seems to us that if the annual reports are subject to the liabilities of the 1934 Act, the natural tendency will be to make the required "outline" fairly detailed. Even if management and accounting personnel are able to prepare an annual report within the three months period, it does not seem reasonable

to suppose that all these reports can be examined, censored and revised within a shorter period than was required for the examination and censorship of the 10-K reports this year.

It is noted that whereas Item 7 in Form 10-K merely requires a brief description of material changes in the "general character of the business," the proposed new rules would require a description of material changes "in the character of the business." Does the omission of the word "general" indicate that greater detail will be required under the proposed new proxy rules than is now required under Form 10-K?

It occurs to us that the Code of Wartime Practices would prohibit the disclosure of many "changes in the character of an issuer's business." It does not seem to us advisable to require over-burdened personnel to prepare a statement and then have the statement scrapped by the censors.

We assume that the use of the words "other interests and property" are not meant to include material contracts and patents, as the Congress in prescribing the information to be filed with the Securities and Exchange Commission deleted a requirement for the filing of these items.

We note that an outline must be given of material litigation involving any director or officer of the issuer. It would seem that this might require the giving of information even though the litigation arose out of the acts of the director not affecting the issuer.

The proposal requires the furnishing of financial statements which "will clearly disclose" the financial condition of the issuer and its subsidiaries and the results of the operations of the issuer and its subsidiaries. Presumably the Commission, in prescribing the annual report forms for companies having securities registered under the 1934 Act, has not required more information than is necessary to "clearly disclose" the financial condition and operations of the

company. It would seem, therefore, that the issuer, to be safe, would have to include not only the balance sheets and earnings statements, but the schedules required under the Form "K" reports. We wonder whether the accounting profession would agree that any balance sheet or earnings statement would "clearly disclose" the financial condition and results of operations of a company. There is doubt as to whether comparative financial statements will be possible in all cases, and while the Exchange has felt that the furnishing of comparative statements is desirable we have recognized that there are some situations in which they are not practical. We wonder whether the financial statements in the annual report to stockholders may not convey more information to the average stockholder than would a Form "K" report with its multitude of footnotes and schedules. The sheer bulk of the financial data may discourage the average stockholder from reading the report.

SCHEDULE 14A, Item 5(B)

No comment.

SCHEDULE 14A, Item 5(C)

No comment.

SCHEDULE 14A, Item 5(D)

The proposed rule goes further than Form 10-K. The 10-K report merely requires the naming of holders of record of ten percent or more of the outstanding equity securities. The proposed new rules substitute the words "voting securities." We do not know what is meant by a voting security. Presumably any security may be a voting security under certain circumstances.

The change in Rule X-14A-3(c), which is discussed above, becomes important here as it presumably is "reasonably within the power" of a company to write to each security holder and ask his record and beneficial holdings of the issuer's securities.

SCHEDULE 14A, Item 5(E)

The present proxy rules only require statements concerning continuing understandings or arrangements for the nomination of directors. The proposed rule would apparently require the inclusion of past understandings or arrangements whether or not they still continue. The reason for this is not apparent.

SCHEDULE 14A, Item 5(F)

No comment.

SCHEDULE 14A, Item 5(G)

Provision should be made whereby a person soliciting a proxy could vote the proxy for someone not mentioned in the proxy statement in the event that anyone named in the statement died or was otherwise disqualified.

SCHEDULE 14A, Item 5(H)

A voluminous description of the prospective nominee of a stockholder may be received. Would the management have to conduct its own examination as to the business experience of the nominee or would the management be compelled to set forth the description given by the security holder? If derogatory statements are made by a security holder concerning

the other directors the management may well be subject to liability for publishing the statement. Some limitation should be provided as to volume of description and the management should not be compelled to send out anything which in their judgment may subject them to liability.

SCHEDULE 14A, Item 5(I)

Under this proposal the two-year limitation on reflecting the cost to the vendor has been dropped as has the exemption as to property acquired through competitive bidding. It appears that the main question here is the fair value of the property to the purchaser. Where the vendor may have held the property for a long period of time the cost may be difficult of approximation and the spread may be large. Such transactions, while entirely proper, may give rise to many irrelevant questions. It is suggested that the two-year limitation be continued.

In addition this rule has been extended to require a statement concerning all material transactions and proposed material transactions whether or not in the ordinary course of business. It would appear that this may cover supplies of raw material and other matters in the ordinary course of business which would add a great deal of volume to the proxy statement.

If a director happens to be an officer of a subsidiary, that subsidiary is “an associate” of the director and this Item would require a description of all material transactions between the parent and the subsidiary, with the cost data in case the transactions were those of purchase and sale.

SCHEDULE 14A, Item 5(J)

The purpose of this proposal is apparently to curb “practices involving disproportionately high compensation paid to management and employees of corporations

engaged in war work." It would seem that any such practice is not peculiar to companies whose securities are listed on a national securities exchange. The proposed remedy can only apply to a fraction of the field. Furthermore if there are any listed companies paying disproportionately high compensation to management and employees those companies may very easily avoid the "remedy" either by delisting their securities or by failing to solicit proxies. If a company adopts the alternative of delisting, stockholders will not receive information as to compensation and may not receive the information required under the rules of the various exchanges and the 1934 Act, so that the stockholders will actually be worse off than they are today so far as information is concerned. In addition, they will be deprived of the benefit of having their securities traded on a regulated auction market. If an issuer adopts the second alternative, the stockholder will not receive information as to management and employee compensation and management will perpetuate itself in office in order to avoid disclosure.

In our discussions with companies contemplating registering under the 1934 Act, we have found that the question of salary disclosure in the proxy statement is one of the important deterrents to listing. Prior to the adoption of the 1937 proxy rules there were only 1.8% of our companies having common stock listed on the Exchange which did not solicit proxies. In the current year there were approximately 11% of such companies which did not solicit proxies. We fear that the adoption of the proposed new rules may increase the number of non-solicitors.

SCHEDULE 14A, Item 5(K)

No comment.

SCHEDULE 14A, Item 5(L)

See comment under Item (J).

SCHEDULE 14A, Item 5(M)

In addition to requiring the amount of each class of security of the issuer beneficially owned by the security holder proposing to nominate and support a candidate, his record ownership of stock should also be included.

SCHEDULE 14A, Item 6

Where a solicitation is to be made otherwise than by or on behalf of the management, it would seem that the solicitor should be required to give such of the information which the issuer is required to give as may be obtained from the issuer's registration statement and annual and supplemental reports.

SCHEDULE 14A, Item 7

No comment.

PLW:hm