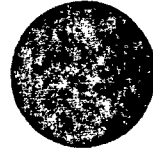


THE WHITE HOUSE

WASHINGTON

July 13, 1988



MEMORANDUM FOR GREGORY M. JONES  
LEGISLATIVE ATTORNEY  
LEGISLATIVE REFERENCE DIVISION  
OFFICE OF MANAGEMENT AND BUDGET

FROM: C. DEAN MCGRATH, JR. *CDM*  
ASSOCIATE COUNSEL TO THE PRESIDENT

SUBJECT: Securities and Exchange Commission Proposed  
Legislation Concerning Shareholder Communication  
Rules

Counsel's office has reviewed the Securities and Exchange Commission's proposed legislation "to amend the Securities Exchange Act of 1934 to require that members of exchanges, brokers, dealers, banks, associations, or other entities that exercise fiduciary powers holding securities as nominees provide proxy and other shareholder communications to investment company beneficial security holders; to require these same entities, holding securities as nominees, to provide information statements to investment company and non-investment company beneficial security holders; and to require investment companies to provide information statements to record holders prior to any security holder vote when proxies, consents, or authorizations are not solicited." We have no comments on this proposed legislation at this time. We would, however, appreciate an opportunity to review the comments of other agencies before they are submitted to the Congress.

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**EXECUTIVE OFFICE OF THE PRESIDENT  
OFFICE OF MANAGEMENT AND BUDGET  
WASHINGTON, D.C. 20503**

**SPECIAL**

June 30, 1988

**LEGISLATIVE REFERRAL MEMORANDUM**

**TO:** Department of Justice - Jack Perkins (633-2113)  
Department of Commerce - Joyce Smith (377-3151)  
Department of the Treasury - Carole Toth (566-8523)  
Council of Economic Advisers  
Federal Trade Commission - Craig Brightup (326-2195)

**SUBJECT:** Securities and Exchange Commission proposal concerning  
shareholder communication rules.

**The Office of Management and Budget requests the views of your agency on the above subject before advising on its relationship to the program of the President, in accordance with OMB Circular A-19.**

**Please provide us with your views no later than 7/13/88.**

**NOTE:** This legislative proposal has already been submitted to Congress and is being circulated for the purpose of determining the Administration's position.

**Direct your questions to Branden Blum (395-3454), the legislative attorney in this office.**

*Gregory M. Jones for*  
**Assistant Director for  
Legislative Reference**

**Enclosure**

**cc:** A.B. Culvahouse, Jr.  
Alan Raul/Bob Damus  
Alan Rhinesmith  
Bob Neal

Betty Johnston  
Bill Hannon  
A. Al-Samarrie  
Karen Wilson



**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

June 13, 1988

The Honorable Jim Wright, Jr.  
Speaker of the House of Representatives  
H-204 Capitol Building  
Washington, D.C. 20515

Dear Mr. Speaker:

I am pleased to transmit on behalf of the Securities and Exchange Commission the attached legislative proposal to amend Sections 14(b) and 14(c) of the Securities Exchange Act of 1934. The proposal would eliminate an unintended gap in the statutory scheme.

The proposal would amend Section 14(b) in two ways. First, it would extend to mutual fund and other investment company security holders the benefits of the Commission's shareholder communication rules which require brokers and dealers ("brokers"), banks, associations, and other entities that exercise fiduciary powers ("banks") holding securities in nominee name to deliver proxy materials to the beneficial owners and to supply registrants, upon request, with beneficial owner information so that registrants can send annual reports and voluntary communications directly to beneficial owners. This will facilitate communication between investment company registrants and the beneficial owners of investment company securities held in nominee name.

Second, it would require broker and bank nominees to transmit information statements to the beneficial owners of the securities. A registrant must transmit information statements to security holders of record when it has a security holder vote but does not solicit proxies. Information statements contain information substantially equivalent to that which would be contained in a proxy statement if a solicitation were made so that security holders will be informed of the matters to be considered. This change will assure that the information required to be provided to security holders who directly hold their securities will be provided to beneficial owners of securities whose securities are held in nominee name.

The proposed amendment of Section 14(c) will assure that all mutual fund and other investment company security

The Honorable Jim Wright, Jr.

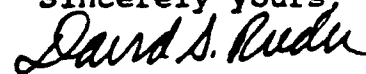
Page 2

holders of record will receive information statements when a security holder vote is held but proxies are not solicited. If the previously discussed amendments to Section 14(b) are enacted, beneficial owners of investment company securities also will be included among those security holders to whom nominees must deliver information statements. Enactment of the proposed amendments will improve communication between registrants of investment company securities and their record and beneficial security holders.

The views expressed here and in the accompanying materials are those of the Commission, and do not necessarily express the views of the President. These materials are being submitted simultaneously to the Office of Management and Budget ("OMB"). We will inform you of any advice received from OMB concerning the relationship of these materials to the program of the administration.

Questions concerning the proposed legislation may be directed to Nina Gross, Director of Legislative Affairs. (272-2500).

Sincerely yours,



David S. Ruder  
Chairman

cc: Mr. James Frey  
Office of Management and Budget

Attachments

## A Bill

To amend the Securities Exchange Act of 1934 to require that members of exchanges, brokers, dealers, banks, associations, or other entities that exercise fiduciary powers holding securities as nominees provide proxy and other shareholder communications to investment company beneficial security holders; to require these same entities, holding securities as nominees, to provide information statements to investment company and non-investment company beneficial security holders; and to require investment companies to provide information statements to record holders prior to any security holder vote when proxies, consents, or authorizations are not solicited.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Sec. 1. This Act shall be cited as the "Shareholder Communications Improvement Act of 1988."

Sec. 2. Section 14(b)(1) of the Securities Exchange Act of 1934 (15 U.S.C. 78n(b)(1)) is amended by --

(1) striking out "section 12 of this title" and inserting in lieu thereof "section 12 of this title or any security issued by an investment company registered under the Investment Company Act of 1940"; and

(2) striking out "or authorization" and inserting in lieu thereof "authorization, or information statement".

Sec. 3. Section 14(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78n(c)) is amended by striking out "title" and inserting in lieu thereof "title or a security issued by an investment company registered under the Investment Company Act of 1940".

Sec. 4. Sections 2 and 3 of this Act shall be effective one hundred and eighty days after the date of enactment.

## SUMMARY OF THE PROPOSED LEGISLATION

Section 2 of the proposed bill contains two amendments of Section 14(b) of the Securities Exchange Act of 1934 ("Exchange Act"). First, paragraph (1) of Section 2 of the proposed bill will extend to investment company security holders the benefits of the shareholder communication rules which require brokers and dealers ("brokers"), banks, associations, and other entities that exercise fiduciary powers ("banks") holding securities as nominees to provide proxies, consents, and authorizations ("proxies") to beneficial security holders and to provide registrants, upon request, with beneficial owner information so that registrants can send annual reports and voluntary communications directly to the beneficial security holders. Currently, Section 14(b) and the rules adopted thereunder only apply with respect to securities registered under Section 12 of the Exchange Act which most investment company securities are not. The proposed amendment recognizes the changes that have occurred in the form of ownership of investment company securities and will facilitate communication between investment companies and beneficial owners of investment company securities.

Second, paragraph (2) of Section 2 of the proposed bill will amend Section 14(b) to require broker and bank nominees to transmit information statements to the beneficial owners of securities. Currently, only proxies, consents, and authorizations are required to be delivered to beneficial

owners of securities when securities are held in nominee name. This amendment of Section 14(b) will assure that beneficial owners of securities held in nominee name receive information statements as well as proxies.

Section 3 of the proposed bill will amend Section 14(c) of the Exchange Act to require investment companies, in addition to other registrants, to transmit information statements to security holders of record. Currently, Section 14(c) requires the issuance of information statements only with respect to securities registered pursuant to Section 12 of the Exchange Act. Like the amendments to Section 14(b), this amendment will facilitate communication between security holders and issuers of information statements and will provide investment company security holders the same communication as that accorded to non-investment company security holders.

Section 4 of the proposed bill provides for its effective date. The amendment of Section 14(b) will be effective one-hundred and eighty days after the date of enactment so that nominees can integrate investment company security holders into their established proxy delivery and communication systems. The delayed effective date also will permit broker and bank nominees to extend existing proxy delivery systems to include information statements. The amendment of Section 14(c) also would take effect one hundred and eighty days after the date of enactment to allow

investment companies to extend established communication systems for proxy delivery to include information statements.



MEMORANDUM OF THE SECURITIES AND EXCHANGE COMMISSION  
IN SUPPORT OF LEGISLATION TO EXPAND THE COVERAGE OF THE  
SHAREHOLDER COMMUNICATION REQUIREMENTS UNDER SECTIONS  
14(b) AND 14(c) OF THE SECURITIES EXCHANGE ACT OF 1934

On April 27, 1988, the Securities and Exchange Commission determined to propose legislation that would amend Sections 14(b) and 14(c) of the Securities Exchange Act of 1934 ("Exchange Act"). One amendment of Section 14(b) will extend to investment company security holders the benefits of the shareholder communication rules which require brokers, dealers ("brokers"), banks, associations, or other entities that exercise fiduciary powers ("banks") holding securities as nominees to provide proxies, consents, and authorizations ("proxies") to the beneficial owners of investment company securities and to provide registrants, upon request, with beneficial owner information so that registrants can send annual reports and voluntary communications directly to the beneficial security holders. The Commission's proposal is intended to facilitate communication between persons soliciting proxies and the beneficial owners of investment company securities held in nominee name.

The legislation would further amend Section 14(b) to require broker and bank nominees to provide information statements to beneficial owners of securities. A registrant must transmit information statements to security holders of record when it has a security holder vote but it does not solicit proxies. Information statements contain information

substantially equivalent to that which would be contained in a proxy statement if a solicitation were made so that security holders will be informed of the matters to be considered. Information statements provide security holders with not only the opportunity to review the disclosure, but also the opportunity to seek equitable relief, if they wish, regarding the corporate action to be undertaken, and to attend any security holders' meeting. This amendment will provide parity in the regulatory treatment of proxy statements and information statements.

The amendment of Section 14(c) would require registrants to transmit information statements to record holders of investment company securities prior to a security holder meeting when proxies are not solicited. The Commission's proposal is intended to provide the same disclosure about actions to be taken in connection with a security holder vote as would be provided if proxies were being solicited.

This legislative proposal is part of a Commission program to improve communication between beneficial security holders and registrants of securities when securities are held in nominee name. This program included the establishment of the Commission's Advisory Committee on Shareholder Communications, and continued with adoption of rules designed to facilitate communication between persons soliciting proxies and the beneficial owners of securities

held by brokers in nominee name. Subsequently, the Commission proposed and Congress enacted the Shareholder Communications Act of 1985, 1/ which authorized the Commission to similarly regulate the proxy processing activities of banks. Rule 14b-2 sets forth banks' obligations in connection with proxy processing activities and direct communication between beneficial owners and registrants. 2/

Despite these improvements in shareholder communications, the Commission has identified three deficiencies in the statutory scheme that are addressed by this proposal.

1. Amendment of Section 14(b): Delivery of Proxy Material to the Beneficial Owners of Investment Company Securities

The Section 14(b) requirement that broker and bank nominees forward proxy material to beneficial owners of securities held in nominee name does not apply to most investment company security holders. Section 14(b) imposes this obligation only with respect to Section 12 securities which most investment company securities are not. 3/

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1/ Pub. L. 99-222, 99 Stat. 1737 (Dec. 28, 1985), amending 15 U.S.C. 78n(b) (1982).

2/ Paragraphs (a) through (c) of Rule 14b-2 became effective July 1, 1987, while paragraphs (d) through (i) of Rule 14b-2 became effective December 28, 1986.

3/ Section 12(g) and Rule 12g-1, which otherwise would require the registration of all investment companies having total assets of \$5 million and a class of non-

(continued...)

Because of this, investment company security holders are deprived of the benefits of the Commission's shareholder communications rules. This is a statutory anomaly that would be remedied by the enactment of the recommended amendments to Section 14(b) of the Exchange Act.

2. Amendment of Section 14(b): Delivery of Information Statements to Beneficial Security Holders

Section 14(b) requires brokers and banks holding securities in nominee name to forward proxies to the

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3/ (...continued)

exempt equity security holders of 500, specifically exclude registered investment companies. Exchange-traded closed-end investment companies must register under Section 12(b). Business development companies, a type of closed-end investment company, also must register under Section 12(b) because Section 54(a)(1) of the 1940 Act requires them to do so. There are approximately 91 exchange-traded closed-end investment companies and 46 business development companies and there are approximately 193 other closed-end investment companies and 2,438 open-end investment companies. Thus, approximately 95% of all registered investment companies that issue voting stock are not covered by the Section 14(b) shareholder communication rules. The legislative history of Sections 12 and 14 of the Exchange Act does not discuss the reason for the omission of investment companies from the proxy delivery provisions of Section 14(b). See H. Rep. No. 1418, 88th Cong., 2d Sess. reprinted in 1964 U.S. Code Cong. & Ad. News 3013, 3027; S. Rep. No. 379, 88th Cong., 2d Sess. 1, 9; H. Rep. No. 95-640, 95th Cong., 1st Sess. 1; S. Rep. No. 114, 95th Cong., 1st Sess. reprinted in 1977 U.S. Code Cong. & Ad. News 4098, 4117. Moreover, the 1985 amendments to Section 14(b) were intended to effect the recommendation of the Advisory Committee on Shareholder Communications that the Commission have the authority to regulate the proxy processing activities of banks. Delivery of proxy material to investment company security holders was not a focus of the Advisory Committee's recommendation.

beneficial owners. However, there is no concurrent requirement for these nominees to forward information statements. Currently, registrants of securities are only required to provide information statements to record holders but not beneficial owners. The Commission recommends that Section 14(b) be amended to provide beneficial security holders with information statements in the same manner as they would receive proxy statements if proxies were solicited.

3. Amendment of Section 14(c): Delivery of Information Statements to Investment Company Security Holders

Like Section 14(b), Section 14(c) of the Exchange Act only applies to securities registered under Section 12 and thus does not generally require investment companies to transmit information statements to their security holders. <sup>4/</sup> Enactment of this recommended amendment will result in regulatory parity between investment company and non-investment company security holders.

4. Effective Date of the Proposed Amendments of Sections 14(b) and 14(c)

The amendment of Section 14(b) will be effective one-hundred and eighty days after the date of enactment so that bank and broker nominees can integrate all investment company security holders into their established proxy

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<sup>4/</sup> Section 14(c) only applies to companies registered under Section 12. See discussion of Section 14(b), supra, note 3.

communication and delivery systems. The delayed effective date also will permit broker and bank nominees to extend existing proxy delivery systems to include information statements. The amendment of Section 14(c) would also take effect one-hundred and eighty days after the date of enactment to allow investment companies to extend established communication systems for proxy delivery to include information statements.