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(202) 755-4846

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CHANGING CONCEPTS OF MATERIALITY

BY ROBERTA S. KARMEL, COMMISSIONER*
SECURITIES AND EXCHANGE COMMISSION

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* THE SECURITIES AND EXCHANGE COMMISSION, AS A MATTER OF POLICY, DISCLAIMS RESPONSIBILITY FOR SPEECHES BY ITS COMMISSIONERS. THE VIEWS EXPRESSED HEREIN ARE THOSE OF THE SPEAKER AND DO NOT NECESSARILY REFLECT THE VIEWS OF THE COMMISSION.

ONE OF MY PREVIOUS OCCUPATIONS WAS TEACHING A LAW SCHOOL COURSE ON THE FEDERAL REGULATION OF SECURITIES. EVERY YEAR, I WOULD GIVE ONE CLASS ON THE CONCEPT OF MATERIALITY UNDER THE SECURITIES LAWS. ONE REFLECTION ON THE FLUIDITY OF THE CONCEPT OF MATERIALITY IS THAT EVERY YEAR I WOULD CHANGE MY LECTURE. I DECIDED TO SPEAK TO YOU ON MATERIALITY TODAY SO THAT I WOULD HAVE THE OPPORTUNITY TO UPDATE AND REVISE THIS LECTURE EVEN THOUGH I AM NOT TEACHING A LAW SCHOOL CLASS THIS YEAR.

THE ADVISORY COMMITTEE ON CORPORATE DISCLOSURE, IN ITS NOVEMBER 1977 REPORT TO THE SECURITIES AND EXCHANGE COMMISSION, STATED THAT

> THE CONCEPT OF MATERIALITY IS THE CORNERSTONE OF THE DISCLOSURE SYSTEM ESTABLISHED BY THE FEDERAL SECURITIES LAWS. IT SERVES A VARIETY OF FUNCTIONS, OPERATING BOTH AS A PRINCIPLE FOR INCLUSION AND EXCLUSION OF INFORMATION IN INVESTOR ORIENTED DISCLOSURE DOCUMENTS AND AS A STANDARD FOR DETERMINING WHETHER A COMMUNICATION (FILED OR OTHERWISE) OMITS OR MISSTATES A FACT OF SUFFICIENT SIGNIFICANCE THAT LEGAL CONSEQUENCES SHOULD RESULT.

ALTHOUGH MATERIALITY HAS BEEN DEFINED DIFFERENTLY IN DIFFERENT CONTEXTS, ALL OF THESE DEFINITIONS ARE GROUNDED ON THE LEGITIMATE EXPECTATIONS OF THE REASONABLE INVESTOR. SEC RULE 405 UNDER THE SECURITIES ACT OF 1933 STATES THAT:

> THE TERM 'MATERIAL,' WHEN USED TO QUALIFY A REQUIREMENT FOR THE FURNISHING OF INFORMATION AS TO ANY SUBJECT, LIMITS THE INFORMATION REQUIRED TO THOSE MATTERS AS TO WHICH AN AVERAGE PRUDENT INVESTOR OUGHT REASONABLY TO BE INFORMED BEFORE PURCHASING THE SECURITY REGISTERED.

THIS STANDARD OF MATERIALITY FOR INFORMATION IN A REGISTRATION STATEMENT HAS BEEN ADOPTED IN A NUMBER OF COURT AND COMMISSION CASES AS A STANDARD OF MATERIALITY FOR INFORMATION IN THE SECONDARY TRADING MARKETS.

IN SEC v. TEXAS GULF SULPHUR CO., 401 F.2D 833 (2D CIR. 1968) CERT. DENIED 394 U.S. 976 (1969), THE SECOND CIRCUIT DEFINED A MATERIAL FACT AS INFORMATION WHICH IS LIKELY TO AFFECT THE MARKET PRICE OF ANY OF THE COMPANY'S SECURITIES OR IS LIKELY TO BE CONSIDERED IMPORTANT BY REASONABLE INVESTORS, INCLUDING SPECULATIVE INVESTORS, IN DETERMINING WHETHER TO TRADE IN SUCH SECURITIES. IN AFFILIATED UTE CITIZENS V. UNITED STATES, 406 U.S. 128 (1972), THE SUPREME COURT DEFINED A MATERIAL FACT AS ONE WHICH " A REASONABLE INVESTOR MIGHT HAVE CONSIDERED IMPORTANT" IN THE MAKING OF AN INVESTMENT DECISION. THE COMMISSION, IN INVESTORS MANAGEMENT CO. SECURITIES EXCHANGE ACT RELEASE NO. 9267 (1971), ELABORATED ON THESE CONCEPTS BY STATING THAT A FACT IS MATERIAL WHERE IT IS --

> OF SUCH IMPORTANCE THAT IT COULD BE EXPECTED TO AFFECT THE JUDGMENT OF INVESTORS WHETHER TO BUY, SELL OR HOLD ... /A SECURITY AND I/F GENERALLY KNOWN, ... TO AFFECT MATERIALLY THE MARKET PRICE OF THE STOCK.

DIFFERENT CATEGORIES OF INFORMATION USERS MAY HAVE DIFFERENT PERCEPTIONS OF MATERIALITY. THERE WAS NO CONSENSUS AMONG MEMBERS OF THE ADVISORY COMMITTEE AS TO WHETHER THE MATERIALITY STANDARD IS THE SAME FOR BOTH CORPORATE SUFFRAGE AND INVESTMENT DECISION-MAKING. THE STANDARD OF MATERIALITY FOR PROXY STATEMENTS ARTICULATED BY THE SUPREME COURT IN TSC INDUSTRIES V. NORTHWAY, INC., 426 U.S. 438 (1976) IS THAT A FACT IS MATERIAL IF "THERE IS A SUBSTANTIAL LIKELIHOOD THAT A REASONABLE SHAREHOLDER WOULD CONSIDER IT IMPORTANT IN DECIDING HOW TO VOTE."

THE ADVISORY COMMITTEE POINTED OUT THAT THE COMMISSION HAS TRADITIONALLY VIEWED INVESTORS AS BEING MOTIVATED BY ECONOMIC CONCERNS AND AS BEING INTERESTED IN INFORMATION WHICH REFLECTS ON THE CURRENT AND FUTURE ECONOMIC PERFORMANCE OF THEIR INVESTMENT. NEVERTHELESS, IN A NUMBER OF AREAS THE COMMISSION SEEMS TO BE MOVING AWAY FROM AN OBJECTIVE OR QUANTITATIVE ECONOMIC MEASURE OF MATERIALITY TO A MORE QUALITATIVE TEST. IN MATTERS RANGING FROM THE PROSECUTION OF SENSITIVE PAYMENTS CASES TO THE DENIAL OF NO-ACTION LETTERS ON SHAREHOLDER PROPOSALS CONCERNING INVESTMENT IN SOUTH AFRICA, THE COMMISSION IS JUDGING MATERIALITY BY A NON-NUMERICAL STANDARD.

I HAVE BEEN WORRYING ABOUT THIS MOVEMENT AWAY FROM SOME FIXED AND EASY STANDARD WHICH RELATES MATERIALITY TO EARNINGS PER SHARE OR SECURITY PRICE FLUCTUATIONS. I HAVE BEEN TRYING TO ARTICULATE AN INTELLIGENT DEFINITION OF MATERIALITY WHICH WOULD INCLUDE THOSE MATTERS OF SOCIAL SIGNIFICANCE AND MANAGEMENT INTEGRITY WHICH ARE BECOMING PART OF OUR ANALYSIS OF MATERIALITY.

INFORMATION OF ECONOMIC SIGNIFICANCE TO INVESTORS CONTINUES TO BE THE KEYSTONE OF OUR CONCEPT OF MATERIALTITY; I WOULD TENTATIVELY SUGGEST, HOWEVER, THAT WE ARE EXPANDING OUR CONCEPT OF MATERIALITY TO INCLUDE INFORMATION WHICH REFLECTS UPON THE ACCOUNTABILITY OF OFFICERS AND DIRECTORS, TO SHAREHOLDERS AND TO A WIDER CONSTITUENCY. THERE IS AN INCREASED SENSITIVITY ON THE PART OF THE COMMISSION, AS WELL AS CORPORATIONS, TO SOCIALLY SIGNIFICANT MATTERS. SOME OF THE SENSITIVITY IS A RESPONSE TO CHANGING VALUES IN OUR SOCIETY. WE ALSO ARE REACTING TO THE EFFORTS OF, AND IN SOME INSTANCES THE LAWSUITS INSTITUTED BY, PUBLIC INTEREST GROUPS AND ETHICAL INVESTORS. E.G., NATURAL RESOURCES DEFENSE COUNCIL, V. SEC, 389 F. SUPP. 689 (D.D.C. 1974). WE HAVE COME TO RECOGNIZE THAT A REASONABLE INVESTOR MAY ANALYZE LONG TERM, IF NOT SHORT TERM, PROFITABILITY OF A CORPORATION BY ASSESSING THE POLITICAL AND SOCIAL VIABILITY OF THE ENTERPRISE OVER TIME. CORPORATE SOCIAL RESPONSIBILITY MAY BE AN INDEX TO THE QUALITY OF MANAGEMENT AND THE VIABILITY OF THE ENTERPRISE.

AN EARLY CASE IN WHICH THE COMMISSION FOUND THAT THE QUALITY OF MANAGEMENT WAS AN ESSENTIAL INGREDIENT OF INFORMED INVESTMENT DECISIONS WAS FRANCHARD CORP., 42 S.E.C. 163 (1964). THE COMMISSION THERE HELD THAT THE NON-DISCLOSURE BY AN ISSUER OF THE TRANSFER OF LARGE SUMS OF MONEY FROM THE ISSUER TO MR. GLICKMAN, ITS CHIEF EXECUTIVE OFFICER AND CONTROLLING SHAREHOLDER, FOR USE IN THE OFFICER'S OWN VENTURES WAS MATERIAL. THE COMMISSION'S PREDICATE WAS THAT THE OFFICER'S WITHDRAWAL OF FUNDS FROM THE ISSUER WAS RELEVANT TO AN EVALUATION OF HIS BUSINESS ABILITY AND INTEGRITY. SINCE THAT DECISION, THE QUALITY AND INTEGRITY OF MANAGEMENT HAVE BECOME INCREASINGLY IMPORTANT COMPONENTS OF THE COMMISSION'S APPROACH TO DISCLOSURE.

IN 1974, THE DIVISION OF CORPORATION FINANCE ISSUED A RELEASE STATING ITS VIEW THAT INDICTMENTS, PLEAS OF GUILTY OR NOLO CONTENDERE, AND CONVICTIONS OF CORPORATIONS OR OFFICERS FOR HAVING MADE ILLEGAL CAMPAIGN CONTRIBUTIONS ARE MATERIAL FACTS AND SHOULD BE DISCLOSED. SECURITIES ACT RELEASE NO. 5466 (1974). DISCLOSURE WAS CONSIDERED APPROPRIATE BECAUSE OF THE MATERIALITY OF SUCH MATTERS TO AN EVALUATION OF THE INTEGRITY OF MANAGEMENT PARTICULARLY WITH RESPECT TO THE OPERATION OF THE CORPORATION AND THE USE OF CORPORATE FUNDS.

IN THE OPINION OF ONE OBSERVER:

> /T/HE SEC'S ACTIONS WERE ENTIRELY CONSISTENT WITH THE CONCEPT OF MATERIALITY. THE HEIGHTENED ETHICAL CLIMATE BROUGHT ABOUT BY WATERGATE HAS CAUSED INVESTORS TO BECOME CONCERNED ABOUT SUCH VIOLATIONS, THUS, ALTERING THE MAKE-UP OF THE "AVERAGE PRUDENT INVESTOR." (HEWITT, "DEVELOPING CONCEPTS OF MATERIALITY AND DISCLOSURE," 32 BUSINESS LAWYER 887,898 (APRIL, 1978).)

THE COMMISSION'S WATERGATE RELATED INQUIRIES IN 1973 AND 1974 LED TO THE DISCOVERY THAT SOME CORPORATIONS HAD FALSIFIED THEIR FINANCIAL RECORDS IN ORDER TO CONCEAL THE PRACTICE OF MAKING PAYMENTS INDIRECTLY OR DIRECTLY TO OBTAIN BUSINESS. COMPANIES WHICH HAD MADE "QUESTIONABLE OR ILLEGAL FOREIGN OR DOMESTIC PAYMENTS" GENERALLY WERE REQUIRED TO DISCLOSE THE MATTER IN A PUBLIC FILING.

THE COMMISSION ARTICULATED VARIOUS REASONS FOR DISCLOSURE OF THESE PAYMENTS IN ITS REPORT ON QUESTIONABLE AND ILLEGAL CORPORATE PAYMENTS AND PRACTICES SUBMITTED TO THE SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE IN MAY 1976. IN ADDITION TO REQUIRING DISCLOSURE WHEN THE PAYMENTS WERE OF A MATERIAL SIZE OR A MATERIAL AMOUNT OF BUSINESS DEPENDED ON THEIR CONTINUATION, THE COMMISSION JUSTIFIED A REPORTING OBLIGATION WHEN A COMPANY'S RECORDS WERE INADEQUATE. THE FALSIFICATION OF CORPORATE RECORDS FRUSTRATES THE SYSTEM OF CORPORATE ACCOUNTABILITY DESIGNED TO ASSURE PROPER ACCOUNTING OF THE USE OF CORPORATE FUNDS IN DOCUMENTS FILED WITH THE COMMISSION AND CIRCULATED TO SHAREHOLDERS.

DISCLOSURE THAT PAYMENTS ARE UNKNOWN TO THE BOARD OF DIRECTORS REFLECTS UPON THE ETHICAL QUALITY OF MANAGEMENT AND THEIR EXERCISE OF CORPORATE AUTHORITY. THE COMMISSION'S REPORT EMPHASIZED THAT FINANCIAL MATTERS ARE NOT THE SOLE CRITERIA FOR A DETERMINATION OF MATERIALITY.

THIS SENSITIVITY TO THE QUALITY OF MANAGEMENT HAS RAISED QUESTIONS ABOUT THE ADEQUACY OF THE DISCLOSURE ABOUT COMPENSATION PAID TO MANAGEMENT. ONE OF THE TOPICS ADDRESSED IN THE CORPORATE GOVERNANCE HEARINGS LAST FALL WAS WHETHER INVESTORS SHOULD BE PROVIDED WITH ADDITIONAL INFORMATION ABOUT MANAGEMENT'S COMPENSATION. MANY PEOPLE ARE QUESTIONING WHETHER THE VALUE OF PERSONAL BENEFITS RECEIVED BY MANAGEMENT SHOULD BE DISCLOSED SEPARATELY FROM THE AGGREGATE AMOUNT THEY RECEIVE IN THE FORM OF SALARY, FEES, COMMISSIONS AND BONUSES. OTHERS ARE QUESTIONING WHETHER, IN FACT, SOME OF THESE BENEFITS SHOULD BE DESCRIBED IN DOCUMENTS PROVIDED TO INVESTORS AND SHAREHOLDERS. U.S. SENATOR JOHN CHAFEE URGED THE COMMISSION IN HIS TESTIMONY AT THE CORPORATE GOVERNANCE HEARINGS TO REQUIRE COMPANIES TO DESCRIBE SOME OF THE BENEFITS RECEIVED BY MANAGEMENT.

ADDITIONAL INFORMATION ABOUT MANAGEMENT'S PERQUISITES MAY BE MATERIAL TO AN EVALUATION OF THE QUALITY AND INTEGRITY OF MANAGEMENT. SINCE THE MATERIALITY OF ADDITIONAL INFORMATION ABOUT MANAGEMENT'S COMPENSATION IS AN ISSUE BEFORE THE COMMISSION AND ITS STAFF NOW, IT WOULD BE INAPPROPRIATE FOR ME TO ADDRESS THIS ISSUE. THE FACT THAT THIS IS AN ISSUE AT ALL, HOWEVER, REFLECTS ON THE EVOLUTION OF THE

CONCEPT OF MATERIALITY AWAY FROM AN OBJECTIVE QUANTITATIVE STANDARD TOWARDS A MORE QUALITATIVE BUT, I HOPE, RELEVANT STANDARD.

THE SIGNIFICANCE OF A SHAREHOLDER'S PROPOSAL TO A COMPANY'S BUSINESS IS RELEVANT TO WHETHER IT MUST BE INCLUDED IN A PROXY STATEMENT. AN ANALYSIS OF THE SIGNIFICANCE OF A PROPOSAL DIFFERS FROM A DETERMINATION AS TO THE MATERIALITY OF INFORMATION ABOUT A COMPANY OR EVEN ITS MANAGEMENT. NEVERTHELESS, THE DEVELOPMENT OF THE COMMISSION'S APPROACH TO THIS ANALYSIS HAS BEEN ANALOGOUS TO THE DEVELOPMENT OF OUR APPROACH TO MATERIALITY. A QUANTITATIVE ECONOMIC SIGNIFICANCE TEST IS GIVING WAY TO A QUALITATIVE SIGNIFICANCE STANDARD.

IN PASSING UPON THE PROPRIETY AND INCLUDABILITY OF SHAREHOLDER PROPOSALS, THE COMMISSION HAS NOT ALWAYS JUDGED SIGNIFICANCE BY THE ECONOMIC IMPACT OF INFORMATION. ONE REASON IS THAT THE CONGRESSIONAL PURPOSE IN GIVING THE COMMISSION AUTHORITY OVER PROXY SOLICITATIONS WAS "TO REQUIRE FAIR OPPORTUNITY FOR THE OPERATION OF CORPORATE SUFFRAGE." THE PROXY RULES WERE INTENDED TO ASSURE DISCLOSURE TO SHAREHOLDERS OF THE MATTERS WHICH THE COMPANY PLANNED TO DISCUSS AT THE MEETING AND THOSE WHICH THE COMPANY EXPECTED THAT SHAREHOLDERS WOULD INTRODUCE FOR DISCUSSION.

SINCE THE 1970 CAMPAIGN TO MAKE GENERAL MOTORS RESPONSIBLE SPONSORED BY THE PROJECT ON CORPORATE RESPONSIBILITY, THE USE OF THE SHAREHOLDER PROPOSAL MECHANISM HAS INCREASED CONSIDERABLY. SHAREHOLDERS HAVE USED THIS PROCEDURE TO COMMUNICATE THEIR VIEWS TO OTHER SHAREHOLDERS AND SOLICIT THEIR VOTES ON A LARGE NUMBER OF MATTERS.

THE PROPOSALS HAVE BEEN DIRECTED AT A VARIETY OF SOCIAL, POLITICAL AND ETHICAL ISSUES INCLUDING THE ARAB BOYCOTT, CORPORATE OPERATIONS IN SOUTH AFRICA, RHODESIA, KOREA AND CHILE, CORPORATE POLITICAL ACTIVITIES, QUESTIONABLE PAYMENTS ABROAD, EQUAL EMPLOYMENT OPPORTUNITIES AND THE GENERAL RESPONSIVENESS OF CORPORATIONS TO THE COMMUNITIES THEY SERVE. SOME PERSONS HAVE BEEN CRITICAL OF THIS USE OF SHAREHOLDER PROPOSALS. THEY HAVE ARGUED THAT THERE IS LITTLE INDICATION THAT THE "REASONABLE OR AVERAGE SHAREHOLDER" IS CONCERNED ABOUT SOCIAL ISSUES, AND THAT, GENERALLY, SOCIAL ISSUES ARE IMMATERIAL TO A CORPORATION'S BUSINESS.

IN NOVEMBER 1976, THE COMMISSION ANNOUNCED THE ADOPTION OF AMENDMENTS TO THE SHAREHOLDER PROPOSAL RULE. SECURITIES EXCHANGE ACT RELEASE No. 12999 (Nov. 22, 1976). THE SUGGESTION THAT THE RULE BE AMENDED TO PERMIT OMISSION OF A PROPOSAL WHENEVER THE MATTER INVOLVED DOES NOT BEAR A SIGNIFICANT ECONOMIC RELATION TO THE ISSUER'S BUSINESS WAS REJECTED. INSTEAD, THE REVISED RULE (RULE 14A-8(c)(5)) PERMITS OMISSION WHEN "THE PROPOSAL DEALS WITH A MATTER THAT IS NOT SIGNIFICANTLY RELATED TO THE ISSUER'S BUSINESS." THE COMMISSION STATED IN THE RELEASE ANNOUNCING THE AMENDMENTS THAT THERE ARE MANY INSTANCES IN WHICH THE MATTER INVOLVED IS SIGNIFICANT TO AN ISSUER'S BUSINESS, EVEN THOUGH SUCH SIGNIFICANCE IS NOT APPARENT FROM AN ECONOMIC VIEWPOINT.

DESPITE THIS STATEMENT, THE STAFF SERIOUSLY CONSIDERED THE ECONOMIC SIGNIFICANCE TO THE COMPANY'S BUSINESS OF A MATTER INVOLVED IN A PROPOSAL. THE DIVISION OF CORPORATION FINANCE FREQUENTLY ISSUED NO-ACTION LETTERS WHERE THE COMPANY REPRESENTED THAT LESS THAN ONE PERCENT OF ITS TOTAL SALES, EARNINGS OR ASSETS WERE RELATED TO THE SUBJECT MATTER OF THE PROPOSAL AND THAT THE COMPANY HAD NO PRESENT INTENTION OF INCREASING THE RELEVANT BUSINESS OPERATIONS.

IN FEBRUARY OF THIS YEAR, THE DIVISION OF CORPORATION FINANCE WAS ASKED TO TAKE A NO-ACTION POSITION ON THE OMISSION OF SHAREHOLDER PROPOSALS RELATING TO TWO COMPANIES' BUSINESS ACTIVITIES IN SOUTH AFRICA. THESE COMPANIES ARGUED THAT, AMONG OTHER THINGS, THE PROPOSAL COULD BE OMITTED BECAUSE THEIR BUSINESS ACTIVITIES IN THE REPUBLIC OF SOUTH AFRICA CONSTITUTED LESS THAN ONE PERCENT OF THEIR TOTAL SALES, EARNINGS OR ASSETS. DESPITE THEIR LIMITED ECONOMIC EXPOSURE IN SOUTH AFRICA, THE DIVISION RESPONDED TO THE COMPANIES THAT IT WAS UNABLE TO CONCLUDE THAT THEY HAD MET THEIR BURDEN OF DEMONSTRATING THAT THE SUBJECT MATTER OF THE PROPOSAL WAS NOT SIGNIFICANTLY RELATED TO THEIR BUSINESS. THE LETTERS INCLUDED A REFERENCE TO THE NOVEMBER 1976 RELEASE IN WHICH THE COMMISSION STATED THAT "PROPOSALS ... MAY BE SIGNIFICANT TO THE ISSUER'S BUSINESS, WHEN VIEWED FROM A STANDPOINT OTHER THAN A PURELY ECONOMIC ONE."

I AM HESITANT TO CHARACTERIZE THESE LETTERS AS A REPUDIATION OF THE INFORMAL ONE PERCENT RULE BECAUSE I AM NOT CONVINCED THAT THERE EVER WAS SUCH A RULE. NEVERTHELESS, THE LETTERS DO REPRESENT A REJECTION OF QUANTITATIVE ECONOMIC SIGNIFICANCE AS A STANDARD FOR RELATING SHAREHOLDER PROPOSALS TO AN ISSUER'S BUSINESS. I AM TROUBLED BY THIS LACK OF AN OBJECTIVE STANDARD IN JUDGING WHETHER SHAREHOLDER PROPOSALS SHOULD BE INCLUDED IN PROXY MATERIAL. YET, SHAREHOLDER PROPOSALS ARE TO SOME EXTENT A VEHICLE FOR HOLDING MANAGEMENT ACCOUNTABLE. THEY PROVIDE AN OPPORTUNITY FOR SHAREHOLDERS TO EXPRESS THEIR POINT OF VIEW ON MATTERS OF CONCERN. ACCORDINGLY, INCLUSION OF A PROPOSAL MAY RELATE TO WHETHER IT ADVANCES A REASONABLE CHALLENGE TO MANAGEMENT.

THE BUSINESS ROUNDTABLE HAS CRITICIZED THE USE OF THE SEC PROXY PROPOSAL MECHANISM

> TO TRY TO MAKE THE CORPORATION AN ARENA FOR DEBATE ABOUT ISSUES WHICH SHOULD BE DECIDED THROUGH THE POLITICAL AND LEGISLATIVE PROCESS. CORPORATIONS, CORPORATE BOARDS AND CORPORATE SHARE OWNERS, ARE NOT THE RIGHT BODIES TO RESOLVE ON THEIR OWN, FOR EXAMPLE, ISSUES INVOLVING RELATIONS WITH OTHER COUNTRIES OR U.S. MILITARY POLICY. ("THE ROLE AND COMPOSITION OF THE BOARD OF DIRECTORS OF THE LARGE PUBLICLY OWNED CORPORATION" 12 (1978).)

THE OBSERVATION BY THE ROUNDTABLE THAT SHAREHOLDERS CANNOT DECIDE CERTAIN TYPES OF ISSUES AS SHAREHOLDERS MAY BE CORRECT. BUT IT DOES NOT FOLLOW THAT A REASONABLE SHAREHOLDER WOULD NOT WANT TO CALL THE MANAGEMENT OF HIS CORPORATION TO ACCOUNT FOR ITS VIEWS AND ACTIONS WITH RESPECT TO SUCH ISSUES.

AS GREATER NUMBERS OF AMERICANS BECOME OWNERS OF OUR LARGE PUBLIC CORPORATIONS, WHETHER INDIVIDUALLY OR THROUGH INSTITUTIONAL INVESTORS, AND AS CORPORATIONS BECOME SUBJECT TO INCREASING GOVERNMENT REGULATION, THE DIALOGUE BETWEEN SHAREHOLDERS AND THEIR CORPORATIONS BECOMES PART OF A LARGER POLITICAL PROCESS. NEVERTHELESS, AND DESPITE THE LEGITIMATE CONCERNS OF ETHICAL INVESTORS, I BELIEVE WE SHOULD EXERCISE CAUTION IN APPLYING A NON-ECONOMIC STANDARD OF MATERIALITY TO DISCLOSURE REQUIREMENTS, ALTHOUGH THIS APPROACH MAY BE APPROPRIATE IN ANALYZING SHAREHOLDER PROPOSALS. BECAUSE SOME INVESTORS MAY WANT CERTAIN INFORMATION IN ORDER TO MAKE AN INVESTMENT OR VOTING DECISION DOES NOT MEAN THAT MANDATORY DISCLOSURE OF SUCH INFORMATION WOULD BE NECESSARY OR APPROPRIATE IN THE PUBLIC INTEREST OR FOR THE PROTECTION OF INVESTORS.

THE REASONABLE INVESTOR IS, OF COURSE, SUBJECT TO THE FORCES OF CHANGE GENERALLY AT WORK IN OUR SOCIETY. AS OUR IDEAS ABOUT CORPORATE ACCOUNTABILITY CHANGE, OUR CONCEPT OF MATERIALITY NECESSARILY CHANGES. THESE CHANGES ARE DIFFICULT TO ASSIMILATE. LAW SCHOOL PROFESSORS AND SEC COMMISSIONERS NO DOUBT THRIVE ON CHANGES IN THE SECURITIES LAWS, BUT CORPORATIONS USUALLY PREFER CONTINUITY. GENERALLY, THE COMMISSION DOES WEIGH THE BENEFITS OF DISCLOSURE AGAINST THE EXTENT OF INVESTOR INTEREST AND THE COSTS AND USEFULNESS OF THE PARTICULAR DISCLOSURE.

YET, THOSE OF YOU IN THIS AUDIENCE WHO HAVE FREQUENT CONTACT WITH SHAREHOLDERS KNOW THAT INVESTOR INTEREST SHIFTS FROM ONE ANNUAL MEETING TO THE NEXT, AND EVEN FROM CORPORATION TO CORPORATION. SINCE OUR CONCEPT OF MATERIALITY IS A FUNCTION OF THE REASONABLE INVESTOR, WE CAN BE NO LESS FLUID THAN THE EXPECTATIONS OF OUR MUTUAL CONSTITUENCY -- THE NATION'S SHAREHOLDERS.