

Client Alert

Corporate Department

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SEC Proposes New Shareholder Proxy Access Rules

On May 20, 2009, the U.S. Securities and Exchange Commission (“SEC”) voted to propose a series of rule amendments that would enhance the ability of shareholders to nominate and solicit proxies for the election of their director nominees. Foremost, the proposed rules would require most publicly traded companies to include in their proxy materials a limited number of shareholder nominees under certain circumstances.

As proposed, the rules would require shareholders to meet certain conditions to be eligible to have their nominees included in a company’s proxy materials:

- *Tiered ownership threshold* – A shareholder, or group of shareholders, would need to hold an aggregate of at least 1, 3 or 5 percent of a company’s voting securities, depending on the size of the company.¹
- *Holding period* – Shareholders would be required to have held their shares for at least one year.
- *Continued ownership* – Shareholders would be required to sign a statement declaring their intention to continue to own their shares through the annual meeting.
- *Change of control* – Shareholders would be required to certify that they are not holding their stock for the purpose of changing control of the company, or to obtain more than minority representation on the board.

Several other key provisions of the proposed rules are worth noting:

- *Limitation on number of nominees* – No more than one shareholder nominee, or that number of nominees that represents up to 25 percent of the company’s board of directors, whichever is greater, would be includable in the company’s proxy materials. In the event a company were to receive shareholder nominations of more candidates than it was required to include in its proxy materials, the company would only need to include the candidate(s) that were first nominated.

¹ At least 1% for a “large accelerated filer” (a company with a worldwide market value of \$700 million or more), or of a registered investment company with net assets of \$700 million or more; at least 3% for an “accelerated filer” (a company with a worldwide market value of \$75 million or more but less than \$700 million), or of a registered investment company with net assets of \$75 million or more but less than \$700 million; at least 5% for a “non-accelerated filer” (a company with a worldwide market value of less than \$75 million), or of a registered investment company with net assets of less than \$75 million.

- *Independence* – The shareholder nominees would need to satisfy the independence standards of the national securities exchange on which the company is traded.
- *Nomination agreements* – The nominating shareholder could not have any direct or indirect agreement with the company regarding the nomination of the nominee.
- *Preexisting right to nominate directors* – If the applicable state law or the company’s governing documents prohibited shareholders from nominating directors, a company would not be required to include shareholder nominees in its proxy materials.
- *New Schedule 14N* – The nominating shareholder would be required to file with the SEC a new Schedule 14N that would contain information concerning the nominating shareholder and its nominees. The Schedule 14N would disclose, among other things, the amount and duration of ownership of securities owned by the nominating shareholder, the nominating shareholder’s intention to own securities through the date of the annual meeting and a certification that the nominating shareholder is only seeking to elect a minority slate and is not seeking to change control of the company.
- *Schedule 13G eligibility* – Nominating shareholders who own more than 5% of a company’s securities would not lose their Schedule 13G eligibility solely as a result of submitting nominations or conducting a solicitation in favor of its nominees.

The proposed rules would also require a company, under certain circumstances, to include in its proxy materials shareholder proposals submitted under Rule 14a-8 that would amend, or request an amendment to, the company’s governing documents to address its nomination procedures or other director nomination disclosure provisions (so long as such amendments did not conflict with SEC rules).

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The proposed rules will be subject to a 60-day comment process before they are finalized and considered by the SEC for approval. Similar proxy access rules have been the subject of vehement debate by proponents and detractors since they were first introduced nearly seven years ago. We expect debate on the proposed rules will be especially robust during the upcoming weeks and all interested parties – including public pension funds, law firms, academics and shareholder advocacy groups – will submit comments to the SEC. We are hopeful that the comment process will help flush out various questions and ambiguities that we believe must be addressed and clarified in order for the rules to be effective from not only a legal but also a proxy mechanics standpoint, such as the following:

- How will a shareholder demonstrate that it owns the full 1, 3 or 5 percent, as the case may be, of the voting securities?

- We note that a shareholder will only be permitted to submit nominations if it is not holding its stock for the purpose of “changing control” of the company. Will the SEC define what is meant by “changing control” of the company?
- Will a shareholder be permitted to nominate directors within the process of these rules and simultaneously solicit its own proxies to elect additional nominees outside the process of these rules?
- Will the new Schedule 14N be subject to SEC comment and clearance?
- Will companies have the ability to reject shareholder nominations in their own discretion if they believe the nominations do not comply with the rules or will there be a no-action process overseen by the SEC?
- Will there be restrictions on the company’s ability to state in its proxy materials that management recommends a vote against the shareholder nominee(s) and the reasons for its recommendation?
- If a shareholder nominee appears on the company’s proxy card, will the election be considered a “non-routine” matter under the NYSE rules, in which case brokers would be prohibited from voting on the election of directors absent specific instructions from the beneficial owners of the shares?
- Will the race to be the first shareholder to submit a nomination result in the exclusion of the most qualified candidates from ultimately appearing on the ballot?

Please feel free to contact any of the partners listed below or any corporate partner with whom you work if you would like to discuss the proposed rules and their potential ramifications.

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