1325 AVENUE OF THE AMERICAS ▪ NEW YORK, NEW YORK 10019
TELEPHONE: 212.451.2300 ▪ FACSIMILE: 212.451.2222

Client Alert

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Texas Legislature's Proposed "Bring Business to Texas and Fairness in Disclosure Act" Seeks to Impose Draconian Disclosure Requirements on Shareholder Activists and Proxy Advisory Firms

The Legislature of the State of Texas has proposed a new bill that would require certain investors in publicly traded companies headquartered in Texas and proxy advisory firms making recommendations with respect to publicly traded Texas-based companies to comply with a set of austere disclosure requirements. The proposed "Bring Business to Texas and Fairness in Disclosure Act" (the "Texas Act") is purportedly intended to "foster and promote the immediate and full disclosure of the individual ownership of persons who are activist investors" and "prohibit discrimination by a proxy advisory firm." The unduly burdensome, excessive and inequitable scope of the proposed disclosure requirements is like nothing we have ever seen proposed by any state. If the Texas Act is adopted, it could have a chilling effect on shareholder activism and proxy advisory work with respect to public companies that have a specified presence in Texas, which, in turn, would help entrench management and the Boards of underperforming Texas-based companies.

The Texas Act would apply to any person who (i) beneficially owns any securities of a "Texas-based public company" (defined as a publicly traded company whose "headquarters" are located in Texas) and (ii) is an "activist investor" (defined as any person who directly or indirectly nominates or attempts to nominate directors or makes or attempts to make a shareholder proposal with respect to the company). "Beneficial owner" is defined broadly to capture both economic and beneficial ownership of a security. "Headquarters" is defined broadly to capture any public company with a location at which a president, chief executive officer or any other senior member of the company's management team "routinely performs duties" in such capacities. Accordingly, even if a company does not have its principal place of business in Texas, it appears that the proposed rules would apply to the company if a senior member of its management team

attorneys

Steve Wolosky
swolosky@olshanlaw.com
212.451.2333

Andrew M. Freedman
afreedman@olshanlaw.com
212.451.2250

Ron S. Berenblat
rberenblat@olshanlaw.com
212.451.2296

practice

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performs his or her duties in a different office that happens to be located in Texas.

The bill is currently pending with the Texas House Investments & Financial Services Committee and has a proposed effective date of September 1, 2017.

Disclosure Requirements Applicable to Activists

Under the proposed rules, within 10 days after becoming both a beneficial owner and an activist investor of a Texas-based public company, the shareholder would need to file with the Texas Securities Commissioner and deliver to the company a certified statement containing:

- The name, address and other basic information regarding the shareholder;
- The nature of the shareholder's beneficial ownership;
- All plans, intentions, motives, strategies, and objectives of the shareholder with respect to becoming an activist investor and with respect to the nomination or shareholder proposal;
- All notes, e-mails, memoranda, letters, communications, proposals, analyses, spreadsheets, presentations, instruments, and any other documents relating to the shareholder's plans, intentions and objectives; and
- All costs and expenses paid, incurred and anticipated by the shareholder in connection with these plans, intentions and objectives.

The foregoing information would also need to be disclosed by all beneficial owners of the shareholder, looking through the ownership chain until a natural person is reached. All of the disclosed information would be considered public information "for all purposes" and the shareholder would be prohibited from requesting that the company sign a confidentiality agreement or otherwise treat the information as private.

In addition, any person who could potentially become an activist investor of a Texas-based public company and who solicits money from an investor must, before accepting money and at least once each year, provide written notice to any such prospective investor stating that it could potentially become subject to these rules and a copy of the Texas Act.

Disclosure Requirements Applicable to Proxy Advisory Firms

The Texas Act would also apply to any proxy advisory firm that "publishes or otherwise provides an analysis or a recommendation to one

attorneys

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rberenblat@olshanlaw.com
212.451.2296

practice

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or more shareholders" of a Texas-based public company concerning a nomination to the board or a shareholder proposal of an activist investor. Under the proposed rules, concurrently with providing such an analysis or recommendation, the proxy advisory firm would need to file with the Texas Securities Commissioner and deliver to the company the following information:

- 5 years of financial statements of the proxy advisory firm;
- The names of all beneficial owners of the proxy advisory firm, looking through the ownership chain until a natural person is reached; and
- All notes, e-mails, memoranda, letters, communications, proposals, analyses, spreadsheets, presentations, instruments, and any other documents relating to the discussions and deliberations that resulted in the proxy advisory firm's analysis or recommendation.

As proposed, any violation of the Texas Act would constitute a Class C misdemeanor and any penalty would be imposed on the senior executive officer of the entity that failed to make the disclosure in his or her personal capacity.

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The proposed rules would impose oppressive disclosure requirements upon activists that far exceed the scope of disclosure requirements already established under federal securities laws. Requiring an activist to make its entire body of work regarding an activist situation a matter of public record is alarming and would create a dangerous precedent for other states that may be contemplating similar legislation. Forcing an activist to also disclose internal emails and other private communications is simply beyond the realm of prudence and reasonableness. We would expect the proxy advisory firms to have similar views regarding the proposed disclosure requirements that they would be required to comply with. We have further concerns that, if enacted, public companies incorporated in other states may seek to establish "headquarters" in Texas to avail themselves of these defensive, activism-chilling provisions. Please contact the Olshan attorney with whom you regularly work or one of the attorneys listed below if you have questions.

attorneys

Steve Wolosky
swolosky@olshanlaw.com
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