

Securities Alert

SEC Adopts Proxy Access

August 26, 2010

On August 25, 2010, the Securities and Exchange Commission (SEC), by a 3-2 vote, adopted new rules that will allow shareholders to have their director nominees included in company proxy materials.¹ The new Rule 14a-11 will allow a shareholder (or group of shareholders) who owns at least 3 percent of the voting stock of a company and who has held the shares continually for at least three years to use management's proxy materials for the nomination of up to 25 percent of the company's board of directors, provided the shareholder is not seeking a change of control of the company.

The SEC's action follows on the heels of the recently passed Dodd-Frank Wall Street Reform and Consumer Protection Act, which gave the SEC explicit authority to adopt proxy access rules under terms and conditions that the SEC determines are appropriate. We highlight below some of the key features of the new regime and will distribute a more expansive client alert in the near future detailing the new rules and possible courses of action that companies may need to consider.

- **Shareholder Eligibility Requirements:** Shareholders seeking to have their nominees included in the company's proxy statement must own at least 3 percent of the company's voting stock and must have held the shares continually for at least three years. Shareholders may form groups to aggregate their holdings to satisfy the share ownership requirement, but nominating shareholders cannot hold their stock with the intent of changing control of the company or gaining more seats on the board than is permitted under the new rules. The new rules include detailed provisions on how to calculate ownership for eligibility purposes.
- **Companies Subject to New Rules:** The new rules apply to companies that are subject to the proxy rules under the Securities Exchange Act of 1934 ("Exchange Act") (including registered investment companies), other than companies that are subject to the proxy rules solely because they have a class of registered debt. The SEC has, however, delayed the effectiveness of the new rules for smaller reporting companies² for three years to give these companies additional time to observe how the rules operate and to prepare for their implementation.
- **Maximum Number of Nominees:** A company will be required to include in its proxy materials no more than one shareholder nominee or the number of nominees that represents 25 percent of the company's board of directors, whichever is greater. If a company receives more shareholder director nominees than it is required to include, the company must include the nominee(s) of the nominating shareholder or group with the highest qualifying voting power percentage. Note that this differs from the SEC's proposing release on proxy access, which would have required companies to include director nominees submitted by the nominating shareholder or group that first provided timely notice to the company.

¹ SEC Release Nos. 33-9136; 34-62764, "Facilitating Shareholder Director Nominations" (August 25, 2010), which is available at <http://www.sec.gov/rules/final/2010/33-9136.pdf>

² The definition of "smaller reporting company" is set forth in Exchange Act Rule 12b-2 and includes, subject to certain exceptions, companies that have a public float of less than \$75 million as of the last business day of their most recently completed second fiscal quarter.



- **Nominee Eligibility Requirements:** Director candidates nominated by shareholders must satisfy the following requirements—
 - Nominees must meet any objective independence standards of the applicable securities exchange. Nominees do not, however, have to be independent of the stockholders who nominate them.
 - The nominee’s candidacy or, if elected, board membership must not violate controlling federal law, state law, foreign law or rules of the applicable securities exchange.
 - Neither the nominee nor the nominating shareholder is allowed to have an agreement with the company regarding the nomination.
- **Notice Requirements on Schedule 14N:** A nominating shareholder or group must provide the company with a notice on Schedule 14N and also file the notice with the SEC. Schedule 14N requires detailed information on, among other things, the nominating shareholder or group and its nominee(s) and must be transmitted to the company and filed with the SEC no earlier than 150 calendar days and no later than 120 calendar days before the anniversary of the date that the company mailed its proxy materials for the prior year’s annual meeting.
- **Rule 14a-8 Shareholder Proposals:** The SEC has also amended Rule 14a-8 under the Exchange Act to require companies to include any shareholder proposals that would amend, or request an amendment to, a company’s governing documents concerning director nomination procedures or other director nomination disclosure provisions that do not conflict with new Rule 14a-8, other SEC proxy rules or applicable law. This amendment gives shareholders the flexibility of proposing additional procedures that provide greater access than the new rules described above.
- **Effective Date:** The new rules become effective 60 days after publication in the *Federal Register*. Under the new rules, however, shareholders must submit nominees no later than 120 calendar days before the anniversary date that the company mailed its proxy materials for the prior year’s annual meeting. Therefore, a company will be subject to the new rules during the 2011 proxy season if this 120-day deadline falls on or after the effective date of the new rules.

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