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What Does Proxy Access Mean Today?

Shareholders may be able to gain access to companies' proxy statements through shareholder proposals, even though the Securities and Exchange Commission's (the SEC's) proposed Rule 14a-11 was overturned by the courts. Therefore, companies should consider whether they need to take steps to prepare for shareholders seeking to propose their own directors. This Legal Alert discusses the rules governing a shareholder proposal that seeks to institute proxy access procedures (a proxy access proposal) and how companies should prepare for the upcoming proxy season.

On September 20, 2011, amendments to Rule 14a-8 of the Securities Exchange Act of 1934 (the Rule 14a-8 Amendments) became effective. These amendments modify Rule 14a-8 to permit proxy access proposals that seek to add procedures to companies' organizational documents that would allow shareholders to more easily nominate directors in future proxy statements. As such, proxy access may now be achieved through "private ordering," on a company-by-company basis, rather than the universal proxy access proposed by recently vacated Rule 14a-11.

Where Have We Been?

The SEC adopted the Rule 14a-8 Amendments on August 25, 2010 concurrently with its adoption of Rule 14a-11, the proxy access rule, citing November 15, 2010 as the effective date for both the Rule 14a-8 Amendments and Rule 14a-11. Rule 14a-11 would have required companies to "include information about shareholder nominees for director in company proxy statements, and the names of the nominee or nominees as choices on proxy cards." It generally would have applied to any proposal by a shareholder who had held 3% of the company's voting shares for three years or more prior to the submission of the proposal.¹

On September 29, 2010, before the rules became effective, the Business Roundtable and the U.S. Chamber of Commerce filed a Petition for Review in the U.S. Court of Appeals for the District of Columbia Circuit (the D.C. Circuit) challenging Rule 14a-11's legality. Importantly, the petition did not challenge the legality of the Rule 14a-8 Amendments. Nevertheless, the SEC granted a stay on the effect of both Rule 14a-11 and the Rule 14a-8 Amendments until the D.C. Circuit rendered a decision on the legality of Rule 14a-11.

On July 22, 2011, the D.C. Circuit vacated Rule 14a-11 as an "arbitrary and capricious" exercise of the SEC's authority because the SEC did not properly consider the rule's economic effects. Shortly thereafter, the SEC announced that it would not appeal the D.C. Circuit's decision and would remove the stay on the Rule 14a-8 Amendments. The Rule 14a-8 Amendments are now effective and will be applicable for the 2012 proxy season.

¹ For more on the proxy access rule, see Sutherland [Legal Alert](#): "A New World Order: What Your Board Should Know About Proxy Access," September 23, 2010, and [Legal Alert](#): "What Will Proxy Access Mean? The Debate Over Proxy Access," July 9, 2009.

Where Are We Today?

Subject to the exclusions discussed below, the Rule 14a-8 Amendments require a company to include a proxy access proposal in its proxy materials provided that the proposing shareholder has held at least \$2,000 of the company's securities for at least one year.

From late 2007 until the adoption of the Rule 14a-8 Amendments, a company could have potentially excluded a proxy access proposal under Rule 14a-8(i)(8), or the "election exclusion," which prohibited proposals related to a nomination or election of a director, or procedures for this process. After the Rule 14a-8 Amendments, proposals that would affect the current director elections are still prohibited, so a company may now rely on Rule 14a-8(i)(8) to exclude a proxy access proposal from its proxy statement only if the proposal:

- Would disqualify a nominee who is standing for election;
- Would remove a director from office before his or her term expired;
- Questions the competence, business judgment, or character of one or more nominees or directors;
- Seeks to include a specific individual in the company's proxy materials for election to the board of directors; or
- Otherwise could affect the outcome of the upcoming election of directors.

How to Prepare for Potential Proxy Access Proposals

The upcoming proxy season will reveal whether the Rule 14a-8 Amendments will lead to a spike in proxy access proposals. Shareholders might only focus on a small number of very large companies that have historically been unresponsive to investors. Indeed, during the 2007 proxy season (the last season in which proxy access proposals were permitted), shareholders from only four companies successfully filed proxy access proposals. Of those four proposals, three went to a vote and one received a majority.² In addition, shareholders must satisfy a host of additional procedural and substantive requirements under clauses (1)-(13) of Rule 14a-8(i) before their proposals may appear in a company's proxy materials. Nevertheless, companies should be prepared to address a possible proxy access proposal by taking the following steps:

- **Communicate with significant shareholders.** Consider engaging investors to ensure their concerns are being addressed and the company's current board membership is acceptable.
- **Review nominating procedures.** Ensure shareholder proposals comply with the nominating procedures of company bylaws, including any advance notice provisions, and review the process required to augment or change the nominating procedures.
- **Define director qualifications.** Examine director qualification bylaws or consider adopting such bylaws to ensure they are written in a way that gives the board discretion to interpret the qualifications of any director nominee.
- **Review committee charters.** Review and possibly revise the corporate governance and nominating committee charters and related bylaws to address the vetting of shareholder nominees.

² Ted Allen, "Will Proxy Access Appear on Corporate Ballots in 2012?," ISS Governance Blog, *available at* <http://blog.issgovernance.com/gov/2011/09/proxy-access-on-the-ballot-in-2012.html> (last visited Oct. 12, 2011).

- **Review guidelines issued by proxy advisory firms.** Institutional Shareholder Services (ISS) plans to recommend votes on proxy access proposals on a case-by-case basis, taking into account (i) the ownership threshold proposed in the proposal and (ii) the proponent's rationale for the proposal at the targeted company in terms of board and director conduct.



If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.

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