

SEC Proposes Rules Facilitating Shareholder Director Nominations

June 23, 2009

On June 10, 2009, the Securities and Exchange Commission (the “SEC”) published proposed amendments to the federal proxy rules that would require companies, under certain circumstances, to include in their proxy materials:

- A shareholder’s or group of shareholders’ nominees for director, so long as the shareholder or group is not seeking a change of control of the company and the nomination is not prohibited under state law or the company’s governing documents; and
- Shareholder proposals that would amend, or that request an amendment to, a company’s governing documents regarding nomination procedures or disclosures related to shareholder nominations, provided the proposal does not conflict with the new rules.^{1, 2}

These changes would be implemented mainly through the adoption of new Rule 14a-11 and amendments to Rule 14a-8(i)(8), the so-called “election exclusion.” To facilitate proxy access, the SEC is also proposing additional exemptions from the federal proxy rules and beneficial ownership reporting requirements.

The SEC is soliciting comments on the proposed rules. Comments are due by August 17, 2009.

Director Nominations by Shareholders Using Company Proxy Materials – Proposed Rule 14a-11

Proposed Rule 14a-11 would require companies to include shareholder nominees for director in their proxy statement and form of proxy, if certain requirements are met, provided that:

- The nominating shareholder is not seeking a change of control of the company or to gain more than a limited number of seats on the company’s board; and

¹ See SEC Release No. 33-9046 (Facilitating Shareholder Director Nominations) (June 10, 2009) (the “Proposing Release”), available [here](#). The SEC proposed the new rules at an open meeting on May 20, 2009. See our Client Alert of May 27, 2009 entitled “Proxy Access Developments,” available [here](#).

² On May 19, 2009, Senators Charles Schumer (D-N.Y.) and Maria Cantwell (D-Wash.) introduced the Shareholder Bill of Rights Act of 2009 and on June 12, 2009, Rep. Gary Peters (D-Mich.) introduced the Shareholder Empowerment Act of 2009, each of which would provide shareholders with the ability to include director nominees in companies’ proxy statements. See our Client Alert of June 17, 2009 entitled “The Shareholder Bill of Rights Act of 2009,” available [here](#).

- State law and the company's certificate of incorporation and/or bylaws do not prohibit shareholders from nominating director candidates.

Maximum Number of Nominees

Shareholders would not be permitted to request inclusion in a company's proxy materials of more than one nominee or the number of nominees that represents 25 percent of the company's board of directors, whichever is greater. This is determined based on the size of the whole board, whether the board is classified or not. Thus, eligible shareholders could nominate one director in a three-member board, and up to two directors in an eight-member board. If 25 percent of the board is not a whole number, the maximum number of shareholder nominees required to be included in a company's proxy materials would be rounded down to the nearest whole number. Incumbent directors who had been nominated by shareholders outside of the Rule 14a-11 process (e.g., pursuant to an applicable state law provision, a company's governing documents or a proxy contest) would not be taken into account for purposes of determining the 25 percent limit.

In the case of a board of directors whose members have staggered terms, where one or more directors currently serving on the board were elected pursuant to Rule 14a-11, the maximum number of shareholder nominees allowed under the rule would be calculated relative to the size of the whole board and not the number of directors that are up for election. This is intended to prevent attempts to change control of a company or gain more than a limited number of seats on a company's staggered board by repeatedly nominating additional candidates for director each time a different class of directors is up for election.³

In any given year, if more than one shareholder or group is eligible to have its nominees included in a company's proxy materials pursuant to Rule 14a-11, the company would be required to include the nominee or nominees of the first nominating shareholder or group from which it received timely notice of intent to nominate a director pursuant to the rule, up to and including the total number of shareholder nominees required to be included. If such first nominating shareholder or group does not nominate the maximum number of directors allowed under the rule, the nominee(s) of the next nominating shareholder or group that provided timely notice of intent to nominate a director pursuant to the rule would be included in the company's proxy materials, up to the

³ In the case of an unclassified board, where shareholder nominees have been elected to the board pursuant to Rule 14a-11, those directors, if nominated by the company for election at the next annual meeting, would no longer be counted in determining the maximum number of shareholder nominees allowed under the rule.

maximum available number of shareholder nominees required to be included.⁴

Interaction with State Law and the Company's Governing Documents

Although state law and the company's governing documents⁵ may prohibit shareholders from nominating directors, according to the Proposing Release, there are no laws in any state or the District of Columbia that currently prohibit shareholders from nominating directors (although such laws, or state laws that permit a company to prohibit such nominations in its governing documents, could be enacted in the future).⁶

⁴ In this respect, the current proposal differs from the SEC's 2003 proxy access proposal (SEC Release No. 34-48626) (Oct. 14, 2003) (the "2003 Proposal") that instead gave priority to the largest shareholder or group. The new proposal may provide greater certainty for the company receiving the nomination, and the shareholder or group submitting it, but may also result in a race among nominating shareholders to be first in.

⁵ It is unclear if a company under Delaware law could validly "opt out" of Rule 14a-11 by prohibiting in its governing documents shareholders from nominating director candidates and whether such a provision would be enforceable. The Delaware Chancery Court, in its 2002 decision in *Harrah's Entertainment, Inc. v. JCC Holding Company*, 802 A.2d 294 (Del.Ch. 2002), said that:

Because of the obvious importance of the nomination right in our system of corporate governance, Delaware courts have been reluctant to approve measures that impede the ability of stockholders to nominate candidates. Put simply, Delaware law recognizes that the "right of shareholders to participate in the voting process includes the right to nominate an opposing slate." And, "the unadorned right to cast a ballot in a contest for [corporate] office . . . is meaningless without the right to participate in selecting contestants. As the nominating process circumscribes the range of choice to be made, it is a fundamental and outcome-determinative step in the election of officeholders. To allow for voting while maintaining a closed selection process thus renders the former an empty exercise."

Id. at 310-11 (citations omitted). However, Section 212 of the Delaware General Corporation Law and the courts seem to recognize that companies' governing documents may contain restrictions on fundamental voting rights. For example, in *Harrah's* the court noted that "[w]hen a corporate charter is alleged to contain a restriction on the fundamental electoral rights of stockholders under default provisions of law – such as the right of a majority of the shares to elect new directors or enact a charter amendment – it has been said that the restriction must be 'clear and unambiguous' to be enforceable." *Id.* at 310 (citations omitted).

⁶ In the event of any such prohibition contained in a company's governing documents, shareholders who want to amend the relevant provision may seek to do so by submitting a shareholder proposal under Rule 14a-8(i)(8), as proposed to be amended. As noted in our May 27, 2009 Client Alert, Delaware has recently adopted new Sections 112 and 113 of the Delaware General Corporation Law (to be effective August 1, 2009), expressly authorizing Delaware corporations to adopt bylaws that, respectively, grant shareholders the right to include in the corporation's proxy materials shareholders' nominees for the election of directors and provide for mandatory reimbursement by the corporation of expenses incurred by a shareholder in soliciting proxies in connection with an election of directors, subject in each case to such reasonable procedures or conditions as the bylaws may prescribe. Similar changes are being considered to the Model Business Corporation Act, which many states have adopted as their general corporation statute. Furthermore, in 2007, North Dakota passed the North Dakota Publicly Traded Corporations Act that gives proxy access to shareholders who have owned more than 5 percent of the corporation's voting securities continuously for a period of two years. In addition, the North Dakota Publicly Traded Corporations Act also requires corporations to reimburse nominating shareholders regardless of their level of ownership for proxy solicitation expenses in proportion to the number of nominees who are elected. These requirements only apply to corporations incorporated in North Dakota that have elected to be subject to these requirements.

A company's governing documents may provide for nomination or disclosure rights in addition to those provided by Rule 14a-11 (e.g., inclusion of a nominee regardless of share ownership by the nominating shareholder). State law also could provide for additional rights. However, if a company's governing documents permit the inclusion of shareholder nominees in the company's proxy materials, but impose more restrictive eligibility standards or mandate more extensive disclosures than those required by Rule 14a-11, the company could not exclude a nominee submitted by a shareholder in compliance with Rule 14a-11 on the grounds that the shareholder or the nominee failed to meet the more restrictive standards included in the company's governing documents. As stated in the Proposing Release, "companies may not opt out of Rule 14a-11 by adopting alternate requirements for inclusion of shareholder nominees for director in the company's proxy materials."⁷

Shareholders would be able to continue to use the procedures currently available for election contests (and bear the related expenses). To the extent available, Rule 14a-11 would not be preempted by the pendency of a third-party solicitation in opposition pursuant to Rule 14a-12(c).

Applicability of Rule 14a-11

Rule 14a-11 would apply to all companies subject to the federal proxy rules (except companies that are subject to the proxy rules solely because they have a class of debt securities registered under Section 12 of the Securities Exchange Act of 1934, as amended (the "Exchange Act")),⁸ including investment companies registered under the Investment Company Act of 1940, as amended (the "Investment Company Act").

Unlike the 2003 Proposal (which conditioned the ability of a shareholder to submit director nominations on the occurrence of certain specified events),⁹ the applicability of Rule 14a-11 would not require a triggering event.

⁷ See Proposing Release, footnote 152. As noted by Commissioner Paredes at the SEC's May 20 open meeting, this would be true regardless of whether the alternate requirements were adopted by the company's board of directors in the exercise of its fiduciary duties or pursuant to a shareholder vote.

⁸ Companies that voluntarily register a class of equity securities pursuant to Section 12(g) of the Exchange Act would be subject to the new rule. The rule would not apply to domestic companies that are subject to the reporting requirements of the Exchange Act solely by virtue of Section 15(d) thereof, as they are not covered by the proxy rules, or to "foreign private issuers" (as defined in Rule 3b-4 under the Exchange Act), as they are exempt from the proxy rules pursuant to Exchange Act Rule 3a12-3(b).

⁹ See our May 27, 2009 Client Alert for more details.

Shareholder Eligibility Requirements

The SEC is proposing that only holders of a significant, long-term interest in a company be able to have their nominees for director included in the company's proxy materials pursuant to Rule 14a-11. To meet the minimum ownership requirements described below, shareholders would be permitted to aggregate their holdings and act as a nominating shareholder group.

In order to be eligible, a nominating shareholder (or nominating shareholder group) would have to have beneficially owned the requisite amount of voting securities of the company continuously for at least one year (as of the date the shareholder provides notice to the company of its intent to include a nominee in the company's proxy materials pursuant to Rule 14a-11). Depending on a company's size, the nominating shareholder or group would need to meet one of the following ownership requirements:

- Beneficial ownership of at least 1 percent of the securities entitled to be voted on the election of directors at the annual meeting of shareholders (or a special meeting in lieu of the annual meeting), with respect to "large accelerated filers" (*i.e.*, companies with an aggregate worldwide market value of voting and non-voting common equity held by non-affiliates of \$700 million or more) or registered investment companies with net assets of \$700 million or more;
- Beneficial ownership of at least 3 percent of the securities entitled to be voted on the election of directors at the annual (or special) meeting of shareholders, with respect to "accelerated filers" (*i.e.*, companies with an aggregate worldwide market value of voting and non-voting common equity held by non-affiliates of \$75 million or more but less than \$700 million) or registered investment companies with assets of \$75 million or more but less than \$700 million; or
- Ownership of at least 5 percent of the securities entitled to be voted on the election of directors at the annual (or special) meeting of shareholders, with respect to "non-accelerated filers" (*i.e.*, companies with an aggregate worldwide market value of voting and non-voting common equity held by non-affiliates of less than \$75 million) or registered investment companies with net assets of less than \$75 million.¹⁰

¹⁰ The instructions to Rule 14a-11 specify how and as of what date the net asset determination for registered investment companies would be made, as well as how the securities entitled to be voted on the election of directors would be counted (for both registered investment companies and other reporting companies).

Eligibility also would be conditioned on the nominating shareholder or group intending to own the requisite voting securities through the date of the shareholder meeting.¹¹

The notice to the company would be made on proposed new Schedule 14N, which would be required to be filed with the SEC on the date that it is provided to the company.

Other Rule Changes: Proxy Solicitation, Beneficial Ownership and Section 16

Formation of a Nominating Shareholder Group. In order to permit communications among shareholders intending to aggregate their holdings to meet the minimum ownership thresholds of Rule 14a-11, the SEC is proposing to exempt from the federal proxy rules certain written solicitations made by or on behalf of shareholders in connection with the formation of a nominating shareholder group, provided such materials are filed with the SEC no later than the date the material is first published, sent or given to shareholders.¹² This exemption would not apply to oral communications or to solicitations made when seeking to have a nominee included in a company's proxy materials pursuant to a procedure specified in the company's governing documents or pursuant to applicable state law provisions.¹³

Solicitation Activities. In addition, solicitations by or on behalf of a nominating shareholder or group in support of a nominee included in the company's proxy materials in accordance with Rule 14a-11 would not be subject to the federal proxy rules (and thus require dissemination of proxy materials) if:

- The soliciting party (1) does not, at any time during such solicitation, seek directly or indirectly, either on its own or another's behalf, the power to act as proxy for a shareholder and (2) does not furnish or otherwise request, or act on behalf of a

¹¹ The notice to the company would include a representation that the nominating shareholder or group satisfies the eligibility requirements of the rule and a statement of the shareholder's or group's intent with respect to continued ownership of the requisite voting securities through the date of the shareholder meeting and after the election.

¹² Any such written communication (including any electronic communication, such as an email or website posting) may include no more than (1) a statement of the shareholder's intent to form a nominating shareholder group in order to nominate a director under the proposed rule, (2) identification of, and a brief statement regarding, the potential nominee or nominees or, where no nominee or nominees have been identified, the characteristics of the nominee or nominees that the shareholder intends to nominate, if any, (3) the percentage of securities that the shareholder beneficially owns or the aggregate percentage owned by any group to which the shareholder belongs and (4) the means by which shareholders may contact the soliciting party.

¹³ Shareholders would continue to have the option to structure their solicitations, whether written or oral, to comply with an existing exemption from the proxy rules, including the exemption for solicitations of no more than 10 shareholders, and the exemption for certain communications that take place in an electronic shareholder forum. See Rules 14a-2(b)(2) and (b)(6).

person who furnishes or requests, a form of revocation, abstention, consent or authorization;

- Each written communication includes (1) the identity of the nominating shareholder or group and a description of his or her direct or indirect interests, by security holdings or otherwise and (2) a prominent legend in clear, plain language advising shareholders that a shareholder nominee is or will be included in the company's proxy statement and to read the company's proxy statement when it becomes available because it includes important information (the legend also must explain to shareholders that they can find the proxy statement, other soliciting material and any other relevant documents on the SEC website); and
- Any soliciting material published, sent or given to shareholders is filed by the nominating shareholder or group with the SEC no later than the date the material is first published, sent or given to shareholders (and three copies of the material are at the same time filed with, or mailed for filing to, each national securities exchange on which any class of securities of the company is listed and registered).¹⁴

Beneficial Ownership. To the extent a nominating shareholder group beneficially owns in the aggregate more than 5 percent of a company's securities that are eligible to vote for the election of directors, it will need to consider whether its members have formed a "group" that is required to file beneficial ownership reports under the Exchange Act (and reassess the group's filing obligations after the election has taken place). Under the proposed rules, however, to the extent a nominating shareholder or group is otherwise eligible to file as a passive investor or qualified institutional investor on Schedule 13G, it will not lose such eligibility by reason of forming a shareholder group solely for the purpose of nominating directors pursuant to Rule 14a-11, the nomination of directors pursuant to the rule, soliciting activities in connection with such a nomination (including soliciting in opposition to a company's nominees) or the election of any such nominees to the company's board. After the election of directors, a nominating shareholder or group would need to reassess its eligibility to continue to report on Schedule 13G. For example, if a nominating shareholder is the nominee, and is successful in being elected to the board of a company, the shareholder would most likely be ineligible to continue filing on Schedule 13G because of its ability as a director to influence the management and policies of the company. These exceptions would apply to activities solely in connection with a nomination under

¹⁴ The company can rely on existing Rule 14a-12 to solicit outside the proxy statement if it wishes to solicit in favor of its nominees or against the shareholder nominees, because it will ultimately file a proxy statement with the SEC.

Rule 14a-11 and not to nominating shareholders or groups that submit a nomination pursuant to an applicable state law provision or a company's governing documents.

Insider Reporting and Short-Swing Profit Rules. The SEC is not proposing a similar exclusion with respect to the determination of whether a 10 percent group has been formed for purposes of Section 16 of the Exchange Act. Therefore, such group would be analyzed in the same way any other group would currently be analyzed in determining whether a group has been formed and whether Section 16 applies.¹⁵ Nominating shareholders also should be mindful of the possibility that, if they are successful in getting a nominee elected to a company's board pursuant to Rule 14a-11, they may themselves be deemed directors of that company under the "deputization" theory.¹⁶

Shareholder Nominee Requirements

No Violation of Applicable Law. A company would not be required to include a shareholder nominee in its proxy materials if the nominee's candidacy or, if elected, board membership would violate applicable state law, the company's governing documents, federal law or rules of a national securities exchange or national securities association applicable to the company (other than any such rules regarding director independence).¹⁷ The Proposing Release contemplates the possibility that any such violation could be cured and thus not form the basis for exclusion of a nominee. Consistent with this requirement, the notice to the company would be required to include a representation that, to the knowledge of the nominating shareholder or group, the nominee's candidacy or, if elected, board membership would not

¹⁵ In connection with the 2003 Proposal, the SEC had proposed that a group formed solely for the purpose of nominating a director pursuant to proposed Rule 14a-11, soliciting in connection with the election of that nominee or having that nominee elected as a director would not be viewed as being aggregated for purposes of the 10-percent ownership determination under Section 16. In connection with the current proposal, the SEC is taking the view that, because the ownership thresholds under Rule 14a-11 are significantly lower than 10 percent and are generally lower than those proposed in 2003, the lack of an exclusion should not act as a deterrent on the formation of groups.

¹⁶ As described below, the SEC is not proposing standards for establishing the independence of a shareholder nominee for director from the nominating shareholder or group.

¹⁷ However, where the company is subject to the requirements of a national securities exchange or national securities association, the nominating shareholder or group would be required to include in the notice to the company a representation to the effect that, to its knowledge, the nominee is in compliance with the requirements of the exchange or association that sets forth objective independence standards (*i.e.*, that do not require a subjective determination by the board or a committee of the board) and are applicable to the directors of the company generally (as opposed to just the audit committee members). A company, however, could include disclosure in its proxy materials advising shareholders that the shareholder nominee for director would not meet the company's subjective criteria (or, presumably, the more stringent independence requirements contained in the company's governing documents or corporate governance guidelines, if any), as appropriate. In the case of a registered investment company, the nominating shareholder or group would be required to represent that the nominee is not an "interested person" as defined in Section 2(a)(19) of the Investment Company Act.

violate applicable state law, federal law or rules of a national securities exchange or national securities association applicable to the company (other than any such rules regarding director independence).

No Agreement with the Company. To avoid the potential risk of collusion, the nominating shareholder or group would be required to represent in the notice to the company that neither the nominee nor the nominating shareholder (or any member of the nominating shareholder group) has an agreement with the company regarding the nomination. Should there be such an agreement, any nominee or nominees from such shareholder or group would not be counted towards the maximum number of shareholder nominees allowed under Rule 14a-11. For these purposes, however, the following would not be considered a direct or indirect agreement with the company: (1) negotiations with the nominating committee of the company to have the nominee included on the company's proxy card as a management nominee, where those negotiations are unsuccessful and (2) negotiations that are limited to whether the company is required to include the nominee on the company's proxy card in accordance with Rule 14a-11.

No Requirement of Independence from Nominating Shareholder or Group. Unlike the 2003 Proposal, the new rule would not restrict the ability of shareholders to nominate directors with whom they have a relationship, including themselves or their employees.

Affiliate Status of Nominating Shareholder or Group. The proposed new rules would establish a safe harbor for nominating shareholders or groups, clarifying that a nominating shareholder or group will not be deemed an "affiliate" of the company under the Exchange Act or the Securities Act of 1933, as amended (the "Securities Act"), solely as a result of (1) nominating a director or soliciting for the election of such a director nominee or against a company nominee pursuant to Rule 14a-11 or (2) having nominated a director under the proposed rules, if the nominee is then elected, provided the nominating shareholder or group does not have an agreement or relationship with that director, other than relating to the nomination. No similar safe harbor would apply for nominating shareholders that submit a nominee for inclusion in a company's proxy materials pursuant to an applicable state law provision or a company's governing documents, rather than using Rule 14a-11.

Notice and Disclosure Requirements

A nominating shareholder or group would be required to provide to the company and file with the SEC a notice on new Schedule 14N of its intent to submit a nominee or nominees for inclusion in the company's

proxy materials.¹⁸ The deadline for delivering the notice to the company and filing it with the SEC would be the date specified by the company's advance notice provision or, where no such provision is in place, a date "no later than 120 calendar days before the date that the registrant mailed its proxy materials for the prior year's annual meeting."^{19, 20}

Nominations Pursuant to Rule 14a-11. Insofar as it applies to nominations made pursuant to Rule 14a-11, new Schedule 14N would require, among other things:

- The name and address of the nominating shareholder or each member of the nominating shareholder group;
- Information regarding the amount and percentage of securities beneficially owned and entitled to vote at the meeting;
- If the nominating shareholder is not the registered holder of the shares (and has not filed a Schedule 13D, Schedule 13G, Form 3, Form 4 and/or Form 5, or amendments to those documents), a written statement from the "record" holder (usually a broker or bank) of the shares beneficially owned by the nominating shareholder or each member of the nominating group verifying that, as of the date of the notice on Schedule 14N, the shareholder continuously held the securities for at least one year;
- A certification that to the best of the nominating shareholder's or group's knowledge and belief, the securities are not held for the purpose of, or with the effect of, changing control of the issuer or gaining more than a limited number of seats on the board of directors;²¹
- Representations to the effect that (1) the nominating shareholder or group satisfies the eligibility requirements of Rule 14a-11, (2) to the knowledge of the nominating shareholder or group, the candidate's nomination or service on the board, if elected, would

¹⁸ This new notice and filing requirement (and related disclosures) is established under proposed Rule 14n-1 and would apply to nominations made pursuant to Rule 14a-11, as well as nominations made pursuant to applicable state law provisions or a company's governing documents.

¹⁹ See Rule 14a-18.

²⁰ However, if the company did not hold an annual meeting during the prior year or if the date of the upcoming meeting has changed by more than 30 calendar days from the date of the prior year's meeting, then the nominating shareholder or group must provide notice a "reasonable time" before the company mails its proxy materials. In that situation, the company would be required to file a Form 8-K pursuant to proposed new Item 5.07 within four business days after it determines the anticipated meeting date and disclose in the Form 8-K the date by which a shareholder must submit the notice on Schedule 14N.

²¹ Request for comment C.24 in the Proposing Release suggests that this representation would not survive beyond the date of the election of directors. It is unclear to what extent a nominating shareholder or group could change its mind.

not violate applicable state law, federal law or applicable listing standards (other than a standard relating to independence), (3) to the knowledge of the nominating shareholder or group, the nominee meets the objective criteria for independence from the company that are set forth in applicable rules of a national securities exchange or national securities association (or, in the case of a registered investment company or business development company, that the nominee to the board is not an “interested person” of the company as defined in Section 2(a)(19) of the Investment Company Act) and (4) neither the nominee nor the nominating shareholder (or any member of the nominating shareholder group, if applicable) has an agreement with the company regarding the nomination of the nominee;

- A statement from the nominee that the nominee consents to be named in the company’s proxy statement and to serve on the board if elected, for inclusion in the company’s proxy statement;
- A statement that the nominating shareholder or each member of the nominating shareholder group intends to continue to own the requisite amount of securities through the date of the meeting (as well as a statement regarding the nominating shareholder’s or group’s intent with respect to continued ownership after the election);
- Disclosure about the nominating shareholder or group and the nominee for director similar to the disclosure currently required in contested elections (which would be included in the company’s proxy materials);
- Disclosure regarding the nature and extent of the relationships between the nominating shareholder or group and the nominee and the company or any affiliate of the company;²²
- Disclosure of any website address on which the nominating shareholder or group may publish soliciting materials; and
- If desired to be included in the company’s proxy statement, a statement in support of the shareholder nominee or nominees, which may not exceed 500 words.

²² Including (1) any direct or indirect material interest in any contract or agreement between the nominating shareholder or group or the nominee and the company or any affiliate of the company (including any employment agreement, collective bargaining agreement or consulting agreement), (2) any material pending or threatened litigation in which the nominating shareholder or group or nominee is a party or a material participant and that involves the company, any of its officers or directors or any affiliate of the company and (3) any other material relationship between the nominating shareholder or group or the nominee and the company or any affiliate of the company not otherwise disclosed (such as whether the nominating shareholder or group currently has, or has had in the past, an employment relationship with the company or any affiliate of the company, including consulting arrangements).

Schedule 14N would need to be filed with the SEC on the date the notice is first submitted to the company. If any material change occurs in the facts set forth in the initial Schedule 14N, an amendment would be required to be filed promptly. Examples of material changes include the withdrawal of a nominating shareholder or group, or of a director nominee, and the reasons for any such withdrawal. A final amendment to Schedule 14N would be required to be filed (within 10 days of the final results of the election being announced by the company) disclosing the nominating shareholder's or group's current intention with regard to continued ownership of their shares.

Nominations Pursuant to State Law or a Company's Governing Documents. A shareholder notice on Schedule 14N would be required not only in the context of a shareholder nomination made pursuant to Rule 14a-11, but also for inclusion of shareholder nominees in company proxy materials pursuant to an applicable state law provision or a company's governing documents. In this case, the required disclosure would consist mainly of disclosure about the nominating shareholder or group and the nominee for director similar to that currently required in contested elections, but would not include the representations and certifications required with respect to Rule 14a-11 nominations.

Liability for False or Misleading Statements

A nominating shareholder or group would be liable under proposed new paragraph (c) of Rule 14a-9 for any materially false or misleading statements contained in information that is provided to the company in the shareholder's or group's notice on Schedule 14N and any related amendments (whether in reliance on Rule 14a-11, state law or the company's governing documents) and is then included in the company's proxy materials. The company itself would not be liable for information provided by the nominating shareholder or group and included in the company's proxy materials, unless it knows or has reason to know that the information is false or misleading. This information also would not be incorporated by reference into any company filings under the Securities Act, the Exchange Act or the Investment Company Act, unless the company decides to specifically incorporate that information into the filing (in which case it would be subject to the antifraud and civil liability provisions of those statutes).

Process for Excluding a Shareholder Director Nomination That Does Not Comply with Rule 14a-11

A company would have to notify the nominating shareholder or group in writing, no later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the SEC, as to whether the company will or will not include in its proxy materials any

candidate nominated pursuant to Rule 14a-11. The company would not be required to file its proxy statement with the SEC in preliminary form because under the new rules inclusion of shareholder nominee(s) would not *per se* be deemed a solicitation in opposition under Rule 14a-12(c). A company could identify as such any shareholder nominees included in the proxy materials and recommend whether shareholders should vote for or against or withhold votes on those nominees and management nominees on the form of proxy, which is similar to the current practice with respect to shareholder proposals submitted pursuant to Rule 14a-8.²³

A company would not be required to include in its proxy materials a director nominee put forward by a nominating shareholder or group if it determines that:

- Rule 14a-11 is not applicable to the company;
- The nominating shareholder or group has not complied with the requirements of Rule 14a-11;
- The nominee does not meet the requirements of Rule 14a-11;
- Any representation required to be included in the notice on Schedule 14N to the company is false or misleading in any material respect; or
- The company has received more nominees than it is required to include pursuant to Rule 14a-11.

If the company determines that it may exclude a shareholder nominee from its proxy materials, it bears the burden of demonstrating that it may do so, and the following process (modeled after the staff no-action process used in connection with shareholder proposals under Rule 14a-8) would apply:

- No later than 14 calendar days after receipt of a shareholder notice of intent to nominate, the company would notify the nominating shareholder or group in writing of its determination not to include the nominee. Such deficiency notice would need to include an explanation of the company's basis for excluding the nominee.
- Within 14 calendar days after the nominating shareholder or group's receipt of the company's deficiency notice, the

²³ The company would otherwise be required to present the nominees in an impartial manner in accordance with Rule 14a-4. When a shareholder nominee is included, the proposed rules would not permit a company to provide shareholders the option of voting for or withholding authority to vote for the company nominees as a group, but would instead require that each nominee be voted on separately.

nominating shareholder or group must respond to the company in writing and correct any eligibility or procedural deficiencies identified in the deficiency notice. However, neither the composition of a nominating shareholder group nor a shareholder nominee could be changed to correct a deficiency (except that, if more nominees are submitted than the maximum number required to be included by the company, the nominating shareholder or group may specify which nominee(s) are not to be included in the company's proxy materials).

- No later than 80 calendar days before filing its definitive proxy statement and form of proxy with the SEC (or such later date permitted by the staff if the company demonstrates good cause for missing the deadline), the company would notify the SEC if it determines that the deficiency has not been corrected and it still may exclude the shareholder nominee. The notice to the SEC would need to include (1) the identity of the nominating shareholder (or each member of the nominating shareholder group), (2) the name of the nominee(s), (3) an explanation of the company's basis for excluding the nominee(s) and (4) a supporting opinion of counsel when the company's basis for excluding a nominee relies on a matter of state law. The notice would be filed with the SEC and simultaneously provided to the nominating shareholder (or each member of the nominating shareholder group).
- Within 14 calendar days of receiving the company's notice to the SEC described above, the nominating shareholder or group could submit a response to the notice and simultaneously provide a copy of the same to the company.
- The SEC staff may, at its discretion, provide an informal statement of its views to the company and the nominating shareholder or group.
- No later than 30 calendar days before the company files its definitive proxy statement and form of proxy with the SEC, the company would provide the nominating shareholder or group with a notice of whether it will include or exclude the shareholder nominee or nominees.

If the company or the nominating shareholder or group is not satisfied with the view expressed in the staff's informal statement, it could request that the staff seek the SEC's views with respect to the matter. The decision to seek the SEC's view would be at the staff's discretion and typically involve matters of substantial importance and where the issues are novel or highly complex.

Proxy Access Shareholder Proposals - Proposed Amendments to Rule 14a-8(i)(8)

After clarifying and expanding the “election exclusion” as recently as December 2007,²⁴ the SEC is now proposing to amend Rule 14a-8(i)(8) to allow shareholders, under certain circumstances, to require companies to include in their proxy materials shareholder proposals that would amend, or request an amendment to, a company’s governing documents regarding nomination procedures or disclosures related to shareholder nominations. The amendments would be implemented by (1) eliminating the current general prohibition against proposals relating to “a nomination or an election for membership on the company’s board of directors . . . or a procedure for such nomination or election” and (2) in its place, codifying certain prior SEC staff interpretations on the type of shareholder proposals that would be excludable under Rule 14a-8(i)(8).

Election Exclusion Narrowed

As amended, Rule 14a-8(i)(8) would preclude companies from relying on the rule to exclude from their proxy materials shareholder proposals by qualifying shareholders²⁵ that seek to amend a company’s governing documents with respect to nomination procedures or disclosures related to shareholder nominations.

Proposals under the amended rule would still have to fall outside the other substantive exclusions provided by Rule 14a-8 (e.g., the proposal could not, if implemented, cause the company to violate any state, federal or foreign law to which it is subject, and could not be contrary to the federal proxy rules, including Rule 14a-9).²⁶ In addition, any proposal that is in conflict with Rule 14a-11 or applicable state law could be excluded. Therefore, while shareholders could propose amendments that provide for nomination or disclosure rights in addition to those set forth in Rule 14a-11 (such as lower eligibility thresholds),²⁷ they could not submit proposals that prevent a shareholder or shareholder group meeting the requirements of

²⁴ See our May 27, 2009 Client Alert for more details.

²⁵ The current eligibility requirements of Rule 14a-8 would remain unchanged (*i.e.*, the proposing shareholder must have held at least \$2,000 in market value (or 1 percent, whichever is less) of the company’s securities entitled to vote on the proposal at the meeting, for at least one year prior to submitting the proposal). The SEC considered but did not propose new disclosure requirements for shareholders who submit a proxy access proposal under amended Rule 14a-8(i)(8). If any such proposal were to be approved by the company’s shareholders, however, and a nomination is made pursuant to the newly implemented provisions of the company’s governing documents, the nominating shareholder or group would have to comply with the disclosure requirements of new Schedule 14N described above.

²⁶ See Rules 14a-8(i)(2) and 14a-8(i)(3).

²⁷ As noted above, a state could adopt legislation, or a company could decide to amend its governing documents, to provide for nomination or disclosure rights in addition to those provided pursuant to Rule 14a-11.

This memorandum is intended only as a general discussion of these issues. It is not considered to be legal advice. We would be pleased to provide additional details or advice about specific situations. For additional information on this important topic, please feel free to call upon your Dewey & LeBoeuf relationship partner.

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proposed Rule 14a-11 from having their nominee for director included in the company's proxy materials. Moreover, any proposal that would affirmatively excuse nominating shareholders or their nominees from compliance with the liability provisions of proposed Rule 14a-9(c) or the proposed Rule 14a-19 disclosure requirements applicable to shareholder nominations submitted pursuant to an applicable state law provision or a company's governing documents could be excluded.

Codification of Prior Staff Interpretations

In an effort to clarify the scope of the election exclusion – so that it does not allow for proposals that could result in an election contest between management and shareholder nominees without the protections provided by the disclosure and liability provisions of the federal proxy rules – the proposed amendments to Rule 14a-8(i)(8) also would codify certain prior SEC staff interpretations on the type of proposals that would continue to be excludable.²⁸ Specifically, a company would be permitted to exclude a proposal under Rule 14a-8(i)(8) if it:

- 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;
- Nominates a specific individual for election to the board of directors, other than pursuant to Rule 14a-11, an applicable state law provision or a company's governing documents; or
- Otherwise could affect the outcome of the upcoming election of directors.²⁹

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²⁸ According to the Proposing Release, the proposed codification of existing staff interpretations under Rule 14a-8(i)(8) is not intended to alter the staff's historical approach (embodied in Staff Legal Bulletin No. 14 (July 13, 2001)) to permit revisions to cure deficiencies under Rule 14a-8(i)(8).

²⁹ The Proposing Release notes that this "catch-all" language is intended to avoid that new proposals that may be developed over time undermine the purpose of the exclusion.