

## SEC Adopts Proxy Access Rules

**August 27, 2010**

On August 25, 2010, the Securities and Exchange Commission voted 3-to-2 to adopt changes to the federal proxy rules establishing procedures for shareholders to have their director nominees included in company proxy materials.<sup>1</sup> The final rules will become effective 60 days after publication in the Federal Register and will affect many companies in the 2011 proxy season.<sup>2</sup>

The key features of the SEC's proxy access rules include the following:

### Applicability of New Rule 14a-11

- New Rule 14a-11 establishes a federal right to proxy access that does not require companies or their shareholders to opt in or triggering events to occur to make proxy access available.
- Companies and their shareholders are prohibited from opting out of or limiting the scope of the proxy access rules, but shareholders may submit proposals under Rule 14a-8 to establish a procedure in the company's governing documents to expand the scope of proxy access through conditions that are less restrictive than Rule 14a-11.
- The final rules apply to all companies subject to the SEC's proxy rules,<sup>3</sup> including investment companies, except for
  - companies subject to the proxy rules solely because of debt securities registered under Section 12 of the Exchange Act or
  - where state law, foreign law or the company's governing documents prohibit shareholders from nominating directors.
- The effective date for smaller reporting companies is deferred for three years to allow the SEC to monitor implementation of the

<sup>1</sup> See SEC Release Nos. 33-9136; 34-62764 (Facilitating Shareholder Director Nominations) (August 25, 2010) (the "Adopting Release"), available [here](#).

<sup>2</sup> If the rules become effective November 1, 2010, they would be available to eligible nominating shareholders and groups of shareholders of companies that mailed proxy materials for their 2010 annual meeting on or after March 1, 2010.

<sup>3</sup> Foreign private issuers are not subject to the proxy access rules because they are exempt from the federal proxy rules. See Rule 3a12-3(b) under the Securities Exchange Act of 1934, as amended (the "Exchange Act").

rules and determine whether to amend the rules before they become effective for such companies.

### **Requirements for Use of Rule 14a-11**

- Proxy access is available to a shareholder or shareholder group that has continuously held at least three percent of the total voting power of a company's securities entitled to vote on the election of directors for at least three years as of the date the shareholder or group gives notice on new Schedule 14N of its intent to use Rule 14a-11.
  - Shareholders are permitted to aggregate their holdings to form a nominating shareholder group that satisfies the three percent ownership threshold.
  - A nominating shareholder or group must hold both investment and voting power with respect to the securities, either directly or through a person acting on behalf of the shareholder or group. Voting power is reduced by any shares that have been sold in a short sale.
  - Shares may not be borrowed to satisfy the three percent ownership threshold, but shares loaned to a third party may be counted if the nominating shareholder or group has the right to recall the loaned shares and will do so when notified that any of its director nominees will be included in the company's proxy materials.
- A nominating shareholder or group must continue to hold the amount of securities used to satisfy the three percent ownership threshold through the date of the meeting and state its intent with respect to continued ownership after the election.
- A nominating shareholder or group may not hold any company securities with the purpose or effect of changing control of the company or gaining more seats on the board than permitted by Rule 14a-11.
- Notice on Schedule 14N must be provided during a window period of 120 to 150 days before the anniversary of the mail date for the prior year's annual meeting.

### **Maximum Number of Nominees and Priority**

- A nominating shareholder or group may nominate one director or 25 percent (rounded down) of a company's entire board of directors, whichever is greater, even where the board is classified

and the number of board seats up for election is less than the total number of board seats.

- If more than the maximum number of nominees are submitted by eligible nominating shareholders or groups, the nominating shareholder or group with the highest voting power percentage will have its nominee(s) included in the company's proxy materials.

### **Eligibility of Nominee and Related Disclosure**

- The nominee's candidacy or board membership may not violate applicable federal, state or foreign law or national securities exchange rules.
- A nominating shareholder or group must disclose, to the best of its knowledge, whether its nominee meets the director qualification standards set forth in the company's governing documents.
- The nominee must meet the objective director independence criteria of the national securities exchange or association on which the company's securities are listed.
- The nominating shareholder or group must disclose any relationship with its nominee, and the nominating shareholder or group and its nominee are prohibited from having a direct or indirect agreement with the company regarding the nomination.

### **Notice of Inclusion or Exclusion of Nominee**

- A company must notify the nominating shareholder or group no later than 30 days before the company files its definitive proxy statement if it determines to include the nominee(s).
- A company must notify the nominating shareholder or group no later than 14 days after the applicable deadline for a shareholder to give notice on a Schedule 14N if it determines it may exclude that nominating shareholder's or group's nominee(s) and then follow specific rules for exclusion similar to those in Rule 14a-8.

### **New Proxy Solicitation Exemptions**

- New Rule 14a-2(b)(7) and Rule 14a-2(b)(8) provide limited exemptions from the proxy solicitation rules for oral and written communications by or on behalf of a nominating shareholder or group in connection with
  - forming a nominating shareholder group pursuant to Rule 14a-11 and

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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- supporting the nominating shareholder's or group's nominee that is included in the company's proxy materials or supporting or opposing a company's nominee(s), as long as the nominating shareholder or group does not seek the power to act as proxy of another shareholder.

At the meeting, the SEC and its staff also highlighted significant changes from the proxy access rules proposed by the SEC in June 2009,<sup>4</sup> including the following:

- The sliding scale stock ownership threshold, which ranged from one percent to five percent ownership of voting stock depending on the size of the company, was replaced with a fixed threshold set at three percent.
- The required holding period was extended from one year to three years.
- A window period was established for a nominating shareholder or group to notify a company of its intent to nominate a director under the proxy access rules. The Proposing Release would have permitted nominations at any time prior to 120 days before the anniversary of the mail date.
- The first-in-time standard was replaced with a highest-qualifying-voting-power standard for determining which nominating shareholder's or group's nominees are to be included in the company's proxy materials if there are too many shareholder nominees.
- A nominating shareholder or group must disclose whether its nominee satisfies the company's director qualification standards.

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<sup>4</sup> See SEC Release No. 33-9046; 34-60089 (Facilitating Shareholder Director Nominations) (June 10, 2009) (the "Proposing Release"), available [here](#). Our Client Alert of June 23, 2009 entitled "SEC Proposes Rules Facilitating Shareholder Director Nominations" is available [here](#). Our comment letter on the Proposing Release is available [here](#).