

The New and Improved 14a-8? By Cory White¹

Proxy access has been the darling of the activist shareholder movement for a number of years. Allowing shareholders to include their director nominees with a company's own proxy materials would greatly reduce the costs associated with effectively running those nominees. Still, companies that are bound by SEC's proxy rules have been allowed to exclude shareholder nominees from their proxy materials.² Using the power granted under Dodd-Frank, the SEC has recently amended Rule 14a-8 to make shareholder access to the proxy ballot closer to becoming a reality. Below is a discussion of the amended rule and the merits of those amendments.

What Types of Companies Are Affected

Any company registered under Section 12 of the 34 Act, including investment companies, have to abide by the proxy solicitation rules enumerated under the Act. Consequentially, these companies are required to include certain shareholder proposals with company proxy materials and are permitted to exclude others.

The Old Rule

If certain qualifications are met by the shareholder, companies that are bound by the proxy rules must include shareholder proposals with the companies own proxy materials.³ These rules must be followed regardless of the private ordering of the company, as expressed in its governing documents. Prior to the amendment of Rule 14a-8, companies could specifically exclude shareholder proposals that dealt with the nominations of directors or related election procedures.⁴ If the proposal nominated an individual for election to the board or called for an amendment of the governance documents as they related to such elections, it could have been excluded by the company. The amended Rule changes that.

The New Rule

As amended, Rule 14a-8 removes a company's exclusionary power as it pertains to shareholder proposals that would affect director nominations or elections through the proposal calling for a change in the company's governance documents.⁵ Shareholders who meet the eligibility requirements under the amended Rule will be able to submit, for inclusion with a company's proxy materials, proposals to amend a company's governing documents to allow for shareholder nominees to be included on a company's proxy ballot and/or that would seek a change to the related election procedures.⁶ In order to accrue this right a shareholder must have continuously

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² See generally 17 CFR § 240.14a-8(i).

³ 17 CFR § 240.14a-8.

⁴ 17 CFR § 240.14a-8(i)(8) (company may exclude proposal if, "the proposal relates to an election for membership on the company's board of directors or analogous governing body or a procedure for such nomination or election").

⁵ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

⁶ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

held at least \$2,000 in market value or 1% of the company's securities entitled to vote on the proposal for at least one year, by the date that the proposal is submitted to the company.⁷ The shareholder must continue to hold those securities through the date of the meeting on which the proposal is voted on.⁸ Along with other exclusionary power still contained in 14a-8, A company can still exclude any shareholder proposal 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;
- 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.⁹

When making the proposal the shareholder in question would be subject to the same disclosure requirements that have been previously required under Rule 14a-8.¹⁰ If the shareholder proposal dealing with proxy access is successfully adopted, further disclosures as to the actual nominees in subsequent elections will be governed by Rule 14a-19.¹¹

When will the Rule Become Effective, What About 14a-11?

The amended 14a-8 became effective on September 20, 2011. Up until that point, the effective date had been stayed due to pending litigation in *Business Roundtable et al. v. Securities and Exchange Commission*, in which the legality of proposed rule 14a-11 was at issue.¹² As proposed, Rule 14a-11 would have given shareholders that meet certain eligibility requirements, other than those enumerated in 14a-8, direct and immediate access to the proxy ballot. The D.C. Circuit Court vacated 14a-11 and the SEC did seek to challenge the ruling. Accordingly, with the resolution of the case on September 14, 2011, amended Rule 14a-8 is now effective.

For Better or For Worse?

In the adopting release the SEC took the position that amending the Rule was important to shareholder suffrage, in particular to the traditional state law right that allows shareholders to nominate and elect directors.¹³ When considering the disclosure requirements still in place and the limited nature of the amended Rule, as described above, the amendments seem to serve shareholder suffrage without presenting a detriment to effective corporate governance.

⁷ 17 CFR § 240.14a-8.

⁸ 17 CFR § 240.14a-8.

⁹ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

¹⁰ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

¹¹ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

¹² No. 10-1305 (D.C. Cir. Filed Sept. 29, 2010).

¹³ See Securities and Exchange Release Nos. 33-9136; 34-62746; IC-29384; File No. S7-10-09.

Importantly, the nomination and election procedures in question will still be ultimately determined by private ordering and not the requirements of the SEC. The amended Rule provides consistency in terms of adhering to known shareholder eligibility and disclosure requirements while providing space for greater shareholder power in exercising the traditional right to nominate and elect directors. The codification of prior staff interpretations limiting the amended Rule also serves to keep current limiting standards intact.

All-in-all the amendments to the Rule are a step in the right direction of increasing the shareholders' corporate democratic power. It grants more power to the shareholders while protecting effective disclosure and governance. Whether or not this will lead to greater shareholder activism is something that will have to be assessed at a different time.