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Small Business Securities Bulletin

A periodic bulletin keeping small businesses informed about current developments in securities law and related matters

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November 2009 – Proposed Revisions to Notice & Access; Stockholder Proposal Exclusion Analysis Revised; More on Sox 404(b)

Proposed Revisions to the Notice and Access Model for Proxy Materials

On October 14, the U.S. Securities and Exchange Commission (SEC) released proposed revisions to the notice and access model for the delivery of proxy materials to stockholders. Under notice and access, most SEC reporting companies are required to post their annual meeting proxy materials, including their proxy card, on an internet web site (other than the SEC's EDGAR web site) and provide stockholders with a Notice of Internet Availability of Proxy Materials. Under the proposals companies would continue to be required to provide disclosure that the Notice is only an overview of the complete proxy materials and describe how an investor can receive a paper or e-mailed copy of the proxy materials, but they would have the flexibility to use their own language to address these issues rather than being required to use the boilerplate language currently mandated. The SEC is also proposing to allow companies and other soliciting persons to include with the Notice an explanation of the notice and access model to help mitigate shareholder confusion in this area, which language the SEC assumes will become standardized, and "strongly encourages" companies and others who use notice and access to "better inform shareholders about the … model." Currently companies may not send any materials with the Notice other than a reply card for requesting a copy of the proxy materials and any state-required notice (registered investment companies may also include a prospectus or report to shareholders, and the SEC is proposing to amend this to a summary prospectus consistent with current requirements for mutual funds). The SEC also clarified that the current requirement to "provide a clear and impartial identification of each separate matter to be voted on" in the Notice does not require that the Notice contain the same content and formatting in this regard as the proxy card; rather, the requirement is simply that the Notice identify each matter that will be considered at the meeting generally (for example, election of directors, ratification of auditors, or approval of an equity compensation plan).

Under the existing rules companies that want to use notice and access must send the Notice 40 days before the meeting to which the underlying proxy materials relate, and other soliciting

persons must send their Notice by the later of the same 40-day period or within 10 days of the company sending its Notice or proxy materials to shareholders. While aware that some issuers do not use notice and access due to the difficulty of complying with the 40-day requirement, the SEC is not proposing to shorten the 40-day period at this time. It has, however, asked for comment as to whether a 30-day period would be workable. In order to account for delays caused by the SEC review process that has limited the ability of other reporting persons to use the notice and access model, the SEC also is proposing to revise the 10-day period for other soliciting persons to require only that such persons file their preliminary proxy statements with the SEC within 10 days of the company filing its definitive proxy statement with the SEC.

The SEC in the proposing release also asks generally for comment regarding why participation rates under the notice and access model, particularly for individual investors, are lower and how to improve the model to increase shareholder participation in the voting process.

Importantly, the SEC did not propose or ask about changing the current rule prohibiting companies from including a proxy card with the first copy of the notice. Currently, a proxy card may be sent only with a second copy of the notice, 10 days after sending the first.

New SEC FrameWork for Evaluating Certain Stockholder Proposals

On October 27, the SEC's Division of Corporation Finance released Staff Legal Bulletin (SBL) No. 14E.[1] The SLB revises the Division's framework for analyzing whether companies may exclude certain stockholder proposals from their proxy materials on the basis that the proposal "relat[es] to the company's ordinary business operations" pursuant to Rule 14a-8(i)(7) under the Securities Exchange Act of 1934. Currently, proposals that would require the company to conduct an evaluation of risk, such as environmental, financial or health risks, are excludable under Rule 14a-8(i)(7), while proposals asking a company to address operations that adversely affect the environment or the public's health are not. Going forward, rather than focusing on whether the proposal relates to an evaluation of risk, the Division will focus on the proposal's underlying subject matter; the fact that a proposal may require an evaluation of risk will not be determinative. According to the SLB, if a proposal's "underlying subject matter transcends the day-to-day business matters of the company and raises policy issues so significant that it would be appropriate for a shareholder vote, the proposal generally will not be excludable … as long as a sufficient nexus exists between the nature of the proposal and the company." Proposals regarding the board of director's role in risk oversight may be one such type of proposal.

In addition, pursuant to the SLB companies may no longer rely on the ordinary business exemption to exclude proposals relating to CEO succession. The SLB also instructs companies and proponents on how to notify the Division that they intend to submit correspondence in connection with a no-action request relating to stockholder proposals prior to doing so.

[1] The SLB is available at http://www.sec.gov/interps/legal/cfslb14e.htm.

More on Sox 404(b) With Respect to Smaller Public Companies

In our October Bulletin we discussed a bill introduced by Rep. Scott Garrett that would permanently exempt non-accelerated filers, including smaller reporting companies, from the required auditor attestation of internal control over financial reporting. On November 4, the House Financial Services committee passed this amendment as part of the Investor Protection Act, H.R. 3817, over a competing amendment introduced by Rep. Carolyn Maloney that would have only delayed the application of the requirement to non-accelerated filers, until at least June 2011, while another study on its costs was conducted. We will continue to monitor developments in this area and to keep you updated in this regard.

About Me. I am a former SEC attorney who also has prior "big firm" experience. I assist public as well as private companies with compliance with federal and state securities laws, including assisting public companies with their reporting obligations under the Securities Exchange Act of 1934, and general corporate matters, at competitive billing rates. Please contact me if you would like more information about my practice or to discuss how I can be of assistance to you.

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