

Client Alert.

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SEC Revises the E-Proxy Rules

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As the proxy season gets into full swing, the Securities and Exchange Commission ("SEC") recently amended the rules governing electronic access to proxy materials.¹ The SEC's rulemaking is intended to improve the notice and access model for furnishing proxy materials to shareholders.

One of the biggest concerns with the voluntary notice and access model for furnishing proxy materials has been a significant drop-off in retail shareholder participation in the voting process at many companies where notice and access has been implemented. Concerned about potential shareholder confusion with the required notice and the reduced response rates of shareholders in proxy solicitations, the SEC amended the rules to:

- Provide additional flexibility regarding the format of the Notice of Internet Availability of Proxy Materials (the "Notice");
- Permit issuers and other soliciting persons to better communicate with shareholders by including explanatory materials regarding the reasons for the use of the notice and access model, the process of receiving and reviewing proxy materials, and voting (but not materials designed to persuade shareholders to vote in a particular manner, or change the method of delivery of proxy materials);
- Revise the timeframe for delivering a Notice to shareholders when a soliciting person other than the issuer relies on the notice and access proxy rules; and
- Permit mutual funds to accompany the Notice with a summary prospectus.

REVISIONS TO THE NOTICE REQUIREMENTS AND INCLUSION OF EXPLANATORY MATERIALS

The SEC adopted the notice and access model in 2007. Currently, issuers and other soliciting persons must post their proxy materials on the Internet and may deliver those materials to shareholders in either (i) a "notice-only" method, with no accompanying documents (except notice of a security holder meeting required under state law), or (ii) a "full set delivery" method in paper form, with notice regarding the availability of proxy materials on the Internet.

The amendments to Exchange Act Rule 14a-16 provide companies and other soliciting persons choosing the notice and access model with additional flexibility in designing and preparing the Notice, and in providing explanatory materials to shareholders as to how to access the proxy materials online, request a paper copy of the proxy materials, and vote. The SEC believes that added flexibility should discourage the development of boilerplate disclosure.

The final rule provides that information appearing on the Notice is required to address certain topics, without specifying the exact language to be used:

- Exchange Act Rule 14a-16(d) limits the required legend to the line "Important Notice Regarding the Availability of Proxy Materials for the Shareholder Meeting To Be Held on [insert meeting date]" and calls for the other information currently required in the legend to be included in the Notice, but not as part of a specified legend;

¹SEC Release Nos. 33-9108; 34-61560 (Feb. 22, 2010) available at: <http://www.sec.gov/rules/final/2010/33-9108.pdf>. The amendments were proposed in SEC Release No. 34-60825 (Oct. 14, 2009) (the "Proposing Release"), available at <http://www.sec.gov/rules/proposed/2009/33-9073fr.pdf>.

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- An issuer or other soliciting person must indicate that the Notice is not a form for voting, but is not required to include a prescribed legend that the Notice is not a proxy card, or use a uniform design, or directly mirror the proxy card, or identify proxy items by topic rather than specific identification in the Notice; and
- The final rule permits issuers and other soliciting persons to accompany the Notice with an explanation of the reasons for the use of the notice and access model and an explanation of the process of receiving and reviewing the proxy materials and voting.

AMENDMENT TO NOTICE DEADLINES FOR SOLICITING PERSONS OTHER THAN THE ISSUER

The SEC also amended Exchange Act Rule 14a-16(1)(2)(ii) to require that soliciting persons, other than the issuer, file a preliminary proxy statement within 10 calendar days after the issuer files its definitive proxy statement and to send its Notice to shareholders no later than the date on which it files its definitive proxy statement with the SEC. Prior to the amendments, if a non-issuer soliciting person wanted to use the notice-only method, it had to send its notice to shareholders by a date that is the later of (a) 40 calendar days before the shareholder meeting to which the proxy materials relate, or (b) 10 calendar days after the issuer first sends its notice or proxy statement to shareholders.

The final rule does not provide for a specific period of time before the meeting by which a soliciting person is required to mail the Notice. It is in the soliciting person's best interest, however, to make the Notice and proxy materials available to shareholders with sufficient time to review the materials and make an informed vote.

This final rule addresses the concern that the current 10-day requirement may hinder the ability of non-issuer soliciting parties to use the notice-only method because of the interaction of the requirements of Rule 14(a)-16(b)(4) and Rule 14a-4(f). Rule 14(a)-16(b)(4) requires the provision of a means of executing a proxy at the time the Notice is first sent to the shareholders. Rule 14a-4(f) prohibits a person from providing a form of proxy unless accompanied or preceded by a definitive proxy statement.

Under these current rules a non-issuer soliciting person may be prevented from using the notice-only method for a proxy contest, if comments from the staff of the Division of Corporation Finance on proxy materials remain outstanding at the expiration of the 10-day period, revisions remain unfinished on the proxy statement and the definitive proxy statement is unfiled. Under the final rule, by contrast, the SEC believes that the amended time period will provide sufficient time to prepare a proxy statement and respond to staff comments, while using the notice and access model. The SEC expects this final rule to enhance participation by these non-issuer soliciting persons who may currently be effectively precluded from using the notice-only method.

LOOKING FORWARD

Companies should continue to cautiously evaluate the use of the notice and access model for delivery of proxy materials. The recent change to New York Stock Exchange Rule 452 prohibiting brokers from using discretionary authority to vote uninstructed shares in director elections will likely significantly reduce the participation by retail shareholders in the voting process this year, which could have a direct impact on director elections at companies with a significant retail shareholder base. The combination of Rule 452 and notice and access could thus impact the outcome of director elections in some cases, particularly in situations where companies have a majority voting standard for the election of directors and may face a "just vote no" campaign or otherwise significant shareholder opposition to director candidates because of compensation or other concerns of institutional shareholders and proxy advisory services. Companies have found some success in "stratifying" their use of notice and access, providing only a notice to certain shareholders while using full set

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delivery with other shareholders who may not vote if they only received a notice.

The SEC's recent amendments to the notice and access rules represent a positive step toward improving the notice and access model, but may only result in modest improvements in terms of boosting retail participation. These amendments do not represent drastic changes, such as, for example, revising the notice and access model to permit issuers to send a proxy card and business reply envelope, either with or without a short summary proxy statement accompanying the first Notice in order to increase response rates. Nevertheless, these amendments incorporate public comments regarding factors that cause reduced shareholder response rates by retail shareholders to proxy solicitations under the notice and access model and are an enhancement of the existing model. Further changes may be forthcoming for the next proxy season. At the direction of the Chairman of the SEC, the staff is conducting a comprehensive review of the mechanics by which proxies are voted and the way in which information is conveyed to shareholders.² The SEC is currently preparing a concept release to seek public comment on these issues.

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² See Speech by Chairman Mary Shapiro to the Practicing Law Institute's 41st Annual Institute on Securities Regulation (Nov. 4, 2009) available at <http://sec.gov/news/speech/2009/spch110409mls.htm>.