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SEC’s Division of Corporation Finance Revamps Administration of No-Action Requests Under Rule 14a-8 Regarding Shareholder Proposals

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Changes May Create New Challenges for Public Companies, and Signal a Reduction of the SEC Staff’s Traditional Role As Arbiter Between Companies and Shareholders

On September 6, 2019, the SEC's Division of Corporation Finance announced changes to how it will process no-action requests submitted pursuant to Exchange Act Rule 14a-8 starting with the upcoming proxy season. A copy of the announcement is available here.

Rule 14a-8 permits shareholders to submit proposals for inclusion in a public company’s proxy statement if the shareholder and the proposal comply with the rule's requirements. If a company believes that it has grounds to exclude a proposal because one or more of the substantive or procedural requirements of the rule have not been met, it is required to notify the SEC and the shareholder of its intention to exclude the proposal and its reasons for doing so. The staff of the Division of Corporation Finance has traditionally responded to these notices and expressed its informal views with published no-action letters indicating whether the staff agrees or disagrees with the company’s reasons for excluding the shareholder’s proposal.

Pursuant to the Division’s recent announcement, the staff will make two changes to this process in the upcoming season.

First, the staff will not publish written no-action letters with respect to every notice pursuant to Rule 14a-8 but in some cases will respond orally instead of in writing. According to the announcement, the staff will issue written response letters only when a letter would "provide value," such as providing more broadly applicable guidance about complying with Rule 14a-8.

Second, the staff may decline to state a view with respect to particular requests.

As the announcement was issued solely by the Division of Corporation Finance, it is not immediately clear whether the Division of Investment Management will follow a similar approach to notices for exclusion pursuant to Rule 14a-8 that it processes, such as those filed by registered investment companies and business development companies.

As an initial matter, the staff's announcement should not change how companies analyze and respond to incoming shareholder proposals in the upcoming season. Rule 14a-8(j) will still require companies to notify the SEC and the shareholder of their intention and reasons for excluding a shareholder proposal, and the staff's new processes should not have a substantive impact on how these communications are prepared.

The announcement does not state whether the staff intends to make its oral responses public, and if so, how those responses would be publicized. Accordingly, if a company receives an oral response to its no-action request and excludes a shareholder's proposal, it may need to respond to inquiries from other shareholders or stakeholders regarding its basis for the exclusion of the shareholder's proposal, without having a public statement of the staff to support such exclusion. Further, while the announcement and recent public remarks by Division Director William Hinman indicate that the staff intends to continue to publish written responses when those responses will provide precedential value, there may still be situations where companies seeking no-action relief are not aware of non-public staff guidance provided to other similarly-situated companies.

The Division's announcement also does not specify what types of proposals or issues will lead its staff to decline to state a view. Historically, the staff generally has declined to provide a view only if the company's ability to exclude the proposal was the subject of ongoing litigation or in other limited situations. While the Division's focus appears to be on reducing the number of written responses where the answer is clear-cut based on publicly-available precedent, it is possible that over time the staff may also avoid expressing a view on more controversial proposals under the new procedures. For example, application of Rule 14a-8(i)(7), which permits companies to exclude proposals on "ordinary business" matters, has been controversial in some cases, particularly as it has been applied to proposals that may implicate "significant social policy" issues. The staff may also choose to avoid answering difficult interpretive questions during the shareholder proposal season, consistent with its approach to addressing the exclusion of certain proxy access proposals pursuant to Rule 14a-8(i)(9) in the 2014 - 2015 proxy season. As discussed here, in the proxy access situation, after issuing an initial no-action response letter on this issue the staff published a statement that it would not express further views on the question during that proxy season.

If the staff does not express a view on a company's ability to exclude a proposal, the company remains free to exclude the proposal from its proxy materials. While in all cases the company may decide to exclude the proposal regardless of the nature and format of the staff's response – since the staff's response is non-binding -- the absence of an expressed staff view supporting the company's decision may increase the likelihood that the shareholder proponent will challenge the exclusion of the proposal in court. If the staff provides an oral response favorable to the company's position, it is unclear whether a court would grant such a response the deference that courts have accorded written no-action letters.

The announcement provides that companies and other interested parties should not interpret the staff declining to state a view on a particular request as indicating that the proposal must be included in the company's proxy statement. However, if the staff does decline to state a view on a company's request – or even if the staff orally provides a view -- the company may have a difficult decision to make. Before excluding the proposal without the support of a published no-action letter from the staff, companies and their advisers should carefully evaluate the nature of the proposal, the bases for excluding the proposal, the shareholder proponent and other factors, including the prospect of litigation.

We are continuing to monitor for additional guidance from the staff on these issues. If you have any questions, please contact your usual Proskauer attorney.

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