

ClientAlert

Capital Markets

March 2010

SEC Adopts Amendments to E-Proxy Rules

On February 22, 2010, the Securities and Exchange Commission (the “SEC”) adopted amendments to its “notice and access” rules (generally known as e-proxy), which will become effective on March 29, 2010.¹ All companies with a 2009 calendar year-end can voluntarily adopt the new rules early with respect to shareholder meetings in Spring 2010, as permitted by an unofficial Staff position. The amendments are intended to help boost shareholder response rates to proxy solicitations by reducing confusion caused by the current requirements for e-proxy materials. Specifically, the new rules replace the boilerplate “legend” previously required on the notice with more general guidelines regarding the information companies must include in the notice. Companies are also permitted to include with the notice an explanation of the e-proxy voting method and why the company is using it. The new rules also relax the notice mailing deadlines for soliciting persons other than the company.

Revisions to the Notice

The new rules provide companies with more flexibility regarding the wording they include in the notice to shareholders. Currently, Rule 14a-16(d) under the Securities Exchange Act of 1934 sets forth the exact wording of the legend that must be included in the notice. The new rules:

- shorten the required legend to the following: “Important Notice Regarding the Availability of Proxy Materials for the Shareholder Meeting to Be Held on [date].”
- permit companies to develop their own wording to:
 - explain to shareholders that the notice is only an overview and additional information is available on the Internet or by mail,
 - encourage shareholders to review the proxy statement before voting,
 - inform shareholders how to request paper or email copies of proxy materials at no charge and
 - inform shareholders that the notice is not a form of proxy. The SEC added this last requirement at the request of commenters.

In sum, while the content of the notice will not change significantly, companies will be granted more flexibility to select the words to convey that content.



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1. “Amendments to Rules Requiring Internet Availability of Proxy Materials,” Securities Act Release No. 9,108, Exchange Act Release No. 61,560, Investment Company Act Release No. 29,131 (released February 22, 2010), available at <http://www.sec.gov/rules/final/2010/33-9108.pdf>. The proposing release (Securities Act Release No. 9,073, Exchange Act Release No. 60,825, Investment Company Act Release No. 28,946) which was published on October 14, 2009, is available at <http://www.sec.gov/rules/proposed/2009/33-9073.pdf>.

Inclusion of Explanatory Materials

The new rules permit companies to include with the notice an explanation of the e-proxy voting method and why the company is using that method. The explanation of the method must be limited to the process of receiving and reviewing the proxy materials and voting. Allowing an explanation for the use of the e-proxy voting method was adopted at the request of commenters to enhance understanding of e-proxy among shareholders by informing them of the benefits and helping to distinguish the notice from a proxy card. Currently, companies may not include any materials other than a pre-addressed, pre-paid reply card to request proxy materials and a copy of any notice of a shareholder meeting required by state law. Under the new rules, companies will still be prohibited from including materials designed to persuade shareholders to vote in a particular manner.

Relaxed Deadline for Soliciting Persons other than the Company

Finally, the new rules change the timetable that applies to soliciting persons other than the company. Currently, soliciting persons must send their notice to shareholders by the later of 40 days prior to the meeting or ten days after the company first sent its notice or proxy materials to shareholders. However, because the SEC generally reviews preliminary proxy materials filed by soliciting persons, soliciting persons often found it impossible to send a notice within ten days after the company first sent its notice or proxy statement. Soliciting persons could not send a notice until they filed a definitive proxy statement because they cannot make available a means to execute a proxy—a requirement of the e-proxy rules—until they filed a definitive proxy statement. The new rules address this issue by only requiring a soliciting person relying on this alternative to file a preliminary proxy statement within ten days after the company files its definitive proxy statement but allowing the soliciting person to send its notice to shareholders as late as the date on which the soliciting person files its definitive proxy statement with the SEC. The new rules do not mandate a specific period of time after receipt of the materials and before the meeting since it is in the best interests of the soliciting person to make the notice and proxy materials available to the shareholders with sufficient time to review such materials and make an informed decision.

Additional Guidance and Investor Education

The SEC has also clarified that the requirement under Rule 14a-16(d)(3) to include “a clear and impartial identification of each separate matter intended to be acted on and the soliciting person’s recommendations” does not require companies to mirror, word for word, the actual proxy card. It is sufficient to identify each matter that will be acted upon at the shareholder meeting, such as election of directors, approval of a stock option plan, etc. In addition to this guidance targeted at issuers, the SEC’s Office of Investor Education and Advocacy, in consultation with the SEC’s Division of Corporation Finance, has been directed to develop a program designed to educate and inform shareholders, especially non-institutional shareholders, about the notice and access model.

Commentary

One of the more undesirable impacts of e-proxy has been diminished voting by retail shareholders. According to statistics compiled by Broadridge, when comparing shareholders of companies that used both the notice-only and full-set delivery options in 2009, the response rates of retail shareholders that received notice-only was approximately one-half that of retail shareholders that received full-set delivery.² The SEC’s new rules are intended to allow companies to provide clearer explanations to shareholders as to why they have received a notice and how they can access the proxy materials and vote their shares. The staff hopes that these clearer explanations will help companies maintain the retail shareholder vote they enjoyed prior to adopting e-proxy. It is worth noting that the SEC had already acknowledged that the form of notice provided to shareholders was less than clear and in March 2009 had informally approved a revised form of notice prepared by Broadridge that did not meet the technical requirements of Rule 14a-16, but was significantly clearer. The current release leaves open the question of whether the new rules may be adopted early on a voluntary basis, but the SEC Staff has taken the position that companies can voluntarily adopt the new rules prior to their becoming effective.

The new rules should generally be helpful to companies using the notice-only method. The question is whether the new rules go far enough. On January 1, 2010, recent revisions to NYSE Rule 452 went into effect with the result that brokers are no longer able to vote uninstructed shares in director elections. With companies concerned that this may further (in some cases significantly)

2. Broadridge Notice & Access, Statistical Overview of Use with Beneficial Shareholders (as of June 30, 2009) at <http://www.broadridge.com/notice-and-access/NAStatsStory.pdf>. These results are largely in line with the results of Broadridge’s notice-only option survey of the 2008 annual proxy season that are available at the same address.

decrease retail shareholder voting, more fundamental changes may be necessary to encourage the use of e-proxy. The SEC received comments expressing support for an amendment shortening the notice mailing deadline from 40 days to 30 days before a shareholder meeting. Many companies have found the 40-day requirement difficult to meet because the proxy statement must be accompanied or preceded by an annual report. However, the SEC did not adopt any change to this time period. The SEC also received comments addressing the processing fee structure, the lack of competition for proxy service providers and issuers' inability to negotiate the fees which results in limitations on the amount of the cost savings from switching to the notice and access model. The SEC declined to address these issues at this time but noted that it will continue to consider these proposals and other ways to encourage informed shareholder participation.

One continuing disappointment is that the SEC has not yet allowed issuers to include a proxy card and business reply envelope with the notice. While a means of voting must be available by telephone or the Internet when the notice is mailed, providing a proxy card with the notice would clearly provide one of the easiest means to vote. It is likely that only a small minority of retail shareholders read the proxy statement in detail and those wishing to do so could access it on the Internet before voting.

Background to e-Proxy

In 2007, the SEC amended its proxy rules by, among other things, adopting the notice and access model. The notice and access model was intended to promote the use of the Internet as a reliable and cost-efficient means of making proxy materials available to shareholders. Under the notice and access model, a company or other soliciting person must provide proxy materials to shareholders using one of two methods: the "notice-only option" and the "full-set delivery option." A company or other soliciting person is permitted to provide proxy materials to some shareholders via the notice-only option and to other shareholders via the full-set delivery option. Under both options, the company or other soliciting person must make its proxy materials available on an Internet website. The two options are as follows:

- **Notice-only.** The notice-only option permits a company or other soliciting person to send only a notice to shareholders about the availability of proxy materials. The notice must include, among other things, the Internet website address where shareholders can access the proxy materials and a description of the means by which a shareholder can request paper or electronic copies of the materials. Under this option, a company must send the notice to shareholders at least 40 days prior to the shareholder

meeting to which the proxy materials relate. On or before the date that the notice is first sent, the company must also provide shareholders with a means to vote (which can be electronic, by telephone or by offering the ability to print and mail a proxy card). The company may not mail an actual proxy card to shareholders until ten or more calendar days after the date that it sends the notice to shareholders unless the proxy card is accompanied by full proxy materials. A company or other soliciting person must then provide copies of the proxy materials upon the request of shareholders receiving the Notice.

- **Full-set delivery.** The full-set delivery option permits a company or other soliciting person to send the traditional full set of proxy materials in paper form to shareholders accompanied by the notice or to include the information required in the notice in the proxy materials. Unlike the notice-only option, however, it is not necessary for the company to provide a means to vote on the Internet website (because individuals will have received an actual proxy card) and the 40-day advance notice requirement does not apply. This option does not substantially modify practices that existed before the e-proxy rules other than the requirement that the company or other soliciting person must still make its proxy materials available on an Internet website.

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