

CLIENT UPDATE

SEC MODIFIES APPROACH TO ADVICE ON RISK

The Securities Group provides strategic advice to our clients on all aspects of federal and state securities law and regulation.

Our clients include public and private corporations, partnerships, limited liability companies and other business entities, financial institutions, mutual funds, investment advisers and broker-dealers, as well as executives and entrepreneurs.

In October 2009, the Securities and Exchange Commission, Division of Corporation Finance (the “Staff”) issued Staff Legal Bulletin No. 14E (the “Bulletin”) regarding Rule 14a-8(i)(7) of the Securities Exchange Act of 1934. The Bulletin effectively reverses the Staff’s prior guidance, which allowed companies to exclude most shareholder proposals pertaining to internal assessments of risks, such as health, financial or environmental, on the basis that the proposals and supporting statements related only to the *evaluation* of such risks by the company, which the Staff previously viewed as relating to a company’s ordinary business operations.

Rule 14a-8 allows an eligible shareholder to submit certain proposals for inclusion in the company’s proxy statement. However, Rule 14a-8(i)(7) permits a company to exclude any shareholder proposal that relates to a company’s “ordinary business operations.” Previously, to the extent that a proposal and supporting statement focused on a company engaging in an internal assessment of the risks and liabilities that the company faces as a result of its operations, the Staff has permitted companies to exclude these proposals under Rule 14a-8(i)(7) as relating to an *evaluation* of risk. To the extent that a proposal and supporting statement focused on a company minimizing or eliminating operations that may adversely affect the environment or the public’s health, the Staff has not permitted companies to exclude these proposals under Rule 14a-8(i)(7).

In the Bulletin, the Staff stated it will no longer focus on whether a proposal and supporting statement relate to the company engaging in an evaluation of risk in determining whether a proposal can be excluded under Rule 14a-8(i)(7). Instead, the Staff will focus on the subject matter to which the risk pertains or that gives rise to the risk and will consider whether or not the underlying subject matter of the risk evaluation involves a matter of ordinary business to the company.

Stating that the previous interpretation of the rules resulted in the inadvertent exclusion of proposals dealing with significant policy matters only because such proposals happened also to include an evaluation of risk, the Staff advised that its analysis will now proceed beyond the determination that the proposal involved an evaluation of risk to consider the underlying subject matter. Now, if the underlying subject matter transcends the day-to-day business matters of the company and raises significant policy issues, the Staff will view the proposal as appropriate for a shareholder vote, as long as significant nexus exists between the nature of the proposal and the company.

The commonly anticipated effect of the Bulletin is that public companies and their boards of directors will be spending significantly more time communicating and negotiating with activist shareholders regarding matters of social policy, such as global warming and public health, and proposals on such matters will increasingly appear in proxy materials.