



Court Upholds Exclusion of 14a-8 Proposal For Deficient Proof of Stock Ownership

Posted by Trevor Norwitz, Wachtell, Lipton, Rosen & Katz, on Friday March 12, 2010

Editor's Note: [Trevor Norwitz](#) is a partner in the Corporate Department at Wachtell, Lipton, Rosen & Katz, where he focuses on mergers and acquisitions, corporate governance and securities law matters. This post is based on a Wachtell Lipton firm memorandum by Mr. Norwitz and [Gordon S. Moodie](#). The post relates to the case of *Apache Corporation v. Chevedden*, which was previously discussed on the Forum in [this post](#).

In the first federal judicial decision addressing the requisite proof of share ownership for submission of proposals under Rule 14a-8, a U.S. District Court has upheld, on narrow grounds, a company's exclusion of a shareholder proposal for failing to comply strictly with the proxy rules. *Apache Corporation v. Chevedden*, C.A. H-10-0076 (March 10, 2010).

The case involved a precatory shareholder proposal from activist John Chevedden to eliminate supermajority voting. To prove his eligibility to submit the proposal under the proxy rules (which require continuous ownership for one year of just \$2,000 in market value of a company's voting securities), Chevedden provided a letter from Ram Trust Services (RTS), his "introducing broker". Apache rejected this as deficient because RTS was not a record holder of its stock and gave Chevedden the requisite 14 days to provide proper proof of ownership. Chevedden later – more than 14 days after the deficiency notice – gave Apache a letter from Northern Trust, RTS' custodian participant in the Depository Trust Company (DTC), the registered holder of the shares in question. Apache asserted that it could exclude Chevedden's proposal because neither RTS nor Northern Trust was a record holder. Rather than seeking a "no action" letter from the SEC staff, Apache filed suit seeking a declaratory judgment that only a letter from DTC, the actual registered holder, would suffice.

The Court declined to accept Apache's position that a letter from DTC is required, but also refused to accept Chevedden's position that "would require companies to accept any letter purporting to come from an introducing broker, that names a DTC participating member with a position in the company". In this case, the Court found that Apache had "valid reasons to believe the letter is unreliable as evidence of the shareholder's eligibility," noting that because RTS was

not a DTC participant, Apache could not confirm through DTC that RTS held shares. The Court also accepted that the letter from Northern Trust, which is a DTC participant, could be disregarded as untimely, because it was sent more than 14 days after Apache's deficiency notice.

In suggesting that DTC participants may be deemed "record holders" for certification purposes under the proxy rules, *Apache* is consistent with (although it does not cite) the recent Delaware holding in *Kurz v. Holbrook* that DTC participants are "stockholders of record" for purposes of determining the right to vote under Delaware law. (See our recent [memorandum](#) on this decision, which is being appealed.) Both cases provide fascinating discussions of the historic development and arcane intricacies of our multi-layered proxy system.

The *Apache* decision serves as a welcome reminder that companies are entitled to insist, through litigation if necessary, on strict compliance with federal eligibility criteria by shareholders seeking to include proposals in company proxy statements. Although Rule 14a-8 was intended to "give true vitality to the concept of corporate democracy," the Court noted, "that does not necessitate a complete surrender of a corporation's rights during proxy season."

This case also highlights the costs and distractions imposed on companies (and the SEC) by "gadfly" activists like Chevedden who, by holding tiny stakes in multiple issuers, are able to use Rule 14a-8 to harass companies and drive their personal and political agendas. It is high time for the \$2,000 threshold, which has been in place for over a decade, to be increased.

© 2010 The President and Fellows of Harvard College