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Addressing Rule 14a-8 Shareholder Proposals During and After the Shutdown

As the 2019 proxy season approaches, to the extent the U.S. federal government shutdown continues, companies with Rule 14a-8 shareholder proposals will have some difficult decisions to make. Although a company is not required to submit a no-action letter to the SEC to exclude a Rule 14a-8 shareholder proposal (but is required to submit its reasons for the exclusion to the SEC and to the proponent), the almost universal practice is to ask the SEC Staff to concur with a company's planned exclusion of a proposal. The company's reasons for excluding a Rule 14a-8 shareholder proposal and related requests for SEC no-action letters must be submitted to the SEC, absent good cause, no later than 80 calendar days before the definitive proxy statement is filed to comply with the deadline in Rule 14a-8. Generally, companies follow the guidance of the SEC Staff in response to no-action exclusion requests.

Companies can submit no-action letters to the SEC during the shutdown to attempt to meet the Rule 14a-8 timing deadline. However, unless the shutdown ends, the SEC Staff will not respond to requests for no-action letters and, once the shutdown ends, there is likely to be a significant backlog of requests. For a company that believes it has winning arguments to exclude a shareholder proposal, submitting a no-action letter and excluding a proposal from its proxy statement, even without SEC action, could certainly be the right course of action with an appropriate explanation. However, even with good arguments for an exclusion, companies are well advised to proceed cautiously, depending upon the subject matter of the proposal, the identity of the proponent, the composition of the company's shareholder base, the strength of the company's arguments for exclusion and favorable precedents.

Without the SEC Staff's concurrence, companies will not have the comfort that the Staff will not later recommend enforcement action (or require an amendment to a definitive proxy statement and proxy card) if the Staff subsequently determines the company improperly excluded a proposal. Shareholders that already criticize companies for seeking to exclude proposals (even when the SEC Staff agrees with the company) may be even more inclined to make public statements criticizing the company's decision or may pursue litigation challenging the company's decision.

While not anticipating this government shutdown scenario, ISS has a legacy default policy of possibly issuing withhold votes against companies that exclude shareholder proposals in the absence of a voluntary or negotiated withdrawal, no-action relief from the SEC or a court order. Moreover, Glass Lewis recently announced that it

may recommend against members of a company's governance committee in certain (broader) circumstances when a company has been successful in obtaining a SEC no-action request to exclude a proposal, even though a company has a legal right to exclude non-compliant shareholder proposals and shareholders whose proposals do not comply with Rule 14a-8 have no legal right to require their inclusion in company proxy statements. In addition, both ISS and Glass Lewis scrutinize a company's use of ratification votes to exclude shareholder proposals, even where the SEC has granted no-action relief. Without action from the SEC or a company obtaining a declaratory judgment from a court (which is more costly, creates additional publicity and is rarely worth the effort), proxy advisory firms and shareholders may be even further emboldened to take action against companies who seek to exclude Rule 14a-8 shareholder proposals.

As a result, it is often beneficial (and not only due to the uncertainty created by the shutdown) to seek to discuss the Rule 14a-8 shareholder proposal with the proponent, explain the company's rationale for its preferred outcome and attempt to negotiate the withdrawal of the proposal either by negotiating a compromise or alternative outcome or implementing the proposal or by convincing the proponent that it would be detrimental for the company and/or the shareholders to include the requested proposal in the company's proxy statement. Typically, the earlier such a dialog is started, the greater the likelihood that a successful outcome can be achieved. Companies should also continue to consider approaches for pre-emptively addressing topics being raised by proposals (even if the proposal itself is not being implemented) and whether to submit a management-sponsored proposal (precatory or binding) to a vote so as to increase the likelihood of securing shareholder support for the board's recommendation.

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