

***American Federation of State, County & Municipal Employees v. American Intern. Group, Inc.*, 462 F.3d 121 (CA2, 2006)**

This case raises the question of whether a shareholder proposal requiring a company to include certain shareholder-nominated candidates for the board of directors on the corporate ballot can be excluded from the corporate proxy materials on the basis that the proposal “relates to an election” under Securities Exchange Act Rule 14a-8(i)(8) (“election exclusion” or “Rule 14a-8(i)(8)”). Complicating this question is not only the ambiguity of Rule 14a-8(i)(8) itself but also the fact that the Securities Exchange Commission (the “SEC” or “Commission”) has ascribed two different interpretations to the Rule's language. The SEC's first interpretation was published in 1976, the same year that it last revised the election exclusion. The Division of Corporation Finance (the “Division”), the group within the SEC that handles investor disclosure matters and issues no-action letters,¹ continued to apply this interpretation consistently for fifteen years until 1990, when it began applying a different interpretation, although at first in an ad hoc and inconsistent manner. The result of this gradual interpretive shift is the SEC's second interpretation, as set forth in its amicus brief to this Court. We believe that an agency's interpretation of an ambiguous regulation made at the time the regulation was implemented or revised should control unless that agency has offered sufficient reasons for its changed interpretation. Accordingly, we hold that a shareholder proposal that seeks to amend the corporate bylaws to establish a procedure by which shareholder-nominated candidates may be included on the corporate ballot does not relate to an election within the meaning of the Rule and therefore cannot be excluded from corporate proxy materials under that regulation.

Background

The American Federation of State, County & Municipal Employees (“AFSCME”) is one of the country's largest public service employee unions. Through its pension plan, AFSCME holds 26,965 shares of voting common stock of American International Group (“AIG” or “Company”), a multi-national corporation operating in the insurance and financial services sectors. On December 1, 2004, AFSCME submitted to AIG for inclusion in the Company's 2005 proxy statement a shareholder proposal that, if adopted by a majority of AIG shareholders at the Company's 2005 annual meeting,² would amend the AIG bylaws to require the Company, under certain circumstances, to publish the names of shareholder-nominated candidates for director positions together with any candidates nominated by AIG's board of directors (“Proposal”).³ AIG sought the

¹ Elaborating upon the nature of the no-action process, the Court has stated: “The no-action process works as follows: Whenever a corporation decides to exclude a shareholder proposal from its proxy materials, it “shall file” a letter with the Division explaining the legal basis for its decision. *See* Rule 14a-8(d)(3). If the Division staff agrees that the proposal is excludable, it may issue a no-action letter, stating that, based on the facts presented by the corporation, the staff will not recommend that the SEC sue the corporation for violating Rule 14a-8.... The no-action letter, however, is an informal response, and does not amount to an official statement of the SEC's views.... No-action letters are deemed interpretive because they do not impose or fix legal relationship upon any of the parties.” [...]

² Delaware corporate law, which governs AIG's internal affairs, provides that shareholders have the power to amend bylaws by majority vote. *See* DEL.CODE ANN. tit. 8, § 109(a).

³ The AFSCME Proposal states in relevant part:

input of the Division regarding whether AIG could exclude the Proposal from its proxy statement under the election exclusion on the basis that it “relates to an election.” The Division issued a no-action letter in which it indicated that it would not recommend an enforcement action against AIG should the Company exclude the Proposal from its proxy statement [...] (“AIG No-Action Letter”). Armed with the no-action letter, AIG then proceeded to exclude the Proposal from the Company's proxy statement. In response, AFSCME brought suit in the United States District Court for the Southern District of New York seeking a court order compelling AIG to include the Proposal in its next proxy statement. The district court denied AFSCME's motion for a preliminary injunction, concluding that AFSCME's Proposal “on its face ‘relates to an election.’ Indeed, it relates to nothing else.” [...]

Discussion

Rule 14a-8(i)(8), also known as “the town meeting rule,” regulates what are referred to as “shareholders proposals,” that is, “recommendation[s] or requirement[s] that the company and/or its board of directors take [some] action, which [the submitting shareholder(s)] intend to present at a meeting of the company's shareholders.” If a shareholder seeking to submit a proposal meets

RESOLVED, pursuant to Section 6.9 of the By-laws (the “Bylaws”) of American International Group Inc. (“AIG”) and section 109(a) of the Delaware General Corporation Law, stockholders hereby amend the Bylaws to add section 6.10:

“The Corporation shall include in its proxy materials for a meeting of stockholders the name, together with the Disclosure and Statement (both defined below), of any person nominated for election to the Board of Directors by a stockholder or group thereof that satisfies the requirements of this section 6.10 (the “Nominator”), and allow stockholders to vote with respect to such nominee on the Corporation's proxy card. Each Nominator may nominate one candidate for election at a meeting.

To be eligible to make a nomination, a Nominator must:

- (a) have beneficially owned 3% or more of the Corporation's outstanding common stock (the “Required Shares”) for at least one year;
- (b) provide written notice received by the Corporation's Secretary within the time period specified in section 1.11 of the Bylaws containing (i) with respect to the nominee, (A) the information required by Items 7(a), (b) and (c) of SEC Schedule 14A (such information is referred to herein as the “Disclosure”) and (B) such nominee's consent to being named in the proxy statement and to serving as a director if elected; and (ii) with respect to the Nominator, proof of ownership of the Required Shares; and
- (c) execute an undertaking that it agrees (i) to assume all liability of any violation of law or regulation arising out of the Nominator's communications with stockholders, including the Disclosure (ii) to the extent it uses soliciting material other than the Corporation's proxy materials, comply with all laws and regulations relating thereto.

The Nominator shall have the option to furnish a statement, not to exceed 500 words, in support of the nominee's candidacy (the “Statement”), at the time the Disclosure is submitted to the Corporation's Secretary. The Board of Directors shall adopt a procedure for timely resolving disputes over whether notice of a nomination was timely given and whether the Disclosure and Statement comply with this section 6.10 and SEC Rules.”

certain eligibility and procedural requirements,⁴ the corporation is required to include the proposal in its proxy statement and identify the proposal in its form of proxy, unless the corporation can prove to the SEC that a given proposal may be excluded based on one of thirteen grounds enumerated in the regulations. One of these grounds, Rule 14a-8(i)(8), provides that a corporation may exclude a shareholder proposal “[i]f the proposal relates to an election for membership on the company's board of directors or analogous governing body.”

We must determine whether, under Rule 14a-8(i)(8), a shareholder proposal “relates to an election” if it seeks to amend the corporate bylaws to establish a procedure by which certain shareholders are entitled to include in the corporate proxy materials their nominees for the board of directors (“proxy access bylaw proposal”). [...] The relevant language here - “relates to an election” - is not particularly helpful. AFSCME reads the election exclusion as creating an obvious distinction between proposals addressing a particular seat in a particular election (which AFSCME concedes are excludable) and those, like AFSCME's proposal, that simply set the background rules governing elections generally (which AFSCME claims are not excludable). AFSCME's distinction rests on Rule 14a-8(i)(8)'s use of the article “an,” which AFSCME claims “necessarily implies that the phrase ‘relates to an election’ is intended to relate to proposals that address *particular elections*, instead of simply ‘elections’ generally.” It is at least plausible that the words “an election” were intended to narrow the scope of the election exclusion, confining its application to proposals relating to “a particular election *and not* elections generally.” It is, however, also plausible that the phrase was intended to create a comparatively broader exclusion, one covering “a particular election *or* elections generally” since any proposal that relates to elections in general will necessarily relate to an election in particular. The language of Rule 14a-8(i)(8) provides no reason to adopt one interpretation over the other.

When the language of a regulation is ambiguous, we typically look for guidance in any interpretation made by the agency that promulgated the regulation in question. [...] We are aware of two statements published by the SEC that offer informal interpretations of Rule 14a-8(i)(8). The first is a statement appearing in the amicus brief that the SEC filed in this case at our request. The second interpretation is contained in a statement the SEC published in 1976, the last time the SEC revised the election exclusion. Neither of these interpretations has the force of law. But, while agency interpretations that lack the force of law do not warrant deference when they interpret ambiguous *statutes*, they do normally warrant deference when they interpret ambiguous *regulations*. [...]

⁴ “In order to be eligible to submit a proposal, [a shareholder] must have continuously held at least \$2,000 in market value, or 1%, of the company's securities entitled to be voted on the proposal at the meeting for at least one year by the date [of the proposal's submission].” 17 C.F.R. § 240.14a-8(b)(1). “Each shareholder may submit no more than one proposal to a company for a particular shareholders' meeting.” *Id.* § 240.14a-8(c). “The proposal, including any accompanying supporting statement, may not exceed 500 words.” *Id.* § 240.14a-8(d). The company's “principal executive offices” must have received the shareholder proposal “not less than 120 calendar days before the date of the company's proxy statement released to shareholders in connection with the previous year's annual meeting.” *Id.* § 240.14a-8(e)(2). “[I]f the company did not hold an annual meeting the previous year, or if the date of th[e present] year's annual meeting has been changed by more than 30 days from the date of the previous year's meeting, then the deadline is a reasonable time before the company begins to print and mail its proxy materials.”

In its amicus brief, the SEC interprets Rule 14a-8(i)(8) as permitting the exclusion of shareholder proposals that “would result in contested elections.” The SEC explains that “[f]or purposes of Rule 14a-8, a proposal would result in a contested election if it is a means either to campaign for or against a director nominee or to require a company to include shareholder-nominated candidates in the company's proxy materials.” Under this interpretation, a proxy access bylaw proposal like AFSCME's would be excludable under Rule 14a-8(i)(8) because it “is a means to require AIG to include shareholder-nominated candidates in the company's proxy materials.” However, that interpretation is plainly at odds with the interpretation the SEC made in 1976.

In that year, the SEC amended Rule 14a-8(i)(8) in an effort to clarify the purpose of the existing election exclusion. The SEC explained that “with respect to corporate elections, [] Rule 14a-8 is not the proper means for conducting campaigns or effecting reforms in elections of that nature [i.e., “corporate, political or other elections to office”], *since other proxy rules, including Rule 14a-11, are applicable thereto.*” (emphasis added) (“1976 Statement”). The district court opinion quoted the 1976 Statement but omitted the italicized language and concluded that shareholder proposals were not intended to be used to accomplish any type of election reform. Clearly, however, that cannot be what the 1976 Statement means. Indeed, when the SEC finally adopted the revision of Rule 14a-8(i)(8) four months after publication of the 1976 Statement, it explained that it was rejecting a previous proposed rule (which would have authorized the exclusion of proposals that “relate[] to a corporate, political or other election to office”) in favor of the current version (which authorizes the exclusion of proposals that simply “relate[] to an election”) so as to avoid creating “the erroneous belief that the Commission intended to expand the scope of the existing exclusion to cover proposals dealing with matters previously held not excludable by the Commission, such as cumulative voting rights, general qualifications for directors, and political contributions by the issuer.” (“1976 Adoption”). And yet, all three of these shareholder proposal topics – cumulative voting rights, general qualifications for directors, and political contributions – fit comfortably within the category “election reform.”

In its amicus brief, the SEC places a slightly different gloss on the 1976 Statement than did the district court. The SEC reads the 1976 Statement as implying that the purpose of Rule 14a-8(i)(8) is to authorize the exclusion of proposals that seek to effect, not election reform in general, but only certain types of election reform, namely those to which “other proxy rules, including Rule 14a-11,” are generally applicable. In 1976, Rule 14a-11 was essentially the equivalent of current Rule 14a-12, which requires certain disclosures where a solicitation is made “for the purpose of opposing” a solicitation by any other person “with respect to the election or removal of directors.” The SEC reasons that, based on the 1976 Statement, “a proposal may be excluded pursuant to Rule 14a-8(i)(8) if it would result in an immediate election contest (e.g., by making a director nomination for a particular meeting) or would set up a process for shareholders to conduct an election contest in the future by requiring the company to include shareholder director nominees in the company's proxy materials for subsequent meetings.”

We agree with the SEC that, based on the 1976 Statement, shareholder proposals can be excluded under the election exclusion if they would result in an immediate election contest. We understand the phrase “since other proxy rules, including Rule 14a-11, are applicable thereto” in the 1976 Statement to mean that under Rule 14a-8(i)(8), companies can exclude shareholder proposals dealing with those election-related matters that, if addressed in a proxy solicitation – the alternative to a shareholder proposal – would trigger Rule 14a-12, or the former Rule 14a-11. A proxy solicitation nominating a candidate for a specific election would be made “for the purpose of opposing” the company's proxy solicitation and therefore would clearly trigger Rule 14a-12. Accordingly, based on the 1976 Statement, a shareholder proposal seeking to contest management's nominees would be excludable under Rule 14a-8(i)(8).

By contrast, a proxy solicitation seeking to add a proxy access amendment to the corporate bylaws does not involve opposing solicitations dealing with “the election or removal of directors,” and therefore Rule 14a-12, or, equivalently, the former Rule 14a-11, would not apply to a proposal seeking to accomplish the same end. Thus, we cannot agree with the second half of the SEC's interpretation of the 1976 Statement: that a proposal may be excluded under Rule 14a-8(i)(8) if it would simply establish a process for shareholders to wage a future election contest.

The 1976 Statement clearly reflects the view that the election exclusion is limited to shareholder proposals used to oppose solicitations dealing with an identified board seat in an upcoming election and rejects the somewhat broader interpretation that the election exclusion applies to shareholder proposals that would institute procedures making such election contests more likely. The SEC suggested as much when, four months after its 1976 Statement, it explained that the scope of the election exclusion does not cover shareholder proposals dealing with matters such as cumulative voting and general director requirements, both of which have the potential to increase the likelihood of election contests.

That the 1976 statement adopted this narrower view of the election exclusion finds further support in the fact that it was also the view that the Division adopted for roughly sixteen years following publication of the SEC's 1976 Statement. It was not until 1990 that the Division first signaled a change of course by deeming excludable proposals that *might* result in contested elections, even if the proposal only purports to alter general procedures for nominating and electing directors.

Because the interpretation of Rule 14a-8(i)(8) that the SEC advances in its amicus brief—that the election exclusion applies to proxy access bylaw proposals—conflicts with the 1976 Statement, it does not merit the usual deference we would reserve for an agency's interpretation of its own regulations. [...]

Accordingly, we deem it appropriate to defer to the 1976 Statement, which represents the SEC's interpretation of the election exclusion the last time the Rule was substantively revised. [...] ⁸ We

⁸ AIG suggests that the interpretation of the election exclusion that we adopt here—that it does not apply to proxy access proposals—“improperly conflicts” with a proposed SEC rule that would require corporations in particular circumstances to include certain shareholder-nominated director candidates in the corporate proxy statement (“Proposed Rule 14a-11”). Proposed Rule 14a-11 would entitle a holder of at least 5% of the corporation's voting stock to

therefore interpret the election exclusion as applying to shareholder proposals that relate to a particular election and not to proposals that, like AFSCME's, would establish the procedural rules governing elections generally.

In deeming proxy access bylaw proposals non-excludable under Rule 14a-8(i)(8), we take no side in the policy debate regarding shareholder access to the corporate ballot. There might be perfectly good reasons for permitting companies to exclude proposals like AFSCME's, just as there may well be valid policy reasons for rendering them non-excludable. However, Congress has determined that such issues are appropriately the province of the SEC, not the judiciary. [...]

place a nominee on the corporate ballot but only if the proxy access rule had been “activated” by one of two triggering events, including the adoption, by majority vote, of a shareholder proposal submitted by a holder of more than 1% of the corporation's voting stock. Essentially, Proposed Rule 14a-11 establishes a process by which the shareholder proposal mechanism (subject to the heightened eligibility requirement that the proposal be submitted by a holder of more than 1% of the corporation's voting stock) may be employed to adopt a proxy access rule that is uniform across companies. We recognize that our holding facilitates a process, by means of shareholder proposals subject to the standard eligibility requirements, for adopting non-uniform proxy access rules that are less restrictive than that created by Proposed Rule 14a-11. Thus, there might very well be no reason for a rule based on Proposed Rule 14a-11 to co-exist with the procedure that our holding makes available to shareholders. Accordingly, if the Commission ultimately decides to adopt Proposed Rule 14a-11, then such an action, although certainly not necessary, would likely be sufficient to modify the interpretation of Rule 14a-8(i)(8) that we have adopted here.