

Third Circuit Ruling Allows Wal-Mart to Exclude Trinity's Stockholder Proposal from its Proxy Materials

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In a closely watched corporate governance case, the Third Circuit Court of Appeals ruled on April 14, 2015 that Wal-Mart Stores, Inc. ("Wal-Mart") could exclude a stockholder proposal (the "Proposal") submitted by Trinity Wall Street ("Trinity") from its 2015 proxy materials. Trinity framed its proposal as corporate governance reform, however, many considered it controversial, because it would allow stockholder oversight of products sold by Wal-Mart, particularly certain firearms. Prior to the Third Circuit's ruling, the U.S. District Court for the District of Delaware had issued an opinion requiring Wal-Mart to include the Proposal in its 2015 proxy materials.

The District Court's opinion caused considerable consternation amongst many corporate governance experts and the business community. There was concern that the opinion effectively nullified the well-established ordinary business exclusion provided by Securities and Exchange Commission ("SEC") Rule 14a-8(i)(7), that it conflicted with the SEC's longstanding interpretations, and that it disregarded three decades of consistent SEC staff guidance. Moreover, there was significant concern that the opinion's interpretation of SEC Rule 14a-8 could encourage stockholders to flood corporations with proposals that relate to products for sale by artfully framing them as requests for corporate governance reform.

SEC Rule 14a-8

Trinity submitted the Proposal pursuant to SEC Rule 14a-8. Under SEC Rule 14a-8, if a stockholder proposal complies with specified eligibility and procedural requirements, and is not excludable for substantive reasons, a company must: (i) include the stockholder proposal and related supporting statement in its proxy statement and list the stockholder proposal on its proxy card; and (ii) submit it to a vote at the stockholders' meeting along with the company's proposals.

SEC Rule 14a-(8)(i)(7), management functions, provides a frequently used substantive exclusion. Under SEC Rule 14-8(i)(7), stockholder proposals may be excluded from a

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company's proxy materials if the proposal deals with a matter relating to the company's ordinary business operations.

Case Background

On December 18, 2013, Trinity submitted the Proposal for inclusion in Wal-Mart's 2014 proxy materials, seeking a stockholder vote. The Proposal requested that the charter of Wal-Mart's Board of Directors' Compensation, Nominating and Governance Committee be amended to add the following to the committee's duties:

Providing oversight concerning the formulation and implementation of, and the public reporting of the formulation and implementation of, policies and standards that determine whether or not [Wal-Mart] should sell a product that:

1. especially endangers public safety and well being;
2. has the substantial potential to impair the reputation of the Company; and/or
3. would reasonably be considered by many offensive to the family and community values integral to [Wal-Mart's] promotion of its brand.

On January 30, 2014, as required by SEC Rule 14a-8(j), Wal-Mart submitted a detailed no-action letter request to the SEC notifying the SEC staff and Trinity that Wal-Mart intended to omit the Proposal from its 2014 proxy materials. The no-action letter request explained how the Proposal deals with matters relating to the company's ordinary business operations. On February 4, 2014, Trinity submitted its own detailed letter to the SEC staff, providing Trinity's analysis as to why its Proposal was not excludable and requesting that the SEC staff deny Wal-Mart's request for no-action relief.

On March 20, 2014, the SEC staff granted Wal-Mart's request for no-action relief and advised Wal-Mart that it had reviewed the correspondence and found that "there appears to be some basis for your view that Wal-Mart may exclude the proposal under rule 14a-8(i)(7), as relating to Wal-Mart's ordinary business operations. . . . Accordingly, we will not recommend enforcement action to the [SEC] if Wal-Mart omits the proposal from its proxy materials."

On April 1, 2014, Trinity filed suit in the U.S. District Court for the District of Delaware seeking a declaratory judgment that Wal-Mart's decision to omit the Proposal from the 2014 Proxy Materials violates Section 14(a) of the Securities Exchange Act of 1934 and SEC Rule 14a-8. Also on April 1, 2014, Trinity filed a motion for a preliminary injunction to prevent Wal-Mart from printing, issuing, filing, mailing, or otherwise transmitting its 2014 proxy materials that do not contain the Proposal.

Although the District Court denied Trinity's motion for a preliminary injunction, it later held that the Proposal was improperly excluded from Wal-Mart's 2014 proxy materials. The

District Court also enjoined Wal-Mart from excluding the Proposal from its 2015 proxy materials.

Wal-Mart immediately appealed to the Third Circuit Court of Appeals. On April 14, 2015, the Third Circuit Court of Appeals issued an order reversing the District Court's ruling. The Third Circuit's order states that Wal-Mart may exclude Trinity's proposal from its 2015 proxy materials. The order also indicates that the Third Circuit will issue its opinion on this matter at a later time.

Conclusions

Activist stockholders are likely to continue to submit large numbers of SEC Rule 14a-8 proposals to corporations. The Third Circuit's ruling, however, should alleviate concerns that corporations will be required to include "corporate governance reform" stockholder proposals in their proxy materials that effectively allow stockholder review of a corporation's ordinary business decisions, such as deciding what products to sell. Moreover, the ruling should clear the way to ensure that corporations can continue to rely on the precedent established by the SEC's longstanding interpretations of SEC Rule 14a-8(i)(7)'s ordinary business exclusion. Finally, the order will hopefully discourage stockholders from flooding corporations with proposals that relate to products for sale that are artfully framed as requests for corporate governance reform.

Resources:

[SEC No-Action Letter of March 20, 2014](#)

[U.S. District Court for the District of Delaware Opinion of November 26, 2014](#)

[Third Circuit Court of Appeals Order of April 14, 2015](#)