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Skadden

SEC Reporting & Compliance Alert

If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

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NYSE Revises Exceptions to Shareholder Approval Rules

On March 20, 2019, the Securities and Exchange Commission (SEC) approved an amendment to the New York Stock Exchange (NYSE) requirement that listed companies obtain shareholder approval for certain share issuances. The amendment modifies in particular the method of determining whether, in order to rely on certain exceptions to the shareholder approval requirements, the price at which common stock is sold by a company in a securities transaction exceeds the value of the common stock.

Shareholder Approval Requirements for Related Party and 20 Percent Issuances

NYSE Listed Company Manual Section 312.03(b) requires shareholder approval for certain related party transactions involving issuances of common stock, or securities convertible or exercisable into common stock, if the issuance exceeds 1 percent of the number of shares of common stock outstanding or 1 percent of the voting power outstanding before the issuance (related party issuances). In addition, Section 312.03(c) of the manual requires shareholder approval prior to the issuance of common stock, or securities convertible or exercisable into common stock, if the number of shares of common stock to be issued will equal or exceed 20 percent of the number of shares of common stock outstanding or 20 percent of the voting power outstanding before the issuance (20 percent issuances). Previously, both of these shareholder approval requirements included exceptions that required as one of the conditions that the issuance relate to the sale of common stock (or the sale of securities convertible into or exercisable for common stock) for cash at a price (or a conversion or exercise price) at least as great as each of the book value and market value of the company's common stock to be issued.

Change to the Pricing Condition

The amendment changes the pricing condition discussed above in two ways. First, it removes from the condition the reference to "book value." In proposing the change, the NYSE stated that book value is an accounting measure based on historic asset values rather than current value and, therefore, is not an appropriate measure of whether a transaction is dilutive or should otherwise require shareholder approval.

Second, the amendment replaces the concept of "market value" with that of a "minimum price." Minimum price, as defined by the NYSE, is the lower of (i) the official closing price reported on the NYSE immediately prior to the signing of a binding agreement to issue the securities or (ii) the average official closing price for the five trading days immediately prior to the signing of the binding agreement. In explaining the change, the NYSE acknowledged the widespread practice in commercial transactions involving the issuance of securities of using a five-day average when pricing transactions to avoid unanticipated and inequitable results based on a single day's closing price.

As a result of these changes, the pricing condition to avoid a shareholder vote for certain share issuances will only be satisfied by issuances priced at least as great as the minimum price, as discussed above.

Additional information about the NYSE rule change is available in the SEC's order approving the change. See also the amended Sections 312.03 and 312.04.

Similar Changes to Nasdaq Rule in 2018

In September 2018, the SEC approved similar changes to Nasdaq's analogous shareholder approval requirements applicable to securities issuances in private placements, where the amount of securities to be issued represents 20 percent or more of the outstanding common stock or voting power prior to the issuance (Nasdaq Rule 5635(d)). Previously, shareholder approval of such issuances was required only if the price of the securities sold in the transaction was "less than the greater of book or market value" of the company's common stock. Similar to the NYSE rule change discussed above, amended Rule 5635(d) no longer references "book value" and has replaced the concept of "market value" with "minimum price." Minimum price, as defined by Nasdaq, is the lower of (i) the closing price (as reflected on Nasdaq.com) immediately preceding the signing of the binding agreement or (ii) the average closing price of the common stock for the five trading days immediately preceding the signing of the binding agreement.

In addition, although not a substantive change, amended Rule 5635(d) now separately defines "20 percent issuances" to mean a transaction, other than a public offering, involving the sale, issuance or potential issuance by the company of common stock (or securities convertible into or exercisable for common stock), which, alone or together with sales by officers, directors or substantial shareholders of the company, equals 20 percent or more of the company's common stock or 20 percent or more of the voting power outstanding before the issuance.

Additional information about the Nasdaq rule change is available in the SEC's order approving the change. See also amended Nasdaq Rule 5635.

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