

May 21, 2020

NYSE Provides Temporary COVID-19 Exception From Shareholder Approval Requirements Under 20% Rule

SUMMARY

In light of the impact of the COVID-19 pandemic, the New York Stock Exchange LLC (“NYSE”) filed notice of a [proposed rule change](#) on May 14 with the Securities and Exchange Commission (“SEC”), which became effective immediately.¹ Specifically, Section 312.03T (the “Temporary Rule”) of the NYSE Listed Company Manual (the “Manual”) provides a limited temporary exception from the application of the shareholder approval requirements in Section 312.03 of the Manual—also known as the “20% Rule”—and a limited attendant exception from the requirements of Section 303A.08 of the Manual (Shareholder Approval of Equity Compensation Plans).² The Temporary Rule is substantially similar to Nasdaq Listing Rule 5636T, which was filed by The Nasdaq Stock Market LLC on May 4, 2020 (the “Nasdaq Rule”).³ Like the Nasdaq Rule, any securities issued in reliance on the exception must be issued by the later of June 30, 2020 and 30 calendar days following the date of the binding agreement governing the issuance, in each case, after the company has submitted a certification of its compliance with the requirements of the Temporary Rule and received approval from NYSE. Unlike the Nasdaq Rule, the Temporary Rule requires that a company certify that the proceeds of any issuance made pursuant to the Temporary Rule will not be used to fund any acquisition transaction and does not include a “safe harbor” provision waiving the requirement to obtain NYSE prior approval for transactions that meet specified conditions. The SEC is soliciting comments on the Temporary Rule for 21 days following publication in the Federal Register.⁴

DISCUSSION

NYSE-listed companies must obtain shareholder approval for transactions that involve (i) the issuance of common stock (or securities that are convertible into or exercisable for common stock) equal to 20% or more of the common stock of the company or voting power outstanding before the issuance, other than (a) public offerings for cash and (b) bona fide private financings at a price at or above (1) the NYSE official closing price⁵ immediately preceding the signing of the binding agreement and (2) the average NYSE official closing price of the common stock for the five trading days immediately preceding the signing of the binding agreement (the lower of (1) and (2), the “Minimum Price”);⁶ (ii) the issuance of common stock (or securities that are convertible into or exercisable for common stock) to certain related parties⁷ equal to 1% or more of the common stock of the company or voting power outstanding before the issuance (unless the only related parties in the transaction are substantial security holders and the price is at or above the Minimum Price, in which case the limit is increased to 5%);⁸ and (iii) establishing or materially amending a stock option or purchase plan or other equity compensation arrangement pursuant to which stock may be acquired by officers, directors, employees or consultants (each of (ii) and (iii), a “Related Party Transaction”).⁹

The Temporary Rule provides NYSE-listed companies a general exception to the shareholder approval requirements under the 20% Rule. In addition, the Temporary Rule provides listed companies with an exception to the shareholder approval requirements for Related Party Transactions, but only for issuances that are otherwise covered by the Temporary Rule, and provided that (1) any single person covered by the Related Party Transaction requirements (an “Affiliated Purchaser”) participates for less than 5% of the transaction; (2) all Affiliated Purchasers’ aggregate participation is less than 10% of the transaction; (3) any Affiliated Purchaser’s participation was specifically required by unaffiliated investors; and (4) the Affiliated Purchasers have not participated in negotiating the economic terms of the transaction.

Prior to filing the Temporary Rule, in April 2020 NYSE had already waived certain of the requirements of the 20% Rule through June 30, 2020 in response to the impact of the COVID-19 pandemic. Specifically, NYSE waived (i) the provision in Section 312.03(b) that limits the participation of Related Parties¹⁰ and other purchasers affiliated with a Related Party to no more than 5% of the company’s shares or voting power provided the transaction is at or above the Minimum Price; and (ii) certain of the requirements for meeting the bona fide private financing exception to Section 312.03(c), described above.¹¹

In proposing the Temporary Rule, NYSE noted that while listed companies in financial distress already benefit from an exception from the shareholder vote requirement if the delay associated with securing shareholder approval would seriously jeopardize the financial viability of the company (the “Financial Viability Exception”), the Temporary Rule would cover circumstances where the financial viability of the company may not be in serious jeopardy, but the company nevertheless needs access to additional funding during the COVID-19 pandemic on an accelerated timeline.¹² NYSE further noted that the accelerated

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need for funds, in combination with a company's curtailed operations, may make it impractical to mail notice to all shareholders as required by the Financial Viability Exception.

A NYSE-listed company seeking to avail itself of the temporary exception under the Temporary Rule must demonstrate the following:

- the need for the transaction is due to circumstances related to COVID-19;
- the proceeds will not be used to fund any acquisition transaction;
- the delay in securing shareholder approval would (A) have a material adverse impact on the company's ability to maintain operations under its pre-COVID-19 business plan; (B) result in workforce reductions; (C) adversely impact the company's ability to undertake new initiatives in response to COVID-19; or (D) seriously jeopardize the financial viability of the enterprise;
- the company undertook a process designed to ensure that the proposed transaction represents the best terms available to the company;
- the company's audit committee or a comparable committee comprised solely of independent, disinterested directors (A) expressly approved reliance on the exception and (B) determined that the transaction is in the best interests of shareholders; and
- the company has submitted a supplemental listing application as required by Section 703.01(part one)(A) of the Manual for the applicable transaction along with a certification that the company complies with all of the foregoing requirements and describing with specificity how it complies.

NYSE will review all transactions for compliance with the requirements of the Temporary Rule and must approve a company's reliance on the Temporary Rule before the company may enter into a binding agreement governing the transaction or issue any securities in the applicable transaction. Since the process required to obtain "the best terms available to the company" is unspecified in the Temporary Rule, it is unclear what may be necessary to comply with this requirement. Furthermore, unlike the Nasdaq Rule, the Temporary Rule does not include a "safe harbor" provision waiving the requirement to obtain the exchange's prior approval for transactions that meet specified conditions.

Any company that relies on the Temporary Rule must also make a public announcement by filing a Form 8-K, if required by SEC rules, or by issuing a press release as promptly as possible, but not later than two business days **before** the issuance of the securities. Such public announcement must disclose:

- the terms of the transaction (including the number of shares of common stock that could be issued and the consideration received);
- that shareholder approval would ordinarily be required under NYSE rules but for the fact that the company is relying on an exception to the shareholder approval rules; and
- that the audit committee or a comparable committee comprised solely of independent, disinterested directors expressly approved the company's reliance on the exception and determined that the transaction is in the best interests of shareholders.

After submitting the required notices, obtaining the required approval, making the required announcements and executing a binding agreement governing the issuance of the securities prior to June 30, 2020, a

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company may issue securities governed by such agreement by the later of June 30, 2020 and 30 calendar days following the date of the binding agreement.

All securities issued in reliance on the Temporary Rule will be aggregated with any subsequent issuance by the company (other than a public offering for cash) at a discount to the Minimum Price if the binding agreement for the subsequent issuance is executed within 90 days of the reliant issuance and if, following the subsequent issuance, the aggregate amount of shares issued in the reliant and subsequent issuance equals or exceeds 20% of the total shares or the voting power outstanding before the reliant issuance, shareholder approval will be required under Section 312.03(c) of the Manual prior to the subsequent issuance.

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ENDNOTES

- ¹ Under Rule 19b-4(f)(6)(iii) under the Exchange Act, a proposed rule change may be immediately effective if it does not (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate.
- ² Securities Exchange Act Release No. 34-88875; File No. SR-NYSE-2020-43 (May 14, 2020), *available at* <https://www.sec.gov/rules/sro/nyse/2020/34-88875.pdf>.
- ³ For further information about the Nasdaq Rule, see our Client Memorandum, NASDAQ Provides Temporary COVID-19 Exception From Shareholder Approval Requirements Under 20% Rule, dated May 11, 2020, *available at* <https://www.sullcrom.com/files/upload/SC-Publication-NASDAQ-Provides-Temporary-COVID-19-Exception-From-Shareholder-Approval-Requirements-Under-20-percent-Rule.pdf>.
- ⁴ At any time within 60 days of the filing, the SEC may temporarily suspend the rule change if it appears to the SEC that action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.
- ⁵ Generally, the NYSE Official Closing Price is the official closing price on the Exchange as reported to the Consolidated Tape of the Consolidated Tape Association immediately preceding the signing of a binding agreement to issue the securities. See Section 312.03 for more details, *available at* <https://nyse.wolterskluwer.cloud/listed-company-manual>.
- ⁶ Section 312.03(c) of the Manual, *available at* <https://nyse.wolterskluwer.cloud/listed-company-manual>.
- ⁷ Such parties include (1) a director, officer or substantial security holder of the company (each, a “Related Party”), (2) a subsidiary, affiliate or other closely related person of a Related Party or (3) any company or entity in which a Related Party has a substantial direct or indirect interest.
- ⁸ Section 312.03(b) of the Manual, *available at* <https://nyse.wolterskluwer.cloud/listed-company-manual>.
- ⁹ Sections 312.03(a) and 303A.08 of the Manual, *available at* <https://nyse.wolterskluwer.cloud/listed-company-manual>.
- ¹⁰ See Note 6.
- ¹¹ Securities Exchange Act Release No. 34-88572 (April 6, 2020); 85 FR 20323 (April 10, 2020); File No. SR-NYSE-2020-30, *available at* <https://www.sec.gov/rules/sro/nyse/2020/34-88572.pdf>.
- ¹² Securities Exchange Act Release No. 34-88875; File No. SR-NYSE-2020-43 (May 14, 2020), *available at* <https://www.sec.gov/rules/sro/nyse/2020/34-88875.pdf>.

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