

Client Alert

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SEC Staff Grants First No-Action Relief Under Economic Relevance Exception

On February 22, 2018, the SEC staff issued a No-Action Letter to Dunkin' Brands Group, Inc., permitting the company to exclude a shareholder proposal under Rule 14a-8(i)(5), often referred to as the economic relevance exception. The proposal concerned a request to reduce environmental impact of a business line not integral to the company's core business and in which the products were actually made by third parties under license agreements. This is the first no-action relief granted under the economic relevance exception since the SEC [issued](#) Staff Legal Bulletin No. 14I (SLB 14I) on November 1, 2017, and it could have implications for other companies seeking to exclude shareholder proposals under this rule in the future.

Under Rule 14a-8(i)(5), an issuer may exclude a shareholder proposal that relates to operations that account for less than 5% of a company's total assets and less than 5% of its net earnings and gross sales at the end of its most recent fiscal year, and is not otherwise significantly related to the company's business. In the recent past, the SEC staff has rarely granted no-action relief to permit a company to exclude a proposal under this exemption. SLB 14I, however, signaled a potential change in the staff's approach to this issue.

Shareholder proposals that raise social or ethical concerns need to show that those issues have a significant effect on the company's business, not just possible economic or reputational harm, in order to persuade the staff to reject no-action relief. SLB 14I provides that a company's board of directors is generally in a better position than the SEC's staff to make an initial determination regarding whether a proposal significantly relates to the company's business. Thus, in order to improve the likelihood of excluding a shareholder proposal under Rule 14a-8(i)(5), a company should consider whether to discuss the board's analysis of whether the proposal is significant to the company, including the process used by the board to ensure a sound decision.

Dunkin' Brands Group received a shareholder proposal requesting that its board of directors issue a report assessing the environmental impact of using K-Cup pods brand packaging, and the company sought to exclude the proposal under Rule 14a-8(i)(5). Referencing SLB 14I, Dunkin' Brands Group's no-action request noted that the company's nominating and corporate governance committee of its board of directors had considered the proposal's significance to the company's business and had presented its findings to the entire board. First, most of the company's revenue related to K-Cup pod sales was generated from licensing fees, and the remaining revenue was generated from royalties from K-Cup pod sales in Dunkin' Donuts-franchised locations. The combined revenues related to K-Cup pod sales accounted for less than 5% of the company's total assets, gross sales, and net earnings for the 2016 fiscal year and were expected to remain at less than 5% for the 2017 fiscal year.

Additionally, the proposal did not relate to the company's primary business operations as a franchisor of quick service restaurants, but instead the proposal related to the packaging used in products manufactured by third parties under licensing arrangements. Under this arrangement, the company decides the types of products that are subject to licensing arrangements, but the licensing partner has the experience and expertise to determine which materials to use based on a variety of factors, including environmental impact. The committee had also considered the fact that a prior vote on an almost

identical proposal had received less than 14% support among shareholders, and during the course of the company's significant shareholder engagement efforts, no other shareholder had raised concerns over the environmental impact of K-Cup pods packaging. Therefore, Dunkin' Brands Group contended that there was an insufficient connection between the subject of the proposal and the company's business, which led the board of directors to conclude that the proposal was not significantly related to the company's business.

The SEC staff granted no-action relief, noting that the 5% total assets, net earnings, and gross sales threshold was not met and the proponent had not demonstrated that the proposal was otherwise significant to the company's business. The staff's decision also specifically mentioned the description of the board's analysis process that was included in Dunkin Brands Group's submission. The detailed discussion of factors considered by Dunkin' Brands Group's board of directors, informed by SLB 141, provides useful guidance for other issuers when analyzing shareholder proposals and requesting no-action relief under the economic relevance exception.

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