

A graphic at the top of the page features a large white circle with the words "PROXY VOTE" in bold red capital letters. The circle is surrounded by a blue ring with white stars, reminiscent of the American flag. On the left and right sides, there are stylized hands in blue and red, appearing to hold or support the central circle. The background is a dark blue map of the United States.

# PROXY VOTE

## *Shifting Leverage in Shareholder Votes*

Cross currents with shareholder access to company proxies.

**BY DOUG RAYMOND**

An incumbent director has powerful advantages in any election contest with a challenger. One of the most significant is that the incumbents' nominations are included in the company's proxy statement, and the proxy card that goes to all shareholders makes it very easy to vote for their re-election.

By contrast, challengers must mount their own campaign, and at their own expense prepare and distribute competing proxy statements and cards and try to persuade shareholders not to default to the usual choice. The "proxy access" movement seeks to shift that balance of power away from the incumbents and to level the playing field for challengers.

Proxy access rights allow shareholders who have nominated directors who are challenging management's nominees, to press their nominees' election using the company's proxy statement and more importantly, its proxy card mailed to shareholders. Typically, this allows shareholders (including a group of shareholders) that have held a minimum amount of shares (e.g., three percent of the outstanding) for a stated period of time (often three years) to nominate candidates for up to 20% of the board (or at least two directors).

Being included in the company's proxy statement can greatly increase the chances of a dissident being elected to the board,

it strengthens the leverage of institutional and activist shareholders when dealing with boards over a range of issues. Even without a pending election contest, the incumbent directors know that a credible election contest may emerge if the investors believe that the incumbents are not fully engaged in that dialogue.

The Securities and Exchange Commission originally adopted a version of Proxy Access in 2010 in Exchange Act Rule 14a-11 that applied to all public companies; however, a year later the rule was invalidated by a Federal Appeals Court on the basis that the SEC had adopted it in an arbitrary and capricious manner, without having conducted

a sufficient assessment of its economic impact. But the concept survived, and like the "majority voting" movement for director elections, has been championed by public pension funds and other institutional investors.

While the number of proposals submitted by shareholders seeking adoption of proxy access may have peaked, corporations continue to be pressured to adopt proxy access and many have preemptively adopted management-supported bylaws to avoid having to deal with a shareholder proposal that would need to be included in the company's annual proxy statement. And today, over 70% of S&P 500 companies have adopted some form of proxy access, and in

general, these follow fairly specific pathways, along the lines described above.

Before the rise of index funds and passive investing, institutional shareholders typically would “vote with

attention of the board. Thus, even without launching a contested election they can have greater impact on corporate decisions and in having their concerns addressed.

At the same time, the

of directors, separation of the chairperson and CEO positions, and a range of proposals on executive compensation. (See related article on page 80.)

For many years, a Rule 14a-8 proposal could be submitted by any shareholder holding at least \$2,000 of the company’s shares. In its recent proposal, the SEC proposes instead requiring that the shareholder own at least \$25,000 of stock, although the threshold drops to \$15,000 if the shares have been owned for two years and back to \$2,000 where the shares have been held for at least three years. While these changes will not affect institutional shareholders, they are expected to curtail access for retail holders who may not be able to commit such investments to a single company.

Although these sorts of shareholder proposals are often non-binding, a “win” may not be to impact corporate action. For example, a proposal raised by an Amazon shareholder challenging the company’s reliance on fossil fuels garnered only 31% support but ultimately contributed to Amazon’s pledge to become carbon neutral by 2040. A significant showing of support can encourage change, especial-

ly where the issue is one supported by institutional shareholders.

While some of these proposals may be whimsical or impractical, this rule change could impede smaller shareholders from being able to effectively raise important or innovative issues.

Proposals first raised in this fashion often have subsequently become significant issues that corporations have had to address, including matters such as independent board chairs, majority voting and pay ratio disclosure. While directors can see the growing influence of the institutional investor community, they should consider whether they want to stifle the voices of their smaller, often individual stockholders.

As boards navigate how to interact with the corporation’s stakeholders, they should look to how they can best keep informed of the issues that are important these shareholders, which are often harbingers of future challenges. ■

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their feet,” and sell shares of those companies when they disagreed with management’s direction or its governance practices. Where investors do not have that option, they are motivated to engage directly with management and the board on issues of significance to them. Proxy access, like the majority voting movement before it, gives these shareholders new leverage to make their voices heard in the boardroom. The ability to use the company’s proxy statement to mount a challenge to incumbent directors strengthens the shareholders’ hand in gaining the

SEC is proposing to reduce the ability of smaller, retail holders to be heard.

The SEC recently proposed amendments to Rule 14a-8, which is the rule that requires a public company, subject to various conditions, to include in its annual meeting proxy statement a proposal made even by a small shareholder, other than for the election of directors. Typical proposals address environmental and social issues, such as climate change, child and slave labor, and equal pay initiatives, as well as governance issues such as majority voting, staggered boards