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Recommendations to SEC-IAC on Proxy Access

James McRitchie, February 5, 2015 ,

I'm delighted to see "Discussion of Proxy Access" as one of the items on the **agenda** for the **SEC's Investor Advisory Committee** (SEC-IAC) at the upcoming February 12th meeting. I discuss two recommendations below.

Proxy Access: Rule 14a-11

In light of CFA Institute's ***Proxy Access in the United States: Revisiting the Proposed SEC Rule*** with the following findings, it is time to revisit the SEC's overturned Rule 14a-11.

- Proxy access has the potential to enhance board performance and raise overall US market capitalization by up to $140.3 billion
- Proxy access would "benefit both the markets and corporate boardrooms, with little cost or disruption."

The SEC-IAC should unequivocally recommend to the Commission that they resubmit Rule 14a-11 using the CFA cost analysis.

Proxy Access: Rule 14a-8(i)(9)

I would also like to see the SEC-IAC take a stand on how Rule 14a-8(i)(9) should interpreted (based on Proposing Release **39093**) or rewritten. Proxies should be able to include more than one item on the same general subject matter so that shareholders can express their preferences.

As I am sure many of you are aware, the initial no-action relief granted to Whole Foods Market was similar to ***AFSCME vs AIG***, where the SEC also reinterpreted an existing rule without going through the rulemaking process. In both cases the reinterpretation came about gradually over a number of years, until the original intent was forgotten (or ignored). When rules are changed, the public has a right to notice and input. Download my appeal. (**McRitchieAppealNo-action12-23-2014**). I am delighted with **Chair White's request for review of Rule 14a-8(i)(9) and the Division's decision to express no views** on how to interpret the rule this proxy season.

The staff's position effectively denied shareholders the right to vote on competing proposals involving similar or related topics solely because the proposals contained different terms or thresholds. The interpretation

effectively limited shareholders to consideration of proposals sponsored by the board of directors and eliminates any opportunity for shareholders to present alternative criteria. The interpretation is an unnecessary limitation on the shareholder franchise, effectively depriving shareholders of rights that exist under state law, and is inconsistent with the Commission's intent in adopting subsection (i)(9).

The current iteration of subsection (i)(9) was added in 1998. *See* Exchange Act Release No. 40018 (May 21, 1998) (**adopting release**). In proposing the language, the Commission noted that the provision was consistent with the "long-standing interpretation" that permitted "omission of a shareholder proposal if the company demonstrates that its subject matter directly conflicts with all or part of one of management's proposals." In providing examples of the "long-standing interpretation" the Proposing Release (**39093**) cited two no action letters: *General Electric Corporation* (Jan. 28, 1997) and *Northern States Power Co* . (July 25, 1995).

In *General Electric*, the "conflict" arose out of two proposals that affected stock option plans. The shareholder proposal called for the mandatory indexing of the exercise price. In contrast, the Company proposal assigned to the board the discretion to determine the exercise price so long as the exercise price was not less than the market price. If adopted, therefore, the company would be confronted with pricing formulas that were inconsistent. As a result, the staff agreed that the proposal could be excluded.

In *Northern States Power Co.* (July 25, 1995), the company intended to submit a merger agreement to shareholders. The shareholder proposal at issue would have mandated that management negotiate a more equitable merger agreement, specifically the payment of alternative consideration. To the extent that both passed, neither could be implemented. *See Id.* ("An affirmative shareholder vote on both the Board's proposal and the Proponents' proposal would present the Board with an inconsistent mandate. The Board could not both enter into the merger agreement and negotiate a different agreement."). As a result, the staff permitted the exclusion of the proposal.

These letters illustrate that, at the time of the adoption of the current version of subsection (i)(9) by the full Commission, proposals could be excluded only in very narrow circumstances and only where adoption of competing proposals could be harmful to shareholders. As *General Electric* and *Northern States* demonstrated, proposals could be excluded where adoption resulted in confusion or uncertainty in actual implementation or where, as a result of incompatibility, implementation of both proposals was impossible.

The staff also made clear that subsection (i)(9) could not be used as a tactical weapon in order to exclude shareholder proposals. To the extent company proposals were developed "in response to" a proposal submitted by shareholders, the subsection was unavailable. Finally, the staff only allowed for the exclusion of proposals that raised actual and immediate concerns. The proposals at issue in *General Electric* and *Northern States* were both mandatory and not precatory and, as a result, they raised clear and unavoidable issues with respect to implementation.

The interpretation of subsection (i)(9) by the staff directly interferes with the shareholder franchise and effectively denies shareholders rights that exist under state law. Under state law, shareholders have the right to propose bylaws. Moreover, in at least some jurisdictions, they have the express right to propose bylaws that provide for shareholder access. Without the ability to include a proposal in the proxy statement, shareholders are effectively denied the right to adopt bylaws. Download the full appeal as a pdf (**McRitchieAppealNo-**

action12-23-2014).

This season we will see instances where companies include both their own proposals and the proposal of a shareholder. One case I know of (not involving proxy access) will be a proxy that includes a binding bylaw proposal from the company and a precatory proposal from a shareholder on the same topic. My understanding is the proxy will be filed in early March. Such votes will provide a true measure of shareholder sentiment.

The SEC-IAC should recommend changes to Rule 14a-8(i)(9), if needed, to clarify that it does not preclude inclusion of proposals on the same topic and that the rule cannot be used "in response to" a proposal from shareholders.

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