
November 14, 2019

SEC Proposes Amendments to Improve Accuracy and Transparency of Proxy Voting Advice and Modernize Shareholder Proposal Rules

Last week, the Securities and Exchange Commission voted 3-2 to propose amendments to its proxy solicitation rules as applicable to proxy voting advice and its Rule 14a-8 shareholder proposal procedures. In his statement at the open meeting approving the proposals, Chairman Clayton stated that these amendments are meant to modernize the subject provisions to ensure that investors receive the material information needed to make their investment and voting decisions and facilitate constructive engagement by long-term shareholders. Commissioners Jackson and Lee dissented, however, stating that there could instead be significant harmful unintended consequences, including, for example, increased costs on shareholders that would in fact deter engagement. Needless to say, the split vote reflects similar disagreement among the various stakeholders in this area. Proxy advisory firm Institutional Shareholder Services has sued the SEC to seek injunctive and declaratory relief against the SEC's previous guidance related to proxy voting advice issued in August, some of which is now proposed to be codified by the SEC. The suit is pending in the U.S. District Court for the District of Columbia. Comments on both proposals are due 60 days after their publication in the Federal Register.

Proposed Amendments to Section 14 of the Exchange Act

Codification of Proxy Voting Advice as "Solicitations" under Rule 14a-1(l). The SEC has proposed to codify guidance issued in August 2019, that a "solicitation," as defined under Exchange Act Rule 14a-1(l), includes proxy voting advice (other than research reports or data not used to formulate voting recommendations and administrative or ministerial services). (See our alert on this development [here](#).) The proposing release reiterates that the definition of solicitation is "broad" and includes a "communication to security holders under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy." Extending this concept to the modern proxy advisory industry, the SEC concludes that much of the proxy advisory firms' business is reasonably calculated to result in a proxy voting decision and, therefore, constitutes a solicitation under the proxy rules.

In keeping with this view, the proposed amendments to Rule 14a-1(l) would add that the terms "solicit" and "solicitation" include any "proxy voting advice that makes a recommendation to a shareholder as to its vote, consent, or authorization on a specific matter for which shareholder approval is solicited, and that is furnished by a person who markets its expertise as a provider of such advice, separately from other forms of investment advice, and sells such advice for a fee." Each set of voting recommendations under

different voting policies would constitute separate communications of proxy voting advice, each subject to these proposed rules.

The proposed rules would clarify that any person who furnishes such advice in response to an unprompted request (such as a financial advisor or broker who has received unsolicited inquiries from its clients on how to vote their shares) would continue to not be considered to have engaged in a solicitation.

New Conditions for Exemptions from Proxy Information and Filing Requirements under Rule 14a-2(b) for Proxy Advisory Firms. Notwithstanding that proxy voting advice is proposed to be codified as a solicitation, proxy advisory firms would still be able to rely on exemptions to certain of the SEC's proxy solicitation information and filing requirements so long as they (i) do not seek, directly or indirectly, the power to act as a proxy for a security holder and do not furnish or otherwise request, or act on behalf of a person who furnishes or requests, a form of revocation, abstention consent or authorization, and (ii) satisfy proposed new conditions related to conflicts of interest disclosure; providing a company and soliciting person a review period for proxy voting advice and hyperlinking company and soliciting persons' views on the proxy voting advice, in each case as described in more detail below. Any immaterial or unintentional failures to comply with these new conditions, however, would not result in the loss of the proxy advisory firms' proxy rule exemptions if they made a good faith and reasonable effort to comply and then as soon as practicable after becoming aware of noncompliance and as feasible, use reasonable efforts to substantially comply.

Conflicts of Interest Disclosure. To be able to rely on the Rule 14a-2(b) exemption, proxy advisory firms would have to include in their advice (including in any electronic medium used to deliver the advice) "prominent disclosure" of the following:

- any of its or its affiliates' direct or indirect material interests in the matter or parties concerning which it is providing the advice;
- any material transaction or relationship between it or its affiliates and the company, another soliciting person, shareholder-proponent or affiliates of any of the foregoing (as determined using publicly available information) connected with the matter covered by the proxy voting advice;
- any other information regarding its or its affiliates' interest, transaction or relationship that is material to assessing the objectivity of the proxy voting advice in light of the circumstances of the particular interest, transaction or relationship; and
- any policies and procedures used to identify, and the steps taken to address, any such material conflicts of interest, which disclosure should include a description of the material features of the policies and procedures to be able to understand and evaluate them, such as

the type of transaction or relationship that would be covered and the persons responsible for administering the policies and procedures.

The proposing release states that the conflicts disclosures should be detailed enough so that proxy advisory clients can understand the nature and scope of the interest, transaction or relationship and assess the objectivity and reliability of the advice they receive, which may include the identities of the parties or affiliates and the approximate dollar amount of fees involved in the interest, transaction or relationship. The release warns that boilerplate language that such relationships or interests may or may not exist (which is the current practice among many proxy advisors) would be insufficient.

Review Period. The proposed amendments would mandate a standardized process for all companies and other persons conducting a solicitation covered by any proxy voting advice to review and provide feedback on the advice before its dissemination. The period available for the review depends on when the definitive proxy statement is filed, with a longer review period for earlier filings as follows:

Definitive Proxy Statement Filing Date	Review Period
< 25 days prior to meeting date	None
25-44 days before meeting date	3 business days
45 or more days before meeting date	At least 5 business days

In addition, after the applicable review period and at least two business days before the delivery of the voting advice to clients, proxy advisory firms would be required to send a final notice and copy of the voting advice. Similar review periods would apply to votes, consents or authorizations where no meeting is held. Persons conducting exempt solicitations and shareholder-proponents submitting proposals under Rule 14a-8 would not have the benefit of a review period.

Proxy advisory firms would be permitted to require the company and other soliciting persons reviewing the advice to enter into confidentiality agreements for materials exchanged during the review period. The agreements would have to be similar to those for the clients of the proxy advisory firms and would cease to apply once the advice has been provided to clients. It is unclear whether company and soliciting persons' advisors would be permitted to review such materials in this process.

Hyperlinks to Company/Soliciting Person Views. If requested by the company or soliciting person before the end of the applicable review period, proxy advisory firms would be required to include in their proxy voting advice (including in any electronic medium used to deliver the advice) an active

hyperlink or analogous electronic medium that leads to the company or soliciting persons statement regarding any proxy voting advice.

Expansion of Examples of Potentially Misleading Information under Rule 14a-9. One important aspect of these proposed amendments is that even though proxy advisory firms would be exempt from certain of the SEC's proxy information and filing rules, their voting advice as solicitations would be subject to Rule 14a-9's antifraud provisions. Further, the proposed amendments would add a new section (e) to the note for Rule 14a-9, which states that failure to disclose "material information" with respect to proxy voting advice could be misleading. The types of information that may be material include the proxy advisory firm's methodology, sources of information, conflicts of interest and use of standards that materially differ from relevant standards or requirements approved by the SEC.

Proposed Amendments to Rule 14a-8

Proposed New Tiered Ownership and Holding Period and Other Eligibility Requirements under Rule 14a-8(b). Currently, the eligibility requirements for a shareholder to be permitted to submit a proposal for inclusion in a proxy statement include both an ownership threshold of \$2,000 in market value or 1% of securities entitled to vote and a continuous holding period requirement of at least one year. The proposed amendments would eliminate the 1% threshold and add new tiered ownership and holding period thresholds as follows:

Ownership Threshold (in market value of the company's securities entitled to vote)	Continuous Holding Period
\$2,000	At least 3 years
\$15,000	At least 2 years
\$25,000	At least 1 year

Aggregation of share ownership to meet these thresholds would not be permitted. Shareholders could continue to act as co-filers so long as each shareholder met the ownership and holding period requirements. The proposing release states that it would be a "best practice" for co-filers to identify a lead filer and state whether such filer is authorized to negotiate with the company and withdraw the proposal on co-filers' behalf.

If a shareholder-proponent uses a representative to act on his or her behalf with respect to a proposal, such shareholder-proponent must provide the company with written documentation that:

- identifies the company to which the proposal is directed, the annual or special meeting for which the proposal is submitted, the shareholder as the proponent and the person acting on his or her behalf as a representative and the specific proposal to be submitted;
- includes the shareholder's statement authorizing the designated representative to submit the proposal and/or otherwise act on the shareholder's behalf and the shareholder's statement supporting the proposal; and
- be signed and dated by the shareholder.

Finally, as part of its effort to encourage shareholder/company engagement, the proposed amendments would require that each shareholder-proponent state that he or she is able to meet with the company, either in person or via teleconference, during the 10-30 calendar day period after submission of the shareholder proposal and provide contact information as well as business days and specific times that the shareholder-proponent is available to discuss the proposal with the company.

Clarifying the "One Proposal" Rule under Rule 14a-8(c). The proposed amendments attempt to address company complaints related to "proposal by proxy" situations by establishing a one-person/one-proposal regime. Currently, the rule states that each shareholder may submit a proposal, which led to shareholders or representatives submitting more than one proposal albeit on other shareholders' behalf. Specifically, Rule 14a-8(c) is proposed to be amended so that each "person" (instead of shareholder) may submit only one proposal. In other words, a shareholder would not be able to submit a proposal himself or herself and then act as a representative for another shareholder, and a representative would not be able to act as such for more than one shareholder.

Increasing Resubmission Thresholds under Rule 14a-8(i)(12). The current resubmission thresholds for a shareholder to resubmit a substantially similar proposal are 3%, 6% and 10% if voted on once, twice or three or more times in the last five years. The SEC has proposed to replace these thresholds with 5%, 15% and 25%, respectively. Additionally, even if a proposal that has been voted on three or more times in the last five years and received 25% or more of the votes cast in the last year, the SEC would permit exclusion under proposed new "momentum" provision that would permit companies to exclude the proposal if it experienced a decline in shareholder support of 10% or more compared to the immediately preceding vote.

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The foregoing proposals will be subject to a 60-day comment period. With respect to the proxy voting advice amendments, the SEC has proposed to provide a one-year transition period after the publication of the final rule in the *Federal Register* to give affected parties sufficient time to comply with the proposed new requirements. The Rule 14a-8 proposal is silent as to timing of effectiveness.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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