

Consider Your Options As NY Proxy Access Efforts Continue

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Last month, New York City Comptroller Scott Stringer announced that, as the custodian and trustee of New York City's five public pension funds, he has submitted 72 shareholder proposals to public companies this proxy season calling for the adoption of "meaningful proxy access bylaws."^[1] These proposals build on the "Boardroom Accountability Project" the comptroller's office launched in 2015, pursuant to which it submitted 75 precatory shareholder proposals to companies in diverse industries and with various market capitalizations, seeking the right for shareholders owning 3 percent of the company's outstanding shares for at least three years to nominate up to 25 percent of the board in the company's proxy materials.

The comptroller's initiative was largely responsible for the influx of proxy access shareholder proposals last year and played a significant role in the growing trend of companies adopting proxy access bylaw provisions. Last year, a total of 88 proxy access shareholder proposals were submitted to a vote at Russell 3000 companies, in contrast to 16 in 2014. Of the shareholder proposals that were submitted to a vote among the Russell 3000 last year, 54 (or 61.4 percent) passed, while 34 (or 38.6 percent) failed, with the proposals receiving average shareholder support of 55 percent. Approximately 115 companies adopted proxy access bylaws in 2015, in contrast to merely 11 companies that had implemented proxy access up to and through 2014. While the majority of issuers that adopted proxy access last year did so pursuant to a shareholder proposal, several companies did so voluntarily (i.e., without having received a shareholder proposal) — most of them in the last few months of the year.

As the comptroller's recent press release makes clear, the comptroller's office continues to press ahead with its initiative, pursuing a universal standard of proxy access for shareholders holding at least 3 percent of the company's outstanding stock for at least three years. Like last year, the vast majority of the issuers targeted by the comptroller's office this year are companies with purportedly weak track records on board diversity, climate change or say-on-pay. Interestingly, half of the 72 companies that

received the comptroller’s proxy access proposal this year received the comptroller’s proposal last year, but, according to the comptroller, “have not yet enacted, or agreed to enact, a 3% bylaw with viable terms.” Notably, this group includes companies that enacted so-called “unworkable bylaws requiring 5% ownership, some of which received *binding* proposals to amend their bylaw.”[2]

The 36 companies that received the comptroller’s proposal for the second year in a row can be broken down as follows:

NUMBER OF COMPANIES	SITUATION
17 companies	These companies submitted the Comptroller’s proposal to a shareholder vote last year along with an opposition statement by the board, and the proposal received majority support but has not been implemented (at least as of yet).
12 companies	<p>These companies submitted the Comptroller’s proposal to a shareholder vote last year along with an opposition statement by the board, and the proposal failed.</p> <ul style="list-style-type: none"> In one of these cases, the company subsequently adopted a proxy access bylaw allowing a shareholder or a group of up to 20 shareholders, owning five percent or more of the company’s stock for at least three years, to nominate up to 20 percent of the board.
5 companies	<p>These companies included the Comptroller’s proposal in their proxy materials last year alongside a dueling management proposal on proxy access; in two of these cases, the Comptroller’s proposal passed.</p> <ul style="list-style-type: none"> In one case where the Comptroller’s proposal failed but the management proposal garnered majority support, the company adopted a proxy access bylaw provision permitting a shareholder or a group of up to 10 shareholders, owning five percent or more of the company’s outstanding stock for at least three years, to nominate up to 20% of the board.
2 companies	These companies adopted proxy access for holders of five percent of the company stock and later submitted the Comptroller’s proposal to shareholders with a board opposition statement. One of these shareholder proposals passed, while the other failed; in neither case did the issuer amend its proxy access bylaw after the shareholder vote.

Of the comptroller’s 36 resubmitted proposals, six have already been withdrawn after the respective issuers have enacted, or agreed to enact, proxy access for holders of 3 percent of the company’s outstanding stock. Similarly, of the 36 proposals submitted to new companies, nine have been subsequently withdrawn under the same circumstances.

Implications and Considerations for Public Companies

The proxy access proposals resubmitted by the comptroller's office this year suggest that, in its sustained pursuit of a global standard of proxy access across public companies, the comptroller's office may continue to target those issuers at which its proposal has previously failed, as well as those issuers that have not implemented a proxy access proposal that has garnered majority support. In light of the proxy access trends observed over the last proxy season and the comptroller's continued initiative, publicly traded companies that have not adopted proxy access (or have not adopted proxy access at the 3 percent shareholding threshold) should consider their strategy.

Companies That Had a Majority-Supported Proxy Access Shareholder Proposal

Issuers that received a proxy access shareholder proposal that garnered majority shareholder support last year should consider adopting proxy access or submitting a binding management proposal to shareholders that would implement proxy access. In so doing, issuers should consider, among other things, the views of their large institutional investors regarding the specific parameters of their proxy access bylaw. They should also consider the guidance that Institutional Shareholder Services Inc. released on Dec. 18, 2015, regarding its evaluation of a board's implementation of proxy access in response to a majority-supported shareholder proposal.^[3] Pursuant to its guidance, ISS may issue adverse vote recommendations with regard to individual directors, nominating/governance committee members or the entire board, as it deems appropriate, "if a proxy access policy implemented or proposed by management contains material restrictions more stringent than those included" in the majority-supported shareholder proposal with respect to specified features.

In particular, ISS disfavors ownership thresholds above 3 percent, an ownership duration longer than three years, a limit below 20 shareholders that may be aggregated to reach the ownership threshold, and a cap on proxy access nominees below 20 percent of the board. With regard to an aggregation limit or cap that differs from that provided in the shareholder proposal, ISS has further indicated that "lack of disclosure by the company regarding shareholder outreach efforts and engagement may also warrant negative vote recommendations."

ISS has also clarified that, in addition to "whether the major points of the shareholder proposal are being implemented," ISS will consider whether added provisions that were not included in the shareholder proposal "unnecessarily restrict the use of a proxy access right." The provisions ISS considers "especially problematic" are "[c]ounting individual funds within a mutual fund family as separate shareholders for purposes of an aggregation limit" and imposing "post-meeting shareholding requirements for nominating shareholders." Other provisions ISS deems problematic, "especially when used in combination," include, but are not limited to, prohibitions on resubmissions of failed nominees in subsequent years, restrictions on the use of proxy access and proxy contest procedures for the same meeting, and, at least in some circumstances, counting elected proxy access nominees toward the maximum number of proxy access nominees in subsequent years.

Companies That Had a Failed Proxy Access Shareholder Proposal and/or Adopted Proxy Access at Different Thresholds Than Those Requested in the Proposal

Issuers facing a shareholder proposal on proxy access after having received a failed proposal last year and/or after having implemented their own version of proxy access should again engage with their large institutional shareholders on the issue, as their views may have changed from last year. As with any other potential governance change, it is critical that issuers understand the views of their large

shareholders and take those views into account when deciding how to proceed with regard to proxy access.

Issuers Facing a Proxy Access Shareholder Proposal for the First Time

Because there is no consensus among major institutional investors on the issue of proxy access — and given the strong link observed in 2015 between a company’s shareholder base and its voting results on proxy access — it is critical that issuers grappling with a proxy access shareholder proposal for the first time analyze their shareholder base, study their large shareholders’ policies on proxy access and engage with those shareholders on the issue. Taking their shareholders’ views into account, these issuers should consider whether to oppose the proposal in their proxy statement, submit a dueling management proposal to shareholders with provisions they have determined are more appropriate for the company or voluntarily adopt proxy access.

To the extent a company is open to adopting a proxy access bylaw voluntarily, it should consider what thresholds it would be comfortable with and what “bells and whistles” it might want to include in the provision. Depending on the specifics of the bylaw it adopts and how they align with the provisions of the shareholder proposal, a company may be able to negotiate with the shareholder proponent for the proposal’s withdrawal or obtain no-action relief from the U.S. Securities and Exchange Commission for exclusion of the shareholder proposal.

Issuers That Have Not Yet Received a Proxy Access Shareholder Proposal

To the extent they have not already done so, those that have not yet received a shareholder proposal — whether from the comptroller’s office or from other proponents — should nonetheless consider educating their board of directors regarding the trends that have developed over the last proxy season, as well as the advantages and disadvantages of pursuing each potential option for responding to a proxy access shareholder proposal. These issuers should also consider evaluating their shareholder base and beginning to engage with their shareholders on proxy access. Furthermore, the issuers in this category may consider whether to voluntarily adopt a proxy access bylaw and, if so, what proxy access structure would be in the best interest of the company. By all indications, the “private ordering” of proxy access will likely continue, and spending time on these questions now will give issuers that are not currently under the pressure of a shareholder proposal an opportunity to be thoughtful and prepared for what the next proxy season may bring.

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[1] Press Release of New York City Comptroller Scott M. Stringer, “Comptroller Stringer, New York City Funds, Announce Expansion of Boardroom Accountability Project” (Jan. 11, 2016), available at <http://comptroller.nyc.gov/newsroom/comptroller-stringer-new-york-city-funds-announce-expansion-of-boardroom-accountability-project/>.

[2] Id. (emphasis added).

[3] See Institutional Shareholder Services Inc., “U.S. Proxy Voting Policies and Procedures (Excluding Compensation-Related): Frequently Asked Questions” (Dec. 18, 2015), available at <http://www.issgovernance.com/file/policy/us-policies-and-procedures-faq-dec-2015.pdf>.

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