

CLIENT ALERT

SEC Proposes Use of Universal Proxy Cards in Contested Director Elections

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On October 26, 2016 the Securities and Exchange Commission (the “SEC”) issued a release¹ proposing amendments to the federal proxy rules under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), to require the use of universal proxy ballots in contested director elections that include the names of both management and dissident nominees in a contested director election. The proposed amendments would make it easier for shareholders to vote for any combination of management and dissident nominees that they prefer and, as a result, may make it easier for dissidents to gain board seats as a result of proxy contests.

This client briefing summarizes the key terms of the proposed universal proxy amendments. Comments on the proposed amendments will be due 60 days after publication in the federal register.

Background

Most public company shareholders vote by proxy. Currently, shareholders voting by proxy in a contested director election are effectively required to choose between management’s slate of directors and a slate of directors proposed by a dissident. In contrast, shareholders voting in person at a meeting may choose any combination of management and dissident director nominees.

This current regime is largely a result of the “bona fide nominee” rule, which is proposed to be amended, and the “short slate” rule, which is proposed to be eliminated.

- The current bona fide nominee rule² provides that director nominees may only be listed on a proxy card if such nominees have consented to be named in the proxy statement and to serve if elected. The effect of this rule is that one party cannot name the other party’s nominees on its proxy card without the other party’s consent. Typically, director nominees on the management slate will not consent to being named on the dissident’s proxy card for fear of the appearance that such nominees support the dissident’s position or its director nominees.
- The current short slate rule³ allows a dissident who is nominating a “short slate” (less than a full slate of directors) to “round out its slate” by soliciting proxy authority to vote for some management slate directors on the dissident’s proxy card and to name the management nominees that it will not vote for to fill out its slate. The short slate rule permits the dissident to select which, if any, of the management nominees to vote for using the

dissident's proxy card and, therefore, does not allow shareholders to freely pick and choose between management and dissident director nominees.

Because of the stark contrast between proxy voting and in-person voting in contested elections, the SEC has been considering mandating a universal ballot since its 1992 overhaul of the proxy rules. However, this is the first time that the SEC has proposed rules to allow a shareholder to vote for its own combination of dissident and management nominees on the same proxy card. If adopted, the proposed amendments would make it easier for shareholders to vote for the combination of management and dissident nominees they prefer and, as a result, may make it easier for dissidents to gain board seats in proxy contests. The most significant proposed changes are in the areas of bona fide nominees, the short slate rule, and universal proxies.

Proposed Rules

The table below sets forth a comparison of the current rules and the proposed amendments.

RULE	CURRENT	PROPOSED
Bona Fide Nominee Rule	Requires nominee to consent to being named on a specific proxy card in order to be included on that card ⁴	Allows any nominee who consents to being named on any proxy card to be included on any proxy card ⁵
Short Slate Rule	Allows dissident with less than a full slate to solicit proxy authority to vote for some management nominees in addition to its own nominees ⁶	Eliminated
Use of Universal Proxies	Not required	<p>Mandatory for each party in non-exempt solicitations in contested director elections⁷</p> <p>To use a universal proxy card, a dissident must solicit holders of at least a majority of the outstanding shares entitled to vote in the election of directors⁸</p>
Content Requirements	Each party provides information about its own nominees in its proxy statement, but may refer to other party's proxy statement to satisfy disclosure obligations about the other party's nominees ⁹	Parties must refer shareholders to other party's proxy statement for information about that party's nominees ¹⁰

RULE	CURRENT	PROPOSED
Notice Requirements	Any advance notice required under the company's governing documents	<p>Dissident must notify company of intent to solicit proxies in support of non-management nominees</p> <p>Company and dissident must notify each other of their nominees within a specific time frame¹¹</p>
Filing Deadline for Proxy Statement	No requirement for dissidents who elect full-set delivery in a contested election	Dissident proxy statement must be filed by a certain time ¹²

Bona Fide Nominee Rule

Under the new proposed bona fide nominee rule, the definition of “bona fide nominee” would be expanded to include a nominee who has consented to being named in any proxy statement relating to the company’s meeting of shareholders where directors are being elected. This would remove the restriction currently preventing dissidents from listing management slate nominees on their proxy card without such nominees’ permission and would allow the company or a dissident to include the other party’s nominees on its proxy card.

Short Slate Rule

The SEC is proposing to eliminate the short slate rule. The main purpose of the short slate rule was to mitigate the concern that dissidents proposing less than a full slate of nominees would not allow a shareholder to vote for a full slate of directors on its proxy card. When combined with the new proposed bona fide nominee rule and the introduction of universal proxies (discussed below), the need for the short slate rule would be eliminated under the proposed amendments.

Universal Proxies and Content

The SEC is proposing amendments to the proxy rules to mandate that each soliciting party in a contested election distribute a universal proxy that includes the names of all director nominees. Each card would indicate the party on behalf of whom the proxy is solicited, provide clear instructions about the shareholder’s ability to split votes between management and dissident nominees, and clearly distinguish between the management and dissident slates of nominees. A mandated universal proxy would allow a shareholder to vote for any combination of management and dissident director nominees and mirror the way shareholders can vote in person at a meeting.

In order to prevent a dissident from taking a free ride on the management proxy, a dissident would not be able to take advantage of a universal proxy card unless such dissident solicited the holders of at least a majority of the voting power of shares entitled to vote in the election of directors. Under this proposed “majority solicitation” rule, it is possible that some shareholders would not receive dissident proxy materials and information about dissident

directors. To address this concern, the proposed rule would add a requirement that each party direct shareholders to the other party's proxy materials for information about opposing candidates and inform shareholders that the other party's proxy statement is available for free on the SEC's website.

Notice Requirements

In order to provide a definitive date by which the parties to a contested election would know that the requirement for universal proxies had been triggered, the proposed rules would require a dissident to notify a company of its intent to solicit proxies in support of non-management nominees no later than 60 days prior to an annual shareholders meeting. This deadline is likely to be shorter than the advance notice period provided by a company's governing documents. The proposed rules would also require a company to notify a dissident of the names of its nominees no later than 50 days before the annual shareholders meeting.

Filing Deadline

Under the proposed rules, a dissident in a contested election would be required to file its definitive proxy statement by the later of 25 days before the annual shareholder meeting date or five days after the company files its definitive proxy statement. The proposed deadline would give shareholders access to information about all nominees in advance of making proxy decisions.

Applicability

The proposed amendments would apply in all non-exempt solicitations in connection with contested elections of directors, other than those involving investment companies registered under Section 8 of the Investment Company Act, and business development companies as defined in Section 2(a)(48) of the Investment Company Act.

Next Steps

A number of constituencies are expected to weigh in on the proposed rules. In addition to comments from public companies, activist investors, and shareholder watchdog groups, new SEC commissioners who are appointed by the next administration beginning in 2017 are likely to have their own views of the propriety of the proposed rules. In any case, even if they are adopted, the proposed rules would not be in effect for the 2017 proxy season.

¹ Universal Proxy, Release No. 34-79164 (Oct. 26, 2016). For a copy of the release, see <https://www.sec.gov/rules/proposed/2016/34-79164.pdf>.

² Exchange Act Rule 14a-4(d)(1).

³ Exchange Act Rule 14a-4(d)(4).

⁴ Rule 14a-4.

⁵ Proposed Rule 14a-4.

⁶ Rule 14a-4(d)(4).

⁷ Proposed Rule 14a-19(e).

⁸ Proposed Rule 14a-19.

⁹ Schedule 14A and Rule 14a-5(c).

¹⁰ Proposed Item 7(h) of Schedule 14A.

¹¹ Proposed Rule 14a-19.

¹² Rule 14a-19(e).

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