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Chairman Atkins' bid to reframe shareholder proposals puts Delaware in the crosshairs

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SEC Chairman Paul Atkins' speech last week in Delaware sounded to many like a death knell for shareholder proposals under Rule 14a-8. In fact, it was far more strategic: the opening move to test whether Delaware corporate law even permits non-binding, or precatory, environmental and social proposals that have proliferated in recent proxy seasons.

A new legal theory, and a Delaware gambit

Chairman Atkins urged Delaware corporations to consider challenging E&S proposals on the ground that Delaware law does not permit shareholders to submit non-binding resolutions for a vote. The argument, originally advanced by a Delaware practitioner, posits that Delaware law recognizes only binding shareholder actions, and precatory proposals are ultra vires and therefore improper, violating Rule 14a-8(i)(1).

The Chairman suggested that companies could exclude these proposals by submitting no-action letters supported by a legal opinion from Delaware counsel. If the proponent were to submit a contrary opinion, the resulting conflict would create a case or controversy that the SEC could certify to the Delaware Supreme Court for resolution.

This is a novel and uncertain path. The Delaware Supreme Court is not obligated to take a certified question from the SEC, and it has never been asked to opine on whether Rule 14a-8 proposals are compatible with Delaware corporate law. But a well-framed test case could open the door to state law limits on a federal disclosure mechanism— a significant recalibration of the balance between the SEC and Delaware in corporate governance

The broader context: Corporate proxy statements as political battleground

To understand why this approach resonates is to recognize how Rule 14a-8 has evolved. Originally intended to facilitate limited shareholder communications through proxy statements, E&S proposals today, representing all sides of the political spectrum, often ask companies to adopt or abandon specific and fundamental business practices, disclose detailed metrics, or commit to policies far beyond the concerns of most shareholders. To many companies and their boards, it appears there are few issues that are too minor and requests too prescriptive that would be prohibited by the rules, and with little regard to the costs of implementation.

Many of these proposals are advanced by professional advocates who represent beneficial owners the company never meets, empowering a growing cottage industry that thrives on the access to corporate proxy statements that Rule 14a-8 provides as leverage to effectuate their agenda.

Even as support for such proposals as evidenced by shareholder votes has declined in recent years, companies still expend substantial time and resources addressing them. Some institutional investors continue to expect engagement with every proponent, no matter how tenuous the proposal's connection to shareholder value or the futility of the conversation.

The SEC’s staff’s dilemma in determining no-action requests

The SEC staff remains the gatekeeper for excluding proposals that fail Rule 14a-8’s procedural or substantive requirements, committing significant resources every season to reviewing the no-action requests. But decades of evolving precedent, including decisions made by the last SEC administration that included the continued expansion of social policy exceptions to the ordinary business argument, have made application difficult. Chairman Atkins’ roadmap to involve Delaware attempts to shift interpretive authority away from the SEC.

Open questions and implications

The outcome of the question before the Delaware Supreme Court, assuming the court would even entertain the case, remains to be seen. If there are no competing legal opinions, the SEC staff would need to evaluate the merits of the company’s legal opinion and make a decision on that basis. Similar challenges could arise from corporations not incorporated in Delaware, in states that do not provide the right to certify the case to the courts.

The bottom line

Chairman Atkins’ remarks outline a potential realignment of authority over shareholder access to proxy statements as a forum to debate E&S issues – from the SEC’s interpretive discretion to the Delaware courts’ corporate law jurisdiction. For companies and their boards, the possibility of any change that would stem the annual wave of E&S proposals is appealing.

Beyond the state law scheme, the Chairman also made clear that the SEC is reevaluating Rule 14a-8 for potentially significant reform, rather than the piecemeal efforts that have taken place in past administrations that have both failed to meaningfully change the system and been subject to pendulum swings.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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