

Financial CHOICE Act Imposes Sweeping Shareholder Proposal Reforms

April 25, 2017 | Client Update | 3-minute read

The modified version of the legislation, CHOICE Act 2.0, released by House Financial Services Committee Chairman Jeb Hensarling (R-TX), is mostly known for proposing major financial regulatory reforms. Tucked into the lengthy bill, however, are several significant changes that would completely overhaul the shareholder proposal process. Some are similar to proposals by the Business Roundtable, which we previously discussed [here](#).

Ownership Threshold. Currently, Rule 14a-8 allows any shareholder who owns at least \$2,000, or 1%, of a company's stock to offer a proposal for inclusion in the company's proxy statement for the annual meeting. The CHOICE Act changes that ownership and holding requirement to permit submission of proposals by only a shareholder owning 1% of the company's securities entitled to vote on the proposal, or such greater percentage as determined by the SEC, so long as the shareholder has held the stock for a minimum of three years. This change eliminates the dollar threshold entirely.

Since 1% of a large-cap company could be billions of dollars of stock ownership, the amendment would render ineligible almost all of the shareholder proponents who submit proposals today, particularly several prolific retail shareholders, but even some of the major pension funds and social activists.

Resubmission Threshold. The CHOICE Act revives a 1997 SEC rule proposal, never adopted, for when shareholders may resubmit a similar proposal in the following year after it was voted on in a proxy statement. The statute excludes proposals that, in the past five years, received less than 6% of favorable support once, 15% if proposed twice and 30% if proposed three times. The current rule allows resubmission if a proposal received more than 3%, 6% and 10%, respectively, which means a proposal that receives more than 10% can be sent to a company indefinitely.

The statute is silent on the length of time that a proposal can be excluded on this basis, but the current rule would exclude a proposal without the requisite vote thresholds for any meeting held within the last three years of the last time the proposal was in the proxy statement. This change would permit more social-based proposals to be excluded.

Proposal by Proxy. Companies have complained for years that only a shareholder who actually owns stock should be allowed to submit proposals, rather than a proponent who acts as a designee for one proposal while submitting another one on his or her own behalf, or entities that have sprung up largely to develop and advocate for proposals without owning any company shares. Various no-action letters arguing that forms of "proposal by proxy" should be banned have failed to convince the SEC staff.

The CHOICE Act prevents these practices, and states that companies can block a proposal submitted by a person in that person's capacity as a "proxy, representative, agent, or person otherwise acting on behalf of a shareholder."

A hearing is scheduled for tomorrow, and a markup of the bill is expected next month.

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.

Ning Chiu

+1 212 450 4908

ning.chiu@davispolk.com

This communication, which we believe may be of interest to our clients and friends of the firm, is for general information only. It is not a full analysis of the matters presented and should not be relied upon as legal advice. This may be considered attorney advertising in some jurisdictions. Please refer to the firm's privacy notice for further details.