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SEC issues new guidance on shareholder proposals

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The SEC signaled increased unwillingness to allow companies to exclude shareholder proposals from proxy statements.

On November 3, the SEC issued Staff Legal Bulletin (SLB) No. 14L setting forth new guidance on shareholder proposals includable in proxy statements. The bulletin rescinds much of the guidance that the SEC published in the last few years affording more leeway to companies seeking to exclude shareholder proposals that seek to micromanage or are of scant relevance to the company's business.

"Ordinary business" grounds for proposal exclusion

A frequently used grounds to justify excluding a shareholder proposal from a company's proxy statement permits the company to omit a proposal that deals with "a matter relating to the company's ordinary business operations," although longstanding SEC practice makes this justification unavailable when the proposal relates to something the SEC staff believes involves a "significant social policy."

Significant social policy

Under guidance announced in 2017 but rescinded this week, the staff suggested a company-specific approach that would consider whether the social policy issue raised by a proposal was significant to the company seeking to exclude it from the proxy statement. Under the new guidance, the staff will focus instead on the "broad[er] societal impact" of the issue, rather than evaluating the company's argument about the insignificance of the issue to its business. As an example, the new guidance notes that proposals raising human capital management issues with a broad societal impact would not be excludable solely because the proponent did not demonstrate that the issue was significant to the company, and regardless of whether the company's board considers the issue significant to the company.

The new guidance does not specify how the staff will determine which social policy issues have a broad societal impact, and leaves open the possibility that the staff may find other issues that fall into this category. Recently, the staff took the view that shareholder proposals on virtual shareholder meetings, previously considered ordinary business, fit within the social policy exception and must proceed to vote.

Micromanagement

In guidance announced in 2018 and 2019 and now rescinded, the staff was of the view that proposals impermissibly sought to "micromanage" the company, and were therefore excludable, when they sought intricate details or would impose a specific method or timeline for implementing a directive. The new guidance states that the staff will instead take a "measured approach" and focus on the level of detail sought in the proposal and whether it "inappropriately" limits the board's or management's discretion. The new guidance cites a recent example of a proposal that would direct the company to set emission reduction targets covering greenhouse gas emissions of its operations and products, but would

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not impose a specific method for doing so, as being non-excludable. Going forward, a proposal would need to be highly restrictive, such as a recent proposal asking a company to terminate its operations in a specific jurisdiction, to be deemed excludable on the basis of micromanagement. Presumably the staff will use future no-action letter requests to flesh out its views on when it is appropriate, as a matter of federal law, for shareholders to limit the discretion of management and the board.

“Economic relevance” grounds for proposal exclusion

Under the “economic relevance” argument for excluding a shareholder proposal from the proxy statement, a company may exclude a proposal that relates to less than 5% of its total assets, net earnings and gross sales, if the proposal is not otherwise significantly related to the company’s business. The new guidance eliminates the 2018 staff position that an analysis by the company’s board of directors can be used to demonstrate that a proposal is insignificant, and returns to disallowing exclusion where a proposal raises issues of broad social or ethical concern related to the company’s business.

Proof of ownership and repeated deficiency notices

Although the new guidance updates the suggested format by which a shareholder may demonstrate required levels of stock ownership in order to submit a proposal (“As of [date the proposal is submitted], [name of shareholder] held, and has held continuously for at least [one year] [two years] [three years], [number of securities] shares of [company name] [class of securities]”), the guidance makes clear that companies may not use a shareholder’s failure to use this format to prove stock ownership as a basis for excluding the proposal.

The new guidance also states that even where a company has previously sent the shareholder a deficiency notice, it should notify the shareholder of any specific defects in a subsequently provided proof of ownership, and afford the shareholder an opportunity to remedy the defect. The staff accordingly may expect companies to send more than one notice of deficiency, depending on the circumstances.

Use of email

Nodding to the common use of email in correspondence between shareholder proponents and companies, the new guidance suggests that the sender seek a reply email from the recipient to prove delivery of an email and encourages both companies and shareholders to acknowledge receipt of emails when requested. Electronic read-receipts may also help establish that emails were delivered.

When a company does not provide an email address in the proxy statement, the staff encourages shareholder proponents to contact the company to obtain the correct email address for submitting proposals and encourages companies to provide it upon request. If a company uses email to deliver a deficiency notice, the staff encourages the company to seek confirmation of receipt from the proponent and notes that the company has the burden to prove timely delivery of the notice. If a shareholder uses email to respond to a company’s deficiency notice, the burden is on the shareholder to use an appropriate email address (e.g., an email address provided by the company, or the email address of the counsel who sent the deficiency notice), and the shareholder should seek confirmation of receipt.

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In a statement commenting on the new guidance, Commissioners Peirce and Roisman called the focus on human capital management and climate issues “disappointing,” though perhaps “not altogether surprising given current SEC priorities.” The new guidance marks a meaningful shift from the approach taken in the last few years expanding lines of argument a company may use to attempt to exclude proposals—even if in practice such arguments were not often successful. Federal courts have in the past taken a skeptical view of an agency’s decision to revise prior legal interpretations in the absence of significant changed circumstances or new legislation, and it remains to be seen whether companies seeking to exclude proposals with little relevance to their business or that plainly relate to ordinary business operations may be willing to challenge adverse SEC determinations in court—or bypass the voluntary SEC staff review process entirely and seek judicial confirmation of a decision to omit a proposal.

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