

Challenging the Legality of the Harvard Shareholder Rights Projects' Declassification Shareholder Proposals

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Professor Joseph Grundfest of Stanford Law School and SEC Commissioner Daniel Gallagher have co-authored an [academic paper](#) with the provocative title "Did Harvard Violate Federal Securities Law? The Campaign Against Classified Boards of Directors." The paper pointedly criticizes the work of the Harvard Shareholder Rights Project, which assists several pension funds and other investors in submitting shareholder proposals to declassify boards of directors.

These proposals are the most frequent governance topic and they are often cited as the primary reason that the number of S&P 500 companies with classified boards have declined 80% since 2000, from 300 to 60 in 2013. The Harvard Project claims responsibility for the overwhelming majority of S&P 500 declassifications since it started the program in 2010.

The crux of the paper is to question whether Harvard violated federal securities laws by the way it uses and cites empirical academic research in the proposal to support their claim that classified boards contribute to lower corporate financial performance. According to the paper, the characterization of the overall empirical evidence, and thereby the proposal, is false and misleading in violation of the federal proxy rules. The authors contend that by at least January 2014, the description of the research available fails to include more recent studies that declassification is harmful to shareholders, and that staggered boards actually improve financial performance, which directly contradicts the proposition advocated by the Harvard Project's proposal. Recent research also indicates that having staggered boards does not have the same effect across all companies.

The paper argues that the absence of studies with alternative viewpoints in the proposal is material because it could have caused a reasonable investor to change his vote, since the proposal frames the literature used for support as relating to lowering company valuations and decreasing the amount of gains to shareholders. In omitting a contradictory line of research in the proposal, the paper concludes that Harvard is exposed to liability in SEC enforcement proceedings or in private actions, since the Harvard Project is listed among the school's clinical and pro bono programs and those running the project are employed by the university.

The SEC could decide that the Harvard Project was negligent in failing to include a description of the contrasting academic findings in the proposal, as the "maker" of the defective statement, and that Harvard, as a university, could be held liable for those activities. While proving causation would be more challenging in a private action, given the precatory nature of Rule 14a-8 proposals, the paper determines that it can be established that the omission of the contradictory studies had a significant propensity to affect the voting process, as the authors quote the Harvard Project's own words that its work "resulted" in or "produced" destaggered boards.

The paper is also critical of other parties involved in the process. First, the SEC staff, for the view that appears to be taken by the staff that rather than try to judge whether the text in shareholder proposals are accurate, companies should address any potential concerns regarding misrepresentations in their own opposition statements. Also, the proxy advisory firms are faulted for ignoring the research and maintaining a categorical opposition to classified boards.

Finally, the authors state that they are not taking a position as to the merits of the ongoing debate regarding board classification, but instead believe that the current version of the proposal is false and misleading sufficient for the SEC to grant no-action letters or courts to allow declaratory relief to exclude the proposal, or even in an extreme case, to void the declassification that was initiated by the proposal.

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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