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In New Legal Bulletin, SEC Staff Clarifies Last Season's Shareholder Proposal Controversies

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The SEC Division of Corporation Finance has issued a new **Staff Legal Bulletin 14J** to provide guidance on some of the issues that bedeviled us earlier this year as to when the staff would, or would not, permit companies to exclude proposals through the no-action letter process.

Discussion of Board's Analysis in No-Action Letters. Last November, the Division **issued SLB 14I**, which indicated that companies could include, in their no-action letter requests arguing the "economic relevance" exception under Rule 14a-8(i)(5) and the "ordinary business" exception under Rule 14a-8 (i)(7), a discussion reflecting the board's analysis of the particular policy issue raised by the proposal and its significance in relation to the company. Multiple companies put their boards through the exercise of analyzing the proposals and explained the boards' findings in their exclusion requests, but the staff agreed in only one instance, which we previously **described here**. Moreover, some of the decisions issued by the staff raised different perceived shortcomings that were at times difficult to understand, as we **highlighted here**.

The Division continues to encourage companies to include their boards' analysis in their arguments, but the letters should include a list of substantive factors such as:

- The extent to which the proposal relates to the company's core business activities.
- Quantitative data, including financial statement impact, related to the matter that illustrate whether or not a matter is significant to the company.
- Whether the company has already addressed the issue in some manner, including the differences – or the delta – between the proposal's specific request and the actions the company has already taken, and an analysis of whether the delta presents a significant policy issue for the company.
- The extent of shareholder engagement on the issue and the level of shareholder interest expressed through that engagement.
- Whether anyone other than the proponent has requested the type of action or information sought by the proposal.
- Whether the company's shareholders have previously voted on the matter and the board's views as to the related voting results.

Past voting results on a proposal was a sticking point last season, and SLB 14J makes clear now that the "weight" given to those results will depend on the level of support. If a proposal previously received "significant" or "insignificant" support, the staff will consider whether the company has taken any subsequent actions and/or whether other intervening events have occurred since the vote that "may have mitigated the issue's significance to the company."

SLB 14J does not define or otherwise expand on what support levels would be viewed as "significant" for this purpose. More importantly, the staff will consider the length of time that has passed since a matter was last voted on, and the more recent the vote is, the more likely that "such a vote is indicative of the topic's significance." Perhaps that explains some of the staff's decisions last season where they denied exclusion on lobbying proposals that had in the prior year received above 30% in support.

While the above list of factors are suggestions, and are not intended to be "exclusive or exhaustive," it would likely be prudent for companies to at least consider if the discussion should reflect all of them. Some important additional points from the SLB 14H:

- A board's analysis is not required and will not create a "presumption against exclusion." However, the Division stated that the staff may "find it difficult" in some instances to agree with companies in cases where the significance of a particular issue may "depend on factors that are not self-evident." The staff cites a **no-action letter** issued last season about a proposal that asks for a report on a car company's fleet GHG emissions. The company had argued that rather than being about the social policy issue of climate change, the proposal as a whole (including the supporting statement) actually focused on the types of products being sold. In its denial, the staff pointed to the lack of board analysis.
- As indicated in the prior SLB 14I, the staff will not agree to exclude proposals that focus on substantive governance matters on this basis because they are viewed to be significant to companies.
- The staff will also consider the proponent's analysis of the issue. The proponents last season in almost all cases wrote lengthy response letters to the companies' no-action arguments using their boards' analysis.

Ordinary Business Micromanagement Argument. To the ire of proponents and resulting in some fairly negative press, the staff decided last season that certain proposals were excludable as ordinary business matters because they micromanaged the company. SLB 14J explains that the policy underlying the ordinary business exception rests on both the proposal's subject matter and whether it micromanages a company. A proposal may be excludable under micromanagement, even with a proper subject matter, if it "probe[s] too deeply into matters of a complex nature" when it involves "intricate detail, or seeks to impose specific time-frames or methods for implementing complex policies."

The examples from last season noted in the SLB 14J included proposals seeking a plan or a report to reach net-zero greenhouse gas emissions by 2030, which imposed a specific time-frame or method.

Ordinary Business Proposals that Address Senior Executive or Director Compensation

Proposals that relate to the management of the workforce and general employee compensation and benefits are excludable as ordinary business matters, while those focused on senior executive and/or director compensation are viewed as significant policy matters and not excludable. SLB 14J provides the following guidance on different permutations of these types of proposals where there is crossover:

- *Proposals that address both executive or director compensation and also ordinary business matters*. The staff examines whether the underlying concern of the proposal is truly focused on aspects of executive or director compensation, to ensure that a proposal is not included in the proxy statement simply because it addresses a matter that merely touches upon or implicates executive or director compensation.
- *Proposals that address aspects of executive or director compensation that are also available to the general workforce*. The staff examines whether a primary aspect of the targeted compensation is broadly available or applicable to a company's general workforce and the company demonstrates that the executives' or directors' eligibility to receive the compensation does not implicate significant compensation matters. If the proposal addresses element of compensation generally available to the workforce, then it is likely excludable.
- *Proposals that micromanage executive or director compensation*. In a change from prior practice, the Division may now agree that proposals addressing executive or director compensation could be excluded on the basis of micromanagement.

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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