Council of Institutional Investors®
The voice of corporate governance

FAQ: Why CII Supports the SEC's Universal Proxy Proposal

What problem is the SEC trying to solve and how?
Under current rules, when there is a contested election for board seats, shareholders who do not attend the shareholder meeting to vote in person—the vast majority of institutional and retail investors—generally must vote using proxy cards that do not list all board nominees. They vote using management's proxy card or the dissident group's proxy card, and neither card lists all nominees. Typically, each card presents a specific slate of preferred nominees.

Shareholders can choose any combination of nominees if they vote in person at the meeting. For many retail investors and institutional investors, however, attending shareholder meetings is prohibitively costly and time-consuming.

The SEC proposes to require that each party's proxy card list all board nominees, giving shareholders the ability to use either card to choose from both slates to vote for the nominees they believe best serve their interests.

Proxy contests are rare. Why is correcting this problem so important?
The right of shareholders to elect directors to represent them is a fundamental right of share ownership. That right is especially critical when there is a proxy contest. Contested elections are pivotal events for companies and for shareholders, since board seats, and in some cases, board control, are at stake. The dissident group usually advances a specific strategic, operational or financial agenda, so it is important for shareholders to be able to participate fully, regardless of how they vote. The SEC proposal aims to correct the glaring disparity between voting by proxy and voting in person.

Why should both sides provide a complete list of nominees? Why can't universal proxy cards be optional?
Each party to a proxy contest currently has the authority to circulate a card with a full list of board nominees—but only with permission from the opposing party. In practice, on the few occasions when one side has requested permission to list all nominees on its card, the other side has declined, fearing that to acquiesce would be a strategic disadvantage. Sometimes the declining party has been management; at other times the dissident group has declined.

Simply repealing the requirement to obtain permission to list opposing nominees would likely result in gamesmanship. For example, parties could potentially list some but not all board candidates on their cards in an attempt to steer voting.

Mandatory universal proxy cards for all contested elections would guarantee that shareholders are able to choose from among all board nominees, regardless of whether they vote in person or by proxy.

Will universal proxy cards spur more proxy contests?
No. A 2016 Harvard study concluded that universal proxy cards are "unlikely" to lead to more proxy contests.

The SEC proposal does not eliminate the substantial cost and risk associated with waging a dissident campaign. Legal, administrative and solicitation expenses required for a dissident to wage a proxy contest can run to six or seven figures. Furthermore, the SEC proposal requires dissidents to solicit shareholders representing at least a majority of outstanding votes.

Will universal proxy cards empower special interests?
No. The SEC proposal does not change the plurality vote requirement for contested elections for almost all companies. A plurality requirement provides that nominees receiving the most votes are elected until all board seats are filled. No nominee will win unless he or she obtains more votes than at least one nominee put forward by the opposing side. Ultimately, the outcome of the election answers the question of which nominees are truly "special interest" and which nominees are most aligned with the company's owners.

Will universal proxy cards harm retail investors?
No. Universal proxy cards would let retail investors choose among all board nominees without attending the shareholder meeting, which can involve travel and other costs that may be prohibitive.

Moreover, the current system of competing slates of nominees may be disproportionately confusing to retail investors, who are presented with multiple conflicting proxy cards and may not realize that tabulators count only the most recently submitted card.

Retail investors are already familiar with how to select nominees among a complete list of candidates; they do so in every general election in which they vote.

Which side benefits from universal proxies?
The Harvard study referenced above found that universal proxy cards in general favor neither management nor dissidents. Perceptions vary about which side benefits more, and those perceptions depend on contest-specific circumstances. Companies and dissidents have been on both sides of this issue. Tessera Technologies sought universal cards in its 2013 contest with dissident Starboard Value, as did Shutterfly in its 2015 proxy fight with Marathon Partners, but the companies were rebuffed. When dissidents sought universal proxy cards at Target in 2009 (Pershing Square) and DuPont in 2015 (Trian Fund Management), the companies declined. Parties in contests rarely request universal proxy cards because they assume the other side will refuse. The only clear "winner" from universal proxy cards is the investor.

Glossary

Proxy card: A federally regulated substitute for a corporate director election ballot. Shareholders use a proxy card to cast their vote when they are unable to attend the shareholder meeting in person to mark their ballot. State law governs ballots.

Proxy contest: Occurs when two opposing parties circulate their own, separate proxy cards for the same shareholder meeting. The incumbent side, often referred to as "management," circulates one version of the proxy card, and a group of shareholders, often referred to as the "dissident" or "dissident group," circulates an alternative card.

To ensure order and transparency, a dissident group must fulfill certain advance notice and public filing requirements to wage a proxy contest. Management and the dissident group often negotiate prior to the shareholder meeting. Settlements that result in some dissident nominees obtaining board seats are often reached before the meeting takes place.

Not all proxy fights involve contested elections. A dissident group may propose other reforms, such as changes to the company's bylaws, through a proxy fight.

Contested election: Occurs when a dissident group has nominated at least one board candidate, resulting in more nominees than available board seats. Generally a contested election involves a proxy contest, but not always. For example, when a shareholder nominates board candidates through a "proxy access" mechanism, there is no proxy contest *per se* because management's card, listing the company's nominees and the proxy access nominee(s), is the only card that shareholders receive.

In a contested election, management generally supports retaining all incumbent board members, and the dissident typically supports a combination of incumbent directors and alternative nominees recruited by the dissident. Each of these alternative candidates must agree in advance to serving on the board if elected. Most often the dissident's nominees constitute less than a majority of the total board seats, meaning there is no possibility of a change-in-control of the company.

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