Proposed Amendments to the Model Business Corporation Act to Adopt Mandatory Majority Voting for Public Companies

Adopting a mandatory rule for board elections in public companies from plurality voting to majority voting would require the following changes to the Model Business Corporation Act (“MBCA”):

§ 7.28. VOTING FOR DIRECTORS; CUMULATIVE VOTING

(a) Unless the articles of incorporation require a greater number of affirmative votes, in a meeting at which a quorum is present, otherwise provided in the articles of incorporation, directors are elected by the affirmative vote of a majority of the votes of the shares represented at the meeting and a plurality of the votes cast by the shares entitled to vote in the election, unless: at a meeting at which a quorum is present.

(1) fewer than the minimum number of directors, as defined in the company’s articles of incorporation or bylaws, is thereby elected, in which case those directors receiving a plurality of the votes cast by the shares entitled to vote, but not a majority, are elected for a holdover period of 90 days (the “holdover directors”), during which time all the directors having received a majority of affirmative votes, and thus duly elected shall fill the seats of the holdover directors according to the provisions of section 8.10. If no directors receive a majority of the votes cast by the shares entitled to vote, then those directors receiving a plurality of the votes cast by the shares entitled to vote are elected for a period of 180 days; or

(2) one or more board seats is contested, in which case directors are elected by a plurality of the votes cast by the shares entitled to vote; or

(3) the corporation allows cumulative voting; or

(4) the corporation is a closely held company that has elected to be governed by section 7.32 et seq.

(b) Shareholders do not have a right to cumulate their votes for directors unless the articles of incorporation so provide.

(c) A statement included in the articles of incorporation that “[all] [a designated voting group of]” shareholders are entitled to cumulate their votes for directors” (or words of similar import) means that the shareholders designated are entitled to multiply the number of votes they are entitled to cast by the number of directors for whom they are to vote and
cast the product for a single candidate or distribute the product among two or more candidates.

(d) Shares otherwise entitled to vote cumulatively may not be voted cumulatively at a particular meeting unless:

(1) the meeting notice or proxy statement accompanying the notice states conspicuously that cumulative voting is authorized; or

(2) a shareholder who has the right to cumulate votes gives notice to the corporation not less than 48 hours before the time set for the meeting of the shareholder’s intent to cumulate votes during the meeting, and if one shareholder gives this notice, all other shareholders in the same voting group participating in the election are entitled to cumulate their votes without giving further notice.

Commentary:

The purpose of this language is to change the standard for director elections from plurality voting to majority voting, and making the majority voting standard mandatory for public companies, while recognizing exceptions for failed elections, contested elections, and cumulative voting. The core language of § 7.28(a) implementing majority voting is taken from the Illinois Business Corporation Act, 805 ILCS § 7.60 (2012), which has had a majority voting default rule for directors since 1983. Here we suggest a mandatory majority voting rule for public companies. Under this majority voting regime, if a director fails to receive the affirmative vote of more shares in favor of that director’s continuing service than opposed, the director is not elected. A corporation’s organizing documents would provide the procedures for appointing a new director (or directors) to fill the vacancies created, which typically would be for the remaining directors to fill the vacancy, consistent with the provisions of § 8.10.

The statutory approach suggested for § 7.28(a) has two salutary effects. First, it provides a mechanism to effectuate a robust signal of shareowners’ views, one with legal effect, thus promoting board accountability. Second, the power to fill a board vacancy that is created remains with the board, which serves to promote a balance between board power, as identified in § 8.01(b), and board accountability as in the revised § 7.28(a).

Exception 7.28(a)(1) seeks to balance the interests of board accountability represented by the majority voting rule with the need for continuity on the board in the unlikely event that multiple board members fail to garner majority support, resulting in a board with fewer members than required by the corporation’s organizing documents. In that circumstance, which we assume and would hope would be extremely rare, § 7.28(a)(1) permits the board to be constituted by a plurality of the votes cast by the shares entitled to vote for a holdover period of 90 days, during which time the directors who had received a majority of affirmative votes would fill the number of seats necessary to create a full board using the procedures of § 8.10. A 90-day holdover period, while likely longer than necessary to fill the vacancies,
provides for continuity on the board, and adequate time for the board to reflect on why there
had been a failed election, and what characteristics of appointed directors might best
address concerns shareowners had demonstrated through their voting and related
communications. Thus, it advances the policy goal of these proposals, which is to better
balance board power with accountability to the shareowners.

In the extremely unlikely circumstance that an entire board fails to receive a majority of
affirmative votes, § 7.28(a)(1) permits the entire board to be constituted by a plurality of the
votes cast for a holdover period of 180 days, during which time the concerns of shareowners
can be canvassed and understood and a revised slate of directors prepared for proxy voting.

We understand that the potential for failed elections is a concern that has been
expressed about a majority voting rule. We submit that § 7.28(a)(1), in conjunction with the
general parameters of §§ 7.28(a) and 8.10, should allay those concerns.

Exception 7.28(a)(2) continues the plurality voting default rule for contested elections.
Proponents of majority voting recognize that plurality voting is appropriate for contested
elections.

Exception 7.28(a)(3) recognizes that a cumulative voting regime is inconsistent with a
majority voting regime, and so establishes an exception to the default majority voting rule in
those circumstances.

Exception 7.28(a)(4) carves out closely held companies from the mandatory requirement
for a majority voting rule for the election of directors, recognizing that the MBCA permits
tailoring of governance arrangements with respect to closely-held companies in ways that
would not be permitted with respect to publicly-held companies. Many governance
arrangements permitted in closely-held corporations, such as eliminating the board of
directors, entering into irrevocable voting trusts or binding shareowner agreements with
respect to the exercise of board power, are not permitted in publicly-held corporations given
the different considerations applicable to the two different situations.

§8.05. TERMS OF DIRECTORS GENERALLY

(a) The terms of the initial directors of a corporation expire at the first shareholders’ meeting
at which directors are elected.

(b) The terms of all other directors expire at the next, or if their terms are staggered in
accordance with section 8.06, at the applicable second or third, annual shareholders’
meeting following their election, except to the extent (i) provided in section 10.22 if a
bylaw electing to be governed by that section is in effect or (ii) a shorter term is specified
in the articles of incorporation in the event of a director nominee failing to receive a
specified vote for election.

(c) A decrease in the number of directors does not shorten an incumbent director’s term.
(d) The term of a director elected to fill a vacancy expires at the next shareholders’ meeting at which directors are elected.

(e) Except to the extent otherwise provided in the articles of incorporation or under section 10.22 if a bylaw electing to be governed by that section is in effect, despite the expiration of a director’s term, the director continues to serve until the director’s successor is elected and qualified or there is a decrease in the number of directors.

§ 8.10. VACANCY ON BOARD

(a) Unless the articles of incorporation provide otherwise, if a vacancy occurs on a board of directors, including a vacancy resulting from an increase in the number of directors:

(1) the shareholders may fill the vacancy;

(2) the board of directors may fill the vacancy; or

(3) if the directors remaining in office constitute fewer than a quorum of the board, they may fill the vacancy by the affirmative vote of a majority of all the directors remaining in office, or by a sole remaining director (other than holdover directors as defined in section 7.28(a)(1)).

(b) If the vacant office was held by a director elected by a voting group of shareholders, only the holders of shares of that voting group are entitled to vote to fill the vacancy if it is filled by the shareholders, and only the directors elected by that voting group are entitled to fill the vacancy if it is filled by the directors. If no directors elected by a specific voting group are elected with a majority of the votes cast by the shares entitled to vote, the directors are then elected by plurality vote.

(c) A vacancy that will occur at a specific later date (by reason of a resignation effective at a later date under section 8.07(b) or otherwise) may be filled before the vacancy occurs but the new director may not take office until the vacancy occurs.

(d) If a vacancy has been created by a director having failed to receive the affirmative vote of a majority of shares voting in an election, those directors having not received a majority of affirmative votes may not be reappointed to fill the vacant seats.

(e) Directors appointed to fill a vacancy on a classified board that has been created by a director’s failure to receive a majority affirmative vote would need to be affirmatively approved by a majority of the shareholders eligible to vote at the next annual shareholder meeting, and such director’s term on the board would expire at the same time as the class into which that director has been appointed.
Commentary:

Section 8.10 of the MBCA contains a number of procedures for filling vacancies on a board of directors. Section 8.10(a)(3), as currently enacted, recognizes that vacancies on the board of directors can be filled by fewer than a quorum of directors, which procedure should allay general concerns about majority voting and the potential for failed elections.

Amendments suggested here in § 8.10(d) would establish that those directors in any election who failed to receive the affirmative vote of a majority of shares voting are not eligible to be reappointed to the vacancies on the board so created. Moreover, the amendment to § 8.10(a)(3) suggested here, construed in conjunction with changes suggested to § 7.28(a)(1), would provide that in the event of an election where fewer directors than the minimum defined in the company’s organizing documents received a majority affirmative vote, those directors who had received a majority affirmative vote would appoint the directors to fill the number of seats left vacant and necessary to constitute a full board within 90 days. This provision is consistent with § 8.10 as currently enacted, which permits vacancies on the board to be filled by fewer directors than constitutes a quorum. The amendment suggested here also provides for a sole remaining director to fill the seats left vacant, as is permitted under current Delaware law, at Delaware General Corporate Law § 223(a)(1). In the extremely unlikely circumstance that an entire board fails to receive a majority of affirmative votes, the amendment to § 8.10(b), construed in conjunction with changes suggested to § 7.28(a)(1), permits the entire board to be constituted by a plurality of the votes cast for a holdover period of 180 days, during which time the concerns of shareowners can be canvassed and understood and a revised slate of directors prepared for proxy voting.

Section 8.10(e), proposed to be added to this section, contains specific provisions for filling vacancies on a classified board. This proposed amendment establishes that directors appointed to fill a vacancy on a classified board that has been created by a failure to receive a majority affirmative vote would need to be affirmatively approved by a majority of the shareowners eligible to vote at the next annual shareowner meeting, and provides that their term on the board would be reduced by the one year already served. Classified boards present special accountability problems, and thus appointment for a full term without subsequent shareowner approval would undermine the accountability to shareowners that these provisions seek to advance.
§10.22. BYLAW PROVISIONS RELATING TO THE ELECTION OF DIRECTORS

(a) Unless the articles of incorporation (i) specifically prohibit the adoption of a bylaw pursuant to this section, (ii) alter the vote specified in section 7.28(a), or (iii) provide for cumulative voting, a public corporation may elect in its bylaws to be governed in the election of directors as follows:

(1) each vote entitled to be cast may be voted for or against up to that number of candidates that is equal to the number of directors to be elected, or a shareholder may indicate an abstention, but without cumulating the votes;

(2) to be elected, a nominee must have received a plurality of the votes cast by holders of shares entitled to vote in the election at a meeting at which a quorum is present, provided that a nominee who is elected but receives more votes against than for election shall serve as a director for a term that shall terminate on the date that is the earlier of (i) 90 days from the date on which the voting results are determined pursuant to section 7.29(b)(5) or (ii) the date on which an individual is selected by the board of directors to fill the office held by such director, which selection shall be deemed to constitute the filling of a vacancy by the board to which section 8.10 applies. Subject to clause (3) of this section, a nominee who is elected but receives more votes against than for election shall not serve as a director beyond the 90-day period referenced above; and

(3) the board of directors may select any qualified individual to fill the office held by a director who received more votes against than for election.

(b) Subsection (a) does not apply to an election of directors by a voting group if (i) at the expiration of the time fixed under a provision requiring advance notification of director candidates, or (ii) absent such a provision, at a time fixed by the board of directors which is not more than 14 days before notice is given of the meeting at which the election is to occur, there are more candidates for election by the voting group than the number of directors to be elected, one or more of whom are properly proposed by shareholders. An individual shall not be considered a candidate for purposes of this subsection if the board of directors determines before the notice of meeting is given that such individual’s candidacy does not create a bona fide election contest.

(c) A bylaw electing to be governed by this section may be repealed:

(1) if originally adopted by the shareholders, only by the shareholders, unless the bylaw otherwise provides

(2) if adopted by the board of directors, by the board of directors or the shareholders.
Commentary:

One of the advantages of changing the rule from plurality voting to majority voting is that § 10.22 can be deleted in its entirety. Section 10.22 clarified the power of a corporation to adopt a majority voting bylaw, subject to certain exceptions. If § 7.28 is revised as suggested, § 10.22 is no longer necessary.

The power to vary the majority voting rule, in the articles of incorporation or the bylaws, as set forth in § 10.22(a)(1), is no longer appropriate given the suggested revisions to § 7.28 to make majority voting mandatory in public companies. The exceptions to majority voting rules indicated in § 10.22 for cumulative voting and contested elections have been incorporated as exceptions into the majority voting rules proposed for § 7.28.

Section 10.22(a)(2) incorporates a 90-day holdover rule that proponents of majority voting consider unnecessary, given the “fail safe” provisions of § 7.28(a)(1), as proposed, to ensure that enough directors, as defined in the corporation’s organizing documents, have been elected to lawfully constitute the board, and given the power in the board under § 8.10 to fill vacancies. Section 10.22(a)(2) suggests, but does not require (given the reference to § 10.22(a)(3)), that any director who received more votes against than for should not be reappointed. Section 10.22(a)(2) would be unnecessary in a mandatory majority voting regime, since any director who received more votes against than for would not be duly elected (subject to the identified exceptions). Moreover, the implicit power in § 10.22(a)(3) to reappoint “failed” directors would be inconsistent with a true majority voting regime.

Section 10.22(c) is no longer necessary, since § 7.28 anticipates that any supermajority voting requirements for the election of directors must be stated in the articles of incorporation, not in the bylaws, and so protection of shareowner-initiated bylaw amendments is no longer relevant to director voting rules.