

Recent Developments in Proxy Access

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As the 2017 proxy season begins to unfold, proxy access continues to be a focus of shareholder proposals. Last year, companies that had already adopted mainstream proxy access bylaws, or that were planning to put mainstream proxy access bylaws up for a shareholder vote, were largely successful in being able to exclude shareholder proposals to adopt proxy access bylaws on the grounds that such proposals had already been “substantially implemented.” See our prior memos [here](#) and [here](#). This year, companies have received a wave of new shareholder proposals seeking to amend their existing proxy access bylaws. See our prior memo [here](#). Until recently, the SEC staff had generally denied requests to exclude such proposals. In two recent no-action letters, however, the staff has provided relief where the company adopted several of the requested amendments. In addition, for the first time in the United States, a shareholder attempted to use a proxy access bylaw to nominate a director candidate and to have that candidate included in the company’s proxy statement.

Proxy Access 2.0

In large part due to shareholder initiatives, approximately 300 companies have adopted proxy access bylaws during the past two years. The mainstream model adopted by a broad range of S&P 500 companies allows shareholders owning 3% of shares outstanding for at least 3 years to nominate up to 20% of the board (or in some cases, at least two members), with an aggregation limit of 20 shareholders to reach the ownership threshold.

A new wave of shareholder proposals coming this year seeks to amend existing proxy access bylaws, focusing on certain provisions that proponents believe limit the ability of shareholders to use proxy access effectively. These so-called “fix-it” amendments include the following:

- **Ownership Threshold** -- reducing the eligibility requirement from 5% to 3% of the company’s stock.
- **Aggregation Cap** -- increasing or eliminating the limit on the number of shareholders

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permitted to aggregate their holdings to reach the ownership threshold.

- **Board Cap** -- increasing the limit on the number of nominees.
- **Renomination Limit** -- eliminating or reducing the minimum number of votes received by a shareholder nominee in order for that nominee to be renominated in future years.
- **Continued Ownership Requirement** -- eliminating the requirement that the proponent continue to hold shares following the annual meeting.
- **Treatment of Loaned Shares** -- eliminating or liberalizing the conditions for loaned shares to be counted toward the ownership threshold.
- **Eligibility Requirements** -- removing eligibility requirements for shareholder nominees that do not apply to other nominees.

To date, the staff has denied no-action relief to at least seven companies, including *SBA Communications Corporation* (February 12, 2016), *H&R Block, Inc.* (July 21, 2016), *Microsoft Corporation* (October 7, 2016), *Apple, Inc.* (October 27, 2016), *The Walt Disney Company* (November 3, 2016), *Whole Foods Market, Inc.* (November 3, 2016) and *Walgreens Boots Alliance* (November 7, 2016), that sought to have shareholder proposals to amend existing proxy access bylaws excluded on the grounds that the “essential objective” of the shareholder proposal had already been “substantially implemented,” even though the proposal differed from certain specific terms of the bylaw. In applying the “substantially implemented” standard of Rule 14a-8(i)(10), the staff seemed to be distinguishing between a proposal to *adopt* a proxy access proposal and a proposal to *amend* an existing bylaw. The staff also rejected arguments that a proposal to amend more than one provision of a proxy access bylaw constituted more than one proposal under Rule 14a-8(c).

In two no-action letters issued to *Oshkosh Corporation* (November 4, 2016) and *NVR, Inc.* (March 25, 2016), however, the staff granted no-action relief on the grounds of “substantial implementation” where the company adopted some, but not all, of the proposed bylaw amendments. Oshkosh amended its existing proxy access bylaw to implement three of six requested changes after receiving such a proposal. Specifically, the company reduced the ownership threshold from 5% to 3%, eliminated the renomination threshold of 25% of the votes cast, and eliminated the requirement that the nominating shareholder represent that it continue to hold the requisite number of shares for a year following the annual meeting. Oshkosh did not adopt the three other proposed amendments to increase the number of eligible nominees to the greater of 25% or two directors from the greater of 20% or two directors, eliminate the aggregation cap of 20 shareholders and eliminate the requirement regarding loaned securities.

NVR also adopted half of the proposed amendments to its proxy access bylaws, reducing the ownership threshold from 5% to 3% and increasing the number of days within which loaned shares must be recallable to be counted toward the ownership threshold. NVR did not adopt proposals to eliminate the aggregation cap of 20 shareholders and to effectively eliminate the post-meeting holding requirement. It is interesting to note that, prior to the adoption by NVR of two of the four proposed amendments, the staff had denied NVR’s request to exclude all four amendments.

In both Oshkosh and NVR, the staff indicated that the company's policies, practices and procedures compared favorably with the guidelines of the proposal, and therefore the company had substantially implemented the proposal. The distinguishing facts in these two letters when compared with the staff's unsympathetic position on other proposals to amend proxy access bylaws are that both Oshkosh and NVR addressed some of the proposed amendments and one of those amendments was the reduction of the ownership threshold from 5% to the mainstream 3%. While the reduction in the ownership threshold was likely given weight by the staff, it is not clear how the number and nature of the proposals adopted by the companies impacted the staff's decisions.

For the few companies where "fix-it" proposals have already gone to a vote, they received majority support at two companies and substantial support at other companies. Both proposals receiving majority support amended, among other provisions, the ownership threshold to reduce it from 5% to 3%. The "fix-it" proposals voted on so far at companies that have adopted a mainstream proxy access model of 3/3/20/20 were presented at Whole Foods and H&R Block, where the proposals received approximately 39% and 30% of the votes cast, respectively.

First (Attempted) Use of Proxy Access Bylaw

Until recently, proxy access bylaws had never actually been used by shareholders in the United States to advance director nominees. In addition, the conventional wisdom had been that proxy access bylaws, if used, would not likely be used by an activist shareholder because the benefits to the activist of being able to advance its arguments on behalf of its nominee through its own proxy soliciting materials would outweigh the related effort and expense. These are factors that many companies and their boards of directors have considered when deciding whether to voluntarily implement a proxy access bylaw.

That calculus changed on November 10, 2016 when GAMCO Investors, Inc. and its affiliated funds disclosed that they had nominated an individual for election to the board of directors of National Fuel Gas Company pursuant to the company's recently adopted proxy access bylaw. GAMCO has beneficially owned more than 5% of National Fuel Gas since 2010 and has taken an activist role, advocating for the spin-off of certain operations including through a shareholder proposal at the company's 2015 annual meeting. Mario Gabelli, Founder, Chairman and CEO of GAMCO, tweeted on November 14, 2016, that "proxy access was a friendlier approach than a proxy contest at National Fuel Gas." The company subsequently announced that it would not include GAMCO's nominee in the proxy statement, because only stockholders that acquire their shares "in the ordinary course of business and not with the intent to change or influence control" of the company are eligible to nominate a proxy access candidate under the company's bylaws. GAMCO's candidate subsequently withdrew, and GAMCO announced that it will not be pursuing proxy access at this time.

While the situation appears to have passed quickly for National Fuel Gas, it is clear that the concerns raised by the potential use of proxy access bylaws by shareholders are no

longer merely theoretical. We expect that it will only be a matter of time before pension funds and other investors utilize proxy access bylaws to put forward their own director candidates.

What's Next

In light of these and other developments to date relating to proxy access, we expect the following:

- Pressure on companies that have not yet adopted proxy access is likely to continue into and through the 2017 proxy season. Approximately 40% of S&P 500 companies have already adopted proxy access bylaws proactively or following a shareholder proposal or negotiations with a proponent. That number is expected to grow to 50% of the S&P 500 by the end of the 2017 proxy season. Furthermore, small- and mid-cap public companies may see proxy access proposals in a trickle-down effect reminiscent of the majority voting and board declassification campaigns from earlier proxy seasons.
- Companies should be preparing for the possibility of a proxy access bylaw proposal or a proposal to amend an existing bylaw.
- The ability to exclude a shareholder proposal to *adopt* a proxy access bylaw based on substantial implementation remains very strong.
- However, the ability to exclude a shareholder proposal to *amend* an existing proxy access bylaw on the basis of substantial implementation is not likely if the company does not adopt any of the proposed amendments and is highly likely if the company adopts a significant portion of the proposed amendments including an amendment to reduce the share ownership threshold from 5% to 3%. In situations between these two bookends, however, the scope and amount of changes required to obtain no-action relief is not clear.
- Based on the SEC staff's no-action position to date, even companies like Oshkosh and NVR who are able to successfully exclude shareholder proposals this year may receive another round of "fix-it" proposals next year relating to other provisions of their proxy access bylaws that shareholders find objectionable.
- Companies that receive a "fix-it" proposal should be attuned to their investors' policies and preferences on proxy access, and specifically, whether these investors would support the proposed amendments or whether they are satisfied with the existing bylaws. It may be instructive to consider [ISS's FAQ #30](#), which describes the minimum acceptable proxy access terms, as well as problematic provisions, if a board were to implement proxy access in response to a majority supported shareholder proposal. Glass Lewis generally supports proxy access and will evaluate bylaws on a case-by-case basis, with attention to minimum ownership and holding period requirements, as well as company size, board independence and diversity, company performance, existence of anti-takeover protections, board responsiveness to shareholders and shareholders' ability to act by written consent or call a special meeting.
- When analyzing whether to adopt or amend proxy access bylaws, companies and their boards of directors should factor in the likely use of proxy access by pension funds and other investors.