

The SEC Tightens Restrictions on Shareholder Proposals in a Move to Better Align the Interests of Proposing Shareholders With Those of the Company

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On September 23, 2020, the Securities and Exchange Commission (SEC) voted 3-2 to adopt amendments to update its shareholder proposal rule (Rule 14a-8 of the Securities Exchange Act of 1934), which governs the process through which shareholders may submit proposals for inclusion in a company's proxy statement.

The amendments increase the minimum thresholds for shareholders to submit and to resubmit proposals for inclusion on corporate ballots. Proponents of such a change have argued for years that the thresholds required in order to submit proposals have been too low, encouraging frivolous proposals, or proposals that are meaningful to a small subset of shareholders without regard to broader corporate interests. Shareholder activists, however, have steadfastly resisted raising of the thresholds, citing concerns that such a move could silence the voices of small investors.

Submission Thresholds Raised Modestly

Previously, an investor had to own at least US\$2,000 of stock or 1% of a company's securities for at least one year to qualify for inclusion on the ballot. This threshold was adopted in 1998 and had never been adjusted for inflation.

The SEC's new rules replace this threshold with three alternative thresholds: (a) continuous ownership of at least US\$2,000 of the company's securities for a minimum of three years; (b) continuous ownership of at least US\$15,000 of the company's securities for a minimum of two years; or (c) continuous ownership of at least US\$25,000 of the company's securities for a minimum of one year.

Importantly, the amended rule also prohibits the aggregation of the holdings of several shareholders to meet these ownership thresholds.

The amendments further require that a shareholder-proponent using a representative for the purpose of submitting a shareholder proposal provide documentation to make clear that the representative is authorized to act on the shareholder-proponent's behalf. The shareholder-proponent will also need to provide a meaningful degree of assurance as to the shareholder-proponent's identity, role and interest in a proposal that is submitted for inclusion in a company's proxy statement. Additionally, the shareholder-proponent would be required to state that he or she is able to meet with the company, either in person or via teleconference, no less than 10 calendar days, nor more than 30 calendar days, after submission of the shareholder proposal. The shareholder-proponent would also have to provide contact information and specific business days and times that the shareholder-proponent is available to discuss the proposal with the company.

The revised thresholds did not go as far as certain industry groups requested and clearly represented a balancing by the SEC of its desire to continue to facilitate participation by small investors with a long-term investment.

Resubmission Thresholds Changed More Meaningfully

The amendments also modernize the resubmission thresholds for shareholder proposals. Previously, shareholder proposals had to win support from 3% of a company's shareholders the first year they were submitted in order to be eligible for resubmission in the following years. This former resubmission bar moved up to 6% the second year and 10% the third year they were submitted, all within a five-year period.

The SEC's amendments update the resubmission standards for the first time since 1954 and increase these thresholds to 5%, 15% and 25%, respectively.

The SEC declined to include an amendment advocated by many industry groups and included in its proposed rules that would have barred a proposal if it was voted down on three or more times in the last five years. The SEC cited concerns of "anomalous results," under which a proposal that received overall support of over 25% of shareholders, but experienced a 10% decline would be barred, while a proposal of under 25% that retained the same level of support would be permitted to continue. With this consideration in mind, the SEC deleted this amendment from its final rule.

One Proposal Per Meeting Limit

Finally, the SEC's amendments now prevent a shareholder-proponent from submitting more than one proposal at the same meeting. For example, a shareholder-proponent will not be able to submit a proposal on his or her own behalf and on behalf of another shareholder. Likewise, a representative would not be able to submit more than one proposal per meeting, even if he or she were technically submitting a proposal on behalf of multiple different shareholders.

Effective Date and Conclusion

The new shareholder proposal rules will become effective 60 days after publication in the Federal Register (the Effective Date) and will apply to shareholder meetings starting on January 1, 2022. However, the new rules also provide for a transition period for shareholders who are eligible to submit proposals under the current rules as of the effective date, but do not satisfy the new requirements. As long as such a shareholder continuously owns at least US\$2,000 of the company's securities entitled to vote, this shareholder-proponent may continue to submit proposals through January 1, 2023.

According to the SEC, the amendments are meant to ensure that a shareholder submitting proposals has some meaningful “economic stake or investment interest” in the company and is, therefore, more likely to have interests aligned with the company, and to submit good faith proposals.¹ These amendments also relieve companies from the burden of having to consider and expend resources on shareholder proposals that are either frivolous or have an insufficient likelihood of success. In fact, the SEC’s adopting press release clarifies that the new amendments are meant to take into consideration the interests of the company and its other shareholders, who must bear the costs associated with reviewing, considering and voting on shareholder proposals. These new amendments represent a move to protect public companies and a majority of their shareholders from shouldering the burden of proposals that may not represent the best interests of the company, or that may reflect only the interests of a select few.

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¹ See Amendments to Rule 14a-8 Under the Securities Exchange Act of 1934 Relating to Proposals by Security Holders, Release No. 34-20091 (Aug. 16, 1983) [48 FR 38218 (Aug. 23, 1983)], at 38221.