Cooley

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On July 13, 2022, the Securities and Exchange Commission held a lively meeting at which it voted to propose amendments to Rule 14a-8 under the Securities Exchange Act of 1934, the rule governing shareholder proposals to be included in a company's proxy statement to be presented for a shareholder vote. The proposed amendments would amend three of the bases on which a company may exclude a shareholder proposal from its proxy statement:

1. The "substantial implementation" exclusion in Rule 14a-8(i)(10).
2. The "duplication" exclusion in Rule 14a-8(i)(11).
3. The "resubmission" exclusion in Rule 14a-8(i)(12).

The SEC is soliciting comments on the proposed rules, which passed by SEC commissioner votes of 3 to 2 along party lines. For information on the SEC commissioners' views and statements regarding the amendments, refer to our Cooley PubCo blog post. The comment period will be open until the later of 30 days after the proposing release is published in the Federal Register or September 12, 2022 (60 days from the date that the rules were proposed). Interested parties can submit comments on the SEC website.

Background

Rule 14a-8 under the Securities Exchange Act provides a means by which shareholders can submit proposals for inclusion in a company's proxy statement to be presented for a shareholder vote, saving the shareholders the effort and expense of doing a separate proxy solicitation. In addition to setting forth the procedural and eligibility requirements for submitting shareholder proposals to a company, Rule 14a-8 identifies several substantive bases a company can rely on to exclude a shareholder proposal from its proxy statement. Typically, before excluding a shareholder proposal, a company will request assurance from the staff of the SEC's Division of Corporation Finance via a written no-action letter that the staff will not recommend an enforcement action if the company omits the proposal on the basis of one of the exclusions described in the no-action letter requesting relief.

In 2020, the SEC adopted amendments modifying the criteria for eligibility and resubmission of shareholder proposals in Rule 14a-8, which only took effect for meetings held after January 1, 2022. The proposed amendments do not address these requirements, which remain in effect. However, the SEC noted in the proposed rule release that it "continues to assess the impact of these amendments." In addition, in November 2021, the Division of Corporation Finance published Staff Legal Bulletin No. 14L (SLB 14L), which provides guidance on the staff's interpretation of certain bases on which a company may exclude a shareholder proposal, including the "ordinary business" exclusion and the "economic relevance" exclusion, making it more difficult for companies to exclude shareholder proposals including, in particular, social and environmental proposals. (See this Cooley client alert for more information on SLB 14L). The effect of the 2020 amendments and SLB 14L has been an increase in proposals submitted to companies, along with a significant decrease in the number of successfully excluded proposals during the 2022 proxy season. The proposed amendments to Rule 14a-8 aim to provide clarification with respect to three more substantive bases for exclusion, which may further limit the ability of companies to exclude shareholder proposals from proxy materials, if adopted.

Proposed amendments

Substantial implementation exclusion

The "substantial implementation" exclusion in Rule 14a-8(i)(10) permits a company to omit a shareholder proposal that "the company has already substantially implemented." The rationale underlying the exclusion is to avoid shareholders having to consider a proposal that management has already acted upon. The substantial implementation exclusion is one of the most commonly used bases by companies for excluding a shareholder proposal, and has assumed additional importance following the narrowing of other exclusions in SLB 14L. To provide guidance on what "substantially implemented" means, the proposed amendments would specify that a shareholder proposal may be excluded on this basis if "the company has already implemented the **essential elements** of the proposal" (emphasis added). The SEC believes that an analysis that focuses on the specific

elements of a proposal will provide more predictability in determining whether it has been substantially implemented, though the SEC acknowledges that the amendment would still require a substantive analysis to determine which elements of the proposal are "essential elements."

Importantly, a company would only be permitted to exclude a shareholder proposal on this basis if **all** of its essential elements have been implemented. As an example of the practical implications of this proposed amendment, the SEC points to a proposal seeking the adoption of a proxy access provision that allows an unlimited number of shareholders meeting certain ownership thresholds to nominate up to 25% of a company's board, where the company had already adopted a proxy access provision allowing 20 shareholders meeting certain ownership thresholds to nominate up to 20% of a company's board. While the SEC staff has historically concurred in excluding this proposal on the basis of substantial implementation under these facts, the release notes that exclusion would not be appropriate under the proposed amendments, as the ability of an unlimited number of shareholders to aggregate their shareholdings would be an essential element of the proposal. As another example, the SEC describes a proposal requesting a report from the company's board of directors on a particular topic, noting that the staff may determine that the company has not implemented an essential element of this proposal if the company has an existing report that comes from management, rather than the board.

Duplication exclusion

Rule 14a-8(i)(11), the "duplication" exclusion, permits a company to exclude a shareholder proposal that "**substantially duplicates** another proposal previously submitted to the company by another proponent that will be included in the company's proxy materials for the same meeting" (emphasis added). The purpose of this exclusion is to "eliminate the possibility of shareholders having to consider two or more substantially identical proposals submitted to an issuer by proponents acting independently of each other," and is utilized far less frequently than the substantial implementation exclusion. To add clarity to this exclusion, the proposed amendments would provide that a proposal "substantially duplicates" another proposal if it "addresses the same subject matter and seeks the same objective by the same means."

As an example of the change contemplated by this amendment, the release provides two proposals: "(1) a proposal requesting that the company publish in newspapers a detailed statement of each of its direct or indirect political contributions or attempts to influence legislation; and (2) a proposal requesting a report to shareholders on the company's process for identifying and prioritizing legislative and regulatory public policy advocacy activities." While the SEC staff historically has concurred with applying the duplication exclusion to these proposals, given that they concern the same subject matter, these proposals would not be deemed substantially duplicative under the proposed amendment, as they seek different objectives by different means. The release also notes that the proposed amendments would reduce incentives for shareholder proponents to submit a proposal quickly, as the amendments would potentially enable consideration of a later-received proposal, even if similar and covering the same subject matter as the earlier proposal.

Resubmission exclusion

The "resubmission" exclusion in Rule 14a-8(i)(12), a rarely used basis for exclusion, allows a company to exclude a shareholder proposal if it "addresses substantially the same subject matter as a proposal, or proposals, previously included in the company's proxy materials within the preceding five calendar years" – if the issue was voted on at least once in the last three years and received support below specified thresholds (which were amended as recently as 2020). The underlying rationale for this exclusion is to prevent companies from having to include proposals that have been recently presented for a shareholder vote and did not receive much support. In 1983, the SEC specified that this exclusion would apply to a proposal with "substantially the same subject matter" as a prior proposal. The proposed amendments would revise this standard to a proposal that "substantially duplicates" a prior proposal, which would be defined as a proposal that "addresses the same subject matter and seeks the same objective by the same means" as the prior proposal, matching the amendments proposed to the duplication exclusion. The SEC believes that this change would enable shareholder proponents to make adjustments to their proposals to obtain broader support and allow other shareholders to offer their own proposals with different means of addressing the same issues.

The release provides two proposals as an example to which the resubmission exclusion applies under the existing standard but would not apply under the proposed amendment: "(1) a proposal requesting that the board adopt a policy prohibiting the vesting of equity-based awards for senior executives due to a voluntary resignation to enter government service (a 'government service golden parachute'); and (2) a proposal requesting that the board prepare a report to shareholders regarding the vesting of such government service golden parachutes that identifies eligible senior executives and the estimated dollar value of each senior executive's government service golden parachute." Although these proposals address the same subject matter, government service

golden parachutes, according to the proposed amendment to Rule 14a-8(i)(11), these proposals do not seek the same objectives by the same means and, therefore, the later proposal would not be excludable on this basis.

Observations and commentary

If adopted, the paths to exclude shareholder proposals will continue to narrow. After the publication of SLB 14L, which narrowed the "ordinary business" exclusion, the 2022 proxy season has seen dramatic declines in the success rate of companies attempting to exclude shareholder proposals from their proxy statements for a shareholder vote. The proposed rules, if adopted, will further narrow the fact patterns in which these bases would be available to companies. This is particularly important for the "substantial implementation" exclusion, which historically has been one of the most commonly used bases. Final rules, if adopted as proposed, would meaningfully alter the rate at which these requests are granted – and would leave companies with significantly reduced options compared to a couple of years ago for excluding a shareholder proposal from their proxy statements. This narrowing of options is especially important given the significant increases in shareholder proposals in recent years, including many covering matters related to environmental, social and governance factors.

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