

## Legal Updates & News

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#### Far-Reaching Shareholder Bill of Rights Introduced in Senate

May 2009

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On May 19, 2009, Senator Charles Schumer (D-NY) and Senator Maria Cantwell (D-WA) introduced the Shareholder Bill of Rights Act of 2009 (the "Shareholder Bill of Rights") in the United States Senate.<sup>[1]</sup> The origins of the Shareholder Bill of Rights are rooted in the current national and global financial and economic crisis, which the bill describes as being caused by "a widespread failure of corporate governance" and "lack of accountability of boards to . . . the shareholders." The primary goal of the Shareholder Bill of Rights is "[t]o provide shareholders with enhanced authority over the nomination, election, and compensation of public company executives," and the bill includes a wide-ranging set of corporate governance mandates, including:

- Establishing an advisory shareholder vote on compensation for executives, including in the context of any acquisition, merger, consolidation, or disposition of substantially all assets;
- Establishing parameters for the Securities and Exchange Commission (the "SEC") to set rules allowing easier shareholder access to company proxy solicitation materials for purposes of nominating directors;
- Establishing enhanced corporate governance standards related to the chairperson of the board and the election of directors;
- Requiring the elimination of staggered boards; and
- Requiring each public company to have an independent risk committee of its board of directors.

As with the Sarbanes-Oxley Act of 2002, the high-profile nature of the Shareholder Bill of Rights, combined with the momentum afforded by the ongoing economic crisis, could result in a major and lasting impact on the corporate governance policies of U.S. public companies.

#### Advisory Shareholder Vote on Executive Compensation and Golden Parachutes

Section 3 of the Shareholder Bill of Rights would require an annual advisory shareholder vote to approve executive compensation, as such compensation is disclosed in the company's proxy statement pursuant to the SEC's compensation disclosure rules, "which disclosure shall include the compensation discussion

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and analysis, the compensation tables, and any related material.” The legislation would mandate the inclusion of a separate executive compensation resolution subject to shareholder approval in the proxy solicitation for each annual meeting (or any meeting for which the proxy rules require disclosure of executive compensation).

Section 3 of the Shareholder Bill of Rights would also require an advisory shareholder vote on “Golden Parachute Compensation.” In particular, the bill requires persons soliciting proxies in connection with any “acquisition, merger, consolidation, or proposed sale or other disposition of substantially all of the assets of an issuer” to disclose, in “clear and simple form,” any agreements or understandings the person has with the principal executive officers of the issuer concerning compensation that is based on or otherwise related to the transaction, and that has not already been approved by the annual shareholder vote.

With respect to both shareholder advisory votes, the Shareholder Bill of Rights clarifies that the results of the vote shall not be binding on the board of directors and would neither change the current fiduciary duties nor create additional fiduciary duties for directors on the board. The bill also states that the new shareholder votes do not restrict the ability of shareholders to submit proxy proposals regarding executive compensation. The Shareholder Bill of Rights would give the SEC one year to issue final rules to implement the new requirements, and the provisions of Section 3 of the bill would be effective for meetings held more than one year after the date of enactment.

### **Shareholder Access to the Company’s Proxy Statement**

Section 4 of the Shareholder Bill of Rights confirms the SEC’s authority to enact rules regarding shareholder access to company proxy solicitation materials for purposes of nominating directors for election to the company’s board. The bill would not mandate the content of such rules, other than to state that the SEC shall not allow access to company proxy materials unless the shareholder, or group of shareholders acting by agreement, has beneficially owned, directly or indirectly, not less than one percent (1%) of the company’s securities for at least two years prior to the date of the next annual meeting. Notably, these provisions could limit the flexibility of Delaware corporations under recently adopted Section 112 of the Delaware General Corporation Law, which provided companies with the ability to set conditions around such nominations, including minimum stock ownership and duration of ownership. The Shareholder Bill of Rights would not establish a deadline for the SEC’s enactment of shareholder access rules. At an open meeting previously scheduled for today on this topic, the SEC proposed a set of revisions to the proxy rules relating to shareholder access, and we will provide further updates as that rule proposal becomes publicly available.

### **Separation of Chairperson and CEO; Elimination of Staggered Boards and Majority Voting**

Section 5 of the Shareholder Bill of Rights includes a number of additional corporate governance requirements related to the boards of public companies, and would direct the SEC to establish within one year rules prohibiting national securities exchanges and national securities associations from listing any company not in compliance with the new standards. The legislation would require that any such listing rules provide an opportunity for a non-compliant company to cure defects prior to such prohibition and also permits the SEC to exempt certain companies based on criteria “the Commission deems necessary or appropriate.” The proposed new requirements include:

- The chairperson of the board of directors shall be “independent,” as defined by the SEC’s and the securities exchange’s rules and regulations, and shall not have previously served as an executive officer of the company.
- Each member of the company’s board of directors must be subject to annual election by the shareholders. This requirement would effectively eliminate the practice of “staggered boards” among public companies.
- For elections where the number of nominees exceeds the number of directors being elected, a vote of a plurality of the shares at the meeting and entitled to vote shall be sufficient for election to the board. For uncontested elections, a nominee must receive a majority of the votes cast with respect to such nominee to be elected to the board. An incumbent director who does not receive a majority of the votes cast in an uncontested election must tender his or her resignation from the board, and the board is required to accept such resignation.

## **Risk Committees Required**

An additional requirement under the corporate governance standards imposed by Section 5 of the Shareholder Bill of Rights would mandate that each public company establish an independent risk committee, “which shall be responsible for the establishment and evaluation of the risk management practices of the issuer.” The Shareholder Bill of Rights gives the SEC one year from the enactment of the legislation to issue final rules regarding such risk committees and provides companies one year from the issuance date of such rules to comply with the new risk committee requirements.

## **Conclusion**

The Shareholder Bill of Rights Act of 2009 is certain to prompt a lively debate regarding the causes of the current economic crisis, the benefits of increased shareholder access and oversight, and federal preemption of state corporate law. The Shareholder Bill of Rights is among several legislative proposals expected to be introduced in the current session of Congress to address perceived corporate governance shortfalls. Together with the proposed new SEC rules regarding shareholder access and possible action by the SEC to approve the amendment of New York Stock Exchange Rule 452 to eliminate the casting of broker votes in uncontested director elections, this year has the potential to mark the beginning of a transformational era in corporate law.

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## **Footnotes**

[1] Shareholder Bill of Rights Act of 2009, S. 1074, 111th Cong. (2009).