

# Legal Update

## SEC Adopts Universal Proxy Rules

On November 17, 2021, the US Securities and Exchange Commission (SEC) adopted mandatory universal proxy rules that will apply for all contested director elections,<sup>1</sup> which it had previously proposed in 2016. Under the final rules, each universal proxy card must list all management and dissident nominees for director, enabling shareholders voting by proxy to pick and choose among the different slates of candidates, similar to the manner in which they would be able to vote for directors in person at a contested shareholders meeting. At the same time, the SEC also made changes to proxy cards and proxy statement disclosure requirements regarding voting standards and certain voting options applicable to all director elections.

The amendments requiring universal proxy cards for contested director elections, as well as the amendments relating to all director elections, will apply to shareholders meetings held after August 31, 2022.

The amendments to the proxy rules are summarized below.

### Implementation of Universal Proxy Rules

**Mandatory Universal Proxy Cards.** The final rules provide for mandatory use of a universal proxy card for all proxy solicitations in connection with contested elections for directors that are not exempt under Rule 14a-2(b). A universal proxy card is permitted but not required for other types of solicitations, including, for example, a “vote no” campaign or solicitations of proxies in support of a shareholder proposal.

Each party in a contested election would distribute its own universal proxy card. Each universal proxy card would include the names of all nominees for director for whom proxies are solicited, either by the company or by dissident shareholders. The universal proxy card must clearly distinguish between registrant and dissident nominees, as well as proxy access nominees, if applicable. If there are proxy access nominees but no dissident nominees, the universal proxy rules will not apply.

Within each group on a universal proxy card, the nominees must be listed in alphabetical order by last name. All nominees have to be presented in the same font type, style and size on the proxy card. The proxy card will have to prominently disclose the maximum number of nominees for which voting authority can be granted. It will also have to prominently disclose the treatment and effect of a proxy that is executed in a manner that grants authority to vote for fewer or more nominees than the number of directors being elected or that does not grant authority to vote with respect to any nominees.

The key amendments to implement use of universal proxy cards are contained in new Rule 14a-19, "Solicitation of proxies in support of director nominees other than the registrant's nominees," with related proxy card provisions set forth in amendments to Rule 14a-4, "Requirements as to proxy."

**Notice, Timing and Solicitation Requirements.** A dissident that intends to solicit proxies for its own nominees in a contested election for directors will have to give the company notice of the names of its nominees. The notice must be postmarked or transmitted electronically to the company at least 60 calendar days prior to the anniversary of the previous year's annual meeting date. In effect, this requirement precludes a dissident from launching an election contest less than 60 days prior to the anniversary of the previous year's annual meeting of shareholders. The notice requirement is in addition to any advance notice requirements set forth in the company's governing documents, which frequently provide for earlier notice of director nominations by dissidents.

The universal proxy rules require the company to inform the dissident of the names of the company's nominees for director unless the names of all nominees have been provided in a preliminary or definitive proxy statement. This notice must be postmarked or transmitted electronically to the dissident at least 50 calendar days prior to the anniversary of the previous year's annual meeting date. The dissident will be obligated to file its definitive proxy materials with the SEC by the later of 25 calendar days prior to the meeting date or five calendar days after the company files its definitive proxy statement with the SEC.

In a change from the proposal, the dissident will be required to solicit the holders of shares representing at least 67 percent of the voting power for the election of directors in order to trigger the universal proxy card requirements. The dissident will have to promptly notify the company of any change in its intent to comply with this minimum solicitation requirement or with respect to the names of its nominees.

**Abandoned Solicitations.** The dissident's plans could change after it provides the company with notice of its intention to solicit proxies for its own nominees for directors. Therefore, the amendments to the SEC's proxy rules require the company to disclose in its proxy statement how it intends to treat proxies granted in favor of a dissident's nominees if the dissident abandons its solicitation or if it fails to comply with the universal proxy rules. If the dissident abandons its solicitation after the company has distributed its universal proxy card, the company could elect to distribute a new, non-universal proxy card with only its nominees. If there is a change in the dissident's nominees after the company has disseminated a universal proxy card, the company could, but would not be required to, distribute a new universal proxy card reflecting the new dissident nominees.

**Nominee Consent and Information.** To facilitate the requisite consent of a nominee to being named in proxy materials, the Rule 14a-4(d) definition of a "bona fide nominee" for director has been amended to encompass a person who has consented to being named in *any* proxy statement relating to the company's next shareholder meeting at which directors are to be elected. In other words, by consenting to be named in the company's proxy statement, the nominee would also have to consent to be named in the dissident's proxy statement, and vice versa. This enables both the company and the dissident to include the other party's nominees on their universal proxy cards even if a nominee's consent did not expressly mention that party's proxy statement. Both the company and the dissident would have to refer to the other party's proxy statement for information about that party's nominees and explain how shareholders can access that proxy statement.

**Elimination of Short Slate Rule.** The amendments eliminate the existing short slate rule (other than for funds or business development corporations) contained in Rule 14a-4(d)(4), which had allowed a

dissident to nominate a partial slate of directors by using its proxy authority to vote for some nominees named in the company's proxy statement to round up its slate of directors. The SEC believes the short slate rule is no longer needed because universal proxies will give shareholders the ability to cast a vote for a full slate of directors.

**Explanation of Key Terms.** Certain terms are used but not defined in the universal proxy rules. The adopting release contained explanations of its intended meanings for some of these terms. For example, the term "dissident" for the purposes of the adopting release refers to a soliciting person, other than the company, who is soliciting proxies in support of director nominees other than the company's nominees.<sup>2</sup> In addition, "contested election" as used in the adopting release refers to an election of directors where a company is soliciting proxies in support of nominees and a person or group of persons is soliciting proxies in support of director nominees other than the company's nominees.<sup>3</sup>

**Companies and Solicitations Not Subject to Mandatory Universal Proxy Rules.** Neither investment companies registered under Section 8 of the Investment Company Act of 1940 nor business development companies as defined under Section 2(2)(48) of the Investment Company Act of 1940 are subject to the universal proxy rules. Because foreign private issuers and companies with reporting obligations only under Section 15(d) of the Securities Exchange Act of 1934 are not subject to US proxy solicitation rules, they also are not subject to the universal proxy rules.

The amendments do not apply to solicitations exempted under Rule 14a-2(b), including, for example, solicitations in which a person is not seeking a proxy and does not furnish or request a form of revocation, abstention, consent or authorization and solicitations limited to a maximum of 10 persons. The amendments also do not apply to solicitations that are not related to the election of directors. In addition, universal proxy rules do not apply to a dissident's consent solicitation to remove directors and replace them with nominees of the dissident, where written consents are solicited to take action without a meeting.

## Director Election Voting Standards and Voting Options

The SEC also adopted additional amendments to the proxy rules relating to voting options and standards that are applicable to all director elections. The SEC has amended Rule 14a-4(b) to require proxy cards for all director elections to include an "against" option instead of a "withhold authority to vote" option if governing law gives legal effect to a vote against a nominee. When applicable state law does not give legal effect to votes cast against a nominee, the form of proxy may not provide a means to vote against any nominee, and the form of proxy must clearly provide specified means to withhold authority to vote for each nominee. The amendments also provide that when a director election is governed by a majority voting standard, shareholders that neither support nor oppose a nominee be given the opportunity to "abstain" as opposed to withholding authority to vote. In addition, under the amendments, proxy statements will be expressly required to disclose the methods by which votes will be counted, including the treatment and effect of a "withhold" vote in an election of directors.

## Practical Considerations

The adoption of universal proxy card requirements is an important topic that will impact proxy fights and, potentially, board governance. Companies should therefore understand the new universal proxy card requirements so that they will be familiar with the concept and procedures and plan accordingly should a proxy contest arise in the future.

As an immediate step, companies should review their bylaws to assess whether any amendments are appropriate to take the universal proxy rules into account, such as revising or adopting advance notice provisions.

Companies should also consider updating their proxy season calendars and checklists to reference deadlines contained in the universal proxy rules. For example, one of the technical requirements under the universal proxy rules is an amendment to Rule 14a-5, "Presentation of information in proxy statement," requiring proxy statements to disclose the deadline for providing notice of a solicitation of proxies in support of director nominees other than the company's nominees pursuant to the universal proxy rules for the company's next annual meeting. Therefore, companies should make a note to include this disclosure in their proxy statements for shareholders meetings held after the August 31, 2022 compliance date.

The universal proxy rules are different from proxy access in a number of key ways. For example, the universal proxy card procedures require a significant investment of resources by dissident shareholders. Universal proxy cards do not provide dissidents with access to a company's proxy materials to the extent provided by proxy access bylaws. Under the universal proxy rules, a dissident's access to the company's proxy materials is limited to the company listing the names of the dissident's nominees on its proxy card, and this access would be accompanied by an obligation of the dissident to prepare a proxy statement and to solicit proxies on behalf of its own nominees.

The universal proxy rules may increase the number of contested elections. And, to the extent that shareholders may be more willing to select just a small number of the nominees recommended by a dissident while supporting most of the slate recommended by the Board, the universal proxy rules may potentially result in more activists winning a seat on public company boards of directors.

The fact that the SEC has addressed distinctions between abstaining from a vote and withholding a vote suggests that the SEC has not been comfortable that proxy cards and related proxy statement disclosure are sufficiently clear with respect to voting standards for the election of directors. Although the amendments will not apply to shareholders meetings held on or before August 31, 2022, it would be useful for companies to evaluate the adequacy of their proxy statement descriptions of director voting standards and consider whether refinements could be made to such discussions to enhance the clarity of the disclosure in their upcoming proxy statements, even for meetings being held before the compliance date. In particular, companies that only include "for" and "withhold" boxes on their proxy cards for director elections should review applicable governing law to determine whether it gives legal effect to "against" votes.

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## Endnotes

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<sup>1</sup> The adopting release is available at <https://www.sec.gov/rules/final/2021/34-93596.pdf>

<sup>2</sup> See footnote 11 of the adopting release.

<sup>3</sup> See footnote 9 of the adopting release.

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