

SHAREHOLDER PROPOSAL DEVELOPMENTS DURING THE 2019 PROXY SEASON

August 26, 2019

To Our Clients and Friends:

This client alert provides an overview of shareholder proposals submitted to public companies during the 2019 proxy season,¹ including statistics and notable decisions from the staff (the “Staff”) of the Securities and Exchange Commission (the “SEC”) on no-action requests.²

I. TOP SHAREHOLDER PROPOSAL TAKEAWAYS FROM THE 2019 PROXY SEASON

As discussed in further detail below, based on the results of the 2019 proxy season, there are several key takeaways to consider for the coming year:

- ***Shareholder proposal submissions continue to trail their five-year average, but divergent trends for social and environmental proposals have emerged.*** The number of proposals submitted increased by 1% to 792, but is still down 9% from the five-year average of 875. A 22% decline in environmental proposals was offset by increases in other major proposal categories, such as social (9%), governance (3%) and civic engagement (7%). The five most popular proposals, representing 39% of all shareholder proposal submissions, were political contributions and lobbying (with political contribution proposals trending up and lobbying proposals trending down), independent chair, anti-discrimination and diversity (with board diversity proposals up more than 50%), climate change (down 33%), and written consent proposals (consistent with the number submitted during the 2018 proxy season).

¹ For purposes of reporting statistics regarding shareholder proposals and no-action requests, references to the “2019 proxy season” refer to the period between October 1, 2018, and June 1, 2019. Data regarding no-action letter requests as well as no-action letters was derived from the information available on the SEC’s website. Unless otherwise noted, all data on shareholder proposals submitted, withdrawn, and voted on is derived from Institutional Shareholder Services (“ISS”) publications and the ISS shareholder proposals and voting analytics databases, and generally includes proposals submitted and reported in these databases at any time prior to June 1, 2019, for annual meetings of shareholders at Russell 3000 companies held in 2019. References in this alert to proposals “submitted” include shareholder proposals voted on or excluded pursuant to a no-action request, or that the proponent withdrew, and do not include proposals that may have been delivered to a company and subsequently withdrawn without any public disclosure. All shareholder proposal data should be considered approximate. Voting results are reported on a votes cast basis calculated under Rule 14a-8 (votes for or against) and without regard to whether the company’s voting standards take into account the impact of abstentions. Where statistics are provided for prior years, the data is for a comparable period in those years.

² Gibson, Dunn & Crutcher LLP assisted companies in submitting the shareholder proposal no-action requests discussed in this alert that are marked with an asterisk (*).

- ***Proliferation of new proponents and co-filers.*** The number of shareholders using the Rule 14a-8 shareholder proposal process continues to grow, with more than 300 different proponents in 2019 (compared to less than 200 proponents two years ago). Almost 75% of proposals were submitted by individuals and religious-affiliated organizations and, as in prior years, John Chevedden and his associates were the most frequent proponents (representing almost one-third of proposals in 2019). This year also saw a continuation of the trend of proposals submitted by numerous co-filers—for example, the number of proposals submitted by at least five co-filers more than tripled over the prior year.
- ***Negotiated withdrawals trending up and SEC challenges trending down.*** There continues to be an increasing trend of companies and proponents negotiating a withdrawal, as the percentage of proposals withdrawn has more than doubled over the last two years and the percentage challenged through the SEC no-action request process continues to decrease. This is due, in part, to the increasing proportion of proposals that are focused on social or environmental issues, which are more likely to implicate potential reputational risks. The shutdown of the U.S. government appears not to have affected the number of withdrawals compared to last year, and may have discouraged or delayed engagement between companies and proponents.
- ***Continued increase in voting support, particularly for social and environmental shareholder proposals.*** Average voting support for all shareholder proposals was 33.6%, up slightly from 2018 and up more significantly from 2017. Governance shareholder proposals continued to receive the highest support, though the gap between these proposals and social/environmental proposals continued to narrow (dropping from more than 20.1% to 11.9% over the last two years). This year also saw a 72% increase in the number of shareholder proposals that received majority support (43 in total), with an increasing number focused on issues other than traditional governance topics.
- ***Overall no-action request success rates steady, but board analyses remain challenging.*** The overall success rate for no-action requests held about steady at 66%, driven by substantial implementation, ordinary business, and procedural arguments. Although expectations were high upon the Staff's October release of updated guidance for including a board analysis in ordinary business and economic relevance arguments, companies continued to face difficulties in this area. While the Staff has informally stated that it has found board analyses useful, the Staff granted no-action relief citing a board's analysis in only one letter this season.
- ***Proponents continue to use all available tools at their disposal.*** As we predicted last year, there was continued proliferation in the use of exempt solicitation filings, with the number of filings reaching a record high again this year and increasing more than 40% over the last two years. This continues to be an area for abuse—for example, approximately 25% of exempt solicitation filings in 2019 failed to comply with the guidance the Staff released last July. In addition, this year we saw a couple of interesting litigation developments, with one proponent turning to the courts to fight the exclusion of a proposal even before the SEC had issued its response on the related no-action request and another proponent turning to the courts in connection with a proposal that raised questions as to the legality under state law of a mandatory arbitration bylaw.

- **Shareholder proposal reform on the horizon.** There appears to be a meaningful chance for reform of the shareholder proposal rules over the next year, with Chairman Clayton’s February appointment of Commissioner Roisman to lead the SEC’s “task force” to improve the proxy process (including shareholder proposals) and Rule 14a-8 thresholds appearing for the first time on the SEC’s Reg Flex Agenda in May (notably, on the portion of the agenda that the SEC expects to complete over the coming year). The Staff has also stated that it is considering potentially significant changes to its traditional practice of responding to all shareholder proposal no-action requests.

II. SHAREHOLDER PROPOSAL STATISTICS AND VOTING RESULTS

A. Overview of Shareholder Proposals Submitted

Shareholders submitted 792 shareholder proposals during the 2019 proxy season, up 1% from 788 in 2018 but down 9% from the five-year average of 875.

Across five broad categories³ of shareholder proposals in 2019—social, environmental, governance, civic engagement, and executive compensation—similar to 2018, social and environmental proposals combined continued to be the most frequently submitted proposals (representing 42% of all proposals submitted), followed by governance proposals (36%), civic engagement proposals (12%), executive compensation proposals (7%), and other proposals (3%). Key year-over-year trends in these categories include:

- **Social proposals.** The number of social shareholder proposals submitted during the 2019 proxy season increased 9% to 220 (compared to 202 in 2018). The largest sub-category, representing 29% of these proposals, continued to be anti-discrimination and diversity-related proposals, with 63 submitted in 2019 (down from 68 in 2018).

³ Categorizing shareholder proposals can, at times, be a subjective endeavor. We categorize shareholder proposals based on subject matter as follows:

Social proposals cover a wide range of issues and include proposals relating to: (i) discrimination and other diversity-related issues (including board diversity); (ii) gender/ethnicity pay gap; (iii) board committees on social and environmental issues; (iv) social and environmental qualifications for director nominees; and (v) reporting on societal concerns, such as human rights, employment or workplace policies, animal welfare, and the opioid crisis.

Environmental proposals include proposals addressing: (i) climate change (including climate change reporting, greenhouse gas emissions goals, and climate change risks); (ii) recycling or sustainable packaging; (iii) renewable energy; (iv) environmental impact reports; and (v) sustainability reporting.

Governance proposals include proposals addressing: (i) shareholder special meeting rights; (ii) proxy access; (iii) majority voting for director elections; (iv) independent board chairman; (v) board declassification; (vi) shareholder written consent; (vii) elimination/reduction of supermajority voting; (viii) director term limits; and (ix) stock ownership guidelines.

Civic engagement proposals include proposals addressing: (i) political contributions disclosure; and (ii) lobbying policies and practices disclosure.

Executive compensation proposals include proposals addressing: (i) performance metrics, including the incorporation of sustainability-related goals; (ii) compensation clawback policies; (iii) severance and change of control payments; (iv) equity award vesting; (v) executive compensation disclosure; and (vi) limitations on executive compensation.

- **Environmental proposals.** Environmental shareholder proposals declined by 22% during the 2019 proxy season, with 109 proposals submitted (down from 139 in 2018). The largest sub-category, representing 44% of these proposals, continued to be climate change proposals, with 48 submitted in 2019 (down from 72 in 2018).
- **Governance proposals.** The number of governance shareholder proposals submitted during the 2019 proxy season increased 3% to 289 (compared to 281 in 2018). The largest sub-category, representing 22% of these proposals, was independent chair proposals, with 64 submitted (up from 51 in 2018). This reflects continued shifts in focus from 2018 and 2017, when the largest sub-category of these shareholder proposals was shareholder special meeting rights and proxy access, respectively.
- **Civic engagement proposals.** The number of civic engagement proposals submitted during the 2019 proxy season increased 7% to 98 (compared to 92 in 2018). Trends diverged among the different types of these proposals, with political contribution proposals (the largest sub-category, representing 62% of these proposals) increasing from 38 to 61 in 2019 and lobbying expenditure proposals decreasing from 47 to 37 in 2019.
- **Executive compensation proposals.** The number of executive compensation proposals submitted during the 2019 proxy season was flat at 54 (compared to 55 in 2018). The largest sub-category, representing 35% of these proposals, was proposals seeking to include social or environmental-focused performance measures in executive compensation programs (such as diversity, cybersecurity, data privacy and risks arising from drug pricing), with 19 submitted in 2019 (compared to 20 in 2018).

The five most popular proposal topics are shown in the table below. These largely remained the same year-over-year, though there was some shuffling in order below the most frequently submitted shareholder proposal. Notably, the top five shareholder proposals collectively represented only 39% of all shareholder proposals submitted in 2019, down from 46% in 2018 and 47% in 2017.

Top Shareholder Proposals by Percentage of Total Submitted	
2019	2018
Political contributions & lobbying (12%)	Political contributions & lobbying (11%)
Independent chair (8%)	Shareholder special meeting rights (10%)
Anti-discrimination & diversity (8%)	Climate change (9%)
Climate change (6%)	Anti-discrimination & diversity (9%)
Written consent (5%)	Independent chair (7%)

B. Overview of Shareholder Proposal Proponents

In terms of who submitted shareholder proposals, there were at least 324 different proponents and co-filers during the 2019 proxy season, up 45% from 224 in 2018. A substantial majority of proposals were submitted by individuals (48%) and religious-affiliated organizations (25%). As in prior years, John Chevedden and shareholders associated with him (including James McRitchie, Kenneth Steiner, and Myra Young) submitted or co-filed the most shareholder proposals during the 2019 proxy season—239 proposals (up from 187 in 2018) or 30% of all proposals. The table below shows the proponents who have submitted (or co-filed) at least 20 proposals this year.

Top Proponents by Number Submitted			
Proponent	2019	2018	Primary focus areas
John Chevedden (& associates)	239	187	Governance & executive compensation
As You Sow Foundation	56	28	Environmental
NY City Comptroller	48	25	Political, diversity & environmental
Mercy Investment Services	42	23	Political, diversity & environmental
NY State Common Retirement Fund	32	48	Political, diversity & environmental
Trillium Asset Management	30	35	Environmental
CalPERS	25	3	Governance
Friends Fiduciary	23	11	Political, diversity & environmental
Walden Asset Management	22	26	Political & environmental

Influx of co-filers. Over the past several years, we have also seen a growing trend in the number of proposals with multiple co-filers. For example, during the 2019 proxy season there were approximately 217 proposals submitted by two or more co-filers (up from 141 in 2018 and 83 in 2017), 58 of which were submitted by five or more co-filers (up from 18 in 2018 and six in 2017). Obviously, this creates more work for companies to vet the propriety of the submissions and, to the extent a lead proponent is not identified, can impede productive negotiations to implement and withdraw the proposal.

C. Overview of Shareholder Proposal Outcomes

In terms of shareholder proposal outcomes, as shown in the table below, the 2019 proxy season saw a continuation of two significant trends from recent years—the percentage of proposals excluded through the no-action letter process continued to decline, while the percentage of proposals withdrawn continued to increase, more than doubling from 2017 to 2019 and now exceeding no-action letter exclusions. This increase is due, in part, to the increasing proportion of social and environmental proposals and the fact that there is a higher tendency for social or environmental shareholder proposals to be withdrawn in contrast to other types of proposals. For example, 77% of all shareholder proposals withdrawn during the 2019 proxy season were social or environmental proposals. Moreover, it is widely known that certain frequent proponents of governance shareholder proposals as a matter of practice do not withdraw their proposals.

Shareholder Proposal Outcomes⁴			
	2019	2018	2017
Total number of proposals submitted	792	788	827
Excluded pursuant to a no-action request	15% (119)	16% (125)	23% (189)
Withdrawn by the proponent	20% (155)	15% (116)	9% (77)
Voted on	38% (299)	41% (325)	40% (331)
Pending a vote	18% (146)	19% (153)	28% (234)

Support levels. Shareholder proposals voted on during the 2019 proxy season averaged support of 33.6%, up slightly from the 32.7% average in 2018 and up more significantly from the 29.0% average in 2017. Continuing the trend from the prior year, average support for governance

⁴ Excludes proposals that, for other reasons, were not in the proxy or were not voted on, including, for example, due to postponement of the meeting or failure of the proponent to present the proposal at the meeting. As a result, in each year, percentages may not add up to 100%.

proposals declined to 38.3% while average support for social and environmental proposals increased to 26.4%, which narrowed the gap between the two to 11.9% (down from 20.1% in 2017). Notably, looking at just environmental proposals, average support declined from 30.5% to 26.2% support as fewer climate change proposals went to a vote. The table below shows those proposals voted on at least three times that received the highest average support, including three categories of proposals that averaged majority support.

Top Proposals by Voting Results⁵			
Proposal	2019	2018	2017
Board declassification	68.5% (3)	83.3% (4)	70.2% (3)
Eliminate/reduce supermajority voting	65.7% (14)	74.7% (8)	64.3% (7)
Adopt proxy access	53.2% (4)	34.8% (5)	62.8% (17)
Majority voting in director elections	47.9% (11)	59.9% (2)	62.3% (7)
Employment diversity	45.0% (6)	38.8% (7)	29.5% (6)
Shareholder special meeting rights	44.4% (21)	41.2% (51)	42.9% (15)
Shareholder action by written consent	39.1% (32)	41.8% (33)	45.6% (12)
Political contributions & lobbying	34.2% (47)	29.5% (45)	27.8% (20)
Climate change	30.8% (9)	32.8% (20)	32.6% (28)

Majority-supported proposals. Overall, 43 or 14.4% of shareholder proposals voted on during the 2019 proxy season received majority support, up from 10.2% of proposals the prior year. The table below shows the proposals that received majority support.⁶

Proposals that Received Majority Support			
Proposal	2019	2018	2017
Eliminate/reduce supermajority voting	11	8	6
Shareholder action by written consent	7	5	3
Majority voting in director elections	5	1	4
Shareholder special meeting rights	4	5	2
Board declassification	3	4	2
Adopt proxy access	2	1	13
Board diversity	2	0	2
Employment diversity	2	0	0
Political contributions	2	0	0
Report on opioids	2	1	0
Clawback policies	1	0	0
Lobbying payments	1	0	0
Report on human rights policies	1	0	0

⁵ The numbers in the parentheticals indicate the number of times these proposals were voted on.

⁶ Voting results are reported on a votes cast basis calculated under Rule 14a-8 (votes for or against) and without regard to whether the company's voting standards take into account the impact of abstentions.

III. SHAREHOLDER PROPOSAL NO-ACTION REQUESTS

A. Overview of No-Action Requests

Submission and withdrawal rates. As shown in the table below, the 2019 proxy season saw a continued decline in the number of no-action requests submitted to the Staff, with submissions down 11% from 2018 and 21% from 2017. The submission rate—that is, the number of no-action requests as a percentage of the total number of proposals received—also continued to decline, dropping from 33% to 29% in 2019.

After an uptick in 2018, the withdrawal rate for no-action requests in 2019 remained steady at 19%. Accordingly, the government shutdown did not appear to significantly affect the rate of withdrawals. Notably, however, the shutdown may have affected the timing of withdrawals. Only six withdrawal letters were dated between December 22, 2018 and January 25, 2019, when the government was closed, compared to 14 withdrawal letters during the same period in the prior season. There were 11 withdrawal letters dated between January 26 and February 1, 2019, the week following the shutdown.

No-Action Request Statistics			
	2019	2018	2017
Total no-action requests submitted	228	256	288
Submission rate ⁷	29%	33%	35%
No-action requests withdrawn	43 (19%)	52 (20%)	41 (14%)
Pending no-action requests	5	10	5
Staff responses	180	194	242
Exclusions granted	119 (66%)	125 (64%)	189 (78%)
Exclusions denied	61 (34%)	69 (36%)	53 (22%)

Types of arguments made. In terms of the most common substantive arguments made, 110 no-action requests included an ordinary business argument, 86 included a substantial implementation argument, and 54 included a false/misleading argument. These numbers were consistent with the prior year, except that there was a 24% decline in false/misleading arguments, potentially due to the low success rate for this exclusion basis in recent years.

Success rates. This year, the Staff granted 66% of no-action requests, a slight increase from 64% in 2018. Similar to 2018, the most common grounds for the Staff to grant no-action requests were substantial implementation, representing 34% of successful requests (likely reflecting the fact that one group of prominent proponents typically refuses to withdraw its proposals even when a company implements the proposal), followed by ordinary business (31%) and procedural grounds (18%). Trends in success rates by exclusion basis were mixed. For example, the success rates for ordinary business and conflicting proposals continued to decline; but, the success rate for economic relevance continued to increase, and procedural and

⁷ Submission rates calculated by dividing the number of no-action requests submitted to the Staff by the total number of proposals submitted to companies.

substantial implementation arguments maintained about the same relatively high success rates as in 2018.

Success Rates by Exclusion Ground⁸			
Exclusion ground	2019	2018	2017
Procedural	70%	68%	79%
Substantial implementation	67%	66%	79%
Ordinary business ⁹	54%	58%	74%
Conflicting proposals	50%	88%	100%
Economic relevance	20%	14%	0%
Vague or false/misleading	5%	0%	11%

Key developments. Key developments in no-action requests this year, some of which are discussed in more detail below, include:

- **Recent Staff guidance.** The Staff issued updated guidance in October on the types of factors it expects to see in a board analysis included in an ordinary business or economic relevance argument, and also provided additional guidance on micromanagement and executive compensation-related shareholder proposals.
- **U.S. government shutdown.** It was anticipated that the U.S. federal government shutdown would have significantly disrupted the no-action letter process for the 2019 proxy season, but the actual impact appears to have been somewhat muted.
- **Ordinary business exclusions.** Companies continued to face headwinds on these requests, in part due to continued struggles with developing a sufficiently robust board analysis, but there was a significant increase in the number of successful micromanagement exclusions, in part due to the Staff's recent guidance clarifying how it analyzes such proposals.
- **Substantial implementation exclusions.** Companies continued to experience high success rates on these requests, with one-third of all successful no-action requests granted on this basis.
- **Vague or false/misleading exclusions.** Companies continued to experience very low success rates on these requests, with the Staff concurring with the exclusion of only one proposal on this basis.
- **Conflicting proposal exclusions.** Despite success in 2018 on special meeting proposals, these arguments waned in 2019 (only two such requests were submitted), partly due to recent updates to proxy advisory firm policies threatening retaliatory voting recommendations against directors at companies that exclude proposals on this basis in certain circumstances.

⁸ Success rates calculated by dividing the number of no-action requests granted on a particular ground by the total number of no-action requests granted or denied on that ground.

⁹ Excluding no-action requests that included a board analysis, the success rate was 63% in 2019 and 2018.

B. Recent Staff Guidance – Staff Legal Bulletin No. 14J

Last October, the Staff published additional guidance on shareholder proposals (Staff Legal Bulletin No. 14J (“SLB 14J”))¹⁰ covering: (1) the use of board analyses in ordinary business (Rule 14a-8(i)(7)) and economic relevance (Rule 14a-8(i)(5)) arguments; (2) ordinary business arguments based on micromanagement; and (3) ordinary business arguments in the context of proposals about senior executive and/or director compensation.

1. Updated Guidance on Board Analyses

Background. Last proxy season, in Staff Legal Bulletin 14I (“SLB 14I”)¹¹, the Staff stated that it expected certain no-action requests on the basis of ordinary business or economic relevance grounds to include a discussion, if relevant, reflecting a board of directors’ substantive analysis of a proposal’s significance to the company. However, out of 29 no-action requests that included a board analysis in 2018, in only one instance did the Staff concur with the exclusion of the proposal and reference the board’s analysis, suggesting that additional guidance was needed on the Staff’s expectations in this area.

Additional guidance on what to include in a board analysis. In SLB 14J, the Staff noted that the most helpful board discussions were the ones that “focused on the . . . specific substantive factors the board considered in arriving at its conclusion” and provided a list of potential factors to consider for this purpose, including: the extent to which the proposal relates to the company’s core business activities; quantitative data, including financial statement impact, illustrating whether or not the matter is significant to the company; whether the company has already addressed the issue in some manner, including a discussion of the differences between the proposal’s specific requests and actions already undertaken by the company and whether this “delta” represents a significant policy issue for the company; the extent of shareholder engagement on the issue and the level of shareholder interest on the matter; whether anyone other than the proponent has previously requested the information or action sought in the proposal; and voting results on any similar proposals previously voted on at the company and related facts and circumstances (such as subsequent actions taken by the company, engagement with shareholders, intervening events, and how much time has passed since the most recent vote). The Staff explained that this list is not exhaustive and that a board analysis would not necessarily need to address each factor.

Additional guidance on when a board analysis should be provided. In terms of when a board analysis should be provided, the Staff explained that it is not necessary to include a board analysis in all ordinary business and economic relevance no-action requests, but that “without having the benefit of the board’s views on the matters raised, the [S]taff may find it difficult in some instances to agree that a proposal may be excluded.” The Staff cited as an example *General Motors Co.*¹² and noted that a board analysis would be particularly helpful when “the significance of a particular issue to a particular company and its shareholders may depend on

¹⁰ See Staff Legal Bulletin No. 14J (Oct. 23, 2018), available [here](#).

¹¹ See Staff Legal Bulletin No. 14I (Nov. 1, 2017), available [here](#).

¹² See *General Motors Co.* (avail. Apr. 18, 2018) (denying relief for a proposal requesting a report on the GHG emissions impact for the company’s automobile fleet as a result of regulatory changes and specifically noting the absence of a board analysis).

factors that are not self-evident and that the board may be well-positioned to consider and evaluate.”

Impact of SLB 14J in 2019. When SLB 14J was issued, it was thought to have provided a “roadmap” that companies could use in developing an effective board analysis to exclude proposals. However, this new line of analysis has not come to fruition, despite the significant time and effort spent by companies putting together board analyses. During the 2019 proxy season, 25 no-action requests (representing 69% of all economic relevance arguments and 20% of all ordinary business arguments) included a board analysis compared to 29 the prior year. Like the 2018 proxy season, the Staff highlighted the board’s analysis in only one letter concurring that a proposal was excludable.¹³ Continuing its practice from the prior year, in two instances when denying no-action relief, the Staff specifically noted the absence of a board analysis as a factor in its decision.¹⁴

Expectations going forward. The Staff continues to reiterate that board analyses will be helpful to the Staff going forward because it believes that boards are better positioned to evaluate how significant a proposal, particularly an environmental or social proposal, is to the company. However, board analyses take time and effort to prepare and can involve logistical challenges when trying to schedule a board review in advance of the no-action request deadline. In light of this, as well as the challenging results experienced by companies during both the 2019 and 2018 proxy seasons, we would not be surprised if the use of board analyses declines in future years.

2. Clarification of Micromanagement Exclusion Framework

In SLB 14J, the Staff elaborated on the existing framework for the “micromanagement” prong of the ordinary business exclusion basis, underscoring the continued vitality of this exclusion basis. SLB 14J follows an increase in the number of no-action requests granted based on micromanagement arguments (11 in 2018, up from four in 2017, and zero in 2016 and 2015).

Framework for micromanagement analysis. The Staff reiterated that the framework for analyzing if a proposal “probe[s] too deeply into matters of a complex nature” and, thus, micromanages the company, is whether the proposal “involves intricate detail, or seeks to impose specific time-frames or methods for implementing complex policies.” As an example of a proposal that micromanages, the Staff pointed to proposals that request a plan to reach net-zero GHG emissions within a specified timeframe. We understand that the focus of the micromanagement analysis is whether the proposal attempts to dictate a specific strategy, method, or timeline, and not whether the proposal deals with highly complex issues.

Micromanagement applies to proposals calling for a report/study. The Staff also reiterated that proposals calling for a study or a report may be excludable on micromanagement grounds. The

¹³ See *Reliance Steel & Aluminum Co.* (avail. Apr. 2, 2019) (concurring in the exclusion of a political contributions report proposal on economic relevance grounds and noting “in particular the description of how [the] board of directors has analyzed [the] matter”). Notably, the company did not engage in any conduct of the type addressed in the proposal, which has traditionally been a basis for exclusion under Rule 14a-8(i)(5).

¹⁴ See *Verizon Communications Inc.* (avail. Feb. 14, 2019) (*Association of BellTel Retirees Inc.*) (noting that a board analysis would be helpful, particularly in light of the 28% of votes cast on a similar proposal the prior year); *Walgreens Boots Alliance, Inc. (Mercy Investment Services, Inc.)* (avail. Nov. 20, 2018) (noting the absence of the board’s analysis, specifically with respect to the significance of the dispensing or prior distribution of opioid products on the company’s business operations).

Staff explained that this would be the case if the proposal requested an “intricately detailed” study or report or if the underlying substance of the matters to be addressed by the study or request implicate specific timeframes or methods for implementing complex policies.

What we saw in 2019. Following SLB 14J’s release, the number of successful micromanagement exclusions almost doubled to 21 during the 2019 proxy season. One popular set of proposals for which companies made micromanagement arguments requested reports on reducing GHG emissions in the context of the Paris Climate Agreement’s objective of maintaining global warming below two degrees Celsius. The Staff generally concurred that these “2 degree” proposals were excludable when the proposal required adopting a specific strategy that would change operations,¹⁵ but denied relief when the proposal did not specify how management should implement the proposal.¹⁶ For example, compare the report requested in *Devon Energy Corp.* (“disclosure of short-, medium- and long-term greenhouse gas targets aligned with the greenhouse gas reduction goals established by the Paris Climate Agreement to keep the increase in global average temperature to well below 2 degrees Celsius and to pursue efforts to limit the increase to 1.5 degrees Celsius . . . [and] should cover both the corporation’s operations and products”), which the Staff concurred was excludable, with the report requested in *Anadarko Petroleum Corp.* (“describing if, and how, [the company] plans to reduce its total contribution to climate change and align its operations and investments” with the two degree goal), which the Staff did not concur was excludable. Notably, the Staff permitted exclusion of a proposal on micromanagement grounds where the company argued that, among other things, implementation would “inherently require[] the creation of specific, time-bound benchmarks” (even though the proposal did not on its face call for specific adoption strategies) and implicate “complex ‘choice of technology’ decisions.”¹⁷

3. When Executive Compensation Proposals Are Ordinary Business

In general, shareholder proposals addressing management of the workforce or general employee compensation and benefits are excludable as ordinary business, in contrast to proposals that focus only on executive or director compensation.¹⁸ In SLB 14J, the Staff provided further guidance around the excludability of proposals that touch upon both executive/director compensation and other matters as well as the application of the micromanagement prong of the ordinary business rule to executive/director compensation proposals.

Substance over form. SLB 14J stated that, if the focus of a proposal is on ordinary business matters, the proposal is excludable even if it also touches upon senior executive and/or director compensation matters. The Staff explained that “[i]ncluding an aspect of senior executive or director compensation in a proposal that otherwise focuses on an ordinary business matter will not insulate a proposal from exclusion.”¹⁹ As a result, assessing the applicability of this guidance to a specific proposal will necessitate an analysis of the proposal and supporting statement to determine its focus.

¹⁵ See, e.g., *Devon Energy Corp.* (avail. Mar. 4, 2019, recon. denied Apr. 1, 2019).

¹⁶ See, e.g., *Anadarko Petroleum Corp.* (avail. Mar. 4, 2019).

¹⁷ See *J.B. Hunt Transport Services, Inc.* (avail. Feb. 14, 2019) (concurring with exclusion of a proposal that requested adoption of “company-wide, quantitative targets to reduce total [GHG] emissions”).

¹⁸ See Exchange Act Release No. 40018 (May 21, 1998); Staff Legal Bulletin No. 14A (July 12, 2002).

¹⁹ See Staff Legal Bulletin No. 14J (Oct. 23, 2018).

The Staff stated that its “framework ensures that form is not elevated over substance and that a proposal is not included simply because it addresses an excludable matter in a manner that is connected to or touches upon senior executive or director compensation matters.” Nevertheless, only one shareholder proposal was excluded during the 2019 proxy season in reliance on this guidance, essentially allowing ordinary business matters to be put before shareholders when framed as relating to executive compensation policies. The Staff concurred that AT&T could exclude a proposal seeking the addition of the company’s debt rating as a performance metric in the company’s executive compensation program.²⁰ In permitting exclusion, the Staff noted that “although the [p]roposal relates to executive compensation, the focus of the [p]roposal is on the ordinary business matter of management of existing debt.” In contrast, four pharmaceutical companies were denied no-action relief with respect to shareholder proposals regarding “the extent to which risks related to public concern over drug pricing strategies are integrated into the [c]ompany’s incentive compensation policies, plans and programs for senior executives.” The Staff noted that each proposal “transcend[ed] ordinary business matters because it focuses on the performance measures used to determine awards for senior executives and on the Company’s drug pricing strategy.”²¹ Unlike the supporting statement in the debt management proposal at AT&T, which did not discuss the company’s compensation programs (suggesting that the focus of the proposal really was on the company’s debt management practices), the supporting statements in the pharmaceutical pricing proposals discussed the companies’ executive compensation programs.

Shareholder proposals involving broad-based compensation programs or policies in which executives/directors can participate. SLB 14J further clarified that proposals focusing on executive/director compensation may still be excludable as ordinary business to the extent that the following two-part test is satisfied: (1) the compensation programs or policies targeted by the proposal are broadly available or applicable to the general workforce; and (2) the executives’ or directors’ eligibility to participate “does not implicate significant compensation matters.” The Staff suggested that there may be a bias towards exclusion when the first prong of this test is satisfied.²² However, no company was able to exclude a proposal under this guidance during the 2019 proxy season and, in the three instances that were decided on the basis of this test, the Staff did not permit exclusion because the company failed to address the *second* prong in its no-action request.²³

Executive compensation shareholder proposals that micromanage. Historically, the Staff did not view executive compensation proposals as excludable on the basis of micromanagement. In SLB 14J, the Staff announced that going forward it would treat executive compensation

²⁰ See *AT&T Inc. (Third Generational Financial LLC)* (avail. Jan. 29, 2019).

²¹ See, e.g., *Bristol-Myers Squibb Co.* (avail. Mar. 8, 2019).

²² See Staff Legal Bulletin No. 14J (Oct. 23, 2018) (“it is difficult to conclude that a proposal does not relate to a company’s ordinary business when it addresses aspects of compensation that are broadly available or applicable to a company’s general workforce, even when the proposal is framed in terms of the senior executives and/or directors”).

²³ See *New York Community Bancorp, Inc.* (avail. Apr. 11, 2019) (“you have not demonstrated that the [proposal] does not implicate significant compensation matters”); *Verizon Communications Inc.* (avail. Feb. 15, 2019) (noting the absence of a discussion of the second prong); *Verizon Communications Inc. (Association of BellTel Retirees Inc.)* (avail. Feb. 14, 2019) (“we note the absence of the board’s analysis addressing whether the Proposal implicates a significant compensation matter to the Company’s shareholders”).

proposals the same as other proposals such that if an executive compensation proposal “seek[s] intricate detail, or seek[s] to impose specific timeframes or methods for implementing complex policies” it can be excluded on the basis of micromanagement. During the 2019 proxy season, five proposals were excluded based on this guidance.²⁴

C. Impact of U.S. Government Shutdown

On December 22, 2018, the U.S. federal government, including the SEC, partially shut down when Congress was unable to come to an agreement on an appropriations bill for the 2019 fiscal year. The shutdown lasted 35 days, making it the longest in U.S. history. Although it seemed at the time that the shutdown would have a significant impact on the no-action letter process, the Staff was able to make significant progress once the government reopened on January 25, 2019 and managed to issue 85% of the no-action letters by the end of March. As a result, the impact on the no-action letter process was to shift the bulk of the decisions towards the end of the first quarter from what is typically a fairly even distribution throughout the first few months of the year. The table below compares the number of no-action letters issued by the Staff from October to May during the 2019 and 2018 proxy seasons.

Month	No-Action Letters Issued			
	2019	% of Total	2018	% of Total
October	1	0.4%	3	1.2%
November	8	3.6%	2	0.8%
December	12	5.4%	25	10.2%
January	15	6.7%	58	23.6%
February	70	31.4%	66	26.8%
March	83	37.2%	71	28.9%
April	32	14.3%	19	7.7%
May	2	0.9%	2	0.8%

The shutdown also did not appear to have much of an impact on no-action request withdrawals. As noted above, the withdrawal rate for the 2019 proxy season remained about the same as the prior year.

Where the shutdown may have had the biggest impact is on companies’ front-end decisions of whether to submit a no-action request at all versus attempting to negotiate a withdrawal of the proposal or letting it go to a vote. Some proposals that otherwise would have been challenged may not have been due to expected delays from the Staff as a result of the shutdown.²⁵ This is consistent with the year-over-year trends discussed above regarding the decline in the no-action

²⁴ See, e.g., *General Electric Co.* * (avail. Mar. 5, 2019) (request to hire an accounting firm to review the compensation of the 25 highest paid individuals for specified years to determine whether recoupment is appropriate and report on recoupment decisions).

²⁵ See, e.g., Anthem, Inc. 2019 Proxy Statement (Mar. 29, 2019), available [here](#) (“We believe that the Company has substantially implemented this shareholder proposal and thus it does not qualify for inclusion in these proxy materials under SEC rules. However, due to the impact of the federal government shutdown on the SEC, we did not believe that the SEC could respond to a no-action request to exclude this shareholder proposal on the basis of substantial implementation before the deadline to distribute these proxy materials. Therefore, the Board of Directors recommends that shareholders approve the Company’s Director Election Proposal set forth in Proposal No. 4 and makes no recommendation on this shareholder proposal” (emphasis added)).

request submission rate (from 33% to 29% in 2019) and increase in the proposal withdrawal rate (from 15% to 20% in 2019). While there are other, larger shareholder proposal dynamics driving these trends, we suspect that the shutdown played a small role.

IV. KEY SHAREHOLDER PROPOSAL TOPICS DURING THE 2019 PROXY SEASON

A. *Environment*

Although environmental shareholder proposals continued to be popular during the 2019 proxy season, the number submitted decreased significantly, from 139 proposals in 2018 to 109 in 2019. Average support for these proposals decreased from 30.5% in 2018 (38 proposals) to 24.5% in 2019 (22 proposals).

Climate change proposals. As was the case in 2018, the largest group of environmental shareholder proposals related to climate change, with 48 submitted in 2019 (down from 72 in 2018). The 11 climate change proposals voted on in 2019 averaged support of 26.6% (down from 32.8% in 2018). No climate change-related proposals received majority support in 2019 (compared to four in 2018). Of the climate change proposals that were voted on, nine requested reports on reducing GHG emissions (averaging 30.8% support) (of which seven referred to the Paris Climate Agreement’s objective of maintaining global warming below two degrees Celsius), and two requested the establishment of a board committee on climate change (averaging 7.5% support). Of the nine proposals requesting reports on reducing GHG emissions that were voted on, six requested the adoption of specific goals or targets to achieve GHG reduction. ISS supported 83% of climate change proposals in 2019 (including all proposals requesting reports on reducing GHG emissions) compared to 90% in 2018. Notably, almost half of the 2019 climate change proposals were withdrawn, up from approximately 26% in 2018, signaling a continued trend in companies’ willingness to discuss reasonable means to address these proposals. Withdrawn proposals included those related to reducing GHG emissions, assessing portfolio impacts to meet the two degrees Celsius scenario, and evaluating transition risks and opportunities related to climate change.

Other proposals. Other popular environmental proposals included: 22 proposals requesting sustainability reports, with only one proposal voted on, receiving 28.2% support (16 of these proposals were withdrawn, three did not appear in the proxy, and two were excluded); 16 proposals focusing on the environmental impact in communities (e.g., supply chain impacts on deforestation, health risks from coal use, food waste policies, etc.), with six proposals averaging 22.2% support; and, new for 2019, four proposals requesting reports on efforts to reduce plastic pollution, with three withdrawn after the companies agreed to implement the proposals.²⁶

²⁶ See, e.g., “Second Large Plastics Manufacturer — Chevron Phillips Chemical — Agrees to Report on Plastic Pollution Pellet Spills,” As You Sow (Apr. 9, 2019), available [here](#).

B. Human Capital Management

Against a backdrop of increasing investor focus,²⁷ shareholder proposals focused on how companies manage their human capital continued to be popular during the 2019 proxy season, with shareholders submitting 66 proposals (up from the 62 submitted in 2018). The main focus areas of these proposals included gender pay equity, employment diversity, equitable employment practices and policies (with this year’s focus primarily on mandatory arbitration policies), and sexual harassment. Excluding shareholder proposals requesting a review of company sexual harassment policies (which proposals were new for 2019 and are discussed below), average support for these proposals decreased slightly to 34.9% (16 proposals) compared to 35.9% in 2018 (eight proposals), with ISS supporting all but one of these proposals.

Gender pay equity proposals. Shareholder proposal campaigns calling for a report on the size of a company’s gender pay gap and policies and goals to reduce that gap increased in prominence during the 2019 proxy season. Shareholders submitted 28 proposals (up from 24 in 2018)—with Arjuna Capital responsible for at least 12 of them—again targeting financial services and, increasingly, technology companies. Nine of these proposals were voted on, receiving average support of 28.2% (up from 15.1% for the one proposal voted on in 2018). The notable trend this year was a shift in the proposals’ focus from reporting on an adjusted basis to an unadjusted basis. Specifically, unlike previous “equal pay for equal work” shareholder proposals that requested wage gap information for comparable jobs (i.e., what women are paid compared to their most directly comparable male peers, adjusted for seniority, geography, and other factors), the 2019 Arjuna shareholder proposal targeted unadjusted pay gaps, which are driven by female representation among the higher-paid employee ranks.

In contrast to 2018, when at least 10 companies agreed to report their adjusted pay gaps, this year only two companies publicly agreed to implement the shareholder proposal on unadjusted pay gaps (Citigroup and Pfizer). An adjusted pay gap often refers to “equal pay for equal work,” whereas an unadjusted pay gap measures whether women and ethnic minorities are holding high-paying positions. Citigroup, which reported an adjusted pay gap last year, reported on both an adjusted and unadjusted basis this year.²⁸

Employment diversity proposals. The number of employment diversity proposals submitted decreased to 15 in 2019 (compared to 23 in 2018). These proposals generally requested a report on the company’s employment diversity and related diversity policies. While the overall number of these proposals decreased, support increased with the six voted on in 2019 averaging 45% support (compared to 38.8% in 2018) and two receiving majority support. In addition, a significant portion of these proposals were withdrawn after negotiations with the proponent.²⁹

²⁷ See, e.g., “BlackRock Investment Stewardship—Protecting our and enhancing our clients’ assets for the long term,” BlackRock (Jan. 2019), available [here](#) (listing human capital as one of BlackRock’s five engagement priorities for 2019); “Institutional Investor Survey 2019,” Morrow Sodali (Feb. 2019), available [here](#) (noting that 83% of investors surveyed would like to see more disclosure around human capital management); “Aligning Corporate Culture with Long-Term Strategy,” State Street Global Advisors (Jan. 15, 2019), available [here](#).

²⁸ See Sara Wechter, “Global Pay Equity at Citi,” Citigroup Blog (Jan. 16, 2019), available [here](#).

²⁹ See, e.g., “Shareholder Proposals—Workplace Diversity,” Trillium Asset Management, available [here](#) (listing the outcomes of the workplace diversity proposals it submitted to companies).

Sexual harassment proposals. Against the backdrop of the #MeToo movement, the 2019 proxy season saw sexual harassment reporting emerge as a new proposal topic. These proposals requested a review of the company’s sexual harassment policies. Of the 10 proposals submitted, six have been voted on, averaging 12.9% support. ISS’ recommendations were mixed on these proposals, but ISS generally supported those proposals calling for a review of the company’s workplace sexual harassment policies in connection with related high-profile incidents involving company employees. At these three companies, the proposals averaged 20.7% support.

C. Board Diversity

What we saw this year. Board diversity continued to be a hot button issue. During the 2019 proxy season, shareholders submitted 47 proposals requesting the adoption of a board diversity policy or a report on board diversity (up more than 50% from 30 proposals in 2018). Excluding “ideological diversity” proposals (a recent variant of board diversity proposals discussed below), the two proposals voted on in 2019 averaged support of 69.0% (up significantly from 24.5% for three proposals in 2018), with both receiving majority support (compared to zero in 2018). ISS supported both of these proposals. Continuing the trend from prior years, a significant number of board diversity proposals (45%) were withdrawn. We expect continued momentum on these proposals in light of the increased focus on board diversity by investors,³⁰ proxy advisors,³¹ and state and federal governments.³²

“Ideological diversity” proposals. The 2019 proxy season saw an increase in the number of proposals focusing on ideological perspectives rather than characteristics such as gender, race, or ethnicity. Of the eight proposals submitted for 2019 (up from two in 2018), five were voted on, averaging 2.0% support, and ISS recommended votes against all of them.

D. Corporate Governance

During the 2019 proxy season, the most common governance proposals were proxy access, special shareholder meeting rights, supermajority voting, shareholder written consent rights, and independent board chairs. As noted above, the focus this year shifted away from proxy access and shareholder special meeting rights given the widespread adoption of these rights among the S&P 500.

³⁰ See, e.g., “Larry Fink’s 2019 Letter to CEOs—Purpose & Profit,” BlackRock (Jan. 2019), available [here](#) (listing board diversity as one of BlackRock’s five engagement priorities for 2019).

³¹ See, e.g., “2019 Proxy Paper Guidelines,” Glass Lewis, available [here](#) (highlighting new policy for 2019 where it will recommend votes against nominating committees at boards without at least one female).

³² See, e.g., Vanessa Fuhrmans, “California Becomes First State to Mandate Female Board Directors,” Wall Street Journal (Sept. 30, 2018), available [here](#); Zachary Warmbrodt, “House Democrats to push for more diversity in top corporate ranks,” Politico (Jan. 1, 2019), available [here](#).

1. Proxy Access

<u>Major Proponents</u>	<u>S&P 500 Adoption Rate</u>	<u>YoY³³ Proposal Trend</u>	<u>Proposal Statistics</u>			
<ul style="list-style-type: none"> Chevedden & associates NYC Comptroller 	<p>>75% (as of June 2019)</p>	<p>↓</p>				
<u>Key Takeaways</u>						
<ul style="list-style-type: none"> As proxy access has become majority practice in the S&P 500, proxy access proposals continue to wane “Amend” proposals still do not appear to have gained much traction with big investors 						
				2019	2018	2017
			<i>Total # submitted</i>	38	48	112
			Adopt Proxy Access			
			<i># voted on</i>	4	5	18
			<i>Average support</i>	53.2%	34.8%	62.1%
			<i># majority support</i>	2	1	13
			Amend Proxy Access			
			<i># voted on</i>	18	21	20
			<i>Average support</i>	28.3%	28.0%	28.5%
			<i># majority support</i>	0	0	0

2. Shareholder Right to Call a Special Meeting

<u>Major Proponents</u>	<u>S&P 500³⁴ Adoption Rate</u>	<u>YoY Proposal Trend</u>	<u>Proposal Statistics</u>			
<ul style="list-style-type: none"> Chevedden & associates 	<p>~65% (as of June 2019)</p>	<p>↓</p>				
<u>Key Takeaways</u>						
<ul style="list-style-type: none"> After a dramatic increase in 2018, these proposals declined in 2019 as more companies have adopted or lowered the threshold for these provisions “Lower” proposals appear to be gaining some traction 						
				2019	2018	2017
			<i>Total # submitted</i>	32	75	27
			Adopt Special Meeting Right			
			<i># voted on</i>	1	16	10
			<i>Average support</i>	42.4%	44.9%	42.8%
			<i># majority support</i>	0	2	1
			Lower Threshold			
			<i># voted on</i>	21	35	5
			<i>Average support</i>	44.4%	39.5%	43.2%
			<i># majority support</i>	4	3	1

3. Supermajority Voting

<u>Major Proponents</u>	<u>S&P 500 Adoption Rate</u>	<u>YoY Proposal Trend</u>	<u>Proposal Statistics</u>			
<ul style="list-style-type: none"> Chevedden & associates 	<p>>50% (as of June 2019)</p>	<p>↑</p>				
<u>Key Takeaways</u>						
<ul style="list-style-type: none"> Proposals have doubled over the last two years Average support levels remain among the highest 						
				2019	2018	2017
			<i>Total # submitted</i>	41	24	20
			<i># excluded (i(10))</i>	13	9	5
			<i># voted on</i>	14	8	7
			<i>Average support</i>	65.7%	74.7%	64.3%
			<i># majority support</i>	11	8	6

³³ “YoY” refers to year-over-year.

³⁴ Includes all companies that permit shareholders to call a special meeting, regardless of the requisite ownership threshold specified in the bylaws.

4. Shareholder Right to Act by Written Consent

<u>Major Proponents</u>	<u>S&P 500 Adoption Rate</u>	<u>YoY Proposal Trend</u>	<u>Proposal Statistics</u>			
<ul style="list-style-type: none"> Chevedden & associates 	<p>~30%</p> <p>(as of June 2019)</p>	<p>↑</p>				
<u>Key Takeaways</u>						
<ul style="list-style-type: none"> High number of submissions, with shareholder focus returning to written consent after success of other campaigns (e.g., proxy access, special meetings) Although average support has declined, the number of majority-supported proposals has increased 						
			<i>Total # submitted</i>	2019	2018	2017
			<i># excluded (i(10))</i>	42	42	15
			<i># voted on</i>	3	1	0
			<i>Average support</i>	32	33	12
			<i># majority support</i>	39.1%	41.8%	45.6%
				7	5	3

5. Independent Board Chair

<u>Major Proponents</u>	<u>S&P 500 Adoption Rate</u>	<u>YoY Proposal Trend</u>	<u>Proposal Statistics</u>			
<ul style="list-style-type: none"> Chevedden & associates SumOfUs Teamsters 	<p>>30%</p> <p>(as of May 2018)³⁵</p>	<p>↑</p>				
<u>Key Takeaways</u>						
<ul style="list-style-type: none"> Steady increase in number of proposals over last few years Support levels have held steady around ~30% as no investor consensus as to “best” leadership structure 						
			<i>Total # submitted</i>	2019	2018	2017
			<i># voted on</i>	64	51	47
			<i>Average support</i>	46	33	30
			<i># majority support</i>	28.7%	32.0%	30.4%
				0	0	0

V. OTHER SHAREHOLDER PROPOSAL DEVELOPMENTS

A. Proponents’ Use of Litigation

Although in the past, both companies³⁶ and shareholder proponents³⁷ have used litigation as a tactic in dealing with shareholder proposals, including to challenge Staff decisions with respect to no-action requests, during the 2019 proxy season one proponent took the unusual step of seeking to enjoin a company from omitting the proponent’s proposal *before* the Staff issued its response to a pending no-action request.

³⁵ See “2018 United States Spencer Stuart Board Index,” Spencer Stuart (2018), available [here](#).

³⁶ See, e.g., *Waste Connections, Inc. v. Chevedden*, No. 4:13-cv-00176 (S.D. Tex. June 3, 2013), *aff’d* 2014 U.S. App. LEXIS 2731 (5th Cir. Feb. 13, 2014); *KBR, Inc. v. Chevedden*, 2011 U.S. Dist. LEXIS 36431 (S.D. Tex. Apr. 4, 2011), *aff’d* 478 F. App’x. 213 (5th Cir. June 11, 2012); *Apache Corp. v. Chevedden*, 696 F. Supp. 2d 723 (S.D. Tex. 2010).

³⁷ See, e.g., *Trinity Wall Street v. Wal-Mart Stores, Inc.*, No. 14-4764 (3d Cir. July 6, 2015); Amended Complaint, *Silberstein v. Aetna, Inc.*, No. 1:13-CV-08759 (AJN) (S.D.N.Y. Mar. 3, 2014).

Background on the proposal. In September 2018, the New York City Comptroller, on behalf of the New York City Employees' Retirement System and other pension funds overseen by the Comptroller, submitted a shareholder proposal to TransDigm requesting that TransDigm adopt a "policy with time-bound, quantitative, company-wide goals for managing GHG emissions, taking into account the objectives of the Paris Climate Agreement," and issue a report on its plans to meet these targets. In November 2018, TransDigm filed a no-action request seeking to exclude the proposal as ordinary business on the theory that the proposal would micromanage the company.³⁸

The Comptroller takes TransDigm to court. While TransDigm's no-action request was pending, on December 5, 2018, the Comptroller filed a complaint in the Southern District of New York seeking to enjoin TransDigm from soliciting proxies without including the proposal and requesting the District Court provide declaratory relief that the exclusion of the proposal violated the proxy rules. In its complaint, the Comptroller argued that its submission was sufficient to establish the proposal's proper inclusion and claimed that the ordinary business exclusion rule did not apply to the proposal. Notably, the Comptroller argued that the no-action process "merely serves as an informal means for the company and the proponent to learn the Division's non-binding view on the company's planned omission of the proposal."³⁹ Instead of responding directly to TransDigm's no-action request, on December 7, 2018, the Comptroller advised the Staff that it was seeking injunctive relief from the District Court and requested that the Staff "follow its prior practice and decline to issue any response to TransDigm's no-action request" while the litigation was pending.⁴⁰

TransDigm's response. On December 28, 2018, TransDigm withdrew its no-action request and notified the Staff that it intended to include the Comptroller's proposal in its proxy materials. TransDigm and the Comptroller settled the litigation in January 2019. Notably, despite the Comptroller successfully leveraging the threat of costly and prolonged litigation and the additional publicity generated by the Comptroller's litigation,⁴¹ the Comptroller's proposal failed to pass, receiving support from 34.3% of votes cast at TransDigm's annual meeting.

B. SEC Defers on Legality of Corporate Law Proposal

As described above, both companies and shareholder proponents have in the past turned to litigation in connection with, or in some cases in the place of, the SEC no-action process. During the 2019 proxy season, a proponent turned to litigation to seek legal support for a proposal implicating state corporate law.

Background on the proposal. In February 2019, the Staff concurred with the exclusion of a shareholder proposal submitted to Johnson & Johnson that sought to require that its board of

³⁸ See *TransDigm Group Inc.* (avail. Jan. 28, 2019).

³⁹ See Complaint, *The New York City Employees' Retirement System v. TransDigm Group, Inc.*, No. 1:18 CV 11344 (KPF) (S.D.N.Y. Dec. 5, 2018).

⁴⁰ See *TransDigm Group Inc.* (avail. Jan. 28, 2019).

⁴¹ See, e.g., Lydia DePillis, "Shareholder activism is on the rise, but companies are fighting back," CNN (Jan. 31, 2019), available [here](#); Rachel Abbey McCafferty, "Activist shareholders push TransDigm on greenhouse gas," Crain's Cleveland Business (Feb. 24, 2019), available [here](#); Robert Steyer, "NYC pension funds settle suit against aerospace company," Pensions & Investments (Jan. 24, 2019), available [here](#).

directors adopt a mandatory arbitration bylaw for shareholder disputes with the company.⁴² In its no-action request, the company argued that the implementation of the mandatory arbitration bylaw would cause the company to violate both federal and New Jersey state law, and thus was properly excludable under Rule 14a-(8)(i)(2).⁴³ In support of its state law argument, in addition to the typical opinion from local counsel, Johnson & Johnson provided the Staff with a letter from the New Jersey Attorney General who opined that the proposal would cause the company to violate “[l]ongstanding principles of New Jersey law [which] limit the subject matter of corporate bylaws to matters of internal concern to the corporation.” The Staff concurred that the proposal was properly excludable and indicated that the Attorney General’s letter was “a legally authoritative statement that [the Staff is] not in a position to question.”

The proponent turns to the courts. In March 2019, the shareholder proponent filed suit in the District of New Jersey arguing that implementing the proposal would not cause Johnson & Johnson to violate state law.⁴⁴ After Johnson & Johnson filed a motion to dismiss the proponent’s complaint, two pension funds—the California Public Employees’ Retirement System (CalPERS) and Colorado Public Employees’ Retirement Association (PERA)—separately filed motions to intervene and thereafter motions to dismiss the proponent’s complaint.⁴⁵ Both CalPERS and PERA indicated that the funds were motivated to intervene because neither Johnson & Johnson nor the shareholder proponent represents the interests of institutional shareholders.⁴⁶ It remains unclear how the case will ultimately be resolved, but, like the TransDigm case above, it may result in more proponents determining to litigate in the future.

C. Proponents’ Use of Exempt Solicitation Filings

During the 2019 proxy season, exempt solicitation filings proliferated as proponents continued to use them as a means of generating greater publicity for their proposals (and other issues) in advance of the shareholders meeting. As of July 1, 2019, there were a record-high 170 filings since the beginning of the calendar year, up from 140 and 120 as of the same dates in 2018 and 2017, respectively.

Background on PX14A6G filings. Under Rule 14a-6(g), larger shareholders (owning more than \$5 million of a company’s securities) generally are required to file with the SEC a Notice of Exempt Solicitation (an “Exempt Notice”) when soliciting other shareholders on a topic. The rule was adopted as part of a set of rules that exempted certain solicitations from the proxy filing requirements and was designed to address concerns that institutional investors and other large

⁴² See *Johnson & Johnson* (avail. Feb. 11, 2019, *recon. denied* Feb. 22, 2019).

⁴³ Johnson & Johnson argued that implementation of the bylaw would cause the company to violate federal law on the grounds that the mandatory arbitration bylaw would “weaken the ability of investors in Johnson & Johnson’s securities to pursue a private right of action under Exchange Act Section 10(b) and Rule 10b-5.”

⁴⁴ See Complaint, *The Doris Behr 2012 Irrevocable Trust v. Johnson & Johnson*, No. 3:19-CV-08828 (MAS) (LHG) (D.N.J. Mar. 21, 2019) (arguing that “neither Johnson & Johnson nor the New Jersey Attorney General has identified any New Jersey statute or court decision that prohibits the enforcement of the arbitration agreements”).

⁴⁵ See Motion to Dismiss, *The Doris Behr 2012 Irrevocable Trust v. Johnson & Johnson*, No. 3:19-CV-08828 (MAS) (LHG) (D.N.J. May 31, 2019).

⁴⁶ See Alison Frankel, “J&J, pension funds file tag-team dismissal motions in shareholder arbitration case,” Reuters (June 3, 2019), available [here](#).

shareholders would conduct “secret” solicitations. This Exempt Notice appears on the company’s EDGAR page as a PX14A6G filing and sets forth all written materials used in the solicitation. However, in recent years, these filings have primarily been used by smaller shareholders to publicize their views on various proposals. In this regard, in 2019, more than 60% of Exempt Notices were identified as voluntary filings by shareholders who do not meet the \$5 million ownership threshold. As a result, these filings are being used in a manner that is inconsistent with Rule 14a-6(g) and can be confusing to shareholders when evaluating the items to be voted on.

Recent SEC guidance. In July 2018, the Staff released two new Compliance and Disclosure Interpretations (“C&DIs”)⁴⁷ that attempted to address some of the concerns around Exempt Notices.

- **The first C&DI** takes the position that “voluntary” Exempt Notices are permitted to be filed by a shareholder who does not meet the \$5 million threshold, but the filer must specifically state that the Exempt Notice is being provided on a voluntary basis, which the Staff claims will alert investors that the filer does not beneficially own more than \$5 million of the company’s stock.
- **The second C&DI** clarifies that all Exempt Notices must include a cover page setting forth the information required under Rule 14a-103 (generally the name and address of the soliciting party as well as the name of the company to which the filing relates), which must come before any written soliciting materials, and that a failure to do so may be considered materially misleading under Rule 14a-9.

Continued potential for abuse. Notwithstanding the new C&DIs, there continue to be a number of problematic practices in connection with voluntary filings of Exempt Notices. Aside from the problem of filers who do not include the required cover page (approximately 25% of PX14A6G filings did not have the requisite cover page in 2019),⁴⁸ there are several ongoing issues that the C&DIs do not address. First, it is unclear the magnitude of the filer’s ownership position, or whether the filer is in fact a shareholder at all, because the filer’s stock ownership is not required to be disclosed (other than to indicate whether or not the filer crosses the \$5 million threshold). Although ownership disclosure is not required under the rule, there is no indication that the SEC anticipated that shareholders who did not meet the \$5 million threshold would be permitted to use the notice as a platform for disseminating their solicitations. Second, although the C&DIs affirmed that Exempt Notices must not be materially false or misleading, there still is no practical and timely recourse for companies when such filings contain materially false or misleading information as the Staff, as a matter of policy, continues to refuse to remove them from EDGAR, and even if the Staff contacts a filer about false or misleading statements, requiring the filing of a correction risks giving the voluntary filers even greater prominence.

As long as the SEC continues to permit shareholders who do not meet the \$5 million ownership threshold to make these filings, we expect their use among proponents to continue to grow in coming years given the broad dissemination of, and publicity generated by, such filings. We

⁴⁷ See Questions 126.06 and 126.07 of the Staff Proxy Rules and Schedules 14A/14C Compliance and Disclosure Interpretations (July 31, 2018), available [here](#).

⁴⁸ We understand from the Staff that they review Exempt Notices, are aware of the compliance issues, and have contacted non-compliant filers.

recommend companies actively monitor their EDGAR feed for these filings and, to the extent they believe an exempt solicitation filing contains materially false or misleading information, or may not have been filed by a shareholder of the company, they should inform the Staff.

VI. POTENTIAL REFORM OF THE SHAREHOLDER PROPOSAL RULES

The 2019 proxy season saw continued momentum to amend the shareholder proposal rules.

A. SEC Proxy Process Roundtable

In November 2018, the Staff held a roundtable (the “Roundtable”) to provide an opportunity for market participants to engage with the Staff on various aspects of the proxy process.⁴⁹ The Roundtable covered a number of topics, including the shareholder proposal rule, voting process, retail shareholder participation, and regulation of proxy advisors. With respect to the shareholder proposal rule, Roundtable participants disagreed on the benefits of shareholder proposals and debated whether eligibility requirements should be increased.

In December 2018, Chairman Clayton provided an update on SEC rulemaking initiatives and noted that a “significant initiative for 2019 is improving the proxy process.”⁵⁰ In his speech, the Chairman called for a review of the thresholds for the submission and resubmission of shareholder proposals, stating that the “current \$2,000 ownership threshold was adopted 20 years ago, and the resubmission thresholds have been in place since 1954.”⁵¹ Chairman Clayton further noted that any changes to these thresholds need to consider the interests of the long-term retail investors who invest directly in public companies and indirectly through mutual funds, ETFs, and other products, and that the SEC should consider if there are factors in addition to these thresholds “that reasonably demonstrate that the proposing shareholder’s interests are aligned with those of a company’s long-term investors.”

B. SEC Efforts

In February 2019, Chairman Clayton announced that Commissioner Elad Roisman would lead the SEC’s efforts to improve the proxy voting process and infrastructure.⁵² In a March 2019 speech regarding the SEC’s review of its rules governing the proxy process,⁵³ Commissioner Roisman indicated that he, like Chairman Clayton, was interested in reviewing the current thresholds for the submission and resubmission of shareholder proposals, with a focus on “achiev[ing] a balance . . . [to] allow for robust shareholder engagement without providing a

⁴⁹ See “Spotlight on Proxy Process,” SEC (Nov. 15, 2018), available [here](#).

⁵⁰ See “SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks,” Chairman Jay Clayton (Dec. 6, 2018), available [here](#).

⁵¹ The SEC’s current resubmission thresholds allow a company to exclude proposals that were voted on at the company in the past five years and most recently received less than 3% if voted on once, 6% if voted on twice, and 10% if voted on three times.

⁵² See “Remarks for Telephone Call with SEC Investor Advisory Committee Members,” Chairman Jay Clayton (Feb. 6, 2019), available [here](#).

⁵³ See “Keynote Remarks: ICI Mutual Funds and Investment Management Conference,” Commissioner Elad L. Roisman (Mar. 18, 2019), available [here](#).

mechanism for certain shareholders with idiosyncratic views to use the shareholder proposal system in a way that does not benefit the interests of the majority of long-term shareholders.”

Another area Commissioner Roisman expressed interest in reviewing is the SEC’s current view towards “proposal by proxy,” which is when a shareholder delegates authority to a proxy to submit a proposal on its behalf. He acknowledged the Staff’s recent affirmation that a shareholder’s submission of a proposal by proxy is permissible as long as the submission is consistent with Rule 14a-8,⁵⁴ but wants to “understand how it is in the long-term interest of shareholders to allow this practice, when the proponent either is not a shareholder or cannot qualify to bring the proposal on his or her own.”

C. Reg Flex Agenda

In May 2019, the SEC released its Spring 2019 Regulatory Flexibility Agenda (the “Reg Flex Agenda”).⁵⁵ The Reg Flex Agenda identifies rulemaking projects that the SEC expects to address, and classifies those projects as being either in the “Proposed & Final Rule Stages” (which the SEC expects to propose or adopt during the coming year) or the “Long-Term Actions” stage (which the SEC is more likely to address over a longer timeframe). With respect to those rulemaking projects identified as being in the “Proposed & Final Rule Stages,” the Reg Flex Agenda reflects Chairman Clayton’s approach to be more focused than under prior Commissions and to list “(1) what initiatives the agency could reasonably expect to complete over the next 12 months and (2) of those initiatives, which ones would have the most positive impact on our Main Street investors.”⁵⁶

Notably, the Reg Flex Agenda for the first time included amending the shareholder proposal thresholds and indicated that the SEC expects to address this through rulemaking over the coming year (as opposed to a longer timeframe). As is typical, the SEC did not provide any additional guidance for these items, but as discussed above, it is generally expected that the SEC rule proposals will include increasing the ownership and resubmission thresholds for shareholder proposals, as well as related issues such as proposals by proxy.

In July 2019, at an event held by the Center for Capital Markets Competitiveness of the U.S. Chamber of Commerce, both Chairman Clayton and the Director of the SEC’s Division of Corporation Finance William Hinman spoke on the Rule 14a-8 process and the need to assess the ownership and resubmission thresholds.⁵⁷ Noting that the resubmission thresholds have not been updated since 1954, Chairman Clayton stated “it’s probably time to take a look” at how those rules should be modernized. Suggesting that he also believes the current thresholds are out-of-date, Director Hinman noted that the current resubmission shareholder proposals are “reflective of a different era when it was harder to get momentum on issues” and are “pretty low bars.” Similarly, Director Hinman posited that the submission thresholds, which have not been updated

⁵⁴ See Staff Legal Bulletin No. 14I (Nov. 1, 2017), available [here](#).

⁵⁵ See “Agency Rule List - Spring 2019: Securities and Exchange Commission,” Office of Information and Regulatory Affairs (2019), available [here](#).

⁵⁶ See “SEC Rulemaking Over the Past Year, the Road Ahead and Challenges Posed by Brexit, LIBOR Transition and Cybersecurity Risks,” Chairman Jay Clayton (Dec. 6, 2018), available [here](#).

⁵⁷ See “Corporate Governance: Making the Case for Reform” Chairman Jay Clayton and Director William Hinman (Jul. 16, 2019), available [here](#).

since 1998 and have not been adjusted for inflation, do not “necessarily reflect a meaningful stake in a company.” Director Hinman indicated that the SEC still wants smaller shareholders to have a voice in the process and, accordingly, the SEC is evaluating thresholds based on the amount held and how long it has been held to create “a more meaningful ticket to entry in the 14a-8 process.”

D. Possible Changes to No-Action Request Process

In addition to discussing the ownership and resubmission thresholds at the July 2019 Chamber of Commerce event, Director Hinman also previewed possible changes to the Rule 14a-8 no-action request process, including the possibility that the Staff may not provide a formal response to every submitted Rule 14a-8 no-action request.

Director Hinman explained that, unlike with respect to other no-action requests, the SEC has historically provided a formal response to every Rule 14a-8 no-action request. However, Director Hinman indicated that while the SEC intends to continue to “actively monitor” the Rule 14a-8 no-action request process, going forward the Staff will consider whether every Rule 14a-8 no-action request needs a formal response “in the same way that [the Staff] may not give a formal response on a Rule 144A request.” In considering whether to issue a formal response, Director Hinman suggested the SEC will consider whether the SEC is “adding value” through its response. Chairman Clayton voiced his support for Director Hinman’s remarks explaining that the shareholder proposal rules are “designed to promote company and shareholder engagement.” Chairman Clayton indicated that if the shareholder proposal rules are being used either by companies or shareholders to inhibit engagement, the Staff needs to ask whether its rules are “driving the right way” to enhance company-shareholder engagement.

Traditionally, both companies and shareholder proponents have looked to the Staff as a neutral arbiter in the Rule 14a-8 no-action request process, and the issuance of formal responses has provided transparency to the process. In response to Director Hinman’s recent comments, representatives of both sides have voiced concern that selective responses to Rule 14a-8 no-action requests could frustrate the company-shareholder engagement process and lead to more uncertainty about how companies may properly exclude shareholder proposals.⁵⁸

If the SEC does ultimately retreat from its role in the Rule 14a-8 no-action request process, companies and shareholder proponents will be deprived of the main avenue for resolution of disputes over shareholder proposals. While both companies and shareholder proponents have in the past turned to litigation in connection with, or in some cases in the place of, the SEC no-action process, recourse to the courts is costly for both sides and the process is often too slow.

⁵⁸ See Andrea Vittorio, “SEC May Curb Review of Contested Shareholder Proposals,” Bloomberg Law (Jul. 16, 2019), available [here](#).

Moreover, in light of voting policies of both ISS⁵⁹ and Glass Lewis⁶⁰, companies face increasing pressure to either include shareholder proposals or negotiate their withdrawal. We will continue to monitor this area and keep our clients apprised as developments emerge.

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⁵⁹ ISS has stated, “[U]nder our governance failures policy, ISS will generally recommend a vote against one or more directors (individual directors, certain committee members, or the entire board based on case-specific facts and circumstances), if a company omits from its ballot a properly submitted shareholder proposal when it has not obtained” a voluntary withdrawal, a no-action letter, or a court ruling supporting exclusion of the proposal. See U.S. Proxy Voting Research Procedures & Policies (Excluding Compensation-Related) Frequently Asked Questions (Aug. 13, 2018), FAQ 67, available [here](#).

⁶⁰ Glass Lewis has indicated that if it determines that the exclusion of a shareholder proposal is “detrimental to shareholders” it may recommend against directors serving on the board’s governance committee. See “2019 Proxy Paper Guidelines,” Glass Lewis, available [here](#).