As a concerned shareowner I have seen SEC Rule 14a-8(i)(9) used many times by entrenched boards to block reform efforts by investors. I hope the SEC-IAC will recommend amendments to the Commission. The current language is problematic. Below I explain why, using my recent proposal at Disney to allow shareowners to call a special meeting as an example and I outline how the rule might be changed to avoid silencing shareowners. Here's the text of the SEC rule:

SEC Rule 14a-8(i)(9) *Conflicts with company's proposal:* If the proposal directly conflicts with one of the company's own proposals to be submitted to shareholders at the same meeting;

Note to paragraph (*i*)(9): A company's submission to the Commission under this section should specify the points of conflict with the company's proposal.

Right now at Disney, shareowners cannot call a special meeting, even in the case of an obvious emergency. On September 13, 2013, I filed a proxy proposal with Disney asking the board to include my proposal in the proxy. The heart of my proposal was as follows:

Shareowners ask our board to take the steps necessary unilaterally (to the fullest extent permitted by law) to amend our bylaws and each appropriate governing document to give holders of 10% of our outstanding common stock (or the lowest percentage permitted by law above 10%) the power to call a special shareowner meeting.

According to an October 29, 2013 "no-action" request filed with the SEC, after receiving my proposal

...the Board of Directors of the Company determined on October 4, 2013, that it would include a proposal (the "Company Proposal") in the Proxy Materials to amend the Certificate of Incorporation of the Company to provide shareholders the right to call a special meeting of shareholders, provided that the request for such a meeting was made by holders of 25% of the outstanding shares of the Company's common stock at the time of the request, and each requesting shareholder had maintained a net long position in such shares for at least one year prior to the date of the request.

SEC staff granted the no-action request and issued a letter indicating the SEC would take no action against Disney if it left my proposal off the proxy, in reliance on Rule 14a-8(i)(9) because:

...inclusion of both proposals would present alternative and conflicting decisions for the shareholders and would create the potential for inconsistent and ambiguous results.

Here's the problem as I see it. Under the current rule, complacent and entrenched boards can simply ignore bad corporate governance practices until threatened by shareowner activists. When it looks like those activist will prevail, the board can simply remove that threat by substituting a very watered down version of the shareowner's proposal.

The board doesn't even have to recommend in favor of their own proposal. If it fails to pass, the board can simply trot out the same proposal whenever a shareowner seeks change. If it passes, the board's prior proposal can be modified ever so slightly to block any future efforts by shareowners. For example, if shareowners pass

Disney's 25% threshold and I come back next year with another 10% threshold proposal; Disney's board could propose a 24.9% threshold.

Let's compare my special meeting proposal to Disney's. Under my proposal, it would take the three largest shareowners at Disney to call a meeting. Vanguard, SSgA and BlackRock would all have agree an emergency meeting is called for. This is highly unlikely because none of these funds are known activists. How about a more likely scenario. Looking only at activist funds that own Disney, it would take a combination of Norges, Childrens, CalPERS, CalSTRS, Citadel Advisors, Third Point, SAC Capital, CR Intrinsic and GAMACO. But wait, that only gets us up to 1.58% of outstanding Disney common stock and I've already gone through the top 500 shareowners.

Under Disney's proposal to call a special meeting, it would take their top 9 shareowners: Vanguard, SSgA, BlackRock, Fidelity, MFS, State Farm, Capital Research, Northern Trust and T. Rowe Price Associates. Of these, none can be described as an activist fund, although T. Rowe Price might be considered something of a borderline activist. Disney even rules out most hedge funds by requiring all participants to have been net long for at least a year. Read Gilson and Gordon's The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights. Funds, like the top nine holders of Disney are "'rationally reticent' – willing to respond to governance proposals but not to propose them."

The SEC granted Disney no-action relief because, as Disney argued (my emphasis),

...if both proposals are included in the Company's Proxy Materials, shareholders would be presented with alternative and conflicting proposals that could result in shareholder ***confusion***. Further, if both proposals are approved by shareholders, there would be no way for the board to implement both, or to know ***which should be implemented***, which would result in the "inconsistent and ambiguous results" that Rule 14a-8(i)(9) seeks to avoid.

This is nonsense. Shareowners are not so stupid or so easily confused as imagined. If both proposals are on the proxy there is no inherent confusion, shareowners simply need to decide if 10% of shareowners should be able to call a special meeting or if it should take 25%, excluding the very type of activist funds who would mostly likely have invested the necessary money, time and expertise to call such a meeting.

The rule should be amended to allow shareowner proposals to go on the proxy unless the company has already publicly announced and filed a conflicting proposal before the shareowner proposal has arrived. First to file is a time-honored way of choosing, seen by most as a fair way to determine what goes on a ballot. Another option would be to allow both proposals on the proxy. It shouldn't be hard for the board to know which should be implemented; implement whichever gets the highest vote. Boards shouldn't be able to game the system with proposals simply meant to thwart the will of shareowners.

Please do not hesitate to e-mail or phone if additional information or examples would be helpful in fully understanding the issue discussed above.

Sincerely,

James McRitchie, Publisher
Corporate Governance
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