Segal Marco Advisors

550 W. Washington Blvd, Suite 900 Chicago, IL 60661
T 312.575.9000
F 312.575.0085
segalmarco.com

February 3, 2020

Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8 - File No. S7-23-19

Dear Secretary Countryman:

Segal Marco Advisors ("Segal Marco") appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "Commission") regarding its proposal to amend the shareholder resolution process proposed through the Securities Exchange Act of 1934 (the "Exchange Act") Release No. 87458, "Procedural Requirements and Resubmission Thresholds under Exchange Act Rule 14a-8" (the "Release") dated November 5, 2019. We commend the Commission for reviewing aspects of these rules; however, as discussed in further detail below, we have concerns about the changes proposed in the Release (the "Proposed Amendments"). These include a concern that, if adopted as currently written, the Proposed Amendments would unduly prevent shareholders from submitting proposals that promote valuable corporate reforms, while providing insignificant cost savings to companies. In our view, the Release provides inadequate evidence of the need to limit shareholder proposals, relies on insufficient economic analysis, proposes changes that would not appropriately address the issues with the shareholder proposal process, fails to address negative impacts to shareholders and their representatives, especially those affecting small shareholders, and provides minimal benefits to companies.

We urge the Commission to reconsider the Proposed Amendments and either take no further action or, if moving forward with final rules, more proportionately tailor the Proposed Amendments to the vast benefits of the shareholder proposal process and the limited cost of potential shareholder abuse of the system.

Background

Segal Marco[1] provides engagement services to private and public pension funds to whom we provide consulting and proxy voting services, assisting them with all aspects of the shareholder

---

[1] Segal Marco Advisors is the trade name of Segal Advisors, Inc. (CRD# 114687 / SEC# 801-61280).

proposal process. The submission process is complex and grows more so with increased regulation. Our clients use our engagement services to help them navigate complexities around language and process in an efficient and cost-effective manner. We help our clients submit proposals on their own letterhead, and may be listed as the contact person for company outreach, notices of deficiency and no-action requests, but our clients always have full discretion and control over the process, including identifying companies to engage, formulating initiatives, and negotiating settlements.

Our clients provide retirement and other benefits to working people. Thus, they invest on behalf of the "Main Street" investors of whom Chairman Clayton so often speaks.[2] We believe that the Proposed Amendments, which would sacrifice many value-enhancing benefits of the shareholder proposal process in exchange for minimal cost savings for companies, would harm our clients and, by extension, the small investors the Commission is focused on protecting. We feel that, if adopted as proposed, the Proposed Amendments would also degrade corporate governance standards and, over time, raise the cost of capital for U.S. public companies.

The Proposed Amendments

The Proposed Amendments would:

1. Substantially raise the ownership threshold that a shareholder must satisfy in order to be eligible to file a proposal;

2. Substantially raise the level of voting support a proposal must obtain in order to avoid exclusion in later years;

3. Limit shareholders' representatives to submitting only one proposal to a company for a particular shareholders' meeting, and require such representatives to submit additional documentation proving their authority to act on behalf of shareholders; and

4. Compel shareholder proponents to make themselves available, shortly after they submit a proposal, for a meeting with the company to discuss the proposal.

Although the Commission conducted an economic analysis to assess the impact of the Proposed Amendments, we believe that the analysis does not sufficiently satisfy the standards for rulemaking pursuant to the Commission's guidance[3] and judicial precedent.[4]. The Release:

---

[2] Chairman Clayton has recognized that most "Main Street" investors invest through intermediaries like our clients: "Actually, the direct retail money is small but, you know, channeling after mutual funds or other things, it's a lot. And so at the Commission, we should be looking at that audience when we're making decisions." (Transcript, "Perspectives on Securities Regulation Featuring a Conversation With U.S. Securities and Exchange Commission Chairman Jay Clayton," Brookings Institution (Sept. 28, 2017) (https://www.brookings.edu/wp-content/uploads/2017/10/es_20170928_securities_clayton_transcript.pdf).

[3] Memorandum to Staff of the Rulewriting Divisions and Offices from the Division of Risk, Strategy and Financial Innovation and Office of General Counsel re: Current Guidance on Economic Analysis in SEC Rulemaking, at 1 (Mar. 16, 2012) (https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf) ("2012 Guidance").

[4] See cases discussed in 2012 Guidance, at 13, n.34.

- Provides inadequate basis to conclude that limiting a shareholder representative's ability to submit only one proposal to a company per shareholder meeting, or requiring shareholders' representatives to show their authority to act on behalf of the shareholder, is necessary to address abuse of the shareholder proposal process;

- Bases its estimate of the Proposed Amendments' benefits to companies on outdated and unreliable data, as well as statements made by companies, which serve their own interests at the expense of shareholders;

- Does not adequately identify, analyze or weigh the benefits provided by the shareholder proposal process, which the Proposed Amendments would undermine by reducing the number of proposals;

- Does not justify why a 12-fold increase in the ownership threshold is appropriate to prevent shareholder abuse of the proposal process, or adequately analyze the costs associated with excluding proposals by smaller shareholders;

- Does not sufficiently explain why it is necessary to adopt the Momentum Requirement (defined below), or analyze the extent to which these changes would cause value-enhancing proposals to be excluded; and

- Would impose a one-sided obligation for proponents to offer to meet with companies, at specific times shortly after submitting the proposal, with no evidence to support that such compelled engagement would lead to any beneficial outcome.

Accordingly, we encourage the Commission to reconsider the Proposed Amendments and either take no further action or, if moving forward with final rules, more proportionately tailor the Proposed Amendments to the vast benefits of the shareholder proposal process and the limited costs of any potential shareholder abuse of the system. In particular, we ask that Commission to: avoid drastically increasing the shareholder ownership thresholds for submitting proposals; encourage resubmission of proposals that do not abuse the system; and continue to allow shareholder representatives, such as Segal Marco, to submit proposals for multiple investors at a single shareholder meeting.

The Release Does Not Establish That Limiting Shareholders' Ability to Act Through Representatives, and Interfering With Relationships Traditionally Governed by Contract or State Agency Law, is Necessary to Prevent Abuse

The Commission has proposed to limit the ability of shareholders to use a representative of their choosing to submit a shareholder proposal by shifting from a "one proposal per shareholder" to "one-proposal-per-person" (*i.e*. representative) rule. The Release further constrains the services a representative can provide to a shareholder, by requiring that the shareholder make itself available to meet with the company about the proposal shortly after its submission. (We discuss the meeting requirement in more detail in a following section.)

The Release contains no evidence that the use of a representative is associated with abuse or that representatives have submitted proposals on behalf of shareholders who were unaware of the proposal or had no interest in it. Our clients authorize the submission of proposals, as well as all other steps involved in the proposal process. Our contracts with our clients – and the fiduciary duties we owe them – prohibit us from submitting any proposal that "actually represents" our interests, rather than theirs. The Release cites testimony from Darla Stuckey, the President and CEO of Society for Corporate Governance, (the "Stuckey Testimony"), which states that "so much abuse has occurred with these types of submission, that it is impossible for companies to determine whether a proposal actually reflects the interests of the shareholder rather than the proponent, who is not a shareholder."[5] But the abuse to which Ms. Stuckey refers involved a single proponent whose investment adviser submitted a proposal without enough information to tell whether the client had authorized the proposal. That letter predated the 2017 guidance from the Staff of the Division of Corporation Finance requiring proof of authorization,[6] so it does not represent the current baseline.

The relationship between a representative and its client is governed by state agency law and, in some cases, contract. The Proposed Amendments would interfere with that relationship with no justification. Under the proposed one-proposal-per-person rule, we could be put in the position of having to choose among multiple clients that wish to submit a particular proposal at the same company, which could cause us to violate our obligations to all but one of them. The Commission's arguments that the one-proposal-per-person rule "would prohibit shareholders from imposing disproportionate costs on the company and other shareholders by submitting multiple proposals for the same meeting"[7] and that allowing a representative to submit multiple proposals at a company is an "unreasonable exercise of the right to submit proposals at the expense of other shareholders and also may tend to obscure other material matters in the proxy statement"[8] are not based in evidence. Under the Proposed Amendments, multiple shareholders would be eligible to individually submit more than one proposal without using representatives, but a single representative would not be able to submit the same number of proposals on behalf of each of those shareholders. The Release does not reconcile why allowing multiple shareholders to submit proposals is not problematic, while a single representative submitting these same proposals on behalf the shareholders would impose "disproportionate costs" and constitute an "unreasonable exercise" of shareholder proposal rights.[9]

Finally, we are concerned that the lack of clarity in the proposed standard will result in significant disputes between companies and shareholders, requiring Staff involvement. Revised Rule 14a-8(c) would state that "each person, directly or indirectly," may file only one proposal for a meeting. We envision that, in certain situations, companies may argue that multiple proposals have been submitted "indirectly" by a shareholder. For example, a shareholder

---

[5] Written Testimony of Darla C. Stuckey, President and CEO, Society for Corporate Governance, House Committee on Financial Services, Subcommittee on Capital Markets and Government Sponsored Enterprises, at 10 (Sept. 21, 2016) (https://republicans-financialservices.house.gov/uploadedfiles/hhrg-114-ba16-wstate-dstuckey-20160921.pdf))

[6] Staff Legal Bulletin 14I (Nov. 1, 2017) (https://www.sec.gov/interps/legal/cfslb14i.htm)

[7] Release, at 139.

[8] Release, at 38.

[9] Release, at 38.

sometimes submits a proposal that was submitted in the previous year by another shareholder. A company might ask the Staff to infer that both proposals were actually submitted by the earlier-submitting shareholder, one directly and the other indirectly, through the new shareholder. With no evidence of abuse under the one-proposal-per-shareholder rule, such complexity is unjustified.

Company-Provided Data Regarding the Costs of Proposals is Unreliable

The economic consequences of proposed SEC rules should be measured against a baseline representing the "best assessment" of the current environment.[10] The Release creates a baseline for costs of the current shareholder proposal process in an attempt to claim that the Proposed Amendments will offer cost savings to companies; however, the data the Commission uses to establish the baseline cost of proposals for companies is outdated and unreliable. The Release supports its baseline for current company costs associated with proposals by citing three different figures provided in comment letters on the Statement Announcing SEC Staff Roundtable on the Proxy Process (the "Roundtable"). The Release states, "Two commenters cited an estimate indicating an average cost to companies of $87,000 per shareholder proposal, another commenter estimated its own cost at more than $100,000 per proposal, and a third commenter cited a cost of approximately $150,000 per proposal."[11]

BlackRock, Inc. ("BlackRock") and the Society for Corporate Governance (the "Society") each provided the $87,000 per proposal cost estimate in Roundtable comments. Although BlackRock is a public company and sought to exclude shareholder proposals in 2016 and 2019, it based the $87,000 figure on a 2008 study by Joao Dos Santos and Chen Song. Dos Santos and Song's paper was funded by the U.S. Chamber of Commerce, which also directed a portion of the study's methodology.[12]

During their study, Dos Santos and Chen cited a 2003 law review article, which in turn based the cost estimate on Commission survey data from 1997.[13] The underlying data is thus more than 20 years old. Since 1997, proxy distribution and voting have shifted from paper proxy materials and cards to emailed proxy materials (through Notice and Access) and electronically submitted votes. Proxy tabulator Broadridge Financial Solutions, Inc. ("Broadridge") reports that improved technology substantially reduced proxy cost. In a recent report, Broadridge stated that its "technologies and processing for e-delivery, householding and account consolidations... saved corporate issuers and mutual funds over $1.7 billion in paper, printing and postage in comparison to what they would have spent had all materials been mailed as full sets" in 2019 alone. Broadridge distributed proxy materials for 4,216 meetings, so the average cost savings per meeting was over $403,000.[14]

---

[10] 2012 Guidance, at 6.
[11] Release, at 12 (footnotes omitted).
[12] See Joao Dos Santos & Chen Song, ""Analysis of the Wealth Effects of Shareholder Proposals," at 1, 6 (2008)(https://www.uschamber.com/sites/default/files/legacy/reports/080722wfi_shareholder.pdf)
[13] See Dos Santos & Song, at 13; Exchange Act Release No. 40018 (May 21, 1998) (describing results of 1997 survey).
[14] Broadridge, "2019 Proxy Season Key Statistics and Performance Rating."

In addition to the age of the data, several aspects of the Commission survey data itself raise concerns. Data from two survey questions was combined to produce the $87,000 number. First, companies were asked to indicate what they spent to determine whether to include or exclude a proposal. Only 80 companies responded, and the average of their responses was $37,000. The variance, though, was huge; responses ranged from a low of $10 to a high of "approximately $1.2 million."[15] An outlier estimate of more than one million dollars in a relatively small sample size (i.e. 80 responses) may skew the mean response, making it difficult to trust that the average cost cited by the SEC's data is representative of the actual cost borne by most companies. The average value would have been lower without high outliers, as shown by the fact that the median response, $10,000, was significantly lower than the average. To illustrate how far-fetched the $1.2 million figure appears, we can assume a law firm partner bills at $1,000 per hour (a generous assumption since a partner would not be doing the bulk of this kind of work). Based on the $1.2 million fee the partner would require 1,200 billable hours to handle a single proposal. It is possible that this and other very high estimates relate to multiple proposals: The Commission acknowledged that some responses "may have accounted for consideration of more than one proposal."[16] (The Release also acknowledges this weakness.[17])

The other survey question cited in the Release, which asked companies to estimate the cost of printing, postage and tabulation for a single proposal, has similar issues. The $50,000 average figure was derived from 67 estimates ranging from $200 to nearly $900,000, which also "may have accounted for the printing of more than one proposal."[18] Given these problems, the cost estimates on figures from the Dos Santos and Song study are not reliable enough to serve as the basis for the Commission's cost estimates.[19]

The ExxonMobil Corporation ("ExxonMobil") submitted the Roundtable comment letter cited for the $100,000 per-proposal estimate. ExxonMobil estimated that each proposal, even "identical, repeat proposals,"[20] costs the company $100,000. It seems unusual that a sophisticated institution like ExxonMobil paid outside counsel the same amount to draft a no-action challenge on a proposal that was challenged on similar grounds the year before. In our experience, later no-action requests on the same proposal duplicate a substantial amount of material from earlier requests and are therefore less time consuming. Statements in opposition also tend to be reused with minor changes. Thus, less staff and board time would need to be devoted to a repeat proposal.

---

[15] Exchange Act Release No. 40018 n.95 and accompanying text (May 21, 1998)

[16] Id.

[17] Release, at 158.

[18] Exchange Act Release No. 40018, n.107 and accompanying text (May 21, 1998).

[19] The Release also cites a Roundtable comment letter from the Society, which offered the same $87,000 figure as BlackRock/Dos Santos and Song, crediting the Center for Capital Markets Competitiveness ("CCMC") but not citing a source. Given that the CCMC is a US Chamber of Commerce initiative (https://www.bloomberg.com/profile/company/0815774D:US), it seems reasonable to assume that the $87,000 figure proffered by the Society came from the Dos Santos and Song study. The Stuckey Testimony explained that her cost estimates were based on both the $87,000 figure and "anecdotal discussions with Society members." (at the Stucky Testimonry, supra note 4, at 8)

[20] https://www.sec.gov/comments/4-725/4725-5879063-188728.pdf

The Commission based its Paperwork Reduction Act calculations on a $150,000 per-proposal estimate, which lacks support entirely. The figure came from a Roundtable comment by the American Securities Association ("ASA"), a trade association representing regional financial services firms.[21] The ASA's figure did not reflect its members' experiences, but instead relied on a report by the House Financial Services Committee. However, that report asserted the $150,000 figure without citing any source or describing what it included.[22] Thus, the ASA's figure is also too unreliable to serve as the basis for the Commission's cost savings estimates.

The Commission's baseline for economic analysis also defers to company estimates and relies on the comment process to elicit data, without conducting its own research. The absence of other tangible benefits of the Proposed Amendments puts additional importance on the cost savings estimates. The Commission is well-positioned to obtain information about costs, from companies (via a new survey), vendors (e.g. by asking Broadridge to estimate the incremental cost of adding a ballot item), and by analyzing data in the Commission's possession, such as no-action requests.

We note that, even if the cost savings is calculated using the highest estimate of $150,000 per proposal, the total savings would still be between $4.5 million and $79.5 million for the entire Russell 3000 index, which is tiny in comparison to the market capitalization of the index. Dividing that savings between the 3,020 companies in the index[23] produces an average per-company savings of between $1,490.07 and $26,324.50. Given the size of Russell 3000 companies, whose market capitalizations range from $152.3 million to over $900 billion,[24] this savings is not significant. Indirect costs such as the use of management or board members' time to address a proposal are also unlikely to be significant because the average Russell 3000 company receives one shareholder proposal every 7.7 years.[25] In our view, even relatively modest costs stemming from adoption of the Proposed Amendments would outweigh these cost saving benefits.

The Release Does Not Adequately Analyze the Lost Benefits of the Shareholder Proposal Process

The Release does not sufficiently identify and analyze what benefits would be lost as a result of the projected 37% reduction in shareholder proposals. The Commission cannot fulfill its obligation to weigh the benefits against the costs without identifying and analyzing the positive aspects of the shareholder proposal process. The Commission mentions but does not analyze the value-promoting corporate reforms and communication that would be sacrificed, and does not address other benefits of the shareholder resolution process at all. Such a glib treatment does not satisfy the Commission's obligation under the 2012 Guidance to clearly define the baseline for

---

[21] See https://www.sec.gov/comments/4-725/4725-5646621-185668.pdf

[22] Report on H.R. 5756, "To Require the Securities and Exchange Commission to Adjust Certain Resubmission Thresholds," at 2 (Aug. 24, 2018) (https://republicans-financialservices.house.gov/uploadedfiles/crpt-115hrpt904.pdf) It is worth noting that the report stated that the "cost of a proposal *can run* $150,000 per measure" (emphasis added), suggesting that this figure is at the high end of a range of costs.

[23] https://www.ftserussell.com/research-insights/russell-reconstitution/market-capitalization-ranges

[24] https://www.ftserussell.com/research-insights/russell-reconstitution/market-capitalization-ranges

[25] See https://www.cii.org/files/10_10_Shareholder_Proposal_FAQ(2).pdf

evaluating the economic impact of the Proposed Amendments and to analyze the costs and benefits of adopting them, including "costs arising from changes to the behavior of regulated firms or persons beyond those that the rule was intended to achieve…"[26]

Moreover, we find that the Release's characterization of the shareholder proposal process is unbalanced. The 2012 Guidance mandates that, "[t]he release should evaluate the costs and benefits even-handedly and candidly,"[27] but the Release focuses disproportionately on companies' complaints about the Rule 14a-8 process. Such one-sidedness invalidates the economic baseline established in the Release, as well as its evaluation of the costs and benefits of the Proposed Amendments.

The shareholder proposal process has played a key role in achieving value-enhancing governance reforms, which the Release mentions[28] but fails to analyze. Although companies may voluntarily adopt governance reforms that promote value creation, without receiving a proposal, in our experience the threat of a proposal operates in the background to motivate companies to adopt desirable improvements. In addition, shareholder resolutions allow shareholders to pursue governance reforms on a company-by-company basis, through private ordering, thereby reducing the need for the kind of regulation companies often criticize as "one-size-fits all."

The Release does not appropriately consider the voluminous academic literature on the value of specific governance arrangements or superior environmental, social, and governance ("ESG") performance more generally. The Commission noted that shareholder proposals may help to limit entrenchment,[29] which has been the subject of substantial empirical research,[30] but did not discuss those studies or attempt to analyze the impact of losing proposals designed to limit entrenchment. Likewise, the Release does not mention other kinds of reforms obtained through shareholder proposals that could be value-enhancing. Studies have linked common subjects of shareholder proposals, such as board and upper management diversity,[31] proxy access,[32] and

---

[26] 2012 Guidance, at 11.
[27] 2012 Guidance, at 14.
[28] Release, at 141 (""To the extent that [newly excludable] shareholder proposals would be value-enhancing, the potential exclusion of value-enhancing proposals could be detrimental to companies and their shareholders.").
[29] Release, at 112.
[30] See, e.g., Lucian Bebchuk et al., "What Matters in Corporate Governance," Rev. Fin. Stud., Vol. 22, No. 2, 783-827 (Feb. 2009) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=593423); Paul Gompers et al., "Corporate Governance and Equity Prices," Quant. J. Econ., 118(1), 107-155 (Feb. 2003) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=278920; Martijn Cremers & Allen Ferrell, "Thirty Years of Shareholder Rights and Firm Valuation" (2013) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1413133).
[31] https://newsroom.bankofamerica.com/system/files/2019_Environmental_Social_Governance.pdf; Credit Suisse, "Does Gender Diversity Improve Performance?" Jul. 31, 2012 (https://www.credit-suisse.com/us/en/about-us/research/research-institute/news-and-videos/articles/news-and-expertise/2012/07/en/does-gender-diversity-improve-performance.html); Vivian Hunt, Dennis Layton & Sara Prince, "Diversity Matters," McKinsey & Company, Feb. 2, 2015 (http://www.diversitas.co.nz/Portals/25/Docs/Diversity%20Matters.pdf).
[32] See CFA Institute, "Proxy Access in the United States" (Aug. 2014) (https://www.cfainstitute.org/-/media/documents/article/position-paper/proxy-access-in-united-states-revisiting-proposed-sec-rule.ashx).

better ESG performance generally[33] to higher firm value and superior performance. Other studies have found that particular governance arrangements are associated with lower levels of fraud.[34]

The Release neglects cross-sectional studies like those cited above, while instead emphasizing event studies of stock price reactions to specific shareholder proposals. The Commission excuses its focus on "short-term market reactions to shareholder proposals"[35] because it says that long-term effects are more difficult to attribute to proposals. We do not believe that short-term stock price fluctuations should be deemed dispositive evidence, one way or the other, of shareholder proposals' value, especially given the Release's focus on long-term ownership. Event studies, by their nature, can measure only market participants' reactions to shareholder proposal-related events, not the value over time of reforms achieved through those proposals.

Also, the appropriate inference to draw from market reactions is not always obvious. For example, reactions to majority votes may reflect beliefs about the likelihood (and not just the desirability) of implementation. Shareholders vote on many items at shareholder meetings, including director elections and executive compensation, muddying the link between a shareholder proposal vote and the market's reaction. Because companies do not have to disclose vote results until several days after a shareholder meeting, share price movements on the meeting day may not even incorporate information about such results.

The shareholder proposal process has permitted our clients to obtain many value-enhancing corporate reforms. For example, The City of Philadelphia Public Employees Retirement System spearheaded an effort at companies involved in the opioid epidemic, asking them to improve accountability by not removing legal and compliance costs from executive incentive compensation metrics, and providing enhanced disclosure that will better enable investors to determine the extent to which opioid-related costs are being excluded. A similar proposal at Equifax, filed by our client the AFL-CIO Equity Index Fund, led the company to add back costs related to its costly 2017 data breach into metrics used for executive incentive pay. Several of our clients successfully pushed boards during the 2018 proxy season to adopt more robust diversity policies for the director search process and we saw seven companies add female directors.

Without shareholder proposals, many of the value-enhancing corporate governance practices now considered best practices, such as declassified boards, performance-based compensation, and majority voting for director elections, would not have been adopted or would have taken much longer to gain widespread acceptance. Proposals prompt companies to make disclosures beyond what is mandated by the Commission. The Release should analyze these benefits of

---

[33] GMI 2007 on S&P 500 companies TSR; Guido Giese, "Foundations of ESG Investing: How ESG Affects Equity Valuation, Risk, and Performance," J. Portfolio Mgmt., at 4-5 (July 2019) (https://www.msci.com/documents/10199/03d6faef-2394-44e9-a119-4ca130909226) (finding that high ESG-rated companies paid higher dividends, earned more profits, and had fewer "idiosyncratic risk incidents" involving large stock price drops).

[34] Hatice Uzun et al. "Board Composition and Corporate Fraud," *Financial Analysts J.* Vol. 60, Issue 3 (2004) (https://www.cfainstitute.org/en/research/financial-analysts-journal/2004/board-composition-and-corporate-fraud).

[35] Release, at 113 n.214.

shareholder resolutions and incorporate them into both the economic baseline and the evaluation of costs and benefits resulting from the Proposed Amendments.

An additional benefit of the proposal process, mentioned but not analyzed in the Release, is shareholder communication. Votes on proposals aggregate shareholder preferences and communicate them unambiguously to management.[36] Non-proponent shareholders, who might be disinclined to submit proposals themselves, are also able to communicate using their votes.

The 14a-8 process brings fresh perspectives to the board and management, which can help corporate leadership identify potential blindspots. Shareholder proposals warned companies of risks from climate change, compensation practices that promote excessive risk-taking (including at Wells Fargo), and the dangers of subprime lending and mortgage securitization, well before those issues were recognized by many companies or even other investors.

Finally, across the market, shareholder resolutions improve corporate governance and transparency. The Commission is charged with considering the impact of proposed rules on capital formation, and we believe that lower governance standards would make U.S. companies less attractive as investments, raising the cost of capital. There is empirical evidence that better ESG performance leads to a lower cost of capital,[37] and BlackRock CEO Larry Fink recently predicted that "companies and countries that do not respond to stakeholders and address sustainability risks will encounter growing skepticism from the markets, and in turn, a higher cost of capital."[38]

In sum, although the Release concedes that the Proposed Amendments could limit value-enhancing proposals and proponents' ability to communicate with other shareholders,[39] it does not properly weigh the loss of those benefits, together with other benefits on which the Release is silent, against the cost savings generated by the Proposed Amendments. The Commission has thus not adequately established that the benefits of the Proposed Amendments outweigh the costs.

The Commission Has Not Justified Why the Need to "Update" the Ownership Threshold Requires Radical Changes or Analyzed the Extent to Which Value-enhancing Proposals Would Be Excluded as a Result

The Release urges that the ownership threshold for shareholder proposals (i.e. continuous ownership of $2,000 worth of stock for one year) needs to be updated because more than 20 years have passed since the last time the Commission adjusted the thresholds and both inflation and the growth in the equity markets have eroded the value of that $2,000 threshold.[40] The

---

[36] Alan R. Palmiter, "The Shareholder Proposal Rule: A Failed Experiment in Merit Regulation," 45 Ala. L. Rev. 879, 901 (1994) (https://wakespace.lib.wfu.edu/handle/10339/26139)
[37] See, e.g., Guido Giese, "Foundations of ESG Investing: How ESG Affects Equity Valuation, Risk, and Performance," J. Portfolio Mgmt., at 10-11 (July 2019) (https://www.msci.com/documents/10199/03d6faef-2394-44e9-a119-4ca130909226); Sadok El Ghoul, "Does Corporate Social Responsibility Affect the Cost of Capital?" J. Banking & Fin., Vol. 35, Issue 9, 2388-2406 (2011) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1546755).
[38] https://www.blackrock.com/corporate/investor-relations/larry-fink-ceo-letter
[39] Release, at 142.
[40] Release, at 19-20.

Proposed Amendments would move to a tiered threshold in which shareholders owning $25,000 or more in company stock could submit a resolution after one year of ownership; owners of at least $15,000 but less than $25,000 could file after owning for two years; and owners of at least $2,000 but less than $15,000 could not file until they had held for at least three years. The 2012 Guidance requires the Commission to analyze the economic benefits of a proposed rule, which "correspond to the justification for the rulemaking."[41] The Release does not satisfy that standard because its justification for increasing the threshold is not consistent with the large increase proposed in the Proposed Amendments.

Chairman Clayton often asserts his commitment to small investors, but the higher ownership thresholds would, according to the Release, disproportionately affect such investors.[42] In fact, the Release cautiously suggests that individuals may submit more value-enhancing proposals than institutions.[43] Also, there is a negative and statistically significant relationship between ownership level and the likelihood of majority support.[44] The data, in fact, argues in favor of lowering the threshold rather than raising it.

The Release never explains why a 12-fold threshold increase is an appropriate response to a need for updating occasioned by inflation and the growth of the equity markets. In a bit of circular reasoning, the Release urges that "holding $2,000 worth of stock for a single year does not demonstrate enough of a meaningful economic stake or investment interest in a company to warrant the inclusion of a shareholder's proposal in the company proxy statement."[45] The Commission implies that if small investors want to participate, they should simply hold their shares for longer. However, where reforms are urgently needed, such a delay would be value-destroying. Many institutional investors, including our clients, separate their investment and stewardship activities. Being "mindful of concerns" that raising the ownership threshold could have a "greater effect on shareholders with smaller investments"[46] does not address why updating necessitates such a large increase in the threshold.

The Release estimates that the increased ownership threshold could cause up to a 56% reduction in shareholder proposals. Such a precipitous drop would be justified only if there existed strong evidence that the benefits of a much higher threshold outweigh the negative impacts on shareholders and the capital markets. There is not enough of this evidence, thus there is no basis for adopting the Proposed Amendments.

The Commission's Justification for Increasing the Resubmission Thresholds and Imposing the Momentum Requirement Rests on Faulty Logic

Currently, the resubmission thresholds in Rule 14a-8(i)(12) allow a company to exclude a proposal if it has been voted on once in the past five years and not obtained support from holders of 3% of shares voted; if it has been voted on twice in the past five years and not achieved 6%

41 2012 Guidance, at 10.
42 Release, at 144,
43 Release, at 144.
44 Release, at 94 fn.188.
45 Release, at 19.
46 Release, at 25.

voting support; or if it has come to a vote three times in the last five years and not obtained support from 10% of shares voted (3/6/10%). The Commission has proposed to raise those thresholds to 5/15/25%. Also, the Release would allow exclusion if a proposal has been voted on three or more times in the past five years and voting support decreased by 10% or more between the two most recent votes. (This provision is referred to as the "Momentum Requirement".)

The Release makes its case for these significant increases on two mistaken assumptions. First, it assumes that excluding fewer proposals, pursuant to the resubmission thresholds means that those thresholds are not doing their job of screening out proposals that are not of broader interest to shareholders beyond the proponent. The Release notes that "the current resubmission thresholds may not have the same effect today on resubmissions as they did when they were initially adopted. According to one commenter, the percentage of shareholder proposals eligible for resubmission today is considerably higher than at the time the thresholds were first introduced, when 'between one-half and three-quarters of proposals failed to win sufficient support for resubmission.'"[47] But many factors may account for that development; in addition to those identified by the Commission—the role of proxy advisory firms and greater participation in proxy voting by institutional investors[48] —it seems likely that more skillful crafting of proposals and outreach by proponents also play a role. Thus, fewer exclusions do not necessitate an increase in the resubmission threshold.

Second, the Release assumes that the value-enhancement benefits of shareholder proposals are dependent on obtaining majority shareholder support. This assumption conflates "meaningful" and "majority" support in this discussion.[49] The Release criticizes the current resubmission thresholds for not "adequately distinguish[ing] between proposals that are more likely to obtain majority support upon resubmission and those that are not."[50] The Commission also justifies this focus by citing evidence that proposals that receive majority support are more likely to be implemented than those that do not.

It is our view that the Release overstates the importance of majority support. Our clients regularly settle proposals with companies, obtaining value-enhancing reforms, after non-majority votes or even before a proposal goes to a vote. One study showed that boards reduce the rate of executive compensation increases if a shareholder proposal on the subject "receives unexpectedly high shareholder support," even if that support is short of a majority.[51] The Commission would cut this process off after three years despite the fact that there have been many instances where a proposal needed time to build support and eventually achieved majority support, but would be excludable under the Proposed Amendments. In addition to the proxy access and executive stock sales examples Commissioner Jackson identified in his dissent,[52] board declassification proposals, which now routinely obtain substantial majority support, started

---

[47] Release, at 49-50.
[48] Release, at 50.
[49] Release, at 52.
[50] Release, at 49.
[51] Randall S. Thomas & James F. Cotter, "Shareholder Proposals in the New Millennium: Shareholder Support, Board Response, and Market Reaction," at 6 (2007) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=868652).
[52] Commissioner Robert J. Jackson, Jr., "Statement on Proposals to Restrict Shareholder Voting" (Nov. 5, 2019) (https://www.sec.gov/news/public-statement/statement-jackson-2019-11-05-open-meeting#_ftnref13).

out with very low support levels. Resolutions asking companies to report on climate change risk took many years to reach their current level, which includes majority votes and may not yet have reached a ceiling.

We do not believe that the Commission has justified the Momentum Requirement or the 10% decline it selected to use in that requirement. The Release states that the Commission "believe[s] that a 10 percent decline in the percentage of votes cast may demonstrate a sufficiently significant decline in shareholder interest to warrant a cooling-off period."[53] The Release's use of qualifying language, such as "believes" and "may," suggests that the Commission does not have concrete evidence demonstrating a need for a "cooing-off period" for certain shareholder proposal resubmissions. The example provided in the Release, of a proposal whose support dips from 30 to 26%, is just as likely to represent normal volatility as a permanent decline. The Commission has not provided any data on proposal vote volatility by which to benchmark the 10% figure or any data on which kinds of proposals or proponents would be most affected by the Momentum Requirement. The Release cannot determine the economic impact of the Momentum Requirement without identifying the justification for the requirement and analyzing its effect on potentially value-enhancing proposals.

The Proposed Amendments' One-Sided Requirement That Proponents Must Make Themselves Available to Meet With Companies Shortly After Proposal Submission Would Not Improve the Engagement Process

The Proposed Amendments mandate that a proponent state that it is available to meet with the company on specific days and times within the period from 10 days to 30 days after the proposal is submitted. The Commission claims it has proposed this requirement in order to "encourag[e] engagement."[54]

The Release is devoid of evidence that the mandatory meeting requirement would improve the quality or quantity of engagement. The requirement further only burdens the shareholder – the Commission has not proposed to impose a meeting requirement on companies. Accordingly, it is possible that shareholders could provide days and times, hold that availability open, and then end up never meeting with the company. In our experience, any obstruction of the engagement process results from companies' unwillingness to meet, not shareholders'.

The timeframe for the proposed meeting is also suboptimal. The late fall period, in which most shareholder proposals are due, is a busy one for shareholders. During this quarter, shareholders may submit proposals at multiple companies, and the companies fielding submissions review them for procedural defects, provide notices where such defects exist, and decide whether to seek no-action relief. The Thanksgiving and Christmas/Hanukkah holidays also fall during this period. Under these circumstances, it is unlikely that companies would be able to put together the appropriate personnel to engage substantively. Companies typically reach out to Segal Marco and our clients in January and February, far outside the 10-30 day period proposed.

---

[53] Release, at 59.
[54] Release, at 33.

Shareholders would be significantly burdened by this meeting requirement. It is not clear how long shareholders would be required to hold open the day/time slots they would identify in their proposal submission letters. It would be unfair if a company could wait until the last minute to select a slot because shareholders would bear opportunity costs. It is also unclear what standard would be applied to determine whether the shareholder-proponent has satisfied the requirement. Would a good cause standard apply if a shareholder became unable to meet during one of the identified time slots? The requirement would be unduly burdensome and subject to abuse,"[55] without sufficient evidence of benefit.

For these reasons, it is our belief that the Commission has not met the standard set forth in the 2012 Guidance. The Release provides inadequate justification for the Proposed Amendments, does not sufficiently evaluate the corporate governance benefits conferred by the current shareholder proposal process, does not provide adequate evidence about how the Proposed Amendments would address investor abuse of the shareholder proposal process, and does not give appropriate consideration to the potential costs associated with the Proposed Amendments, including the loss of value-enhancing proposals. Accordingly, we urge the Commission to either take no further action or, if moving forward with final rules, more proportionately tailor the Proposed Amendments to the vast benefits of the shareholder proposal process and the limited costs of any potential shareholder abuse.

*　　　　*　　　　*　　　　*　　　　*

Segal Marco appreciates the opportunity to weigh in on this important issue. Please contact me with any questions at [redacted] or [redacted]

Best regards,

Maureen O'Brien
Vice President, Corporate Governance Director

cc: Hon. Jay Clayton, Chairman
Hon. Robert J. Jackson, Jr., Commissioner
Hon. Allison Herren Lee, Commissioner
Hon. Hester M. Peirce, Commissioner
Hon. Elad L. Roisman, Commissioner

55 Release, at 35.