

**Recommendations of the Investor Advisory Committee
Regarding SEC Rulemaking to Explore Universal Proxy Ballots
(Adopted July 25, 2013)**

Preliminary Observations:

- Currently, retail investors and institutional investors other than the largest in the U.S. do not have the practical ability to vote their shares at shareholder meetings in the same manner that is available to shareholders who attend shareholder meetings in person.
- Shareholders in attendance at meetings, particularly in proxy contests, have the ability to receive a legal ballot that allows them to pick and choose among all of the candidates who are duly nominated. Shareholders who are not in attendance do not have that ability and typically can only choose from among nominees that appear on management’s or a dissident’s ballot – but not both.
- Congress has granted the Commission authority over the corporate proxy process as a means of ensuring that it functions, “as nearly as possible, as a replacement for an actual in-person meeting of shareholders.”¹ The complexity and expense of exercising full voting rights for the election of directors while not attending a shareholders meeting in person are substantial, and typically only large institutional holders ever avail themselves of these procedures.²
- The current “bona fide nominee” rule codified in Rule 14a-4, is a significant inhibiting factor to the adoption of so-called universal proxy ballots (“Universal Ballots”) and relaxation of this rule should be explored. Universal Ballots are shareholder voting cards on which shareholders can choose to vote for one or more director candidates regardless of who nominated any individual candidate, so long as the candidates are duly nominated under state law and the particular company’s charter and bylaws.

¹ See <http://www.sec.gov/news/press/2009/2009-116.htm>

² See <http://www.sec.gov/Archives/edgar/data/27419/000095012309009445/y01588ydfan14a.htm>

IAC Recommendations:

Universal Ballot Recommendation

The Commission should explore relaxing the “bona fide nominee” rule embodied in Rule 14a-4(d)(1) promulgated in 1966 under Section 14 of the Securities Exchange Act of 1934 to provide proxy contestants with the option (but not the obligation) to use Universal Ballots in connection with short slate director nominations (in other words, where the candidates nominated by shareholders would, if elected, constitute a minority of the board of directors). In connection with that process, specific inquiry should be made as to whether all or only a portion of duly nominated candidates must or may appear on Universal Ballots.

Supporting Rationale:

Rule 14a-4(d)(1) promulgated in 1966 under Section 14 of the Securities Exchange Act of 1934 provides that no proxy shall confer authority upon the solicitor to vote for any person who is not a bona fide nominee.³ This is the so-called “bona fide nominee rule.” Under Rule 14a-4(d) a bona fide nominee is one who consents to being named in a particular proxy statement and agrees to serve if elected. It is important to note that the consent required is the consent to be named in a particular proxy statement, and not a general consent to be nominated for election or to serve as a director. Directors nominated by an incumbent board have only very rarely consented to being named as nominees in a proxy statement issued by a shareholder in opposition to management.

The practical effect of the bona fide nominee rule, in conjunction with typical “last in time” state corporate law provisions,⁴ is that shareholders have no practical ability to “split their tickets” and vote for a combination of shareholder nominees and management nominees. In many cases shareholders who desire to vote for a full slate of directors attempted to split their tickets by seeking to vote for both shareholder and management nominees on a single card, leading to the invalidation of their votes, disenfranchising shareholders and disadvantaging nominating shareholders seeking minority representation on the board of directors.⁵

In final rules promulgated in 1992,⁶ the Commission modified the bona fide nominee rule by “choosing a partial solution to the problem, opting *not* for the most simple approach that would permit inclusion of some management nominees on the dissident’s proxy.”⁷ In adopting the 14a-4 amendments, the Commission noted “the difficulty experienced by shareholders in gaining a voice in determining the composition of the board of directors,” but

³ 17 CFR 240.14a-4(d).

⁴ State law almost universally provides that the latest dated proxy revokes any previous proxy, thus forcing shareholders to vote on a single card.

⁵ Ronald J. Gilson, Lilli A. Gordon and John Pound, “*How the Rules Discourage Constructive Engagement: Regulatory Barriers to Electing a Minority of Directors*,” 17 J. CORP. L. 29 (1992).

⁶ Regulation of Communications Among Shareholders, Exchange Act Release No. 31,326, Investment Company Act Release No. 19,031 (October 16, 1992) (hereinafter the “Short Slate Release”).

⁷ Remarks of SEC Commissioner Mary L. Schapiro Before the National Investor Relations Institutes Fall Conference, November 6, 1992 (emphasis added).

stated the following with regard to providing shareholder access to the company's proxy materials:

Proposals to require the company to include shareholder nominees in the company's proxy statement would represent a substantial change in the Commission's proxy rules. This would essentially mandate a universal ballot including both management nominees and independent candidates for board seats.⁸

Rather than mandating a Universal Ballot the Commission revised the bona fide nominee rule so that it allows a shareholder who nominates a short slate of directors (i.e., a number of directors which, if elected, would constitute a minority of the board) to obtain authority to vote for some of management's nominees as well (the "short slate rule"). Under the modified rule, and upon compliance with its conditions,⁹ the solicited shareholder is able to support the nominating shareholder's minority short slate while preserving the ability to vote for a full slate of directors by authorizing the nominating shareholder to vote for management nominees as well.

Soliciting parties can identify the management nominees they will *not* vote for and can indicate that they will vote for the rest of management's slate, but the soliciting party *cannot* include the management nominees it *will* vote for by name in its proxy statement or form of proxy. For example, "if a shareholder wishes to nominate only two candidates to a seven person board, the short slate rule permits the shareholder to choose five of management's nominees to fill out his or her ballot, provided that the shareholder does not name those management nominees on his or her proxy card, but instead only those management candidates that the shareholder is opposing."¹⁰ The Commission addressed certain of the perceived defects in the bona fide nominee rule without formally amending it – by allowing a nominating shareholder to identify the management nominees it would not vote for rather than permitting it to take the more direct approach of identifying those management nominees for whom it would vote.

By enabling Universal Ballots, the Commission can more directly improve this basic element of corporate democracy. Recent experience in Canada (including large-cap issuers with substantial shareholders in the U.S.) suggests that technical implementation for a Universal Ballot regime is cost effective.

The IAC encourages the Commission to further inform itself and market participants, including by way of one or more roundtable discussions, regarding the concept of

⁸ The Short Slate Release, *supra* note 5 at 57 Fed. Reg. 48,276 at 48,288 (Oct. 22, 1992).

⁹ Rule 14a-4(d) requires that four conditions be met to allow the incorporation of management's nominees into the nominating shareholder's card: (1) the nominating shareholder must seek authority to vote in the aggregate for all of the board seats then up for election; (2) the nominating shareholder must disclose its intention to vote for all of management's nominees except for those specified; (3) the solicited shareholder must have an opportunity to withhold authority with respect to any other management nominee by writing the name of such nominee on the form; and (4) both the form and the statement must disclose that there is no assurance that management's nominees, if elected, will serve with any of the nominating shareholder's nominees.

¹⁰ *SEC Staff Report: Review of the Process Regarding the Nomination and Election of Directors*, Division of Corporate Finance, July 15, 2003.

Universal Ballots and the challenges and opportunities available for proxy modernization in this area.

Deliberations:

In connection with deliberations on the Universal Ballot Recommendation, the committee members considered whether the current Rule 14a-4 is operating satisfactorily or, if Universal Ballots would offer improvement, whether Universal Ballots should be made mandatory in all circumstances (so-called “mandatory use”) or whether contestants should be enabled at their own choosing to include some or all of a competing nominee slate (so-called “optional use”).

Proponents of mandatory use point out the virtue of allowing all shareholders to have a low-cost, equal opportunity to vote in a manner that is available to all in-person attendees at shareholder meetings. Moreover, these commentators point out that the inability to choose from among the individuals nominated from all parties limits shareholder choice and diminishes director accountability by precluding shareholders from choosing the best candidates amongst all of those who are nominated. In their view, these limitations weaken basic notions of corporate democracy.

Proponents of optional use point out that mandatory use could be viewed as a new form of shareholder proxy access, which many have objected to for reasons that are well documented, and adoption of mandatory use could prove for the same reasons to be unnecessarily controversial. These proponents also point out the virtue of a less proscriptive regime that allowed contestants to pick and choose between individual nominees (if any) on their proxy cards, particularly when contestants found all or certain individuals on a competing slate to be particularly objectionable.

Separately, in the course of deliberations, questions from previous exploration of Universal Ballots were raised including (1) the potential for voter confusion (i.e., voter inability to easily determine the recommended candidates nominated by a contestant) and (2) the risk of over-voting (i.e., the selection of a greater number of nominees than open seats available for election).

In the case of potential voter confusion, a consensus was reached that this risk could be mitigated with conspicuous disclosure on proxy cards. Further, reference was made to the fact that in contested elections professional proxy solicitors and other soliciting persons are typically made available to facilitate the voting process for both institutional and retail holders, thereby mitigating potential for voter confusion.

In the case of over-voting, the point was made that under state laws, which currently govern the terms of legal ballots, selection of a greater number of nominees than open seats could render a proxy card invalid and thereby disenfranchises shareholders. In addition to noting that the common use of proxy solicitors and other soliciting persons mitigates this risk, reference was made to the fact that increasingly both institutional and retail shareholders vote by way of electronic means that could be configured to mitigate this risk by mechanically requiring voters to fix problems before ballots are submitted.

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