
Latest SEC Staff Legal Bulletin May Make Shareholder Proposals Harder to Exclude

On November 3, 2021, the staff of the Division of Corporation Finance (the “Staff”) of the Securities and Exchange Commission (the “Commission”) issued new guidance on its review of requests to exclude shareholder proposals from proxies that could make it less likely that a company will be able to exclude a proposal if it raises significant social policy questions. In the 2021 proxy season, more environmental and social proposals were submitted by shareholders than in any prior year, and of those that went to a vote, more proposals were approved than in any prior year. (See 2021 Proxy Season Review, Harvard Law School Forum on Corporate Governance, August 5, 2021) This latest guidance from the Staff could embolden shareholder activists and present a challenge for public companies as they prepare for the next proxy season.

At Rule 14a-8 under the Securities Exchange Act provides a means by which shareholders can present proposals for consideration in a company’s proxy statement and sets forth several bases for exclusion of such proposals. Companies often request assurance that the Staff will not recommend enforcement action if they omit a proposal based on one of these exclusions (“no-action” relief). The Staff has issued Staff Legal Bulletin (“SLB”) 14L, which can be found [here](#), outlining its current views on Rule 14a-8(i)(7), the “ordinary business” exception, and Rule 14a-8(i)(5), the “economic relevance” exception. The new SLB rescinds prior bulletins that provided guidance on these matters (SLBs 14I, 14H and 14K).

There are two bases for exclusion under the ordinary business exception: the subject matter of the proposal and the degree to which the proposal micromanages the company’s business. Regarding subject matter, SLB 14L indicates that the Staff will realign its approach for determining whether a proposal relates to “ordinary business” and no longer focus on determining the nexus between a policy issue and the company (as it had been doing based on the rescinded SLBs) but will instead focus on the social policy significance of the issue that is the subject of the proposal. In making this determination, the Staff will consider whether the proposal raises issues with a broad societal impact, such that they transcend the ordinary business of the company. The Staff explained that, for example, proposals squarely raising human capital management issues with a broad societal impact would not be subject to exclusion solely because the proponent did not demonstrate that the human capital management issue was significant to the company. In a footnote, the Staff explained that “matters related to employment discrimination are but one example of the workforce management proposals that may rise to the level of transcending the company’s ordinary business operations.”

Regarding micromanagement, SLB 14L indicates that the Staff will take a “measured approach” that focusses on the “level of granularity sought in the proposal and whether and to what extent it inappropriately limits discretion of the board or management.” Proposals seeking detail or seeking to promote timeframes or methods will not per se constitute micromanagement, but instead will be evaluated based on whether they seek the level of detail needed “to enable investors to assess an issuer’s impacts, progress towards goals, risks or other strategic matters appropriate for shareholder input.” The Staff pointed to a recent example of a proposal that was not excluded as

micromanaging where the proponent requested that the company set emission reduction targets covering its greenhouse gas emissions, without requesting a specific method of reducing the emissions. Recognizing that the rescinded SLBs dealt mainly with proposals that relate to timeframes and targets to address climate change, the Staff explained it would not “concur in the exclusion of similar proposals that suggest targets or timelines so long as the proposals afford discretion to management as to how to achieve such goals.”

In a further nod to the rising importance of environmental, social and governance (ESG) matters, SLB 14L provides that the “economic relevance” exception in Rule 14a-8(i)(5) (which permits a company to exclude a proposal if it relates to operations that account for less than 5% of the company’s total assets, net earnings and gross sales for its most recent fiscal year if not otherwise significantly related to the company’s business) will no longer provide a basis to exclude a proposal that raises issues of broad social or ethical concern related to the company’s business. Previously, the Staff recommended issuers submit a board analysis to help assess economic relevance. Given its new position stated in the SLB, the Staff will no longer expect a board analysis for its consideration of a no-action request under Rule 14a-8(i)(5).

SLB 14L also makes some clarifications and changes to the procedural requirements of Rule 14a-8. The Staff explained that graphics and images are not prohibited by the 500-word maximum applicable to shareholder proposals (although any words in the graphics will count toward the 500-word count) and that proof of ownership need not follow a specific form of letter but simply needs to be clear and sufficiently evidence the requisite ownership. Recognizing that emails are a common and valid means of communicating, the Staff also recommended that the sender should obtain a confirmation of receipt to be able to prove timely delivery.

While SLB 14L states it is being issued “to streamline and simplify our process for reviewing no-action requests, and to clarify the standards staff will apply when evaluating these requests,” Commissioners Hester M. Peirce and Elad L. Roisman issued a statement of dissent that expressed dismay at the Staff’s “flavor-of-the-day regulatory approach” and expressed concern that the new approach leaves many unanswered questions that will burden the Staff and embroil it further in questions that are outside their expertise and would be better handled by Commission action or state corporate laws.

While the Staff asserts that SLB 14L realigns certain aspects of its approach with the original intent of the rule and the Commission’s 1976 and 1998 releases, the impact of SLB 14L will only become evident as the 2022 proxy season unfolds.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email author Helene Banks (partner) at 212.701.3439 or hbanks@cahill.com; or email publications@cahill.com.

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