A PRACTICAL GUIDE TO SEC PROXY AND COMPENSATION RULES

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CHAPTER 10

THE SHAREHOLDER COMMUNICATIONS PROXY RULES AND THEIR PRACTICAL EFFECT ON SHAREHOLDER ACTIVISM AND PROXY CONTESTS

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§ 10.01 INTRODUCTION

The last two decades have witnessed a slow, but steady, shift in the balance of power from boards of directors and corporate management to institutional shareholders and other institutional activists. The SEC's proxy rules have both followed and facilitated this shift. Some of the proxy reforms adopted over this period have focused on process, such as the shareholder communications rules adopted in 1992, the Internet availability of proxy materials adopted in 2007, the NYSE's elimination of broker discretionary voting approved by the SEC in 2009, and the proxy access rules adopted by the SEC in 2010 (which were subsequently vacated as "arbitrary and capricious" by the D.C. Circuit Court of Appeals). Other rules have focused on disclosure requirements designed to enhance the ability of shareholder activists to target specific issues on their agendas. These include the nominating process disclosure rules adopted in 2003, the rules requiring disclosure of proxy voting by mutual funds adopted the same year, the expanded disclosure adopted in 2009 relating to director qualifications, board diversity, and separation of Chair and CEO, and the ever expanding compensation disclosure requirements detailed in other chapters of this book. The SEC's rules have also been supplemented by federal and state legislation, as well as stock exchange rules, that have given activists additional tools to further their corporate governance agenda.

The cumulative impact of these rule changes and reforms has been significant. The SEC's 1992 amendments gave institutional shareholders and activists broad freedom to communicate with each other, express their views on proxy solicitations publicly, and put together organized campaigns to bring pressure to bear on corporate targets with respect to a wide array of governance issues. The rules have also allowed proxy advisory firms, such as Institutional Shareholder Services (ISS) and Glass, Lewis & Co., to flourish, giving these firms tremendous power over the proxy process, which they have used to enhance the ability of institutional activists to pursue their corporate governance agenda. Activists are now able to present a credible threat of an orchestrated campaign to withhold votes from directors, or even to replace some or all of the board, if a company does not follow the activists' wishes.

As the environment has evolved over the last two decades, corporate management has had little choice but to recognize the increased power of the institutional shareholders and the need to be responsive to their concerns. Discussions and negotiations between management and

shareholders have often replaced the confrontational atmosphere of the 1980s. But these discussions and negotiations carry the implicit threat of more direct institutional shareholder action if the institutions are not satisfied with management's response. And the rise of hedge fund activism over the last several years has, in many cases, reintroduced a tone of hostility and confrontation. As a result, the frequency with which companies are bowing to the wishes of institutional activists, or at least reaching compromise solutions that satisfy the activists, continues to increase. In particular, activist campaigns and pressure have led companies to systematically dismantle their takeover defenses, removing their poison pills or letting them expire, declassifying boards of directors, and otherwise making their companies more vulnerable to hostile takeovers. These campaigns have also led to widespread adoption of majority voting policies, a renewed focus on whether to separate the positions of Chair and CEO, and ongoing scrutiny of compensation practices. The frequency with which dissident directors are elected to company boards, or appointed as a means of settling a proxy contest, has steadily increased.

There are some who would argue that the net result of the onslaught of rules and shift in power has been to force boards and management to focus unduly on short-term results, as they try to appease hedge funds and other activists who bring pressure on them to take actions to boost immediate stock prices. While the recent economic downturn might have been an opportunity to reexamine whether this type of pressure contributed to the economic crisis and should be addressed, the political narrative seems to have gone in the opposite direction, blaming corporate boards and management for the downturn and seeking ways to shift even more power into the hands of hedge funds, institutional shareholders and activists. As a result, it appears that the shift in power from boards and management to activists will continue for the foreseeable future.

The next section of this chapter provides an overview of the shareholder communications rules and subsequent legislation, rules and reforms. Section 10.03 sets forth examples of the effect of the rules and reforms on proxy contests and shareholder activism. Section 10.04 explores corporate responses and sets forth recommendations for the future.

§ 10.02 THE SHAREHOLDER COMMUNICATIONS PROXY RULES AND SUBSEQUENT REFORMS AND PROPOSALS

This section describes the requirements of the shareholder communications proxy rules, including discussion of subsequent reforms and legislative and regulatory proposals.

[A] Private Proxy Solicitations

The most significant of the shareholder communications rules effectively permits a wide array of private proxy solicitations. These rules allow solicitation of an unlimited number of shareholders, with no proxy statement or public disclosure, so long as the person making the solicitation does not ask for a proxy card or proxy revocation and does not have a special interest in the subject matter of the solicitation.[1]

If the private solicitation is made by a person who holds more than $5 million of the company's stock, any written solicitation material must be filed with the SEC within three days of its use.[2] Otherwise, no filing or disclosure is required at all. Persons who solicit their own proxy card or proxy revocation, or who have a special interest in the matter to be voted on, continue to be subject to the full proxy statement and disclosure requirements. Others ineligible for the no disclosure rule include (i) the issuer; (ii) officers, directors, or affiliates of the issuer or of any other ineligible person; (iii) director nominees; (iv) any person soliciting in opposition to a merger or similar transaction who is affiliated with a competing alternative transaction; (v) any Schedule 13D filer who has disclosed a possible control intent; and (vi) anyone who is paid to solicit by an ineligible person.[3]

In 2004, the federal court of appeals for the Second Circuit ruled that dissident shareholders who enclosed a copy of management's proxy card with their solicitation could not rely on the no disclosure exemption.[4] The court held that enclosing the management proxy card, which

[1] Rule 14a-2(b)(1).
[2] Rule 14a-6(g).
[3] Rule 14a-2(b)(1).
[4] *MONY Group, Inc. v. Highlands Capital Mgmt., L.P.*, 369 F.3d 138 (2d Cir. 2004).

allowed shareholders to change their votes and thereby revoke any previous proxy card, was the functional equivalent of soliciting a proxy revocation, and that the dissidents were therefore disqualified from relying on the Rule 14a-2(b)(1) exemption. In 2009, the SEC proposed an amendment to Rule 14a-2(b)(1) to provide that supplying an unmarked management proxy card would not constitute a disqualifying solicitation of a form of revocation.[5] To date, however, the SEC has not acted on the proposed amendment.

These rules on private solicitations permit private discussions among a company's major shareholders, and private lobbying of major shareholders, all out of the view of the public and the company itself. No notice or filing with respect to oral communications among shareholders who do not solicit their own proxy card, and are not otherwise ineligible, need ever be made. Written material need be filed only by persons who hold more than $5 million of the company's stock, and even then need not be filed if it is published or broadcast. Given the size of institutional holdings—approximately 73% of the equity securities in the 1,000 largest U.S. companies as of 2009[6]—these rules give institutional holders in many companies the power, if they so desire, to decide in private the outcome of any given matter presented for shareholder vote.

In late 2007, the SEC adopted an additional exemption from the proxy disclosure rules for any proxy solicitation made in an electronic shareholder forum maintained or operated under Rule 14a-17, so long as the person making the solicitation does not seek proxy authority or a form of revocation, and so long as the solicitation is made at least 60 days before the company's next shareholder meeting (or, if later, no more than two days after public announcement of the date of the meeting).[7] The stated purpose of the rule was to "open up new avenues for real-time communications among shareholders, and between shareholders and the companies they own."[8]

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[5] Proposed Rule: Proxy Disclosure and Solicitation Enhancements, Securities Exchange Act Release No. 34-60280 (July 10, 2009) at 49–51, 124.

[6] As of May 1, 2009, institutional investors, defined as pension funds, investment companies, insurance companies, banks, and foundations, held approximately 73% of the equity of the largest 1,000 U.S. corporations, up from approximately 57% a decade earlier. *See* The Conference Board, *2010 Institutional Investment Report.*

[7] Rules 14a-2(b)(6) and 14a-17.

[8] SEC Press Release No. 2007-247 (Nov. 28, 2007).

As outlined in Section 10.03 below, the private solicitation rules, together with subsequent reforms and governance developments, have greatly enhanced the influence of institutional shareholder activists. While the effect has been demonstrated in the context of formal proxy contests, the most important impact has been on the leverage the rules give institutional activists to negotiate with a company short of any formal action. Institutional shareholders are regularly able to gain direct access to corporate managements and even boards of directors to discuss their dissatisfaction with corporate policies or personnel. In recent years, companies have taken voluntary action with respect to a variety of takeover or governance-related issues in the face of institutional pressure. The range of more formal measures favored by activists—such as bringing a Rule 14a-8 shareholder proposal, withholding authority from a company's slate of director nominees as a vote of no confidence, seeking the election of representatives to the board, or seeking the appointment of a shareholder advisory committee—still remains as a backdrop to reinforce the institutional investors' power. The ability of institutions to communicate among themselves in private, without being deemed to be engaged in a solicitation, gives such measures an increased likelihood of success. Together with the sheer size of institutional holdings, the increased ability and willingness of institutional shareholders to act collectively has changed the dynamics of the interaction between a company and its major shareholders, giving the shareholders more access and more power to influence the company's direction.

[B] Announcement of Voting Decisions

The shareholder communications rules provide that a shareholder's public announcement of how the shareholder intends to vote on any matter (and the reasons for such vote) does not constitute a proxy solicitation.[9] This rule enables shareholder activists to apply public pressure on targeted companies. The announcement of a voting decision such as the withholding of authority for a company's board slate, combined with a public critique of company policy or performance, can be a very powerful weapon for a shareholder activist, particularly given the ability of the activist to lobby other shareholders in private to take the same position. A number of institutional investors, such as CalPERS, regularly disclose

[9] Rule 14a-1(1)(2)(iv).

their voting decisions on their Web sites. And even the threat of such an announcement may also be a powerful weapon.

In 2003, the SEC took this concept one step further, adopting rules to require mutual funds and other registered management investment companies to disclose information on how they cast their proxy votes, as well as on their voting policies and procedures.[10] This rule not only ensures more widespread dissemination of voting positions by major shareholders, it also opens up the prospect of a campaign within a campaign. Shareholders may not only seek to apply pressure on a company in which they invest, but may also seek to apply pressure on mutual funds and investment advisers who are investors in the same company and whose voting decisions must now be disclosed. And pursuant to the Dodd-Frank Act, enacted in 2010, every institutional investment manager subject to Section 13(f) of the Securities Exchange Act is required to report at least annually how it voted on the say-on-pay votes required by the Dodd-Frank Act.[11]

[C] Dissident Nominees

The shareholder communications rules allow a dissident's proxy card to "round out" a less than full slate of dissident nominees by granting authority to vote for the incumbents' nominees (other than those incumbent nominees whom the dissident would replace), subject to the right of the incumbents to state that they will not serve if the dissidents are elected.[12] For example, if a dissident sought to elect two directors to a board of ten, the dissident's proxy card could grant a proxy to vote for Mr. Brown and Ms. Green (the two dissident nominees), and for all of the incumbents' nominees other than Mr. Smith and Ms. Jones (the two incumbents sought to be replaced).

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[10] *See* Final Rule: Disclosure of Proxy Voting Policies and Proxy Voting Records by Registered Management Investment Companies, Securities Act Release No. 33-8188 (Jan. 31, 2003).

[11] Securities Exchange Act Section 14A(d). The SEC has proposed rules to implement this requirement; *see* Proposed Rule: Reporting of Proxy Votes on Executive Compensation and Other Matters, Securities Exchange Act Release No. 34-63123 (Oct. 18, 2010).

[12] Rule 14a-4(d).

In crafting this rule, the SEC struck a compromise in that the rule does not permit the dissident proxy to name the incumbent board's nominees for whom votes will be cast, thereby avoiding the potential implication that some of the incumbent board's nominees have joined the dissident slate. Instead, to use the "rounding out" option, the dissident proxy must: (1) name the incumbent board's nominees for whom votes will *not* be cast; (2) represent that votes will be cast for all of the incumbent board's nominees *other* than those so named; (3) provide space for a shareholder to withhold authority for any nominee; and (4) disclose that there is no assurance that the incumbent board's nominees will actually agree to serve with the dissident nominees.

In recent years, it has become common to see short-slate election contests, due in part to increased hedge fund activism. With the success of a number of recent short-slate contests, and with institutional shareholders and proxy advisory firms growing more supportive of the concept of replacing a minority of the board as a means of shaking things up or sending a message, the frequency of short-slate contests is expected to continue to increase. Indeed, in the 2009 proxy season, the situation arose in which two different dissidents ran short slate contests at the same company.[13] This situation also presented the question of whether a dissident could round out a short slate with some of the other dissident's nominees as well as some of the incumbent nominees. In response, the SEC proposed to amend the rules to make clear that a dissident may round out a short slate with another dissident's nominees, so long as the two dissidents are not acting together.[14] This proposed amendment has not yet been adopted.

A number of activists have also been pushing for new rules to adopt a universal proxy card format that would list all incumbent nominees and dissident nominees on a single card. This type of universal proxy card would have been required by the SEC's proxy access rules, and may still be required if proxy access bylaws are ultimately adopted that require a company to put one or more dissident nominees in its own proxy statement and proxy card.[15] But some activists have argued that a universal

[13] *See* Steven M. Davidoff, *Icahn, Amylin and the Nuances of Activist Investing*, N.Y. Times DealBook, Apr. 20, 2009.

[14] Proposed Rule: Proxy Disclosure and Solicitation Enhancements, Securities Exchange Act Release No. 34-60280 (July 10, 2009) at 53–59, 125–126.

[15] Final Rule: Facilitating Shareholder Director Nominations, Securities Exchange Act Release No. 34-62764 (Aug. 25, 2010).

proxy card should be mandated even where a dissident uses separate proxy materials to nominate candidates for election to a company's board.[16] In the Pershing Square-Canadian Pacific proxy contest in 2012, Canadian Pacific adopted a universal proxy card listing all 15 of its nominees together with all seven of Pershing Square's nominees. The company then argued that shareholders could vote for whomever they wanted on the company's proxy card and need not use any Pershing Square proxy card. The strategy may have been successful in getting shareholders to use Canadian Pacific's proxy card, but it was not successful in helping the company's election results, as all of Pershing Square's nominees were elected.[17]

[D] Preliminary Filings

The proxy rules require preliminary filing and SEC review of proxy materials only for the basic proxy statement and proxy card. All other proxy materials, including letters to shareholders, newspaper advertisements, and other supplemental materials, need not be filed in advance of their use and are not subject to prior SEC review.[18] As discussed in the next section, many of the proxy contests waged since adoption of these provisions have been particularly aggressive compared to proxy contests prior to adoption. The other major effect of the absence of prior review is to permit both sides of the contest to respond more rapidly to each other in the midst of the fight.

[E] Public Availability of Filings

Most proxy materials that are still required to be filed in preliminary form are available to the public upon filing, rather than remaining confidential until definitive materials are filed.[19] Only proxy materials to

[16] *See* Zachery Kouwe, *Ackman and Target Tangle in Ballot Brawl*, N.Y. Times DealBook, Apr. 21, 2009.

[17] *See* Steven M. Davidoff, *How Ackman Won in the Fight Over Canadian Pacific*, N.Y. Times DealBook, May 17, 2012.

[18] Rule 14a-6(a)-(c). No preliminary filing is required for an annual meeting proxy statement if only routine matters are to be considered at the meeting and there is no proxy contest with respect to these matters.

[19] Rule 14a-6(e)(1).

be used in connection with business combinations (other than going-private transactions and partnership roll-ups) are now eligible for confidential treatment while in preliminary form.[20] And even this exception was largely undercut by proxy rule amendments adopted by the SEC in 1999, which permit confidential treatment only if the company confines itself to very limited public statements with respect to the business combination.[21] Because virtually any company announcing a business combination will want to explain the transaction publicly, the practical effect of the SEC's 1999 amendment is to eliminate the 1992 exception that permitted confidential treatment for preliminary proxies relating to business combinations.

[F] Commencement of Solicitations

Under the SEC's 1999 amendments, even a party that is required to file a proxy statement may commence a proxy solicitation before filing.[22] In order to take advantage of this rule, the party making the solicitation: (i) must file any written material used for the solicitation with the SEC no later than its first use; (ii) must include a legend advising shareholders to read the proxy statement when it becomes available and providing shareholders with information about the participants in the solicitation or advising shareholders where they can find that information; and (iii) may not furnish a form of proxy until shareholders receive the final proxy statement. The e-proxy rules, discussed in Chapters 9 and 13, have not affected this rule. This rule has particular importance in the context of business combinations, where it has now become routine for company management to conduct extensive presentations and follow-up discussions with major shareholders following announcement of a transaction, but before filing a proxy statement. Amendments adopted concurrently in 1999 under the Securities Act of 1933, as amended (the "Securities Act") work in tandem with the proxy rules to permit this activity even in the context of a stock for stock transaction, without violating Securities Act rules relating to the registration of stock offerings.[23]

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[20] Rule 14a-6(e)(2).
[21] Rule 14a-6(e)(2)(ii).
[22] Rule 14a-12.
[23] *See* Rule 165 under the Securities Act.

[G] Unbundling of Related Proposals

The proxy rules do not permit a company to present a group of related matters as a single proposal for shareholder action.[24] Instead, the proxy card requires separate boxes to give shareholders the opportunity to vote on each matter separately. Each related matter may, however, be conditioned on passage of the others.[25]

This provision is largely an outgrowth of the SEC's unhappiness with the bundling of matters such as antitakeover charter provisions with an economic transaction such as a merger or spin-off. However, the unbundling requirement may result in shareholder confusion in circumstances where matters that are truly interrelated, and mutually conditional, are presented for separate votes.

In 2004, the SEC provided guidance on its interpretation of the unbundling rule in the context of merger and acquisition transactions.[26] Under this guidance, a separate "unbundled" shareholder vote is required for any charter, bylaw, or similar provision effected by a merger or acquisition if: (1) the provisions in question were not previously part of the target company's charter or bylaws; (2) the provisions in question were not previously part of the charter or bylaws of a public acquiring company; and (3) state law, securities exchange listing standards, or the target company's charter or bylaws would require shareholder approval of the proposed changes if they were presented on their own. The SEC's guidance applies this interpretation both in the context of a merger or acquisition involving existing public companies and in the context of a newly formed company, with a new charter, that is formed for purposes of the merger or acquisition. In the latter situation, a separate vote is not required if the charter of the newly formed company is substantially the same as the preexisting charter of the company forming the new acquisition vehicle. This interpretation, of course, discourages companies from adopting new governance arrangements as part of a merger or acquisition. While the SEC permits the transaction and the governance arrangements to be conditioned on each other, the separate vote requirement increases the risk that the governance arrangements will become a lightning rod for shareholder

[24] Rule 14a-4.

[25] Rule 14a-4(a)(3) and (b)(1).

[26] SEC Division of Corporation Finance, *Manual of Publicly Available Telephone Interpretations*, Fifth Supplement (Sept. 2004).

activists and result in a vote-no campaign that could put the overall transaction in jeopardy.

[H] Shareholder Lists

The shareholder communications rules require a company to provide a requesting shareholder with a shareholder list only for solicitations involving a roll-up or going-private transaction. In the case of all other solicitations, the company may mail a dissident's materials in lieu of turning over a shareholder list.[27] Rule 14a-7 provides that any shareholder is entitled to request a shareholder list or have the company mail soliciting materials for the shareholder. The company is required to respond to the request within five business days of receipt.

Noting that there is no exception to a company's obligations under Rule 14a-7 based on a deficient request, a 1993 SEC release states that "a failure to meet the requirement for a timely response to a Rule 14a-7 request is excusable only if the issuer informs the holder within the five business day period of any deficiencies in the request and what additional information is required to perfect a request."[28] The release also states that any "comprehensible request" for a shareholder list or for a mailing triggers the Rule 14a-7 requirements, even if the request references state law rather than the federal proxy rules, unless it expressly disclaims reliance on Rule 14a-7.[29] The release notes that Rule 14a-7 is intended "to provide shareholders a meaningful means to exercise their rights to communicate with other shareholders" and should not be conditioned on the requesting shareholder being aware of technical distinctions or of "the particular requirements of Rule 14a-7."[30] As a result of the "householding" rules adopted by the SEC in 2000,[31] a single proxy statement can be sent to an address for which there are multiple shareholders with similar names at the same address. Third party solicitations are eligible to use the "householding" rules on the same basis as issuers.

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[27] Rule 14a-7.

[28] Compensation Disclosure; Security Holder List and Mailing Requests, Securities Exchange Act Release No. 34-32723 (Aug. 6, 1993) at 37.

[29] *Id.*

[30] Compensation Disclosure; Security Holder List and Mailing Requests, Securities Exchange Act Release No. 34-32723 (Aug. 6, 1993) at 36–37.

[31] Rule 14a-3(e)(1).

[I] Published or Broadcast Solicitations

The shareholder communications rules allow solicitations by means of broadcast or publication without the delivery of a proxy statement, so long as a definitive proxy statement is on file with the SEC and no form of proxy is provided with the solicitation.[32] This allows broad-based solicitations without the expense of mailing proxy materials to all shareholders.

[J] Disclosure of Voting Results

In 2010, detailed disclosure of voting results became required on Form 8-K within four business days after the meeting at which the vote was held, including disclosure of withheld votes and abstentions, and a separate tabulation with respect to each nominee in the event of an election of directors, with the applicable requirements being set forth in Appendix B to this treatise.[33] The immediate disclosure of voting results, and the requirement of a separate tabulation that includes withheld votes and abstentions, increases the effectiveness of a withheld vote or an abstention as a protest vote.

The proxy rules also require disclosure in the proxy statement of the effect of abstentions in tabulating the vote on any given matter in accordance with state law and the company's charter and bylaws.[34] This is designed to inform the shareholder whether an abstention will in essence be counted as a negative vote or a nonvote.

[K] Internet Availability of Proxy Materials

In 2007, the SEC adopted Rule 14a-16 and other amendments to the proxy rules to permit issuers and others soliciting proxies to distribute proxy materials by posting them on an Internet Web site and providing shareholders with notice of their availability.[35] Later in 2007, the SEC adopted amendments to Rule 14a-16 to require issuers to make proxy

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[32] Rule 14a-3(f).

[33] Item 5.07 of Form 8-K.

[34] Item 21 of Schedule 14A.

[35] Final Rule: Internet Availability of Proxy Materials, Securities Exchange Act Release No. 34-55146 (Jan. 22, 2007).

materials available by the Internet and provide notice of such Internet availability, though issuers still have the option to mail a full set of printed proxy materials so long as the notice and instructions for accessing the proxy materials on the Internet are included with the mailing.[36] Under Rule 14a-16, a Notice of Internet Availability must be sent to all shareholders at least 40 calendar days prior to the shareholder meeting, indicating that the proxy materials are available and explaining, in plain English, how to access them on the Internet. The 40-day advance notice requirement does not apply, however, if the issuer sends a full set of proxy materials with the Notice of Internet Availability.

Rule 14a-16 provides that shareholders must be given the opportunity to request a paper copy or e-mail copy of the proxy materials at the issuer's expense, but the issuer is required to provide a paper or e-mail copy only if requested. The issuer must post a proxy card to the Web site with the proxy statement no later than the time the Notice is sent. If the issuer chooses the Notice-only option, the issuer may send a proxy card to shareholders, with another copy of the Notice, no earlier than 10 days after the original Notice is sent. The Notice and Internet access method of distributing proxy materials may also be used by persons other than the issuer, with the Notice required to be sent by the later of 40 days prior to the meeting or 10 days after the issuer first sends proxy materials or its Notice to shareholders. Such persons are required to provide Internet availability of their proxy materials with respect to solicitations they may conduct. Persons other than the issuer, however, are not required to solicit all shareholders but may solicit only selected shareholders if they so choose. Rule 14a-16 does not apply to proxy materials relating to a business combination transaction.

These e-proxy rules are discussed more fully in Chapters 9 and 13. Internet distribution of proxy materials greatly reduces the cost of soliciting proxies, both for issuers and for dissidents who want to run a proxy contest. By reducing the cost to a dissident of running a proxy contest, the rule could increase the frequency of such contests over time.

[36] Final Rule: Shareholder Choice Regarding Proxy Materials, Securities Exchange Act Release No. 34-56135 (July 26, 2007).

[L] Elimination of Broker Discretionary Voting in Uncontested Elections and Other Matters

In 2009, the SEC approved amendments to NYSE Rule 452 to provide that a broker may not exercise discretionary voting in elections of directors, *i.e.,* the broker may not cast a vote for the election of directors with respect to any shares for which the broker has not received instructions as to how to vote from the beneficial owner of the shares.[37] Because brokers generally voted uninstructed shares in favor of a company's slate in an uncontested election, the inability of brokers to vote these shares shifts more power to institutional shareholders and activists, and increases the ability to run a successful withhold authority campaign with respect to an uncontested election of directors. In 2012, the NYSE extended the elimination of broker discretionary voting to management proposals on governance matters generally, including proposals for the repeal of classified boards and supermajority charter provisions.[38] This change may make it more difficult to obtain the necessary vote for such proposals, particularly where the proposal requires a supermajority of the outstanding shares to pass. Eli Lilly, for example, has proposed to declassify its board every year since 2006 but has failed to receive the required vote of 80% of the company's outstanding shares. In 2012, following the elimination of broker discretionary voting on such proposals, the vote in favor of declassification dropped to 63% of the outstanding, compared to percentages above 70% in recent years.

[M] Enhanced Proxy Disclosure of Governance Matters

In addition to continuing to push for changes in the proxy solicitation process, institutional activists have also pushed the SEC to expand proxy disclosure requirements, particularly in the areas of compensation, as discussed elsewhere in this book, and corporate governance. The latter includes enhanced disclosure requirements adopted in 2003 relating to a company's nominating process, and additional disclosure requirements

[37] Securities Exchange Act Release No. 34-60215 (July 1, 2009).

[38] *See* Ted Allen, *NYSE Bars Broker Votes From Governance Proposals*, ISS Governance Blog, Jan. 26, 2012 at <http://blog.issgovernance.com/gov/2012/01/nyse-takes-new-position-on-broker-votes.html>.

adopted in 2009 relating to board qualifications, diversity, and leadership structure.

[1] Nominating Process

The rules adopted in 2003 require enhanced proxy statement disclosure about the company's board-nominating process and the means by which shareholders may communicate with the board.[39] A company must set forth whether it has a standing nominating committee or another committee that performs similar functions and, if the company has no such committee, it must state the reasons for that decision and the names of the directors who participate in considering board nominees.[40]

With respect to any nominating committee, or any other committee or group of directors serving that function (which may be the entire board), the company is required to make a number of disclosures, including: (1) whether any committee charter is available on the company's Web site (if it is not, the company must attach any charter to the proxy statement at least once every three years, or disclose that it has no such charter); (2) how the committee considers nominees recommended by shareholders; (3) procedures to be followed by shareholders who want to recommend nominees; (4) how the committee identifies and evaluates their own nominees and shareholder nominees; (5) minimum qualifications that a nominee must meet and any specific qualities or skills the committee believes are necessary for directors to possess; (6) the specific source of each new nominee approved for inclusion on the proxy card; and (7) the role of any third party the company engages to help identify potential board nominees. Companies must also disclose whether the members of any nominating committee or group satisfy the definition of "independence" set forth in applicable listing standards.[41]

If the company receives notice, at least 120 days prior to the anniversary of the prior year's release of its proxy statement, of a nominee recommended by any shareholder or group owning greater than 5% of the company's voting common stock for at least one year as of the date of

[39] Final Rule: Disclosure Regarding Nominating Committee Functions and Communications Between Security Holders and Boards of Directors, Securities Exchange Act Release No. 34-48825 (Nov. 24, 2003).

[40] Schedule 14A, Item 7, paragraphs (d)(1) and (d)(2)(i).

[41] Schedule 14A, Item 7, paragraphs (d)(2)(ii)(A) through (K).

recommendation, and if the candidate and recommending shareholder or group provide their consent at the time of the recommendation, the company must disclose the name of the candidate and of the recommending shareholder or group, as well as whether the company chose to include the candidate in the company proxy statement.[42]

These rules also require the company to disclose in its proxy statement or on its Web site whether (and if not, why not) the board provides a process by which shareholders may send communications to the board. If the company does provide a process, it must disclose how and to whom shareholders may send such communications, and disclose the process for determining which communications are relayed to the board (unless all communications are relayed). The company must also describe any policy regarding board members' attendance at annual meetings and disclose how many board members attended the prior year's annual meeting.[43]

These rules are clearly designed to enhance the ability of shareholders to have direct input into the company's own nominating process, and to encourage companies to consider seriously nominees suggested by shareholders. The disclosure requirements relating to communications with the board are also designed to enhance the shareholders' ability to have direct input into the management and policies of the company.

[2] Board Qualifications, Diversity, and Leadership Structure

In 2009, the SEC adopted another set of expanded governance disclosures for proxy statements.[44] These rules require an annual proxy statement discussion of the specific experiences and skills relevant to service as a director, as well as whether, and if so, how, the nominating committee considers diversity in board composition.[45] If the nominating committee has a policy regarding board diversity, the company must describe how the nominating committee implements, and assesses the effectiveness of, the policy. The rules also require a proxy statement description of, and explanation for, the board's leadership structure,

[42] Schedule 14A, Item 7, paragraph (d)(2)(ii)(L).

[43] Schedule 14A, Item 7, paragraphs (h)(1) and (h)(2).

[44] Final Rule: Proxy Disclosure Enhancements, Securities Exchange Act Release No. 34-61175 (Dec. 16, 2009).

[45] Regulation S-K, Items 401(e)(1) and 407(c)(2)(vi).

including whether and why a company has chosen to combine or separate the Chair and CEO positions, and whether and why a company has a lead independent director (including what specific role the lead independent director plays if the company has one).[46]

These enhanced disclosure requirements focus on items that have been on the shareholder activists' agenda in recent years, including a growing effort to push companies to separate their Chair and CEO positions, an issue that has often been the subject of shareholder proposals. Companies may, however, have good reasons for not separating the positions, and the requirement that they make disclosures on this issue does not mean that they will necessarily feel pressure to move to an independent Chair structure. The appointment of a lead independent director, who may perform some of the roles that an independent Chair would perform, is an alternative approach that the disclosure rules recognize and that many companies have already adopted.

[N] Stock Exchange Listing Standards and Sarbanes-Oxley

The perceived corporate governance crisis created by the corporate scandals of the early 2000s led to the Sarbanes-Oxley Act in 2002, as well as NYSE and NASDAQ revised listing rules containing new corporate governance standards. Certain of the provisions of these reforms, which interact with the shareholder communications rules and further facilitate shareholder activism in corporate governance, are referenced below.

The thrust of a number of the NYSE corporate governance rules adopted in 2003[47] was to require disclosure of corporate governance practices and enhance channels of communication with shareholders to increase the ability of institutional investors to police corporate practices, and cause corporations to be more likely to adhere to good practices for fear of censure from shareholders. One of the most significant provisions in this respect is not in the rules themselves, but in the commentary to Rule 303A.03. The substance of Rule 303A.03 requires non-management directors of a company to meet at regularly scheduled executive sessions without management. The last sentence of the commentary to the rule

[46] Regulation S-K, Item 407(h).

[47] Securities Exchange Act Release No. 34-48745 (Nov. 4, 2003), as amended by Securities Exchange Act Release No. 34-50298 (Aug. 31, 2004).

imposes an additional requirement, stating: "In order that interested parties may be able to make their concerns known to the non-management directors, a listed company must disclose a method for such parties to communicate directly with the presiding director or with the non-management directors as a group." The rule thus requires an avenue for a direct line of communication between shareholders and outside directors, bypassing management. In the years since adoption of this rule, it has become increasingly common for institutional activists to ask for, and often receive, meetings with outside directors to convey their views.

A number of other NYSE governance rules require more detailed disclosure of various corporate governance practices, including: requiring a listed company's board to make an affirmative determination as to each director's independence and to disclose the basis for this determination or the categorical standards by which a determination of independence is made;[48] requiring that listed companies adopt and disclose corporate governance guidelines that address, among other things, director qualification standards, director responsibilities, director access to management and advisers, and director compensation;[49] and requiring that listed companies adopt and disclose a code of business conduct and ethics, and disclose any waivers granted under that code.[50] The disclosure requirements are designed to open these policies to greater shareholder scrutiny and activism. NASDAQ has adopted a similar set of corporate governance rules.[51]

The Sarbanes-Oxley Act focuses largely on accounting and auditing issues, but a few Sarbanes-Oxley provisions, like some NYSE and NASDAQ governance rules, are designed to influence corporate behavior by requiring disclosures that give shareholders more information about the company's corporate governance practices. For example, the SEC implemented rules pursuant to Section 406 of the Sarbanes-Oxley Act that require companies to disclose whether they have adopted (and if not, why not) a code of ethics for senior financial officers.[52] These rules also require companies that have adopted such a code of ethics to disclose

[48] NYSE *Listed Company Manual,* Rule 303A.02.

[49] NYSE *Listed Company Manual,* Rule 303A.09.

[50] NYSE *Listed Company Manual,* Rule 303A.10.

[51] Securities Exchange Act Release No. 34-48745 (Nov. 4, 2003).

[52] Final Rule: Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002, Securities Act Release No. 33-8177 (Jan. 23, 2003); *see also* technical corrections in Securities Act Release No. 33-8177A (Mar. 26, 2003).

immediately any change in or waiver of the code. Section 406 of Sarbanes-Oxley relies on disclosure and the threat of shareholder censure to push companies into adopting a code of ethics that will meet with shareholder approval, and to limit any waivers under the code. Similarly, SEC rules adopted pursuant to Section 407 of Sarbanes-Oxley require companies to disclose whether (and if not, why not) at least one member of the company's audit committee is a "financial expert."[53] Again, although expressed as a disclosure requirement, Section 407 relies on the power of shareholder pressure to push companies to include at least one financial expert on their audit committees.

[O] Majority Voting Policies

Over the past several years, shareholder activists have successfully pushed companies to adopt majority voting policies or bylaws, under which a director candidate in an uncontested election who does not receive a majority vote in favor of election is either not elected or must submit an offer of resignation to the board. Under the laws of most jurisdictions, directors are elected by plurality vote, so that a candidate in an uncontested election who receives even a single vote would be elected. In 2006, Delaware amended its General Corporation Law to facilitate the adoption by public companies of the majority voting standard.[54] Under these amendments, a director may submit a resignation that becomes irrevocable if the director fails to receive a specified vote for election. The amendments also provide that a shareholder-adopted bylaw specifying the required vote for the election of directors may not be amended or repealed by the company's board. As of July 2012, over 80% of S&P 500 companies had adopted a majority voting bylaw or policy.[55]

The widespread adoption of majority voting provisions has greatly enhanced the power of withhold authority campaigns. Originally conceived as a protest vote, under the majority voting provisions a successful withhold authority campaign now can result in removal of the targeted director or directors. The impact of this enhanced threat has been felt in

[53] *Id.*

[54] Del. Gen. Corp. Law §§ 141(b) and 216.

[55] Shark Repellent, Takeover Defense Trend Analysis, July 31, 2012.

recent proxy seasons, both in the greater prevalence of withhold authority campaigns, and in the greater responsiveness of companies to the requests of the institutional activists.

[P] Proxy Access Rules

In 2010, the SEC adopted rules for the inclusion of shareholder nominees in company proxy statements.[56] These rules included a new Rule 14a-11, setting forth the requirements, eligibility criteria, and other details with respect to proxy access, as well as amendments to Rule 14a-8 to permit proxy access shareholder resolutions so that shareholders may vote to adopt their own proxy access provisions on a company-by-company basis. The Delaware legislature previously enacted amendments to the Delaware General Corporation Law designed to facilitate bylaws that would implement proxy access on a company-by-company basis.[57] Prior to the amendments to Rule 14a-8, the SEC had held that proxy access shareholder resolutions could be omitted under Rule 14a-8(i)(8).

Rule 14a-11 provided that shareholders and shareholder groups who held at least 3% of the voting power of a company's securities continuously for at least three years would have the right to include nominees for director in the company's ballot and proxy statement.[58] Eligible shareholders and shareholder groups would have been entitled to nominate up to a maximum of 25% of the entire board. The Business Roundtable and the U.S. Chamber of Commerce challenged the legality of Rule 14a-11 and, in 2011, the U.S. Court of Appeals for the D.C. Circuit vacated the rules as "arbitrary and capricious."[59] The challenge did not attack the SEC's amendments to Rule 14a-8, however, and shareholders are now able to bring proxy access proposals under Rule 14a-8.

Proxy access would make it far easier for shareholders or groups to run board election contests. To the extent proxy access is adopted through

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[56] Final Rule: Facilitating Shareholder Director Nominations, Securities Exchange Act Release No. 34-62764 (Aug. 25, 2010).

[57] Del. Gen. Corp. Law § 112.

[58] Rule 14a-11(a), (b), and (c).

[59] *See* Business Roundtable and Chamber of Commerce of the United States of America v. Securities and Exchange Commission, No. 10-1305 slip op. (D.C. Cir. July 22, 2011).

shareholder proposals on a widespread basis, the disruption of such contests could become a regular feature of the corporate landscape every year. To the extent that increased numbers of dissident directors are elected, this could also disrupt the collegiality of the boardroom. And given the already increased demands placed on corporate directors in the current environment, the prospect of frequent and regular election contests could deter some well-qualified individuals from serving as directors. Companies have begun to advance these and other arguments in opposition to proxy access proposals brought by shareholders under Rule 14a-8. Of nine proxy access proposals brought to a vote in the 2012 proxy season, only two, both precatory proposals setting thresholds consistent with Rule 14a-11, achieved majority support.[60]

[Q] Dodd-Frank Act

While the primary focus of the Dodd-Frank Act[61] was financial reform, the Act also contains several governance and compensation-related provisions. For example, the Dodd-Frank Act includes provisions requiring the SEC to mandate disclosure of whether a company has separated its Chair and CEO positions and why (though it is unclear whether this mandate goes beyond the rules already adopted by SEC, discussed above, that require similar disclosure). It also requires the stock exchanges to prohibit broker discretionary voting in connection with the election of directors, executive compensation, or any other significant matter, as determined by the SEC. On the compensation-related side, as further discussed in Chapter 4, the Dodd-Frank Act contains provisions requiring companies to conduct advisory votes on compensation no less frequently than once every three years (with a separate advisory vote on the frequency of this "say-on-pay" vote); requiring an advisory vote on golden parachute compensation in connection with merger and acquisition transactions submitted to shareholders; setting independence standards for compensation committee members and advisers; requiring companies to adopt clawback policies applicable in the event of accounting restatements due to material noncompliance with financial reporting

[60] *See* The Institute of Delaware Corporate & Business Law, *Proxy Access Votes 2012*, at <http://blogs.law.widener.edu/delcorp/2012/05/21/proxy-access-votes-2012/>.

[61] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 111th Cong., 2d Sess. (2010) (the "Dodd-Frank Act").

requirements; and requiring additional compensation disclosures including the ratio between the CEO's compensation and the median compensation of all other employees.

[R] Proxy System Concept Release

In 2010, the SEC issued a wide-ranging concept release on the U.S. proxy system.[62] The release solicited comments on a number of specific issues, grouped within three general areas: (1) the accuracy, transparency, and efficiency of the voting process; (2) shareholder communications and shareholder participation in the proxy process; and (3) the alignment of voting power and economic interest. The release also welcomed comments on any other aspect of the proxy process.

In discussing the SEC's concerns with respect to accuracy, transparency, and efficiency, the release notes the use of securities intermediaries for the ownership of stock, and highlights the mechanical issues this structure raises in the distribution of proxy materials, the solicitation of voting instructions, and the voting and tabulation process. These issues include broker over-voting that may result from securities lending or failures to deliver, the ability to confirm that voting instructions have been accurately recorded, the ability to call back shares that are on loan in advance of a record date in order to be able to vote those shares, and the fees for broker distribution of proxy materials.

With respect to shareholder communications and participation, the release focuses on communications between issuers and beneficial owners who hold stock in street name, communications among shareholders with respect to matters presented to shareholders for a vote, the relatively low level of proxy participation by retail holders, and the possibility of interactive data formats in proxy statements. The release notes the NYSE's elimination of broker discretionary voting in director elections as one reason for focusing on the ability of issuers to identify and communicate with beneficial owners, and for the importance of increasing participation to limit the number of shares that cannot be voted.

The third area of focus in the release is the separation of voting power and economic interest that arises from a variety of sources, including hedging, securities lending, the use of derivative securities, and the

[62] Concept Release on the U.S. Proxy System, Securities Exchange Act Release No. 34-62495 (July 14, 2010).

gap between record dates and meeting dates. The release also discusses the role of proxy advisory firms that may influence or control a significant percentage of the vote in any company despite having no direct economic interest, potential conflicts these firms may have in formulating their voting recommendations, and concerns about factual inaccuracies in the reports issued by these firms. The release suggests possible responses, including enhanced disclosure, dual record dates (one for notice of the meeting and a second for voting that is closer in time to the meeting), expanded regulation of proxy advisory firms, and/or new regulations designed to align more closely voting rights and economic interest.

While the SEC has not yet proposed any new rules to address the issues raised by the 2010 concept release, the SEC is continuing to study these issues and may take action to try to address some of these issues in the future.

§ 10.03 PROXY CONTESTS AND SHAREHOLDER ACTIVISM

This section sets forth examples of the effect of the shareholder communications proxy rules and reforms on proxy contests and shareholder activism.

[A] Proxy Contests and Withhold Authority Campaigns

The shareholder communications rules make institutional shareholder participation in a proxy contest easier and allow more varying levels of participation in proxy contests. Shareholders who are not willing to go to the expense of a full-blown proxy solicitation are still able to circulate soliciting material or make oral solicitations so long as they do not seek their own proxy authority. The approach of simply mailing materials to or otherwise contacting a limited group of the largest shareholders, without formally soliciting a separate proxy, has become common practice for shareholder activists under the private solicitation rules. The ability of institutional shareholders to discuss their voting decisions in private and to announce their voting decisions publicly, the ability of institutional shareholder groups to engage in private lobbying of their members, and the advent of proxy advisory firms that discuss proxy contests with major shareholders and then make voting recommendations, have changed the dynamics of proxy contests and increased the likelihood of a dissident's success. The shareholder activists' ability under the rules to

solicit and lobby privately, combined with the widespread adoption of majority voting policies, have also given rise to the use of withhold authority campaigns as the functional equivalent of a proxy contest. And proxy access, if ultimately adopted on a widespread basis through shareholder proposals, carries the potential for a further explosion in proxy challenges to incumbent boards.

[1] Dissident Slates

Until the last few years, the number of election contests, particularly short-slate election contests in which the dissident seeks to replace a minority of the board, had been growing, and the success rate had been growing as well. The number of election contests abated somewhat in the 2010 through 2012 proxy seasons, perhaps in part due to the economic downturn and in part due to the pendency of the SEC's proxy access rules. But high-profile election contests have still continued, with a significant rate of success. And some have speculated that, now that the SEC's proxy access rules have been struck down and the SEC has stated that it has no current intention to repropose new access rules, the pre-2010 rise in election contests may resume.[63]

There were 116 election contests in each of 2008 and 2009, up from 99 in 2007, with 72% of the contests in each of 2008 and 2009, seeking less than majority representation, up from 67% in each of 2007 and 2008.[64] Dissidents won board seats, through a complete or partial election victory or through settlement, in 44% of the contests in 2009, up from 41% in 2008 and 39% in 2007.[65] Since then, the number of election contests has declined to 90 in 2010, 81 in 2011, and 71 in 2012. The success rate, however, has continued, with dissidents gaining board seats through election victories or settlement in about half of these contests.[66]

High-profile election contests in the 2011 and 2012 proxy seasons included Third Point's fight with Yahoo, Pershing Square's proxy contest with Canadian Pacific, Starboard Value's contest at AOL, Carl Icahn's

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[63] *See* Steven M. Davidoff, *Quiet Proxy Season Means Fewer Fights in the Boardroom*, N.Y. Times DealBook, May 3, 2011; Stephen Taub, *Fewer Proxy Fights This Year, And Fewer Activist Wins*, Institutional Investor, Sept. 27, 2010; ISS Preliminary 2011 U.S. Postseason Report at 11.

[64] Shark Repellent, Proxy Fight Trend Analysis, 2007-2009 (Nov. 15, 2010).

[65] *Id.*

[66] Shark Repellent, Proxy Fight Trend Analysis, 2001-2012 (July 21, 2012).

battles with Forest Labs, Clorox, CVR Energy, Genzyme and Mentor Graphics, and the threatened proxy fight at Occidental by Relational Investors and CalSTRS. These contests produced a range of outcomes. The Third Point contest with Yahoo and the Pershing Square contest with Canadian Pacific were particularly aggressive in their rhetoric. In each case, the dissident sought to oust the target's CEO and attacked with harsh language. Third Point's Dan Loeb, after discovering errors in Yahoo CEO Scott Thompson's résumé, wrote letters referring to a "botched CEO hiring process" and the "Board's unchecked value destruction," and stating that Thompson and lead director Patti Hart had "clearly demonstrated that they lack even the minimum qualifications for service as a director of the company." He also wrote, "It seems farcical to us that the Board will most likely spend more time deliberating over whether Mr. Thompson should be fired than it did properly vetting whether he should have been hired." Shortly after these letters, Yahoo and Third Point entered into a settlement under which Thompson stepped down as CEO and three of Third Point's four nominees, including Loeb, were added to the Yahoo board.[67] Pershing Square ran seven nominees in the Canadian Pacific battle, sought to replace CEO Frederic Green with its own candidate, E. Hunter Harrison, and suggested that their "border skirmish" could turn into "nuclear winter" if Green were not replaced. Notwithstanding this threat, Canadian Pacific decided to fight. After a "long, often bruising public battle," Pershing Square prevailed in electing all its nominees and removing Green as CEO. Six weeks later, Harrison was appointed as the new CEO.[68] In contrast, AOL was successful in defeating all three of Starboard Value's nominees, despite ISS's recommendation of two of the three and Glass Lewis's recommendation of one of the three.[69]

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[67] *See* Michael J. de La Merced, *Hedge Fund Intensifies Attack on Yahoo Amid Storm Over Padded Résumés*, N.Y. Times DealBook, May 4, 2012; Michael J. de La Merced, Hedge Fund *Third Point Calls for Interim C.E.O. at Yahoo*, N.Y. Times DealBook, May 4, 2012; David Benoit, *Thompson Ousted with Hardly a Mention as Yahoo Settles with Loeb*, Wall St. J. Deal Journal, May 13, 2012.

[68] *See* Steven M. Davidoff, *America's Export to Canada: Shareholder Activism*, N.Y. Times DealBook, Feb. 14, 2012; Rebecca Penty, *Bill Ackman's Hedge Fund Faces Toughest Battle Yet: Boost CP Profitability*, Calgary Herald, May 18, 2012; Heather Perlberg, *Ackman Puts Stamp on Canadian Pacific With New CEO*, Bloomberg, June 29, 2012.

[69] *See* William Launder and Jon Kamp, *AOL Wins Proxy Fight, Easing Pressure on CEO*, Wall St. J., June 14, 2012.

Carl Icahn continued a steady stream of proxy contests with mixed results. In the case of CVR Energy, Icahn's proxy fight was launched in support of a takeover bid that was ultimately successful, with Icahn gaining ownership of approximately 80% of the company's shares and seven of nine board seats.[70] Icahn's proxy fight and bid for Clorox, however, were unsuccessful, with Icahn ultimately withdrawing both the contest and the bid.[71] In the case of Genzyme, the fight was settled by the appointment of two Icahn designees to the Genzyme board. Within a year thereafter, Genzyme had agreed to be acquired by Sanofi in a $20 billion acquisition.[72] In the case of Mentor Graphics, the fight went all the way to the shareholders meeting and Icahn prevailed, with ISS's support, in electing all three of his nominees to Mentor's eight-person board.[73] In the 2011 Forest Labs fight, Icahn sought four seats on a ten-person board, but ISS recommended in favor of all of Forest Labs' nominees and none of Icahn's four. With ISS's support, Forest Labs succeeded in electing its entire slate and Icahn's nominees were all defeated.[74] However, Icahn came right back in 2012 to launch a second proxy fight against Forest Labs, again seeking four seats on the board. In contrast to 2011, in the 2012 fight, ISS recommended in favor of two of Icahn's nominees, while Glass Lewis recommended in favor of all of the company's slate.[75] One of the two Icahn nominees recommended by ISS was successful in winning election to the Forest Labs board.[76] Finally, in an example of a company successfully addressing concerns in order to avoid a battle,

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[70] *See* Jim Polson, *Carl Icahn Wins CVR Energy After $2.6 Billion Offer*, Bloomberg, May 17, 2012; Saabira Chaudhuri, *CVR Energy Receives No Acquisition Offers; Says Icahn Won't Sell*, Wall St. J., July 26, 2012.

[71] *See* Lauren Coleman-Lochner, *Icahn Withdraws Clorox Slate After Failing to Gain Support for Sale Plan*, Bloomberg, Sept. 23, 2011.

[72] *See* Chris V. Nicholson, *Sanofi Agrees to Buy Genzyme for $20.1 Billion*, N.Y. Times DealBook, Feb. 16, 2011; Robert Weisman, *Genzyme Deal Survived a Culture Clash*, Boston Globe, Feb. 20, 2011.

[73] *See Icahn Gets Backing from ISS on Mentor Graphics,* N.Y. Times DealBook, May 3, 2011; Mike Rogoway, *Mentor Graphics Shareholders Vote for Icahn's Slate,* The Oregonian, May 12, 2011.

[74] *See* Michael J. de la Merced, *Forest Labs Defeats Icahn in Proxy Fight*, N.Y. Times DealBook, Aug. 18, 2011.

[75] *See* Shannon Pettypiece, *Icahn Gets Proxy Adviser Support in Forest Labs Board Battle*, Bloomberg, Aug. 1, 2012; Meg Tirrell, *Forest Labs Board Wins Glass Lewis Backing in Icahn Proxy Fight*, Bloomberg, Aug. 2, 2012.

[76] *See* Meg Tirrell, *Icahn Wins One Seat on Forest Laboratories' Board*, Bloomberg, Aug. 15, 2012.

Relational and CalSTRS agreed not to go forward with a proxy fight after Occidental announced a number of policy changes relating to executive compensation, CEO succession planning, and director retirements.[77]

High-profile election contests in the 2009 and 2010 proxy seasons included Yucaipa's proxy fight at Barnes and Noble, the proxy fight by Air Products in support of its takeover bid for Airgas, Pershing Square's contest at Target, Exelon's proxy fight in support of its takeover bid for NRG Energy, Carl Icahn's proxy fight at Biogen-Idec, and the proxy contest at Amylin Pharmaceuticals, which drew two separate dissident slates, one from Icahn and one from Eastbourne Capital.[78] These contests also raised a number of issues and produced a range of results. Yucaipa lost its proxy fight, despite ISS support, after Barnes and Noble announced its intention to put the company up for sale. Inside ownership of over 30% at Barnes and Noble made Yucaipa's fight an uphill battle, notwithstanding Yucaipa's ownership of close to 20%. A third major shareholder, which was widely viewed as sympathetic to Yucaipa, ended up not being able to vote a portion of the shares that it beneficially owned, because it had loaned the shares as of the record date.[79] The Air Products-Airgas fight may have been one of the most interesting, as Air Products, after commencing a tender offer for Airgas, succeeded in electing three nominees to Airgas's staggered board, only to see its nominees join the rest of the Airgas board in opposing the Air Products bid. Ultimately, after the loss of two subsequent court decisions, one relating to the timing of Airgas's next annual meeting and one relating to the continued use by Airgas of its poison pill, Air Products withdrew its bid.[80]

In the Target proxy contest, Pershing Square agitated loudly for a universal proxy card, which would list the company nominees and the dissident nominees on one card and facilitate "vote splitting"—*i.e.*, voting for some company nominees and some dissident nominees. Under the current rules, a shareholder must use either the dissident's proxy card or

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[77] *See* Marc Lifsher, *CalSTRS Seeks to Unseat 4 Oxy Directors Over Executive Pay*, L.A. Times, Aug. 3, 2011; *CalSTRS and Relational Support Election of All Occidental Directors*, CalSTRS Press Release, Apr. 27, 2011.

[78] RiskMetrics Group 2009 Postseason Report, at 19.

[79] *See* Michael J. de la Merced, *Barnes & Noble Wins Battle Over Board*, N.Y. Times, Sept. 28, 2010.

[80] *See* Jeffrey Cane, *Airgas Board Rejects Air Products' Bid*, N.Y. Times DealBook, Dec. 22, 2010; Steven M. Davidoff, *Air Products Bid Dies as Airgas Poison Pill Lives On*, N.Y. Times DealBook, Feb. 15, 2011.

the company's proxy card to vote by proxy, making it difficult to split votes between the dissident nominees and the company nominees unless the shareholder actually attends the annual meeting or sends a representative to attend. In the Target proxy contest, ISS ended up recommending a vote for two of Pershing Square's five nominees and recommended using Pershing Square's proxy card to vote for those two nominees (and withhold authority on the other three), meaning shareholders who followed ISS's recommendation could not vote for any of the company's nominees. Notwithstanding this recommendation, all of the company's nominees, and none of Pershing Square's, were elected.[81]

The NRG Energy proxy contest was focused on Exelon's takeover bid, with NRG nominating a slate in an effort to take control of the NRG board and force a sale of the company. The NRG shareholders, in effect, rejected the Exelon bid by voting down Exelon's nominees. Following announcement of the election results, Exelon terminated its offer for NRG.[82] Icahn's contest at Biogen-Idec was his second in two years, following a failed effort by Biogen to sell itself in 2007. Icahn set out to take control of Biogen's classified board by nominating a slate of directors in 2008 and stating an intent to follow that with another slate in 2009. While none of his nominees was elected in 2008, he was successful in electing two of his four nominees in 2009. He then nominated a slate once again in 2010, but settled with the company in exchange for the company's agreement to add two new directors, one from Icahn's slate and one additional independent director. The company said the settlement was the result of "constructive dialogue" with Icahn, and also noted that it wanted to avoid the disruption of another proxy fight as it searched for a new CEO after the company's incumbent CEO announced his plan to retire.[83]

As noted earlier, the Amylin proxy fight presented the unusual situation of two separate dissident slates, with Icahn and Eastbourne Capital each nominating five candidates to a 12-person Amylin board. This presented a number of issues, including whether Icahn and Eastbourne could seek proxy authority to vote for the other's nominees under

[81] *See* Zachery Kouwe and Joe Nocera, *Shareholders Support Target Over Ackman*, N.Y. Times DealBook, May 28, 2009.

[82] *See* Mark Peters, *NRG Holders Balk; Exelon Drops Bid*, Wall St. J., July 23, 2009.

[83] *See* Robert Weisman, *Biogen Idec, Icahn Reach Deal on Board*, Boston Globe, Mar. 23, 2010.

Rule 14a-4(d)—the SEC ruled they could[84]—and whether the election of seven or more of the dissident nominees would trigger change of control provisions in Amylin's debt. To avoid the debt change of control issue, Eastbourne ultimately pared its slate back to three nominees and Icahn to two, with each seeking proxy authority to vote for the other's nominees and then rounding out with company nominees. Two dissidents were elected, one from Eastbourne's slate and one from Icahn's slate, with the CEO and the lead director of the company being ousted.[85]

The 2008 proxy fight by The Children's Investment Fund (TCI) and 3G Capital (3G) for seats at CSX Corporation illustrates the difficulties in bringing litigation against a dissident even when the dissident has violated legal requirements. In a case brought by CSX, TCI and 3G were found by a federal district court to have violated the federal securities law's 13(d) rules by failing to disclose their joint activities as a group and TCI's derivative ownership position in CSX total return swaps.[86] Despite the ruling, the court did not enjoin the voting of TCI's and 3G's shares at the 2008 annual meeting, and the dissidents won four seats on CSX's 12-member board. In 2011, the decision was partially vacated by the Second Circuit Court of Appeals.[87]

The Heinz-Trian proxy fight in 2006 illustrates the operation of a number of the shareholder communications rules. In anticipation of an August 2006 annual meeting, the two sides began positioning themselves with shareholders as early as March, filing a series of statements and counterstatements under Rule 14a-12. Heinz and Trian did not file preliminary proxy statements until June, and their proxy statements were not finalized and mailed until July. By then, the proxy fight had already been going for four months, with Trian having presented its "Trian Action Plan" to Heinz shareholders, including posting its plan on its proxy fight Web site, and Heinz having presented to shareholders its "Superior Value and Growth Plan." With no SEC pre-review of any of the materials other than the proxy statements, one observer characterized the fight as "one of

[84] SEC No-Action Letter, *Application of Rule 14a-4(d)(4) to Solicitation for Proposed Minority Slate of Icahn* (Mar. 30, 2009).

[85] *In Victory for Icahn, Amylin Chairman Is Ousted,* N.Y. Times DealBook, June 2, 2009.

[86] *CSX Corp. v. Children's Inv. Fund Mgmt. (UK) LLP,* 08 Civ. 2764 (LAK) (S.D.N.Y. June 11, 2008).

[87] *CSX Corp. v. Children's Inv. Fund Mgmt.*, No. 08-2899-cv, slip op. (2d Cir. July 18, 2011).

the nastiest proxy contests ever, with mudslinging over which candidates have been sued the most, barbs about personal character and both sides accusing the other of stealing their ideas."[88] As the annual meeting date drew closer, the major proxy advisory firms issued recommendations on the fight, with ISS recommending in favor of three of Trian's nominees, Glass Lewis recommending in favor of two Trian nominees, Proxy Governance recommending in favor of one Trian nominee, and Egan-Jones recommending in favor of the entire Heinz slate.[89] CalPERS, PNC Financial, and several other institutional shareholders publicly announced their intentions to vote in favor of the Heinz slate, as highlighted in Heinz press releases. The Heinz fight also highlighted the lack of an effective mechanism for shareholders to split their votes, an issue noted above in the context of the Target proxy fight in 2009.

[2] Testing the Waters

The shareholder communications rules have also given dissidents contemplating a proxy contest the ability to "test the waters" by consulting with major shareholders before commencing a proxy solicitation. In an early example following adoption of these rules, Kirk Kerkorian and his lieutenant, Jerome York, spoke with a number of major Chrysler shareholders in anticipation of a possible proxy contest seeking representation on the Chrysler board of directors.[90] After finding most of Chrysler's major shareholders generally happy with the company, Kerkorian ultimately agreed to a settlement and standstill with Chrysler under which Kerkorian gained one board representative and Chrysler elected another, mutually agreed, outside director.[91] Similarly, Carl Icahn, in the wake of his unsuccessful effort with Bennett LeBow to gain control of the board of RJR Nabisco, began contacting major RJR shareholders to discuss the possibility of mounting a new proxy challenge to RJR.[92] In recent years, hedge funds and other activists have communicated frequently with major institutional shareholders and are generally in a

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[88] Patricia Sabatini, *As Nasty Heinz Fight Nears End, Observers Weigh In,* Pittsburgh Post-Gazette, Aug. 10, 2006.

[89] *Id.*

[90] *Interview—York Finds Chrysler Holders Upbeat,* Reuters, Jan. 2, 1996.

[91] *See Chrysler CEO Pleased with Kerkorian Deal,* Reuters, Feb. 11, 1996.

[92] *See* Glenn Collins, *Icahn Says He May Renew Proxy Fight at RJR Nabisco,* N.Y. Times, June 7, 1996, at D2.

position to gauge shareholder sentiment before deciding whether to bring a proxy contest or other challenge.

This ability to test the waters is also available to takeover bidders contemplating a concurrent proxy contest to pressure the target into accepting the bid. For example, one noted proxy solicitor reports that this flexibility played a role in three hostile bids that turned quickly into negotiated acquisitions: IBM's bid for Lotus Development, Ingersoll Rand's bid for Clark Equipment, and FMC's bid for Moorco. In the context of these bids, "there was little question that IBM, Rand and FMC were able to poll institutional investors beforehand thanks to the relaxed rules, and were confident of prevailing in a proxy fight. Instead, each had only to write a little larger check."[93]

In 1998, the SEC proposed further amendments to the proxy rules that would have extended the ability to "test the waters," without filing proxy materials, to companies and management.[94] The rules as adopted in 1999, however, expressly declined to adopt the "test the waters" provisions.[95] While the 1999 rules expanded the ability of companies to communicate with shareholders, the SEC based its decision not to adopt the even broader "test the waters" proposal on the basis that "it could result in unregulated and secret solicitations." Nevertheless, with the expanded ability to communicate with shareholders, and the increased investor relations focus on regular communication with major shareholders, companies are often able to predict the reactions of their major shareholders to any given proposal without having to test the waters formally. This in turn affects the company's decision as to whether to make the proposal. This effect is one more way in which the shareholder communications rules have enhanced the influence of large institutional shareholders.

[3] Elimination of Preliminary Filing Requirements

The elimination of preliminary filing requirements, and thus of preliminary SEC review, for supplemental proxy materials has a particular

[93] Daniel H. Burch and Stanley J. Kay, *A Proxy Solicitor's Highlights of the 1995 Proxy Contests: The Impact of the "New" Proxy Rules,* Corp. Governance Advisor, Sept./Oct. 1995, at 37.

[94] Regulation of Takeovers and Security Holder Communications, Release No. 33-7607 (Nov. 3, 1998).

[95] Regulation of Takeovers and Security Holder Communications, Release No. 33-7760 (Oct. 22, 1999), at Section II.C.1.c.

effect on proxy contests, where the more contentious and argumentative statements are often found in the supplemental materials rather than in the basic proxy statement. Prior to the 1992 amendments, the SEC generally performed a moderating function in proxy contests, tempering the more aggressive materials and forcing the contestants to provide factual support for their arguments and assertions. Now, the SEC no longer performs this function for most of the materials used in the contest. While all proxy materials continue to be subject to the antifraud rules, enforcement of antifraud provisions in the courts is much more difficult and cumbersome than the reviews previously conducted by the SEC.

Unlike the private solicitation rules, however, which clearly give shareholder activists and dissidents more leverage, the elimination of prescreening applies equally to management and dissident materials. Proxy fights following this change in the rules have shown an aggressive, hard-hitting style.[96] For example, in the proxy fight waged by Carl Icahn and Bennett LeBow to force RJR Nabisco to spin off its food operations, Icahn and LeBow ran full-page advertisements, including one with the headline, "RJR to Shareholders: Drop Dead."[97] For its part, RJR's advertisements included one that said LeBow had wiped out $5 billion of stock market value for RJR and other tobacco companies when Liggett Group, under LeBow's control, agreed to a settlement of a class-action lawsuit brought on behalf of smokers.[98] More recently, as noted above, the 2012 proxy fights between Third Point and Yahoo and between Pershing Square and Canadian Pacific were noted for their particularly aggressive rhetoric, and the 2006 Heinz-Trian proxy fight was dubbed "one of the nastiest proxy contests ever."[99]

[4] Commencement of Proxy Solicitations

The immediate public availability of preliminary filings and the ability to commence solicitations even before filing of a proxy statement combine to give a dissident the ability to commence a proxy contest

[96] Steven N. Gorfman and James K. Baer, *Fight Letters: An Effective Tool in Proxy Contests,* Insights (May 1996), at p. 12.

[97] Hal Lux, *Internet Becomes Tool in Nabisco Proxy Fight; Icahn and LeBow Take Their Message to the Web,* Investment Dealers' Digest (Jan. 29, 1996).

[98] *RJR Attacks LeBow in Paper Ad,* L.A. Times, Mar. 16, 1996, at D2.

[99] Patricia Sabatini, *As Nasty Heinz Fight Nears End, Observers Weigh In,* Pittsburgh Post-Gazette, Aug. 10, 2006.

quickly. These rules allow a dissident to spring a contest shortly before a shareholders meeting, giving the company little time to respond. With the increasingly concentrated institutional ownership of public companies, such a "surprise attack" may be a viable dissident strategy in some cases. As with the elimination of prescreening of supplemental proxy materials, however, the ability to commence solicitation activities before filing a proxy statement provides increased flexibility to management solicitations as well as dissident solicitations.

The increased use of the Internet for proxy solicitations also increases the viability of a surprise attack strategy. As far back as 1996, a group of investors in Professional Bancorp, a California-based community bank holding company, successfully mounted a proxy fight to win control of the board in under three weeks using a Web site, where their proxy materials and fight letters, as well as their court complaint, were instantly posted and accessible to shareholders. Press reports described the battle as "far more of a blitzkrieg than the drawn-out siege usually required to topple management."[100] Other groups since then have looked to the Internet as a forum for ongoing shareholder activism and potential proxy contests. For example, the Web site "eRaider.com" was launched in 2000, affiliated with an investment fund, whose stated purpose was to take positions in "underperforming" companies and then use the Web site to solicit shareholder discussion and agitate for change in the targeted companies.[101] More mainstream institutional activists, such as CalPERS, now also maintain Web sites devoted to their corporate governance activities.[102]

The speed of communication over the Internet has made it an increasingly effective weapon in proxy contests. Dissident Web sites are now a standard feature in proxy contests. These can be used to collect and disseminate information, as well as to facilitate communications among shareholders. In addition, independent chat rooms are often used by shareholders to discuss matters of interest with respect to their companies, including issues raised by proxy contests, which has been encouraged by the SEC's adoption of rules to facilitate electronic shareholder

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[100] Jeffrey Marshall, *Web Helps Proxy Insurgents Capture Bank,* U.S. Banker, Jan. 1997, at 42.

[101] Kate Berry, *A New Activist Fund Will Test Web's Clout,* N.Y. Times, Mar. 19, 2000, Sec. 3, at 10.

[102] *See* <http://www.calpers-governance.org>.

forums.[103] And as discussed above, the SEC's adoption of e-proxy rules in 2007, requiring Web site posting and permitting electronic distribution of proxy materials, further enhances the use of the Internet for proxy fights with greater efficiency and reduced cost.[104]

To address the surprise attack issue, many companies have adopted advance notice bylaw provisions setting forth procedures, including specified time frames, for shareholders who wish to make director nominations or bring any other business before a shareholders' meeting. The increased flexibility under the rules as to a dissident's timing of a proxy contest makes it all the more important that a company's bylaws contain such provisions. Model bylaw provisions for this purpose appear at the end of this chapter as Exhibit 1. This model was designed for a Delaware company and updated in 2010 to reflect a requirement for enhanced disclosure of derivative positions and other recent developments. The model assumes that shareholders cannot call special meetings and includes other provisions that may not be applicable to all companies.

[5] Announcement of Voting Decisions

The unfettered right of shareholders under the communications rules to make public announcements of their voting decisions (and the reasons for their decisions) adds another means of soliciting votes in a proxy contest. The ability to announce and generate publicity for voting decisions in the last days before the shareholders' meeting can be used to try to swing momentum at the end of a close proxy contest. CalPERS now regularly discloses on its governance Web site how it voted its top 300 equity holdings, while other organizations, such as the State of Wisconsin Investment Board ("SWIB") and Teachers Insurance and Annuity Association–College Retirement Equities Fund ("TIAA-CREF"), issue press releases periodically with respect to their voting positions on certain proxy issues. CalPERS and various union activists also regularly make announcements with respect to companies they are targeting for withhold authority campaigns or other proxy campaigns.

As noted above, the SEC has adopted rules requiring mutual funds and other registered management investment companies to disclose information on how they cast their proxy votes, as well as on their voting

[103] Rules 14a-2(b)(6) and 14a-17.
[104] Rule 14a-16.

policies and procedures, and the Dodd-Frank Act includes a requirement that all institutional investment managers disclose how they voted on the say-on-pay votes required by the Dodd-Frank Act. These rules have the effect of increasing the kind of shareholder pressure created by public announcement of voting decisions. Under these rules, a broad class of institutional shareholders, not just shareholder activists, must make public their views on matters put to a shareholder vote, thereby exposing to public view any dissatisfaction with or criticism of a company's proposals. The requirement that mutual funds make their voting decisions public also increases "the pressure on the funds to support challenges to management on hot-button issues." Damon Silvers of the AFL-CIO has noted that, with this rule, "I think we'll be seeing votes we should have seen before."[105]

In addition, proxy advisory firms, such as ISS and Glass Lewis, make voting recommendations to shareholders in contested proxy situations, and these recommendations are widely publicized. Some have estimated that the ISS recommendation can "swing as much as 25% of the votes in proxy contests."[106] Over the last several years, Glass Lewis has also been gaining increasing influence in contested situations. Both firms typically support some or all of the dissident nominees in a very significant number of proxy contests, and they have been a major factor in the increasing level of success of dissidents in these contests. As with the concentration of institutional influence, there are some who question whether these firms' concentrated power over proxy contests is healthy. As discussed above, one of the issues addressed by the SEC's July 2010 proxy system concept release is the role of these firms in the proxy voting process and the potential conflicts of interest they may have.

Public announcement of voting decisions has also been used outside proxy contests as a means of expressing institutional shareholder discontent with corporate policies or management. In particular, "just say no" campaigns, as described below, rely on the announcement of an intention to vote against or withhold authority from management board nominees as a way to publicize their unhappiness with targeted companies.

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[105] Tom Petruno, *A New Era for Investor Activism?,* L.A. Times, Mar. 7, 2004.

[106] Amy Borrus, *A Quiet Guru's Enormous Clout,* Bus. Wk., May 20, 2002, at 64.

[6] Withhold Authority Campaigns

Short of a full-blown election contest, the withhold authority campaign has become the activists' weapon of choice to bring pressure to bear on directors to take corporate actions or to implement governance changes that the activists desire. Under a withhold authority campaign, shareholders vote to withhold proxy voting authority to vote for one or more of the company's nominees in an uncontested election as a means of expressing disapproval of an action the company or board has taken or failed to take. The widespread adoption of majority voting policies and bylaws, under which a company nominee who does not receive a majority vote in favor of election is either not elected or must submit a resignation to the board, greatly enhances the power of the withhold authority campaign.

The SEC's shareholder communications rules—particularly the ability of shareholders to talk to each other in private and solicit support without filing proxy materials, as well as the ability of shareholders to publicly announce their voting decisions—have made effective withhold authority campaigns possible. But the tactic was slow to gain momentum. From the mid-1990s until 2004, only a handful of companies were typically targeted for withhold authority—or so-called "vote no"—campaigns each year.[107] Starting with the 2004 proxy season, however, the number of withhold authority campaigns exploded, targeting a wide range of companies and garnering a majority vote for the first time in the case of Federated Department Stores. In the well-publicized Disney case, a 45% withhold vote against Michael Eisner led to his decision to step down as CEO and to resign from the board. But the 2004 proxy season also saw the more blunderbuss approach of proxy advisory firms such as ISS, as well as public pension and union activists such as CalPERS, AFL-CIO, and AFSCME, who recommended or cast withhold authority votes at hundreds of companies. Indeed, one report indicates that CalPERS may have cast withhold authority votes at as many as 2,700 companies, or roughly 90% of its portfolio, in the 2004 proxy season.[108] ISS began publishing an extensive list of corporate actions, such as adopting or renewing a poison pill without shareholder approval, that would lead to a

[107] *See, e.g., So Far, Three Companies Are Targeted for Vote-No Campaigns,* IRRC Corp. Governance Highlights, Mar. 16, 2001, at 41.

[108] Phyllis Plitch, *Grundfest Waited Since 1990 for Vote-No Campaigns to Pop*, Dow Jones Newswire, Apr. 28, 2004.

withhold authority recommendation with respect to any of the offending company's directors who were up for election. As a result, these withhold authority recommendations and votes extended to a wide range of well-regarded directors and companies, including famed investor Warren Buffett. The indiscriminate use of withhold authority votes may also have generated a backlash, leading many to question whether the activists had gone too far.[109]

Since 2004, the incidence of withhold authority campaigns has steadily declined. While this may be, in part, a reaction to the backlash, it appears also to reflect the greater responsiveness of companies facing the prospect of new withhold authority campaigns and the enhanced threat of those campaigns in light of majority vote policies. Indeed, proxy advisory firms like ISS have actually added to their lists of policy reasons for withhold authority recommendations each year, but ended up steadily reducing the percentage of directors subject to withhold authority recommendations since 2004.[110] The logical conclusion is that more companies have been complying with ISS's policy guidelines to avoid a withhold authority recommendation. And this may be seen starkly in the number of companies that have, for example, eliminated their poison pills, declassified their boards, and adopted majority voting policies. In 2002, approximately 60% of S&P 500 companies had poison pills. By 2012, the percentage had declined to approximately 10%. Similarly, over the same period, the percentage of S&P 500 companies with classified boards declined from about 60% to approximately 25%. And as noted above, by July 2012, over 80% of S&P 500 companies had adopted a majority voting bylaw or policy.[111]

According to ISS, in the 2009 proxy season, 91 directors at 49 U.S. companies received a majority withhold vote, almost three times greater than the number in 2008, but only six of these companies, affecting 12 directors, were S&P 500 companies. Perhaps because of the less widespread adoption of majority voting policies at smaller companies, ISS

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[109] *See id.* (quoting former SEC commissioner Joseph Grundfest as saying that the barrage of withhold authority votes "raises the concern that shareholders will have a mechanistic, check the box mentality, rather than a carefully measured assessment about the best interests of the entity and of the shareholders"); Tom Petruno, *To Foes, CalPERS Needs to Check Itself,* L.A. Times, May 23, 2004.

[110] RiskMetrics Group 2008 Postseason Report, at 33.

[111] Shark Repellent, Poison Pills in Force Year over Year (July 31, 2012) and S&P 1500 Classified Board Trend Analysis (July 31, 2012).

reports that none of these directors stepped down from their boards. Two of the companies had majority voting policies that required the directors to offer their resignations, but the resignations were not accepted.[112] The Delaware Supreme Court has confirmed the ability of a board to reject resignations under these circumstances.[113] Consistent with the recent downturn in proxy contests, by 2011 only 43 directors of U.S. companies received a majority withhold vote, with only four of these directors at S&P 500 companies. Almost 60 S&P 500 company directors, however, received withhold votes over 30%, a level generally sufficient to send a loud and compelling message.[114] In the 2012 proxy season, ISS recommended a withhold or against vote for only 3% of director nominees at S&P 500 companies and, of these relatively few directors who received a negative recommendation, only 9% failed to receive a majority vote.[115]

[B] Shareholder Activism

Perhaps equally important as the use of the shareholder communications rules in conjunction with a formal proxy contest is the ability to conduct a private solicitation outside the full-blown proxy contest arena. The communications rules have increased the likelihood of success of Rule 14a-8 shareholder proposals as well as efforts to defeat management proposals that activists may oppose. The shift in power from management to institutional shareholders, and the increased likelihood of success that the rules give a proxy contest or a withhold authority campaign, have also made it easier for institutional activists to bring pressure to bear through direct negotiation with a company. In recent years, companies have been more willing to make concessions to the activists—to implement proposals advanced by the activists and to seek to negotiate compromises—in order to avoid a shareholder proposal or proxy fight.

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[112] RiskMetrics Group 2009 Postseason Report, at 17.

[113] *City of Westland Police & Fire Ret. Sys. v. Axcelis Techs., Inc.*, No. 594, 2009 (Del. Sup. Ct. Aug. 11, 2010).

[114] ISS, *Preliminary 2011 U.S. Postseason Report* at 15-17.

[115] Alan Prince and Will Ledbetter, *2012 Proxy Season Update*, Thomson Reuters Business Law Currents (July 17, 2012).

[1] Targeting Large Shareholders

As with an election contest or withhold authority campaign, the shareholder communications rules permit activists, without filing their own proxy materials, to attempt to persuade large institutional holders in private to vote against a management proposal or in favor of a Rule 14a-8 shareholder proposal, so long as the activist does not seek its own proxy authority. This type of limited and targeted solicitation campaign can be very cost effective. For example, shortly after adoption of the rules, the State of Wisconsin Investment Board ("SWIB") began targeted solicitations in favor of shareholder resolutions or against management proposals that focused on mailings to large shareholders and follow-up discussions with major institutions. In a solicitation in favor of a shareholder proposal it filed with Allergan, seeking to require a shareholder vote on the company's shareholder rights plan, SWIB mailed materials in support of the proposal to almost all shareholders with 1,000 shares or more, did extensive follow-up with large institutions, and generated a majority vote in favor of the proposal.[116] Patricia Lipton, the executive director of SWIB, stated, "The new rules certainly were the difference in this contest."[117] Ms. Lipton stated that the cost of these efforts "generally ranged from $1,500 to $5,000," compared to the hundreds of thousands of dollars that may be spent on a full-fledged proxy contest.[118]

More recently, but prior to the economic downturn, hedge fund activists began using the private solicitation rules to wage campaigns against mergers and acquisitions as a means of trying to pressure the buyer to increase its price. For example, after Novartis agreed in late 2005 to acquire the 56% of Chiron it did not already own for $45 per share, hedge fund ValueAct Capital, a large Chiron shareholder, began a campaign contending that the price was too low. After another large shareholder also publicly criticized the deal, and ISS issued a recommendation that Chiron shareholders vote against the transaction, Novartis agreed to increase its bid to $48 per share, thereby gaining the support of the

[116] Patricia Lipton, *Experience Under the New Executive Compensation and Shareholder Communications Rules,* Corp. Governance Advisor, Jan./Feb. 1994, at 33.

[117] *Id.*

[118] Lipton, *Experience Under the New Executive Compensation and Shareholder Communications Rules,* Corp. Governance Advisor, Jan./Feb. 1994, at 33.

dissident shareholders.[119] This same tactic was used in the 2007 proxy season to oppose private equity buyouts and/or hold out for a higher price. Shareholders voted down buyouts at Eddie Bauer, Cablevision, and Lear and successfully forced an increase in price in the Clear Channel buyout after a number of hedge fund and institutional shareholders announced they would be voting against the deal.[120] With the economic downturn starting in 2008, and the related decline in takeover activity, this type of opposition to mergers and acquisitions evaporated. But as the economy recovers and mergers and acquisitions activity picks up, we may expect to see these tactics implemented again in the future. For example, in the context of Rock-Tenn's acquisition of Smurfit Stone in 2011, three hedge funds wrote a joint letter stating their intention to vote against the transaction on the ground that the price was too low. They did not, however, follow through with a proxy campaign against the transaction, which was approved by a wide margin.[121]

[2] Pressing for Corporate Changes

Shareholder activists have also used the communications rules to press affirmatively for major corporate changes, such as a corporate restructuring or replacement of management. Citing the ability of shareholders to communicate more freely with each other under the shareholder communications rules, Professor Steven Kaplan of the University of Chicago stated, "Shareholders are figuring out how to use those changes. They can now go to other large shareholders and say, 'We don't like this guy. Come argue along with us.'"[122] Another commentator has observed that the communications rules permit corporate raiders and activist investors to use proposal campaigns as a substitute for the hostile

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[119] Paul Elias, *Novartis Raises Chiron Bid to About $5.4B,* Associated Press, Apr. 3, 2006.

[120] Ted Allen, *Shareholders Object to More Private Equity Buyouts,* RiskMetrics Group 2007 Postseason Report, at 21; *Investors Turn Down Cablevision Buyout,* Associated Press, Oct. 25, 2007.

[121] *See* Michael J. de la Merced, *Activist Funds Oppose Smurfit-Stone's RockTenn Deal,* N.Y. Times DealBook, Feb. 2, 2011; *Rock-Tenn Company and Smurfit-Stone Container Corporation Shareholders Approve Merger,* RockTenn Press Release, May 27, 2011 (over 91% of Smurfit-Stone shares voting at the meeting voted in favor of the merger).

[122] Nancy Millman, *Doing the CEO Bounce: Shareholder Activism Is Shaking Up That Old Gang at the Top,* San Diego Union-Tribune, Mar. 30, 1997, at I1.

tender offers of the 1980s, allowing the investor "to see a potentially larger gain for a smaller investment of time and money."[123]

Carl Icahn is a notable example of an activist who has used the communications rules to wage a number of battles over the last decade. For example, he successfully pressured Nabisco into selling its foods business, and subsequently bought into General Motors in hopes of agitating for a spin-off of General Motors' subsidiary, Hughes Electronics (though he later sold out of his General Motors investment).[124] Icahn surfaced again in 2005, running a successful proxy contest for three board seats at Blockbuster, pressuring Kerr-McGee into selling assets and buying back stock with the threat of an election contest, and threatening to run a proxy contest for one or more board seats at Time Warner's 2006 annual meeting as part of a successful effort to pressure the company into a successful major stock buyback, as discussed in Chapter 12.[125] Icahn followed his campaign for a large stock buyback at Time Warner with a proxy fight for a seat on Motorola's board in an effort to force a similar stock buyback or dividend there.[126] While Icahn's 2007 proxy fight at Motorola was unsuccessful, his renewed threat of a proxy contest in 2008 ultimately resulted in a settlement under which two Icahn nominees joined the Motorola board. As noted above, Icahn ran proxy contests in the 2010 and 2011 proxy seasons at Genzyme, Mentor Graphics and Forest Labs, and in the 2009 proxy season at Biogen-Idec and Amylin Pharmaceuticals. Within a year after Icahn put two nominees on the Genzyme board, the company was sold. Although the Biogen contest was unsuccessful, Biogen's CEO subsequently announced his retirement and, in 2010, the company agreed with Icahn to add two new directors rather than face another proxy fight.[127] Shareholder pressure has also played a role in

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[123] Patrick S. McGurn, *Four "N's" Underpin Activism in 1996,* IRRC Corp. Governance Bull. (Oct.-Dec. 1995) at 15.

[124] Julie Creswell and Mark Borden, *Raiders Reborn*, Fortune, July 10, 2000, at 36; John Schnapp, *Icahn Promises to Shake Up and Slim GM,* Detroit News, Sept. 10, 2000, at 9; Alex Berenson, *Icahn Sells Entire General Motors Stake a Month After Purchase,* N.Y. Times, Sept. 22, 2000, at C1.

[125] *See* Seth Sutel, *Icahn to Propose Time Warner Candidates,* Associated Press, Sept. 12, 2005; Siklos and Sorkin, *Time Warner and Icahn Reach a Settlement,* N.Y. Times, Feb. 18, 2006.

[126] Sinead Carew, *Icahn Asks Motorola Holders to Vote Him to Board,* Reuters, Mar. 12, 2007.

[127] Robert Weisman, *Biogen Idec, Icahn Reach Deal on Board*, Boston Globe, Mar. 23, 2010.

management changes at a number of other companies including, as noted above, at Yahoo and Canadian Pacific in the 2012 proxy season.

Hedge fund activism has increased steadily over the last decade, with threatened or actual proxy contests as a means of pressuring companies to sell or restructure themselves. A notable example is Pershing Square Capital, which threatened proxy contests at Wendy's and McDonald's, and commenced a proxy contest at Ceridian, in each case as a means of pushing for spin-offs at each company.[128] Following Pershing's run at Wendy's, Nelson Peltz's Trian hedge fund took up the fight for more changes, ultimately obtaining three seats on the Wendy's board.[129] Thereafter, Wendy's went forward with a spin-off of its remaining stake in Tim Horton's, while Ceridian put itself up for sale after commencement of the Pershing Square proxy fight, ultimately agreeing to a private equity buyout.[130] In the 2009 proxy season, Pershing Square ran a high-profile proxy contest at Target, following Target's rejection of a series of real estate proposals advanced by Pershing Square. However, Pershing Square's slate did not run on a platform related to the real estate proposals; instead, Pershing Square advanced the argument that its nominees were better qualified than Target's. As noted above, none of the Pershing Square nominees was elected. Shareholder pressure and threatened proxy contests from the likes of Trian, Pershing Square, Jana Partners, and Ralph Whitworth's Relational Investors have also been credited as serving as catalysts for spinoffs at Kraft, ITT and McGraw-Hill, among others, in 2011 and 2012.[131]

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[128] *See* Dennis Berman, *Ackman to Run Own Slate of Directors at Ceridian,* Wall St. J., Jan. 23, 2007; *McDonald's Investor Wants Real Estate Spinoff,* Associated Press, Nov. 15, 2005; *Wendy's to Sell Part of Tim Horton's Chain,* Associated Press, July 29, 2005.

[129] Barnaby Feder, *Wendy's Gives Fund Three Seats,* N.Y. Times, Mar. 3, 2006.

[130] *Wendy's Shares Rise After Spinoff,* Associated Press, Oct. 2, 2006; Neil St. Anthony, *Ceridian Agrees to a $5.3 Billion Buyout,* Minneapolis Star Trib., May 30, 2007.

[131] *See* Gina Chon, Anupreeta Das and Paul Ziobro, *Activists Pressed for Kraft Spinoff,* Wall St. J., Aug. 4, 2011; James R. Hagerty, Gina Chon and Anupreeta Das, *ITT Plans Breakup as Bigness Loses Favor,* Wall St. J., Jan. 13, 2011; Azam Ahmed and Michael J. de La Merced, *To Lift Stock, McGraw-Hill Will Split in Two,* N.Y. Times DealBook, Sept. 12, 2011.

[3] Union Activists

The shareholder communications rules have also encouraged the entry of another class of shareholder activists, the labor unions. In the last two decades, labor unions have been among the most active shareholders in bringing Rule 14a-8 shareholder resolutions, joining the public pension funds as leading shareholder activists.[132] One commentator states, "Union-affiliated groups have mounted a well-coordinated strategy with other labor groups and public pension funds of picking companies and issues. The SEC's rule changes in the early 1990s letting shareholders openly discuss proxy strategies among themselves has aided that effort."[133] Union groups such as AFL-CIO and AFSCME joined with public pension activists such as CalPERS to spearhead the explosion of withhold authority campaigns that began with the 2004 proxy season.[134] Some CalPERS critics have accused the pension fund of being "driven by a union agenda."[135] And unions have been a key force behind the campaign for proxy access and other legislative and regulatory governance proposals.

Union activists have also played the major role in seeking to require majority voting for directors starting with the 2005 proxy season. The United Brotherhood of Carpenters and Joiners, led by its director of corporate affairs, Ed Durkin, spearheaded the campaign, filing more than 40 of these proposals itself. Durkin also led a group studying issues related to majority voting, which included representatives of other unions as well as representatives of 13 major companies that agreed to join the group in exchange for withdrawal of majority voting proposals in the 2005 proxy season.[136] As noted above, majority voting has now been widely adopted among the S&P 500 companies.

In 2006, a number of unions and affiliated pension plans established CtW (Change to Win) Investment Group to organize activism and

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[132] *See* James E. Heard and Jill Lyons, *Labor Unions and Public Funds Set Active Shareholder Agenda for 1995,* INSIGHTS 3 (Dec. 1994); *Labor Again Takes Lead Role in Activism,* IRRC Corp. Governance Bull. (Nov.-Dec. 1994) at 3; *Chalk Up Five More* "Wins" *For the Unions,* IRRC Corp. Governance Highlights (May 10, 1996) at 48.

[133] Vineeta Anand, *Labor Learns Lesson Well; Unions Use Activism as Tool Against Target Companies,* Pensions & Investments, Apr. 3, 1995, at 24.

[134] *See, e.g., AFSCME Joins Campaign to Withhold Votes for Directors,* IRRC Corp. Governance Highlights, May 14, 2004, at 107.

[135] Tom Petruno, *To Foes, CalPERS Needs to Check Itself,* L.A. Times, May 23, 2004.

[136] *See* ISS Preliminary 2005 Postseason Report at 5.

proxy challenges at selected companies. CtW has become progressively more active in subsequent proxy seasons, weighing in on withhold authority campaigns, including at Caremark, Washington Mutual, and Morgan Stanley, and on other issues, including campaigns to declassify the Merrill Lynch board, to force Long's Drug Stores to conduct an auction sale, and to rescind golden parachute payments for Allied Waste executives.[137]

In the 1996 and 1997 proxy seasons, some labor unions attempted a new proxy tactic in an effort to circumvent the procedures and restrictions set forth in Rule 14a-8. The tactic involved sending a notice to a company after the Rule 14a-8 deadline, but well in advance of the company's annual meeting, stating that the union intended to bring a shareholder proposal to the company's annual meeting and arguing that, because the company had notice of the proposal a reasonable period of time before the meeting (even though too late to be included in the company's proxy statement under Rule 14a-8), the company did not have discretionary authority under Rule 14a-4 to vote proxies against the proposal. This left the company with the choice of either including information about the proposal, and the intended vote of management proxies on the proposal, in its proxy statement, even though the union did not comply with Rule 14a-8, or facing the possibility that the company would not have the authority to vote proxies against the proposal at its annual meeting. In 1998, however, the SEC adopted amendments to Rule 14a-4 to address this new tactic. Under amended Rule 14a-4, a company has discretionary voting authority to vote its proxies on any matter if it did not have notice of the matter at least 45 days before the anniversary of the mailing date of the prior year's annual proxy statement (or by such other date as may be specified by advance notice provisions in the company's charter or bylaws).[138] If the annual meeting is moved more than 30 days from the anniversary of the prior year's annual meeting, or in the case of a special meeting, however, the old standard is retained, and discretionary authority is permitted only if the company did not have notice of the matter a reasonable period of time prior to the solicitation.[139]

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[137] <http://www.ctwinvestmentgroup.com>.

[138] Rule 14a-4(c)(1).

[139] Rules 14a-4(c)(1) and 14a-4(c)(3).

[4] Issue-Oriented Activists

The expanded ability to communicate with shareholders has aided issue-oriented activists in promoting and publicizing their causes through proxy campaigns. Shareholder proposals have targeted a wide variety of social issues, including the environment, particularly greenhouse gas emissions and renewable energy concerns; labor and human rights, focusing on international labor standards and outsourcing concerns; and equality and diversity issues, including board diversity and anti-discrimination policies, particularly with respect to sexual orientation. In the 2000 proxy season, shareholder and citizens groups calling themselves Campaign ExxonMobil stated that they had sent mailings to approximately 1,800 stockholders, holding in the aggregate more than 58% of ExxonMobil's shares, urging support for four environmental and social resolutions. These resolutions addressed renewable energy, alleged risks associated with projects in Africa and the Arctic, and executive compensation.[140] Another issue generating a large number of shareholder resolutions is the use of genetically modified foods, which according to one report generated the largest number of issue-oriented resolutions by 2000 since the anti-apartheid resolutions of the early 1990s.[141] While these types of issue-oriented resolutions have not historically garnered even close to a majority of the votes, the shareholder communications rules have increased the proponents' ability to solicit and organize publicity around the issues addressed by the resolutions. As a result, in recent years the level of support for social proposals has been increasing. In the 2008 proxy season, the average support for social and environmental proposals was 14.5%, and 31% of such proposals achieved support above the 20% level.[142] In the 2009 proxy season, for the first time, a climate change proposal, asking utility company Idacorp to set reduction goals for greenhouse gas emissions, won majority support at 51.2%.[143] And by the 2011 proxy season, ISS reports that the average level of support for proposals on environmental and social issues had reached 20.6%, crossing the 20%

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[140] *Dissident Shareholder Coalition Wages Proxy Fight on Environment, Human Rights, Announces Campaign ExxonMobil,* PR Newswire, May 11, 2000.

[141] James Cox, *Shareholders Get to Put Bio-Engineered Foods to Vote,* USA Today, June 6, 2000, at 1B.

[142] RiskMetrics Group 2008 Postseason Report at 36.

[143] *Id.*

mark for the first time.[144] A high number of social issue proposals end up being withdrawn, typically reflecting negotiated settlements under which the company agrees to take some action in exchange for the withdrawal. ISS reports that the 2009 proxy season set a new record for the number of negotiated withdrawals of social issue shareholder proposals.[145] As the level of support for these proposals continues to increase, we can expect to see more negotiated resolutions in the future.

[5] Mandatory Bylaws

A significant development in recent proxy seasons has been the emergence of Rule 14a-8 proposals to adopt mandatory bylaws, *i.e.*, bylaws purporting to be mandatorily binding on the company. Now that the SEC's proxy access rules have been vacated by the D.C. Circuit Court of Appeals, mandatory bylaw proposals for proxy access may become the means by which activists seek to implement proxy access on a company by company basis. Five of the nine proxy access proposals brought to a vote in the 2012 proxy season were mandatory proposals; however, none of these five garnered a majority vote.[146] As noted above, the Delaware General Corporation Law was amended in 2009 to permit (but not require) a corporation to include proxy access provisions in its bylaws.[147]

Prior to the advent of proxy access proposals, the most common example of a mandatory bylaw proposal was a bylaw requiring shareholder approval for a company to adopt a poison pill. Many legal commentators have expressed the view that such a mandatory bylaw would not be valid under Delaware law, where many corporations are incorporated.[148] When a mandatory poison pill bylaw was passed by Chubb's shareholders, Chubb responded that it had been advised that the bylaw was invalid under New Jersey law and that it would not recognize the bylaw.[149] At that time, the primary judicial precedent on the subject was

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[144] ISS Preliminary 2011 U.S. Postseason Report at 11.

[145] *Id.*

[146] *See* The Institute of Delaware Corporate & Business Law, Proxy Access Votes 2012, at <http://blogs.law.widener.edu/delcorp/2012/05/21/proxy-access-votes-2012/>.

[147] Del. Gen. Corp. Law § 112.

[148] *See* Lawrence A. Hamermesh, *Shareholder Rights: Another View,* Del. L. Wkly., Aug. 3, 1999, at 7.

[149] *Two Pill Proposals Receive Strong Shareholder Support,* IRRC Corp. Governance Highlights, Apr. 30, 1999, at 71.

the Oklahoma Supreme Court's decision in *Fleming*,[150] upholding such a bylaw under Oklahoma law. A legal challenge to Chubb's position that a mandatory bylaw was invalid under New Jersey law ended up being dismissed because the proponent of the bylaw had sold its position by the following proxy season and no longer had standing. With the sharp decline in the number of companies that still have a poison pill in force, the number of shareholder proposals addressing poison pills has dropped in recent years.

In 2008, the Delaware Supreme Court ruled against a proposed mandatory bylaw seeking to require reimbursement of dissidents who elect a short slate of directors.[151] The case was decided under a new process that allows the SEC, in reviewing whether to permit exclusion of a shareholder proposal under Rule 14a-8, to certify questions of law to the Delaware Supreme Court. The SEC certified two questions: whether the proposed bylaw was a proper matter for stockholder action under Delaware law, and whether the bylaw might cause the company to violate Delaware law. The court held that the bylaw was a proper matter for stockholder action, but then ruled that the bylaw could require the board to violate its fiduciary duties because it left the board with no discretion to determine that reimbursement of the dissidents' expenses was not appropriate. On this basis, the SEC permitted exclusion of the proposal. While limited to the specific facts at hand, the case suggests that a bylaw that mandates that a board take a specified action, with no exception for the board's fiduciary duties, is not valid under Delaware law.

In 2009, Delaware amended its General Corporation Law to permit (but not require) a corporation's bylaws to provide for the reimbursement by the corporation of expenses incurred by a stockholder in connection with the solicitation of proxies for the election of directors subject to the procedures and conditions set forth in the bylaws.[152] This codifies one of the holdings of the Delaware Supreme Court in *CA, Inc. v. AFSCME Employees Pension Plan* that bylaws permitting reimbursement of expenses of contestants in a successful proxy contest are a proper subject for shareholder action.

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[150] *International Bhd. of Teamsters Gen. Fund v. Fleming Cos.*, 975 P.2d 907 (W.D. Okla. 1999).

[151] *CA, Inc. v. AFSCME Employees Pension Plan*, No. 329, 2008 (Del. Sup. Ct. July 17, 2008).

[152] Del. Gen. Corp. Law § 113.

[6] Private Negotiations with Shareholders

While the private solicitations made by shareholder activists in favor of shareholder resolutions or against management proposals have clearly had an effect on their passage or defeat in a number of instances, arguably the greater impact of the change in the rules lies in the threat that this ability poses. Many shareholder proposals are negotiated away in private discussions between shareholder activists and management before being brought to a vote and, in many other cases, the increased responsiveness of managers to major shareholders is evident before a shareholder proposal is even put on the table. Richard Ferlauto, head of corporate governance at AFSCME, is quoted as saying "Engagement is now part of the landscape."[153] The receptivity of most major corporations to corporate governance surveys and requests for review of corporate governance practices, such as those put forth by TIAA-CREF or by CalPERS, has grown steadily since the SEC's adoption of the shareholder communications rules.[154] Clearly, the sheer size of the shareholdings of these institutions is one reason for this receptivity. But the increased ability to organize other large shareholders in making voting decisions adds greatly to the clout that the activists now wield.

The additional corporate governance reforms and rule changes of the last decade have further increased the ability of institutional shareholders to influence companies through private discussions and negotiations. The widespread adoption of majority voting policies, combined with the ongoing threat of withhold authority campaigns, has increased the leverage that activists have in these discussions. In addition, the NYSE requirement that companies create a process for direct communication to non-management directors, and the SEC rules encouraging similar communications processes, permit major shareholders to circumvent management and bring their concerns directly to the board. The heightened scrutiny of board actions and oversight created by the governance reforms and the governance environment put added pressure on boards to be responsive to the concerns communicated in this manner by major shareholders. And the heightened governance disclosure requirements created by the reforms give shareholders more information about companies' governance practices, allowing them to monitor these practices

[153] Ted Allen, *Executive Summary,* RiskMetrics Group 2007 Postseason Report at 3.
[154] *See Boards of Directors in the Spotlight,* ISSue Alert (May 1995) at 2.

more closely and to communicate any dissatisfaction to the company and its board more quickly.

Institutions and activists have reported a far greater receptivity on the part of targeted companies to discuss, negotiate, and agree to changes in governance policies. As noted earlier, the number of companies rescinding their rights plans or proposing to declassify their boards has continued to increase each year. One story on the 2004 proxy season states, "Now, companies are coming to the negotiating table—a result, some investor advisers say, of the threat that directors or executives could be ousted by large shareholders unhappy with their performance."[155] And another refers to IRRC data indicating "that more companies are agreeing to do what the majority of shareholders ask."[156] Patrick McGurn, then special counsel to ISS, has called it "the bloodless coup. . . . People tally up who won and who lost at the ballot box, and that tends to favor management. But when you throw in settlements, about two-thirds of dissident campaigns have been successful."[157]

Still open to debate is whether the increased clout of institutional shareholders and activists has become or will become too great. At the time the SEC was considering adoption of its shareholder communications rules, concern was expressed that the amendments would give institutions the power to make corporate decisions "in the back room" without public disclosure and open debate.[158] These concerns are enhanced by the increased prevalence of private negotiations between companies and large institutional investors that resolve corporate disputes out of the public eye. Kenneth Bertsch, then of the Investor Responsibility Research Center, commenting on this trend toward private negotiations, stated, "It may stifle public discussion and development of these issues."[159] Concerns have also been raised that private negotiation of these issues may

[155] Gretchen Morgenson, *An Emboldened Investor Class Is Not Likely to Go Away Soon,* N.Y. Times, Mar. 3, 2004, at C1.

[156] Tom Petruno, *A New Era for Investor Activism?,* L.A. Times, Mar. 7, 2004.

[157] Jonathan Burton, *Stockholders May Lose Proxy Battles But Win the War,* Dow Jones Newswire, Mar. 3, 2005.

[158] *See, e.g.,* Steven A. Rosenblum, *Proxy Reform, Takeovers, and Corporate Control: The Need for a New Orientation,* 17 J. Corp. L. 185, 200 (Fall 1991).

[159] Reed Abelson, *Proxy Peace; Prosperity and Hushed Deals Quiet the Annual Meeting,* N.Y. Times, May 28, 1998, at D1.

give large institutions an informational advantage over small shareholders in their investment decisions.[160]

§ 10.04 RECOMMENDATIONS

This section explores corporate responses relating to the requirements of the shareholder communications proxy rules and sets forth recommendations for the future.

[A] Investor Relations

The shareholder communications rules, subsequent corporate governance reforms, and the prospect of proxy access, as well as the increased shareholder activism these rules encourage, make more important than ever an effective investor relations program. Senior executives should maintain regular contact with a company's major institutional investors, while being mindful, of course, of Regulation FD and the need to avoid selective disclosure of material information. Building credibility with major shareholders is essential to the ability to fend off a proxy contest or other challenge if one arises. Companies should also recognize that the kind of activism generated by the more political actors such as unions and public pension funds may not necessarily be supported by mainstream institutions that are more focused solely on economic performance. For the latter group, if they believe the management is doing the right things for the company's business, they may be more inclined to support the management in the face of challenges from shareholder activists. For these reasons, it is important to be able to convey to shareholders an understanding of the company's business strategy, the ways in which the company's performance has been successful, the reasons for lack of successful performance, and the steps being taken to correct problems. Management should not try to deny or avoid discussing issues in the business that may be problematic or challenging, but should have a clear strategy for addressing them. To the extent management can build credibility and a relationship of trust, most mainstream institutional shareholders will be willing to show more patience in allowing management to carry through with its own plans to correct problems and improve performance.

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[160] *Id.*

[B] Understanding Hot Buttons

The company and its management should be sensitive to actions or practices that institutional shareholders may find particularly inflammatory. While the particular "hot buttons" may change over time, for the last several years, executive and director compensation practices have been a particular focus: *e.g.*, the magnitude of compensation packages, the disconnect between pay and performance, interlocking directors on compensation committees, independence of directors, repricing of options to reduce exercise prices, option grants with below-market exercise prices, mega-option grants, and retirement plans for outside directors. Other hot buttons relate to corporate governance items or takeover defenses, such as poison pills and staggered boards. ISS posts on its Web site the list of actions that will cause it to recommend a withhold vote and, in 2010, instituted a new GRIDS ("governance risk indicators") rating system that assigns positive or negative points to various governance and board practices. In addition, many institutional activists such as CalPERS publicize their views and policies on corporate governance issues.

A company should not be a slave to the governance views or ratings systems of activist shareholders and proxy advisory firms, and the foremost consideration should always be focused on what the board believes is in the best interests of the company. But some of the hot buttons would appear relatively painless to avoid, such as interlocking directors on the compensation committees. Director independence is now largely mandated under the federal and stock exchange corporate governance rules, and most companies have already significantly increased the independence of their boards. Other items such as a large pay package or option grants to induce an executive to join or remain at the company, or a staggered board, may have valid business purposes under a particular set of circumstances. Even so, it is important for the company and its board at least to be aware of what types of actions are likely to inflame institutional shareholders, or to cause a reduced governance rating, and to take this into account in the decision-making process.

[C] Deciding When to Compromise

As noted above, many shareholder proposals are withdrawn, and many more are never brought, as a result of a negotiated solution with the proponent or activist. Negotiating or seeking a compromise is certainly

not always the right result, and fighting a proposal may be the best path if the company and its board believe that the proposal is not in the company's best interest. But neither should a company have a knee-jerk reaction against considering a proposal that may be advanced by an activist. Whether it is a governance proposal or an economic or business strategy proposal, the company should make a conscious decision about whether the proposal, or some variation, is worth considering. And if the conclusion is to reject the proposal, the company should be ready to offer a clear explanation for its decision.

For example, in recent years, most companies have concluded that defending a rights plan against attack from activists is not worth it, given that most institutional shareholders will support anti–rights plan shareholder proposals, that ISS recommends a withhold authority vote against a board that adopts or renews a rights plan, and that a rights plan may be adopted on short notice by a board if circumstances arise that make it advisable. At the same time, companies have generally resisted making commitments that they will not adopt a rights plan without shareholder approval, or have added fiduciary duty exceptions to any such commitment. Similarly, many companies have adopted majority voting policies in response to shareholder proposals, or preemptively to avoid such a proposal, but have often provided that a director who does not receive a majority vote must submit an offer of resignation that may be accepted or rejected by the board, thus leaving the board with more flexibility to address the specifics of the situation if and when it arises. Companies may also consider economic or strategic proposals advanced by hedge fund activists, and on occasion have implemented some of these proposals or used the ideas in formulating their own strategic plans. The willingness to listen to and consider proposals can also give management more credibility even if the company ultimately rejects the proposal. In seeking support from other shareholders in response to a subsequent proxy contest or other attack by the activist, it is useful to be able to demonstrate that the company was willing to listen to and consider the activist's proposals and to explain the decision-making process that led to the conclusion that the proposal did not make sense for the company.

[D] Deciding When (and How) to Resist

While companies and their boards and managers should be open to considering proposals advanced by activists, in many cases a proposal

may simply not make sense for the company. Some activists will look to analyst reports to develop their proposals and decide which companies to target. Hedge fund activists, in particular, may become enamored of an idea advanced by an analyst and buy into a company's stock with the idea of promoting the idea. For this reason, companies should be alert to the ideas discussed by analysts in their reports and, if the idea does not make sense, may want to find an opportunity to explain why it does not make sense. This may be done in the context of an earnings call, analyst conference, or other appropriate forum. If the company can make its case convincingly, it may deter the activist from buying into the stock in the first place. With respect to governance proposals, some proposals currently in vogue, such as the separation of the Chair and CEO positions, may be unwise for any given company, and companies, at least to date, have had reasonable success in persuading a majority of their shareholders that separating the positions is not the right choice. Many companies have responded to this type of proposal, or have acted proactively, to adopt alternative arrangements, such as a lead director position, that are more suited to the particular circumstances of the company.

In resisting an activist, or fighting a proxy contest, a company may consider taking more aggressive action, such as litigation or trying to involve the SEC in addressing what the company may view as inappropriate behavior by the activists. For example, while shareholders are free under the proxy rules to discuss and lobby each other in private with respect to matters presented for a shareholder vote, to the extent their actions reach the point of a mutual understanding or agreement with respect to the voting of shares of a company, or otherwise acting together in connection with the investment, they are subject to Schedule 13D disclosure if their aggregate holdings exceed 5% of the company's stock.[161] In 2008, in a case involving a proxy contest at CSX Corporation, a New York federal court found that two hedge funds had violated the Schedule 13D disclosure rules by virtue of acting together without disclosure of a 13D group, as well as by virtue of their use of derivative securities.[162] However, the court declined to enjoin the hedge funds' voting of their shares at the annual meeting, and the two funds were successful in electing four of their five nominees. And, in 2011, the decision in that case

[161] Rule 13d-5(b)(1). *See* Dixon, *Post-Proxy Reform Era: Remaining Pitfall for the Unwary Activist Shareholder,* Corp. Governance Advisor, Oct./Nov. 1993, at 12.

[162] *CSX Corp. v. Children's Inv. Fund Mgmt. (UK) LLP,* 08 Civ. 2764 (LAK) (S.D.N.Y. June 11, 2008).

was reversed on appeal. Although litigation may be appropriate in some cases, a company must always be mindful that, in a proxy contest, its main goal is to persuade other shareholders to support the company, and that litigation and other aggressive tactics run the risk of alienating these other shareholders.

§ 10.05 CONCLUSION

The shareholder communications rules have encouraged increased shareholder activism and have increased the power and leverage of institutional shareholders, both within and outside the context of a formal proxy fight. The corporate governance reforms enacted since 2002 have extended that power. Corporate managers and directors have recognized the realities of shareholder activism and have become increasingly responsive to institutional shareholder concerns. In this environment, it is more important than ever for companies to engage in self-examination, make reforms where necessary to ensure compliance with all rules, and develop effective lines of shareholder communications. If a company's performance has declined, making it a more likely shareholder target, the company should be able to identify and communicate both the reasons for the poor performance and the steps being taken to address it.

Institutional investors, for their part, should recognize that with increased power comes increased responsibility. To the extent that institutional activism encourages a company's board and managers to apply increasing focus to the effectiveness of the company's corporate governance practices and the board's oversight of the company's business operations, it is a healthy development. However, to the extent activists and hedge funds use their increasing power to pursue union or other private agendas, or to force takeovers, spin-offs, restructurings, or other steps to boost short-term stock prices at the expense of long-term business operations, it will not help company performance and will ultimately hurt the health of our economy. Institutional investors, as well as the SEC and other regulatory agencies, should keep this balance in mind in making their policy, voting, and investment decisions.

[*Next page is 10-55.*]

EXHIBIT 1 MODEL BYLAWS FOR ADVANCE NOTICE OF STOCKHOLDER BUSINESS AND NOMINATIONS

SECTION 2.7. Order of Business.

(A) Annual Meetings of Stockholders. At any annual meeting of the stockholders, only such nominations of persons for election to the Board of Directors shall be made, and only such other business shall be conducted or considered, as shall have been properly brought before the meeting. For nominations to be properly made at an annual meeting, and proposals of other business to be properly brought before an annual meeting, nominations and proposals of other business must be (1) specified in the Corporation's notice of meeting (or any supplement thereto) given by or at the direction of the Board of Directors, (2) otherwise properly made at the annual meeting, by or at the direction of the Board of Directors or (3) otherwise properly requested to be brought before the annual meeting by a stockholder of the Corporation in accordance with these By-laws. For nominations of persons for election to the Board of Directors or proposals of other business to be properly requested by a stockholder to be made at an annual meeting, a stockholder must (a) be a stockholder of record at the time of giving of notice of such annual meeting by or at the direction of the Board of Directors and at the time of the annual meeting, (b) be entitled to vote at such annual meeting and (c) comply with the procedures set forth in these By-laws as to such business or nomination. The immediately preceding sentence shall be the exclusive means for a stockholder to make nominations or other business proposals before an annual meeting of stockholders, other than matters properly brought under Rule 14a-8 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and included in the Corporation's notice of meeting.

(B) Special Meetings of Stockholders. At any special meeting of the stockholders, only such business shall be conducted or considered, as shall have been properly brought before the meeting pursuant to the Corporation's notice of meeting. To be properly brought before a special meeting, proposals of business must be (1) specified in the Corporation's notice of meeting (or any supplement thereto) given by or at the direction of the Board of Directors or (2) otherwise properly brought before the special meeting by or at the direction of the Board of Directors. Nominations of persons for election to the Board of Directors may be made at

a special meeting of stockholders at which directors are to be elected pursuant to the Corporation's notice of meeting (a) by or at the direction of the Board of Directors or (b) provided that the Board of Directors has determined that directors shall be elected at such meeting, by any stockholder of the Corporation who (i) is a stockholder of record at the time of giving of notice of such special meeting and at the time of the special meeting, (ii) is entitled to vote at the meeting, and (iii) complies with the procedures set forth in these By-laws as to such nomination. The immediately preceding sentence shall be the exclusive means for a stockholder to make nominations or other business proposals before a special meeting of stockholders, other than matters properly brought under Rule 14a-8 under the Exchange Act and included in the Corporation's notice of meeting.

(C) General. Except as otherwise provided by law, the Certificate of Incorporation or these By-laws, the Chairman of any annual or special meeting shall have the power to determine whether a nomination or any other business proposed to be brought before the meeting was made or proposed, as the case may be, in accordance with these By-laws and, if any proposed nomination or other business is not in compliance with these By-laws, to declare that no action shall be taken on such nomination or other proposal and that such nomination or other proposal shall be disregarded.

SECTION 2.8. Advance Notice of Stockholder Business and Nominations.

(A) Annual Meeting of Stockholders. Without qualification or limitation, subject to Section 2.8(C)(4) of these By-laws, for any nominations or any other business to be properly brought before an annual meeting by a stockholder pursuant to Section 2.7(A) of these By-laws, the stockholder must have given timely notice thereof (including, in the case of nominations, the completed and signed questionnaire, representation and agreement required by Section 2.9 of these By-laws) and timely updates and supplements thereof in writing to the Secretary, and such other business must otherwise be a proper matter for stockholder action. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the close of business on the 120th day and not later than the close of business on the 90th day prior to the first anniversary of the preceding year's annual meeting; provided, however, that in the event that the date of the annual

meeting is more than 30 days before or more than 60 days after such anniversary date, notice by the stockholder must be so delivered not earlier than the close of business on the 120th day prior to the date of such annual meeting and not later than the close of business on the later of the 90th day prior to the date of such annual meeting or, if the first public announcement of the date of such annual meeting is fewer than 100 days prior to the date of such annual meeting, the 10th day following the day on which public announcement of the date of such meeting is first made by the Corporation. In no event shall any adjournment or postponement of an annual meeting, or the public announcement thereof, commence a new time period for the giving of a stockholder's notice as described above. Notwithstanding anything in the immediately preceding paragraph to the contrary, in the event that the number of directors to be elected to the Board of Directors is increased by the Board of Directors, and there is no public announcement by the Corporation naming all of the nominees for director or specifying the size of the increased Board of Directors at least 100 days prior to the first anniversary of the preceding year's annual meeting, a stockholder's notice required by this Section 2.8(A) shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it shall be delivered to the Secretary at the principal executive offices of the Corporation not later than the close of business on the 10th day following the day on which such public announcement is first made by the Corporation.

In addition, to be considered timely, a stockholder's notice shall further be updated and supplemented, if necessary, so that the information provided or required to be provided in such notice shall be true and correct as of the record date for the meeting and as of the date that is ten (10) business days prior to the meeting or any adjournment or postponement thereof, and such update and supplement shall be delivered to the Secretary at the principal executive offices of the Corporation not later than five (5) business days after the record date for the meeting in the case of the update and supplement required to be made as of the record date, and not later than eight (8) business days prior to the date for the meeting, or any adjournment or postponement thereof, in the case of the update and supplement required to be made as of ten (10) business days prior to the meeting or any adjournment or postponement thereof.

(B) Special Meetings of Stockholders. Subject to Section 2.8(C)(4) of these By-laws, in the event the Corporation calls a special meeting of stockholders for the purpose of electing one or more directors to the Board of Directors, any stockholder may nominate a person or persons

(as the case may be) for election to such position(s) to be elected as specified in the Corporation's notice calling the meeting, provided that the stockholder gives timely notice thereof (including the completed and signed questionnaire, representation and agreement required by Section 2.9 of these By-laws) and timely updates and supplements thereof in writing to the Secretary. In order to be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the close of business on the 120th day prior to the date of such special meeting and not later than the close of business on the later of the 90th day prior to the date of such special meeting or, if the first public announcement of the date of such special meeting is fewer than 100 days prior to the date of such special meeting, the 10th day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the Board of Directors to be elected at such meeting. In no event shall any adjournment or postponement of a special meeting, or the public announcement thereof, commence a new time period for the giving of a stockholder's notice as described above.

In addition, to be considered timely, a stockholder's notice shall further be updated and supplemented, if necessary, so that the information provided or required to be provided in such notice shall be true and correct as of the record date for the meeting and as of the date that is ten (10) business days prior to the meeting or any adjournment or postponement thereof, and such update and supplement shall be delivered to the Secretary at the principal executive offices of the Corporation not later than five (5) business days after the record date for the meeting in the case of the update and supplement required to be made as of the record date, and not later than eight (8) business days prior to the date for the meeting, or any adjournment or postponement thereof, in the case of the update and supplement required to be made as of ten (10) business days prior to the meeting or any adjournment or postponement thereof.

(C) Disclosure Requirements.

(1) To be in proper form, a stockholder's notice (whether given pursuant to Section 2.8(A) or 2.8(B) of these By-laws) to the Secretary must include the following, as applicable.

(a) As to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made, a stockholder's notice must set forth: (i) the name and address of such stockholder, as they appear on the Corporation's books, of such beneficial owner, if

any, and of their respective affiliates or associates or others acting in concert therewith, (ii) (A) the class or series and number of shares of the Corporation which are, directly or indirectly, owned beneficially and of record by such stockholder, such beneficial owner and their respective affiliates or associates or others acting in concert therewith, (B) any option, warrant, convertible security, stock appreciation right, or similar right with an exercise or conversion privilege or a settlement payment or mechanism at a price related to any class or series of shares of the Corporation or with a value derived in whole or in part from the value of any class or series of shares of the Corporation, or any derivative or synthetic arrangement having the characteristics of a long position in any class or series of shares of the Corporation, or any contract, derivative, swap or other transaction or series of transactions designed to produce economic benefits and risks that correspond substantially to the ownership of any class or series of shares of the Corporation, including due to the fact that the value of such contract, derivative, swap or other transaction or series of transactions is determined by reference to the price, value or volatility of any class or series of shares of the Corporation, whether or not such instrument, contract or right shall be subject to settlement in the underlying class or series of shares of the Corporation, through the delivery of cash or other property, or otherwise, and without regard to whether the stockholder of record, the beneficial owner, if any, or any affiliates or associates or others acting in concert therewith, may have entered into transactions that hedge or mitigate the economic effect of such instrument, contract or right or any other direct or indirect opportunity to profit or share in any profit derived from any increase or decrease in the value of shares of the Corporation (any of the foregoing, a "Derivative Instrument") directly or indirectly owned beneficially by such stockholder, the beneficial owner, if any, or any affiliates or associates or others acting in concert therewith, (C) any proxy, contract, arrangement, understanding, or relationship pursuant to which such stockholder has a right to vote any class or series of shares of the Corporation, (D) any agreement, arrangement, understanding, relationship or otherwise, including any repurchase or similar so-called "stock borrowing" agreement or arrangement, engaged in, directly or indirectly, by such stockholder, the purpose or effect of which is to mitigate loss to, reduce the economic risk (of ownership or otherwise) of any class or series of the shares of the Corporation incurred by, manage the risk of share price changes for, or increase or decrease the voting power of, such stockholder with respect to any class or series of the shares of the Corporation, or which provides,

directly or indirectly, the opportunity to profit or share in any profit derived from any decrease in the price or value of any class or series of the shares of the Corporation (any of the foregoing, "Short Interests"), (E) any rights to dividends on the shares of the Corporation owned beneficially by such stockholder that are separated or separable from the underlying shares of the Corporation, (F) any proportionate interest in shares of the Corporation or Derivative Instruments held, directly or indirectly, by a general or limited partnership in which such stockholder is a general partner or, directly or indirectly, beneficially owns an interest in a general partner of such general or limited partnership, (G) any performance-related fees (other than an asset-based fee) that such stockholder is entitled to based on any increase or decrease in the value of shares of the Corporation or Derivative Instruments, if any, including without limitation any such interests held by members of such stockholder's immediate family sharing the same household, (H) any significant equity interests or any Derivative Instruments or Short Interests in any principal competitor of the Corporation held by such stockholder, and (I) any direct or indirect interest of such stockholder in any contract with the Corporation, any affiliate of the Corporation or any principal competitor of the Corporation (including, in any such case, any employment agreement, collective bargaining agreement or consulting agreement), and (iii) any other information relating to such stockholder and beneficial owner, if any, that would be required to be disclosed in a proxy statement and form of proxy or other filings required to be made in connection with solicitations of proxies for, as applicable, the proposal and/or for the election of directors in a contested election pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder;

(b) If the notice relates to any business other than a nomination of a director or directors that the stockholder proposes to bring before the meeting, a stockholder's notice must, in addition to the matters set forth in paragraph (a) above, also set forth: (i) a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting and any material interest of such stockholder and beneficial owner, if any, in such business, (ii) the text of the proposal or business (including the text of any resolutions proposed for consideration), and (iii) a description of all agreements, arrangements and understandings between such stockholder and beneficial owner, if any, and any other person or persons (including their names) in connection with the proposal of such business by such stockholder;

(c) As to each person, if any, whom the stockholder proposes to nominate for election or reelection to the Board of Directors, a stockholder's notice must, in addition to the matters set forth in paragraph (a) above, also set forth: (i) all information relating to such person that would be required to be disclosed in a proxy statement or other filings required to be made in connection with solicitations of proxies for election of directors in a contested election pursuant to Section 14 of the Exchange Act and the rules and regulations promulgated thereunder (including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected) and (ii) a description of all direct and indirect compensation and other material monetary agreements, arrangements and understandings during the past three years, and any other material relationships, between or among such stockholder and beneficial owner, if any, and their respective affiliates and associates, or others acting in concert therewith, on the one hand, and each proposed nominee, and his or her respective affiliates and associates, or others acting in concert therewith, on the other hand, including, without limitation all information that would be required to be disclosed pursuant to Rule 404 promulgated under Regulation S-K if the stockholder making the nomination and any beneficial owner on whose behalf the nomination is made, if any, or any affiliate or associate thereof or person acting in concert therewith, were the "registrant" for purposes of such rule and the nominee were a director or executive officer of such registrant; and

(d) With respect to each person, if any, whom the stockholder proposes to nominate for election or reelection to the Board of Directors, a stockholder's notice must, in addition to the matters set forth in paragraphs (a) and (c) above, also include a completed and signed questionnaire, representation and agreement as required by Section 2.9 of these By-laws. The Corporation may require any proposed nominee to furnish such other information as may reasonably be required by the Corporation to determine the eligibility of such proposed nominee to serve as an independent director of the Corporation or that could be material to a reasonable stockholder's understanding of the independence, or lack thereof, of such nominee.

(2) For purposes of these By-laws, "public announcement" shall mean disclosure in a press release reported by a national news service or in a document publicly filed by the Corporation with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Exchange Act and the rules and regulations promulgated thereunder.

(3) Notwithstanding the provisions of these By-laws, a stockholder shall also comply with all applicable requirements of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in these By-laws; provided, however, that any references in these By-laws to the Exchange Act or the rules promulgated thereunder are not intended to and shall not limit the requirements applicable to nominations or proposals as to any other business to be considered pursuant to Section 2.7 of these By-laws.

(4) Nothing in these By-laws shall be deemed to affect any rights (a) of stockholders to request inclusion of proposals in the Corporation's proxy statement pursuant to Rule 14a-8 under the Exchange Act, or (b) of the holders of any series of Preferred Stock if and to the extent provided for under law, the Certificate of Incorporation or these By-laws. Subject to Rule 14a-8 under the Exchange Act, nothing in these By-laws shall be construed to permit any stockholder, or give any stockholder the right, to include or have disseminated or described in the Corporation's proxy statement any nomination of director or directors or any other business proposal.

SECTION 2.9. Submission of Questionnaire, Representation and Agreement.

To be eligible to be a nominee for election or reelection as a director of the Corporation, a person must deliver (in accordance with the time periods prescribed for delivery of notice under Section 2.8 of these By-laws) to the Secretary at the principal executive offices of the Corporation a written questionnaire with respect to the background and qualifications of such person and the background of any other person or entity on whose behalf the nomination is being made (which questionnaire shall be provided by the Secretary upon written request), and a written representation and agreement (in the form provided by the Secretary upon written request) that such person (A) is not and will not become a party to (1) any agreement, arrangement or understanding with, and has not given any commitment or assurance to, any person or entity as to how such person, if elected as a director of the Corporation, will act or vote on any issue or question (a "Voting Commitment") that has not been disclosed to the Corporation or (2) any Voting Commitment that could limit or interfere with such person's ability to comply, if elected as a director of the Corporation, with such person's fiduciary duties under applicable

law, (B) is not and will not become a party to any agreement, arrangement or understanding with any person or entity other than the Corporation with respect to any direct or indirect compensation, reimbursement or indemnification in connection with service or action as a director that has not been disclosed therein, and (C) in such person's individual capacity and on behalf of any person or entity on whose behalf the nomination is being made, would be in compliance, if elected as a director of the Corporation, and will comply with all applicable corporate governance, conflict of interest, confidentiality and stock ownership and trading policies and guidelines of the Corporation publicly disclosed from time to time.